

# Multifamily Selling and Servicing Guide

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#### **1807.05** Cap Cost Factor Included in Maximum Note Rate

#### ✓ Requirements

When determining the Maximum Note Rate used to calculate the minimum required Underwritten DSCR, you must include a cap cost factor based on the term of the

- Credit Enhancement Mortgage Loan, and
- initial Interest Rate Cap.

You do not need to include a cap cost factor if the initial Interest Rate Cap term equals the Credit Enhancement Mortgage Loan term.

You must ensure the cap cost factor equals the

- estimated cost of the replacement cap (when the term of the initial cap expires), divided by
- term of the initial cap.

# **%** Operating Procedures

For example, to calculate the cap cost factor assuming a 5-year Interest Rate Cap and 10-year Credit Enhancement Mortgage Loan term:

- You must include an annual cap cost factor in the Maximum Note Rate.
- If the Credit Enhancement Mortgage Loan term is 10 years and an initial cap is purchased for a 5-year term, the cap cost factor equals the estimated cost of a replacement cap divided by 5 (the number of years of the initial interest rate term).
- The replacement cap has a 5-year term and a Cap Strike Rate equal to that of the initial cap.
- If a 5-year Interest Rate Cap at the initial Cap Strike Rate costs 20 basis points, you must divide 20 by 5, then add the result (4 basis points) to the Maximum Note Rate.

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# **Glossary**

#### C

Cap Strike Rate

Index interest rate specified in the Interest Rate Cap Agreement at or above which a payment obligation will be triggered by the Interest Rate Cap provider.

Credit Enhancement Mortgage Loan Mortgage Loan financed by a Bond issuance where Fannie Mae provides credit enhancement by

- a Credit Enhancement Instrument, or
- an MBS for Bonds.

#### **Synonyms**

Credit Enhancement Mortgage Loans

## T

Interest Rate Cap

Interest rate agreement between the Borrower and a provider for which the Borrower receives payments at the end of each period when the interest rate exceeds the Cap Strike Rate. The Interest Rate Cap provides a ceiling (or cap) on the Borrower's Mortgage Loan interest payments.

## **Synonyms**

- Interest Rate Caps
- Interest Rate Hedge
- Interest Rate Hedges
- Interest Rate Swap
- Interest Rate Cap's

## M

Maximum Note Rate

Equals the sum of the:

minimum Cap Strike Rate as set by Fannie Mae; and

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- Mortgage Loan margin equal to the sum of the
  - Investor spread,
  - Guaranty Fee, and
  - Servicing Fee.