Accessory Dwelling Unit (ADU) Expansion

Freddie Mac's ADU policies provide multiple options for adding an ADU to a home or financing a purchase with the intention to rent or build an ADU, including allowing the borrower to use rental income to qualify. Our policies allow you to offer ADU flexibility on any Freddie Mac mortgage, giving your customers more choice in the purchase or renovation financing process.

This resource provides a summary of requirements that must be met for mortgages secured by properties with an ADU.

First things first: What is an ADU?

An ADU can be part of the main home, such as a converted basement, an addition; above a garage, or a detached structures built on the main home's lot, which could include a manufactured home.

Bottom line… **an ADU is an additional living area that:**

- ✓ Includes a kitchen
- ✓ Includes a separate entrance
- ✓ Contributes less to the value of the property than the primary dwelling unit
- ✓ Includes a bathroom
- ✓ Independent of the primary dwelling unit
- ✓ Subordinate in living area

The following tables provide information on our eligibility and appraisal requirements for a property with an ADU, and requirements on using rental income generated from an ADU on a subject 1-unit Primary Residence.

Eligibility Requirements for a Property with an ADU

Topic	General Requirements
Property Type	Only one ADU is allowed on 1-, 2- and 3-unit properties.
Transaction Type	▪ Purchase ▪ No cash-out refinance ▪ Cash-out refinance **Note:** A cash-out refinance is not allowed when using rental income generated from an ADU on a subject 1-unit primary residence.

Topic	General Requirements
Occupancy Type	▪ Primary residence ▪ Second home ▪ Investment property (Reminder: Rental income generated from the borrower's second home may not be used as stable monthly income.)
Eligible Mortgages	Any Freddie Mac offering is eligible. **Note:** A CHOICERenovation® Mortgage provides an option to use a no cash-out refinance mortgage to pay off short-term financing that financed ADU renovations, including the addition or renovation of an ADU that is completed prior to the note date.
Ineligible Mortgages	Mortgages secured by: ▪ A 2- to 3-unit property with an ADU that does not comply with zoning and land use requirements. ▪ A 1-, 2-, or 3-unit property with two or more ADUs. ▪ A 4-unit property with one or more ADUs.
Manufactured Home as an ADU	A 1-, 2-, or 3-unit property that contains a manufactured home as an ADU is eligible if the requirements in Section 5601.2(d) and 5703.2 and 5703.7 are met. The subject property cannot be a manufactured home, unless the subject property is a CHOICEHome®.

Appraisal Requirements (Guide Section 5601.2)	

General	▪ The appraiser must identify whether the subject property has an ADU and report the appraisal on the appropriate report form.
	 Consider:
	    ○ Zoning and land use requirements.
	    ○ All property characteristics, specifically, the unit's utility and the property's highest and best use.
	    ○ Refer to the ADU FAQs for more information.

Appraisal Requirements (Guide Section 5601.2)		
Appraisal Forms	**1-unit Property with an ADU**	**2- to 3-unit Property with an ADU**
	▪ Form 70 (Uniform Residential Appraisal Report) ▪ Form 70D (Uniform Residential Appraisal Report – Desktop), if eligible	▪ Form 72 (Small Residential Income Property Appraisal Report) **Note:** When Form 72 is utilized for a 2- or 3-unit property with an ADU, the ADU is included as an additional unit.
ADU Description	The appraiser must describe the ADU in the appraisal report and reflect any effect the ADU has on the market value or marketability of the subject property. Describe: • General condition • Square footage of the ADU's living area • Total room count • An indication ADU is allowed per zoning and • # of bedrooms land use requirements • # of baths Reminder: If the appraiser has identified an ADU, confirm the "Accessory Unit" box has been checked on the appraisal report.		

Topic	General Requirements
Zoning Requirements	**Comparable Sales** | **Properties with Legal or Legal Non-Conforming Zoning Compliance or Locations without Zoning**	**Properties with Illegal Zoning Compliance** | |---|---|
The appraisal report must include the following: ▪ At least **one** comparable sale with an ADU, when available, to demonstrate the property's conformity and marketability to its market area. ▪ If a recent comparable sale with an ADU is not available in the subject neighborhood, the appraiser can use an older sale with an ADU from the subject neighborhood or a sale with an ADU from a competing neighborhood as a comparable sale or as supporting market data. The appraiser may always use more than three comparable sales, including contract sales (pending sales) and/or current listings, to justify and support any adjustments and opinion of market value, as long as at least three are actual closed (settled) sales. ▪ If a comparable sale with an ADU is not available, the appraiser can use a comparable sale in the subject neighborhood without an ADU as long as the appraiser can justify and support such use in the appraisal report. Freddie Mac will purchase eligible mortgages secured by a property with an ADU if the appraiser can develop an accurate opinion of market value for the property.	▪ The subject property must be a 1-unit property with an ADU. ▪ The "Site" section of the appraisal report indicates that the ADU does not comply with zoning and land use requirements. ▪ At least two comparable sales with an ADU must be included in the appraisal report. The ADU of each comparable sale must also be non-compliant with the zoning and land use requirements (illegal zoning) to demonstrate the marketability of the subject property to its market area; and ▪ The Seller confirms that the existence of the ADU will not jeopardize future hazard insurance claims. | **Note:** If using rental income from an ADU on a subject 1-unit primary residence to qualify, refer to Section 5306.3 for comparable sales and rental requirements.

