II. ORIGINATION THROUGH POST-CLOSING/ENDORSEMENT

A. TITLE II INSURED HOUSING PROGRAMS FORWARD MORTGAGES

The Title II Insured Housing Programs Forward Mortgages, Origination through Post-Closing/Endorsement section in this *FHA Single Family Housing Policy Handbook (SF Handbook)* provides the origination, underwriting, closing, post-closing, and endorsement standards and procedures applicable to all Single Family (one- to four-units) Mortgages insured under Title II of the National Housing Act, except for Home Equity Conversion Mortgages (HECM). The Mortgagee must fully comply with all of the following standards and procedures in originating, underwriting, and closing for obtaining Federal Housing Administration (FHA) mortgage insurance on a Mortgage. If there are any exceptions or program-specific standards or procedures that differ from those set forth below, the exceptions or alternative program or product specific standards and procedures are explicitly stated. Terms and acronyms used in this *SF Handbook* have their meanings defined in the Glossary and Acronyms and in the specific section of the *SF Handbook* in which the definitions are located.

1. Origination/Processing

a. Applications and Disclosures

The Mortgagee must obtain a completed Fannie Mae Form 1003/Freddie Mac Form 65, *Uniform Residential Loan Application (URLA)* from the Borrower and provide all required federal and state disclosures in order to begin the origination process. The Mortgagee is responsible for using the most recent version of all forms as of the date of completion of the form.

i. Contents of the Mortgage Application Package

The Mortgagee must maintain all information and documentation that is relevant to its approval decision in the mortgage file. All information and documentation that is required in this *SF Handbook,* and any incidental information or documentation related to those requirements, is relevant to the Mortgagee's approval decision.

If after obtaining all documentation required below, the Mortgagee has reason to believe it needs additional support of the approval decision, the Mortgagee must obtain additional explanation and documentation, consistent with information in the mortgage file to clarify or supplement the information and documentation submitted by the Borrower.

(A) General Requirements

(1) Maximum Age of Mortgage Documents

(a) General Document Age

Documents used in the origination and underwriting of a Mortgage may not be more than 120 Days old at the Disbursement Date. Documents whose validity for underwriting purposes is not affected by the passage of time, such as divorce decrees or tax returns, may be more than 120 Days old at the Disbursement Date.

For purposes of counting Days for periods provided in this *SF Handbook*, Day one is the Day after the effective or issue date of the document, whichever is later.

(b) Appraisal Validity

(i) Initial Appraisal Validity

The 120 Day validity period for an appraisal (see Ordering Appraisals) may be extended for 30 Days at the option of the Mortgagee if (1) the Mortgagee approved the Borrower or HUD issued the Firm Commitment before the expiration of the original appraisal; or (2) the Borrower signed a valid sales contract prior to the expiration date of the appraisal.

(ii) Appraisal Update

An appraisal update must be performed before the initial appraisal, with no extension, has expired. Where the initial appraisal is subsequently updated, the updated appraisal is valid for a period of 240 Days after the effective date of the initial appraisal report that is being updated.

(2) Handling of Documents

Mortgagees must not accept or use documents relating to the employment, income, assets, or credit of Borrowers that have been handled by, or transmitted from or through the equipment of unknown parties, or Interested Parties. Mortgagees may not accept or use any third party verifications that have been handled by, or transmitted from or through any Interested Party, or the Borrower.

(a) Information Sent to the Mortgagee Electronically

The Mortgagee must authenticate all documents received electronically by examining the source identifiers (e.g., the fax banner header or the sender's email address) or contacting the source of the document by telephone to verify the document's validity. The Mortgagee must document the name and telephone number of the individual with whom the Mortgagee verified the validity of the document.

(b) Information Obtained via Internet

The Mortgagee must authenticate documents obtained from an Internet website and examine portions of printouts downloaded from the Internet including the Uniform Resource Locator (URL) address, as well as the date and time the documents were printed. The Mortgagee must visit the URL or the main website listed in the URL if the page is password protected to verify the website exists and print out evidence documenting the Mortgagee's visit to the URL and website.

Documentation obtained through the Internet must contain the same information as would be found in an original hard copy of the document.

(c) Confidentiality Policy for Credit Information

Mortgagees must not divulge sources of credit information, except as required by a contract or by law. All personnel with access to credit information must ensure that the use and disclosure of information from a credit report complies with:

- Title VIII of the Civil Rights Act of 1968 (Fair Housing Act);
- the Fair Credit Reporting Act, Public Law 91-508;
- the Right to Privacy Act, Public Law 93-579;

- the Financial Privacy Act, Public Law 95-630; and
- the Equal Credit Opportunity Act, Public Law 94-239 and 12 CFR Part 202.

(3) Signature Requirements for all Application Forms

All Borrowers must sign and date the initial and final Fannie Mae Form 1003/Freddie Mac Form 65, *Uniform Residential Loan Application* (URLA). All Borrowers must sign and date page two of the initial form HUD-92900-A, *HUD/VA Addendum to Uniform Residential Loan Application*, and sign and date the complete final form HUD-92900-A. The application may not be signed by any party who will not be on the Note.

- For Borrowers that are Entities, the signatory must be a representative who is duly authorized to bind the Entity.
- A Power of Attorney (POA) may not be used unless the Mortgagee verifies and documents that all of the following requirements have been satisfied:
  - For military personnel, a POA may only be used for one of the applications (initial or final), but not both:
    - when the service member is on overseas duty or on an unaccompanied tour;
    - when the Mortgagee is unable to obtain the absent Borrower's signature on the application by mail or via fax; and
    - where the attorney-in-fact has specific authority to encumber the Property and to obligate the Borrower. Acceptable evidence includes a durable POA specifically designed to survive incapacity and avoid the need for court proceedings.
  - For incapacitated Borrowers, a POA may only be used where:
    - a Borrower is incapacitated and unable to sign the mortgage application;
    - the incapacitated individual will occupy the Property to be insured, or the Property is being underwritten as an eligible Investment Property; and
    - the attorney-in-fact has specific authority to encumber the Property and to obligate the Borrower. Acceptable evidence includes a durable POA specifically designed to survive incapacity and avoid the need for court proceedings.

For guidance on use of POA on closing documents refer to Use of Power of Attorney at Closing.

Prohibition on Documents Signed in Blank

Mortgagees are not permitted to have Borrowers sign documents in blank, incomplete documents, or blank sheets of paper.

(4) Policy on Use of Electronic Signatures

(a) Definition

An Electronic Signature refers to any electronic sound, symbol, or process attached to or logically associated with a contract or record and executed or adopted by a person with the intent to sign the record. FHA does not accept an electronic signature that is solely voice or audio. Digital signatures are a subset of electronic signatures.

(b) Use of Electronic Signatures

An electronic signature conducted in accordance with the Electronic Signature Performance Standards (Performance Standards) is accepted on FHA documents requiring signatures to be included in the case binder for mortgage insurance, unless otherwise prohibited by law.

Electronic Signatures meeting the Performance Standards are treated as equivalent to handwritten signatures.

(c) Electronic Signature Performance Standards

The Performance Standards are the set of guidelines that govern FHA acceptance of an electronic signature. The use of electronic signatures is voluntary. However, Mortgagees choosing to use electronic signatures must fully comply with the Performance Standards.

(i) The Electronic Signatures in Global and National Commerce Act (E-SIGN Act) Compliance and Technology

A Mortgagee's electronic signature technology must comply with all requirements of the E-SIGN Act, including those relating to disclosures, consent, signature, presentation, delivery, retention and any state law applicable to the transaction.

(ii) Third Party Documents

Third Party Documents are those documents that are originated and signed outside of the control of the Mortgagee, such as the sales contract. FHA will accept electronic signatures on Third Party Documents included in the case binder for mortgage insurance endorsement in accordance with the E-SIGN Act and the Uniform Electronic Transactions Act (UETA). An indication of the electronic signature and date should be clearly visible when viewed electronically and in a paper copy of the electronically signed document.

(iii) Authorized Documents

Authorized Documents refer to the documents on which FHA accepts electronic signatures provided that the Mortgagee complies with the Performance Standards.

- **Mortgage Insurance Endorsement Documents:** Electronic signatures will be accepted on all documents requiring signatures included in the case binder for mortgage insurance except the Note. FHA will accept electronic signatures on the Note for forward Mortgages only. FHA will not accept electronic signatures on HECM Notes.

- **Servicing and Loss Mitigation Documentation:** Electronic signatures will be accepted on any documents associated with servicing or loss mitigation services for FHA-insured Mortgages.

- **FHA Insurance Claim Documentation:** Electronic signatures will be accepted on any documents associated with the filing of a claim for FHA insurance benefits, including form HUD-27011, *Single Family Application for Insurance Benefits*.

- **HUD Real Estate Owned (REO) Documents:** Electronic signatures will be accepted on the HUD REO Sales Contract and related addenda.

(iv) Associating an Electronic Signature with the Authorized Document

The Mortgagee must ensure that the process for electronically signing authorized documents provide for the document to be presented to the signatory before an electronic signature is obtained. The Mortgagee must ensure that the electronic signature is attached to, or logically associated with, the document that has been electronically signed.

(v) Intent to Sign

The Mortgagee must be able to prove that the signer certified that the document is true, accurate, and correct at the time signed. Electronic signatures are only valid under the E-SIGN Act if they are "executed or adopted by a person with the intent to sign the record." Establishing intent includes:

- identifying the purpose for the Borrower signing the electronic record;
- being reasonably certain that the Borrower knows which electronic record is being signed; and

- providing notice to the Borrower that their electronic signature is about to be applied to, or associated with, the electronic record.

Intent to use an electronic signature may be established by, but is not limited to:

- an online dialog box or alert advising the Borrower that continuing the process will result in an electronic signature;
- an online dialog box or alert indicating that an electronic signature has just been created and giving the Borrower an opportunity to confirm or cancel the signature; or
- a click-through agreement advising the Borrower that continuing the process will result in an electronic signature.

***(vi)* Single Use of Signature**

Mortgagees must require a separate action by the signer, evidencing intent to sign, in each location where a signature or initials are to be applied.

This provision does not apply to documents signed by Mortgagee employees or Mortgagee contractors provided the Mortgagee obtains the consent of the individual for the use of their electronic signature. The Mortgagee must document the employee's or contractor's consent.

***(vii)* Authentication**

Definition

Authentication refers to the process used to confirm a signer's identity as a party in a transaction.

Standard for Authentication

Before a Mortgagee submits the case for endorsement, the Mortgagee must confirm the identity of the signer by authenticating data provided by the signer with information maintained by an independent source. Independent sources include, but are not limited to:

- national commercial credit bureaus;
- commercially available data sources or services;
- state motor vehicle agencies; or
- government databases.

The Mortgagee must verify a signer's name and date of birth, and either their Social Security Number (SSN) or driver's license number.

(viii) Attribution

Definition

Attribution is the process of associating the identity of a signer with their signature.

Standard for Attribution

The Mortgagee must maintain evidence sufficient to establish that the electronic signature may be attributed to the individual purported to have signed.

The Mortgagee must use one of the following methods, or combinations of methods, to establish attribution:

- selection by or assignment to the individual of a Personal Identification Number (PIN), password, or other shared secret, that the individual uses as part of the signature process;
- delivery of a credential to the individual by a trusted third party, used either to sign electronically or to prevent undetected alteration after the electronic signature using another method;
- knowledge base authentication using “out of band/wallet” information;
- measurement of some unique biometric attribute of the individual and creation of a computer file that represents the measurement, together with procedures to protect against disclosure of the associated computer file to unauthorized parties; or
- public key cryptography.

(ix) Credential Loss Management

Mortgagees must have a system in place to ensure the security of all issued credentials. One or a combination of the following loss management controls is acceptable:

- maintaining the uniqueness of each combined identification code and password, such that no two individuals have the same combination of identification code and password;
- ensuring that identification code and password issuances are periodically checked, recalled, or revised;
- following loss management procedures to electronically de-authorize lost, stolen, missing, or otherwise compromised identification code or password information, and to issue temporary or permanent replacements using suitable, rigorous controls;
- using transaction safeguards to prevent unauthorized use of passwords or identification codes; or

- detecting and reporting any attempts at unauthorized use of the password or identification code to the system security unit.

(d) Required Documentation and Integrity of Records

Mortgagees must ensure that they employ industry-standard encryption to protect the signer's signature and the integrity of the documents to which it is affixed. Mortgagees must ensure that their systems will detect and record any tampering with the electronically signed documents. FHA will not accept documents that show evidence of tampering.

If changes to the document are made, the electronic process must be designed to provide an "audit trail" showing all alterations, the date and time they were made, and identify who made them.

The Mortgagee's system must be designed so that the signed document is designated as the Authoritative Copy. The Authoritative Copy of an electronically signed document refers to the electronic record that is designated by the Mortgagee or holder as the controlling reference copy.

(B) Mortgage Application and Initial Supporting Documentation

(1) URLA and HUD/VA Addendum to the URLA

Unless otherwise noted, *URLA* and *HUD/VA Addendum to the URLA* refer to both initial and final applications.

The Mortgagee must obtain the Borrower's initial complete, signed *URLA* (Fannie Mae Form 1003/Freddie Mac Form 65) and page two of form HUD-92900-A before underwriting the mortgage application.

The Mortgagee must also include the debt of a non-borrowing spouse on the *URLA* if the Borrower resides in or the Property to be purchased is located in a community property state.

The loan originator identified on the *URLA* must be the actual licensed loan originator regardless of whether the loan originator is employed by a sponsored Third-Party Originator (TPO) or the Mortgagee. The *URLA* must contain the loan originator's name, Nationwide Mortgage Licensing System and Registry (NMLS) identification number, telephone number, and signature.

(2) Mortgage Application Name Requirements

(a) Standard

All mortgage applications must be executed in the legal names of all parties.

All mortgage applications must be executed in the name of one or more individuals.

Mortgage applications from a corporation, partnership, sole proprietorship, or trust must be in the name of the Entity and also be in the name of one or more individuals.

Exception

Mortgage applications for Governmental Entities and HUD-approved Nonprofits that provide assistance to low or moderate income families may be solely in the corporation's name.

(b) Required Documentation

The Mortgagee must include a statement that it has verified the Borrower's identity using valid government-issued photo identification prior to endorsement of the Mortgage or the Mortgagee may choose to include a copy of such photo identification as documentation.

For nonprofit Borrowers, the Mortgagee must obtain a copy of the FHA approval letter from the nonprofit. The Mortgagee must also verify that the nonprofit is eligible to be a Borrower as indicated on the U.S. Department of Housing and Urban Development (HUD) Nonprofit Agency Roster.

(C) Borrower Authorization for Verification Information

(1) Borrower's Authorization

(a) Standard

The Mortgagee must obtain the Borrower's authorization to verify the information needed to process the mortgage application. The Mortgagee must obtain a non-borrowing spouse's consent and authorization where necessary to verify specific information required to process the mortgage application, including the non-borrowing spouse's consent for the Mortgagee to verify their SSN with the Social Security Administration (SSA).

(b) Required Documentation

For each individual or Entity, Borrower authorization may be accomplished through a blanket authorization form.

(2) Form HUD-92900-A Part IV: Borrower Consent for Social Security Administration to Verify Social Security Number

The Mortgagee must obtain the Borrower's signature on Part IV of form HUD-92900-A to verify the Borrower's SSN with the SSA.

(3) Tax Verification Form or Equivalent

The Mortgagee must obtain the Borrower's signature on the appropriate Internal Revenue Service (IRS) form to obtain tax returns directly from the IRS for all credit-qualifying Mortgages at the time the final *URLA* is executed.

(D) Borrower's Authorization for Use of Information Protected under the Privacy Act

(1) Standard

The Mortgagee must obtain the Borrower's consent for use of the Borrower's information for any purpose relating to the origination, servicing, loss mitigation, and disposition of the Mortgage or Property securing the Mortgage, and relating to any insurance claim and ultimate resolution of such claims by the Mortgagee and FHA.

