4. Underwriting the Borrower Using the TOTAL Mortgage Scorecard (TOTAL)

a. Underwriting with an Automated Underwriting System (11/07/2023)

FHA's Technology Open To Approved Lenders (TOTAL) Mortgage Scorecard is not an Automated Underwriting System (AUS) but a scorecard that must interface through a system-to-system connection with an AUS.

Each AUS using TOTAL Mortgage Scorecard provides a Feedback Certificate/Finding Report, which documents results of the credit risk evaluation, and identifies the credit report utilized for the scoring event. The Feedback Certificate/Finding Report upon which the Mortgagee makes its underwriting decision prior to endorsement must be included in the case binder.

i. Use of TOTAL Mortgage Scorecard

All transactions must be scored through TOTAL Mortgage Scorecard, except Streamline Refinance transactions, assumptions, Mortgages made to nonprofit/Governmental Entity Borrowers, and Mortgages made to Borrowers who do not have Social Security Numbers (SSN), but who are otherwise eligible under the Social Security Number requirements.

If the Mortgage involves a HUD employee, the Mortgagee must score the transaction through TOTAL. If the file receives an Accept, the Mortgagee must underwrite the transaction in accordance with the guidance in this Underwriting the Borrower Using the TOTAL Mortgage Scorecard section. The Mortgagee must submit the underwritten mortgage application to the Processing and Underwriting Division Director at the Jurisdictional HOC for final underwriting approval.

Mortgagees using TOTAL remain solely responsible for prudent underwriting practices and the Final Underwriting Decision.

ii. Requirements for the Submission of Data through TOTAL Mortgage Scorecard

The Mortgagee must submit data to TOTAL Mortgage Scorecard through an approved AUS vendor in a data format acceptable to the AUS vendor, to meet the requirements described in the TOTAL Mortgage Scorecard Developer's Guide.

iii. Function of TOTAL Mortgage Scorecard

TOTAL Mortgage Scorecard evaluates the overall credit risk posed by the Borrower, based on a number of credit variables, when combined with the functionalities of an AUS.

The Mortgagee may not accept or deny an FHA-insured Mortgage based solely on a risk assessment generated by TOTAL Mortgage Scorecard.

The Mortgagee must ensure full compliance with all FHA eligibility requirements, and all requirements of this section. The Mortgagee must verify the information used to score the Mortgage through TOTAL but does not need to analyze the credit history, unless otherwise stated in this section, if an Accept or Approve recommendation is received.

The underwriter must still underwrite all appraisals according to standard FHA requirements.

The underwriter must fully underwrite those applications where TOTAL issues a Refer.

(A) Automated Underwriting System Data Entry Requirements

(1) Mortgagees

The Mortgagee must verify the integrity of all data elements entered into the AUS to ensure the outcome of the Mortgage credit risk evaluation is valid including:

- Borrower’s Credit Report
- Borrower’s Liabilities/Debt
- Borrower’s Effective Income
- Borrower’s Assets/Reserves
- Adjusted Value
- Borrower’s total Mortgage Payment including Principal, Interest, Taxes, and Insurance (PITI)

The Borrower’s total Mortgage Payment includes:

- Principal and Interest (P&I);
- real estate taxes;
- Hazard Insurance;
- Flood Insurance as applicable;
- Mortgage Insurance Premium;
- HOA or condominium association fees or expenses;
- Ground Rent;
- special assessments;
- payments for any acceptable secondary financing; and
- any other escrow payments.

(a) Section 8 Housing Choice Voucher

The Mortgagee may deduct the amount of the Section 8 Housing Choice Voucher if it is paid directly to the Servicer.

(b) Abated Real Estate Taxes

Where real estate taxes are abated, Mortgagees may use the abated amount provided that (1) the Mortgagee 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.

(c) Temporary Interest Rate Buydowns

The Mortgagee must use the Note rate when calculating principal and interest for Mortgages that involve a temporary interest rate buydown.

(2) Sponsored Third-Party Originators

The Mortgagee may permit a sponsored TPO to enter data into the AUS. Both the Mortgagee and its sponsored TPO must ensure and verify all data entered into the AUS. The Mortgagee remains ultimately responsible for ensuring the data entered into the AUS is correct.

The Mortgagee must ensure the Employer Identification Number (EIN) of its sponsored TPO is entered into the AUS. If the Mortgagee is using an AUS that is unable to transmit the sponsored TPO EIN, the Mortgagee must enter "6999609996" in the Lender ID field.

(B) New Versions of TOTAL Mortgage Scorecard

From time to time, FHA will release new versions of TOTAL Mortgage Scorecard. FHA will announce the date that the new version will be available. All Mortgages being scored for the first time will be scored using the new version. For Mortgages with a case number, the Mortgages will be scored using the version that was effective when the case number was assigned. Existing Mortgages scored without a case number will be scored according to the version number tag that is provided in the TOTAL file by the AUS provider (if none, then the current version will be used). All Mortgages without a case number will be scored using the new version 90 Days after the new version is implemented.

iv. Feedback Certificates: Risk Classification and Related Responsibilities (TOTAL)

If the Feedback Certificate/Finding Report shows an Accept or Approve, it will be referred to as Accept.

(A) Accept/Eligible

If the Feedback Certificate/Finding Report shows an Accept/Eligible recommendation, the Mortgage may be eligible for FHA's insurance endorsement provided the Mortgagee verified that data entered into the AUS is accurate and complete and that the entire mortgage application complies with all FHA requirements.

The Mortgagee must verify that all supporting documentation and information entered into TOTAL Mortgage Scorecard is consistent with the final underwriting decision if the Mortgage receives an Accept/Eligible.

(B) Accept/Ineligible

If the Feedback Certification/Finding Report shows an Accept/Ineligible recommendation, the Borrower's credit and capacity would meet the threshold for approval, but the Mortgage does not fully comply with FHA's eligibility requirements. The Feedback Certificate will identify the specific eligibility requirement that the Mortgage does not meet.

The Mortgagee must analyze the Feedback Certificate and determine if the reason for the ineligibility is one that can be resolved in a manner that complies with FHA underwriting requirements. If the Mortgagee can correct the reason for ineligibility, the Mortgagee may rescore the Mortgage in the AUS.

When the reason for ineligibility cannot be corrected in the AUS, the Mortgagee may underwrite the Mortgage using the following requirements for an Accept Mortgage, but must resolve the reason for ineligibility in accordance with FHA requirements and must provide an explanation of the resolution in the remarks section of form HUD-92900-LT, *FHA Loan Underwriting and Transmittal Summary*.

(C) Refer

The underwriter must manually underwrite any mortgage application for which the Feedback Certificate shows a Refer recommendation or any result other than those described above.

v. Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (TOTAL)

The Mortgagee must downgrade and manually underwrite any Mortgage that received an Accept recommendation if:

- the mortgage file contains information or documentation that cannot be entered into or evaluated by TOTAL Mortgage Scorecard;
- additional information, not considered in the AUS recommendation affects the overall insurability of the Mortgage;
- the Borrower has $1,000 or more collectively in Disputed Derogatory Credit Accounts;
- the date of the Borrower's bankruptcy discharge as reflected on bankruptcy documents is within two years from the date of case number assignment;
- the case number assignment date is within three years of the date of the transfer of title through a Pre-Foreclosure Sale (Short Sale);
- the case number assignment date is within three years of the date of the transfer of title through a foreclosure sale;

- the case number assignment date is within three years of the date of the transfer of title through a Deed-in-Lieu (DIL) of foreclosure;
- the Mortgage Payment history, for any mortgage trade line reported on the credit report used to score the application, requires a downgrade as defined in Housing Obligations/Mortgage Payment History (TOTAL);
- the Borrower has Undisclosed Mortgage Debt (TOTAL) that requires a downgrade; or
- business income shows a greater than 20 percent decline over the analysis period.

vi. Applicability of Automated Underwriting System Rules (TOTAL)

If a determination is made that the Mortgage must be downgraded to manual underwriting, the Mortgagee must cease its use of the AUS and comply with all requirements for manual underwriting when underwriting a downgraded Mortgage.

vii. TOTAL Mortgage Scorecard Tolerance Levels for Rescoring

The Mortgagee must rescore a Mortgage when any data element of the Mortgage change and/or new Borrower information becomes available.

