

## **MORTGAGES: Unless your bank will *hold* the mortgage rather than selling it on to Fannie Mae or Freddie Mac, your property ownership could be at risk**



[FROM [http://www.americanbanker.com/issues/178\\_218/fracking-boom-gives-banks-mortgage-headaches-1063561-1.html?zkPrintable=1&nopagination=1](http://www.americanbanker.com/issues/178_218/fracking-boom-gives-banks-mortgage-headaches-1063561-1.html?zkPrintable=1&nopagination=1):]

... The uniform New York state mortgage agreement, used by Fannie Mae and Freddie Mac, states that "you cannot cause or permit any hazardous materials to be on your property and it specifically references oil and gas," says Greg May, vice president of residential mortgage lending at Tompkins. "That alone would make it a problem."

The mortgage agreement says homeowners can sell an oil or gas lease to an energy firm *with prior consent from a lender*, but May says, "I don't know any lenders who are granting that right now."

If Fannie Mae owns the mortgage, it's unlikely it would approve such a transfer. Fannie Mae generally does not "allow surface instruments," such as an oil rig, on property it owns...

A greater concern for homeowners is that Fannie Mae or Freddie Mac could force the entire outstanding loan balance to become due immediately. ...

The ultimate warning sign for banks may be insurance, May says. A borrower can't get a mortgage without homeowners' insurance. "We're actually seeing insurance companies cancel [insurance] renewals when they find a [gas or oil] lease on the property," May says.  
[\*SEE BACK FOR INSURANCE INFORMATION\*]

**Idaho State Senator Michelle Stennett asked the Idaho Dept. of Lands about the impact of gas leases on mortgages. IDL sent Sen. Stennett this info in February of 2015. It has not been published on the IDL site. WHY?**

### **Impact of Gas Leases on Mortgages**

Prepared by Idaho Department of Lands, February 2015

The Idaho Department of Lands has received questions about how oil and gas leasing could affect mortgages, particularly when an oil and gas lease is issued after securing a mortgage on the property.

### **Fannie Mae and Freddie Mac**

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Mortgage Corporation (Freddie Mac) do not originate mortgages, but purchase them from primary lenders. **Because Fannie Mae and Freddie dominate the secondary mortgage market for residential mortgages, lenders must follow their guidelines to ensure their mortgages are eligible for sale to Fannie Mae and Freddie Mac. Such guidelines have several provisions relevant to oil and gas leases.**

Section 39.4 of the Freddie Mac seller-servicer guide for title insurance requirements provides that exceptions for “outstanding oil, gas, water or mineral rights are acceptable if commonly granted by private institutional Mortgage investors in the area where the Mortgaged Premises are located,” and:

- “The exercise of such rights will not result in damage to the Mortgaged Premises or **impairment of the use or marketability of the Mortgaged Premises for residential purposes** and there is no right of surface or subsurface entry within 200 feet of the residential structure, or
- There is a comprehensive endorsement to the title insurance policy that affirmatively insures the lender against damage or loss due to the exercise of such rights.”

In addition to such title insurance requirements, Fannie Mae and Freddie Mac require primary lenders to use standard mortgage language potentially prohibiting the borrower from entering into an oil and gas lease without the lender’s permission:

- Section 18 of the Fannie Mae and Freddie Mac uniform mortgage agreement for Idaho **allows the lender to call the mortgage if the borrower sells or transfers any portion of the property, or “any right in the property,” without the lender’s prior written permission. If the lender calls the mortgage the borrower must immediately pay in full the outstanding loan amount.**
- Section 21 of the Fannie Mae and Freddie Mac uniform mortgage agreement for Idaho **prohibits environmental hazardous substances, including flammable petroleum, from being stored, used, disposed of, discharged, or released on the mortgaged property. The prohibition applies both to the borrower and to anyone acting with the borrower’s permission.**

According to the Fannie Mae servicing guide, **a lease of oil and gas rights is a transfer of a right in property that requires prior permission of the lender.** The borrower must submit an “Application for Release of Security.”

The Congressional Research Service published a report in 2011 titled “How Fannie Mae and Freddie Mac Typically Handles Requests to Create Oil, Gas, or Mineral Leases on Residential Properties” (Attachment 2). The report found that **“entering into an oil, gas, or mineral lease on a property that is subject to a mortgage owned or guaranteed by Fannie Mae or Freddie Mac without prior approval generally will be considered an act of default under the mortgage.”** But both **Fannie Mae and Freddie Mac will consider applications for releases allowing oil and gas leases to proceed.** The Servicing Guide for Fannie Mae single family loans sets forth the following **criteria for issuing such releases:**

- **The extent to which the rights granted by the lease infringe on the property owner’s rights.**
- **Any hazards, nuisances, or damages that may result from the exercise of the rights granted by the lease.**

After considering the above factors, the lender must determine whether the proposed lease meets the following conditions:

- Granting of oil, gas, or mineral leases is customary in the area.