(2) Required Documentation

The Mortgagee must obtain a signed statement from the Borrower that clearly expresses the Borrower's consent for the use of the Borrower's information as required above.

(E) Sales Contract and Supporting Documentation

(1) Sales Contract

(a) Standard

The Mortgagee must not originate an insured Mortgage for the purchase of a Property if any provision of the sales contract violates FHA requirements.

The Mortgagee must ensure that (1) all purchasers listed on the sales contract are Borrowers, and (2) only Borrowers sign the sales contract.

An addendum or modification may be used to remove or correct any provisions of the sales contract that do not conform to these requirements.

The Family Member of a purchaser, who is not a borrower, may be listed on the sales contract without modification or removal.

Family Member is defined as follows, regardless of actual or perceived sexual orientation, gender identity, or legal marital status:

- child, parent, or grandparent;
  - a child is defined as a son, stepson, daughter, or stepdaughter;
  - a parent or grandparent includes a step-parent/grandparent or foster parent/grandparent;
- spouse or domestic partner;
- legally adopted son or daughter, including a child who is placed with the Borrower by an authorized agency for legal adoption;
- foster child;
- brother, stepbrother;
- sister, stepsister;
- uncle;
- aunt; or
- son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law of the Borrower.

(i) Amendatory Clause

If the Borrower does not receive form HUD-92800.5B, *Conditional Commitment Direct Endorsement Statement of Appraised Value*, before signing the sales contract, the sales contract must be amended before closing to include an amendatory clause that contains the following language:

> "It is expressly agreed that notwithstanding any other provisions of this contract, the purchaser shall not be obligated to complete the purchase of the property described herein or to incur any penalty by forfeiture of earnest money deposits or otherwise, unless the purchaser has been given, in accordance with HUD/FHA or VA requirements, a written statement by the Federal Housing Commissioner, Department of Veterans Affairs, or a Direct Endorsement lender setting forth the appraised value of the property of not less than $___________*. The purchaser shall have the privilege and option of proceeding with consummation of the contract without regard to the amount of the appraised valuation. The appraised valuation is arrived at to determine the maximum mortgage the Department of Housing and Urban Development will insure. HUD does not warrant the value or condition of the property. The purchaser should satisfy himself/herself that the price and condition of the property are acceptable."

* Mortgagees must ensure the actual dollar amount of the sales price stated in the contract has been inserted in the amendatory clause. Increases to the sale price require a revised amendatory clause.

An amendatory clause is not required in connection with:

- HUD REO sales;
- FHA's 203(k) mortgage program;
- sales in which the seller is:
  - Fannie Mae;
  - Freddie Mac;
  - U.S. Department of Veterans Affairs (VA);
  - United States Department of Agriculture (USDA) Rural Housing Services;
  - other federal, state, and local government agencies;
  - a Mortgagee disposing of REO assets; or
  - a seller at a foreclosure sale; or
- sales in which the Borrower will not be an owner-occupant (for example, sales to nonprofit agencies).

***(ii)* Real Estate Certification**

The Borrower, seller, and the real estate agent or broker involved in the sales transaction must certify, to the best of their knowledge and belief, that (1) the terms and conditions of the sales contract are true and (2) any other agreement entered into by any parties in connection with the real estate transaction is part of, or attached to, the sales agreement.

A separate certification is not needed if the sales contract contains a statement that (1) there are no other agreements between parties and the terms constitute the entire agreement between the parties, and (2) all parties are signatories to the sales contract submitted at the time of underwriting.

***(iii)*Property Assessed Clean Energy**

Where the subject Property is encumbered with a Property Assessed Clean Energy (PACE) obligation, the sales contract must include a clause specifying whether the PACE obligation will remain with the Property or be satisfied by the seller at, or prior to, closing. Where the PACE obligation will remain, all terms and conditions of the PACE obligation must be fully disclosed to the Borrower and made part of the sales contract between the seller and the Borrower.

(b) Required Documentation

The Mortgagee must obtain all signed copies of sales contract(s), including a complete copy of the final sales contract with any modifications or revisions agreed upon by Borrower and seller.

(2) Statement of Appraised Value

The Borrower must receive a copy of form HUD-92800.5B.

A statement of appraised value is not required in connection with:

- HUD REO sales;
- FHA's 203(k) mortgage program;
- sales in which the seller is:
  - Fannie Mae;
  - Freddie Mac;
  - the VA;
  - USDA Rural Housing Services;
  - other federal, state, and local government agencies;
  - a Mortgagee disposing of REO assets; or
  - a seller at a foreclosure sale; or
- sales in which the Borrower will not be an owner-occupant (for example, sales to nonprofit agencies).

ii. Disclosures and Legal Compliance

(A) HUD Required Disclosures

The Mortgagee must provide or ensure the Borrower is provided with any disclosure required by FHA, including the following disclosures.

(1) Informed Consumer Choice Disclosure

The Mortgagee must provide the Borrower with an Informed Consumer Choice Disclosure (FHA INFO 13-32) in accordance with the requirements of 24 CFR § 203.10 if the Borrower may qualify for similar non FHA-insured mortgage products offered by the Mortgagee.

(2) Form HUD-92900-B, Important Notice to Homebuyers

The Mortgagee must provide the Borrower with a copy of form HUD-92900-B, *Important Notice to Homebuyers*, signed by the Borrower and provide the Borrower with a copy to keep for the Borrower's records when the Borrower applies for the Mortgage. The Mortgagee must retain the original form HUD-92900-B signed by the Borrower.

(3) Lead-Based Paint

If the Property was built before 1978, the seller must disclose any information known about lead-based paint and lead-based paint hazards before selling the house, in accordance with the HUD-EPA Lead Disclosure Rule (24 CFR 35, subpart A, and the identical 40 CFR 745, subpart F). For such Properties, the Mortgagee must ensure that:

- the Borrower has been provided the EPA-approved information pamphlet on identifying and controlling lead-based paint hazards ("Protect Your Family From Lead In Your Home");

- the Borrower was given a 10-Day period before becoming obligated to purchase the home to conduct a lead-based paint inspection or risk assessment to determine the presence of lead-based paint or lead-based paint hazards, or waived the opportunity;
- the sales contract contains an attachment in the language of the contract (e.g., English, Spanish), signed and dated by both the seller and purchaser:
  - containing a lead warning statement as set forth in 24 CFR § 35.92(a)(1).
  - providing the seller's disclosure of the presence of any known lead-based paint and/or lead-based paint hazards in the target housing being sold, or indication of no knowledge of such presence;
  - listing any records or reports available to the seller pertaining to lead-based paint and/or lead-based paint hazards in property housing being sold, or indication by the seller that no such records or reports exist; and
  - affirming that the Borrower received the pamphlet, disclosure, and records or reports, above; and
- when any agent is involved in the transaction on behalf of the seller, the sales contract includes a statement that the agent has informed the seller of the seller's Lead Disclosure Rule obligations, the agent is aware of his/her duty to ensure compliance with the requirements of the Rule, and the agent has signed and dated the contract.

(4) Form HUD-92564-CN, For Your Protection: Get a Home Inspection

Mortgagees are required to provide form HUD-92564-CN, *For Your Protection: Get a Home Inspection,* to prospective homebuyers at first contact, be it for pre-qualification, pre-approval, or initial application.

(B) Compliance with all Applicable Laws, Rules and Requirements

The Mortgagee is required to comply with all federal, state and local laws, rules, and requirements applicable to the mortgage transaction, including all applicable disclosure requirements and the requirements of the Consumer Financial Protection Bureau (CFPB), including those related to:

- Truth in Lending Act (TILA); and
- Real Estate Settlement Procedure Act (RESPA).

(C) Nondiscrimination Policy

The Mortgagee must fully comply with all applicable provisions of:

- Title VIII of the Civil Rights Act of 1968 (Fair Housing Act);
- the Fair Credit Reporting Act, Public Law 91-508; and
- the Equal Credit Opportunity Act, Public Law 94-239 and 12 CFR Part 202.

The Mortgagee must make all determinations with respect to the adequacy of the Borrower's income in a uniform manner without regard to race, color, religion, sex, national origin, familial status, handicap, marital status, actual or perceived sexual orientation, gender identity, source of income of the Borrower, or location of the Property.

iii. Application Document Processing

(A) Mortgagee Responsibilities

The Mortgagee must order the FHA case number and perform any associated tasks in FHA Connection (FHAC). The Mortgagee may use non-employees in connection with its origination of FHA-insured Mortgages only as described below. The Mortgagee ultimately remains responsible for the quality of the Mortgage and for strict compliance with all applicable FHA requirements, regardless of the Mortgagee's relationship to the person or Entity performing any particular service or task.

(1) Sponsored Third-Party Originator

The Mortgagee is responsible for dictating the specific application and processing tasks to be performed by the sponsored TPO. Only HUD-approved Mortgagees acting in the capacity of a sponsored TPO may have direct access to FHAC.

(2) Housing Counseling Services

Mortgagees must ensure that Borrowers receive all required counseling, and that all counseling is provided by HUD-approved housing counseling agencies.

(3) Other Contract Service Providers

The Mortgagee may utilize Eligible Contractors to perform the following administrative and clerical functions: typing of mortgage documents, mailing out and collecting verification forms, ordering credit reports, and/or preparing for endorsement and shipping Mortgages to investors.

(4) Excluded Parties

The Mortgagee may not contract with Entities or persons that are suspended, debarred, or otherwise excluded from participation in HUD programs, or under a Limited Denial of Participation (LDP) that excludes their participation in FHA programs. The Mortgagee must ensure that no sponsored TPO or contractor engages such an Entity or person to perform any function relating to the origination of an FHA-insured Mortgage. The Mortgagee must check the System for Award Management (SAM) and must follow appropriate procedures defined by that system to confirm eligibility for participation.

(B) Initial Document Processing

The Mortgagee begins processing the Mortgage by obtaining an initial *URLA* (Fannie Mae Form 1003/Freddie Mac Form 65) and Part V of form HUD-92900-A.

(1) Ordering Case Numbers

The Mortgagee must use FHAC to order FHA case numbers. A case number can be obtained only when the Mortgagee has an active mortgage application for the subject Borrower and Property.

In order to obtain a case number, the Mortgagee must:

- provide the subject Borrower's name, SSN, and date of birth;
- provide the property address; and
- certify that the Mortgagee has an active mortgage application for the subject Borrower and Property.

The Mortgagee is not required to input appraiser information at the time the case number is ordered.

(a) Automated Data Processing Codes

FHA Automated Data Processing (ADP) Codes are derived from the section of the National Housing Act under which the Mortgage is to be insured. The Mortgagee must select the correct ADP code for each Mortgage in FHAC.

(b) Case Numbers on Sponsored Originations

The Mortgagee will not be able to order case numbers for sponsored originations unless their sponsored TPO has been registered in FHAC.

(2) Holds Tracking

If FHAC detects that a case number currently exists for the Property, a case number will not be assigned. The Mortgagee will receive notification that the case number assignment has been placed in Holds Tracking. The Mortgagee must review the Holds Tracking screen in FHAC to determine the necessary actions to obtain a case number.

(3) Canceling and Reinstating Case Numbers

(a) Canceling a Case Number

The Mortgagee may request cancellation of a case number by submitting a request to HUD. A case number will be canceled only if:

- an appraisal has not been completed and the Borrower will not close the Mortgage as an FHA-insured Mortgage;

- the FHA mortgage insurance will not be sought; or
- the appraisal has already expired.

The Mortgagee must submit a request for cancellation to the FHA Resource Center at answers@hud.gov using the Case Cancellation Request Template.

(b) Automatic Case Number Cancellations

Case numbers are automatically canceled after six months if one of the following actions is not performed as a last action:
- appraisal information entered;
- Firm Commitment issued by FHA;
- insurance application received and subsequent updates; or
- Notices of Return (NOR) or resubmissions.

Updates to the Borrower's name and/or property address, an appraisal update, or a transmission of the Upfront Mortgage Insurance Premium (UFMIP) do not constitute Last Action Taken.

(c) Reinstatement of Case Numbers

The Mortgagee may request reinstatement of canceled case numbers by submitting a request to the FHA Resource Center using the Case Reinstatement Request Template.

Case numbers that were automatically canceled will be reinstated only if the Mortgagee provides evidence that the subject Mortgage closed prior to cancellation of the case number, such as a Closing Disclosure or similar legal document.

(4) Transferring Case Numbers

(a) Requirements for the Transferring Mortgagee

The original Mortgagee must assign the case number to the new Mortgagee using the Case Transfer function in FHAC immediately upon the Borrower's request.

The original Mortgagee may provide processing documents but is not required to do so.

The original Mortgagee may not charge the Borrower for the transfer of any documents, but the original Mortgagee may negotiate a fee with the new Mortgagee for providing the processing documents. The original Mortgagee is never entitled to a fee for the transfer of processing documents for a Streamline Refinance.

(b) Case Number Transfer Involving a Rejected Mortgage

If the transfer involves a rejected Mortgage, the original Mortgagee must complete the Mortgage Credit Reject function in FHAC prior to transferring the Mortgage.

(c) Case Number Transfer Involving a Sponsored Third-Party Originator

Where a case number is transferred to a new approved Mortgagee or sponsored TPO, the original Mortgagee, its authorized agent, or sponsored TPO that is also an FHA-approved Mortgagee must complete the appropriate sections in FHAC as described in the FHAC Guide – Case Processing Support Functions.

(5) Ordering Title Commitments

The Mortgagee must order a title commitment to ensure the Property will be properly titled and the Mortgage secured in accordance with FHA requirements.

(6) Ordering Appraisals

The Mortgagee must order a new appraisal for each case number assignment and may not reuse an appraisal that was performed under another case number, even if the prior appraisal is not yet more than 120 Days old.

(a) Appraisal Integrity

The Mortgagee is responsible for identifying any problems or potential problems with the integrity, accuracy and thoroughness of an appraisal submitted to FHA for mortgage insurance purposes.

Appraisers must comply with the Uniform Standards of Professional Appraisal Practice (USPAP), including the Competency Rule, when conducting appraisals of Properties intended as security for FHA-insured financing. In appraising any Property for the purpose of obtaining FHA mortgage insurance, the Appraiser must certify that they are capable of performing the appraisal because they have the necessary qualifications and access to all necessary data.

The Mortgagee must ensure that FHA is listed on the appraisal report as an Intended User of the appraisal.

(b) Selection of a Qualified Appraiser

The Mortgagee must order an appraisal from an Appraiser who is listed on the FHA Appraiser Roster and is qualified and knowledgeable in the specific market area in which the Property is located. The Mortgagee must evaluate the Appraiser's education, training and actual field experience to determine whether the Appraiser has sufficient qualifications to perform the appraisal before assignment.

The Mortgagee may not discriminate on the basis of race, color, religion, national origin, sex, age, disability, or actual or perceived sexual orientation and gender identity in the selection of an Appraiser.

(c) Use of Appraisal Management Company or Third-Party Contractors

The Mortgagee may engage an Appraisal Management Company (AMC) to perform services related to the obtaining of an appraisal. The Mortgagee remains responsible for the acts of its AMC or third-party contractors.

The Mortgagee may not pay the AMC and other third-party contractors fees in excess of what is customary and reasonable for such services in the market area where the Property being appraised is located. Any management fees must be for actual services related to the ordering process, or review of appraisal for FHA financing.

(d) Appraiser Independence

The Mortgagee must ensure it does not compromise the Appraiser's independence.

The Mortgagee may not allow the Appraiser to be selected, retained, managed, or compensated by a mortgage broker or any member of a Mortgagee's staff who is compensated on a commission basis tied to the successful completion of a Mortgage or who is not independent of the Mortgagee's mortgage production staff or processes.