The Mortgagee is not required to rescore a Mortgage if the following data elements change from the last scoring event within the described tolerance levels:

When assessing...	**Rescore is not required if:**
Cash Reserves	Cash Reserves verified are not less than 10% below the previously scored amount
Income	Income verified is not less than 5% below the previously scored amount
Tax and Insurance Escrow	The cumulative monthly tax and insurance escrow does not result in more than a 2% increase in the Total Mortgage Payment to Effective Income Ratio (PTI)

b. Credit Requirements (TOTAL) (11/07/2023)

i. General Credit Review Requirements (TOTAL)

The Mortgagee must obtain a credit report for each Borrower who will be obligated on the mortgage Note. The Mortgagee may obtain a joint report for individuals with joint accounts.

The Mortgagee must obtain a credit report for a non-borrowing spouse who resides in a community property state, or if the subject 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 Mortgagee 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.

ii. Credit Reports (TOTAL)

The Mortgagee must use a traditional credit report. If a traditional credit report is not available or the traditional credit report is insufficient, the Feedback Certificate will show a Refer recommendation, and the Mortgagee must manually underwrite the Mortgage.

The Mortgagee must obtain a Tri-Merged Credit Report (TRMCR) from an independent consumer reporting agency.

(A) Requirements for the Credit Report (TOTAL)

Credit reports must contain 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. The Mortgagee must retain copies of all credit reports.

The credit report must include:

- the name of the Mortgagee 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 FHA mortgage insurance purposes provided that the mortgage 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
- for each Borrower debt listed:
  - the date the account was opened
  - high credit amount

- required payment amount
- unpaid balance
- payment history

(B) New Credit Report (TOTAL)

The Mortgagee must obtain a new credit report and rescore the Mortgage through TOTAL if the underwriter identifies inconsistencies between any information in the mortgage file and the original credit report.

iii. Evaluating Credit History (TOTAL)

The Mortgagee must analyze the Borrower's credit history in accordance with the Accept Risk Classifications Requiring a Downgrade to Manual Underwriting (TOTAL) section.

If a determination is made that the Mortgage must be downgraded to manual underwriting, the Mortgagee must cease its use of the AUS and comply with all requirements for manual underwriting when underwriting a downgraded Mortgage.

(A) Collection Accounts, Charge Off Accounts, Accounts with Late Payments in the Previous 24 Months, and Judgments (TOTAL)

The Mortgagee is not required to obtain an explanation of collection accounts, Charge Off Accounts, accounts with late payments, Judgments or other derogatory information.

(B) Disputed Derogatory Credit Accounts (TOTAL)

(1) 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.

(2) Standard

If the credit report utilized by TOTAL Mortgage Scorecard indicates that the Borrower has $1,000 or more collectively in Disputed Derogatory Credit Accounts, the Mortgage must be downgraded to a Refer and manually underwritten.

Exclusions from cumulative balance include:

- disputed medical accounts; and
- disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use. To exclude these balances, the Mortgagee must include a copy of the police report or other documentation from the creditor to support the status of the accounts.

Disputed Derogatory Credit Accounts of a non-borrowing spouse in a community property state are not included in the cumulative balance for determining if the mortgage application is downgraded to a Refer.

(C) Non-derogatory Disputed Accounts and Disputed Accounts Not Indicated on the Credit Report (TOTAL)

(1) 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
- disputed accounts that are current and paid as agreed

(2) Required Documentation and Standard

If a Borrower is disputing non-derogatory accounts, or is disputing accounts which are not indicated on the credit report as being disputed, the Mortgagee is not required to downgrade the application to a Refer. However, the Mortgagee must analyze the effect of the disputed accounts on the Borrower's ability to repay the Mortgage. If the dispute results in the Borrower's monthly debt payments utilized in computing the Debt-to-Income (DTI) ratio being less than the amount indicated on the credit report, the Borrower must provide documentation of the lower payments.

Non-derogatory disputed accounts are excluded from the $1,000 cumulative balance limit.

(D) Judgments (TOTAL)

(1) 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.

(2) Standard

The Mortgagee 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, with the exception of obligations excluded by state law.

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 FHA-insured mortgage lien. The Borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments.

The Mortgagee must include the payment amount in the agreement in the Borrower's monthly liabilities and debt.

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

(3) Required Documentation

The Mortgagee 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, and a subordination agreement for any liens existing on title.

(E) Inaccuracy in Debt Considered (TOTAL)

When an inaccuracy in the amount or type of debt or obligation is revealed during the application process and the correct information was not considered by the AUS, the Mortgagee must:

- verify the actual monthly payment amount;
- resubmit the Mortgage for evaluation by TOTAL if the cumulative change in the amount of the liabilities that must be included in the Borrower's debt increases by more than $100 per month; and
- determine that the additional debt was not/will not be used for the Borrower's Minimum Required Investment (MRI).

(F) Bankruptcy (TOTAL)

(1) Standard

The Mortgagee must document the passage of two years since the discharge date of any bankruptcy. If the bankruptcy was discharged within two years from the date of case number assignment, the Mortgage must be downgraded to a Refer and manually underwritten.

(2) 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 Mortgagee must obtain the bankruptcy and discharge documents.

(G) Pre-Foreclosure Sales (Short Sales) (TOTAL)

(1) 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.

(2) Standard

The Mortgagee must document the passage of three years since the date of the Short Sale. If the Short Sale occurred within three years of the case number assignment date, the Mortgage must be downgraded to a Refer and manually underwritten.

This three-year period begins on the date of transfer of title by Short Sale.

(3) Required Documentation

If the credit report does not verify the date of the transfer of title by Short Sale, the Mortgagee must obtain the Short Sale documents.

(H) Foreclosure (TOTAL)

(1) Standard

The Mortgagee must manually downgrade to a Refer if the Borrower had a foreclosure in which title transferred from the Borrower within three years of case number assignment.

(2) Required Documentation

If the credit report does not verify the date of the transfer of title through the foreclosure, the Mortgagee must obtain the foreclosure documents.

(I) Deed-in-Lieu of Foreclosure (TOTAL)

(1) Definition

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

(2) Standard

The Mortgagee must manually downgrade to a Refer if the Borrower had a DIL of Foreclosure in which title transferred from the Borrower within three years of case number assignment.

(3) Required Documentation

If the credit report does not verify the date of the transfer of title by DIL of Foreclosure, the Mortgagee must obtain a copy of the DIL of Foreclosure.

(J) Credit Counseling/Payment Plan (TOTAL)

Participating in a consumer credit counseling program does not require a downgrade to a manual underwriting.

No explanation or other documentation is needed.

(K) Housing Obligations/Mortgage Payment History (TOTAL)

(1) Definition

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

(2) Standard

A Mortgage Payment 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.

(a) Late Mortgage Payments for Purchase and No Cash-Out Refinance

The Mortgage must be downgraded to a Refer and manually underwritten if any mortgage trade line, including mortgage line-of-credit payments, during the 12 months prior to case number assignment reflects:

- three or more late payments of greater than 30 Days;

- one or more late payments of 60 Days plus one or more 30-Day late payments;
- one payment greater than 90 Days late; or
- that the Borrower has made less than three consecutive payments since completion of a mortgage Forbearance Plan.

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 time 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 has been granted forbearance must utilize the payment history in accordance with the Forbearance Plan for the time period of forbearance in determining late housing payments. Where any mortgage in forbearance will remain open after the closing of the new FHA-insured Mortgage, the Forbearance Plan must be terminated at or prior to closing. 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.

(b) Cash-Out Refinance Transactions

The Mortgage must be downgraded to a Refer and manually underwritten if any mortgage trade line, including mortgage line-of-credit payments, reflects:

- a current delinquency;
- any delinquency within 12 months of the case number assignment date; or
- the Borrower has made less than 12 consecutive monthly payments since completion of a mortgage forbearance plan.

A Mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.

Where a Borrower who was granted a mortgage payment forbearance and continues to make payments as agreed under the terms of the original Note, the Mortgage is not required to be downgraded to a Refer provided the Forbearance Plan is terminated at or prior to closing.

(3) Required Documentation

Where a Mortgage reflects payments under a modification or Forbearance Plan within the 12 months prior to case number assignment, the Mortgagee must obtain:

- a copy of the modification or Forbearance Plan; and
- evidence of the payment amount and date of payments during the agreement term.

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

(L) Positive Rental Payment History (TOTAL)

(1) Definitions

Positive Rental Payment History refers to the on-time payment by a Borrower of all rental payments in the previous 12 months. A rental payment is considered to be on time when it is paid within the month due.

A First-Time Homebuyer refers to an individual who has not held an ownership interest in another property in the three years prior to the case number assignment. First-Time Homebuyer includes an individual who is divorced or legally separated and who has had no ownership interest in a Principal Residence (other than joint ownership interest with a spouse) during the three years prior to case number assignment.

