SECTION 184 INDIAN HOUSING LOAN GUARANTEE PROGRAM POLICY HANDBOOK

Chapter II – Origination to Final Underwriter Approval

D. MANUALLY UNDERWRITING THE BORROWER

DG Lenders must manually underwrite all loans intended for the Section 184 Program. For transactions with complex factors, the DG Underwriter **may** provide a narrative to the file on the final signed and dated Mortgage Credit Analysis Worksheet.

1. Credit Requirements

a. General Credit Requirements; Debt-To-Income Ratios

Lenders must analyze the Borrower's credit history, liabilities, and debts to determine creditworthiness.

Lenders must not use a Borrower's credit score when evaluating the Borrower for creditworthiness.

Without compensating factors, to qualify for a Section 184 loan, the maximum Total Fixed Payments to Effective Income Ratio, or DTI, is 41 percent. The maximum DTI may be up to 45 percent with compensating factors. Discussion regarding compensating factors is in Subsection D.4.viii.

Lenders must obtain a Tri-Merged Credit Report (TRMCR) or a Residential Mortgage Credit Report (RMCR) from an independent consumer reporting agency for each Borrower who will be obligated on the mortgage Note. Lenders may obtain a joint report for individuals with joint accounts.

Lenders must obtain a credit report for a non-borrowing spouse who resides in a community property state, or if the Eligible Property is located in a community property state. The credit report must indicate the non-borrowing spouse's SSN, where an SSN exists, was matched with the SSA, or the

Lender must either provide separate documentation indicating that the SSN was matched with the SSA or provide a statement that the non-borrowing spouse does not have an SSN. Where an SSN does not exist for a non-borrowing spouse, the credit report must contain, at a minimum, the non-borrowing spouse's full name, date of birth, and previous addresses for the last two years.

Lenders are not required to obtain a credit report for a Streamline Refinance with or without an appraisal transaction. Lenders may choose to obtain a mortgage only credit report to meet the payment history requirement.

b. Types of Credit History

If a traditional credit report, (a Tri-Merged Credit Report (TRMCR) or a Residential Mortgage Credit Report (RMCR)), is available, Lenders must use a traditional credit report. However, if a traditional credit report is not available, Lenders must develop the Borrower's credit history using the requirements for Non-traditional and Insufficient Credit.

i. Traditional Credit

If the TRMCR or RMCR generates a credit score, Lenders must utilize traditional credit history.

If the TRMCR or RMCR does not generate a credit score, Lenders must utilize Non-Traditional Credit history.

a) Requirements for Credit Report

Credit reports must obtain all information from at least two credit repositories pertaining to credit, residence history, and public records information; be in an easy to read and understandable format; and not require code translations. The credit report may not contain whiteouts, erasures, or alterations. Lenders must retain copies of all credit reports.

The credit report must include:

- the name of the Lender ordering the report;
- the name, address, and telephone number of the consumer reporting agency;
- the name and SSN of each Borrower; and
- the primary repository from which any particular information was pulled, for each account listed.
- A truncated SSN is acceptable for Section 184 Program loan purposes provided that the loan application captures the full nine-digit SSN.

The credit report must also include:

- all inquiries made within the last 90 Days;
- all credit and legal information not considered obsolete under the Fair Credit Reporting Act (FCRA), including

- information for the last seven years, which consumer reporting agencies have reported as verified and currently accurate, regarding: bankruptcies, Judgments, lawsuits, foreclosures, tax liens; and

- for each Borrower debt listed: the date the account was opened, high credit amount, required monthly payment amount, unpaid balance, and payment history.

b) Updated Credit Report or Supplement to the Credit Report

Lenders must obtain an updated credit report or supplement if Lenders identifies inconsistencies between any information in the loan file and the original credit report.

c) Credit Information Not Listed on Credit Report

Lenders must develop credit information separately for any open debt listed on the loan application but not referenced in the credit report by using the procedures for Independent Verification of Non-traditional Credit Providers.

d) Specific Requirements for Residential Mortgage Credit Report

In addition to meeting the general credit report requirements, the RMCR must:

- provide a detailed account of the Borrower's employment history

- verify each Borrower's current employment and income through an interview with the Borrower's employer or explain why such an interview was not completed

- contain a statement attesting to the certification of employment for each Borrower and the date the information was verified; and

- report a credit history for each trade line within 90 Days of the credit report for each account with a balance.

ii. Non-traditional and Insufficient Credit

For Borrowers without a conventional credit history (as reported by the three major credit bureaus) or a minimum conventional credit history, Lenders must either obtain a Non-Traditional Mortgage Credit Report (NTMCR) from a credit reporting company or independently develop the Borrower's credit history using the requirements outlined below. Non-traditional Credit may not be used to replace or offset derogatory credit shown on a traditional credit report.

a) Non-Traditional Mortgage Credit Report

(1) Definition

A Non-Traditional Mortgage Credit Report (NTMCR) refers to a type of credit report designed to access the credit history of a Borrower who does not have the types of trade references that appear on a traditional credit report.

(2) Standard

An NTMCR is used either as:

- a substitute for a TRMCR or an RMCR; or
- a supplement to a traditional credit report that has an insufficient number of trade items reported to meet Section 184 requirements.

Lenders may use an NTMCR developed by a credit reporting agency that verifies the following information for all non-traditional credit references:

- the existence of the credit providers;
- that the credit was actually extended to the Borrower; and
- the creditor has a published address or telephone number.

The NTMCR must not include subjective statements such as "satisfactory" or "acceptable," and must be formatted in a similar fashion to traditional references, and provide the:

- creditor's name;
- date of opening;
- high credit;
- current status of the account;
- 12-month history of the account;
- required monthly payment;
- unpaid balance; and
- payment history in the delinquency categories (for example, 0x30 and 0x60).

b) Independent Verification of Non-Traditional Credit Providers

Lenders may independently verify the Borrower's credit references by documenting the existence of the credit provider and that the provider extended credit to the Borrower.

c) Sufficiency of Credit References

When Lenders utilizes independent verification of the Non-traditional Credit Providers, Lenders must obtain the most recent 12 months of canceled checks, or equivalent proof of payment, demonstrating the timing of payment to the credit provider.

The credit history must include two credit references, including at least one of the following:

- rental housing payments in compliance with 2(b) above;
- telephone service; or
- a utility company reference (when not included in the rental housing payment), from one of the following: gas, electricity, water, television service, or internet service.

If Lenders cannot obtain two credit references from the list above, the Lender may use the following sources of unreported recurring debt:

- insurance premiums not payroll deducted (for example, medical, auto, life, renter's insurance);

- payment to childcare providers made to businesses that provide such services;

- school tuition;

- retail store credit cards (for example, from department, furniture, appliance stores, or specialty stores);

- rent-to-own (for example, furniture, appliances);

- payment of that part of medical bills not covered by insurance;

- a documented 12-month history of savings evidenced by regular deposits resulting in an increased balance to the account that: were made at least quarterly, were not payroll deducted, and caused no Insufficient Funds (NSF) checks;

- an automobile lease;

- a personal loan from an individual with repayment terms in writing and supported by canceled checks to document the payments; or

- a documented 12-month history of payment by the Borrower on an account for which the Borrower is an authorized user.

c. Evaluating Credit History

i. General Credit

Lenders must examine the Borrower's overall pattern of credit behavior, not just isolated unsatisfactory or slow payments, to determine the Borrower's creditworthiness.

Lenders must not consider the credit history of a non-borrowing spouse, when utilizing the liability payment in Community Property States.

ii. Types of Payment Histories

Lenders must evaluate the Borrower’s payment histories in the following order: (1) previous housing expenses and related expenses, including utilities; (2) installment debts; and (3) Revolving Charge Accounts.

a) Satisfactory Credit

Lenders may consider a Borrower to have an acceptable payment history if the Borrower has made all housing and installment debt payments on time for the previous 12 months and has no more than two 30-Day late Mortgage Payments or installment payments in the previous 24 months.

Lenders may approve the Borrower with an acceptable payment history if the Borrower has no major derogatory credit on Revolving Charge Accounts in the previous 12 months.

Major derogatory credit excludes Medical Collections. On Revolving Accounts, major derogatory credit must include any payments made more than 90 Days after the due date, or three or more payments more than 60 Days after the due date.

b) Payment History Requiring Additional Analysis

If a Borrower’s credit history does not reflect satisfactory credit as stated above, the Borrower’s payment history requires additional analysis.

Lenders must analyze the Borrower’s delinquent accounts to determine whether late payments were based on a disregard for financial obligations, an inability to manage debt, or extenuating circumstances. The DG

Lender must comment on the final signed and dated MCAW. Any explanation or documentation of delinquent accounts must be consistent with other information in the file.

The DG Underwriter may only approve a Borrower with a credit history not meeting the satisfactory credit history above if the underwriter has documented the delinquency was related to extenuating circumstances.

iii. Housing Obligations

a) Definition

Housing Obligation refers to the monthly payment due for rental and/or Properties owned.

b) Standard

A Housing Obligation is considered delinquent if not paid within the month due.

A Borrower who was granted a mortgage payment forbearance and continues to make payments as agreed under the terms of the original Note is not considered delinquent or late and shall be treated as if not in forbearance provided the Forbearance Plan is terminated at or prior to closing.

Lenders must determine the Borrower's Housing Obligation payment history through:

- the credit report;
- verification of rent received directly from the landlord (for landlords with no Identity of Interest with the Borrower);
- verification of Mortgage received directly from the Servicer; or
- a review of canceled checks that cover the most recent 24-month period.

Lenders must verify and document the previous 24 months' housing history.

For Borrowers who indicate they are living rent-free, Lenders must obtain verification from the property owner where they are residing that the Borrower has been living rent-free and the amount of time the Borrower has been living rent-free.

For both purchase and no cash-out refinance transactions, a Mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the period of modification in determining late housing payments. In addition, where a Mortgage has been modified, the Borrower must have made at least six payments under the modification agreement to be eligible for a no-cash out refinance.

A Mortgage that was subject to mortgage payment forbearance must utilize the Mortgage Payment history in accordance with the Forbearance Plan for the period of the forbearance in determining late housing payments.
Any Borrower who is granted a forbearance and is otherwise performing under the terms of the Forbearance Plan is not considered to be delinquent for purposes of credit underwriting.

c) Required Documentation

Where a Mortgage reflects payments under a modification or Forbearance Plan within the 12 months prior to case number assignment, Lenders must obtain: a copy of the modification or Forbearance Plan, and evidence of the payment amount and date of payments during the forbearance term.

A Forbearance Plan is not required if the forbearance was due to the impacts of the COVID-19 National Emergency.

iv. Collection Accounts

a) Definition

A Collection Account is a Borrower's loan or debt that has been submitted to a collection agency through a creditor.

b) Standard

Lenders must determine if collection accounts were a result of:

- the Borrower's disregard for financial obligations;
- the Borrower's inability to manage debt; or
- extenuating circumstances.

When the credit report used in the analysis shows cumulative outstanding collection account balances of $2,000 or greater, the Lender must:

- verify that the debt is paid in full at the time of or prior to settlement using an acceptable source of funds;

- verify that the Borrower has made payment arrangements with the creditor; or

- if a payment arrangement is not available, calculate the monthly payment using 5 percent of the outstanding balance of each collection and include the monthly payment in the Borrower's DTI ratio.

Collection accounts of a non-borrowing spouse in a community property state must be included in the $2,000 cumulative balance and analyzed as part of the Borrower's ability to pay all collection accounts, unless specifically excluded by state law.

c) Required documentation

DG Lenders must document reasons for approving the loan when the Borrower has any collection accounts.

The Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account. The explanation and supporting documentation must be consistent with other credit information in the file.

v. Charge Off Accounts

a) Definition

Charge Off Account refers to a Borrower's loan or debt that has been written off by the creditor.

b) Standard

Lenders must determine if Charge Off Accounts were a result of:

- the Borrower's disregard for financial obligations.
- the Borrower's inability to manage debt; or
- extenuating circumstances.

c) Required Documentation

Lenders must document reasons for approving a Mortgage when the Borrower has any Charge Off Accounts.

The Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding Charge Off Account. The explanation and supporting documentation must be consistent with other credit information in the file.

vi. Disputed Derogatory Credit Accounts

a) Definition

Disputed Derogatory Credit Account refers to disputed Charge Off Accounts, disputed collection accounts, and disputed accounts with late payments in the last 24 months.

b) Standard

Lenders must analyze the documentation provided for consistency with other credit information to determine if the derogatory credit account should be considered in the underwriting analysis.

The following items may be excluded from consideration in the underwriting analysis:

- disputed medical accounts; and
- disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use provided Lenders includes a copy of the police report or other documentation from the creditor to support the status of the account in the mortgage file.

c) Required Documentation

If the credit report indicates that the Borrower is disputing derogatory credit accounts, the Borrower must provide a letter of explanation and documentation supporting the basis of the dispute.

If the disputed derogatory credit resulted from identity theft, credit card theft or unauthorized use balances, the Lenders must obtain a copy of the police report or other documentation from the creditor to support the status of the accounts.

vii. Judgments

a) Definition

Judgment refers to any debt or monetary liability of the Borrower, and the Borrower's spouse in a community property state unless excluded by state law, created by a court, or other adjudicating body.

b) Standard

Lenders must verify that court-ordered Judgments are resolved or paid off prior to or at closing.
Judgments of a non-borrowing spouse in a community property state must be resolved or paid in full prior to or at closing, except for obligations excluded by Tribal or state law.

Lenders must determine if the Judgment was a result of:

- the Borrower's disregard for financial obligations;
- the Borrower's inability to manage debt; or
- extenuating circumstances.

c) Exception

A Judgment is considered resolved if the Borrower has entered into a valid agreement with the creditor to make regular payments on the debt, the Borrower has made timely payments for at least three months of scheduled payments and the Judgment will not supersede the Section 184 lien. The Borrower cannot prepay scheduled payments to meet the required minimum of three months of payments.

Lenders must include the payment amount in the agreement in the calculation of the Borrower's DTI ratio.

Lenders must obtain a copy of the agreement and evidence that payments were made on time in accordance with the agreement.

d) **Required Documentation**

Lenders must provide the following documentation:

- evidence of payment in full, if paid prior to settlement;
- the payoff statement, if paid at settlement;
- the payment arrangement with creditor, if not paid prior to or at settlement, and a subordination agreement for any liens existing on title.

In addition to the above:

- A written letter of explanation from the applicant.

viii. Bankruptcy

a) **Standard: Chapter 7**

A Chapter 7 bankruptcy (liquidation) does not disqualify a Borrower from obtaining a Section 184 loan if, at the time of case number assignment, at least two years have elapsed since the date of the bankruptcy discharge. During the most recent two years, the Borrower must have:

- reestablished good credit; or

- chosen not to incur new credit obligations.