The Mortgagee must ensure that it does not:

- compensate the Appraiser at a rate that is not commensurate in the market area of the Property being appraised with the assignment type, complexity and scope of work required for the appraisal services performed;
- withhold or threaten to withhold timely payment or partial payment for an appraisal report;
- prohibit the Appraiser from recording the fee paid for the performance of the appraisal in the appraisal report;
- condition the ordering of an appraisal report or the payment of an appraisal fee, salary, or bonus on the opinion, conclusion or valuation to be reached, or on a preliminary value estimate requested from an Appraiser;

- provide to the Appraiser, appraisal company, AMC or any Entity or person related to the Appraiser, appraisal company or AMC, stock or other financial or non-financial benefits;
- order, obtain, use, or pay for a second or subsequent appraisal or Automated Valuation Model (AVM) in connection with a Mortgage financing transaction unless:
  - there is a reasonable basis to believe that the initial appraisal was flawed or tainted and such belief is clearly and appropriately noted in the mortgage file; or
  - such appraisal or AVM was completed pursuant to written, pre-established bona fide pre- or post-Disbursement appraisal review or quality control process or underwriting guidelines and the Mortgagee adheres to a policy of selecting the most reliable appraisal, rather than the appraisal that states the highest value;
- withhold or threaten to withhold future business from an Appraiser, or demote or terminate or threaten to demote or terminate an Appraiser in order to influence an Appraiser to arrive at a predetermined or desired value;
- make expressed or implied promises of future business, promotions or increased compensation for an Appraiser in order to influence an Appraiser to arrive at a predetermined or desired value;
- allow the removal of an Appraiser from a list of qualified Appraisers or the addition of an Appraiser to an exclusionary list of qualified Appraisers, used by any Entity, without prompt written notice to such Appraiser. The notice must include written evidence of the Appraiser's illegal conduct, violation of USPAP or state licensing standards, improper or unprofessional behavior or other substantive reason for removal;
- request that an Appraiser provide an estimated, predetermined or desired valuation in an appraisal report prior to the completion of the appraisal report, or request that an Appraiser provide estimated values or comparable sales at any time prior to the Appraiser's completion of an appraisal report;
- provide to the Appraiser an anticipated, estimated, encouraged or desired value for a subject Property or a proposed, or target amount to be loaned to the Borrower, except that a copy of the sales contract for purchase and any addendum must be provided; or
- perform any other act or practice that impairs or attempts to impair an Appraiser's independence, objectivity, or impartiality, or that violates any applicable law, regulation, or requirement.

(e) Additional Requirements When Ordering an Appraisal

The Mortgagee must provide to the selected Appraiser the FHA case number and a complete copy of the subject sales contract including all addendums, land lease, surveys and other legal documents contained in the mortgage file necessary to analyze the Property.

The Mortgagee must disclose all known information regarding any environmental hazard that is in or on the subject Property, or in the vicinity of the Property, whether obtained from the Borrower, the real estate broker, or any other party to the transaction.

Where the Mortgagee determines that the Property will remain subject to a PACE obligation, it must notify the Appraiser and provide to the Appraiser all terms and conditions of the PACE obligation.

(7) Appraisal Effective Date

(a) Standard

The effective date of the appraisal cannot be before the FHA case number assignment date unless the Mortgagee certifies, via the certification field in the Appraisal Logging Screen in FHAC, that the appraisal was ordered for conventional lending or government-guaranteed loan purposes and was performed by a FHA Roster Appraiser.

The Mortgagee must ensure that the appraisal was performed in accordance with FHA appraisal reporting instructions as detailed in this *SF Handbook* and the Appraisal Report and Data Delivery Guide. The intended use of the appraisal must indicate that it is solely to assist FHA in assessing the risk of the Property securing the FHA-insured Mortgage. Additionally, FHA and the Mortgagee must be indicated as the intended users of the appraisal report.

(b) Required Documentation

The Mortgagee must retain documentation in the case binder substantiating conversion of the Mortgage to FHA.

(8) Transferring Existing Appraisals

In cases where a Borrower has switched Mortgagees, the first Mortgagee must, at the Borrower's request, transfer the appraisal to the second Mortgagee within five business days. The Appraiser is not required to provide the appraisal to the new Mortgagee. The client name on the appraisal does not need to reflect the new Mortgagee. If the original Mortgagee has not been reimbursed for the cost of the appraisal, the Mortgagee is not required to transfer the appraisal until it is reimbursed.

The second Mortgagee may not request the Appraiser to re-address the appraisal. If the second Mortgagee finds deficiencies in the appraisal, the Mortgagee must order a new appraisal.

Where a Mortgagee uses an existing appraisal for a different Borrower, the Mortgagee must enter the new Borrower's information in FHAC. The Mortgagee must collect an appraisal fee from the new Borrower and refund the fee to the original Borrower.

If a Case Transfer is involved, the new Mortgagee must enter the Borrower's information in FHAC. The new Mortgagee must collect an appraisal fee from the Borrower, and send the fee to the original Mortgagee, who, in turn, must refund the fee to the original Borrower.

(9) Ordering Second Appraisal

The Mortgagee is prohibited from ordering an additional appraisal to achieve an increase in value for the Property and/or the elimination or reduction of deficiencies and/or repairs required.

The Mortgagee may order a second appraisal for Mortgages that are in accordance with requirements on Property Flipping.

(a) Second Appraisal by Original Mortgagee

A second appraisal may only be ordered if the Direct Endorsement (DE) underwriter (underwriter) determines the first appraisal is materially deficient and the Appraiser is unable or uncooperative in resolving the deficiency. The Mortgagee must fully document the deficiency and status of the appraisal in the mortgage file. The Mortgagee must pay for the second appraisal.

Material deficiencies on appraisals are those deficiencies that have a direct impact on value and marketability. Material deficiencies include, but are not limited to:

- failure to report readily observable defects that impact the health and safety of the occupants and/or structural soundness of the house;
- reliance upon outdated or dissimilar comparable sales when more recent and/or comparable sales were available as of the effective date of the appraisal; and
- fraudulent statements or conclusions when the Appraiser had reason to know or should have known that such statements or conclusions compromise the integrity, accuracy and/or thoroughness of the appraisal submitted to the client.

(b) Second Appraisal by Second Mortgagee

A second appraisal may only be ordered by the second Mortgagee under the following limited circumstances:

- the first appraisal contains material deficiencies as determined by the underwriter for the second Mortgagee;

- the Appraiser performing the first appraisal is prohibited from performing appraisals for the second Mortgagee; or
- the first Mortgagee fails to provide a copy of the appraisal to the second Mortgagee in a timely manner, and the failure would cause a delay in closing and harm to the Borrower, including loss of interest rate lock, violation of purchase contract deadline, occurrence of foreclosure proceedings and imposition of late fees.

(c) Use of Second Appraisal

For the first two cases outlined above, the Mortgagee must rely only on the second appraisal and ensure that copies of both appraisals are retained in the case binder. For the third case above, the first appraisal must be added to the case binder if it is received.

(d) Required Documentation

The Mortgagee must document why a second appraisal was ordered and retain the explanation and all appraisal reports in the case binder.

(10) Ordering an Update to an Appraisal

The Mortgagee may only order an update if (1) it is a Mortgagee listed as an Intended User of the original appraisal or (2) it has received permission from the original client and the Appraiser. The Appraiser incorporates the original report being updated by attachment rather than by reference per Advisory Opinion 3 of the USPAP.

The Mortgagee may use an update of appraisal only if:

- it is performed by the FHA Appraiser who performed the original appraisal, who is currently in good standing on the FHA Appraiser Roster;
- the Property has not declined in value;
- the building improvements that contribute value to the Property can be observed from the street or a public way;
- the exterior inspection of the Property reveals no deficiencies or other significant changes;
- the update of appraisal was ordered by the Mortgagee and completed by the Appraiser prior to the expiration of the initial 120-Day period; and
- the original appraisal report was not previously updated.

(11) Appraisal Delivery – Electronic Appraisal Delivery Portal

(a) Definition

The Electronic Appraisal Delivery (EAD) portal is a web-based platform where Mortgagees or their designated third-party service providers electronically deliver FHA Single Family appraisal reports prior to endorsement.

(b) Standard

Mortgagees or their designated third-party service providers must deliver appraisals through the EAD portal.

(c) Required Documentation

Appraisals submitted through the EAD are the appraisal of record for endorsement.

b. General Mortgage Insurance Eligibility

i. Mortgage Purpose

FHA offers various mortgage insurance programs which insure approved Mortgagees against losses on Mortgages. FHA-insured Mortgages may be used to purchase housing, improve housing, or refinance existing Mortgages.

(A) Purchase/Construction to Permanent

The Borrower may finance the purchase of an existing one- to four-unit residence, and may also finance construction of a one- to four-unit residence through a Construction to Permanent Mortgage.

Properties to be acquired through an unrecorded land contract must be treated as a purchase.

(B) Rehabilitation

(1) 203(k) Standard and Limited Rehabilitation Mortgages

The Section 203(k) Rehabilitation Mortgage Insurance is used to:

- rehabilitate an existing one- to four-unit Structure, which will be used primarily for residential purposes;
- rehabilitate such a Structure and refinance the outstanding indebtedness on the Structure and the Real Property on which the Structure is located; or
- purchase and rehabilitate the Structure and purchase the Real Property on which the Structure is located.

(2) 203(h) and 203(k) for Disaster Victims

The Section 203(h) Mortgage Insurance for Disaster Victims program allows FHA to insure Mortgages made by qualified Mortgagees to victims of a Presidentially-Declared Major Disaster Area (PDMDA) who have lost their housing, or whose housing was damaged and are in the process of rebuilding or buying another house.

(C) Refinance

A refinance transaction is used to pay off the existing debt or to withdraw equity from the Property with the proceeds of a new Mortgage for a Borrower with legal title to the subject Property.

Types of Refinances

FHA insures several different types of refinance transactions:

1. Cash-out refinances are designed to pull equity out of the Property.
2. No cash-out refinances of FHA-insured and non FHA-insured Mortgages are designed to pay existing liens. These include: Rate and Term refinance, Simple Refinance, and Streamline Refinance.
3. Refinances of non FHA-insured Mortgages are available for qualified Borrowers in negative equity positions (Short Refi).
4. Refinances for rehabilitation or repair (Section 203(k)).

ii. Borrower Eligibility

(A) General Borrower Eligibility Requirements

In order to obtain FHA-insured financing, all Borrowers must meet the eligibility criteria in this section.

A party who has a financial interest in the mortgage transaction, such as the seller, builder or real estate agent, may not be a co-Borrower or a Cosigner. Exceptions may be granted when the party with the financial interest is a Family Member.

(1) Social Security Number

(a) Standard

Each Borrower must provide evidence of their valid SSN to the Mortgagee.

Exception

State and local government agencies, Instrumentalities of Government and HUD-approved Nonprofit organizations are not required to provide an SSN.

(b) Required Documentation

The Mortgagee must:

- validate and document an SSN for each Borrower, co-Borrower, or Cosigner on the Mortgage by:

    - entering the Borrower's name, date of birth, and SSN in the Borrower/address validation screen through FHAC; and
    - examining the Borrower's original pay stubs, W-2 forms, valid tax returns obtained directly from the IRS, or other document relied upon to underwrite the Mortgage; and
- resolve any inconsistencies or multiple SSNs for individual Borrowers that are revealed during Mortgage processing and underwriting using a service provider to verify the SSN with the SSA.

(2) Borrower Age Limits

The Borrower must be old enough to enter into a mortgage Note that can be legally enforced in the state, or other jurisdiction, where the Property is located ("State Law"). There is no maximum age limit for a Borrower.

(3) Borrower Minimum Decision Credit Score

(a) Definition

The Minimum Decision Credit Score (MDCS) refers to the credit score reported on the Borrower's credit report when all reported scores are the same. Where three differing scores are reported, the middle score is the MDCS. Where two differing scores are reported, the MDCS is the lowest score. Where only one score is reported, that score is the MDCS.

An MDCS is determined for each Borrower. Where the Mortgage involves multiple Borrowers, the Mortgagee must determine the MDCS for each Borrower, and then select the lowest MDCS for all Borrowers.

Where the Mortgage involves multiple Borrowers and one or more of the Borrowers do not have a credit score (non-traditional or insufficient credit), the Mortgagee must select the lowest MDCS of the Borrower(s) with credit score(s).

(b) Eligibility Standard

The Borrower is not eligible for FHA-insured financing if the MDCS is less than 500.

(4) Borrower and Co-Borrower Ownership and Obligation Requirements

To be eligible, all occupying and non-occupying Borrowers and co-Borrowers must take title to the Property in their own name or a Living Trust at settlement, be obligated on the Note or credit instrument, and sign all security instruments.

In community property states, the Borrower's spouse is not required to be a Borrower or a Cosigner. However, the Mortgage must be executed by all parties necessary to make the lien valid and enforceable under State Law.

(5) Cosigner Requirements

Cosigners are liable for the debt and therefore, must sign the Note. Cosigners do not hold an ownership interest in the subject Property and therefore, do not sign the security instrument.

(6) Principal Residence in the United States

Non-occupying co-Borrowers or Cosigners must either be United States (U.S.) citizens or have a Principal Residence in the U.S.

(7) Military Personnel Eligibility

(a) Standard

Borrowers who are military personnel, who cannot physically reside in a Property because they are on Active Duty, are still considered owner occupants and are eligible for maximum financing if a Family Member of the Borrower will occupy the subject Property as their Principal Residence, or the Borrower intends to occupy the subject Property upon discharge from military service.

(b) Required Documentation

The Mortgagee must obtain a copy of the Borrower's military orders evidencing the Borrower's Active Duty status and that the duty station is more than 100 miles from the subject Property.

The Mortgagee must obtain the Borrower's intent to occupy the subject Property upon discharge from military service, if a Family Member will not occupy the subject Property as their Principal Residence.

(8) Citizenship and Immigration Status

U.S. citizenship is not required for Mortgage eligibility.

(9) Residency Requirements

The Mortgagee must determine the residency status of the Borrower based on information provided on the mortgage application and other applicable documentation. In no case is a Social Security card sufficient to prove immigration or work status.

(a) Lawful Permanent Resident Aliens

(i) Standard

A Borrower with lawful permanent resident alien status may be eligible for FHA-insured financing provided the Borrower satisfies the same requirements, terms and conditions as those for U.S. citizens.

(ii) Required Documentation

The mortgage file must include evidence of the permanent residency and indicate that the Borrower is a lawful permanent resident alien on the *URLA*.

The U.S. Citizenship and Immigration Services (USCIS) within the Department of Homeland Security provides evidence of lawful, permanent residency status.

(b) Non-Permanent Resident Aliens

A Borrower who is a non-permanent resident alien may be eligible for FHA-insured financing provided:

- the Property will be the Borrower's Principal Residence;
- the Borrower has a valid SSN, except for those employed by the World Bank, a foreign embassy, or equivalent employer identified by HUD;
- the Borrower is eligible to work in the United States, as evidenced by the Employment Authorization Document issued by the USCIS; and
- the Borrower satisfies the same requirements, terms and conditions as those for U.S. citizens.

The Employment Authorization Document is required to substantiate work status. If the Employment Authorization Document will expire within one year and a prior history of residency status renewals exists, the Mortgagee may assume that continuation will be granted. If there are no prior renewals, the Mortgagee must determine the likelihood of renewal based on information from the USCIS.

A Borrower residing in the U.S. by virtue of refugee or asylee status granted by the USCIS is automatically eligible to work in this country. The Employment Authorization Document is not required, but documentation substantiating the refugee or asylee status must be obtained.

(c) Non-U.S. Citizens without Lawful Residency

Non-U.S. citizens without lawful residency in the U.S. are not eligible for FHA-insured Mortgages.