(2) Standard

A Mortgagee may submit the transaction to TOTAL Mortgage Scorecard indicating a Positive Rental Payment History provided:

- the transaction is a purchase;
- at least one Borrower is identified as a First-Time Homebuyer;
- the Minimum Decision Credit Score (MDCS) is 620 or greater; and
- at least one Borrower has a documented history of a Positive Rental Payment History with monthly payments of $300 or more for the previous 12 months.

(3) Required Documentation

To verify the Borrower’s rental payment history, the Mortgagee must obtain a copy of the executed rental or lease agreement and one of the following:

- written verification of rent from a landlord with no Identity of Interest with the Borrower;
- 12 months’ canceled rent checks;
- 12 months’ bank or payment service statements documenting rents paid; or
- landlord reference from a rental management company.

Borrowers renting from a Family Member must provide a copy of the executed rental or lease agreement and 12 months' canceled checks or bank statements to demonstrate the satisfactory rental payment history.

iv. Evaluating Liabilities and Debts (TOTAL)

The Mortgagee must review all credit report inquiries to ensure that all debts, including any new debt payments resulting from material inquiries listed on the credit report, are used to calculate the debt ratios. The Mortgagee must also determine that any recent debts were not incurred to obtain any part of the Borrower's required funds to close on the Property being purchased.

Material Inquiries refer to inquires which may potentially result in obligations incurred by the Borrower for other Mortgages, auto loans, leases, or other Installment Loans. Inquiries from department stores, credit bureaus, and insurance companies are not considered material inquiries.

(A) General Liabilities and Debts (TOTAL)

The Mortgagee 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 the balance in order 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 the Mortgagee 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.

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.

The Mortgagee 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.

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

(B) Undisclosed Debt Other Than a Mortgage (TOTAL)

When a debt or obligation (other than a Mortgage) not listed on the mortgage application and/or credit report and not considered by the AUS is revealed during the application process, the Mortgagee must:

- verify the actual monthly payment amount;
- resubmit the Mortgage for evaluation by TOTAL if the cumulative change in the amount of the liabilities that must be included in the Borrower's debt increases by more than $100 per month; and
- determine that any funds borrowed were not/will not be used for the Borrower's MRI.

(C) Undisclosed Mortgage Debt (TOTAL)

When an existing debt or obligation that is secured by a Mortgage but is not listed on the credit report and not considered by the AUS is revealed during the application process, the Mortgagee must obtain one of the following that reflects an acceptable mortgage payment history in accordance with Housing Obligations/Mortgage Payment History (TOTAL):

- a copy of the note and either:
  - a bank statement; or
  - canceled checks;
- a credit report supplement; or
- a verification of Mortgage.

The Mortgage must be downgraded to a Refer and manually underwritten if the mortgage history reflects:

- a current delinquency;
- any delinquency within 12 months of the case number assignment date; or
- more than two 30 Day late payments within 24 months of the case number assignment date.

A Mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the time period of modification in determining late Mortgage Payments.

(D) Federal Debt (TOTAL)

(1) Definition

Federal Debt refers to debt owed to the federal government for which regular payments are being made.

(2) Standard

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

(3) Required Documentation

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

(E) Alimony, Child Support, and Maintenance (TOTAL)

(1) Definition

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

(2) Standard

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

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

(3) Required Documentation

The Mortgagee must verify and document the monthly obligation by obtaining the official signed divorce decree, separation agreement, maintenance agreement, or other legal order.

The Mortgagee 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.

(4) Calculation of Monthly Obligation

The Mortgagee 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.

(F) Non-Borrowing Spouse Debt in Community Property States (TOTAL)

(1) Definition

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

(2) Standard

If the Borrower resides in a community property state or the Property being insured 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.

(3) Required Documentation

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

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

The Mortgagee must obtain a credit report for the non-borrowing spouse in order to determine the debts that must be included in the liabilities. The credit report for the non-borrowing spouse is for the purpose of establishing debt only, and is not submitted to TOTAL Mortgage Scorecard for the purpose of credit evaluation. The credit report for the non-borrowing spouse may be traditional or non-traditional.

(G) Deferred Obligations (TOTAL)

(1) 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.

(2) Standard

The Mortgagee must include deferred obligations in the Borrower's liabilities.

(3) Required Documentation

The Mortgagee 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. The Mortgagee must obtain evidence of the actual monthly payment obligation, if available.

(4) Calculation of Monthly Obligation

The Mortgagee 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, the Mortgagee must utilize the terms of the debt or 5 percent of the outstanding balance to establish the monthly payment.

(H) Student Loans (TOTAL)

(1) Definition

Student Loan refers to liabilities incurred for educational purposes.

(2) Standard

The Mortgagee must include all Student Loans in the Borrower’s liabilities, regardless of the payment type or status of payments.

(3) Required Documentation

If the payment used for the monthly obligation is less than the monthly payment reported on the Borrower’s credit report, the Mortgagee 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.

The Mortgagee may exclude the payment from the Borrower’s 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.

(4) Calculation of Monthly Obligation

For outstanding Student Loans, regardless of the payment status, the Mortgagee 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.

Exception

Where a student loan payment has been suspended in accordance with COVID-19 emergency relief, the Mortgagee 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.

(I) Installment Loans (TOTAL)

(1) 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.

(2) Standard

The Mortgagee 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, the Mortgagee must use the amount of the monthly payment shown in the loan agreement or payment statement and enter it into TOTAL Mortgage Scorecard.

(3) 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 Mortgagee 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 (TOTAL) section.

(J) Revolving Charge Accounts (TOTAL)

(1) 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.

(2) Standard

The Mortgagee 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 Mortgagee must use the payment shown on the current account statement or 5 percent of the outstanding balance.

(3) Required Documentation

The Mortgagee 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, the Mortgagee must obtain a copy of the most recent charge account statement or use 5 percent of the outstanding balance to document the monthly payment.

(K) 30-Day Accounts (TOTAL)

(1) 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.

(2) Standard

The Mortgagee 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, the Mortgagee must utilize 5 percent of the outstanding balance as the Borrower's monthly debt to be included in the DTI.

(3) Required Documentation

The Mortgagee must use the credit report to document that the Borrower has paid the balance on the account monthly for the previous 12 months. The Mortgagee 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.

(L) Contingent Liabilities (TOTAL)

(1) Definition

A Contingent Liability refers to a liability that may result in the obligation to repay only when 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 Co-signer liabilities and liabilities resulting from a mortgage assumption without release of liability.

(2) Standard

The Mortgagee must include monthly payments on contingent liabilities in the calculation of the Borrower's monthly obligations unless the Mortgagee verifies and documents 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.

(3) Calculation of Monthly Obligation

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

(4) Required Documentation

(a) Mortgage Assumptions

The Mortgagee must obtain the agreement creating the contingent liability or assumption agreement and deed showing transfer of title out of the Borrower's name.

(b) Cosigned Liabilities

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

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

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

(M) Collection Accounts (TOTAL)

(1) Definition

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

(2) Standard

If the credit reports used in the TOTAL Mortgage Scorecard analysis show cumulative outstanding collection account balances of $2,000 or greater, the Mortgagee must:

- verify that the debt is paid in full at the time of or prior to settlement using acceptable Sources of Funds (TOTAL);
- verify that the Borrower has made payment arrangements with the creditor and include the monthly payment in the Borrower's DTI; 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.

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 excluded by state law.

(3) Required Documentation

The Mortgagee 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 the Mortgagee uses 5 percent of the outstanding balance, no documentation is required.

(N) Charge Off Accounts (TOTAL)

(1) Definition

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

(2) Standard

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

(O) Private Savings Clubs (TOTAL)

(1) Definition

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

(2) Standard

If the Borrower is obligated to continue making ongoing contributions under the pooled savings agreement, this obligation must be counted in the Borrower's total debt.

The Mortgagee 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.

(3) Required Documentation

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

(P) Business Debt in Borrower's Name (TOTAL)

(1) 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.

(2) Standard

When business debt is reported on the Borrower's personal credit report, the debt must be included in the DTI calculation, unless the Mortgagee 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.

(3) Required Documentation

When a self-employed Borrower states debt appearing on their personal credit report is being paid by their business, the Mortgagee 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.

