# Section D. Energy Efficient Mortgage Program

## **Overview**

## **In This Section**

This section contains the topics listed in the table below.

Topic	Topic Name	See Page
1	General Information on the EEM Program	6-D-2
2	Basic EEM Program Requirements and	6-D-6
	Criteria	
3	Home Energy Rating System (HERS) Report	6-D-12
	Requirements	
4	Processing an EEM	6-D-15

## 1. General Information on the EEM Program

#### Introduction

This topic contains general information on the Energy Efficient Mortgage (EEM) Program, including

- the purpose of the EEM program
- features of the EEM program
- escrow account required prior to installation of improvements, and
- lender responsibilities for the EEM escrow account.

#### **Change Date**

March 24, 2011

### 4155.1 6.D.1.a Purpose of the EEM Program

The Energy Efficient Mortgage (EEM) Program allows a borrower to finance 100% of the expense of a cost effective "energy package," that is, the property improvements to make the house more energy efficient. The EEM Program recognizes that the improved energy efficiency of a house can increase its affordability by reducing operating costs.

Because the home is energy efficient, the occupant(s) will save on utility costs, and therefore, be able to devote more income to the monthly mortgage payment.

A cost effective energy package is one where the cost of improvements, including maintenance, is less than the present value of the energy saved over the useful life of those improvements.

Energy efficiency improvements can include energy saving equipment, and active and passive solar technologies.

## 1. General Information on the EEM Program, Continued

4155.1 6.D.1.b Features of the EEM Program Under the EEM Program, a borrower can finance 100% of the cost of eligible energy efficient improvements into the mortgage, subject to certain dollar limitations, without an appraisal of the energy efficient improvements. For the EEM Program, the

- mortgage amount includes the cost of the energy efficient improvements, in addition to the usual mortgage amount normally permitted
- FHA maximum loan limit for the area *may* be exceeded by the cost of the energy efficient improvements
- energy efficient improvements *must* be cost effective in order to be included into the mortgage, and
- amount of the cost effective energy package is added to the approved base loan amount before adding any upfront mortgage insurance premium (UFMIP).

For existing properties, energy-related weatherization items may be combined with the EEM, where the maximum dollar amount allowed under an EEM does not cover the cost of the entire energy package. The weatherization amount would be the cost of the improvements not covered by the EEM amount. With a 203(k), the excess improvements would be included in the rehabilitation work.

*Note*: While the energy package may be financed into the loan, the borrower does not need to qualify with the additional financing or provide additional downpayment.

References: For more information on

- cost-effectiveness of the improvements, see HUD 4155.1 6.D.2.d
- the calculation Worksheet, see HUD 4155.1 6.D.4.b, and
- maximum mortgage additions, see HUD 4155.1 2.A.5.g.

## 1. General Information on the EEM Program, Continued

4155.1 6.D.1.c Escrow Account Required for Prior to Installation of Improvements FHA *will* endorse a mortgage for an existing property before the energy-efficient improvements are installed, provided that the lender establishes an escrow account and deposits funds into the account to pay for the energy-efficient improvements.

The escrow account must be established for no more than 90 days, or 180 days for a Section 203(k) rehabilitation mortgage.

#### Notes:

- If the improvements are not completed within 90 days, or 180 days for a 203(k) mortgage, the lender must apply the funds held in escrow to a prepayment of the mortgage principal.
- For new construction, there is no escrow account necessary, since the energy package is installed as part of the total construction, which must be completed prior to closing. The energy package must be completed before the mortgage is eligible for insurance, if using an FHA Construction-Permanent mortgage.

## References: For more information on

- lender responsibilities for the EEM escrow account, see HUD 4155.1 6.D.1.d, and
- construction-permanent mortgages, see HUD 4155.1 6.A.3.

## 1. General Information on the EEM Program, Continued

4155.1 6.D.1.d Lender Responsibilities for the EEM Escrow Account In order for FHA to insure a mortgage prior to installation of energy-efficient improvements, the lender must

- ensure that an escrow account is established and insured at a financial institution supervised by a Federal agency, and that the appropriate funds are deposited into the account
- administer the account, or arrange for administration by a
  - utility company
  - nonprofit organization, or
  - government agency
- execute Form HUD-92300, *Mortgage Assurance of Completion*, to indicate that the escrow for the improvements has been established, and
- upon completion of the improvements
  - inspect the improvements, or arrange for inspection by the rater or an FHA fee inspector, and
  - notify FHA, through the FHA Connection (FHAC), that the improvements have been made and that the escrow has been cleared.

*Note*: The borrower *cannot* 

- be paid for labor he/she performed (sweat equity), or
- receive cash back from the mortgage transaction.