(10) Borrower Ineligibility Due to Delinquent Federal Non-Tax Debt

(a) Standard

Mortgagees are prohibited from processing an application for an FHA-insured Mortgage for Borrowers with delinquent federal non-tax debt, including deficiency Judgments and other debt associated with past FHA-insured Mortgages. Mortgagees are required to determine whether the Borrowers have delinquent federal non-tax debt. Mortgagees may obtain information on delinquent Federal Debts from public records, credit reports or equivalent, and must check all Borrowers against the Credit Alert Verification Reporting System (CAIVRS).

(b) Verification

If a delinquent Federal Debt is reflected in a public record, credit report or equivalent, or CAIVRS or an Equivalent System, the Mortgagee must verify the validity and delinquency status of the debt by contacting the creditor agency to whom the debt is owed. If the debt was identified through CAIVRS, the Mortgagee must contact the creditor agency using the contact phone number and debt reference number reflected in the Borrower's CAIVRS report.

If the creditor agency confirms that the debt is valid and in delinquent status as defined by the Debt Collection Improvement Act, then the Borrower is ineligible for an FHA-insured Mortgage until the Borrower resolves the debt with the creditor agency.

The Mortgagee may not deny a Mortgage solely on the basis of CAIVRS information that has not been verified by the Mortgagee. If resolved either by determining that the information in CAIVRS is no longer valid or by resolving the delinquent status as stated above, the Mortgagee may continue to process the mortgage application.

(c) Resolution

In order for a Borrower with verified delinquent Federal Debt to become eligible, the Borrower must resolve their federal non-tax debt in accordance with the Debt Collection Improvement Act.

The creditor agency that is owed the debt can verify that the debt has been resolved in accordance with the Debt Collection Improvement Act.

(d) Required Documentation

The Mortgagee must include documentation from the creditor agency to support the verification and resolution of the debt. For debt reported through

CAIVRS, the Mortgagee may obtain evidence of resolution by obtaining a clear CAIVRS report.

(11) Eligibility Period for Borrowers Delinquent on FHA-Insured Mortgages

If a Borrower is currently delinquent on an FHA-insured Mortgage, they are ineligible for a new FHA-insured Mortgage unless the delinquency is resolved.

(12) Delinquent Federal Tax Debt

(a) Standard

Borrowers with delinquent Federal Tax Debt are ineligible.

Tax liens may remain unpaid if the Borrower has entered into a valid repayment agreement with the federal agency owed to make regular payments on the debt and the Borrower has made timely payments for at least three months of scheduled payments. 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 calculation of the Borrower's Debt-to-Income (DTI) ratio.

(b) Verification

Mortgagees must check public records and credit information to verify that the Borrower is not presently delinquent on any Federal Debt and does not have a tax lien placed against their Property for a debt owed to the federal government.

(c) Required Documentation

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

(13) Valid First Liens

The Mortgagee must ensure that the mortgaged Property will be free and clear of all liens, except the insured Mortgage and any secondary liens permitted by FHA regulations at 24 CFR §§ 203.32 and 203.41.

(a) Consent of Non-Borrowing Spouses

If necessary to perfect a valid first lien under state law, the Mortgagee must require a non-borrowing spouse to execute either the security instrument or documentation indicating that they are relinquishing all rights to the Property.

(b) Tax Liens

Tax liens may remain unpaid if the Borrower has entered into a valid repayment agreement with the lien holder to make regular payments on the debt and the Borrower has made timely payments for at least three months of scheduled payments. The Borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments. The lien holder must subordinate the tax lien to the FHA-insured Mortgage.

(14) Additional Eligibility Requirements for Nonprofit Organizations and State and Local Government Agencies

(a) Eligibility Criteria for a Mortgage for Nonprofit Organizations

***(i)* Standard**

HUD-approved Nonprofit organizations may be eligible for FHA-insured Mortgages. Nonprofits are not eligible for cash-out refinances.

HUD-approved Nonprofit organizations are eligible for the same percentage of financing that is available to an owner-occupant on their Principal Residence.

HUD-approved Nonprofit organizations may only obtain FHA-insured fixed rate Mortgages.

***(ii)* Required Documentation**

A HUD-approved Nonprofit must be listed on the HUD Nonprofit Agency Roster and intend to sell or lease the Property to Low- to Moderate-Income families.

(b) Eligibility Criteria for a Mortgage for State and Local Government Agencies

***(i)* Standard**

State and local government agencies and instrumentalities of government may obtain FHA-insured financing provided:

- the agency has the legal authority to become the Borrower;
- the particular state or local government is not in bankruptcy; and
- there is no legal prohibition on obtaining a deficiency Judgment based solely on its status as a state and local government.

State and local government agencies are eligible for the same percentage of financing that is available to an owner-occupant on their Principal

Residence. State and local government agencies are not eligible for cash-out refinances.

State and local government agencies may only obtain FHA-insured fixed rate Mortgages.

***(ii)* Required Documentation**

The Mortgagee must obtain an opinion from counsel verifying the legal status requirements of the agency.

State and local government agencies are not required to be listed on the HUD-approved Nonprofit roster.

(15) Eligibility Requirements for Living Trusts

(a) Property Held in Living Trusts

The Mortgagee may originate a Mortgage for a living trust for a Property held by the living trust, provided the beneficiary of the living trust is a Cosigner and will occupy the Property as their Principal Residence, and the trust provides reasonable means to assure that the Mortgagee will be notified of any changes to the trust, including transfer of beneficial interest and any changes in occupancy status of the Property.

(b) Living Trusts and Security Instruments

***(i)* Standard**

The name of the living trust must appear on the security instrument, such as the Mortgage, deed of trust, or security deed.

The name of the individual Borrower must appear on the security instrument when required to create a valid lien under state law. The names of the owner-occupant and other Borrowers, if any, must also appear on the Note with the trust.

The name of the individual Borrower is not required to appear on the property deed or title.

***(ii)* Required Documentation**

The Mortgagee must obtain a copy of the trust documentation.

(B) Excluded Parties

The Mortgagee must establish that no participants are Excluded Parties and document the determination on form HUD-92900-LT, *FHA Loan Underwriting and Transmittal Summary*.

(1) Borrower

(a) Standard

A Borrower is not eligible to participate in FHA-insured mortgage transactions if they are suspended, debarred, or otherwise excluded from participating in HUD programs.

(b) Required Documentation

The Mortgagee must check the HUD LDP list to confirm the Borrower's eligibility to participate in an FHA-insured mortgage transaction.

The Mortgagee must check SAM and follow appropriate procedures defined by that system to confirm eligibility for participation.

The Mortgagee must check the "Yes" box on form HUD-92900-LT if the Borrower appears on either the LDP or SAM list.

(2) Other Parties to the Transaction

(a) Standard

A Mortgage is not eligible for FHA insurance if anyone participating in the mortgage transaction is listed on HUD's LDP list or in SAM as being excluded from participation in HUD transactions. This may include but is not limited to:

- seller (except where selling the Principal Residence)
- listing and selling real estate agent
- loan originator
- loan processor
- underwriter
- Appraiser
- 203(k) Consultant
- Closing Agent
- title company

(b) Required Documentation

The Mortgagee must check the HUD LDP list and SAM and follow appropriate procedures defined by that system to confirm eligibility for all participants involved in the transaction.

iii. Occupancy Types

(A) Principal Residence

(1) Definition

A Principal Residence refers to a dwelling where the Borrower maintains or will maintain their permanent place of abode, and which the Borrower typically occupies or will occupy for the majority of the calendar year. A person may have only one Principal Residence at any one time.

(2) Standard

(a) FHA Requirement for Owner Occupancy

At least one Borrower must occupy the Property within 60 Days of signing the security instrument and intend to continue occupancy for at least one year.

203(k) Rehabilitation products may have different requirements for the length of time to occupy the Property.

(b) FHA-Insured Mortgages on Principal Residences

FHA will not insure more than one Property as a Principal Residence for any Borrower, except as noted below. FHA will not insure a Mortgage if it is determined that the transaction was designed to use FHA mortgage insurance as a vehicle for obtaining Investment Properties, even if the Property to be insured will be the only one owned using FHA mortgage insurance.

Properties previously acquired as Investment Properties are not subject to these restrictions.

(c) Exceptions to the FHA Policy Limiting the Number of Mortgages per Borrower

The table below describes the only circumstances in which a Borrower with an existing FHA-insured Mortgage for a Principal Residence may obtain an additional FHA-insured Mortgage on a new Principal Residence.

Policy Exceptions	Eligibility Requirements
Relocation	A Borrower may be eligible to obtain another FHA-insured Mortgage without being required to sell an existing Property covered by an FHA-insured Mortgage if the Borrower is: • relocating or has relocated for an employment-related reason; and • establishing or has established a new Principal Residence in an area more than 100 miles from the Borrower's current Principal Residence. If the Borrower moves back to the original area, the Borrower is not required to live in the original house and may obtain a new FHA-insured Mortgage on a new Principal Residence, provided the relocation meets the two requirements above.
Increase in family size	A Borrower may be eligible for another house with an FHA-insured Mortgage if the Borrower provides satisfactory evidence that: • the Borrower has had an increase in legal dependents and the Property now fails to meet family needs; and • the Loan-to-Value (LTV) ratio on the current Principal Residence is equal to or less than 75% or is paid down to that amount, based on the outstanding Mortgage balance and a current residential appraisal.
Vacating a jointly-owned Property	A Borrower may be eligible for another FHA-insured Mortgage if the Borrower is vacating (with no intent to return) the Principal Residence which will remain occupied by an existing co-Borrower.
Non-occupying co-Borrower	A non-occupying co-Borrower on an existing FHA-insured Mortgage may qualify for an FHA-insured Mortgage on a new Property to be their own Principal Residence.

(3) Required Documentation

The Borrower must indicate on the *URLA* (Fannie Mae Form 1003/ Freddie Mac Form 65) that the Property will be the Borrower's Principal Residence and certify to that fact on form HUD-92900-A, *HUD/VA Addendum to URLA.*

(B) Secondary Residence

(1) Definition

Secondary Residence refers to a dwelling that a Borrower occupies in addition to their Principal Residence, but less than a majority of the calendar year. A Secondary Residence does not include a Vacation Home.

(2) Standard

Secondary Residences are only permitted with written approval from the Jurisdictional HOC after a determination that:

- the Borrower has no other Secondary Residence;
- the Secondary Residence will not be a Vacation Home or be otherwise used primarily for recreational purposes;
- the commuting distance to the Borrower's workplace creates an undue hardship on the Borrower and there is no affordable rental housing meeting the Borrower's needs within 100 miles of the Borrower's workplace; and
- the maximum mortgage amount is 85 percent of the lesser of the appraised value or sales price.

(3) Required Documentation

The Mortgagee must demonstrate the lack of affordable rental housing, and include:

- a satisfactory explanation of the need for a Secondary Residence and the lack of available rental housing; and
- written evidence from local real estate professionals who verify a lack of acceptable housing in the area.

(C) Investment Property

(1) Definition

An Investment Property refers to a Property that is not occupied by the Borrower as a Principal or Secondary Residence.

(2) Standard

Investment Properties are not eligible for FHA insurance.

Exception

Investment Properties are eligible if the borrower is a HUD-approved Nonprofit Borrower, or a state and local government agency, or an Instrumentality of Government.

Investment Properties are eligible for insurance under the HUD Real Estate Owned (REO) Purchasing product, except under the 203(k) program.

iv. Property Eligibility and Acceptability Criteria

(A) General Property Eligibility

The Property must be located within the U.S., Puerto Rico, Guam, the Virgin Islands, the Commonwealth of the Northern Mariana Islands, or American Samoa.

(1) Special Flood Hazard Areas

The Mortgagee must determine if a Property is located in a Special Flood Hazard Area (SFHA) as designated by the Federal Emergency Management Agency (FEMA). The Mortgagee must obtain flood zone determination services, independent of any assessment made by the Appraiser to cover the Life of the Loan Flood Certification.

A Property is not eligible for FHA insurance if:

- a residential building and related improvements to the Property are located within SFHA Zone A, a Special Flood Zone Area, or Zone V, a Coastal Area, and insurance under the National Flood Insurance Program (NFIP) is not available in the community; or
- the improvements are, or are proposed to be, located within a Coastal Barrier Resource System (CBRS).

(a) Eligibility for Proposed or New Construction in SFHAs

If any portion of the dwelling, related Structures or equipment essential to the value of the Property and subject to flood damage is located within an SFHA, the Property is not eligible for FHA mortgage insurance unless the Mortgagee:

- obtains from FEMA a final Letter of Map Amendment (LOMA) or final Letter of Map Revision (LOMR) that removes the Property from the SFHA; or
- obtains a FEMA National Flood Insurance Program Elevation Certificate (FEMA Form 81-31) prepared by a licensed engineer or surveyor. The elevation certificate must document that the lowest floor including the basement of the residential building, and all related improvements/equipment essential to the value of the Property, is built at or above the 100-year flood elevation in compliance with the NFIP criteria, and insurance under the NFIP is obtained.

(b) Eligibility for Existing Construction in SFHAs

When any portion of the residential improvements is determined to be located within an SFHA, insurance under the NFIP must be obtained.

(c) Eligibility for Condominiums in SFHAs

The Mortgagee must ensure the Homeowners' Association (HOA) obtains insurance under the NFIP on buildings located within the SFHA. The flood insurance coverage must protect the interest of the Borrowers who hold title to an individual unit, as well as the common areas of the Condominium Project.

(d) Eligibility for Manufactured Housing in SFHAs

The finished grade level beneath the Manufactured Home must be at or above the 100-year return frequency flood elevation. If any portion of the dwelling, related Structures or equipment essential to the Property Value and subject to flood damage for both new and existing Manufactured Homes are located within an SFHA, the Property is not eligible for FHA mortgage insurance unless the Mortgagee obtains:

- a FEMA issued LOMA or LOMR that removes the Property from the SFHA; or
- a FEMA National Flood Insurance Program (NFIP) Elevation Certificate (FEMA Form 81-31) prepared by a licensed engineer or surveyor stating that the finished grade beneath the Manufactured Home is at or above the 100-year return frequency flood elevation, and insurance under the NFIP is obtained.

(e) Required Flood Insurance Amount

For Properties located within an SFHA, flood insurance must be maintained for the life of the Mortgage in an amount at least equal to the lesser of:

- the outstanding balance of the Mortgage, less estimated land costs; or
- the maximum amount of the NFIP insurance available with respect to the property improvements.

(f) Required Documentation

The Mortgagee must obtain a Life of Loan Flood Certification for all Properties. If applicable, the Mortgagee must also obtain a:

- FEMA Letter of Map Amendment;
- FEMA Letter of Map Revision; or
- FEMA National Flood Insurance Program Elevation Certificate (FEMA 81-31).

(g) Restrictions on Property Locations within Coastal Barrier Resources System

In accordance with the Coastal Barrier Resources Act, a Property is not eligible for FHA mortgage insurance if the improvements are or are proposed to be located within the Coastal Barrier Resources System.

(2) Seller Must Be Owner of Record

(a) Standard

To be eligible for a mortgage insured by FHA, a Property must be purchased from the owner of record. The transaction may not involve any sale or assignment of the sales contract.

(b) Required Documentation

The Mortgagee must obtain documentation verifying that the seller is the owner of record.

Such documentation may include, but is not limited to:

- a property sales history report;
- a copy of the recorded deed from the seller; or
- other documentation, such as a copy of a property tax bill, title commitment, or binder, demonstrating the seller's ownership of the Property and the date it was acquired.

This requirement applies to all FHA purchase money Mortgages, regardless of the time between resales.

(3) Restrictions on Property Flipping

Property Flipping is indicative of a practice whereby recently acquired Property is resold for a considerable profit with an artificially inflated value.

(a) Definition

Property Flipping refers to the purchase and subsequent resale of a Property in a short period of time.

(b) Standard

(i) Time Restriction on Transfers of Title

The eligibility of a Property for a Mortgage insured by FHA is determined by the time that has elapsed between the date the seller has acquired title to the Property and the date of execution of the sales contract that will result in the FHA-insured Mortgage.