Topic	Requirements (Guide Section 5306.3)
Transaction Type	▪ Purchase ▪ No cash-out refinance
Rental Income Calculation (Subject 1-unit primary residence with an ADU)	▪ Rental income from ADU used for qualifying cannot exceed **30%** of the **total stable monthly income** used to qualify the borrower.

Rental Income Documentation	Net Rental Income Calculation
Lease	**75%** of the gross monthly rent or gross monthly market rent.
ADU rental analysis	**Note:** The 25% adjustment is made to compensate for vacancies, operating and maintenance costs and any other unexpected expenses.
Schedule E	Calculate the net rental income from **Schedule E** using Form 92. Net Rental Income Calculations-Schedule E or a similar alternative form.

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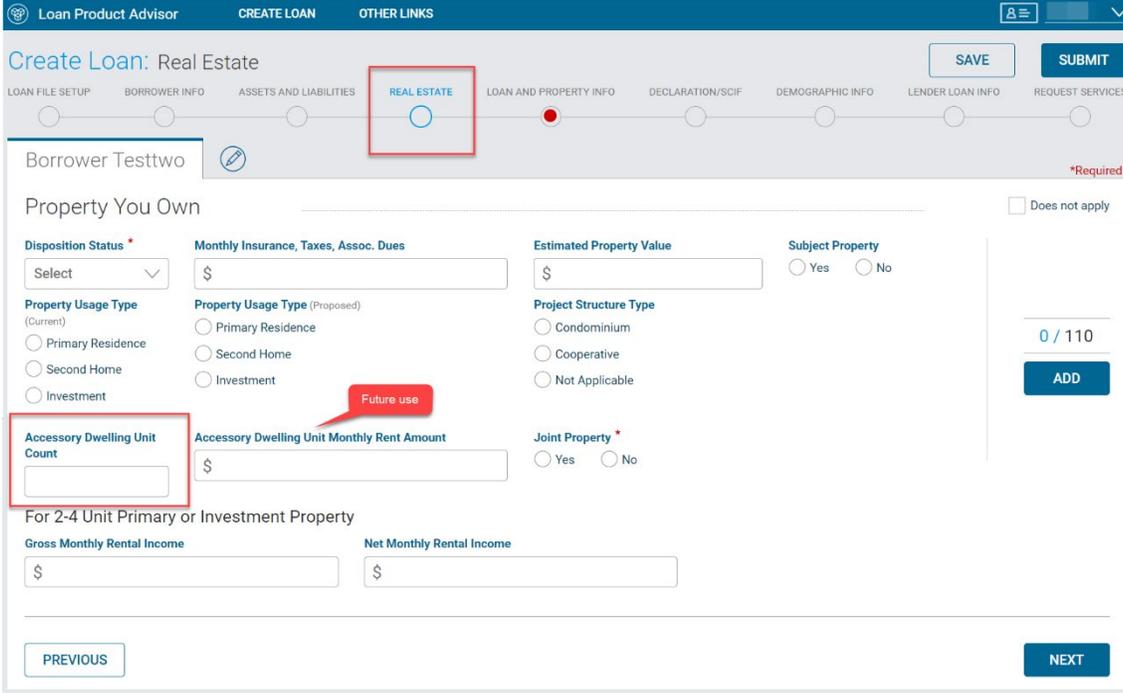| Topic	Requirements (Guide Section 5306.3)		
Rental Income Documentation (Subject 1-unit primary residence with an ADU)	**Purchase**	**No Cash-out Refinance**	
		ADU placed in service in **current** calendar year	ADU owned in **prior** calendar year
	- If a lease[1] is **available**, then the lease must be used to determine the net rental income, and - ADU rental analysis, as described in Section 5306.3(b)(iii), must support the income reflected on the lease. If the lease is not available, the ADU rental analysis must be used to determine the net rental income.	- A lease[1] must be used to determine the net rental income, and - ADU rental analysis, as described in Section 5306.3(b)(iii). Must support the income reflected on the lease, and - The loan file must contain documentation reflecting the date the ADU was placed in service.	- The borrower's complete federal income tax returns (IRS Form 1040), including Schedule E for the most recent year must be used to determine the net rental income, except as stated below: A lease[1] and ADU rental analysis as described in Section 5306.3(b)(iii) may be used if: - The property was out of service for anytime period in the prior year and the loan file contains a documented event such as a renovation and the Schedule E supports this by a reduced number of days in use and reflects repair costs, or - The property was purchased later in the calendar year and the Schedule E supports this by a reduced number of days in use. In either of the above instances, an ADU rental analysis is required to support the income reflected on the lease.
	[1] When a lease is used, it must be current and fully executed with a minimum original term of one year. If the lease is documented as assigned from the property seller to the borrower and is in the automatically renewable month-to-month phase of an original one-year (or longer) term lease, then a month-to-month is acceptable.		
Landlord Education (Subject 1-unit primary residence with an ADU)	- Purchase transactions only ✓ At least one qualifying borrower must participate prior to the Note Date unless the borrower has a minimum of one-year investment property management experience or ADU rental management experience. ✓ Must not be provided by an interested party to the transaction, the originating lender or the Seller. ✓ A copy of the certificate evidencing the successful completion of the program must be retained in the loan file.		