(Q) Obligations Not Considered Debt (TOTAL)

Obligations not considered debt include:

- medical collections
- federal, state, and local taxes, if not delinquent and no payments are 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
- child care
- commuting costs
- union dues
- insurance, other than property insurance
- open accounts with zero balances
- voluntary deductions, when not associated with another type of obligation

c. Income Requirements (TOTAL) (11/07/2023)

Effective Income Definition

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

Effective Income Standard

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

i. General Income Requirements (TOTAL)

The Mortgagee 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.

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

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

If FHA requires tax returns as required documentation for any type of Effective Income, the Mortgagee must also analyze the tax returns in accordance with Appendix 2.0 – Analyzing IRS Forms.

ii. Employment Related Income (TOTAL)

(A) 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*.

(B) Standard

The Mortgagee may use Employment related Income as Effective Income in accordance with the standards provided for each type of Employment related Income.

(C) Required Documentation

For all Employment related Income, the Mortgagee 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.

(1) Traditional Current Employment Documentation

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

- the most recent pay stub 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 Mortgagee to verify income and employment; and
  - the date of the data contained in the completed verification conforms with FHA requirements in Maximum Age of Mortgage 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.

(2) Alternative Current Employment Documentation

If using alternative documentation, the Mortgagee 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.

(3) 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:

- The current employer confirms a two-year employment history, or a paystub reflects a hiring date.
- Only base pay is used to qualify (no Overtime, Bonus, or Tip Income).
- 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 the Mortgagee must obtain one or a combination of the following for the most recent two years to verify the applicant's employment history:

- IRS Form W-2(s);
- written VOE(s);
- direct electronic verification by a TPV vendor, subject to the following requirements:
  - the Borrower has authorized the Mortgagee to verify income and employment; and
  - the date of the data contained in the completed verification conforms with FHA requirements in Maximum Age of Mortgage Documents; and/or
- evidence supporting enrollment in school or the military during the most recent two full years.

iii. Primary Employment (TOTAL)

(A) Definitions

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.

(B) Standard

The Mortgagee may use primary Employment Income as Effective Income.

(C) Calculation of Effective Income

(1) Salary

(a) Standard

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

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

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

(2) Hourly

(a) Standard

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

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

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

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

For employees who are paid hourly and whose hours vary, the Mortgagee 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 earned since the COVID-19 Related Economic Event.

iv. Part-Time Employment (TOTAL)

(A) 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.

(B) Standard

The Mortgagee 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.

(C) Calculation of Effective Income

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

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

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

For employees who are paid hourly and whose hours vary, the Mortgagee 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.

v. Overtime, Bonus, or Tip Income (TOTAL)

(A) Definition

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

(B) Standard

The Mortgagee 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 less than two years may be considered Effective Income if the Mortgagee documents 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.

(C) Calculation of Effective Income

(1) Standard

For employees with Overtime, Bonus, or Tip Income, the Mortgagee must calculate the 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, Bonus, or Tip Income earned over the previous year.

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

For employees with Overtime, Bonus, or Tip Income, the Mortgagee 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.

vi. Seasonal Employment (TOTAL)

(A) 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.

(B) Standard

The Mortgagee 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 Mortgagee may consider unemployment income as Effective Income for those with Effective Income from Seasonal Employment.

(C) Required Documentation

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

(D) Calculation of Effective Income

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

vii. Employer Housing Subsidy (TOTAL)

(A) Definition

Employer Housing Subsidy refers to employer-provided mortgage assistance.

(B) Standard

The Mortgagee may utilize Employer Housing Subsidy as Effective Income.

(C) Required Documentation

The Mortgagee must verify and document the existence and the amount of the housing subsidy.

(D) Calculation of Effective Income

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

viii. Employed by Family-Owned Business (TOTAL)

(A) 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.

(B) Standard

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

(C) Required Documentation

The Mortgagee 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, the Mortgagee must obtain copies of signed personal tax returns or tax transcripts.

(D) Calculation of Effective Income

(1) Salary

(a) Standard

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

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

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

(2) Hourly

(a) Standard

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

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

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

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

For employees who are paid hourly and whose hours vary, the Mortgagee 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 earned since the COVID-19 Related Economic Event.

ix. Commission Income (TOTAL)

(A) Definition

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

(B) Standard

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

(C) Required Documentation

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

(D) Calculation of Effective Income

(1) Standard

The Mortgagee must calculate Effective Income for commission by using the lesser of:

- the average Commission Income earned over either:
  - the previous two years; or
  - the length of time Commission Income has been earned if less than two years; or
- the average Commission Income earned over the previous year.

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

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

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

x. Self-Employment Income (TOTAL)

(A) 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.

(B) Standard

(1) Minimum Length of Self-Employment

The Mortgagee 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, the Mortgagee 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.

(2) 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 Mortgagee must downgrade and manually underwrite.

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

The Mortgagee may consider Self-Employment Income if the Borrower has an aggregate self-employment history before and after the COVID-19 Related Economic Event totaling two years.

If the Borrower has an aggregate self-employment history before and after the COVID-19 Related Economic Event totaling between one and two years, the Mortgagee 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.

For self-employed Borrowers with a COVID-19 Related Economic Event that have since regained income at a level less than 80 percent of their income prior to the COVID-19 Related Economic Event, the Mortgagee must downgrade and manually underwrite.

(C) Required Documentation

(1) Individual and Business Tax Returns

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

The Mortgagee must obtain the Borrower's business tax returns for the most recent two years unless the following criteria are met:

- individual federal income tax returns show increasing Self-Employment Income over the past two years;
- funds to close are not coming from business accounts; and
- the Mortgage to be insured is not a cash-out refinance.

In lieu of signed individual or business tax returns from the Borrower, the Mortgagee 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

The Mortgagee 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 must be obtained from the IRS.

(3) 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, the Mortgagee 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.

(D) Calculation of Effective Income

(1) Standard

The Mortgagee 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.

The Mortgagee 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 that 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 Mortgagee 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.

xi. Additional Required Analysis of Stability of Employment Income (TOTAL)

(A) 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, the Mortgagee 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). The Mortgagee must obtain:

- transcripts of training and education demonstrating qualification for a new position; or
- employment documentation evidencing continual increases in income and/or benefits.

(B) Addressing Gaps in Employment

For Borrowers with gaps in employment of six months or more (an extended absence), the Mortgagee 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.

(C) Addressing Temporary Reduction in Income

For Borrowers with a temporary reduction of income due to a short-term disability or similar temporary leave, the Mortgagee 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 Mortgage taking into account any reduction of income due to the circumstance.

For federal, state, tribal, 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 Mortgage Payment due date, the Mortgagee may use the Borrower's pre-leave income as Effective Income.

For Borrowers returning to work after the first Mortgage Payment due date, the Mortgagee may use the Borrower's current income plus available surplus liquid asset Reserves, above and beyond any required Reserves, 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.

Required Documentation

The Mortgagee 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; 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.

(D) Addressing Gaps in Employment or Reduction of Income Due to COVID-19 Related Economic Event

(1) Non-Self-Employment Income

For Borrowers with gaps in employment, reduction of income, or reduction of hours due to a COVID-19 Related Economic Event, the Mortgagee may consider the Borrower's income calculated in accordance with the Exception Due to COVID-19 Related Economic Event for the applicable income type 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.

Required Documentation

The Lender must provide the following documentation for the Borrower to verify:

- written VOE identifying the time period of temporary loss of employment, temporary loss of income, or temporary loss of hours.

(2) Self-Employment Income

For Borrowers with gaps in self-employment, reduction in income, or reduction of hours due to a COVID-19 Related Economic Event, the Mortgagee 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.

xii. Other Sources of Effective Income (TOTAL)

(A) Disability Benefits (TOTAL)

(1) Definition

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

(2) Required Documentation

The Mortgagee must verify and document the Borrower's receipt of benefits from the SSA, VA, or private disability insurance provider. The Mortgagee 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 mortgage application, that income cannot be used as Effective Income.

If the Notice of Award or equivalent document does not have a defined expiration date, the Mortgagee may consider the income effective and reasonably likely to continue. The Mortgagee 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 the Mortgagee inquire into or request documentation concerning the nature of the disability or the medical condition of the Borrower.

(a) Social Security Disability

For Social Security Disability income, including Supplemental Security Income (SSI), the Mortgagee 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:

- federal 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 evidences income from the SSA; or
- a copy of the Borrower's form SSA-1099/1042S, *Social Security Benefit Statement*.

(b) Department of Veterans Affairs Disability

For VA disability benefits, the Mortgagee 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:

- federal 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, the Mortgagee may consider the income effective and reasonably likely to continue for at least three years.