FHA defines the seller's date of acquisition as the date the seller acquired legal ownership of that Property. FHA defines the resale date as the date of execution of the sales contract by all parties intending to finance the Property with an FHA-insured Mortgage.

(ii) Restriction on Resales Occurring 90 Days or Fewer After Acquisition

A Property that is being resold 90 Days or fewer following the seller's date of acquisition is not eligible for an FHA-insured Mortgage.

(iii) Resales Occurring Between 91 Days and 180 Days After Acquisition

A Mortgagee must obtain a second appraisal by another Appraiser if:

- the resale date of a Property is between 91 and 180 Days following the acquisition of the Property by the seller; and
- the resale price is 100 percent or more over the price paid by the seller to acquire the Property.

If the second appraisal supports a value of the Property that is more than 5 percent lower than the value of the first appraisal, the lower value must be used as the Property Value in determining the Adjusted Value.

The cost of the second appraisal may not be charged to the Borrower.

(iv) Exceptions to Time Restrictions on Resale

Exceptions to time restrictions on resale are:

- Properties acquired by an employer or relocation agency in connection with the relocation of an employee;
- resales by HUD under its REO program;
- sales by other U.S. government agencies of Single Family Properties pursuant to programs operated by these agencies;
- sales of Properties by nonprofits approved to purchase HUD owned Single Family Properties at a discount with resale restrictions;
- sales of Properties that are acquired by the seller by inheritance;
- sales of Properties by state and federally-chartered financial institutions and Government-Sponsored Enterprises (GSE);
- sales of Properties by local and state government agencies; and
- sales of Properties within PDMDAs, only upon issuance of a notice of an exception from HUD.

The restrictions listed above and those in 24 CFR § 203.37a do not apply to a builder selling a newly built house or building a house for a Borrower planning to use FHA-insured financing.

(c) Required Documentation

The Mortgagee must obtain a 12 month chain of title documenting compliance with time restrictions on resales.

(4) Restriction on Investment Properties for Hotel and Transient Use

(a) Standard

The Mortgagee must obtain the Borrower's agreement that Investment Properties using FHA-insured financing will not be used for hotel or transient purposes, or otherwise rented for periods of less than 30 Days.

(b) Required Documentation

The Mortgagee must obtain a completed form HUD-92561, *Borrower's Contract with Respect to Hotel and Transient Use of Property*, for each Mortgage secured by:

- a two- to four-unit dwelling; or
- a Single Family dwelling that is one of a group of five or more dwellings owned by the Borrower within a two block radius.

(5) Mixed Use of Property

Mixed Use refers to a Property suitable for a combination of uses including any of the following: commercial, residential, retail, office or parking space. Mixed Use one- to four-unit Single Family Properties are eligible for FHA insurance, provided:

- a minimum of 51 percent of the entire building square footage is for residential use; and
- the commercial use will not affect the health and safety of the occupants of the residential Property.

(6) Property Assessed Clean Energy

Property Assessed Clean Energy (PACE) refers to an alternative means of financing energy and other PACE-allowed improvements for residential properties using financing provided by private enterprises in conjunction with state and local governments. Generally, the repayment of the PACE obligation is collected in the same manner as a special assessment tax; it is collected by the local government rather than paid directly by the Borrower to the party providing the PACE financing.

Generally, the PACE obligation is also secured in the same manner as a special assessment tax against the Property. In the event of a sale, including a foreclosure sale, of the Property with outstanding PACE financing, the obligation will continue with the Property causing the new homeowner to be responsible for the payments on the outstanding PACE amount. In cases of foreclosure, priority collection of delinquent payments for the PACE assessment may be waived or relinquished.

Properties which will remain encumbered with a PACE obligation are eligible for FHA-insured financing provided that the Mortgagee determines that the following requirements have been met:

- under the laws of the state where the Property is located, the PACE obligation is collected and secured by the creditor in the same manner as special assessment taxes against the Property;
- the Property may only become subject to an enforceable claim (i.e., lien) that is superior to the FHA-insured Mortgage for delinquent regularly scheduled PACE special assessment payments. The Property shall not be subject to an enforceable claim (i.e., lien) superior to the FHA-insured Mortgage for the full outstanding PACE obligation at any time (i.e., through acceleration of the full obligation). However, a notice of the lien for the full PACE obligation may be recorded in the land records;
- there are no terms or conditions that limit the transfer of the Property to a new homeowner. Legal restrictions on conveyance arising from a PACE obligation that could require consent of a third party before the owner can convey the Real Property are prohibited, unless such provisions may be terminated at the option of, and with no cost to, the homeowner;
- the existence of a PACE obligation on a Property is readily apparent to Mortgagees, Appraisers, Borrowers and other parties to an FHA-insured Mortgage transaction in the public records and must show the obligation amount, the expiration date and cause of the expiration of the assessment. In no case may default accelerate the expiration date; and
- in the event of a sale, including a foreclosure sale, of the Property with outstanding PACE financing, the obligation will continue with the Property causing the new homeowner to be responsible for the payments on the outstanding PACE amount.

(7) Dwelling Unit Limitation

(a) Standard

If the Mortgage will be secured by an Investment Property, including Mortgages for Governmental Entities or nonprofit Borrowers, the Borrower may not have a financial interest, regardless of the ownership or financing type, in more than seven Dwelling Units within a two block radius. In determining the number of Dwelling Units owned by the Borrower, the Mortgagee must count each Dwelling Unit in a two-, three-, and four-family Property.

(b) Required Documentation

If the Borrower owns six or more units within a two block radius, a map must be provided disclosing the locations of the units as evidence of compliance with FHA's seven unit limitation.

(B) Property Types

FHA's programs differ from one another primarily in terms of what types of Properties and financing are eligible. Except as otherwise stated in this *SF Handbook,* FHA's Single Family programs are limited to one- to four-family Properties that are owner-occupied Principal Residences. FHA insures Mortgages on Real Property secured by:

- detached or semi-detached dwellings
- Manufactured Housing
- townhouses or row houses
- individual units within FHA-approved Condominium Projects

FHA will not insure Single Family Mortgages secured by:

- commercial enterprises
- boarding houses
- hotels, motels and condotels
- tourist houses
- private clubs
- bed and breakfast establishments
- other transient housing
- Vacation Homes
- fraternity and sorority houses

(1) One Unit

A one-unit Property is a one-family dwelling.

(2) Two Unit

A two-unit Property is a Single Family residential Property with two individual dwellings.

The Mortgagee must obtain a completed form HUD-92561, *Borrower's Contract with Respect to Hotel and Transient Use of Property.*

(3) Three to Four Unit

A three- to four-unit Property is a Single Family residential Property with three to four individual dwellings.

The Mortgagee must obtain a completed form HUD-92561.

Self-Sufficiency Rental Income Eligibility

(a) Definition

Net Self-Sufficiency Rental Income refers to the Rental Income produced by the subject Property over and above the Principal, Interest, Taxes, and Insurance (PITI).

(b) Standard

The PITI divided by the monthly Net Self-Sufficiency Rental Income may not exceed 100 percent for three- to four-unit Properties.

(c) Calculation

Net Self-Sufficiency Rental Income is calculated by using the Appraiser's estimate of fair market rent from all units, including the unit the Borrower chooses for occupancy, and subtracting the greater of the Appraiser's estimate for vacancies and maintenance, or 25 percent of the fair market rent.

(4) Condominium Unit

A Condominium Unit is a Property contained in a multi-unit project that has individually-owned Dwelling units, which may be either attached in one or more Structures or detached from each other, and is primarily residential in use.

(a) Standard

A condominium development is created by state or local law and is characterized by fee-simple ownership of a unit, which is defined in the condominium documents, together with common areas. The property interest in these areas is both common and undivided on the part of all unit owners, each of whom belongs to the HOA that typically maintains the Property and collects assessments or dues from each unit owner.

A Condominium Project must be FHA approved before a Mortgage on an individual condominium unit can be insured.

(b) Site Condominiums

Site Condominiums are Single Family detached dwellings encumbered by a declaration of condominium covenants or condominium form of ownership and do not need to be FHA-approved.

Manufactured Housing condominium units may not be processed as Site Condominiums.

(5) Manufactured Housing

(a) Definition

Manufactured Housing is a Structure that is transportable in one or more sections. It may be part of a Condominium Project, provided the project meets applicable FHA requirements.

(b) Standard

To be eligible for FHA mortgage insurance as a Single Family Title II Mortgage, all Manufactured Housing must:

- be designed as a one-family dwelling;
- have a floor area of not less than 400 square feet;
- have the HUD Certification Label affixed or have obtained a letter of label verification issued on behalf of HUD, evidencing the house was constructed on or after June 15, 1976, in compliance with the Federal Manufactured Home Construction and Safety Standards;
- be classified as real estate (but need not be treated as real estate for purposes of state taxation);
- be built and remain on a permanent chassis;
- be designed to be used as a dwelling with a permanent foundation built in accordance with the Permanent Foundations Guide for Manufactured Housing (PFGMH); and
- have been directly transported from the manufacturer or the dealership to the site.

(c) Required Documentation

(i) HUD Certification Label

If the appraisal indicates the HUD Certification Label is missing from the Manufactured Housing unit, the Mortgagee must obtain label verification from the Institute for Building Technology and Safety (IBTS).

(ii) PFGMH Certification

The Mortgagee must obtain a certification by an engineer or architect, who is licensed/registered in the state where the Manufactured Home is located, attesting to compliance with the PFGMH.

The Mortgagee may obtain a copy of the foundation certification from a previous FHA-insured Mortgage, showing that the foundation met the guidelines published in the PFGMH that were in effect at the time of certification, provided there are no alterations and/or observable damage to the foundation since the original certification.

If the Appraiser notes additions or alterations to the Manufactured Housing unit, the Mortgagee must ensure the addition was addressed in the foundation certification.

If the additions or alterations were not addressed in the foundation certification, the Mortgagee must obtain:

- an inspection by the state administrative agency that inspects Manufactured Housing for compliance; or
- certification of the structural integrity from a licensed structural engineer if the state does not employ inspectors.

(C) Property Valuation

The Mortgagee is responsible for obtaining an appraisal to verify the value of the Property and the Property's compliance with HUD's Minimum Property Standards (MPS).

(1) Integrity of Valuation Process: Communications with Mortgagees

The Mortgagee must ensure the integrity of the valuation process by ensuring the valuation process is free from conflicts of interest and the appearance of conflicts of interest.

(a) Standard

The Mortgagee must prevent its staff, or any person who is compensated on a commission basis upon the successful completion of a Mortgage, or who reports, ultimately, to any officer of the Mortgagee not independent of the mortgage production staff and process, from having substantive communications with an Appraiser relating to or having an impact on valuation, including ordering or managing an appraisal assignment. Normal communications necessary to processing of a case is permissible, but cannot attempt to influence the Appraiser.

The underwriter who has responsibility for the quality of the appraisal report is allowed to request clarifications and discuss with the Appraiser components of the appraisal that influence its quality.

(b) Exception for Smaller Mortgagees

When absolute lines of independence cannot be achieved because of the Mortgagee's small size and limited staff, the Mortgagee must clearly demonstrate that it has prudent safeguards to isolate its collateral evaluation process from influence or interference from its mortgage production process.

(2) Communications with Third Parties

The underwriter may request a clarification or reconsideration of value from the Appraiser, following the requirements in Reconsideration of Value. The Mortgagee may not discuss the contents of an appraisal with anyone other than the Borrower.

(3) Verifying HUD's Minimum Property Standards/Minimum Property Requirements

As the on-site representative for the Mortgagee, the Appraiser provides preliminary verification that a Property meets the Property Acceptability Criteria, which include HUD's Minimum Property Requirements (MPR) or Minimum Property Standards (MPS).

When examination of a Property reveals noncompliance with the Property Acceptability Criteria, the Appraiser must note all repairs necessary to make the Property comply with HUD's Property Acceptability Criteria, together with the estimated cost to cure.

v. Legal Restrictions on Conveyance (Free Assumability)

The Mortgagee must determine if there are any legal restrictions on conveyance in accordance with 24 CFR § 203.41.

A Property that contains leased equipment, or operates with a leased energy system or Power Purchase Agreement (PPA), may be eligible for FHA-insured financing but only when such agreements are free of restrictions that prevent the Borrower from freely transferring the Property.

Such agreements are acceptable, provided they do not cause a conveyance (ownership transfer) of the insured Property by the Borrower to:

- be void, or voidable by a third party;
- be the basis of contractual liability of the Borrower (including rights of first refusal, pre-emptive rights or options related to a Borrower's efforts to convey);
- terminate or be subject to termination all or part of the interest held by the Borrower;
- be subject to the consent of a third party;
- be subject to limits on the amount of sales proceeds a Borrower can retain (e.g., due to a lien, "due on sale" clause, etc.);
- be grounds for accelerating the insured Mortgage; or
- be grounds for increasing the interest rate of the insured Mortgage.

Any restrictions resulting from provisions of the lease or PPA do not conflict with FHA regulations unless they include provisions encumbering the Real Property or restricting the transfer of the Real Property.

Legal restrictions on conveyance of Real Property (i.e., the house) that could require the consent of a third party (e.g., energy provider, system owner, etc.), include but are not limited to, credit approval of a new purchaser before the seller can convey the Real Property, unless such provisions may be terminated at the option of, and with no cost to, the owner.

If an agreement for an energy system lease or PPA could cause restriction upon transfer of the house, the Property is subject to impermissible legal restrictions and is generally ineligible for FHA insurance.

2. Allowable Mortgage Parameters

This section provides the basic underwriting standards for Single Family (one to four units) Mortgages insured under the National Housing Act. When underwriting a Mortgage, the Mortgagee must determine the Borrower's creditworthiness, capacity to repay, and available capital to support the Mortgage. The Mortgagee must also examine the Property to ensure it provides sufficient collateral for the Mortgage.

For each Mortgage the Federal Housing Administration (FHA) insures, the Mortgagee must fully comply with the following underwriting procedures.

a. Maximum Mortgage Amounts

A Mortgage that is to be insured by FHA cannot exceed the Nationwide Mortgage Limits, the nationwide area mortgage limit, or the maximum Loan-to-Value (LTV) ratio. The maximum LTV ratios vary depending upon the type of Borrower, type of transaction (purchase or refinance), program type, and stage of construction.

Under most programs, the maximum Mortgage is the lesser of the Nationwide Mortgage Limit for the area, or a percentage of the Adjusted Value.

For purchase transactions, the Adjusted Value is the lesser of:

- purchase price less any inducements to purchase; or
- the Property Value.

For refinance transactions:

- For Properties acquired by the Borrower within 12 months of the case number assignment date, the Adjusted Value is the lesser of:
  - the Borrower's purchase price, plus any documented improvements made subsequent to the purchase; or
  - the Property Value.
- Properties acquired by the Borrower within 12 months of case number assignment by inheritance or through a gift from a Family Member may utilize the calculation of Adjusted Value for properties purchased 12 months or greater.
- For properties acquired by the Borrower greater than or equal to 12 months prior to the case number assignment date, the Adjusted Value is the Property Value.

i. National Housing Act's Statutory Limits

The National Housing Act establishes the maximum Mortgage limits and the mortgage amounts for all FHA mortgage insurance programs.

ii. Nationwide Mortgage Limits

Mortgage limits are calculated based on the median house prices in accordance with the statute. FHA's Single Family mortgage limits are set by Metropolitan Statistical Area and county and will be published periodically. FHA's Single Family mortgage limits are available by MSA and county, or by downloading a complete listing. FHA publishes updated limits effective for each calendar year.

These limits will be set at or between the low cost area and high cost area limits based on the median house prices for the area.

