

Green Loans Are Taking Center Stage

A hot housing trend sweeping across the nation is the “net zero home,” bolstered by the U.S. Department of Energy’s Zero Energy Ready Home program. This is a certification for high-performance homes with renewable-energy resources to offset the property’s annual energy use.

According to the Department of Energy (DOE), these homes are 40% to 50% more efficient than the typical new home. In 1995, the DOE introduced the Energy Star certified home program and there are now about 2 million homes in the U.S. that have the Energy Star certification label.

Zero Energy Ready Homes, the latest step in the Energy Star program, are verified through independent analyses conducted by certified home-energy experts. Most often, reports are ordered by homeowners who are contemplating energy-related improvements. Depending upon the extent of the improvements, lenders will request a copy of a home’s energy report for applicants seeking an energy-efficient purchase or refinance mortgage program.

Energy raters are often certified by the Residential Energy Services Network (RESNET), and energy testing of homes is administered through a RESNET accredited-rating software program. The analysis produces a Home Energy Rating System (HERS) score, as well as a cost-benefit analysis and an expected financial return for the homeowner’s investment. The lower the HERS score, the more energy efficient the home is considered.

To help clients who are interested in lowering their utility costs — and to capitalize on these market opportunities — mortgage originators should look to utilize green-financing options. These loans are available through the government-sponsored enterprises (GSEs), the Federal Housing Administration (FHA) and the U.S. Department of Veterans Affairs (VA).

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GSE options

Freddie Mac’s GreenCHOICE program is one path for energy- and water-efficient home improvements. GreenCHOICE mortgages allow borrowers to finance up to 15% of the as-completed value of the property for environmentally friendly upgrades.

Basic energy-efficiency improvements with an aggregate cost of \$6,500 or less can be completed without obtaining an energy report. GreenCHOICE is available for both purchase and refinance transactions (but not cash-out refinances), and for many property types, including one- to four-unit homes and condominiums. Manufactured homes are eligible, as long as the energy-efficiency improvements do not impact the property’s structural integrity.

The program is available in tandem with other types of Freddie Mac fixed-rate and adjustable-rate mortgages, including Home Possible purchase transactions with downpayments of as little as 3%. Energy-efficient features that can be financed with the GreenCHOICE mortgage include solar panels, photovoltaic systems, low-flow water fixtures, high-efficiency appliances, or window and door replacements.

Fannie Mae’s HomeStyle Energy mortgage is another option for purchases and refinances. This product includes a loan-to-value ratio of up to 97%. Primary residences, second homes and investment properties are eligible, as well as homes with up to four units and manufactured homes. Similar to Freddie Mac’s GreenCHOICE mortgage, HomeStyle Energy financing is available for up to 15% of the as-completed appraised value of the home. Fannie Mae also allows borrowers to refinance previous energy-related upgrades, such as those financed with Property Assessed Clean Energy liens.

Borrowers must obtain an energy report to identify the recommended improvements to the property and the estimated cost savings. The cost of the energy report can be included in the eligible loan amount. Borrowers may finance up to \$3,500 in weatherization or water-efficiency improvements without obtaining an energy report. Other types of improvements, such as the installation of solar panels, wind-power devices or geothermal systems, as well as repairs and retrofits to improve resiliency against natural disasters, also do not require an energy report.

FHA and VA

The FHA offers energy-efficient mortgages for purchase and refinance transactions. The property must be the borrower’s primary residence and FHA will insure the mortgage plus the cost of energy-efficient improvements to be completed. A positive for the borrower is that the funds for improvements are excluded from the loan-qualification assessment.

The maximum “energy package” that can be added to the FHA loan amount is generally limited to the cost-effective improvements recommended by a home-energy assessment. In other cases, however, these additional costs may be restricted to the lesser of 5% of the home’s as-completed appraised value; 115% of the median area price of a single-family home; or 150% of the national conforming loan limit.

FHA allows the borrower’s debt-to-income ratio to increase by two percentage points due to the savings achieved by the energy improvements. A qualified energy rater must prepare an analysis of the potential savings for each type of improvement. The agency has a policy for solar and wind technologies stating that borrowers can have a higher mortgage amount to have these systems installed, as long as that is accomplished at the time of the home purchase or refinance. FHA also allows up to \$3,500 in financing for basic weatherization items, including thermostats and insulation.

The VA insures energy-efficient purchase and refinance mortgages. Acceptable improvements include — but are not limited to — solar-powered heating, cooling and water systems; insulation; storm windows and doors; weather-proofing; heat pumps; and furnace up-grades. Lenders must evaluate whether proposed improvements are reasonable for the home in question.

As part of the VA appraisal process, borrowers will be given notice that they may wish to have a qualified party complete an energy audit. Mortgage financing may be increased by up to \$3,000 based solely on the documented costs without an energy audit, and by up to \$6,000 with an audit as long as the increase in the borrower’s monthly payment does not exceed the estimated reduction in their monthly utility costs. Improvements of more than \$6,000 are subject to a value determination from the VA.

Many types of energy-improvement features will save money while shrinking the homeowner’s carbon footprint.

Popular features

Significantly reducing a home’s energy consumption can take time, but each step of the way can make a difference. Many types of energy-improvement features will save money while shrinking the homeowner’s carbon footprint.

Solar photovoltaic panels, for example, can be placed in many places to convert sunlight into electricity. Solar water-heating panels contain water-based fluid that transmit the sun’s heat into the home’s hot-water tank. Wind turbines mechanically generate electricity that must be stored in batteries. Residential use of wind power is generally found in rural locations, but wildlife protection should be considered.

Geothermal technology uses the thermal properties below the earth to heat and cool homes, utilizing a ground-source heat pump that can reduce energy consumption by up to 65%. Geothermal technology can operate in any climate, although the most recent data from DOE shows that the bulk of these devices are located in cold-weather states such as Illinois, Indiana, Michigan, Minnesota, Ohio and Pennsylvania.

Energy Star ratings can apply to an entire home or they can be found on a wide variety of devices. These include heating and cooling systems such as thermostats, air conditioners, heat pumps, boilers, furnaces and ventilation fans; appliances such as refrigerators, freezers, dishwashers, washers and dryers; and other areas of the home, including windows, doors, roofs, insulation, light fixtures and bulbs, and smart-home energy-management systems.



In addition to the financing programs available to mortgage originators and their clients, there are thousands of incentives available to consumers who conserve energy, including federal tax credits and rebates. The Bipartisan Budget Act of 2018, for example, reinstated a bill that allows homeowners to apply for a rebate for the purchase of fuel cells, geothermal heat pumps and small wind turbines.

In 2020, the federal income-tax credit is 26% of the cost of these systems. Information about energy ratings, types of improvements and program listings for every state can be found through a DOE database at dsireusa.org.

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