(c) Private Disability

For private disability benefits, the Mortgagee 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:

- federal tax returns; or
- the most recent bank statement evidencing receipt of income from the insurance provider.

(3) Calculation of Effective Income

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

(B) Alimony, Child Support, and Maintenance Income (TOTAL)

(1) 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.

(2) Required Documentation

The Mortgagee 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, the Mortgagee 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.

The Mortgagee must document the voluntary payment agreement with 12 months of canceled checks, deposit slips, or tax returns.

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

(3) 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, the Mortgagee 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, the Mortgagee 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, the Mortgagee 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 Mortgagee must use the average over the time of receipt.

(C) Military Income (TOTAL)

(1) 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
- proficiency pay

The Mortgagee may not use military education benefits as Effective Income.

(2) Required Documentation

The Mortgagee must obtain a copy of the Borrower's military Leave and Earnings Statement (LES). The Mortgagee 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 Mortgage, Military Income may only be considered Effective Income if the Borrower represents their intent to continue military service.

(3) Calculation of Effective Income

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

(D) Mortgage Credit Certificates (TOTAL)

(1) Definition

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

(2) Required Documentation

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

(3) Calculating Effective Income

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

(E) Section 8 Housing Choice Vouchers (TOTAL)

(1) Definition

Section 8 Housing Choice Vouchers refer to housing subsidies received under the Housing Choice Voucher homeownership option from a Public Housing Agency (PHA).

(2) Required Documentation

The Mortgagee must verify and document the Borrower's receipt of the Housing Choice Voucher homeownership subsidies. The Mortgagee may consider that this income is reasonably likely to continue for three years.

(3) Calculation of Effective Income

The Mortgagee may only use Section 8 Housing Choice Voucher subsidies as Effective Income if it is not used as an offset to the monthly Mortgage Payment. The Mortgagee must use the current subsidy rate to calculate the Effective Income.

(F) Other Public Assistance (TOTAL)

(1) Definition

Public Assistance refers to income received from government assistance programs.

(2) Required Documentation

Mortgagees must verify and document the income received from the government agency.

If any Public Assistance income is due to expire within three years from the date of mortgage application, that income cannot be used as Effective Income. If the documentation does not have a defined expiration date, the Mortgagee may consider the income effective and reasonably likely to continue.

(3) Calculation of Effective Income

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

(G) Automobile Allowances (TOTAL)

(1) Definition

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

(2) Required Documentation

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

(3) Calculation of Effective Income

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

(H) Retirement Income (TOTAL)

Retirement Income refers to income received from Pensions, 401(k) distributions, and Social Security.

(1) Social Security Income (TOTAL)

(a) Definition

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

(b) Required Documentation

The Mortgagee 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, the Mortgagee must obtain any one of the following documents:

- federal 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 evidences income from the SSA; or
- a copy of the Borrower's form SSA-1099/1042S.

In addition to verification of income, the Mortgagee must document the continuance of this income by obtaining from the Borrower (1) a copy of the last Notice of Award letter which states the SSA's determination on the Borrower's eligibility for SSA income or (2) an equivalent document that establishes award benefits to the Borrower (equivalent document). If any income from the SSA is due to expire within three years from the date of case number assignment, that income may not be used for qualifying.

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

(c) Calculation of Effective Income

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

(2) Pension (TOTAL)

(a) Definition

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

(b) Required Documentation

The Mortgagee 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.

The Mortgagee must obtain any one of the following documents:

- federal 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.

(c) Calculation of Effective Income

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

(3) Individual Retirement Account and 401(k) (TOTAL)

(a) Definition

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

(b) Required Documentation

The Mortgagee 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.

The Mortgagee must obtain the most recent IRA/401(k) statement and any one of the following documents:

- federal tax returns; or
- the most recent bank statement evidencing receipt of income.

(c) Calculation of Effective Income

For Borrowers with IRA/401(k) Income that has been and will be consistently received, the Mortgagee must use the current amount of IRA Income received to calculate Effective Income. For Borrowers with fluctuating IRA/401(k) Income, the Mortgagee 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, the Mortgagee must use the average over the time of receipt.

(I) Rental Income (TOTAL)

(1) Definition

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

(2) Rental Income Received from the Subject Property (TOTAL)

(a) Standard

The Mortgagee may consider Rental Income from existing and prospective tenants if documented in accordance with the following requirements.

Rental Income from the subject Property may be considered Effective Income when the Property is a two- to four-unit dwelling, or an acceptable one- to four-unit Investment Property.

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

(b) Required Documentation

Documentation varies depending upon the length of time the Borrower has owned the Property.

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

Where the Borrower does not have a history of Rental Income from the subject since the previous tax filing:

Two- to Four-Units

The Mortgagee 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, *Small Residential Income Property Appraisal Report*) and, if available, the prospective leases.

One Unit

The Mortgagee must verify and document the proposed Rental Income by obtaining a Fannie Mae Form 1004/Freddie Mac Form 70, *Uniform Residential Appraisal Report (URAR)*; Fannie Mae Form 1007/Freddie Mac Form 1000, *Single Family Comparable Rent Schedule*; and Fannie Mae Form 216/Freddie Mac Form 998, *Operating Income Statement,* showing fair market rent and, if available, the prospective lease.

(ii) **History of Rental Income**

Where the Borrower has a history of Rental Income from the subject since the previous tax filing, the Mortgagee must verify and document the existing Rental Income by obtaining the Borrower's most recent tax returns, including Schedule E, from the previous two years.

For Properties with less than two years of Rental Income history, the Mortgagee must document the date of acquisition by providing the deed, Closing Disclosure or similar legal document.

(c) Calculation of Effective Income

The Mortgagee must add the net subject property Rental Income to the Borrower's gross income to calculate Effective Income. The Mortgagee may not reduce the Borrower's total Mortgage Payment by the net subject property Rental Income.

(i) Limited or No History of Rental Income

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, the Mortgagee must use the lesser of:

- the monthly operating income reported on Fannie Mae Form 216/Freddie Mac Form 998; or
- 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 Rental Income

The Mortgagee must calculate the Rental Income by averaging the amount shown on Schedule E.

Depreciation, mortgage 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 for less than two years, the Mortgagee must annualize the Rental Income for the length of time the Property has been owned.

(3) Rental Income from Other Real Estate Holdings (TOTAL)

(a) 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. The Mortgagee must obtain a lease agreement of at least one year's duration after the Mortgage is closed and evidence of the payment of the security deposit or first month's rent.

(b) 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 previous tax filing, including Property being vacated by the Borrower, the Mortgagee 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 an FHA Roster Appraiser.

Two- to Four-Units

The Mortgagee 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, if available, the prospective leases.

One Unit

The Mortgagee must verify and document the proposed Rental Income by obtaining a *URAR*, Fannie Mae Form 1007/Freddie Mac Form 1000, *Single Family Comparable Rent Schedule*, and Fannie Mae Form 216/Freddie Mac Form 998, *Operating Income Statement*, showing fair market rent and, if available, the prospective lease.

***(ii)* History of Rental Income**

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

(c) Calculation of Effective Net Rental 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 Mortgagee must deduct the Principal, Interest, Taxes, and Insurance (PITI) from the lesser of:

- the monthly operating income reported on Fannie Mae Form 216/Freddie Mac Form 998; or
- 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 Mortgagee 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.

If the Property has been owned for less than two years, the Mortgagee must annualize the Rental Income for the length of time the Property has been owned.

For Properties owned less than two years, the Mortgagee must document the date of acquisition by providing the deed, Closing Disclosure or similar legal document.

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

(4) Boarders of the Subject Property (TOTAL)

(a) Definition

Boarder refers to an individual renting space inside the Borrower's Dwelling Unit.

(b) Standard

Rental Income from Boarders is only acceptable if the Borrower has a two-year history of receiving income from Boarders that is shown on the tax return and the Borrower is currently receiving Boarder income.

(c) Required Documentation

The Mortgagee must obtain two years of the Borrower's tax returns evidencing income from Boarders and the current lease.

For purchase transactions, the Mortgagee must obtain a copy of the executed written agreement documenting their intent to continue boarding with the Borrower.

(d) Calculation of Effective Income

The Mortgagee must calculate the Effective Income by using the lesser of the two-year average or the current lease.

(J) Investment Income (TOTAL)

(1) Definition

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

(2) Required Documentation

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

(3) Calculation of Effective Income

The Mortgagee 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.

The Mortgagee 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.

(K) Capital Gains and Losses (TOTAL)

(1) Definition

Capital Gains refer 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.