(A) Requests for Local Increases

Any requests to change high-cost area Mortgage limits determined by HUD must be received by FHA's Santa Ana Homeownership Center (HOC) at the address below no later than 30 Days from the publication of the limits each year. Any changes in area Mortgage limits as a result of valid appeals will be retroactively in effect for case numbers assigned on or after January 1 of each year.

Each request to change Mortgage limits must contain sufficient housing sales price data, listing one-family Properties sold in an area within the look-back period, January through August of the previous year. Requests should differentiate between Single Family residential Properties, and condominiums or cooperative housing units. Ideally, data provided should also distinguish between distressed and non-distressed sales. Requests for a change will only be considered for counties for which HUD does not already have home sales transaction data for the calculation of Mortgage limits.

All requests for local area increases in all areas will be handled exclusively by FHA's Santa Ana HOC:

Attn: Program Support/Loan Limits
U.S. Department of Housing and Urban Development
Santa Ana Homeownership Center
Santa Ana Federal Building
34 Civic Center Plaza, Room 7015
Santa Ana, CA 92701-4003

(B) Low Cost Area

The FHA national low cost area mortgage limits, which are set at 65 percent of the national conforming limit of $424,100 for a one-unit Property, are, by property unit number, as follows:

- One-unit: $275,665
- Two-unit: $352,950
- Three-unit: $426,625
- Four-unit: $530,150

(C) High Cost Area

The FHA national high cost area mortgage limits, which are set at 150 percent of the national conforming limit of $424,100 for a one-unit Property, are, by property unit number, as follows:

- One-unit: $636,150
- Two-unit: $814,500
- Three-unit: $984,525
- Four-unit: $1,223,475

(D) Special Exceptions for Alaska, Hawaii, Guam, and the Virgin Islands

FHA adjusts mortgage limit ceilings for the special exception areas of Alaska (AK), Hawaii (HI), Guam (GU) and the Virgin Islands (VI) to account for higher costs of construction. These Special Exception Area limit ceilings are set at 150 percent of FHA's High Cost Area mortgage limits, rounded down to the nearest $25. These four special exception areas have a higher ceiling as follows:

- One-unit: $954,225
- Two-unit: $1,221,750
- Three-unit: $1,476,775
- Four-unit: $1,835,200

iii. Financing of Upfront Mortgage Insurance Premium

Unless otherwise stated in this section (Origination through Post-Closing/Endorsement), restrictions to mortgage amounts and LTVs are based upon the amount prior to the financing of the Upfront Mortgage Insurance Premium (UFMIP) (Base Loan Amount). The total mortgage amount may be increased by the financed UFMIP amount.

iv. Calculating Maximum Mortgage Amounts on Purchases

The maximum mortgage amount that FHA will insure on a specific purchase is calculated by multiplying the appropriate LTV percentage by the Adjusted Value.

In order for FHA to insure this maximum mortgage amount, the Borrower must make a Minimum Required Investment (MRI) of at least 3.5 percent of the Adjusted Value.

v. Additions to the Mortgage Amount for Repair and Improvement

(A) Appraiser Required Repairs

A Mortgagee may add repair costs to the sales price before calculating the mortgage amount if:

- the repairs are required by the Appraiser to meet HUD's MPR;
- the repairs are paid for by the Borrower; and

- the sales contract or addendum identifies the Borrower as the party responsible for payment and completion of the repairs.

The maximum amount of repair costs that may be added to the sales price is the lesser of:

- the amount by which the value of the Property exceeds the sales price;
- the Appraiser's estimate of repairs; or
- the amount of the contractor's bid.

(B) Energy-Related Weatherization Repairs and Improvements

A Mortgagee may add energy-related weatherization costs, to be paid for by the Borrower, in accordance with Weatherization policies.

(C) Solar Energy Systems

A Mortgagee may add the cost of a solar energy system (including active and passive solar- and wind-driven systems) to the Mortgage in accordance with Solar and Wind Technologies policies.

When adding the cost of a solar energy system to the mortgage amount, the maximum insurable mortgage limit may be exceeded by up to 20 percent.

b. Loan-to-Value Limits

The determination of the maximum LTV percentage available is influenced by:

- the particular mortgage insurance program (See Programs and Products); and
- the transaction type.

The Mortgagee must apply the lowest applicable LTV percentage as determined under the requirements in this section.

i. LTV Limitations Based on Borrower's Credit Score (Applies to All Transactions)

The Mortgagee must review the credit report to determine the Borrower's Minimum Decision Credit Score (MDCS), except for Mortgages to be insured under Section 247, Section 248, Streamline Refinances, and Assumptions.

The MDCS will be used to determine the maximum insured financing available to a Borrower with traditional credit.

The table below describes the relationship between the Borrower's MDCS and the LTV ratio for which they are eligible. Borrowers with non-traditional or insufficient credit histories are eligible for maximum financing, but must be underwritten using the procedures in Manual Underwriting.

If the Borrower's Minimum Decision Credit Score is...	Then the Borrower is...
at or above 580	eligible for maximum financing.
between 500 and 579	limited to a maximum LTV of 90%.

ii. Purchase

For purchase transactions, the maximum LTV is 96.5 percent of the Adjusted Value.

For special programs and products including refinances, the maximum LTV is determined in accordance with requirements listed in this *SF Handbook's* Programs and Products section.

(A) LTV Limitations Based on Identities of Interest

(1) Definitions

An Identity-of-Interest Transaction is a sale between parties with an existing Business Relationship or between Family Members.

Business Relationship refers to an association between individuals or companies entered into for commercial purposes.

(2) Maximum LTV for Identity-of-Interest and Tenant/Landlord Transactions

The maximum LTV percentage for Identity-of-Interest transactions on Principal Residences is restricted to 85 percent.

The maximum LTV percentage for a transaction where a tenant-landlord relationship exists at the time of contract execution is restricted to 85 percent.

(3) Exceptions to the Maximum LTV

The 85 percent maximum LTV restriction does not apply for Identity-of-Interest transactions under the following circumstances.

(a) Family Member Transactions

The 85 percent LTV restriction may be exceeded if a Borrower purchases as their Principal Residence:

- the Principal Residence of another Family Member; or
- a Property owned by another Family Member in which the Borrower has been a tenant for at least six months immediately predating the sales contract. A lease or other written evidence to verify occupancy is required.

(b) Builder's Employee Purchase

The 85 percent LTV restriction may be exceeded if an employee of a builder, who is not a Family Member, purchases one of the builder's new houses or models as a Principal Residence.

(c) Corporate Transfer

The 85 percent LTV restriction may be exceeded if a corporation transfers an employee to another location, purchases the employee's house, and sells the house to another employee.

(d) Tenant Purchase

The 85 percent LTV restriction may be exceeded if the current tenant purchases the Property where the tenant has rented the Property for at least six months immediately predating the sales contract.

A lease or other written evidence to verify occupancy is required.

(B) LTV Limitations Based on Non-Occupying Borrower Status

(1) Definition

A Non-Occupying Borrower Transaction refers to a transaction involving two or more Borrowers in which one or more of the Borrower(s) will not occupy the Property as their Principal Residence.

(2) Maximum LTV for Non-Occupying Borrower Transaction

For Non-Occupying Borrower Transactions, the maximum LTV is 75 percent. The LTV can be increased to a maximum of 96.5 percent if the Borrowers are Family Members, provided the transaction does not involve:

- a Family Member selling to a Family Member who will be a non-occupying co-Borrower; or
- a transaction on a two- to four-unit Property.

iii. Refinance

For refinance transactions, the maximum LTV is determined in accordance with Refinance program specific requirements.

iv. New Construction

For New Construction transactions, the maximum LTV is determined in accordance with New Construction program specific requirements.

c. Required Investment

i. Total Required Investment

Total Required Investment refers to the amount the Borrower must contribute to the transaction including the Borrower's downpayment and the Borrower-paid transaction costs. The Total Required Investment includes the Minimum Required Investment (MRI).

ii. Minimum Required Investment

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.

d. Maximum Mortgage Term

The maximum mortgage term may not exceed 30 years from the date that amortization begins. FHA does not require that mortgage terms be in five year multiples.

e. Mortgage Insurance Premiums

FHA collects a one-time Upfront Mortgage Insurance Premium (UFMIP) and an annual insurance premium, also referred to as the periodic or monthly MIP, which is collected in monthly installments.

i. Upfront Mortgage Insurance Premium

(A) Upfront Mortgage Insurance Premium Amount

Most FHA mortgage insurance programs require the payment of UFMIP, which may be financed into the Mortgage. The UFMIP is not considered when calculating the area-based Nationwide Mortgage Limits and LTV limits.

The UFMIP charged for all amortization terms is 175 Basis Points (bps), unless otherwise stated in the applicable Programs and Products or in the MIP chart.

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

The mortgage amount must be rounded down to the nearest whole dollar amount, regardless of whether the UFMIP is financed or paid in cash.

(B) Refund and Credit of Upfront Mortgage Insurance Premium

The UFMIP is not refundable, except in connection with the refinancing to a new FHA-insured Mortgage. See the Refinances Section.

ii. Annual (or Periodic) Mortgage Insurance Premium

The periodic MIP is an annual MIP that is payable monthly. The amount of the annual MIP is based on the LTV ratio, Base Loan Amount and the term of the Mortgage.

Calculation of the MIP

The MIP rate and duration of the MIP assessment period vary by mortgage term, Base Loan Amount, and LTV ratio for the Mortgage, as shown in the MIP chart.

3. Underwriting the Property

The Mortgagee must underwrite the completed appraisal report to determine if the Property provides sufficient collateral for the FHA-insured Mortgage. The appraisal and Property must comply with the requirements in Appraiser and Property Requirements for Title II Forward and Reverse Mortgages. The appraisal must be reported in accordance with Acceptable Appraisal Reporting Forms and Protocols.

a. Property Acceptability Criteria

The Mortgagee must evaluate the appraisal and any supporting documentation to determine if the Property complies with HUD's Property Acceptability Criteria. Existing and New Construction Properties must comply with Application of Minimum Property Requirements and Minimum Property Standards by Construction Status.

i. Defective Conditions

The Mortgagee must evaluate the appraisal in accordance with Defective Conditions to determine if the Property is eligible for an FHA-insured Mortgage. If defective conditions exist and correction is not feasible, the Mortgagee must reject the Property.

ii. Minimum Property Requirements and Minimum Property Standards

As the on-site representative for the Mortgagee, the Appraiser provides preliminary verification that a Property meets the Property Acceptability Criteria, which includes HUD's Minimum Property Requirements (MPR) and Minimum Property Standards (MPS).

Minimum Property Requirements refer to general requirements that all homes insured by FHA be safe, sound, and secure.

Minimum Property Standards refer to regulatory requirements relating to the safety, soundness and security of New Construction.

When examination of a Property reveals noncompliance with the Property Acceptability Criteria, the Appraiser must note all repairs necessary to make the Property comply with HUD's Property Acceptability Criteria, together with the estimated cost to cure. If the Appraiser cannot determine that a Property meets HUD's MPR or MPS, the Mortgagee may obtain an inspection from a qualified Entity to make the determination. Mortgagees must use professional judgment in determining when inspections are necessary to determine that a property meets MPR or MPS. Mortgagees must also use professional judgment in determining when a Property condition poses a threat to the health and safety of the occupant and/or jeopardizes the soundness and structural integrity of the Property, such that additional inspections and/or repairs are necessary.

The Mortgagee must confirm that the Property complies with the following eligibility criteria. If the Mortgage is to be insured under the 203(k) program, the Mortgagee must confirm that the Property will comply with the following eligibility criteria upon completion of repairs and improvements.

(A) Encroachment

The Mortgagee must ensure the subject's dwelling, garage, or other improvements do not encroach onto an adjacent Property, right-of-way, utility Easement, or building restriction line. The Mortgagee must also ensure a neighboring dwelling, garage, or other improvements do not encroach onto the subject Property. Encroachment by the subject or adjacent Property fences is acceptable provided such Encroachment does not affect the marketability of the subject Property.

(B) Overhead Electric Power

The Mortgagee must confirm that any Overhead Electric Power Transmission Lines do not pass directly over any dwelling, Structure or related property improvement, including pools. The power line must be relocated for a Property to be eligible for FHA-insured financing.

The residential service drop line may not pass directly over any pool, spa or water feature.

If the dwelling or related property improvements are located within the Easement area, the Mortgagee must obtain a certification from the appropriate utility company or local regulatory agency stating that the relationship between the improvements and Local Distribution Lines conforms to local standards and is safe.

(C) Access to Property

The Mortgagee must confirm that the Property is provided with a safe pedestrian access and Adequate Vehicular Access from a public or private street. Streets must either be dedicated to public use and maintenance, or retained as private streets protected by permanent recorded Easements.

Private streets, including shared driveways, must be protected by permanent recorded Easements, ownership interest, or be owned and maintained by an HOA. Shared driveways do not require a joint maintenance agreement.

(D) Onsite Hazards and Nuisances

The Mortgagee must require corrective work to mitigate potential adverse effects from any onsite hazards or nuisances reported by the Appraiser.

(E) Abandoned Gas and Oil Well

If the Property contains any abandoned gas or oil wells, the Mortgagee must obtain a letter from the local jurisdiction or appropriate state agency stating that the subject well was permanently abandoned in a safe manner.

If the Property contains any abandoned petroleum product wells, the Mortgagee must ensure that a qualified petroleum engineer has inspected the Property and assessed the risk, and that the appropriate state authorities have concurred on clearance recommendations.

(F) Requirements for Living Unit

The Mortgagee must confirm that each living unit contains:

- a continuing and sufficient supply of safe and potable water under adequate pressure and of appropriate quality for all household uses;
- sanitary facilities and a safe method of sewage disposal. Every living unit must have at least one bathroom, which must include, at a minimum, a water closet, lavatory, and a bathtub or shower;
- adequate space for healthful and comfortable living conditions;
- heating adequate for healthful and comfortable living conditions;
- domestic hot water; and
- electricity adequate for lighting, cooking and for mechanical equipment used in the living unit.

The Mortgagee must ensure that appliances that are to remain and that contribute to the market value opinion are operational.

FHA does not have a minimum size requirement for one- to four-family dwellings and condominium units. For Manufactured Housing requirements, see the Manufactured Housing section.

(G)Swimming Pools

The Mortgagee must confirm that any swimming pools comply with all local ordinances.

(H)Structural Conditions

The Mortgagee must confirm that the Structure of the Property will be serviceable for the life of the Mortgage.

The Mortgagee must confirm that all foundations will be serviceable for the life of the Mortgage and adequate to withstand all normal loads imposed.

(I) Economic Life/Section 223(e)

The Mortgagee must confirm that the term of the Mortgage is less than or equal to the remaining economic life of the Property.

If the Property is located in an older, declining urban area and the remaining economic life produces an unreasonably short mortgage term by reason of its location, the Property may be acceptable under Section 223(e), provided:

- the area is reasonably able to support adequate housing and living conditions for families of lower income levels;
- the location features adversely affecting the desirability and usefulness of the Property do not endanger the health and safety of its occupants;
- the Property is marketable to the typical occupant of the area;
- the physical life of the Property is greater than or equal to the term of the Mortgage; and
- the Mortgage represents an overall acceptable risk as determined by the Jurisdictional HOC.

All Mortgages to be insured under Section 223(e) must be submitted to the Jurisdictional HOC for prior approval.

(J) Environmental

The Mortgagee must confirm that the Property is free of all known environmental and safety hazards and adverse conditions that may affect the health and safety of the occupants, the Property's ability to serve as collateral, and the structural soundness of the improvements.

(K) Lead-Based Paint

The Mortgagee must confirm that the Property is free of lead paint hazards.

(L) Methamphetamine Contamination

If the Mortgagee or the Appraiser identifies a Property as contaminated by the presence of methamphetamine (meth), either by its manufacture or by consumption, the Property is ineligible due to this environmental hazard until the Property is certified safe for habitation.