An elapsed period of less than two years, but not less than 12 months, may be acceptable, if the Borrower:

- can show that the bankruptcy was caused by extenuating circumstances beyond the Borrower's control; and

- has since exhibited a documented ability to manage their financial affairs in a responsible manner.

b) **Standard: Chapter 13**

A Chapter 13 bankruptcy does not disqualify a Borrower from obtaining a Section 184 Guaranteed Loan, if at the time of case number assignment at least 12 months of the payout period under the bankruptcy has elapsed.

Lenders must determine that during the most recent 12 months, the Borrower's payment performance has been satisfactory, and all required payments have been made on time; and the Borrower has received written permission from bankruptcy court to enter into the mortgage transaction.

c) Required Documentation

If the credit report does not verify the discharge date or additional documentation is necessary to determine if any liabilities were discharged in the bankruptcy, the Lenders must obtain the bankruptcy and discharge documents.

Lenders must also document that the Borrower's current situation indicates that the events which led to the bankruptcy are not likely to recur.

ix. Foreclosures

a) Definition

Foreclosure refers to the actions taken by the entity that is named on the Promissory Note or any successor or assigns to take possession of the property guaranteed under the mortgage.

b) Standard

Three Year Period. A Borrower is ineligible for a Section 184 loan when the Borrower had a mortgage/loan complete foreclosure on a non-Section 184 Guaranteed Loan or the Borrower had a foreclosure on a Section 184 Guaranteed Loan, which did not result in any claim payment by ONAP.

The period of ineligibility shall be three years. The three-year period begins on the date the title to the Property transferred to the foreclosing entity.

A DG Lender may submit a Case Number Request for the Borrower on or after the expiration of the three-year waiting period.

Seven Year Period. A Borrower is ineligible for a Section 184 loan when the Borrower had a Section 184 Guaranteed Loan foreclosed upon which resulted in a claim payment by HUD. The period of ineligibility shall be seven years. The seven-year period begins on the date title to the Property transferred to the foreclosing entity.

A DG Lender may submit a Case Number Request for the Borrower on or after the expiration of the seven-year waiting period.

c) Required Documentation

If the credit report does not indicate the date of the foreclosure, the DG Lender must obtain the Closing Disclosure, deed or other legal documents evidencing the date the foreclosed property transferred.

x. Pre-Foreclosure Sales (Short Sales), and Lease-in-Lieu/Deed-in-Lieu

a) Definition

Pre-Foreclosure Sales, also known as Short Sales, refer to the sales of real estate that generate proceeds that are less than the amount owed on the Property and the lien holders agree to release their liens and forgive the deficiency balance on the real estate.

A Lease-in-Lieu (LIL) or a Deed-in-Lieu (DIL) of Foreclosure is a loss mitigation home disposition option in which a Borrower voluntarily offers the lease/deed to the Holder in exchange for a release from all obligations under the Mortgage.

b) Standard

<u>Three Years</u>. A Borrower is ineligible for a Section 184 loan when the Borrower had a Short Sale or executed a LIL/DIL on a non-Section 184 Guaranteed Loan or the Borrower had a Short Sale or executed a LIL/DIL on a Section 184 Guaranteed Loan, which did not result in a claim payment by HUD.

The period of ineligibility shall be three years. The three-year period begins on the date title to the Property transferred to the purchaser or Holder.

A DG Lender may submit a Case Number Request for the Borrower on or after the expiration of the three-year waiting period.

<u>Five Years</u>. A Borrower is ineligible for a Section 184 loan when the Borrower had a Short Sale or executed a LIL/DIL on a Section 184 Guaranteed Loan, which resulted in a claim

payment by HUD.

The period of ineligibility shall be five years. The five-year period begins on the date title to the Property transferred to the purchaser or Holder.

A DG Lender may submit a Case Number Request for the Borrower on or after the expiration of the five-year waiting period.

c) Exception for Extenuating Circumstances to the Three-Year Period

DG Lenders may grant an exception to the three-year requirement if the Short Sale or completed LIL/DIL was the result of documented extenuating circumstances that were beyond the control of the Borrower, such as a serious illness or death of a wage earner, and the Borrower has reestablished good credit since the Short Sale/LIL/DIL.

Divorce is not considered an extenuating circumstance. An exception may, however, be granted where a Borrower's Mortgage was current at the time of the Borrower's divorce, the ex-spouse (not the Borrower) received the Property, and there was a subsequent Short Sale by the ex-spouse.

The inability to sell the Property due to a job transfer or relocation to another area does not qualify as an extenuating circumstance.

d) Required Documentation

If the credit report does not indicate the date of the Short Sale, LIL/DIL, Lenders must obtain the Closing Disclosure, deed or other legal documents evidencing the date of property transfer.

If the Short Sale/LIL/DIL was the result of a circumstance beyond the Borrower's control, and an exception to the three-year period applies, Lenders must obtain an explanation of the circumstance and document that the circumstance was beyond the Borrower's control.

xi. Credit Counseling/Payment Plan

Participating in a consumer credit counseling program does not disqualify a Borrower from obtaining a Section 184 Guaranteed Loan, provided Lenders documents that:

- one year of the payout period has elapsed under the plan;
- the Borrower's payment performance has been satisfactory, and all required payments have been made on time; and
- the Borrower has received written permission from the counseling agency to enter into the mortgage transaction.

d. Evaluating Liabilities and Debts

i. General Liabilities and Debts

a) Standard

Lenders must determine the Borrower's monthly liabilities by reviewing all debts listed on the credit report, Fannie Mae Form 1003/Freddie Mac Form 65, *Uniform Residential Loan Application (URLA)*, and required documentation.

All applicable monthly liabilities must be included in the qualifying ratio. Closed-end debts do not have to be included if they will be paid off within 10 months from the date of closing and the cumulative payments of all such debts are less than or equal to 5 percent of the Borrower's gross monthly income. The Borrower may not pay-down any balance to meet the 10-month requirement.

Accounts for which the Borrower is an authorized user must be included in a Borrower's DTI ratio unless Lenders can document that the primary account holder has made all required payments on the account for the previous 12 months. If less than three payments have been required on the account in the previous 12 months, the payment amount must be included in the Borrower's DTI.

Negative income must be subtracted from the Borrower's gross monthly income, and not treated as a recurring monthly liability unless otherwise noted.

Loans secured against deposited funds, where repayment may be obtained through extinguishing the asset and these funds are not included in calculating the Borrower's assets, do not require consideration of repayment for qualifying purposes.

b) Required Documentation

Lenders must document that the funds used to pay off debts prior to closing came from an acceptable source, and the Borrower did not incur new debts that were not included in the DTI ratio.

ii. Undisclosed Debt and Inquiries

a) Standard

When a debt or obligation is revealed during the application process that was not listed on the loan application and/or credit report, Lenders must:

- verify the actual monthly payment amount;
- include the payment amount in the agreement in the Borrower's monthly liabilities and debt; and
- determine that any unsecured funds borrowed were not/will not be used for the Borrower's MRI.

Lenders must obtain a written explanation from the Borrower for all inquiries shown on the credit report that were made in the last 90 Days.

b) Required Documentation

Lenders must document all undisclosed debt and support for its analysis of the Borrower's debt.

iii. Federal Debt

a) Definition

Federal Debt refers to debt owed to the federal government.

b) Standard

Lenders must include the debt. The amount of the required payment must be included in the calculation of the Borrower's total debt to income.

c) Required Documentation

Lenders must include documentation from the federal agency evidencing the repayment agreement and verification of payments made, if applicable.

iv. Alimony, Child Support, and Maintenance

a) Definition

Alimony, Child Support, and Maintenance are court-ordered or otherwise agreed upon payments.

b) Standard

For Alimony, if the Borrower's income was not reduced by the amount of the monthly alimony obligation in Lenders' calculation of the Borrower's gross income, Lenders must verify and include the monthly obligation in its calculation of the Borrower's debt.

Child Support and Maintenance are to be treated as a recurring liability and Lenders must include the monthly obligation in the Borrower's liabilities and debt.

c) Required Documentation

Lenders must obtain the official signed divorce decree, separation agreement, maintenance agreement, or other legal order.

Lenders must also obtain the Borrower's pay stubs covering no less than 28 consecutive Days to verify whether the Borrower is subject to any order of garnishment relating to the Alimony, Child Support, and Maintenance.

d) Calculation of Monthly Obligation

The DG Lender must calculate the Borrower's monthly obligation from the greater of:

- the amount shown on the most recent decree or agreement establishing the Borrower's payment obligation; or

- the monthly amount of the garnishment.

v. Non-Borrowing Spouse Debt in Community Property States

a) Definition

Non-Borrowing Spouse Debt refers to debts owed by a spouse that are not owed by, or in the name of the Borrower.

b) Standard

If the Borrower resides in a community property state or the Property being insured/guaranteed is located in a community property state, debts of the non-borrowing spouse must be included in the Borrower's qualifying ratios, except for obligations specifically excluded by state law.
The non-borrowing spouse's credit history is not considered a reason to deny a mortgage application.

c) Required Documentation

Lenders must verify and document the debt of the non-borrowing spouse.

Lenders must make a note in the file referencing the specific state law that justifies the exclusion of any debt from consideration.

Lenders must obtain a credit report for the non-borrowing spouse to determine the debts that must be counted in the DTI ratio.

d) Calculation of monthly Obligation

Lenders must use the actual monthly payment to be paid on a deferred liability, whenever available.

If the actual monthly payment is not available for installment debt, Lenders must utilize the terms of the debt or 5 percent of the outstanding balance to establish the monthly payment.

vi. Deferred Obligations

a) Definition

Deferred Obligations (excluding Student Loans) refer to liabilities that have been incurred but where payment is deferred or has not yet commenced, including accounts in forbearance.

b) Standard

Lenders must verify and include deferred obligations in the calculation of the Borrower's liabilities.

c) Required Documentation

Lenders must obtain written documentation of the deferral of the liability from the creditor and evidence of the outstanding balance and terms of the deferred liability. Lenders must obtain evidence of the actual monthly payment obligation, if available.

d) Calculation of monthly Obligation

Lenders must use the actual monthly payment to be paid on a deferred liability, whenever available.

If the actual monthly payment is not available for installment debt, Lenders must utilize the terms of the debt or 5 percent of the outstanding balance to establish the monthly payment.

vii. Student Loans

a) Definition

Student Loan refers to liabilities incurred for educational purposes.

b) Standard

Lenders must include all Student Loans in the Borrower's liabilities, regardless of the payment type or status of payments.

c) Required Documentation

If the payment used for the monthly obligation is less than the monthly payment reported on the Borrower's credit report, Lenders must obtain written documentation of the actual monthly payment, the payment status, and evidence of the outstanding balance and terms from the creditor or student loan servicer.

Lenders may exclude the payment amount from the monthly debt calculation where written documentation from the student loan program, creditor, or student loan servicer indicates that the loan balance has been forgiven, canceled, discharged, or otherwise paid in full.

d) Calculation of monthly Obligation

For outstanding Student Loans, regardless of the payment status, Lenders must use:

- the payment amount reported on the credit report or the actual documented payment, when the payment amount is above zero; or

- 0.5 percent of the outstanding loan balance, when the monthly payment reported on the Borrower's credit report is zero.

e) Exception

Where a student loan payment has been suspended in accordance with COVID-19 emergency relief, the Non-DG/DG Lender may use the payment amount reported on the credit report or the actual documented payment prior to suspension, when that payment amount is above $0.

viii. Installment Loans

a) Definition

Installment Loans (excluding Student Loans) refer to loans, not secured by real estate, that require the periodic payment of P&I. A loan secured by an interest in a timeshare must be considered an Installment Loan.

b) Standard

DG Lender must include the monthly payment shown on the credit report, loan agreement or payment statement to calculate the Borrower's liabilities.

If the credit report does not include a monthly payment for the loan, Lenders must use the amount of the monthly payment shown in the loan agreement or payment statement.

c) Required Documentation

If the monthly payment shown on the credit report is utilized to calculate the monthly debts, no further documentation is required.

If the credit report does not include a monthly payment for the loan, or the payment reported on the credit report is greater than the payment on the loan agreement or payment statement, the Lenders must use the loan agreement or payment statement to document the amount of the monthly payment. If the credit report, loan agreement or payment statement shows a deferred payment arrangement for an Installment Loan, refer to the Deferred Obligations section.

ix. Revolving Charge Accounts

a) Definition

A Revolving Charge Account refers to a credit arrangement that requires the Borrower to make periodic payments but does not require full repayment by a specified point of time.

b) Standard

Lenders must include the monthly payment shown on the credit report for the Revolving Charge Account. Where the credit report does not include a monthly payment for the account, the Lenders must use the payment shown on the current account statement or 5 percent of the outstanding balance.

c) Required Documentation

Lenders must use the credit report to document the terms, balance and payment amount on the account, if available.

Where the credit report does not reflect the necessary information on the charge account, Lenders must obtain a copy of the most recent charge account statement or use 5 percent of the outstanding balance to document the monthly payment.

x. 30-Day Accounts

a) Definition

A 30-Day Account refers to a credit arrangement that requires the Borrower to pay off the outstanding balance on the account every month.

b) Standard

Lenders must verify the Borrower paid the outstanding balance in full on every 30-Day Account each month for the past 12 months. 30-Day Accounts that are paid monthly are not included in the Borrower's DTI. If the credit report reflects any late payments in the last 12 months, Lenders must utilize 5 percent of the outstanding balance as the Borrower's monthly debt to be included in the DTI.

c) Required Documentation

Lenders must use the credit report to document that the Borrower has paid the balance on the account monthly for the previous 12 months. Lenders must use the credit report to document the balance and must document that funds are available to pay off the balance, in excess of the funds and Reserves required to close the Mortgage.

xi. Business Debt in Borrower's Name

a) Definition

Business Debt in Borrower's Name refers to liabilities reported on the Borrower's personal credit report, but payment for the debt is attributed to the Borrower's business.

b) Standard

When business debt is reported on the Borrower's personal credit report, the debt must be included in the DTI calculation, unless the Lenders can document that the debt is being paid by the Borrower's business, and the debt was considered in the cash flow analysis of the Borrower's business. The debt is considered in the cash flow analysis where the Borrower's business tax returns reflect a business expense related to the obligation, equal to or greater than the amount of payments documented as paid out of company funds. Where the Borrower's business tax returns show an interest expense related to the obligation, only the interest portion of the debt is considered in the cash flow analysis.

c) Required Documentation

When a self-employed Borrower states debt appearing on their personal credit report is being paid by their business, the Non-Lenders must obtain documentation that the debt is paid out of company funds and that the debt was considered in the cash flow analysis of the Borrower's business.

xii. Disputed Derogatory Credit Accounts

a) Definition

Disputed Derogatory Credit Accounts refer to disputed Charge Off Accounts, disputed collection accounts, and disputed accounts with late payments in the last 24 months.

b) Standard

If the Borrower has $1,000 or more collectively in Disputed Derogatory Credit Accounts, DG Lenders must include a monthly payment in the Borrower's debt calculation.