- ✓ The community's acceptance of oil and gas development is an important factor. **In areas where oil exploration is a well-established part of the economy, the risk may be considered acceptable, whereas it might be unacceptable in areas where such exploration is new or limited.**

- **Exercise of the lease would not have a material impact on the value of the property.**
- Exercise of the lease does not prevent use of the property as a residence.
- **Exercise of the lease does not expose the residents to health or safety hazards.**

Fannie Mae considers all the above-listed conditions. If all conditions are met the lender can approve the lease; if one or more conditions are not met, then the lease must be submitted to Fannie Mae's National Servicing Organization (NSO) for approval.

## Split Estates

Split estates, where the mineral rights are owned by an individual or entity, not the surface owner, are not explicitly addressed in the Fannie Mae and Freddie Mac seller-service guides, but **would likely be considered "outstanding rights" that may affect the marketability of the property for residential purposes.** Additionally, **if the estate is split and the surface owner enters into an agreement with the operator regarding surface access, then such agreement may be a conveyance of a property interest requiring the lender's permission.**

## Federal Agricultural Mortgage Corporation

Fannie Mae does not buy mortgages for ranches or farms; such mortgages are purchased by the **Federal Agricultural Mortgage Corporation (Farmer Mac), which, like Fannie Mae, requires lender permission before transferring any property rights by means of an oil and gas lease.** Farmer Mac Seller/Service Guide § 304.3. Farmer Mac mortgages also **prohibit causing or permitting the presence of hazardous substances on the property, and defines hazardous substances to include flammable petroleum products.** Id. The Farmer Mac Seller/Service Guide does not establish setback requirements for oil or gas wells.

## FHA

The Federal Housing Administration (FHA) defines standards for existing properties to be eligible for FHA mortgage insurance. Those standards provide:

- No existing dwelling may be located closer than 300 feet from an active or planned drilling site. This applies to the site boundary, not to the actual well location.
- Homes may be within 10 feet of abandoned wells if the State certifies the well is safely and permanently abandoned. If the state does not so certify, then the dwelling must be located at least 300 feet from the abandoned well.

HUD Handbook 4910.1 Minimum Property Standards for Housing (1994).

The FHA will not insure loans for new construction of single family one-to-four unit dwellings within 75 feet of an operating well, unless mitigation measures are taken to reduce noise and reduce the likelihood of spills or contamination. HUD Handbook 4150.2 Valuation Analysis for Single Family one to Four Unit Dwellings § 2-2.D.

## WHAT HARM CAN A GAS LEASE DO TO MY INSURABILITY?

*[FROM <http://www.nerdwallet.com/blog/insurance/2014/10/07/fracking-homeowners-insurance/>]*

“Nationwide Insurance made headlines in 2012 when an internal memo stating that its policies did not cover homeowners for fracking damage was leaked. In response to the fallout, Nationwide said that this was business as usual.

“Bob Hartwig of the Insurance Information Institute agrees: ‘All homeowners insurance policies exclude damage from such things as environmental contamination. This is nothing new.’

“Of course, pollution isn’t the only risk from fracking that activists have cited – and some of these risks may be covered. Homeowners with an earthquake endorsement can get coverage for earthquake damage, even if the quake is linked to fracking. ‘If there’s a fire or explosion, as a general rule, that would be covered,’ Hartwig adds.\*

**“This only applies to homeowners who live near fracking sites. For those who’ve leased their land – in effect, making it a business – insurance is more complicated.**

**“‘The liabilities arising from a business are not covered by a homeowners policy,’** Hartwig said. ‘Any agreements should be reviewed by an attorney to determine that the liability will be assumed by the company engaging in the activity.’”

*[FROM <http://www.nationwide.com/about-us/071312-nw-statement-on-fracking.jsp>]*

“Nationwide’s personal and commercial lines insurance policies were not designed to provide coverage for any fracking-related risks.

“Insurance works when a carrier can accurately price the coverage to match the risks. When information and claims experience are not available to fully understand the scope of a given risk, carriers aren’t able to price protection that would be fair to both the customer and the company.

“From an underwriting standpoint, we do not have a comfort level with the unique risks associated with the fracking process to provide coverage at a reasonable price. ... **Risks like natural gas and oil drilling are not part of our contracts, and this is common across the industry.**”

*[FROM <http://www.insureme.com/insurance/glossary/earthquake-insurance/>]*

“Earthquake coverage may be purchased from private insurance companies as an endorsement or a separate policy.\* Because of the claims risk involved, this type of policy usually includes a large deductible.”

*[FROM [http://www.shalereporter.com/industry/article\\_edaa4986-6576-11e2-8af1-001a4bcf6878.html](http://www.shalereporter.com/industry/article_edaa4986-6576-11e2-8af1-001a4bcf6878.html)]*

“If you want to be covered in the event of an earthquake or earth movement, the homeowner has to buy either a (rider) to their existing standard homeowners policy or a freestanding earthquake policy,”\* said Mike Barry, vice president of media relations at the Insurance Information Institute, a national nonprofit institute funded by the insurance industry.”

**\*BUT some companies choose not to accept the financial risks of offering earthquake insurance coverage in seismically active areas, or in areas undergoing gas & oil development.**