(M) Repair Requirements

The Mortgagee must determine which repairs must be made for an existing Property to be eligible for FHA-insured financing.

(N) Utility Services

If utilities are not located on Easements that have been permanently dedicated to the local government or appropriate public utility body, the Mortgagee must confirm that this information is recorded on the deed record.

(O) Water Supply Systems

(1) Public Water Supply System

The Mortgagee must confirm that a connection is made to a public or Community Water System whenever feasible and available at a reasonable cost. If connection costs to the public or community system are not reasonable, the existing onsite systems are acceptable, provided they are functioning properly and meet the requirements of the local health department.

(2) Individual Water Supply Systems (Wells)

When an Individual Water Supply System is present, the Mortgagee must ensure that the water quality meets the requirements of the health authority with jurisdiction.

If there are no local (or state) water quality standards, then water quality must meet the standards set by the EPA, as presented in the National Primary Drinking Water regulations in 40 CFR §§ 141 and 142.

Soil poisoning is an unacceptable method for treating termites unless the Mortgagee obtains satisfactory assurance that the treatment will not endanger the quality of the water supply.

Requirements for the location of wells for FHA-insured Properties are located in 24 CFR § 200.926d (f) (3).

The following tables provide the minimum distance required between wells and sources of pollution for Existing Construction:

	Individual Water Supply System for Minimum Property Requirements for Existing Construction*
1	Property line/10 feet
2	Septic tank/50 feet
3	Drain field/100 feet
4	Septic tank drain field reduced to 75 feet if allowed by local authority
5	If the subject Property line is adjacent to residential Property then local well distance requirements prevail. If the subject Property is adjacent to non-residential Property or roadway, there needs to be a separation distance of at least 10 feet from the property line.
* distance requirements of local authority prevail if greater than stated above	

The following provides the minimum requirements for water wells:

	Water Wells Minimum Property Standards for New Construction 24 CFR § 200.926d(f)(1)
1	Lead-free piping
2	If no local chemical and bacteriological water standards, state standards apply
3	Connection of public water whenever feasible
4	Wells must deliver water flow of five gallons per minute over at least a four-hour period

	Water Wells Minimum Property Requirements for Existing Construction
1	Existing wells must deliver water flow of three to five gallons per minute
2	No exposure to environmental contamination
3	Continuing supply of safe and potable water
4	Domestic hot water
5	Water quality must meet requirements of local jurisdiction or the EPA if no local standard

(3) Shared Wells

The Mortgagee must confirm that a Shared Well:

- serves existing Properties that cannot feasibly be connected to an acceptable public or Community Water supply System;
- is capable of providing a continuous supply of water to involved Dwelling Units so that each existing Property simultaneously will be assured of at least three gallons per minute (five gallons per minute for Proposed Construction) over a continuous four-hour period. (The well itself may have a lesser yield if pressurized storage is provided in an amount that will make 720 gallons of water available to each connected existing dwelling during a continuous four-hour period or 1,200 gallons of water available to each proposed dwelling during a continuous four-hour period. The shared well system yield must be demonstrated by a certified pumping test or other means acceptable to all agreeing parties.);
- provides safe and potable water. An inspection is required under the same circumstances as an individual well. This may be evidenced by a letter from the health authority having jurisdiction or, in the absence of local health department standards, by a certified water quality analysis demonstrating that the well water complies with the EPA's National Interim Primary Drinking Water Regulations;

- has a valve on each dwelling service line as it leaves the well so that water may be shut off to each served dwelling without interrupting service to the other Properties; and
- serves no more than four living units or Properties.

For both proposed and existing Properties, the Mortgagee must ensure that the shared well agreement complies with the guidance provided in the following table.

Item	Provisions that must be reflected in any acceptable shared well agreement include the following:
1	Require that the agreement is binding upon signatory parties and their successors in title, recorded in local deed records when executed and recorded, and reflects joiner by any Mortgagee holding a Mortgage on any Property connected to the Shared Well.
2	Permit well water sampling and testing by the local authority at the request of any party at any time.
3	Require that corrective measures be implemented if testing reveals a significant water quality deficiency, but only with the consent of a majority of all parties.
4	Ensure continuity of water service to “supplied” parties if the “supplying” party has no further need for the shared well system. (“Supplied” parties normally should assume all costs for their continuing water supply.)
5	Prohibit well water usage by any party for other than bona fide domestic purposes.
6	Prohibit connection of any additional living unit to the shared well system without: • the consent of all parties; • the appropriate amendment of the agreement; and • compliance with item 3.
7	Prohibit any party from locating or relocating any element of an individual sewage disposal system within 75 feet (100 feet for Proposed Construction) of the Shared Well.
8	Establish Easements for all elements of the system, ensuring access and necessary working space for system operation, maintenance, improvement, inspection and testing.
9	Specify that no party may install landscaping or improvements that will impair use of the Easements.
10	Specify that any removal and replacement of preexisting site improvements, necessary for system operation, maintenance, replacement, improvement, inspection or testing, will be at the cost of their owner, except for costs to remove and replace common boundary fencing or walls, which must be shared equally between or among parties.

Item	Provisions that must be reflected in any acceptable shared well agreement include the following:
11	Establish the right of any party to act to correct an emergency in the absence of the other parties onsite. An emergency must be defined as failure of any shared portion of the system to deliver water upon demand.
12	Permit an agreement amendment to ensure equitable readjustment of shared costs when there may be significant changes in well pump energy rates or the occupancy or use of an involved Property.
13	Require the consent of a majority of all parties upon cost sharing, except in emergencies, before actions are taken for system maintenance, replacement or improvement.
14	Require that any necessary replacement or improvement of a system element(s) will at least restore original system performance.
15	Specify required cost sharing for: • the energy supply for the well pump; • system maintenance, including repairs, testing, inspection and disinfection; • system component replacement due to wear, obsolescence, incrustation or corrosion; and • system improvement to increase the service life of a material or component to restore well yield or to provide necessary system protection.
16	Specify that no party is responsible for unilaterally incurred shared well debts of another party, except for correction of emergency situations. Emergency correction costs must be equally shared.
17	Require that each party be responsible for: • prompt repair of any detected leak in this water service line or plumbing system; • repair costs to correct system damage caused by a resident or guest at their Property; and • necessary repair or replacement of the service line connecting the system to the dwelling.
18	Require equal sharing of repair costs for system damage caused by persons other than a resident or guest at a Property sharing the well.
19	Ensure equal sharing of costs for abandoning all or part of the shared system so that contamination of ground water or other hazards will be avoided.
20	Ensure prompt collection from all parties and prompt payment of system operation, maintenance, replacement or improvement costs.
21	Specify that the recorded agreement may not be amended during the term of a federally-insured or -guaranteed Mortgage on any Property served, except as provided in items 5 and 11 above.

Item	Provisions that must be reflected in any acceptable shared well agreement include the following:
22	Provide for binding arbitration of any dispute or impasse between parties with regard to the system or terms of agreement. Binding arbitration must be through the American Arbitration Association or a similar body and may be initiated at any time by any party to the agreement. Parties to the agreement must equally share arbitration costs.

(P) Individual Residential Water Purification Systems

(1) Definition

An Individual Residential Water Purification System refers to equipment, either point-of-entry or point-of-use, installed on Properties that otherwise do not have access to a continuous supply of safe and potable water.

(2) Standard

If a Property does not have access to a continuous supply of safe and potable water without the use of a water purification system, the Mortgagee must ensure that the Property has an individual residential water purification system as well as a service contract for the ongoing maintenance of the Property, a plan approved by the local or state health authority, and an escrow account.

(a) Approved Equipment for Individual Residential Water Purification Systems

Water purification equipment must be approved by a nationally recognized testing laboratory acceptable to the local or state health authority. The Mortgagee must obtain a certification from a local or state health authority which certifies that:

- A point-of-entry or point-of-use water purification system is on the Property. If the system employs point-of use equipment, the purification system must be employed on each water supply source (faucet) serving the Property. Where point-of-entry systems are used, separate water supply systems carrying untreated water for flushing toilets may be constructed.
- The system is sufficient to ensure an uninterrupted supply of safe and potable water adequate to meet household needs.
- The water supply, when treated by the equipment, meets the requirements of the local or state health authority, and has been determined to meet local or state quality standards for drinking water. If neither state nor local standards are applicable, then quality must be determined in accordance with standards set by the Environmental

Protection Agency (EPA) pursuant to the Safe Drinking Water Act in 40 CFR Parts 141 and 142.

- A plan exists that provides for the monitoring, servicing, maintenance, and replacement of the water equipment, and the plan meets the service contract requirements.

(b) Borrower Notice of Water Purification System

The Mortgagee must provide written notification to the Borrower that the Property has a hazardous water supply that requires treatment in order to remain safe and acceptable for human consumption. The notification to the Borrower must identify specific contaminants in the water supply serving the Property, and the related health hazard arising from the presence of those contaminants.

The Mortgagee must ensure that the Borrower has received a written estimate of the maintenance and replacement costs of the equipment necessary to ensure continuous safe drinking water.

(c) Service Contract for Individual Residential Water Purification Systems

Before mortgage closing, the Mortgagee must ensure that the Borrower has entered into a service contract with an organization or individual specifically approved by the local or state health authority to carry out the provisions of the required plan for the servicing, maintenance, repair, and replacement of the water purification equipment.

(d) Approved Plan for Individual Residential Water Purification Systems

An approved plan is a contract entered into by the Borrower and Mortgagee and approved by the local or state health authority, and that sets out conditions as described below that must be met by the parties as a condition to insurance of the Mortgage by HUD.

The plan must set forth the respective responsibilities to be assumed by the Borrower and the Mortgagee, as well as the other entities who will implement the plan, such as the health authority and the service contractor. In particular:

- The plan must set out the responsibilities of the health authority for monitoring and enforcing the performance of the service contractor, including any successor contractor that the health authority may later have occasion to name. By its approval of the plan, the health authority documents its acceptance of these responsibilities, and the plan should so indicate.
- The plan must provide for the monitoring of the operation of the water purification equipment, as well as for servicing (including

disinfecting) and repairing and replacing the system as frequently as necessary, taking into consideration the system's design, anticipated use, and the type and level of contaminants present. Installation, servicing, repair, and replacement of the water purification system must be performed by an individual or organization approved for this purpose by the local or state health authority and identified in the plan. The plan must refer to specific terms and conditions of the required service contract.

- Under the plan, responsibility for monitoring the performance of the service contractor and for ensuring that the water purification system is properly serviced, repaired, and replaced rests with the local or state health authority that approved the plan. The plan must confer on the health authority all powers necessary to effect compliance by the service contractor. The health authority's powers must include the authority to notify the Borrower of any noncompliance by the service contractor. The plan must provide that upon any notification of noncompliance received from the health authority, the Borrower may discharge the service contractor for cause and appoint a successor organization or individual as service contractor.
- The Mortgagee must ensure that any plan developed in accordance with this section must provide that an analysis of the water supply must be obtained from the local or state health authority no less frequently than annually, but more frequently if determined at any time to be necessary by the health authority or by the service contractor.

The plan must provide that if the dwelling served by the water purification system is refinanced, or is sold or otherwise transferred with a HUD-insured Mortgage, the plan will:

- continue in full force and effect;
- impose an obligation on the Borrower to notify any subsequent purchaser or transferee of the necessity for the water purification system and for its proper maintenance, and of the obligation to make escrow payments; and
- require the Borrower to furnish the purchaser with a copy of the plan before any sales contract is signed.

(e) Escrow for Maintenance and Replacement of Individual Residential Water Purification Systems

The Mortgagee must establish and maintain an escrow account to ensure proper servicing, maintenance, repair, and replacement of the water purification equipment. To the extent permitted under RESPA, the amount to be collected and escrowed by the Mortgagee must be based upon information provided by the manufacturer for the maintenance and replacement of the water purification equipment and for other charges anticipated by the service contractor. The initial monthly escrow amount must be stated in the plan. Disbursements from the account will be limited to costs associated with the normal servicing, maintenance, repair, or replacement of the water purification equipment. Disbursements may only be made to the service contractor or its successor, to equipment suppliers, to the local or state health authority for the performance of testing or other required services, or to another entity approved by the health authority. The Mortgagee must maintain the escrow account as long as water purification remains necessary and the Mortgage is insured by HUD.

The Mortgagee must provide the Borrower with the Water Purification Equipment Rider for signature.

(3) Required Documentation

(a) Borrower Notice of Water Purification System

A copy of the notification statement (including cost estimates), dated before the date of the sales contract and signed by the prospective Borrower to acknowledge its receipt, must accompany the submission for insurance endorsement. If a sales contract is signed in advance of the disclosure required by this paragraph, an addendum must be executed after the information is provided to the prospective Borrower and after they have acknowledged receipt of the disclosure.

(b) Borrower's Certification of Water Purification System

At the time the application is signed, the Borrower must sign a certification acknowledging that the Property has a water purification system that must be maintained.

(c) Approved Plan for Individual Residential Water Purification Systems

The Mortgagee must ensure a copy of the approved plan is provided to HUD.

(d) Service Contract for Individual Residential Water Purification Systems

The Mortgagee must ensure a copy of the service contract signed by the Borrower is provided to HUD.

(e) Water Purification Equipment Rider for Individual Residential Water Purification Systems

The Mortgagee must ensure a copy of the Water Purification Equipment Rider is provided to HUD.

(Q) Sewage System

The Mortgagee must confirm that a connection is made to a public or community sewage disposal system whenever feasible and available at a reasonable cost. If connection costs to the public or community system are not reasonable, the existing Onsite Sewage Disposal Systems are acceptable provided they are functioning properly and meet the requirements of the local health department

When the Onsite Sewage Disposal System is not sufficient and an off-site system is available, the Mortgagee must confirm connection to an off-site sewage system. When the Onsite Sewage Disposal System is not sufficient and an off-site system is not available, the Mortgagee must reject the Property unless the Onsite Sewage Disposal System is repaired or replaced and complies with local health department standards.

(R) Termites

For existing Properties, the Mortgagee must confirm that the Property is free of wood destroying insects and organisms. If the appraisal is made subject to inspection by a qualified pest control specialist, the Mortgagee must obtain such inspection and evidence of any required treatment to confirm the Property is free of wood destroying insects and organisms.

iii. Minimum Required Repairs

When the appraisal report or inspection from a qualified Entity indicates that repairs are required to make the Property meet HUD's MPR or MPS, the Mortgagee must comply with Repair Requirements.

If repairs for Existing Construction cannot be completed prior to closing, the Mortgagee may establish an escrow account in accordance with Repair Completion Escrow Requirements.

iv. Leased Equipment

The Mortgagee must ensure that the Property Value does not include the value of any equipment, including an energy system, that is not fully owned by the Borrower. The Mortgagee must review the terms of the lease on any equipment to ensure they do not contain any Legal Restrictions on Conveyance (Free Assumability).

Appraisal Review

The Mortgagee must review the appraisal and ensure that it is complete, accurate, and provides a credible analysis of the marketability and value of the Property.

v. Quality of Appraisal

The Mortgagee must evaluate the appraisal and ensure it complies with the requirements in Valuation and Reporting Protocols, and any additional appraisal requirements that are specific to the subject Property.

vi. Chain of Title

The Mortgagee must review the appraisal to determine if the subject Property was sold within 12 months prior to the case number assignment date. If the subject Property was sold within the previous 12 months the Mortgagee must review evidence of prior ownership and determine if there are any undisclosed Identity-of-Interest transactions, and for compliance with Restrictions on Property Flipping.

vii. Opinion of Market Value

The Mortgagee must ensure the Market Value of the Property is sufficient to adequately secure the FHA-insured Mortgage.

viii. Reconsideration of Value

The underwriter may request a reconsideration of value when the Appraiser did not consider information that was relevant on the effective date of the appraisal. The underwriter must provide the Appraiser with all relevant data that is necessary for a reconsideration of value.