## 2. Basic EEM Program Requirements and Criteria

#### Introduction

This topic contains information on basic EEM program requirements and criteria, including

- eligible EEM properties and programs
- underwriting the EEM
- EEM appraisal requirements
- the cost of energy efficient improvements
- HERS report for EEM
- when EEM work differs from the approved energy package
- the required inspection by a HERS representative
- requirements for the HERS representative
- the requirement for streamline refinance transactions, and
- fees for the Home Energy Rating on EEM.

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#### 4155.1 6.D.2.a Eligible EEM Properties and Programs

New and existing one to four unit properties, including one unit condominiums and manufactured housing properties, are eligible for the Energy Efficient Mortgage (EEM) Program.

EEMs may be used for both purchases and refinances, including streamline refinances, with

- Section 203(b)
- Section 203(k) rehabilitation loans
- Section 234(c) units in FHA-approved condominium projects, and
- 203(h) mortgages for disaster victims

*Note*: For multiple unit properties, the allowable EEM dollar amount is for the entire property, and not calculated on a per-unit amount.

## 2. Basic EEM Program Requirements and Criteria, Continued

4155.1 6.D.2.b Underwriting the EEM The EEM is initially underwritten as if the energy package did not exist, using standard FHA underwriting guidelines, qualifying income ratios, and maximum mortgage/minimum downpayment requirements, without regard to the energy package.

In addition to the cost of improvements, the borrower can get "stretch ratios" of 33% and 45% for an EEM on

- new construction, or
- homes that
  - were built to the 2000 International Energy Conservation Code (IECC) formerly known as the Model Energy Code, or
  - are being retrofitted to that standard.

For new construction, when qualifying the borrower, the cost of the energy package should be subtracted from the sales price (since the builder has included the EEM improvements in the sales price) and the qualifying ratios are calculated on this lower amount.

**Note**: FHA's Technology Open To Approved Lenders (TOTAL) Mortgage Scorecard may also be used for underwriting EEMs. If the lender obtains an "accept" or "approve" on a mortgage loan application, FHA will recognize the risk rating from TOTAL and permit the increase to the mortgage payment without re-underwriting or rescoring, provided that the lender's Direct Endorsement (DE) underwriter attests that he/she has reviewed the calculations associated with the energy efficient improvements, and found the mortgage and the property to be in compliance with FHA's underwriting instructions.

**References**: For more information on the TOTAL Mortgage Scorecard, see

- HUD 4155.1 6.A.1, and
- the TOTAL User Guide.

## 2. Basic EEM Program Requirements and Criteria, Continued

#### 4155.1 6.D.2.c EEM Appraisal Requirements

On an EEM, there is no need for a second appraisal that reflects the expense of the energy package and the improvements. The appraisal does not need to reflect the value of the energy package that will be added to the property for either new or existing construction.

On a Section 203(k), the after-improved value is to be used for the EEM process.

### 4155.1 6.D.2.d Cost of EEM Improvements

Once the borrower and the property are determined eligible for FHA-insured financing, the lender, using the energy rating report and the EEM worksheet, determines the dollar amount of the cost-effective energy package that may be added to the mortgage amount.

The cost of any improvement to the property that will increase the property's energy efficiency, and that is determined to be cost effective, is eligible for financing into the mortgage.

The cost that may be added to the mortgage amount is up to the *greater* of

- 5% of the property's value, not to exceed \$8,000, or
- \$4,000.

*Note*: Regardless of the property's value, every borrower who otherwise qualifies can finance at least \$4,000 of the costs of the energy package, if the cost exceeds \$4,000.

**Reference**: For more information on the EEM worksheet, see HUD 4155.1 6.D.4.b.

## 2. Basic EEM Program Requirements and Criteria, Continued

4155.1 6.D.2.e HERS Report for EEM The energy package is the set of improvements agreed to by the borrower, based on recommendations and analysis performed by a qualified home energy rater using the HERS tool.

The HERS must

- meet the minimum requirements of the Department of Energy (DOE) approved ratings guidelines, and
- achieve passing results for DOE's Building Energy Simulation Test (BESTTEST), or subsequent testing requirements.

For new construction, the energy package includes those cost-effective energy improvements over and above the requirements of the 2000 IECC.

4155.1 6.D.2.f When EEM Work Differs From the Approved Energy Package The table below describes the actions required if the improvement work differs from the approved energy package.

When the	Then
work that is done differs from	submit a change order, along with a
the approved energy package	revised HERS report to the DE
	underwriter for approval.
changes still meet the cost-	further analysis is <i>not</i> required.
effectiveness test	
changes do not meet the cost-	the funds for the work not included in the
effectiveness test	approved energy package must be used to
	pay down the loan principal.