The following items are excluded from the cumulative balance:

- disputed medical accounts; and
- disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use.

Disputed Derogatory Credit Accounts of a non-borrowing spouse in a community property state are not included in the cumulative balance.

xiii. Non-derogatory Disputed Account and Disputed Accounts Not Indicated on the Credit Report

a) Definition

Non-derogatory Disputed Accounts include the following types of accounts:

- disputed accounts with zero balance;

- disputed accounts with late payments aged 24 months or greater; or

- disputed accounts that are current and paid as agreed.

b) Standard

If a Borrower is disputing non-derogatory accounts or is disputing accounts which are not indicated on the credit report as being disputed, Lenders must analyze the effect of the disputed accounts on the Borrower's ability to repay the loan. If the dispute results in the Borrower's monthly debt payments utilized in computing the DTI ratio being less than the amount indicated on the credit report, the Borrower must provide documentation of the lower payments.

xiv. Contingent Liabilities

a) Definition

A Contingent Liability is a liability that may result in the obligation to repay only where a specific event occurs. For example, a contingent liability exists when an individual can be held responsible for the repayment of a debt if another legally obligated party defaults on the payment. Contingent liabilities may include cosigner liabilities and liabilities resulting from a mortgage assumption without release of liability.

b) Standard

Lenders must include monthly payments on contingent liabilities in the calculation of the Borrower's monthly obligations unless the Lenders verifies that there is no possibility that the debt holder will pursue debt collection against the Borrower should the other party default or the other legally obligated party has made 12 months of timely payments. When a contingent liability is created by a divorce decree or other court order, evidence that the other legally obligated party has made 12 months of timely payments is not required.

c) Required Documentation

(1) Mortgage Assumptions

Lenders must obtain the agreement creating the contingent liability or assumption agreement and deed showing transfer of title out of the Borrower's name and release of liability if applicable.

(2) Cosigned Liabilities

If the cosigned liability is not included in the monthly obligation, Lenders must obtain documentation to evidence that the other party to the debt has been making regular on-time payments during the previous 12 months.

(3) Court-Ordered Divorce Decree or Other Court Order

Lenders must obtain a copy of the divorce decree or other court order ordering the spouse or other legally obligated party to make payments.

(4) Calculation of Monthly Obligation

Lenders must calculate the monthly payment on the contingent liability based on the terms of the agreement creating the contingent liability.

xv. Collection Accounts

a) Definition

A Collection Account refers to a Borrower's loan or debt that has been submitted to a collection agency by a creditor.

b) Standard

Lenders must determine if collection accounts were a result of:

- the Borrower's disregard for financial obligations;
- the Borrower's inability to manage debt; or
- extenuating circumstances.

When the credit report used in the analysis shows cumulative outstanding collection account balances of $2,000 or greater, the Lender must:

- verify that the debt is paid in full at the time of or prior to settlement using an acceptable source of funds;
- verify that the Borrower has made payment arrangements with the creditor; or
- if a payment arrangement is not available, calculate the monthly payment using 5 percent of the outstanding balance of each collection and include the monthly payment in the Borrower's DTI ratio.

Collection accounts of a non-borrowing spouse in a community property state must be included in the $2,000 cumulative balance and analyzed as part of the Borrower's ability to pay all collection accounts, unless specifically excluded by state law.

c) Required Documentation

Lenders must document reasons for approving the loan when the Borrower has any collection accounts.
The Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account. The explanation and supporting documentation must be consistent with other credit information in the file.

Where applicable, Lenders must provide the following documentation:

- evidence of payment in full, if paid prior to settlement;
- the payoff statement, if paid at settlement; or
- the payment arrangement with creditor, if not paid prior to or at settlement.

If Lenders uses 5 percent of the outstanding balance, no documentation is required.

xvi. Charge Off Accounts

a) Definition

Charge Off Account refers to a Borrower's loan or debt that has been written off by the creditor.

b) Standard

Charge Off Accounts do not need to be included in the Borrower's liabilities or debt.

xvii. Private Savings Clubs

a) Definition

Private Savings Club refers to a non-traditional method of saving by making deposits into a member-managed resource pool.

b) Standard

If the Borrower is obligated to continue making ongoing contributions under the pooled savings agreement, this obligation must be counted in the Borrowers' total debt. Lenders must verify and document the establishment and duration of the Borrower's membership in the club and the amount of the Borrower's required contribution to the club.

c) **Required Documentation**

Lenders must also obtain the club's account ledgers and receipts, and verification from the club treasurer that the club is still active.

xviii. Obligations Not Considered Debt

Obligations not considered debt include:

- medical collections;
- federal, state, and local taxes, if not delinquent and no payments required;
- automatic deductions from savings, when not associated with another type of obligation;
- Federal Insurance Contributions Act (FICA) and other retirement contributions, such as 401(k) accounts;
- collateralized loans secured by depository accounts;
- utilities;
- childcare;
- commuting costs
- union dues;
- insurance, other than property insurance;
- open accounts with zero balances; and
- voluntary deductions, when not associated with another type of obligation.

2. Income Requirements

a. Definition

Effective Income refers to income that may be used to qualify a Borrower for a Loan.

b. Standard

Effective Income must be reasonably likely to continue through at least the first three years of the Loan, and meet the specific requirements described below.

c. General Income Requirements

i. Lenders must document the Borrower's income and employment history, verify the accuracy of the amounts of income being reported, and determine if the income can be considered as Effective Income in accordance with the requirements listed below.

ii. Lenders may only consider income if it is legally derived and, when required, properly reported as income on the Borrower's tax returns.

iii. Lenders must obtain IRS tax transcripts for the most recent 2-year periods for all loan applications prior to underwriting.

iv. Negative income must be subtracted from the Borrower's gross monthly income and not treated as a recurring monthly liability unless otherwise noted.

v. When tax returns are required to support any type of Effective Income, Lenders must also analyze the tax returns in accordance with Appendix 2.0 —Analyzing IRS Forms.

d. Employment Income

i. Definition

Employment Income refers to income received as an employee of a business that is reported on IRS Form W-2, Wage and Tax Statement.

ii. Standard

Lenders shall use Employment Income as Effective Income in accordance with the standards provided for each type of Employment related Income.

iii. Required Documentation

For all Employment related Income, Lenders must verify the Borrower's most recent two years of employment and income, and document current employment using either the traditional or alternative method, and past employment as applicable.

a) Traditional Current Employment Documentation

Lenders must obtain one of the following to verify current employment and income:

- the most recent pay stubs covering a minimum of 30 consecutive Days (if paid weekly or biweekly, pay stubs must cover a minimum of 28 consecutive Days) that show the Borrower's year-to-date earnings, and a written Verification of Employment (VOE) covering two years; or

- direct electronic verification of employment by a TPV vendor covering two years, subject to the following requirements:

    - the Borrower has authorized the Lender to verify income and employment; and

    - the date of the data contained in the completed verification conforms with Section 184 requirements in Maximum Age of Loan Documents.

Reverification of employment must be completed within 10 Days prior to the date of the Note. Verbal or electronic reverification of employment is acceptable. Electronic reverification employment data must be current within 30 days of the date of the verification.

b) Alternative Current Employment Documentation

If using alternative documentation, Lenders must:

- obtain copies of the most recent pay stub that shows the Borrower's year-to-date earnings;

- obtain copies of the original IRS Form W-2s from the previous two years; and

- document current employment by telephone, sign, and date the verification documentation, and note the name, title, and telephone number of the person with whom employment was verified.

Reverification of employment must be completed within 10 Days prior to the date of the Note. Verbal or electronic reverification of employment is acceptable. Electronic reverification employment data must be current within 30 days of the date of the verification.

c) Past Employment Documentation

Direct verification of the Borrower's employment and income history for the previous two years is not required if all of the following conditions are met:

(1) The current employer confirms a two-year employment history, or a paystub reflects a hiring date.

(2) Only base pay is used to qualify (no Overtime, Bonus, or Tip Income).

(3) The Borrower executes IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-C, *IVES Request for Transcript of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, for the previous two tax years.

If the applicant has not been employed with the same employer for the previous two years and/or not all conditions immediately above can be met, then Lenders must obtain one or a combination of the following for the most recent two years to verify the applicant's employment history:

(4) IRS Form W-2(s);

(5) written VOE(s);

(6) direct verification of employment by a TPV vendor, subject to the following requirements:

- the Borrower has authorized the Non-DG and DG Lender to verify income and employment; and

- the date of the data contained in the completed verification conforms with Section 184 requirements in Maximum Age of Loan Documents; and/or

(7) evidence supporting enrollment in school or the military during the most recent two full years.

e. Primary Employment

i. Definition

Primary Employment is the Borrower's principal employment, unless the income falls within a specific category identified below. Primary employment is generally full-time employment and may be either salaried or hourly.

COVID-19 Related Economic Event refers to temporary loss of employment, temporary reduction of income, or temporary reduction of hours worked during the Presidentially Declared COVID-19 National Emergency.

ii. Standard

Lenders may use primary Employment Income as Effective Income.

iii. Calculation of Effective Income

a) Salary

(1) Standard

For employees who are salaried and whose income has been and will likely be consistently earned, the DG Lender must use the current salary to calculate Effective Income.

(2) Exception Due to COVID-19 Related Economic Event

For employees who are salaried and whose current income will likely be consistently earned, the DG Lender must use the current salary to calculate Effective Income.

b) Hourly

(1) Standard

For employees who are paid hourly and whose hours do not vary, Lenders must consider the Borrower's current hourly rate to calculate Effective Income.

For employees who are paid hourly and whose hours vary, Lenders must use the average income over the previous two years. If Lenders can document an increase in pay rate the DG Lender may use the most recent 12-month average of hours at the current pay rate.

(2) Exception Due to COVID-19 Related Economic Event

For employees who are paid hourly and whose hours do not vary, Lenders must use the current hourly rate to calculate Effective Income.

For employees who are paid hourly and whose hours vary, Lenders must calculate the Effective Income by using the lesser of:

- the average of the income in accordance with the Hourly Standard Section above for the period prior to the COVID-19 Related Economic Event; or
- the average of the income since the COVID-19 Related Economic Event.

f. Part-Time Employment

i. Definition

Part-Time Employment refers to employment that is not the Borrower's primary employment and is generally performed for less than 40 hours per week.

ii. Standard

Lenders may use Employment Income from Part-Time Employment as Effective Income if the Borrower has worked a part-time job uninterrupted for the past two years and the current position is reasonably likely to continue.

iii. Calculation of Effective Income

Lenders must average the income over the previous two years. If Lenders can document an increase in pay rate the Lenders may use a 12-month average of hours at the current pay rate.

iv. Exception Due to COVID-19 Related Economic Event

For employees who are paid hourly and whose hours do not vary, Lenders must use the current hourly rate to calculate Effective Income.

For employees who are paid hourly and whose hours vary, Lenders must calculate the Effective Income by using the lesser of:

- the average of the income in accordance with the Calculation of Effective Income Section above for the time period prior to the COVID-19 Related Economic Event; or

- the average of income earned since the COVID-19 Related Economic Event.

g. Overtime, Bonus, or Tip Income

i. Definition

Overtime, Bonus, or Tip Income refers to income that the Borrower receives in addition to the Borrower's normal salary.

ii. Standard

Lenders may use Overtime, Bonus, or Tip Income as Effective Income if the Borrower has received this income for the past two years and it is reasonably likely to continue.

Periods of Overtime, Bonus, or Tip Income for the past two years may be considered as a compensating factor if Lenders document that the Overtime, Bonus, or Tip income has been consistently earned over a period of not less than one year and is reasonably likely to continue.

iii. Calculation of Effective Income

For employees with Overtime, Bonus, or Tip Income, the DG Lender must calculate Effective Income by using the lesser of:

- the average Overtime, Bonus, or Tip Income earned over the previous two years or, if less than two years, the length of time Overtime, Bonus, or Tip Income has been earned; or

- the average Overtime.

iv. Exception Due to COVID-19 Related Economic Event

For employees with Overtime, Bonus, or Tip Income, the DG Lender must calculate the Effective Income by using the lesser of:

- the average of the income in accordance with the Overtime, Bonus, or Tip Income Standard Section above for the time period prior to the COVID-19 Related Economic Event; or
- the average Overtime, Bonus, or Tip Income earned since the COVID-19 Related Economic Event.

h. Seasonal Employment

i. Definition

Seasonal Employment refers to employment that is not year-round, regardless of the number of hours per week the Borrower works on the job.

ii. Standard

The DG Lender may consider Employment Income from Seasonal Employment as Effective Income if the Borrower has worked the same line of work for the past two years and is reasonably likely to be rehired for the next season. The DG Lender may consider unemployment income as Effective Income for those with Effective Income from Seasonal Employment.

iii. Required Documentation

For seasonal employees with unemployment income, the Non-DG/DG Lender must document the unemployment income for two full years and there must be reasonable assurance that this income will continue.

iv. Calculation of Effective Income

For employees with Employment Income from Seasonal Employment, Lenders must average the income earned over the previous two full years to calculate Effective Income.

i. Employer Housing Subsidy

i. Definition

Employer Housing Subsidy refers to employer-provided mortgage assistance.

ii. Standard

Lenders may utilize Employer Housing Subsidy as Effective Income.

iii. Required Documentation

Lenders must verify and document the existence and the amount of the housing subsidy.

iv. Calculation of Effective Income

For employees receiving an Employer Housing Subsidy, Lenders may add the Employer Housing Subsidy to the total Effective Income but may not use it to offset the Loan Payment.

j. Employed by Family-Owned Business

i. Definition

Family-Owned Business Income refers to Employment Income earned from a business owned by the Borrower's family, but in which the Borrower is not an owner.

ii. Standard

Lenders may consider Family-Owned Business Income as Effective Income if the Borrower is not an owner in the family-owned business.

iii. Required Documentation

Lenders must verify and document that the Borrower is not an owner in the family-owned business by using official business documents showing the ownership percentage.

Official business documents include corporate resolutions or other business organizational documents, business tax returns or [Schedule K-1 (IRS Form 1065)](), *U.S. Return of Partnership Income*, or an official letter from a certified public accountant on their business letterhead.
In addition to traditional or alternative documentation requirements for

the type of income earned from a Family-Owned Business, Lenders must obtain copies of signed personal tax returns or tax transcripts.

iv. Calculation of Effective Income

a) Salary

(1) Standard

For employees who are salaried and whose income has been and will likely continue to be consistently earned, Lenders must use the current salary to calculate Effective Income.