(2) 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.

(3) 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.

(L) Expected Income (TOTAL)

(1) 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.

(2) Standard

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

(3) Required Documentation

The Mortgagee 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, the Mortgagee must verify the amount and that it is guaranteed to begin within 60 Days of the mortgage closing.

(4) Calculation of Effective Income

Income is calculated in accordance with the standards for the type of income being received. The Mortgagee 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.

(M) Trust Income (TOTAL)

(1) Definition

Trust Income refers to income that is regularly distributed to a Borrower from a trust.

(2) Required Documentation

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

The Mortgagee must verify that regular payments will continue for at least the first three years of the mortgage term.

(3) Calculation of Effective Income

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

(N) Annuities or Similar (TOTAL)

(1) Definition

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

(2) Required Documentation

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

(3) Calculation of Effective Income

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

The Mortgagee 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.

(O) Notes Receivable Income (TOTAL)

(1) 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.

(2) Required Documentation

The Mortgagee must verify and document the existence of the Note. The Mortgagee 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 Mortgage.

(3) Calculation of Effective Income

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

(P) Nontaxable Income (Grossing Up) (TOTAL)

(1) 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;
- Section 8 Housing Choice Vouchers;
- military allowances; and
- other income that is documented as being exempt from federal income taxes.

(2) Required Documentation

The Mortgagee 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.

(3) 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 greater of 15 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, the Mortgagee may Gross Up the Nontaxable Income by 15 percent.

The Mortgagee may not make any additional adjustments or allowances based on the number of the Borrower's dependents.

(Q) Foster Care Payment

(1) Definition

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

(2) 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.

(3) Required Documentation

The Mortgagee 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.

(4) Calculation of Effective Income

The Mortgagee 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.

(R) Foreign Income

(1) 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.

(2) Standard

The Mortgagee 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.

(3) Required Documentation

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

For all Foreign Income, the Mortgagee must satisfy Standard Documentation Requirements in accordance with the requirements listed based on source and type of income as outlined in Income Requirements (TOTAL).

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

(4) Calculation of Effective Income

The Mortgagee must analyze the Borrower's tax returns to determine gross Foreign Income. The Mortgagee must average the Foreign Income over the previous two years to calculate of Effective Income.

d. Asset Requirements (TOTAL) (04/18/2023)

i. General Asset Requirements (TOTAL)

The Mortgagee 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.

(A) Earnest Money Deposit (TOTAL)

The Mortgagee 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 electronic verification by a TPV vendor, subject to the following requirements:
  - the Borrower has authorized the Mortgagee to verify assets;
  - the date of the completed verification conforms with FHA requirements in Maximum Age of Mortgage 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, the Mortgagee must verify that the Gift is in compliance with Gifts (Personal and Equity) (TOTAL).

(B) Cash to Close (TOTAL)

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

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

(1) Determining the Amount Needed for Closing

For a purchase transaction, the amount of cash needed by the Borrower to close an FHA-insured Mortgage is the difference between the total cost to acquire the Property and the total mortgage amount.

For a refinance transaction, the amount of cash needed by the Borrower to close an FHA-insured Mortgage is the difference between the total payoff requirements of the Mortgage being refinanced and the total mortgage amount.

(2) Mortgagee 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 mortgage settlement.

(a) Origination Fees and Other Closing Costs

The Mortgagee or sponsored TPO may charge a reasonable origination fee.

The Mortgagee or sponsored TPO may charge and collect from Borrowers those customary and reasonable closing costs and prepaid items necessary to close the Mortgage. Charges may not exceed the actual costs.

The Mortgagee must comply with HUD's Qualified Mortgage Rule at 24 CFR § 203.19.

(b) Discount Points

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

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

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

(d) Non-realty or Personal Property

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

(e) Upfront Mortgage Insurance Premium Amounts

Any UFMIP amounts paid in cash are added to the total cash settlement requirements. The UFMIP must be entirely financed into the Mortgage or paid entirely in cash. However, if the UFMIP is financed into the Mortgage, the entire amount is to be financed except for any amount less than $1.00.

(f) 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 settlement requirements.

(g) Repairs and Improvements

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

(h) Premium Pricing on FHA-Insured Mortgages

Premium Pricing refers to the aggregate credits from a Mortgagee or TPO 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 Mortgagee or TPO is the property seller, real estate agent, builder or developer.

The funds derived from a premium priced Mortgage:

- 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 Mortgage Payments, or Judgments.

(i) Interested Party Contributions on the Closing Disclosure

The Mortgagee may apply Interested Party credits toward the Borrower's origination fees, other closing costs including any items Paid Outside Closing (POC), prepaid items, and Discount Points.

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

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

(j) 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 the Mortgagee 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.

(C) Reserves (TOTAL)

The Mortgagee must verify and document all assets submitted to the AUS.

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;
- equity in another Property; or
- borrowed funds from any source.

Required Reserves for Three- to Four-Unit Properties

The Mortgagee must verify and document Reserves equivalent to three months' PITI after closing for three- to four-unit Properties.

ii. Source Requirements for the Borrower's Minimum Required Investment (TOTAL)

(A) Definition

Minimum Required Investment (MRI) refers to the Borrower's contribution in cash or its equivalent required by Section 203(b)(9) of the National Housing Act, which represents at least 3.5 percent of the Adjusted Value of the Property.

(B) Standard

The Mortgagee may only permit the Borrower's MRI to be provided by a source permissible under Section 203(b)(9)(C) of the National Housing Act, which means the funds for the Borrower's MRI must not come from:

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

While additional funds to close may be provided by one of these sources if permitted under the relevant requirements above, none of the Borrower's MRI may come from these sources. The Mortgagee must document permissible sources for the full MRI in accordance with special requirements noted above.

Additionally, in accordance with Prohibited Sources of Minimum Cash Investment Under the National Housing Act – Interpretive Rule, HUD does not interpret Section 203(b)(9)(C) of the National Housing Act to prohibit Governmental Entities, when acting in their governmental capacity, from providing the Borrower's MRI where the Governmental Entity is originating the insured Mortgage through one of its homeownership programs.

(C) Required Documentation

Where the Borrower's MRI is provided by someone other than the Borrower, the Mortgagee 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 a manner consistent with HUD's Interpretive Rule, the Mortgagee must document that the Governmental Entity incurred prior to or at closing an enforceable legal liability or obligation to fund the Borrower's MRI. It is not sufficient to document that the Governmental Entity has agreed to reimburse the Mortgagee for the use of funds legally belonging to the Mortgagee to fund the Borrower's MRI.

The Mortgagee 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 the Mortgagee is 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.

iii. Sources of Funds (TOTAL)

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

(A) Checking and Savings Accounts (TOTAL)

(1) Definition

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

(2) Standard

The Mortgagee 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, the Mortgagee must obtain documentation of the deposits. The Mortgagee must also verify that no debts were incurred to obtain part, or all, of the MRI.

(3) Required Documentation

(a) Traditional Documentation

The Mortgagee 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, subject to the following requirements:
  - the Borrower has authorized the Mortgagee 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.

(b) 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, the Mortgagee must obtain statement(s) for the most recent two months.

(B) Cash on Hand (TOTAL)

(1) Definition

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

(2) Standard

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

(3) Required Documentation

The Mortgagee 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.

The Mortgagee must also determine the reasonableness of the accumulation based on the time period during which the funds were saved and the Borrower's:

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

(C) Retirement Accounts (TOTAL)

(1) Definition

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

(2) Standard

The Mortgagee 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) 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.

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

(3) Required Documentation

The Mortgagee 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.

(D) Stocks and Bonds (TOTAL)

(1) Definition

Stocks and Bonds are investment assets accumulated by the Borrower.

(2) Standard

The Mortgagee 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, the Mortgagee 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 Mortgagee verifies and documents that the bonds are eligible for redemption when cash to close is calculated.

(3) Required Documentation

The Mortgagee 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 the Mortgagee must obtain a copy of each stock or bond certificate.

(E) Private Savings Clubs (TOTAL)

(1) Definition

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

(2) Standard

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

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

(3) Required Documentation

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

(F) Gifts (Personal and Equity) (TOTAL)

(1) Definition

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

(2) Standards for Gifts

(a) 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 governmental agency or public entity that has a program providing homeownership assistance to:
  - 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 (TOTAL).

(b) Donor's Source of Funds

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

(3) Required Documentation

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

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

Documenting the Transfer of Gifts

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

- 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.
- 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.
- 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, the Mortgagee must have the donor provide written evidence that the funds were borrowed from an acceptable source, not from an Interested Party.