## 2. Basic EEM Program Requirements and Criteria, Continued

4155.1 6.D.2.g Required Inspection by HERS Representative The cost of the energy improvements, including maintenance costs, and the estimate of the energy savings must be determined based upon a physical inspection of the property, or the plans and specifications of a house being built, by a home energy rater using HERS.

The rater must be trained to perform the physical inspection and/or diagnostic tests that provide the data on the property. The home energy rater, using the HERS, prepares a written home energy rating report, and provides copies to both the borrower and the lender.

The lender must include a copy of the HERS report and Energy Efficient Mortgage Worksheet in the closing package, placed behind Form HUD-92900-LT, *FHA Loan Underwriting and Transmittal Summary* when requesting insurance endorsement.

**References**: For more information on requirements for the HERS

- representative, see HUD 4155.1 6.D.2.h, and
- report, see HUD 4155.1 6.D.3.

4155.1 6.D.2.h Requirements for the HERS Representative The HERS representative or energy consultant, must be an independent entity. He/she cannot be related directly or indirectly to the seller of the property, the prospective borrower, or the contractor selected by the borrower to install the energy efficient improvements.

The HERS representative or energy consultant may be a(n)

- utility company
- local, state, or Federal government agent
- entity approved by a local, state, or Federal government agency specifically for the purpose of providing home energy ratings on residential properties, or
- nonprofit organization experienced in conducting home energy ratings of residential properties.

## 2. Basic EEM Program Requirements and Criteria, Continued

4155.1 6.D.2.i Streamline Refinance Transactions with EEM For a streamline refinance with EEM, the borrower's principal and interest (P&I) payment on the new loan, including the energy package, may be greater than the P&I payment on the current loan, provided the estimated monthly energy savings shown on the HERS report exceeds the increase in the P&I.

On a streamline refinance without an appraisal, the original principal balance substitutes for an appraised value.

4155.1 6.D.2.j 1 Fees for the Home Energy Rating on EEM FHA does not set the fees for the Home Energy Rating, including the physical inspection, the HERS Report, and any post-installation test. The fees charged to the borrower for the Home Energy Rating must be customary and reasonable for the area.

These fees may be included and financed as part of the energy package if the entire package, including those fees, is cost-effective. If not, such fees are considered closing costs.

With a Section 203(k), the rating fee and inspections would be in addition to the consultant's fee.

## 3. Home Energy Rating System (HERS) Report Requirements

#### Introduction

This topic contains information on the requirements for the home energy rating report, including

- HERS report requirements
- required information for the HERS report, and
- the HERS representative certification statement.

#### **Change Date**

March 24, 2011

## 4155.1 6.D.3.a HERS Report Requirements

The Home Energy Rating System (HERS) representative or energy consultant is responsible for preparing the home energy rating report. He/she must

- prepare the report in writing, and
- provide a copy to the
  - prospective borrower, and
  - lender.

*Note*: The lender must include a copy of the home energy rating report in the closing package when requesting insurance endorsement.

# 3. Home Energy Rating System (HERS) Report Requirements, Continued

4155.1 6.D.3.b Required Information for the HERS Report The energy package report prepared by the HERS representative must include the information described in the table below.

Type of	Includes	
Information		
General Information	Address of the property	
	Name of the borrower	
	• FHA case number (if applicable)	
	Name of lender (if applicable)	
	• Type of property	
	Classification as new or existing property, and	
	Date of the	
	– physical inspection of the existing property, or	
	<ul> <li>plan review for new construction.</li> </ul>	
Energy Features	A description of the energy features currently at the	
Description	property (or proposed features if new construction),	
	including, at a minimum, a description of the	
	• insulation R values in ceilings, walls, and floors	
	• infiltration levels and barriers (caulking,	
	weatherstripping, and sealing)	
	• windows (storm, double pane, triple pane) and	
	doors, and	
	• heating (including water heating) and cooling	
	systems.	
Energy Package	A description of the energy package, which, for	
Description		
	• existing properties, includes cost-effective	
	improvements recommended to improve the	
	energy efficiency of the property, or	
	• new construction, includes cost-effective	
	improvements to be included in the home that	
	exceeded the requirements of 2000 International	
	Energy Conservation Code (IECC).	