(2) Exception Due to COVID-19 Related Economic Event

For employees who are salaried and whose income will likely be consistently earned, the DG Lender must use the current salary to calculate Effective Income.

b) Hourly

(1) Standard

For employees who are paid hourly and whose hours do not vary, the Lenders must consider the Borrower's current hourly rate to calculate Effective Income.
For employees who are paid hourly and whose hours vary, Lenders must average the income over the previous two years. If the Lenders can document an increase in pay rate the DG Lender may use the most recent 12-month average of hours at the current pay rate.

(2) Exception Due to COVID-19 Related Economic Event

For employees who are paid hourly and whose hours do not vary, Lenders must use the current hourly rate to calculate Effective Income.

For employees who are paid hourly and whose hours vary, Lenders must calculate the Effective Income by using the lesser of:

- the average of the income in accordance with the Hourly Standard Section above for the time period prior to the COVID-19 Related Economic Event; or

- the average of the income for the time period since the COVID-19 Related Economic Event.

k. Commission Income

i. Definition

Commission Income refers to income that is paid contingent upon the conducting of a business transaction or the performance of a service.

ii. Standard

Lenders may use Commission Income as Effective Income if the Borrower earned the income for at least two years in the same or similar line of work and it is reasonably likely to continue.

iii. Required Documentation

For all Commission Income, Lenders must use traditional or alternative employment documentation.

iv. Calculation of Effective Income

a) Standard

Lenders must calculate Effective Income for commission by using the average Commission Income earned over the previous two years for all employers in the same or similar line of work.

b) Exception Due to COVID-19 Related Economic Event

For employees with Commission Income, Lenders must calculate the Effective Income by using the lesser of:

- the average of the income in accordance with Commission Income Standard above for the time period prior to the COVID-19 Related Economic Event; or

- the average of the Commission Income for the time period since the COVID-19 Related Economic Event.

l. Self-Employment Income

i. Definition

Self-Employment Income refers to income generated by a business in which the Borrower has a 25 percent or greater ownership interest. There are four basic types of business structures. They include:

- sole proprietorships;
- corporations;
- limited liability or "S" corporations; and
- partnerships.

ii. Standard

a) Minimum Length of Self-Employment

Lenders may consider Self-Employment Income if the Borrower has been self-employed for at least two years.

If the Borrower has been self-employed between one and two years, Lenders may only consider the income as Effective Income if the Borrower was previously employed in the same line of work in which the Borrower is self-employed or in a related occupation for at least two years.

b) Stability of Self-Employment Income

Income obtained from businesses with annual earnings that are stable or increasing is acceptable. If the income from businesses shows a greater than 20 percent decline in Effective Income over the analysis period, the Lenders must document that the business income is now stable.

Lenders may consider income as stable after a 20 percent reduction if Lenders can document the reduction in income was the result of an extenuating circumstance, the Borrower can demonstrate the income has been stable or increasing for a minimum of 12 months, and the Borrower qualifies utilizing the reduced income. DG Lender must explain the income calculation with a memorandum to the file.

c) Exception Due to COVID-19 Related Economic Event

The Borrower must have an aggregate two-year self-employment history before and after the COVID-19 Related Economic Event.

If the Borrower has an aggregate self-employment history between one and two years before and after the COVID-19 Related Economic Event, Lenders may only consider the income as Effective Income if the Borrower was previously employed in the same line of work in which the Borrower is self-employed or in a related occupation for at least two years.

Lenders may consider income as stable after a 20 percent reduction if the Lender can document the reduction in income was the result of a COVID-19 Related Economic Event and the Borrower can demonstrate the income has been stable or increasing for a minimum of six months, and the Borrower qualifies utilizing the reduced income.

d) Required Documentation

(1) Individual and Business Tax Returns

Lenders must obtain complete individual federal income tax returns for the most recent two years, including all schedules.

In lieu of signed individual or business tax returns from the Borrower, the Non-DG/DG Lender may obtain a signed IRS Form 4506, IRS Form 4506-C, or IRS Form 8821, and tax transcripts directly from the IRS.

(2) Profit & Loss Statements and Balance Sheets

Lenders must obtain a year-to-date Profit and Loss (P&L) statement and balance sheet if more than a calendar quarter has elapsed since the date of the most recent calendar or fiscal year-end tax period. A balance sheet is not required for self-employed Borrowers filing Schedule C income.

If income used to qualify the Borrower exceeds the two-year average of tax returns, an audited P&L or signed quarterly tax return obtained from the IRS is required.

(3) Business Credit Reports

Lenders must obtain a business credit report for all corporations and "S" corporations.

(4) Exception Due to COVID-19 Related Economic Event

For self-employed Borrowers with a reduction of income due to a COVID-19 Related Economic Event, Lenders must provide the following documentation in addition to the current Self-Employment Income required documentation:

- letter of explanation for the time period of income loss or reduction;

- the Borrower's business tax returns for the most recent two years; and

- either of the following:

  - an audited year-to-date P&L statement reporting business revenue, expenses, and net income up to and including the most recent month preceding the case assignment date; or

  - an unaudited year-to-date P&L statement signed by the Borrower reporting business revenue, expenses, and net income up to and including the most recent month preceding the case assignment date, and three of the most recent business bank statements no older than the latest three months represented on the year-to-date P&L statement. Monthly deposits on the business bank statements must support the earnings on the unaudited year-to-date P&L.

e) Calculation of Effective Income

(1) Standard

Lenders must analyze the Borrower's tax returns to determine gross Self- Employment Income. Requirements for analyzing self-employment documentation are found in Analyzing IRS Forms.

Lenders must calculate gross Self-Employment Income by using the lesser of:

- the average gross Self- Employment Income earned over either: the previous two years; or the length of time Self-Employment Income has been earned if less than two years (where permitted); or
- the average gross Self-Employment Income earned over the previous one year.

(2) Exception Due to COVID-19 Related Economic Event

For self-employed Borrowers with a COVID-19 Related Economic Event who have since regained income at a level greater than or equal to 80 percent of their income prior to the COVID-19 Related Economic Event for a minimum of six months, the DG Lender must calculate gross Self-Employment Income by using the lesser of:

- the average gross Self-Employment Income earned over the previous two years prior to the COVID-19 Related Economic Event; or
- the average gross Self-Employment Income earned over the previous six months after the COVID-19 Related Economic Event.

m. Additional Required Analysis of Stability of Employment Income

i. Frequent Changes in Employment

If the Borrower has changed employers more than three times in the previous 12-month period, or has changed lines of work, Lenders must take additional steps to verify and document the stability of the Borrower's Employment Income. Additional analysis is not required for fields of employment that regularly require a Borrower to work for various employers (such as Temp Companies or Union Trades). Lenders must obtain:

- transcripts of training and education demonstrating qualification for a new position; or

- employment documentation evidencing continual increases in income and/or benefits.

ii. Addressing Gaps in Employment

For Borrowers with gaps in employment of 30 days or more (an extended absence), Lenders may consider the Borrower's current income as Effective Income if it can verify and document that:

- the Borrower has been employed in the current line of work for at least six months at the time of case number assignment; and

- a two-year work history prior to the absence from employment using standard or alternative employment verification.

iii. Addressing Temporary Reduction in Income

For Borrowers with a temporary reduction of income due to a short-term disability or similar temporary leave, the DG Lender may consider the Borrower's current income as Effective Income, if it can verify and document that:

- the Borrower intends to return to work;

- the Borrower has the right to return to work; and

- the Borrower qualifies for the Loan considering any reduction of income due to the circumstance.

For Tribal, federal, state, or local government employees temporarily out of work due to a government shutdown or other similar, temporary events (where lost income is anticipated to be recovered), income preceding the shutdown can be considered as Effective Income.

For Borrowers returning to work before or at the time of the first Loan Payment due date, Lenders may use the Borrower's pre-leave income as Effective Income.

For Borrowers returning to work after the first Loan Payment due date, DG Lenders may use the Borrower's current income plus available surplus liquid asset Reserves, above and beyond the funds required to close the loan, as an income supplement up to the amount of the Borrower's pre-leave income as Effective Income. The amount of the monthly income supplement is the total amount of surplus Reserves divided by the number of months between the first payment due date and the Borrower's intended date of return to work.

a) Required Documentation

Lenders must provide the following documentation for Borrowers on temporary leave:

- a written statement from the Borrower confirming the Borrower's intent to return to work, and the intended date of return;
- documentation generated by current employer confirming the Borrower's eligibility to return to current employer after temporary leave, anticipated return to work date; and
- documentation of sufficient liquid assets, in accordance with Sources of Funds, used to supplement the Borrower's income through intended date of return to work with current employer.

iv. Addressing Gaps in Employment or Reduction of Income Due to COVID-19 Related Economic Event

a) Employment Income

For Borrowers with gaps in employment, reduction of income, or reduction of hours due to a COVID-19 Related Economic Event, Lenders may consider the Borrower's current income as Effective Income if it can verify and document that:

- the Borrower has been employed in the current job or same line of work for at least one month at the time of case number assignment; or
- the Borrower has been employed in a different job or line of work for at least six months at the time of case number assignment; and the Borrower has an aggregate two-year work history prior to case number assignment excluding gaps in employment using traditional or alternative employment verification.

b) Required Documentation

Lenders must obtain written VOE identifying the time period of temporary loss of employment, temporary loss of income, or temporary loss of hours.

c) Self-Employment Income

For Borrowers with gaps in self-employment, a reduction in income, or reduction of hours due to a COVID-19 Related Economic Event, Lenders may exclude the months where the business was closed, or income was reduced when calculating Effective Income. The total time period of the Borrower's self-employment must still meet the minimum length of self-employment in accordance with Exception Due to COVID-19 Related Economic Event.

n. Other Sources of Effective Income

i. Disability Benefits

a) Definition

Disability Benefits refer to benefits received from the Social Security Administration (SSA), Department of Veterans Affairs (VA), or a private disability insurance provider.

b) Required Documentation

Lenders must verify and document the Borrower's receipt of benefits from the SSA, VA, or private disability insurance provider. Lenders must obtain documentation that establishes award benefits to the Borrower.

If any disability income is due to expire within three years from the date of Loan application, that income cannot be used as Effective Income. If the Notice of Award or equivalent document does not have a defined expiration date, Lenders may consider the income effective and reasonably likely to continue. Lenders may not rely upon a pending or current re-evaluation of medical eligibility for benefit payments as evidence that the benefit payment is not reasonably likely to continue.

Under no circumstance may Lenders inquire into or request documentation concerning the nature of the disability or the medical condition of the Borrower.

(1) Social Security Disability

For Social Security Disability income, including Supplemental Security Income (SSI), Lenders must obtain:

A copy of the last Notice of Award letter, or an equivalent document that establishes award benefits to the Borrower, and one of the following documents:

- Tax Returns;
- the most recent bank statement evidencing receipt of income from the SSA;
- a Proof of Income Letter, also known as a "Budget Letter" or "Benefits Letter" that evidence income from the SSA; or
- a copy of the Borrower's form SSA-1099/1042S, *Social Security Benefit Statement*.

(2) Department of Veterans Affairs Disability

For VA disability benefits, Lenders must obtain from the Borrower a copy of the veteran's last Benefits Letter showing the amount of the assistance, and one of the following documents:

- Tax Returns; or
- the most recent bank statement evidencing receipt of income from the VA.

If the Benefits Letter does not have a defined expiration date, Lenders may consider the income effective and reasonably likely to continue for at least three years.

(3) Private Disability

For private disability benefits, Lenders must obtain:

Documentation from the private disability insurance provider showing the amount of the assistance and the expiration date of the benefits, if any, and one of the following documents:

- Tax Returns; or
- the most recent bank statement evidencing receipt

of income from the insurance provider.

c) Calculation of Effective Income

Lenders must use the most recent amount of benefits received to calculate Effective Income.

ii. Alimony, Child Support, and Maintenance Income

a) Definition

Alimony, Child Support, and Maintenance Income refers to income received from a former spouse or partner or from a noncustodial parent of the Borrower's minor dependent.

b) Required Documentation

Lenders must obtain a fully executed copy of the Borrower's final divorce decree, legal separation agreement, court order, or voluntary payment agreement with documented receipt.

When using a final divorce decree, legal separation agreement or court order, Lenders must obtain evidence of receipt using deposits on bank statements; canceled checks; or documentation from the child support agency for the most recent three months that supports the amount used in qualifying.

Lenders must document the voluntary payment agreement with 12 months of canceled checks, deposit slips, or Tax Returns.

Lenders must provide evidence that the claimed income will continue for at least three years. Lenders may use the front and pertinent pages of the divorce decree/settlement agreement and/or court order showing the financial details.

c) **Calculation of Effective Income**

When using a final divorce decree, legal separation agreement or court order, if the Borrower has received consistent Alimony, Child Support, and Maintenance Income for the most recent three months, Lenders may use the current payment to calculate Effective Income.

When using evidence of voluntary payments, if the Borrower has received consistent Alimony, Child Support, and

Maintenance Income for the most recent six months, Lenders may use the current payment to calculate Effective Income.

If the Alimony, Child Support, and Maintenance Income have not been consistently received for the most recent three months if court ordered or six months if voluntary, Lenders must use the average of the income received over the previous two years to calculate Effective Income. If Alimony, Child Support, and Maintenance Income have been received for less than two years, the Lenders must use the average over the time of receipt.

iii. Military Income

a) Definition

Military Income refers to income received by military personnel during their period of active, Reserve, or National Guard service, including:

- base pay;
- Basic Allowance for Housing;
- clothing allowances;
- flight or hazard pay;
- Basic Allowance for Subsistence; and
- proficiency pay.

Lenders may not use education benefits as Effective Income.

b) Required Documentation

Lenders must obtain a copy of the Borrower's military Leave and Earnings Statement (LES). Lenders must verify the Expiration Term of Service date on the LES. If the Expiration Term of Service date is within the first 12 months of the Loan, Military Income may only be considered Effective Income if the Borrower represents their intent to continue military service.

c) **Calculation of Effective Income**

Lenders must use the current amount of Military Income received to calculate Effective Income.

iv. **Mortgage Credit Certificate (MCC)**

a) **Definition**

Mortgage Credit Certificates refer to government Mortgage Payment Subsidies other than Section 8 Housing Choice Vouchers.

b) **Requirements**

The Lender must verify and document the amount of the tax rebate.

c) **Calculating Effective Income**

Mortgage Credit Certificate income may be included as Effective Income. The Lender must use the current subsidy rate to calculate the Effective Income.

v. **Public Assistance**

a) **Definition**

Public Assistance refers to income received from Tribal, Federal, State or local government assistance programs. Examples of Public Assistance may include Mortgage Credit Certificates (MCC) and Section 8 Housing Choice Vouchers.

b) **Required Documentation**

Lenders must verify and document the income received from the Tribal, Federal, State or local government agency.
If any Public Assistance income is due to expire within three years from the date of Loan application, that income cannot be used as Effective Income. If the documentation does not have a defined expiration date, the DG Lender may consider the income effective and reasonably likely to continue.

c) **Calculation of Effective Income**

Lenders must use the current rate of Public Assistance received to calculate Effective Income.

vi. Automobile Allowances

a) **Definition**

Automobile Allowance refers to the funds provided by the Borrower's employer for automobile related expenses.

b) **Required Documentation**

Lenders must verify and document the Automobile Allowance received from the employer for the previous two years.

c) **Calculation of Effective Income**

Lenders must use the full amount of the Automobile Allowance to calculate Effective Income.

vii. Retirement Income

Retirement Income refers to income received from Pensions, 401(k) distributions, 403(b), Thrift Savings Plan, and Social Security.

a) **Social Security**

(1) Definition

Social Security Income or Supplemental Security Income (SSI) refers to income received from the SSA other than disability income.