The Mortgagee and its 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, the Mortgagee must be able to make a reasonable determination that the gift funds were not provided by an unacceptable source.

(4) Standards for Gifts of Equity

(a) Who May Provide Gifts of Equity

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

(b) Required Documentation

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

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

(G) Interested Party Contributions (TOTAL)

(1) Definition

Interested Parties refer to sellers, real estate agents, builders, developers, Mortgagees, Third-Party Originators (TPO), 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.

(2) Standard

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 mortgage interest for fixed rate Mortgages;
- Mortgage Payment protection insurance; and
- payment of the UFMIP.

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.

Exceptions

Premium Pricing credits from the Mortgagee or TPO are excluded from the 6 percent limit, provided the Mortgagee or TPO is 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.

(3) Required Documentation

The Mortgagee must document the total Interested Party Contributions on the sales contract or applicable legally binding document, form HUD-92900-LT, 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 Mortgagee must provide a copy of this document to the assigned Appraiser.

(H) Inducements to Purchase (TOTAL)

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 Adjusted Value of the 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;
- 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.

(1) Personal Property (TOTAL)

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
- other items determined appropriate by the HOC

(2) Sales Commission (TOTAL)

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.

(3) Rent Below Fair Market (TOTAL)

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.

(I) Downpayment Assistance Programs (TOTAL)

FHA does not "approve" downpayment assistance programs administered by charitable organizations, such as nonprofits. FHA also does not allow nonprofit entities to provide Gifts to pay off:

- Installment Loans
- credit cards
- collections
- Judgments
- liens
- similar debts

The Mortgagee must ensure that a Gift provided by a charitable organization meets the appropriate FHA requirements, and that the transfer of funds is properly documented.

(1) 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, FHA 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.

(2) Mortgagee Responsibility for Ensuring that Downpayment Assistance Provider is a Charitable Organization

The Mortgagee is responsible for ensuring that an entity providing downpayment assistance is a charitable organization as defined by Section 501(a) of the Internal Revenue Code (IRC) of 1986 pursuant to Section 501(c) (3) of the IRC.

One resource for this information is the IRS Exempt Organization Select Check, which contains a list of organizations eligible to receive tax-deductible charitable contributions.

(J) Secondary Financing (TOTAL)

Secondary Financing is any financing other than the first Mortgage that creates a lien against the Property. Any such financing that does create a lien against the Property is not considered a Gift or a grant even if it does not require regular payments or has other features forgiving the debt.

(1) Secondary Financing Provided by Governmental Entities and HOPE Grantees (TOTAL)

(a) Definitions

A Governmental Entity refers to any federal, state, or local government agency or instrumentality.

To be considered an Instrumentality of Government, the entity must be established by a governmental body or with governmental approval or under special law to serve a particular public purpose or designated by law (statute or court opinion) and does not have 501(c)(3) status. HUD deems Section 115 entities to be Instrumentalities of Government for the purpose of providing secondary financing.

Homeownership and Opportunity for People Everywhere (HOPE) Grantee refers to an entity designated in the homeownership plan submitted by an applicant for an implementation grant under the HOPE program.

(b) Standard

FHA will insure a first Mortgage on a Property that has a second Mortgage or lien made or held by a Governmental Entity, provided that:

- the secondary financing is disclosed at the time of application;
- no costs associated with the secondary financing are financed into the FHA-insured first Mortgage;
- the insured first Mortgage does not exceed the FHA Nationwide Mortgage Limit for the area in which the Property is located;
- the secondary financing payments are included in the total Mortgage Payment;
- any secondary financing of the Borrower's MRI fully complies with the additional requirements set forth in Source Requirements for the Borrower's Minimum Required Investment (TOTAL);
- 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; and
- the second lien does not provide for a balloon payment within 10 years from the date of execution.

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 Mortgagee 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.

The Mortgagee must enter information on HUD-approved Nonprofits into FHA Connection (FHAC), as applicable.

Secondary financing provided by Governmental Entities or HOPE grantees 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 (TOTAL).

There is no maximum Combined Loan-to-Value (CLTV) for secondary financing loans provided by Governmental Entities or HOPE grantees.

Any secondary financing meeting this standard is deemed to have prior approval in accordance with 24 CFR § 203.32.

(c) Required Documentation

The Mortgagee 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 Mortgage and Note; and
- a letter from the Governmental Entity on their letterhead evidencing the relationship between them and the nonprofit for each FHA-insured Mortgage, signed by an authorized official and containing the following information:
  - the FHA case number for the first Mortgage;
  - 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 Mortgagee 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;
- a written statement from the organization's General Counsel, as an official of the organization;
- a determination or ruling letter issued by the IRS; or
- an equivalent document evidencing Section 115 status.

(2) Secondary Financing Provided by HUD-Approved Nonprofits (TOTAL)

(a) Definition

A HUD-approved Nonprofit is a nonprofit agency approved by HUD to act as a mortgagor using FHA mortgage insurance, purchase the Department's Real Estate Owned (REO) Properties (HUD Homes) at a discount, and provide secondary financing.

HUD-approved Nonprofits appear on the HUD Nonprofit Roster.

(b) Standard

FHA will insure a first Mortgage on a Property that has a second Mortgage or lien held by a HUD-approved Nonprofit, provided that:

- the secondary financing is disclosed at the time of application;
- no costs associated with the secondary financing are financed into the FHA-insured first Mortgage;
- the secondary financing payments must be included in the total Mortgage 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 not be used to meet the Borrower's MRI;
- there is no maximum CLTV for secondary financing loans provided by HUD-approved Nonprofits; and
- the second lien may not provide for a balloon payment within 10 years from the date of execution.

Secondary financing provided by Section 115 entities must follow the guidance in Secondary Financing Provided by Governmental Entities and HOPE Grantees (TOTAL).

Any secondary financing meeting this standard is deemed to have prior approval in accordance with 24 CFR § 203.32.

(c) Required Documentation

The Mortgagee must obtain from the provider of any secondary financing:

- documentation showing the amount of funds provided to the Borrower for each transaction; and
- copies of the Mortgage and Note.

The Mortgagee must enter information into FHAC on the nonprofit and the Governmental Entity as applicable. If there is more than one nonprofit, enter information on all nonprofits.

(3) Family Members (TOTAL)

(a) Standard

FHA will insure a first Mortgage on a Property that has a second Mortgage 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 FHA-insured first Mortgage;
- the secondary financing payments must be included in the total Mortgage 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;
- any periodic payments are level and monthly;
- 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;
- mortgage companies with retail banking Affiliates may have the Affiliate lend the funds to the Family Member. However, the terms and conditions of the loan to the Family Member cannot be more favorable than they would be for any other Borrowers;
- 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.

Any secondary financing meeting this standard is deemed to have prior approval in accordance with 24 CFR § 203.32.

(b) Required Documentation

The Mortgagee 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 Mortgage 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, the Mortgagee 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 the Mortgagee.

(4) Private Individuals and Other Organizations (TOTAL)

(a) Definition

Private Individuals and Other Organizations refer to any individuals or entities providing secondary financing which are not covered elsewhere in this Secondary Financing section.

(b) Standard

FHA will insure a first Mortgage on a Property that has a second Mortgage or lien held by private individuals and other organizations, provided that:

- the secondary financing is disclosed at the time of application;
- no costs associated with the secondary financing are financed into the FHA-insured first Mortgage;
- the secondary financing payments must be included in the total Mortgage 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 not be used to meet the Borrower’s MRI;
- the CLTV ratio of the Base Loan Amount and secondary financing amount must not exceed the applicable FHA LTV limit;
- the Base Loan Amount and secondary financing amount must not exceed the Nationwide Mortgage Limits;
- the second lien may not provide for a balloon payment within 10 years from the date of execution;
- any periodic payments are level and monthly; and
- there is no prepayment penalty, after giving the Mortgagee 30 Days advance notice.

Any secondary financing meeting this standard is deemed to have prior approval in accordance with 24 CFR § 203.32.

(c) Required Documentation

The Mortgagee must obtain from the provider of any secondary financing:
- documentation showing the amount of funds provided to the Borrower for each transaction; and
- copies of the Mortgage and Note.

(K) Loans (TOTAL)

A Loan refers to an arrangement in which a lender gives money or Property to a Borrower and the Borrower agrees to return the Property or repay the money.

(1) Collateralized Loans (TOTAL)

(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 Real 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. The Mortgagee must reduce the amount of the corresponding asset by the amount of the collateralized loan.