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Topic	Requirements (Guide Section 5306.3)

Appraisal Requirements

When Using Rental Income

(Subject 1-unit primary residence with an ADU)

- When rental income generated from the ADU is used to qualify the borrower(s), an appraisal report is required and must provide the following information on the ADU:
  - ✓ General condition of unit.
  - ✓ Square feet of finished area.
  - ✓ Total number of rooms including number of bedrooms and baths.
  - ✓ The appraisal report must indicate the ADU is allowed per zoning and land use requirements (e.g., legal, legal non-conforming, no zoning).
  - ✓ The appraiser must provide at least one comparable sale with an ADU that is rented to support area ADU rentals.
  - ✓ The rental analysis must include a minimum of three comparable rentals to support the opinion of market rent applicable to the ADU and at least one of the comparable rentals must include a rented ADU to support the market rent for ADUs.

    Note: The appraiser may provide this rental analysis data in narrative form within the appraisal report or by attaching a separate rent schedule to the appraisal report.

Refer to the Appraisal Requirements section, and Guide Section 5601.2 for additional requirements for a property with an ADU.

Note: Effective April 3, 2023 when rental income generated by an ADU is used to qualify the borrower, LPA will not grant eligibility for automated collateral evaluation (ACE) or an ACE+ Property Data Report (PDR).

Loan Product Advisor

(Subject 1-unit primary residence with an ADU)

Use the following steps to enter rental income from an ADU on a subject 1-unit primary residence and the number of ADUs on the subject property.

Data Field/Unique ID	Data Entry
Income Type (258.00)	Provide the value "AccessoryUnitIncome" for one borrower only.
Current Income Monthly Total Amount (256.00)	Provide the net rental income amount (reminder the net rental income cannot exceed 30% of the total stable monthly income used to qualify the borrower).
LPA specification version 5.3.00	
Purchase: Accessory Dwelling Unit Count (71.70)	Provide the number of ADUs on a subject property even if ADU income is not being used to qualify.
Refinance (Property You Own): Accessory Dwelling Unit Count (33.60)	Provide the number of ADUs on a subject property even if ADU income is not being used to qualify.
Note: LPA will return a purchase restriction if the ADU rental income exceeds the total stable monthly income used to qualify.	

Topic	Requirements (Guide Section 5306.3)

	If you access LPA using Freddie Mac Loan Advisor® single sign-on portal:
	
	1. Select "Borrower Info" Metro Stop.
	2. Under **Other Income**, select **Income Type** as "Accessory Unit Income".
	3. Enter the net rental income amount for **Monthly Income** (reminder the net ADU rental income cannot exceed 30% of the total stable monthly income used to qualify the borrower).
	4. Provide the number of ADUs on a subject property even if accessory unit income is not being used to qualify, in the "Accessory Dwelling Unit Count" field.
	    a. **Purchase:** Select "Loan and Property Info" Metro Stop. Enter the number of ADUs.
	    b. **Refinance**: select "Real Estate Owned" Metro stop. Enter the number of ADUs on the subject 1-unit property.

Topic	Requirements (Guide Section 5306.3)

	Property Type	ADU Rental Income	ADU Count
Additional Information: Other property types with ADU rental income	Subject **investment** property with an ADU	Include ADU rental income in the total rental income amount for each real estate owned.	Enter the number of ADUs on the subject property.
	Non-subject properties with an ADU	Include ADU rental income in the total rental income amount for each real estate owned.	Do **not** enter ADU count.
	• Subject **2- and 3-unit** property with an ADU • Second home with an ADU	Not permitted.	Enter the number of ADUs on the subject property.

Delivery Requirements	Loan Selling Advisor: A mortgage secured by a 1-unit primary residence where rental income from an ADU is used to qualify the borrower you must deliver the valid value of "J66" for ULDD Data Point, *Investor Feature Identifier* (Sort ID 368).

For additional questions and support reach out to our **Customer Support Contact Center, 800-FREDDIE,** or access the following resources for more information:

Webinar	ADU webpage	Online Reference Tool	FAQs

This information is not a replacement or substitute for the requirements in the Freddie Mac *Single-Family Seller/Servicer Guide* or your other Purchase Documents.   *© 2023 Freddie Mac*

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