(2) Required Documentation

Lenders must verify and document the Borrower's receipt of income from the SSA and that it is likely to continue for at least a three-year period from the date of case number assignment.

For SSI, Lenders must document the continuance of this income by obtaining copy of the last Notice of Award letter which states the SSA's determination on the Borrower's eligibility for SSA income, or equivalent documentation that establishes award benefits to the Borrower (equivalent document) and one of the following:

- Tax Returns;
- the most recent bank statement evidencing receipt of income from the SSA;
- a Proof of Income Letter, also known as a "Budget Letter" or "Benefits Letter" that evidence income from the SSA; or
- a copy of the Borrower's form SSA-1099/1042S.

If the Notice of Award or equivalent document does not have a defined expiration date, the DG Lender must consider the income effective and reasonably likely to continue. The Non-DG/DG Lender may not request additional documentation from the Borrower to demonstrate continuance of Social Security Income.

If the Notice of Award letter or equivalent document specifies a future start date for receipt of income, this income may only be considered effective on the specified start date.

(3) Calculation of Effective Income

Lenders must use the current amount of Social Security Income received to calculate Effective Income.

b) Pension

(1) Definition

Pension refers to income received from the Borrower's former employer(s).

(2) Required Documentation

Lenders must verify and document the Borrower's receipt of periodic payments from the Borrower's Pension and that the payments are likely to continue for at least three years.
Lenders must obtain any one of the following

documents:

- Tax Returns;
- the most recent bank statement evidencing receipt of income from the former employer; or
- a copy of the Borrower's Pension/retirement letter from the former employer.

(3) Calculation of Effective Income

Lenders must use the current amount of Pension income received to calculate Effective Income.

c) Individual Retirement Account (IRA), such as 401(k)

(1) Definition

Individual Retirement Account (IRA)/401(k) Income refers to income received from an IRA, 401(k), or similar account.

(2) Required Documentation

Lenders must verify and document the Borrower's receipt of recurring IRA/401(k) distribution Income and that it is reasonably likely to continue for three years. Lenders must obtain the most recent IRA/401(k) statement and any one of the following documents:

- Tax Returns; or
- the most recent bank statement evidencing receipt of income.

(3) Calculation of Effective Income

For Borrowers with IRA/401(k) Income that has been and will be consistently received, Lenders must use the current amount of IRA Income received to calculate Effective Income. For Borrowers with fluctuating IRA/401(k) Income, Lenders must use the average of the IRA/401(k) Income received over the previous two years to calculate Effective Income. If IRA/401(k) Income has been received for less than two years, Lenders must use the average over the time of receipt.

viii. Rental Income

a) Definition

Rental Income refers to income received or to be received from the subject Property or other real estate holdings.

b) Rental Income Received from the Subject Property

(1) Standard

Standard Transactions. The DG Lender may not consider Rental Income as Effective Income from existing and prospective renters, when purchasing a two to-four-unit dwelling.

Refinance/Rehabilitation Transactions. Rental Income from the subject Property may be considered Effective Income when the Property is a two- to four-unit dwelling, and the borrower has a 2-year rental receipt history or if the borrower is a Tribe or Housing Authority.

No income from commercial space may be included in Rental Income calculations.

(2) Required Documentation

Required documentation varies depending upon the Borrower type.

(i) History of Rental Income

Where the Borrower is an individual and has a history of Rental Income from the subject property since the previous tax filing, Lenders must verify and document the existing Rental Income by obtaining the existing lease, rental history over the previous 24 months that is free of unexplained gaps greater than three months (such gaps could be explained by student, seasonal or military renters, or property rehabilitation), and the Borrower's most recent tax returns, including Schedule E, from the previous two years.

(ii) No Rental Income History

Where the Borrower is a Tribe or TDHE, the Borrower must provide a statement of the Fair Market Rent they intend to collect for the specific units and a copy of the waiting list they have for similar rental units.

(iii) Two-to-Four Units

For all Two to Four Unit properties, Lenders must verify and document the existing or proposed Rental Income by obtaining an appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, Small Residential Income Property Appraisal Report) and the prospective leases if available.

c) Calculation of Effective Income

For eligible Rental Income, Lenders must add the net subject property Rental Income to the Borrower's gross income to calculate Effective Income. Lenders may not reduce the Borrower's total Loan Payment by the net subject property Rental Income.

(1) Limited or No History of Rental Income – Purchases on Trust Land

To calculate the Effective Income from the subject Property where the Borrower does not have a history of Rental Income from the subject Property since the previous tax filing, Lenders must use 75 percent of the lesser of fair market rent reported by the Appraiser, or the rent reflected in the lease or other rental agreement.

(2) One-Unit with Accessory Dwelling Unit (ADU)

The amount of Rental Income from an ADU used as Effective Income must not exceed 30 percent of the total monthly Effective Income used to qualify the Borrower.

(3) **History of Rental Income**

Lenders must calculate the Rental Income by averaging the amount shown on the Schedule E for the previous two years.

Depreciation, Loan interest, taxes, insurance, and any HOA dues shown on Schedule E may be added back to the net income or loss.

If the Property has been owned between one and two years, the Lenders must annualize the Rental Income for the length of time the Property has been owned.

d) **Rental Income from Other Real Estate Holdings**

(1) **Standard**

Rental Income from other real estate holdings may be considered Effective Income if the documentation requirements listed below are met. If Rental Income is being derived from the Property being vacated by the Borrower, the Borrower must be relocating to an area more than 100 miles from the Borrower's current Principal Residence and the borrower has a two-year history of owning and managing other rental property. The Non-Lenders must obtain a lease agreement of at least one year's duration after the Loan is closed and evidence of the payment of the security deposit or first month's rent.

(2) **Required Documentation**

(i) **Limited or No History of Rental Income**

Where the Borrower does not have a history of Rental Income for the Property since the previous tax filing, including Property being vacated by the Borrower, the DG Lender must obtain an appraisal evidencing market rent, and that the Borrower has at least 25 percent equity in the Property. The appraisal is not required to be completed by a FHA Roster Appraiser.

(ii) Two- to-Four Units

Lenders must verify and document the proposed Rental Income by obtaining an appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72) and the prospective leases.

(iii) One Unit or One-Unit with Accessory Dwelling Unit

Lenders must verify and document the proposed Rental Income by obtaining a Fannie Mae Form 1004/Freddie Mac Form 70, *URAR*, and Fannie Mae Form 1007/Freddie Mac Form 1000, Single Family Comparable Rent Schedule, showing fair market rent and, if available, the prospective lease.

(iv) History of Rental Income

Lenders must obtain the Borrower's last two years' tax returns with Schedule E.

(3) Calculation of Effective Income

(i) Limited or No History of Rental Income

To calculate the effective net Rental Income from other real estate holdings where the Borrower does not have a history of Rental Income since the previous tax filing, the DG Lender must deduct PITI from 75 percent of the lesser of fair market rent reported by the Appraiser, or the rent reflected in the lease or other rental agreement.

(ii) History of Net Rental Income

The DG Lender must calculate the net Rental Income by averaging the amount shown on the Schedule E provided the Borrower continues to own all Properties included on the Schedule E. Depreciation shown on Schedule E may be added back to the net income or loss.

Positive net Rental Income must be added to the Borrower's Effective Income. Negative net Rental Income must be included as debt/liability.

If the Property has been owned for less than two years, the DG Lender must annualize the Rental Income for the length of time the Property has been owned and document the date of acquisition by providing the deed, Closing Disclosure, or other legal document.

ix. Investment Income

a) Definition

Investment Income refers to interest and dividend income received from assets such certificates of deposits, mutual funds, stocks, bonds, money markets, and savings and checking accounts.

b) Required Documentation

Lenders must verify and document the Borrower's Investment Income by obtaining tax returns for the previous two years and the most recent account statement.

c) Calculation of Effective Income

Lenders must calculate Investment Income by using the lesser of:

- the average Investment Income earned over the previous two years; or

- the average Investment Income earned over the previous one year.

Lenders must subtract any of the assets used for the Borrower's required funds to close to purchase the subject Property from the Borrower's liquid assets prior to calculating any interest or dividend income.

x. Capital Gains and Losses

a) Definition

Capital Gains refers to a profit that results from a disposition of a capital asset, such as a stock, bond, or real estate, where the amount realized on the disposition exceeds the purchase price.

Capital Losses refer to a loss that results from a disposition of a capital asset, such as a stock, bond, or real estate, where the amount realized on the disposition is less than the purchase price.

b) Standard

Capital gains or losses must be considered when determining Effective Income, when the individual has a constant turnover of assets resulting in gains or losses.

c) Required Documentation

Three years' Tax Returns are required to evaluate an earnings trend. If the trend:

- results in a gain, it may be added as Effective Income; or
- consistently shows a loss, it must be deducted from the total income.

xi. Per Capita Income

a) Definition

Per Capita Income is the distribution of Tribal revenues to Tribal members on a per capita basis.

b) Standard

Lenders must obtain documentation that establishes Per Capita Income payments to the Borrower. The Per Capita Income shall be treated as Non-Taxable Income. See Subsection D.2.l.(xvi).

Lenders may consider a two-year average of the documented payment history as income unless there is a documented decline in the amount received. Lenders must then average the

Per Capita Income amounts received beginning with the time period of the decline. Lenders has the discretion to determine if the period of the decline is a finite period, based on written documentation provided by the Tribe or a permanent reduction warranting the use of the reduced benefit payment.

c) Required Documentation

Verification from the Tribe on Tribal letter head signed by authorized representative stating the Per Capita Income amount and naming the Borrower as the recipient.

The verification must provide a Tribal payment history for the last 24 months, or payment history from when the Per Capita Income amount began, if less than 24 months.

xii. Treaty Rights/ Trust Land Income

a) Definition

Because of treaties with the federal and state governments tribal members may have non-taxable income derived from sources such as timber sales on trust lands, lease payments from trust lands or fishing and gathering rights. Such income is not reported through normal reporting methods.

b) Standard

Lenders may consider the income as effective when it has been received for at least 24 months.

c) Required Documentation

Lenders may obtain statements from the tribe, the BIA office, sales receipts, or banking records. DG Lenders must use prudent underwriting to validate the existence, receipt of income and likelihood of 24 months of continuance.

d) Calculation of Effective Income

Lenders must average Treaty Rights and Trust Land income receipts for the most recent 24-month period.

xiii. Expected Income

a) Definition

Expected Income refers to income from cost-of-living adjustments, performance raises, a new job, or retirement that has not been, but will be received within 60 Days of mortgage closing.

b) Standard

Lenders may consider Expected Income as Effective Income except when Expected Income is to be derived from a family-owned business.

c) Required Documentation

Lenders must verify and document the existence and amount of Expected Income with the employer in writing and that it is guaranteed to begin within 60 Days of mortgage closing. For expected Retirement Income, Lenders must verify the amount and that it is guaranteed to begin within 60 Days of the mortgage closing.

d) Calculation of Effective Income

Income is calculated in accordance with the standards for the type of income being received. Lenders must also verify that the Borrower will have sufficient income or cash Reserves to support the Mortgage Payment and any other obligations between mortgage closing and the beginning of the receipt of the income.

xiv. Trust Income

a) Definition

Trust Income refers to income that is regularly distributed to a Borrower from a trust, other than trust from Tribe.

b) Required Documentation

Lenders must verify and document the existence of the Trust Agreement or other trustee statement. Lenders must also verify and document the frequency, duration, and amount of the distribution by obtaining a bank statement or transaction history from the bank.

Lenders must verify that regular payments will continue for at least the first three years of the Loan term.

c) Calculation of Effective Income

Lenders must use the income based on the terms and conditions in the Trust Agreement or other trustee statement to calculate Effective Income.

xv. Annuities or Similar

a) Definition

Annuity Income refers to a fixed sum of money periodically paid to the Borrower from a source other than employment.

b) Required Documentation

Lenders must verify and document the legal agreement establishing the annuity and guaranteeing the continuation of the annuity for the first three years of the Loan. The Lenders must also obtain a bank statement or a transaction history from a bank evidencing receipt of the annuity.

c) Calculation of Effective Income

Lenders must use the current rate of the annuity to calculate Effective Income.

Lenders must subtract any of the assets used for the Borrower's required funds to close to purchase the subject Property from the Borrower's liquid assets prior to calculating any Annuity Income.

xvi. Notes Receivable Income

a) Definition

Notes Receivable Income refers to income received by the Borrower as payee or holder in due course of a promissory Note or similar credit instrument.

b) Required Documentation

Lenders must verify and document the existence of the Note. Lenders must also verify and document that payments have been consistently received for the previous 12 months by obtaining tax returns, deposit slips or canceled checks and that such payments are guaranteed to continue for the first three years of the Loan.

c) Calculation of Effective Income

For Borrowers who have been and will be receiving a consistent amount of Notes Receivable Income, Lenders must use the current rate of income to calculate Effective Income. For Borrowers whose Notes Receivable Income fluctuates, Lenders must use the average of the Notes Receivable Income received over the previous year to calculate Effective Income.

xvii. Nontaxable Income (Grossing Up)

a) Definition

Nontaxable Income refers to types of income not subject to federal taxes, which includes, but is not limited to:

- some portion of Social Security Income;
- some federal government employee Retirement Income;
- Railroad Retirement benefits;
- some state government Retirement Income;
- certain types of disability and Public Assistance payments;
- Child Support;
- military allowances;
- some Treaty Rights and Trust Land income;
- some Per Capita income; and
- other income that is documented as being exempt from federal income taxes.

b) Required Documentation

Lenders must document and support the amount of income to be Grossed Up for any Nontaxable Income source and the current tax rate applicable to the Borrower's income that is being Grossed Up.

c) Calculation of Effective Income

The amount of continuing tax savings attributed to Nontaxable Income may be added to the Borrower's gross income.

The percentage of Nontaxable Income that may be added cannot exceed the lesser of 25 percent or the appropriate tax rate for the income amount, based on the Borrower's tax rate for the previous year. If the Borrower was not required to file a federal tax return for the previous tax reporting period, Lenders may Gross Up the Nontaxable Income by 25 percent.