(c) 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.

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 (TOTAL).

(d) Required Documentation

The Mortgagee 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.

(2) Retirement Account Loans (TOTAL)

(a) Definition

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

(b) Standard

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

(c) Required Documentation

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

(3) Disaster Relief Loans (TOTAL)

(a) Definition

Disaster Relief Loans refer to loans from a Governmental Entity that provide immediate housing assistance to individuals displaced due to a natural disaster.

(b) Standard

Secured or unsecured disaster relief loans administered by the Small Business Administration (SBA) may also be used. If the SBA loan will be secured by the Property being purchased, it must be clearly subordinate to the FHA-insured Mortgage, and meet the requirements for Secondary Financing Provided by Governmental Entities and HOPE Grantees (TOTAL).

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 (TOTAL).

Any monthly payment arising from this type of loan must be included in the qualifying ratios.

(c) Required Documentation

The Mortgagee must verify and document the promissory Note.

(L) Grants (TOTAL)

(1) Disaster Relief Grants (TOTAL)

(a) Definition

Disaster Relief Grants refer to grants from a Governmental Entity that provide immediate housing assistance to individuals displaced due to a natural disaster. Disaster relief grants may be used for the Borrower's MRI.

(b) Required Documentation

The Mortgagee must verify and document the Borrower's receipt of the grant and terms of use.

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

(2) Federal Home Loan Bank Homeownership Set-Aside Grant Program (TOTAL)

(a) Definition

The Federal Home Loan Bank's (FHLB) Affordable Housing Program (AHP) Homeownership Set-Aside Grant Program is an acceptable source of downpayment assistance and may be used in conjunction with FHA-insured financing. Secondary financing that creates a lien against the Property is not considered a Gift or grant even if it does not require regular payments or has other features forgiving the debt.

(b) Standard

Any AHP Set-Aside funds used for the Borrower's MRI must also comply with the additional requirements set forth in Source Requirements for the Borrower's Minimum Required Investment (TOTAL).

(c) Required Documentation

The Mortgagee must verify and document the Borrower's receipt of the grant and terms of use.

The Mortgagee must also verify and document that the Retention Agreement required by the FHLB is recorded against the Property and results in a Deed Restriction, and not a second lien. The Retention Agreement must:

- provide that the FHLB will have ultimate control over the AHP grant funds if the funds are repaid by the Borrower;
- include language terminating the legal restrictions on conveyance if title to the Property is transferred by foreclosure or DIL, or assigned to the Secretary of HUD; and
- comply with all other FHA regulations.

(M) Employer Assistance (TOTAL)

(1) 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, MIP, 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.

(2) Standard

(a) Relocation Guaranteed Purchase

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

(b) Employer Assistance Plans

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

(3) Required Documentation

(a) Relocation Guaranteed Purchase

If the Borrower is being transferred by their company under a guaranteed sales plan, the Mortgagee 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 mortgage debt.

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

(b) Employer Assistance Plans

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

(N) Sale of Personal Property (TOTAL)

(1) Definition

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

(2) Standard

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

(3) Required Documentation

Borrowers may sell Personal Property to obtain cash for closing.

The Mortgagee 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 mortgage transaction.

(O) Trade-In of Manufactured Home (TOTAL)

(1) Definition

Trade-In of Manufactured Home refers to the Borrower's sale or trade-in of another Manufactured Home that is not considered real estate to a Manufactured Housing dealer or an independent third party.

(2) Standard

The net proceeds from the Trade-In of a Manufactured Home may be utilized as the Borrower's source of funds.

Trade-ins cannot result in cash back to the Borrower from the dealer or independent third party.

(3) Required Documentation

The Mortgagee must verify and document the installment sales contract or other agreement evidencing a transaction and value of the trade-in or sale. The Mortgagee must obtain documentation to support the Trade Equity.

(P) Sale of Real Property (TOTAL)

(1) Definition

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

(2) Standard

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

(3) Required Documentation

The Mortgagee must verify and document the actual sale and the Net Sale Proceeds by obtaining a fully executed Closing Disclosure or similar legal document.

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

(Q) Real Estate Commission from Sale of a Subject Property (TOTAL)

(1) 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.

(2) Standard

Mortgagees may consider Real Estate Commissions from the 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.

(3) Required Documentation

The Mortgagee 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 Sale of Subject Property being purchased.

(R) Sweat Equity (TOTAL)

(1) Definition

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

(2) Standard

The Mortgagee 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 (TOTAL).

The Mortgagee may consider any amount as Sweat Equity that has not already been included in the mortgage amount. The Mortgagee 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.

(3) Required Documentation

For materials furnished, the Mortgagee must obtain evidence of the source of funds and the Market Value of the materials.

For labor, the Mortgagee must verify and document that the work will be completed in a satisfactory manner. The Mortgagee 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 Mortgagee 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 Mortgagee must also obtain the sales contract indicating the tasks to be performed by the Borrower during construction.

(S) Trade Equity (TOTAL)

(1) Definition

Trade Equity refers to when a Borrower trades their Real Property to the seller as part of the cash investment.

(2) 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 an FHA-insured Mortgage, assumption processing requirements and restrictions apply.

(3) Required Documentation

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

(T) Rent Credits (TOTAL)

(1) Definition

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

(2) Standard

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

(3) Required Documentation

The Mortgagee must obtain the rent with option to purchase agreement, the Appraiser's estimate of market rent, and evidence of receipt of payments.

e. Final Underwriting Decision (TOTAL) (09/14/2015)

The Mortgagee may approve the Mortgage as eligible for FHA insurance endorsement if:
- TOTAL Mortgage Scorecard rated the mortgage application as Accept;
- the underwriter underwrote the appraisal according to standard FHA requirements;

- the Mortgagee reviewed the TOTAL Mortgage Scorecard findings, and verified that all information entered into TOTAL Mortgage Scorecard is consistent with mortgage documentation, and is true, complete, and accurate; and
- the Mortgage meets all FHA requirements applicable to Mortgages receiving a rating of Accept from TOTAL Mortgage Scorecard.

While TOTAL Mortgage Scorecard is available for Mortgagees to use in their pre-qualification process of mortgage applicants, the Mortgagee must score the Mortgage at least once after assignment of an FHA case number. FHA will not recognize the risk assessment nor will information be carried from TOTAL Mortgage Scorecard to FHAC for endorsement processing, without an FHA case number. It is imperative that the Mortgagees make certain that they enter the FHA case number into their Loan Origination System or AUS as soon as it is known. This will ensure a more efficient endorsement process.

i. Documentation of Final Underwriting Review Decision (TOTAL)

The Mortgagee must complete the following documents to evidence their final underwriting decision.

(A) Form HUD-92900-LT, *FHA Loan Underwriting and Transmittal Summary*

On form HUD-92900-LT, the Mortgagee must:

- indicate the CHUMS ID of the underwriter who reviewed the appraisal;
- complete the Risk Assessment; and
- enter the identification of “ZFHA” in the CHUMS ID.

When the Feedback Certificate indicates “Accept/Ineligible,” the Mortgagee must document the circumstances or other reasons that were evaluated in making the decision to approve the Mortgage in the Remarks section.

(B) Form HUD-92800.5B, *Conditional Commitment Direct Endorsement Statement of Appraised Value*

The underwriter must confirm that form HUD-92800.5B, *Conditional Commitment Direct Endorsement Statement of Appraised Value,* is completed as directed in the form instructions.

(C) Form HUD-92900-A, *HUD Addendum to Uniform Residential Loan Application*

The Mortgagee must complete form HUD-92900-A, *HUD Addendum to Uniform Residential Loan Application*, as directed in the form instructions.

An authorized officer of the Mortgagee, the Borrower, and the underwriter must execute form HUD-92900-A, as indicated in the instructions.

ii. Conditional Approval (TOTAL)

The Mortgagee 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-92900-A.

iii. HUD Employee Mortgages (TOTAL)

If the Mortgage involves a HUD employee, the Mortgagee must condition the Mortgage on its approval by HUD. The Mortgagee must submit the case binder to the Processing and Underwriting Division Director at the Jurisdictional HOC for final underwriting approval.

iv. Notification of Borrower of Approval and Term of the Approval (TOTAL)

The Mortgagee must timely notify the Borrower of their approval. The underwriter's approval or the *Firm Commitment* is valid for the greater of 90 Days or the remaining life of the:

- Conditional Commitment issued by HUD; or
- the underwriter's approval date of the Property, indicated as Action Date on form HUD-92800.5B.