# 3. Home Energy Rating System (HERS) Report Requirements, Continued

#### 4155.1 6.D.3.b Required Information for the HERS Report (continued)

Type of	Includes	
Information		
Energy Package	Estimated costs of the energy package	
Estimate	• Useful life, and	
	• Costs of any maintenance over the useful life of	
	the improvements.	
Annual Estimates	• The estimated present annual utility costs, before	
	installation of the energy package, for existing	
	property and for new construction (i.e., a	
	referenced house built to 2000 IECC standards).	
	The estimated annual	
	<ul> <li>costs after installation of the energy package,</li> <li>and</li> </ul>	
	– savings in utility costs <i>after</i> installation of the	
	energy package, including the present value of	
	the savings.	
	Note: The massest value test is a statutour.	
	<b>Note</b> : The present value test is a statutory	
	requirement. Actual energy savings cannot be used	
	to determine cost effectiveness in lieu of the present value calculation of the energy savings.	
Inspection Deport		
Inspection Report	Printed name and signature of the person performing	
Names	the inspection and preparing the report, as well as	
	the date of the report.	

## 4155.1 6.D.3.c HERS Representative Certification Statement

The following certification statement must be signed by the person who

- inspected the property, and
- prepared the HERS report.

"I certify, that to the best of my knowledge and belief, the information contained in this report is true and accurate and I understand that the information in this report may be used in connection with an application for an energy efficient mortgage to be insured by the Federal Housing Administration of the United States Department of Housing and Urban Development."

## 4. Processing an EEM

#### Introduction

This topic contains information on processing an Energy Efficient Mortgage (EEM), including

- processing an EEM, and
- the Energy Efficient Mortgage Worksheet.

#### **Change Date**

March 24, 2011

### 4155.1 6.D.4.a Processing an EEM

If the borrower elects to have an Energy Efficient Mortgage (EEM) and add the cost of the energy efficient improvements to the mortgage, the lender must complete the additional processing steps found in the table below.

Step	Action		
1	Obtain the home energy rating report prepared by a Home Energy		
	Rating System (HERS) representative or energy consultant		
	showing the estimated		
	• costs of installing the energy efficient improvements, including		
	any maintenance costs, and		
	• annuals savings in utility costs that will result from the		
	installation of the energy efficient improvements.		
2	Using the HERS report, determine if the energy efficient		
	improvements are "cost effective" by calculating the		
	<ul> <li>present cost of the energy improvements, including maintenance costs (if any) over the useful life of the improvements, and</li> <li>present value of the energy savings over the useful life of the energy improvements</li> </ul>		
	energy improvements.		

# 4. Processing an EEM, Continued

## 4155.1 6.D.4.a Processing an EEM (continued)

Step	Action
3	Determine whether or not the energy-efficient improvements are cost effective (meaning that the present <i>cost</i> of improvements is <i>less</i> than the present value of the energy savings)
	<ul> <li>If yes</li> <li>add 100% of the cost of the energy-efficient improvements, subject to the dollar limits described in HUD 4155.1 6.D.2.d, to the otherwise allowable maximum mortgage amount, and</li> <li>go to Step 4.</li> <li>If no, do not include the additional expense of the energy package in the maximum mortgage amount.</li> </ul>
	<i>Note</i> : If the improvements <i>are</i> determined to be cost effective, no appraisal is necessary and the borrower is not required to meet any further credit standards.
4	Calculate the upfront mortgage insurance premium (UFMIP) on the full mortgage amount, which includes the cost of the energy improvements.

## 4. Processing an EEM, Continued

4155.1 6.D.4.b Energy Efficient Mortgage Worksheet The following is the format of the *Energy Efficient Mortgage Worksheet*.

Energy Efficient Mortgage (EEM) Worksheet		
Borrower's	,	FHA Case No.:
Name:		
Property		
Address:		
A. Qualifying	1. Mortgage (w/o MIP)	A. \$
Mortgage		
Amount		
B. EEM	The Home Energy Rating	
Amount	System (HERS) Report will	
	provide the	
	information on the	
	Recommended Energy Package	
	• cost, and	
	• present value of the energy	
	saved.	
	Compare Cost and PV of energy	
	savings:	
	• Cost of the Energy Package \$	
	• PV of Energy Saved \$	
	• Is PV more than Cost? Y / N	
	• If Yes, Continue:	
	1. If the Cost is less than	B. \$
	\$4,000, enter the Cost in B.	
	2. If the Cost is more than	
	\$4,000, but 5% of the value is	
	less than \$4,000, enter \$4,000 in	
	B.	
	3. If the Cost is less than 5% of	
	the value, but 5% of the value is	
	more than \$4,000, enter the	
	lesser of the cost, or \$8,000 in B.	
	4. If the Cost is greater than 5%	
	of the value, enter the lesser of	
	5% of the value or \$8,000 in B	

C. Final EEM	Add A and B.	C. \$
Mortgage		
Amount		
(without MIP)		
REMARKS:		