Lenders must not make any additional adjustments or allowances based on the number of the Borrower's dependents.

xviii. Foster Care Payment

a) Definition

Foster Care Payment refers to payment received from a tribal, state- or county-sponsored organization for providing temporary care for one or more individuals.

b) Standard

Foster care payment may be considered acceptable and stable income if the Borrower has a two-year history of providing foster care services and receiving foster care payment and that the foster care payment is reasonably likely to continue.

c) Required Documentation

Lenders must obtain a written verification of foster care payment from the organization providing it, verify and document that the Borrower has a two-year history of providing foster care services and receiving foster care payment, and that the foster care payment is reasonably likely to continue.

d) Calculation of Effective Income

Lenders must calculate foster care payment by using the lesser of:

- average foster care payment received over the previous two years; or
- average foster care payment received over the previous year.

xix. Foreign Income

a) Definition

Foreign Income refers to income received by a Borrower from sources located outside of the United States by a foreign corporation or a foreign government and is paid in foreign currency.

b) Standard

Lenders may use Foreign Income as Effective Income if the Borrower has received this income for the previous two years and it is reasonably likely to continue.

c) Required Documentation

Lenders must obtain complete individual federal income tax returns showing Foreign Income for the most recent two years, including all schedules.

For all Foreign Income, Lenders must the requirements listed based on source and type of income as outlined in Income Requirements.

If the Foreign Income documents are not received in English, the Lenders must provide a complete and accurate translation for each document and convert foreign currency to U.S. dollars.

3. Asset Requirements

a. General Asset Requirements

Lenders may only consider assets derived from acceptable sources in accordance with the requirements outlined below.

Closing costs, prepaid items and other fees may not be applied toward the Borrower's MRI.

i. Earnest Money Deposit

Lenders must verify and document the deposit amount and source of funds if the amount of the earnest money deposit exceeds 1 percent of the sales price or is excessive based on the Borrower's history of accumulating savings, by obtaining:

- a copy of the Borrower's canceled check;
- certification from the deposit-holder acknowledging receipt of funds;
- a Verification of Deposit (VOD) or bank statement showing that the average balance was sufficient to cover the amount of the earnest money deposit at the time of the deposit; or
- direct verification by a TPV, subject to the following requirements:
  - the Borrower has authorized the DG Lender to verify assets;
  - the date of the completed verification conforms with Section 184 requirements in Maximum Age of Loan Documents; and
  - the information shows that the average balance was sufficient to cover the amount of the earnest money deposit at the time of the deposit.

If the source of the earnest money deposit was a Gift, Lenders must verify that the Gift is in compliance with Gifts (Personal and Equity) (Manual).

ii. Cash to Close

Lenders must document all funds that are used for the purpose of qualifying for or closing a Loan, including those to satisfy debt or pay costs outside of closing.

Lenders must verify and document that the Borrower has sufficient funds from an acceptable source to facilitate the closing.

Lenders must verify and source the earnest money deposit if needed as Cash to Close.

a) Determining Amount Needed for Closing

For a purchase transaction, the amount of cash needed by the Borrower to close a Section 184 Loan is the difference between the total cost to acquire the Property and the total loan amount.

For a refinance transaction, the amount of cash needed by the Borrower to close a Section 184 Loan is the difference between the total payoff requirements of the Loan being refinanced and the total loan amount.

b) DG Lender Responsibility for Estimating Settlement Requirements

In addition to the MRI, additional Borrower expenses must be included in the total amount of cash that the Borrower must provide at loan settlement.

(1) Origination Fees and Other Closing Costs

Lenders may charge a reasonable origination fee.

Lenders may charge and collect from Borrowers those customary and reasonable closing costs and prepaid items necessary to close the Loan. Charges may not exceed the actual costs.

(2) Discount Points

Discount Points refer to a charge from the Lenders for the interest rate chosen. They can be paid by the Borrower and become part of the total cash required to close.

The agreed upon interest rate must not be based on Lenders' risk-based pricing, if any.

(3) Types of Prepaid Items (Including Per Diem Interest)

Prepaid items may include flood and hazard insurance premiums, MIP, real estate taxes, and per diem interest. They must comply with the requirements of the CFPB.

(4) Non-realty or Personal Property

Non-realty or Personal Property items (chattel) that the Borrower agrees to pay for separately, including all ineligible cost amounts subtracted from the sales price when determining the maximum Loan, are included in the total cash requirements for the Loan.

(5) Upfront Loan Guarantee Fee

Any Upfront Loan Guarantee (LG) Fee amount paid in cash must be added to the total Cash to Close requirements. The Upfront LG Fee may be entirely financed, paid entirely in cash or partially financed and partially paid in cash. When the Upfront LG Fee is financed into the Loan, the amount financed must be in whole dollar amounts and any remaining amount must be paid in cash.

(6) Real Estate Agent Fees

If a Borrower is represented by a real estate agent and must pay any fee directly to the agent, that expense must be included in the total of the Borrower's Cash to Close requirements.

(7) Repairs and Improvements

Repairs and improvements, or any portion paid by the Borrower that cannot be financed into the Loan, are part of the Borrower's total Cash to Close requirements.

(8) Premium Pricing on Section 184-Guaranteed Loans

Premium Pricing refers to the aggregate credits from a DG Lender at the interest rate chosen.

Premium Pricing may be used to pay a Borrower’s actual closing costs and prepaid items. Premium Pricing is not included as part of the Interested Party limitation unless the DG Lender is the property seller, real estate agent, builder or developer. Extra Credits from Premium pricing may not be used for the borrowers MRI or given back to the borrower in the form of cash. Any excess may be used to reduce the principal balance of the loan.

The funds derived from a premium priced Loan:

- must be disclosed in accordance with RESPA.
- must be used to reduce the principal balance if the credit amount exceeds the actual dollar amount for closing costs and prepaid items; and
  may not be used for payment of debts, collection accounts, escrow shortages or missed Loan Payments, or Judgments.

(9) Interested Party Contributions on the Closing Disclosure

Lenders may apply Interested Party credits toward the Borrower’s origination fees, other closing costs including any items POC, prepaid items, and Discount Points.

The refund of the Borrower’s POCs may be used toward the Borrower’s MRI if the DG Lender documents that the POCs were paid with the Borrower’s own funds.

Lenders must identify the total Interested Party credits on the front page of the Closing Disclosure or similar legal document or in an addendum. Lenders must identify each item paid by Interested Party Contributions.

(10) Real Estate Tax Credits

Where real estate taxes are paid in arrears, the seller’s real estate tax credit may be used to meet the MRI, if Lenders documents that the Borrower had sufficient assets to meet the MRI and the Borrower paid closing costs and other prepaid items at the time of underwriting, without consideration of the real estate tax credit.

This permits the Borrower to bring a portion of their MRI to the closing and combine that portion with the real estate tax credit for their total MRI.

iii. Reserves

Reserves refer to the sum of the Borrower's verified and documented liquid assets minus the total funds the Borrower is required to pay at closing.

Reserves do not include:

- the amount of cash taken at settlement in cash-out transactions;
- incidental cash received at settlement in other loan transactions;
- gift funds;
- equity in another Property; or
- borrowed funds from any source.

Lenders must verify and document Reserves when using them as a compensating factor.

b. Source Requirements for the Borrower’s Minimum Required Investment

i. Definition

Minimum Required Investment (MRI) refers to the Borrower’s contribution in cash or its equivalent required by Section 184 Program requirements which represents at least 1.25 percent if base loan amount is less than $50,000, and 2.25 percent if base loan amount is greater than $50,000.

ii. Standard

Lenders may only permit the Borrower’s MRI to be provided by a source permissible under Section 184 Program administrative guidance. The funds for the Borrower’s MRI must not come from:

- the seller of the Property;
- any other person or entity who financially benefits from the transaction (directly or indirectly); or
- anyone who is or will be reimbursed, directly or indirectly, by any party included in (1) or (2) above.

Lenders must document permissible sources for the full MRI.

Tribes, Tribal entities, and other Governmental Entities, when acting in their governmental capacity, may provide the Borrower with funding for the MRI when the Governmental Entity is providing the funding through one of its homeownership programs.

iii. Required Documentation

Where the Borrower’s MRI is provided by someone other than the Borrower, Lenders must also obtain documentation to support the permissible nature of the source of those funds.

- To establish that the Governmental Entity provided the Borrower’s MRI in accordance with Section 184 guidelines. Lenders must document that the Governmental Entity provided the MRI funds from funds legally belonging to the Governmental Entity, when acting in their governmental capacity, at or before closing.

- The funds legally belong to the Governmental Entity, when acting in their governmental capacity, at or before closing.

Lenders must obtain:

- a canceled check, evidence of wire transfer, or other draw request showing that prior to or at the time of closing the Governmental Entity had authorized a draw of the funds provided toward the Borrower’s MRI from the Governmental Entity’s account; or

- a letter from the Governmental Entity, signed by an authorized official, establishing that the funds provided toward the Borrower’s MRI were funds legally belonging to the Governmental Entity, when acting in their governmental capacity, at or before closing.

Where a letter from the Governmental Entity is submitted, the precise language of the letter may vary, but must demonstrate that the funds provided for the Borrower’s MRI legally belonged to the Governmental Entity at or before closing, by stating, for example:

- the Governmental Entity has at or before closing, incurred a legally enforceable liability as a result of its agreement to provide the funds toward the Borrower’s MRI;

- the Governmental Entity has at or before closing, incurred a legally enforceable obligation to provide the funds toward the Borrower’s MRI; or

- the Governmental Entity has at or before closing, authorized a draw on its account to provide the funds toward the Borrower’s MRI.

While Lenders are not required to document the actual transfer of funds in satisfaction of the obligation or liability, the failure of the Governmental Entity to satisfy the obligation or liability may result in a determination that the funds were provided by a prohibited source.

c. Sources of Funds

Lenders must verify liquid assets for cash to close and Reserves as indicated.

i. Checking and Savings Accounts

a) Definition

Checking and Savings Accounts refer to funds from Borrower-held accounts in a financial institution that allows for withdrawals and deposits.

b) Standard

Lenders must verify and document the existence of and amounts in the Borrower’s checking and savings accounts.

For recently opened accounts and recent individual deposits of more than 1 percent of the Adjusted Value, Lenders must obtain documentation of the deposits. The DG Lender must also verify that no debts were incurred to obtain part, or all, of the MRI.

c) Required Documentation

(1) Traditional Documentation

Lenders must obtain:

- a written VOD and the Borrower’s most recent statement for each account; or

- direct verification by a TPV vendor of the Borrower's account covering activity for a minimum of the most recent available month's activity for a minimum of one month, subject to the following requirements:

    - the Borrower has authorized the DG Lender to use a TPV vendor to verify assets; and
    - the date of the data contained in the completed verification is current within 30 days of the date of the verification.

(2) Alternative Documentation

If a VOD is not obtained, a statement showing the previous month's ending balance for the most recent month is required. If the previous month's balance is not shown, Lenders must obtain statement(s) for the most recent two months.

ii. Cash on Hand

a) Definition

Cash on Hand refers to cash held by the Borrower outside of a financial institution.

b) Standard

Lenders must verify that the Borrower's Cash on Hand is deposited in a financial institution or held by the escrow/title company.

c) Required Documentation

Lenders must verify and document the Borrower's Cash on Hand by obtaining an explanation from the Borrower describing how the funds were accumulated and the amount of time it took to accumulate the funds.
Lenders must also determine the reasonableness of the accumulation based on the time during which the funds were saved and the Borrower's:

- income stream;
- spending habits;
- documented expenses; and
- history of using financial institutions.

Lenders must document their determination of the acceptability of the Cash on Hand through a memo to the file.

iii. Retirement Accounts

a) Definition

Retirement Accounts refer to assets accumulated by the Borrower for the purpose of retirement.

b) Standard

Lenders may include up to 60 percent of the value of assets, less any existing loans, from the Borrower's retirement accounts, such as IRAs, Thrift Savings plans, 401(k)/403(b) plan, and Keogh accounts, unless the Borrower provides conclusive evidence that a higher percentage may be withdrawn after subtracting any federal income tax and withdrawal penalties.

Borrowers of retirement age may have 80 percent of the value of assets, less any existing loans for retirement accounts such as IRAs, Thrift Savings Plans, 401(k)/403(b) plan and Keogh accounts used as a part of their application.

The portion of the assets not used to meet closing requirements, after adjusting for taxes and penalties, may be counted as Reserves.

c) Required Documentation

Lenders must obtain the most recent monthly or quarterly statement to verify and document the existence and amounts in the Borrower's retirement accounts, the Borrower's eligibility for withdrawals, and the terms and conditions for withdrawal from any retirement account.

If any portion of the asset is required for funds to close, evidence of liquidation is required.

iv. Stocks and Bonds

a) Definition

Stocks and Bonds are investment assets accumulated by the Borrower.

b) Standard

Lenders must determine the value of the stocks and bonds from the most recent monthly or quarterly statement.

If the stocks and bonds are not held in a brokerage account, Lenders must determine the current value of the stocks and bonds through TPV. Government- issued savings bonds are valued at the original purchase price, unless the Lenders verifies and documents that the bonds are eligible for redemption when cash to close is calculated.

c) Required Documentation

Lenders must verify and document the existence of the Borrower’s stocks and bonds by obtaining brokerage statement(s) for each account for the most recent two months. Evidence of liquidation is not required.

For stocks and bonds not held in a brokerage account Lenders must obtain a copy of each stock or bond certificate.

v. Private Savings Club

a) Definition

Private Savings Club refers to a non-traditional method of saving by making deposits into a member-managed resource pool.

b) Standard

DG Lenders may consider Private Savings Club funds that are distributed to and received by the Borrower as an acceptable source of funds.

Lenders must verify and document the establishment and duration of the club, and the Borrower’s receipt of funds from the club. Lender must also determine that the received funds were reasonably accumulated, and not borrowed.

c) Required Documentation

Lenders must obtain the club's account ledgers and receipts, and a verification from the club treasurer that the club is still active.

vi. Gifts

a) Definition

Gifts refer to the contributions of cash or equity with no expectation of repayment.

b) Standards for Gifts

(1) Acceptable Sources of Gifts Funds

Gifts may be provided by:

- the Borrower's Family Member;
- the Borrower's employer or labor union;
- a close friend with a clearly defined and documented interest in the Borrower;
- a charitable organization;
- a Tribal, state or local governmental agency or public entity that has a program providing homeownership assistance to:
    - Tribal members; or
    - low- or moderate-income families; or
    - first-time homebuyers.

Any Gift of the Borrower's MRI must also comply with the additional requirements set forth in Source Requirements for the Borrower's Minimum Required Investment.

(2) Reserves

Surplus gift funds may not be considered as cash Reserves.

(3) Donor's Source of Funds

Cash on Hand is not an acceptable source of donor gift funds.

c) Required Documentation

Lenders must obtain a gift letter signed and dated by the donor and Borrower that includes the following:

(1) the donor's name, address, telephone number;

(2) the donor's relationship to the Borrower;

(3) the dollar amount of the Gift; and

(4) a statement that no repayment is required.

Documenting the Transfer of Gifts.

Lenders must verify and document the transfer of Gifts from the donor to the Borrower in accordance with the requirements below:

(5) If the gift funds have been verified in the Borrower's account, obtain the donor's bank statement showing the withdrawal and evidence of the deposit into the Borrower's account.

(6) If the gift funds are not verified in the Borrower's account, obtain the certified check or money order or cashier's check or wire transfer or other official check evidencing payment to the Borrower or settlement agent, and the donor's bank statement evidencing sufficient funds for the amount of the Gift.

(7) For Gifts of land, obtain proof of ownership by the donor and evidence of the transfer of title to the Borrower.

If the gift funds are being borrowed by the donor and documentation from the bank or other savings account is not available, Lenders must have the donor provide written evidence that the funds were borrowed from an acceptable source, not from an Interested Party.

Lenders and their Affiliates are prohibited from loaning funds to the donor who will use them as gift funds unless the terms of the loan are equivalent to those available to the general public.

Regardless of when gift funds are made available to a Borrower or settlement agent, Lenders must be able to make a reasonable determination that the gift funds were not provided by an unacceptable source.

d) Standards of Gifts of Equity

(1) Who May Provide Gifts of Equity

Only Family Members may provide equity credit as a Gift on Property being sold to other Family Members.

(2) Required Documentation

Lenders must obtain a gift letter signed and dated by the donor and Borrower that includes the following:

- the donor's name, address, telephone number;
- the donor's relationship to the Borrower;
- the dollar amount of the Gift; and
- a statement that no repayment is required.

vii. Interested Party Contributions

a) Definition

Interested Parties refer to sellers, real estate agents, builders, developers, Lenders, or other parties with an interest in the transaction.

Interested Party Contribution refers to a payment by an Interested Party, or combination of parties, toward the Borrower's origination fees, other closing costs including any items POC, prepaid items, and Discount Points.

b) Standard

An Interested Party or a combination of all Interested Parties may contribute up to 6 percent of the sales price toward the Borrower's origination fees, other closing costs, prepaid items, and Discount Points. The 6 percent limit also includes:

- Interested Party payment for permanent and temporary interest rate buydowns, and other payment supplements;

- payments of loan interest for fixed rate Mortgages;
- Loan Payment protection insurance; and
- payment of the Upfront LG Fee.

Interested Party Contributions that exceed actual origination fees, other closing costs, prepaid items, and Discount Points are considered an inducement to purchase. Interested Party Contributions exceeding 6 percent are considered an inducement to purchase.

Interested Party Contributions may not be used for the Borrower's MRI.

c) Exceptions

Premium Pricing credits from the Lenders are excluded from the 6 percent limit provided Lenders are not the seller, real estate agent, builder or developer.

Payment of real estate agent commissions or fees, typically paid by the seller under local or state law, or local custom, is not considered an Interested Party Contribution. The satisfaction of a PACE lien or obligation against the Property by the property owner is not considered an Interested Party Contribution.

d) Required Documentation

Lenders must document the total Interested Party Contributions on the sales contract or applicable legally binding document, *Section 184/184A Loan Mortgage Credit Analysis Worksheet*, and Closing Disclosure or similar legal document. When a legally binding document other than the sales contract is used to document the Interested Party Contributions, the DG Lender must provide a copy of this document to the assigned Appraiser.

viii. Inducements to Purchase

Inducements to Purchase refer to certain expenses paid by the seller and/or another Interested Party on behalf of the Borrower and result in a dollar-for-dollar reduction to the purchase price when computing the acquisition cost of property before applying the appropriate Loan-to-Value (LTV) percentage.

These inducements include, but are not limited to:

- contributions exceeding 6 percent of the purchase price;
- contributions exceeding the origination fees, other closing costs, prepaid items, and Discount Points;
- decorating allowances;
- repair allowances;
- excess rent credit;
- moving costs;
- paying off consumer debt;
- Personal Property; or
- sales commission on the Borrower's present residence; and below-market rent, except for Borrowers who meet the Identity-of-Interest exception for Family Members.

a) Personal Property

Replacement of existing Personal Property items listed below are not considered an inducement to purchase, provided the replacement is made prior to settlement and no cash allowance is given to the Borrower. The inclusion of the items below in the sales agreement is also not considered an inducement to purchase if inclusion of the item is customary for the area:

- range;
- refrigerator;
- dishwasher;
- washer;
- dryer;

- carpeting;
- window treatment; or
- other items determined appropriate by the ONAP.

b) Sales Commission

An inducement to purchase exists when the seller and/or Interested Party agrees to pay any portion of the Borrower's sales commission on the sale of the Borrower's present residence.

An inducement to purchase also exists when a Borrower is not paying a real estate commission on the sale of their present residence, and the same real estate broker or agent is involved in both transactions, and the seller is paying a real estate commission on the Property being purchased by the Borrower that exceeds what is typical for the area.

c) Rent Below Fair Market

A reduced rent is an inducement to purchase when the sales contract includes terms permitting the Borrower to live in the Property rent-free or has an agreement to occupy the Property at a rental amount greater than 10 percent below the Appraiser's estimate of fair market rent. When such an inducement exists, the amount of inducement is the difference between the rent charged and the Appraiser's estimate of fair market rent pro-rated over the period between execution of the sales contract and execution of the Property sale.

Rent below fair market is not considered an inducement to purchase when a builder fails to deliver a Property at an agreed-upon time and permits the Borrower to occupy an existing or other unit for less than market rent until construction is complete.

ix. Downpayment Assistance Programs

Downpayment Assistance Program Providers must meet requirements in Chapter I, Subsection E.

a) Ineligible Uses

Downpayment Assistance Program Providers assisting borrowers with a loan intended for the Section 184 Program may not provide Gifts to pay off the Borrower's:

- Installment Loans;
- Credit Cards;
- Collections;
- Judgments;
- Liens; and Similar Debts

Lenders must ensure that a downpayment assistance provided by the Downpayment Assistance Program Provider meets the appropriate Section 184 requirements, and that the transfer of funds is properly documented.

b) Downpayment Assistance Conditions

Downpayment Assistance must meet the following minimum conditions:

- The Downpayment Assistance must be subordinate to the Section 184 Guaranteed Loan.
- The Downpayment Assistance must be forgivable under terms prescribed by the Downpayment Assistance Provider.
- The Downpayment Assistance accrues no interest during the term of the Section 184 Guaranteed Loan.

c) Maximum Combined Loan-to-Value

The CLTV for Downpayment Assistance must not exceed 100% of the lower of appraised value or acquisition cost.

d) Nonprofits assisting a Governmental Entity in the operation of its secondary financing programs

Nonprofits assisting a Governmental Entity in the operation of its secondary financing programs must have HUD approval and placement on the Nonprofit Organization Roster unless there is a documented agreement that:

- specifies the functions performed are within the Governmental Entity's secondary financing program; and
- names the Governmental Entity as the DG Lender in the secondary financing legal documents (Note and Deed of Trust).

Secondary financing that will close in the name of the nonprofit and be held by a Governmental Entity must be made by a HUD-approved Nonprofit.

Secondary financing provided by Governmental Entities may be used to meet the Borrower's MRI. Any loan of the Borrower's MRI must also comply with the additional requirements set forth in Source Requirements for the Borrower's Minimum Required Investment.

Required Documentation

- A letter from the Governmental Entity on their letterhead evidencing the relationship between them and the nonprofit for each Section 184-guaranteed Loan, signed by an authorized official and containing the following information:

  - the Section 184 case number for the first Loan.
  - the complete property address.
  - the name, address and Tax ID for the nonprofit.
  - the name of the Borrower(s) to whom the nonprofit is providing secondary financing;
  - the amount and purpose for the secondary financing provided to the Borrower; and

- A statement indicating whether the secondary financing:

  - will close in the name of the Governmental Entity; or
  - will be closed in the name of the nonprofit and held by the Governmental Entity.

Nonprofits assisting a Governmental Entity in the operation of its secondary financing programs must have HUD approval and placement on the Nonprofit Organization Roster unless there is a documented agreement that:

- specifies the functions performed are within the Governmental Entity's secondary financing program; and
- names the Governmental Entity as the DG Lender in the secondary financing legal documents (Note and Deed of Trust).

Where a nonprofit meets the criteria identified in Section 115 of the IRC for exclusion of taxation, the nonprofit must provide one of the following:

- a letter from the organization's auditor; or
- a written statement from the organization's General Counsel, as an official of the organization.

e) Gifts from Charitable Organizations that Lose or Give Up Their Federal Tax-Exempt Status

If a charitable organization makes a Gift that is to be used for all, or part, of a Borrower's downpayment, and the organization providing the Gift loses or gives up its federal tax-exempt status, Section 184 will recognize the Gift as an acceptable source of the downpayment provided that:

- the Gift is made to the Borrower;
- the Gift is properly documented; and
- the Borrower has entered into a contract of sale (including any amendments to purchase price) on or before the date the IRS officially announces that the charitable organization's tax-exempt status is terminated.

x. Secondary Financing

Secondary Financing is any financing other than the first Loan that creates a lien against the Property.

a) Standard

The Section 184 Program will guarantee a first Loan on a Property that has a subordinate lien provided that:

- the secondary financing is disclosed at the time of the Section 184 loan application.
- no costs associated with the secondary financing are financed into the Section 184-guaranteed first Loan.
- the guaranteed first Loan does not exceed the Section 184 Maximum Loan Limits for the area in which the Property is located.
- the secondary financing payments, if any, are included when qualifying the Borrower.
- any secondary financing of the Borrower's MRI must come from the Borrower's own funds, gifts, or Tribal, State, or local funds awarded to the Borrower.
- the secondary financing does not result in cash back to the Borrower except for refund of earnest money deposit or other Borrower costs paid outside of closing.
- The second mortgage must be for a fixed term, have equal monthly payments and may not contain any balloon payment.
- The minimum fixed term for a second mortgage is 5 years.

b) Maximum CLTV

The maximum Combined Loan-to-Value (CLTV) for secondary financing loans is 97.75 percent for loans greater than $50,000 and 98.75 for loans $50,000 or less.

c) Required Documentation

Lenders must obtain from the provider of any secondary financing:

- documentation showing the amount of funds provided to the Borrower for each transaction;

- copies of the Deed of Trust/Mortgage and Note.

d) Secondary Financing Provided by Eligible Non-Profit Organizations

(1) Definition

A non-profit organization established under Tribal law or organization of the type described in section 501(c)(3) of the Internal Revenue Code of 1986 as an organization exempt from taxation under section 501(a) of the Code. The Eligible Non-Proft Organization must have:

- Two years' experience as a provider of downpayment assistance;
- A voluntary board; and

- No part of its net earnings inure to the benefit of any member, founder, contributor or individual.

(2) Standard

A Non-Profit Organization may provide secondary financing to the Borrower so long as the secondary financing complies with 24 CFR 1005.439(b)-(d).

(3) Required Documentation

A copy of the Internal Revenue Service 501(c)(3) determination letter.

e) Family Members

(1) Standard

The Section 184 Program will guarantee a first Loan on a Property that has a second Loan or lien held by a Family Member, provided that:

- the secondary financing is disclosed at the time of application;

- no costs associated with the secondary financing are financed into the loan intended for the Section 184 Program;

- the secondary financing payments must be included in the total Loan Payment;

- the secondary financing must not result in cash back to the Borrower except for refund of earnest money deposit or other Borrower costs paid outside of closing;

- the secondary financing may be used to meet the Borrower's MRI;

- the CLTV ratio of the Base Loan Amount and secondary financing amount must not exceed 100 percent of the Adjusted Value.

- the second lien may not provide for a balloon payment within 10 years from the date of execution;

- there is no prepayment penalty;

- if the Family Member providing the secondary financing borrows the funds, the lending source may not be an entity with an Identity of Interest in the sale of the Property, such as the:

    - seller;

    - builder;

    - loan originator; or

    - real estate agent;

- if funds loaned by the Family Member are borrowed from an acceptable source, the Borrower may not be a co-Obligor on the Note;

- if the loan from the Family Member is secured by the subject Property, only the Family Member provider may be the Note holder; and

- the secondary financing provided by the Family Member must not be transferred to another entity at or subsequent to closing.

(2) Required Documentation

Lenders must obtain from the provider of any secondary financing:

- documentation showing the amount of funds provided to the Borrower for each transaction and source of funds; and

- copies of the Loan and Note.

If the secondary financing funds are being borrowed by the Family Member and documentation from the bank or other savings account is not available, DG Lenders must have the Family Member provide written evidence that the funds were borrowed from an acceptable source, not from a party to the transaction, including DG Lenders.

f) Loans

A Loan refers to an arrangement in which a lender, outside of the Section 184 Loan Guarantee program, gives money to a Borrower and the Borrower agrees to repay the money.

(1) Collateralized Loans

a) Definition

A Collateralized Loan is a loan that is fully secured by a financial asset of the Borrower, such as deposit accounts, certificates of deposit, investment accounts, or property. These assets may include stocks, bonds, and real estate other than the Property being purchased.

b). Standard

Loans secured against deposited funds, where repayment may be obtained through extinguishing the asset, do not require consideration of repayment for qualifying purposes. DG Lenders must reduce the amount of the corresponding asset by the amount of the collateralized loan.

(2) Who May Provide Collateralized Loans

Only an independent third party **may** provide the borrowed funds for collateralized loans.

The seller, real estate agent or broker, lender, or other Interested Party **may not** provide such funds. Unacceptable borrowed funds include:

- unsecured signature loans;
- cash advances on credit cards;
- borrowing against household goods and furniture; and
- other similar unsecured financing.

(3) Required Documentation

Lenders must verify and document the existence of the Borrower's assets used to collateralize the loan, the promissory Note securing the asset, and the loan proceeds.

g) Retirement Account Loans

(1) Definition

A Retirement Account Loan is a loan that is secured by the Borrower's retirement assets.

(2) Standard

Lenders must reduce the amount of the retirement account asset by the amount of the outstanding balance of the retirement account loan.

(3) Required Documentation

Lenders must verify and document the existence and amounts in the Borrower's retirement accounts and the outstanding loan balance.

xi. Employer Assistance

a) Definition

Employer Assistance refers to benefits provided by an employer to relocate the Borrower or assist in the Borrower's housing purchase, including closing costs, prepaid items, Upfront Fee, or any portion of the MRI. Employer Assistance does not include benefits provided by an employer through secondary financing.

A salary advance cannot be considered as assets to close.

b) Standard

(1) Relocation Guaranteed Purchase

Lenders may allow the net proceeds (relocation guaranteed purchase price minus the outstanding liens and expenses) to be used as cash to close.

(2) Employer Assistance Plans

The amount received under Employer Assistance Plans may be used as cash to close.

c) Required Documentation

(2) Relocation Guaranteed Purchase

If the Borrower is being transferred by their company under a guaranteed sales plan, Lenders must obtain an executed buyout agreement signed by all parties and receipt of funds indicating that the employer or relocation service takes responsibility for the outstanding loan debt and outlines expenses to be paid on behalf of the borrower.

Lenders must verify and document the agreement guaranteeing employer purchase of the Borrower's previous residence and the net proceeds from sale.

(3) Employer Assistance

Lenders must verify and document the Borrower's receipt of assistance. If the employer provides this benefit after settlement, Lenders must verify and document that the Borrower has sufficient cash for closing.

xii. Sale of Personal Property

a) Definition

Personal Property refers to tangible property, other than Real Property, such as cars, recreational vehicles, stamps, coins, or other collectibles.

b) Standard

The DG Lender must use the lesser of the estimated value or actual sales price when determining the sufficiency of assets to close.

c) Required Documentation

Borrowers may sell Personal Property to obtain cash for closing.

Lenders must obtain a satisfactory estimate of the value of the item, a copy of the bill of sale, evidence of receipt, and deposit of proceeds. A value estimate may take the form of a published value estimate issued by organizations such as automobile dealers, philatelic or numismatic associations, or a separate written appraisal by a qualified Appraiser with no financial interest in the loan transaction.

xiii. Sale of Real Property

a) Definition

The Sale of Real Property refers to the sale of Property currently owned by the Borrower.

b) Standard

Net proceeds from the Sale of Real Property may be used as an acceptable source of funds.

c) Required Documentation

Lenders must verify and document the ownership of the real property by the borrower, actual sale and the Net Sale Proceeds by obtaining a fully executed Closing Disclosure or similar legal document.

Lenders must also verify and document that it is an Arm's Length Transaction, and that the Borrower is entitled to the Net Sale Proceeds.

xiv. Real Estate Commission from Sale of a Subject Property

a) Definition

Real Estate Commission from Sale of Subject Property refers to the Borrower's (i.e., buyer's) portion of a real estate commission earned from the sale of the Property being purchased.

b) Standard

Lenders may consider Real Estate Commissions from Sale of Subject Property as part of the Borrower's acceptable source of funds if the Borrower is a licensed real estate agent.

A Family Member entitled to the commission may also provide it as a Gift, in compliance with standard gift requirements.

c) Required Documentation

Lenders must verify and document that the Borrower, or Family Member giving the commission as a Gift, is a licensed real estate agent, and is entitled to a real estate commission from the sale of the Property being purchased. All other Gift requirements must also be met. See subsection D.3.c.vi.

xv. Sweat Equity

a) Definition

Sweat Equity refers to labor performed, or materials furnished, by or on behalf of the Borrower before closing on the Property being purchased.

b) Standard

Lenders may consider the reasonable estimated cost of the work or materials as an acceptable source of funds.

Sweat Equity provided by anyone other than the Borrower can only be used as an MRI if it meets the Source Requirements for the Borrower's Minimum Required Investment.

Lenders may consider any amount as Sweat Equity that has not already been included in the mortgage amount. The Lenders may not consider clean up, debris removal, and other general maintenance, and work to be performed using repair escrow as Sweat Equity.

Cash back to the Borrower is not permitted in Sweat Equity transactions.

c) Required Documentation

For materials furnished, Lenders must obtain evidence of the source of funds and the Market Value of the materials.
For labor, Lenders must verify and document that the work will be completed in a satisfactory manner. The Lender must also obtain evidence of Contributory Value of the labor either through an Appraiser's estimate, or a cost-estimating service.

- For labor on Existing Construction, the Lender must also obtain an appraisal indicating the repairs or improvements to be performed. (Any work completed or materials provided before the appraisal are not eligible).

- For labor on New Construction, the Lender must also obtain the sales contract indicating the tasks to be performed by the Borrower during construction.

xvi. Trade Equity

a) Definition

Trade Equity refers to when a Borrower trades their Real

Property to the seller as part of the cash investment.

b) Standard

The amount of the Borrower's equity contribution is determined by:

- using the lesser of the Property's appraised value or sales price; and
- subtracting all liens against the Property being traded, along with any real estate commission.

If the Property being traded has a Section 184-insured Loan, assumption processing requirements and restrictions apply.

c) Required Documentation

Lenders must obtain a residential appraisal report complying with Section 184 appraisal policy to determine the Property's value. Lenders must also obtain the Closing Disclosure or similar legal document to document the sale of the Property.

xvii. Rent Credits

a) Definition

Rent Credits refer to the amount of the rental payment that exceeds the Appraiser's estimate of fair market rent.

b) Standard

DG Lenders may use the cumulative amount of rental payments that exceeds the Appraiser's estimate of fair market rent toward the MRI.

c) Required Documentation

Lenders must obtain the rent with option to purchase agreement, the Appraiser's estimate of market rent, and evidence of rental payments made in accordance with the rent with option to purchase agreement.

4. Final Direct Guarantee Underwriting Decision; Debt-To-Income Rations

DG Underwriters are responsible for making an underwriting decision on behalf of their Direct Guarantee Lender in compliance with all Section 184 Program requirements.

a. DG Underwriter Duty of Care/Due Diligence

DG Underwriters must exercise the same level of care that would be used in underwriting a mortgage entirely dependent on the property as security. Compliance with Section 184 Program requirements is the minimum standard of due diligence required in originating and underwriting a loan intended for guarantee under the Section 184 Program.

b. Specific DG Underwriter Responsibilities

DG Underwriters must review each loan intended for the Section 184 Program as a separate and unique transaction, recognizing that there may be multiple factors that demonstrate a Borrower's ability and willingness to make timely loan payments to make an underwriting decision on behalf of their DG Lender in compliance with Section 184 Program requirements. DG Underwriters must evaluate the totality of the Borrower's circumstances and the impact of layering risks on the probability that a Borrower will be able to repay the mortgage obligation according to the terms of the Section 184 Guaranteed Loan.

The DG Underwriter must:

i. Review appraisal reports, compliance inspections, and credit analyses to ensure reasonable conclusions, sound reports, and compliance with HUD requirements regardless of who prepared the documentation;

ii. Determine the acceptability of the appraisal, the inspections, the Borrower's capacity to repay the Section 184 Guaranteed Loan, and the overall acceptability of the transaction for a Section 184 Loan Guarantee;

iii. Identify any inconsistencies in information obtained by the Lenders in the course of reviewing the Borrower's application, regardless of the materiality of such information to the origination and underwriting of a Section 184 Guaranteed Loan;

iv. Resolve all inconsistencies identified before approving the Borrower's application and document the inconsistencies and their resolutions of the inconsistencies in the file; and

v. DG Underwriters must identify and report any misrepresentations, fraud, or violations of any Section 184 Program requirements to the appropriate party within their organization.

c. Underwriting of Credit and Debt

DG underwriters must determine the creditworthiness of the Borrower, which includes analyzing the Borrower's overall pattern of credit behavior and the credit report.

The lack of traditional credit history or the Borrower's decision to not use credit may not be used as the sole basis for rejecting the Section 184 application.

Compensating factors cannot be used to compensate for any derogatory credit. DG Underwriters must ensure that no unpaid obligations are incurred in connection with the Section 184 transaction or the purchase of the Property.

d. Underwriting Income

DG Underwriters must review the income of a Borrower and verify that it has been supported with the proper documentation. See Income Requirements.

e. Underwriting Assets

DG Underwriters must review the assets of a Borrower and verify that they have been supported with the proper documentation. See Asset Requirements.

f. Verifying Loan Guarantee Fees and Section 184 Loan Amount

DG Underwriters must review the LG Fee and eligible Section 184 Loan amount and verify that they have been supported with the proper documentation. See Underwriting.

g. Calculating Qualifying Ratios

i. General Information about Qualifying Ratios

For all transactions, except non-credit qualifying Streamline Refinances, DG Underwriters must calculate the Borrower's Total Mortgage Payment to Effective Income Ratio (PTI) and the Total Fixed Payment to Effective Income ratio (DTI), and verify compliance with the ratio requirements listed in this Chapter. DG Lenders must exclude any obligation wholly secured by the Borrower's existing assets from the calculation of the Borrower's debts, provided the assets securing the debt are also not considered in qualifying the Borrower.

ii. Calculating Total Mortgage Payment

The Total Mortgage Payment includes Principal and Interest, and where applicable, the following items:

- Real Estate Taxes;
- Hazard Insurance;
- Flood Insurance;
- Annual LG Fee;
- HOA or condominium association fees or expenses;
- Ground Rent;
- special assessments;
- payments for any acceptable secondary financing; and
- any other escrow payments.

a) Estimating Real Estate Taxes

DG Lenders must use accurate estimates of monthly tax escrows when calculating the Total Mortgage Payment.

In New Construction cases and Manufactured Homes converting to real estate, property tax estimates must be based on the land and improvements.

Where real estate taxes are abated, DG Lenders may use the abated amount provided that (1) DG Lenders can document the abated amount with the taxing authority and (2) the abatement will remain in place for at least the first three years of the Mortgage.

Properties located on Trust Land typically are not subject to any Tribal or governmental real estate taxes. No estimated monthly tax escrows are required following verification with the Tribe.

b) Condominium Utility Expenses

The portion of a condominium fee that is clearly attributable to utilities may be subtracted from the HOA fees before computing qualifying ratios, provided the Borrower provides proper documentation, such as statements from the utility company.

c) Temporary Interest Rate Buydowns

DG Lenders must use the Note rate when calculating principal and interest for Loans that involve a temporary interest rate buydown.

iii. Calculating Total Fixed Payment

The Total Fixed Payment includes:

- The Total Mortgage Payment; and
- Monthly obligations on all debts and liabilities.

h. Approvable Ratio Requirements

The maximum Total Fixed Payments to Effective Income Ratio (DTI) is 41 percent.

The maximum DTI may be up to 45 percent with the following compensating factors:

i. Three active tradeline accounts with 12 months credit history.

ii. No Derogatory Credit in the last 12 months.

iii. Documented housing payment history for a period of 12 months.

AND

Two of the following:

i. Verified and documented cash Reserves from borrower's own funds (six months or greater);

ii. Housing payment increase not to exceed 15% of the Borrower's current housing payment;

iii. Significant additional income not reflected in Effective Income; or

iv. Credit score of 700 or greater

i. Documenting Acceptable Compensating Factors

The following describes the compensating factors and required documentation that may be used to justify approval of manually underwritten loans with qualifying ratio of 45 percent.

i. Verified and Documented Cash Reserves

Verified and documented cash Reserves may be cited as a compensating factor when reserves are equal to or exceed six total monthly Mortgage Payments.

Reserves are calculated as the Borrower's total assets as described in Asset Requirements less:

a) The total funds required to close the Mortgage;

b) Gifts;

c) Borrowed funds; and

d) Cash received at closing in a cash-out refinance transaction or incidental cash received at closing in the mortgage transaction.

ii. Minimal Increase in Housing Payments

The Current Total Monthly Housing Payment refers to the Borrower's current Total Mortgage Payment or current total monthly rent obligation.

A minimal increase in housing payment may be cited as a compensating factor subject to the following requirements:

a) The new total monthly Mortgage Payment does not exceed the current total monthly housing payment by more than 15 percent.

b) There is a documented 12 month housing payment history with no late payments. In cash-out transactions, all payments on the Mortgage being refinanced must have been made within the month due for the previous 12 months.

c) If the Borrower has no current housing payment, DG Lenders may not cite this compensating factor.

iii. Significant Additional Income Not Reflected in Effective Income

Additional income from Overtime, Bonuses, Part-Time or Seasonal Employment that is not reflected in Effective Income can be cited as a compensating factor subject to the following requirements:

a) Lenders must verify and document that the Borrower has received this income for at least one year, and it will likely continue; and

b) The income, if included in gross Effective Income, is sufficient to reduce the qualifying ratio to not more than 43 percent.

Income from non-borrowing spouses or other parties not obligated for the Section 184 Loan may not be counted under this criterion.

This compensating factor may be cited only in conjunction with another compensating factor when qualifying ratios exceed 47 percent but are not more than 50 percent.

j. Borrower Approval or Denial

i. Re-underwriting

DG Lenders musts re-underwrite a Section 184 loan application when any income, asset and credit data elements of the loan application changes or new Borrower information becomes available.

ii. Documentation of Final Underwriting Review Decision

DG Underwriters must complete the following documents to evidence their final underwriting decision.

For cases involving a Section 184 Loan to a HUD employee, the DG Lender completes the following and then submits the complete underwritten mortgage application to the Office of Loan Guarantee, Director, for review and issuance of a *Firm Commitment* or Rejection Notice prior to closing.

For cases involving DG Lenders that receive a Direct Guarantee Program Test Case Phase approval letter from HUD, DG Lenders completes the following and then submits the complete underwritten Section 184 loan application package to Section 184 for review and issuance of a *Firm Commitment* or Rejection Notice.

a) **Mortgage Credit Analysis Worksheet**

The DG underwriter must record the following items on form MCAW or a memo to the file attached to the MCAW and clearly reference:

- final underwriting decision;
- any compensating factors;
- any modification of the mortgage amount and approval conditions under "Underwriter Comments;" and
- Underwriter Direct Guarantee Identification Number and signature.

b) **Section 184 Addendum to URLA**

DG Underwriters must complete form HUD-5XXXX, *HUD Addendum to Uniform Residential Loan Application*, as directed in the form instructions.

An authorized officer of the DG Lender, the Borrower, and the DG Underwriter must execute form HUD-5XXX, as indicated in the instructions.

c) **Conditional Approval**

DG Underwriter must condition the approval of the Borrower on the completion of the final *URLA* (Fannie Mae Form 1003/Freddie Mac Form 65) and form HUD-5XXXX at or before closing if the DG underwriter relied on an initial *URLA* and form HUD-50111 in underwriting the Section 184 Loan.

d) **HUD Employee Loans**

If the Section 184 transaction involves a HUD employee, DG Lenders must condition the loan on the approval of the Section 184 Loan by HUD. DG Lenders must submit the case binder directly and only to the ONAP Office of Loan Guarantee Director for the final underwriting approval.

e) **Notification of Borrower Approval and Term of Approval**

DG Lenders must notify the Borrower of their approval in a timely manner. DG Underwriters' approval or the *Firm Commitment* is valid for 60 Days.

f) Responsibilities Upon Denial

When a Section 184 loan application is denied, DG Lenders must comply with all requirements of the FCRA, and the Equal Credit Opportunity Act (ECOA), as implemented by Regulation B (12 CFR Part 1002).

DG Lenders must report the rejected loan application in NTV.