The Appraiser may charge an additional fee if the relevant data was not available on the effective date of the appraisal. If the unavailability of data is not the fault of the Borrower, the Borrower must not be held responsible for the additional costs. The effective date of the appraisal is the date the Appraiser inspected the Property.

b. Required Documentation for Underwriting the Property

If additional inspections, repairs or certifications are noted by the appraisal or are required to demonstrate compliance with Property Acceptability Criteria, the Mortgagee must obtain evidence of completion of such inspections, repairs or certifications.

c. Conditional Commitment Direct Endorsement Statement of Appraised Value

The Conditional Commitment Direct Endorsement Statement of Appraised Value (form HUD-92800.5B) provides the terms upon which the commitment/direct endorsement statement of appraised value is made and the specific conditions that must be met before HUD can endorse a Firm Commitment for mortgage insurance. The underwriter must complete form HUD-92800.5B as directed in the form instructions.

Where a Statement of Appraised Value is required, the Mortgagee must provide the Borrower with a copy of the completed form HUD-92800.5B.

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

a. Underwriting with an Automated Underwriting System

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 and assumptions.

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, including any assessments related to a PACE obligation;
- payments for any acceptable secondary financing; and
- any other escrow payments.

The Mortgagee may deduct the amount of the Mortgage Credit Certificate or Section 8 Homeownership Voucher if it is paid directly to the Servicer. 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.

(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;
- the Borrower has undisclosed mortgage debt 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)

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 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 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.

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.

(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.

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;
- re-submit 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) 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.

(2) 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.

A Mortgage Payment is considered delinquent if not paid within the month due.

(2) 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 most recent 12 months 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; or
- one payment greater than 90 Days late.

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.

(3) 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; or
- any delinquency within 12 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 housing payments.

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, *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 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;
- re-submit 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 a verification of Mortgage directly from the Servicer.

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 1 percent of the outstanding balance reported on the Borrower's credit report; and
- 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.

(4) Calculation of Monthly Obligation

Regardless of the payment status, the Mortgagee must use either:

- the greater of:
  - 1 percent of the outstanding balance on the loan; or
  - the monthly payment reported on the Borrower's credit report; or
- the actual documented payment, provided the payment will fully amortize the loan over its term.

(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 obtain a copy of the loan agreement or payment statement documenting the amount of the monthly payment. If the credit report, loan agreement or payment statement shows a deferred payment arrangement for an Installment Loan, refer to the Deferred Obligations section.

(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 Cosigner 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.

(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, and does not have a history of delinquent payments on the loan.

(c) Court Ordered Divorce Decree

The Mortgagee must obtain a copy of the divorce decree ordering the spouse 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;
- 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)

Definition of Effective Income (TOTAL)

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

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.

(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 using one of the following methods.

(1) Traditional Current Employment Documentation

The Mortgagee must obtain the most recent pay stub and one of the following to verify current employment:

- a written Verification of Employment (VOE) covering two years; or
- an electronic verification acceptable to FHA.

Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.

(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 W-2 forms 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.

Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.

(3) Past Employment Documentation

Direct verification of the Borrower's employment 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 or Bonus Income).
- The Borrower executes IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-T, *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:

- W-2(s)
- VOE(s)
- electronic verification acceptable to FHA
- evidence supporting enrollment in school or the military during the most recent two full years

iii. Primary Employment (TOTAL)

(A) Definition

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

(B) Standard

The Mortgagee may use primary Employment Income as Effective Income.

(C) Calculation of Effective Income

(1) Salary

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.

(2) Hourly

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.

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.

v. Overtime and Bonus Income (TOTAL)

(A) Definition

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

(B) Standard

The Mortgagee may use Overtime and Bonus 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 and Bonus Income less than two years may be considered Effective Income if the Mortgagee documents that the Overtime and Bonus 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

For employees with Overtime or Bonus Income, the Mortgagee must average the income earned over the previous two years to calculate Effective Income. However, if the Overtime or Bonus Income from the current year decreases by 20 percent or more from the previous year, the Mortgagee must use the current year's income.

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

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.

(2) Hourly

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.

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 Commission Income less than or equal to 25 percent of the Borrower's total earnings, the Mortgagee must use traditional or alternative employment documentation.

For Commission Income greater than 25 percent of the Borrower's total earnings, the Mortgagee must obtain signed tax returns, including all applicable schedules, for the last two years. In lieu of signed tax returns from the Borrower, the Mortgagee may obtain a signed IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-T, *Request for Transcript of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, and tax transcripts directly from the IRS.

(D) Calculation of Effective Income

The Mortgagee must calculate Effective Income for commission by using the lesser of (a) the average net Commission Income earned over the previous two years, or the length of time Commission Income has been earned if less than two years; or (b) the average net Commission Income earned over the previous one year. The Mortgagee must calculate net Commission Income by subtracting the unreimbursed business expenses from the gross Commission Income.

The Mortgagee must reduce the Effective Income by the amount of any unreimbursed employee business expenses, as shown on the Borrower's Schedule A. For information on analyzing the Borrower's 1040, review Analyzing IRS Forms.

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.

(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, *Request for Copy of Tax Return*, IRS Form 4506-T, *Request for Transcript of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, 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 date of most recent calendar or fiscal year-end tax return was filed by the Borrower. 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.

(D) Calculation of Effective Income

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 the previous two years; or
- the average gross Self-Employment Income earned over the previous one year.

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 job 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 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.

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. 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.

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) VA 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 non-custodial 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 six months, 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 Homeownership Vouchers.

(2) Required Documentation

The Mortgagee must verify and document that the Governmental Entity subsidizes the Borrower's Mortgage Payments either through direct payments or tax rebates.

(3) Calculating Effective Income

Mortgage Credit Certificate income that is not used to directly offset the Mortgage Payment before calculating the qualifying ratios may be included as Effective Income. The Mortgagee must use the current subsidy rate to calculate the Effective Income.

(E) Section 8 Homeownership Vouchers (TOTAL)

(1) Definition

Section 8 Homeownership 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 Homeownership 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.

The Mortgagee must also obtain IRS Form 2106, *Employee Business Expenses*, for the previous two years.

(3) Calculation of Effective Income

The Mortgagee must determine the portion of the allowance that can be considered Effective Income.

The Mortgagee must subtract automobile expenses as shown on IRS Form 2106 from the Automobile Allowance before calculating Effective Income based on the current amount of the allowance received.

If the Borrower uses the standard per-mile rate in calculating automobile expenses, as opposed to the actual cost method, the portion that the IRS considers depreciation may be added back to income. Expenses that must be treated as recurring debt include:

- the Borrower’s monthly car payment; and
- any loss resulting from the calculation of the difference between the actual expenditures and the expense account allowance.

(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, *Social Security Benefit Statement*.

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.

(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*; 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. 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 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, *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*, 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 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 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.

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 Accounts (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) Non-Taxable Income (Grossing Up) (TOTAL)

(1) Definition

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

- some portion of Social Security Income;
- some federal government employee Retirement Income;
- Railroad Retirement benefits;
- some state government Retirement Income;
- certain types of disability and Public Assistance payments;
- Child Support;
- military allowances; 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 Non-Taxable 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 Non-Taxable Income may be added to the Borrower's gross income.

The percentage of Non-Taxable 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 Non-Taxable Income by 15 percent.

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

d. Asset Requirements (TOTAL)

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 towards 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; or
- 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.

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 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 are 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 a credit from a Mortgagee for the interest rate chosen.

Premium Pricing may be used to pay a Borrower's actual closing costs and/or prepaid items. Closing costs paid in this manner do not need to be included as part of the Interested Party limitation.

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 expenses; 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 to the closing costs and prepaid items including any items Paid Outside Closing (POC).

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 at the time of underwriting.

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 source of funds 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 towards 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 towards 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 towards the Borrower's MRI;
- the Governmental Entity has, at or before closing, incurred a legally enforceable obligation to provide the funds towards the Borrower's MRI; or
- the Governmental Entity has, at or before closing, authorized a draw on its account to provide the funds towards 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

If the Borrower does not hold the deposit account solely, all non-Borrower parties on the account must provide a written statement that the Borrower has full access and use of the funds.

(a) Traditional Documentation

The Mortgagee must obtain a written VOD and the Borrower's most recent statement for each account.

(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 third party verification. 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 MRI.

(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 gift funds from the donor to the Borrower in accordance with the requirements below.

a. 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.

b. 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, and a bank statement showing the withdrawal from the donor's account.

If the gift funds are paid directly to the settlement agent, the Mortgagee must verify that the settlement agent received the funds from the donor for the amount of the gift, and that the funds were from an acceptable source.

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 a party to the transaction.

The Mortgagee and its Affiliates are prohibited from providing the loan of gift funds to the donor 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, 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 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 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 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, 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.

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 form HUD-92900-LT, Closing Disclosure or similar legal document, and the sales contract.

(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 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)

Rent may be an inducement to purchase when the sales agreement reveals that the Borrower has been living in the Property rent-free or has an agreement to occupy the Property at a rental amount considerably below fair market rent.

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 MRI;
- 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:

- the functions performed are limited to the Governmental Entity's secondary financing program; and
- the secondary financing legal documents (Note and Deed of Trust) name the Governmental Entity as the Mortgagee.

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 MRI.

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 loan instruments; 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.

Where a nonprofit assisting a Governmental Entity with its secondary financing programs is not a HUD-approved Nonprofit, a documented agreement must be provided that:

- the functions performed by the nonprofit are limited to the Governmental Entity's secondary financing program; and
- the secondary financing legal documents (Note and Deed of Trust) name the Governmental Entity as the Mortgagee.

(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.

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 loan instruments.

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 loan instruments.

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 loan instruments.

(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 MRI.

(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.

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

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 MRI.

(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 MRI.

(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, 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 Housing (TOTAL)

(1) Definition

Trade-In of Manufactured Housing 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 the transaction was arms-length, 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 MRI].

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 Proposed 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 towards 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)

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 is completed as directed in the form instructions.

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

The Mortgagee must complete form HUD-92900-A 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.

5. Manual Underwriting of the Borrower

The Mortgagee must manually underwrite those applications where the AUS issues a Refer or applications which were downgraded to a manual underwrite.

If a Mortgage receiving the AUS Refer or downgrade to manual processing involves a HUD employee, the Mortgagee must underwrite the transaction in accordance with the guidance in this Manual Underwriting section. The Mortgagee must submit the underwritten mortgage application to the Processing and Underwriting Division Director at the Jurisdictional HOC for final underwriting approval.

a. Credit Requirements (Manual)

i. General Credit Requirements (Manual)

FHA's general credit policy requires Mortgagees to analyze the Borrower's credit history, liabilities, and debts to determine creditworthiness.

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

The Mortgagee must utilize the same credit report and credit scores sent to 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.

The Mortgagee is not required to obtain a credit report for non-credit qualifying Streamline Refinance transactions.

ii. Types of Credit History (Manual)

If a traditional credit report is available, the Mortgagee must use a traditional credit report. However, if a traditional credit report is not available, the Mortgagee must develop the Borrower's credit history using the requirements for Non-Traditional and Insufficient Credit.

(A) Traditional Credit (Manual)

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

(1) Requirements for the Credit Report

Credit reports must obtain all information from at least two credit repositories pertaining to credit, residence history, and public records information; be in an easy to read and understandable format; and not require code translations. The credit report may not contain whiteouts, erasures, or alterations. 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 regarding:
  - bankruptcies;
  - Judgments;
  - lawsuits;
  - foreclosures; and
  - tax liens; and
- for each Borrower debt listed:
  - the date the account was opened;
  - high credit amount;
  - required monthly payment amount;
  - unpaid balance; and
  - payment history.

(2) Updated Credit Report or Supplement to the Credit Report

The Mortgagee must obtain an updated credit report or supplement if the underwriter identifies inconsistencies between any information in the mortgage file and the original credit report.

(3) Credit Information Not Listed on Credit Report

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

(4) Specific Requirements for Residential Mortgage Credit Report

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

- provide a detailed account of the Borrower's employment history;
- verify each Borrower's current employment and income through an interview with the Borrower's employer or explain why such an interview was not completed;
- contain a statement attesting to the certification of employment for each Borrower and the date the information was verified; and
- report a credit history for each trade line within 90 Days of the credit report for each account with a balance.

(B) Non-Traditional and Insufficient Credit (Manual)

For Borrowers without a credit score, the Mortgagee must either obtain a Non-Traditional Mortgage Credit Report (NTMCR) from a credit reporting company or independently develop the Borrower's credit history using the requirements outlined below.

(1) Non-Traditional Mortgage Credit Report

(a) Definition

An NTMCR is designed to access the credit history of a Borrower who does not have the types of trade references that appear on a traditional credit report and used either as:

- a substitute for a TRMCR or an RMCR; or
- a supplement to a traditional credit report that has an insufficient number of trade items reported to generate a credit score.

(b) Standard

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

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

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

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

(2) Independent Verification of Non-Traditional Credit Providers

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

a. To verify the existence of each credit provider, the Mortgagee must review public records from the state, county, or city or other documents providing a similar level of objective information.

b. To verify credit information, the Mortgagee must:
   - use a published address or telephone number for the credit provider and not rely solely on information provided by the applicant; and
   - obtain the most recent 12 months of canceled checks, or equivalent proof of payment, demonstrating the timing of payment to the credit provider.

c. To verify the Borrower's rental payment history, the Mortgagee must obtain a rental reference from the appropriate rental management company, provided the Borrower is not renting from a Family Member, demonstrating the timing of payment of the most recent 12 months in lieu of 12 months of canceled checks or equivalent proof of payment.

(3) Sufficiency of Credit References

To be sufficient to establish the Borrower's credit, the credit history must include three credit references, including at least one of the following:

- rental housing payments (subject to independent verification if the Borrower is a renter);
- telephone service; or
- utility company reference (if not included in the rental housing payment), including:
  - gas;
  - electricity;

- water;
- television service; or
- Internet service.

If the Mortgagee cannot obtain all three credit references from the list above, the Mortgagee may use the following sources of unreported recurring debt:

- insurance premiums not payroll deducted (for example, medical, auto, life, renter's insurance);
- payment to child care providers made to businesses that provide such services;
- school tuition;
- retail store credit cards (for example, from department, furniture, appliance stores, or specialty stores);
- rent-to-own (for example, furniture, appliances);
- payment of that part of medical bills not covered by insurance;
- a documented 12-month history of savings evidenced by regular deposits resulting in an increased balance to the account that:
  - were made at least quarterly;
  - were not payroll deducted, and;
  - caused no insufficient funds (NSF) checks;
- an automobile lease;
- a personal loan from an individual with repayment terms in writing and supported by canceled checks to document the payments; or
- a documented 12-month history of payment by the Borrower on an account for which the Borrower is an authorized user.

iii. Evaluating Credit History (Manual)

(A) General Credit (Manual)

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

The Mortgagee must not consider the credit history of a non-borrowing spouse.

(B) Types of Payment Histories (Manual)

The underwriter must evaluate the Borrower's payment histories in the following order: (1) previous housing expenses and related expenses, including utilities; (2) installment debts; and (3) revolving accounts.

(1) Satisfactory Credit

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

The underwriter may approve the Borrower with an acceptable payment history if the Borrower has no major derogatory credit on revolving accounts in the previous 12 months.

Major derogatory credit on revolving accounts must include any payments made more than 90 Days after the due date, or three or more payments more than 60 Days after the due date.

(2) Payment History Requiring Additional Analysis

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

The Mortgagee must analyze the Borrower's delinquent accounts to determine whether late payments were based on a disregard for financial obligations, an inability to manage debt, or extenuating circumstances. The Mortgagee must document this analysis in the mortgage file. Any explanation or documentation of delinquent accounts must be consistent with other information in the file.

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

(C) Payment History on Housing Obligations (Manual)

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

- the credit report;
- verification of rent received directly from the landlord (for landlords with no Identity of Interest with the Borrower);
- verification of Mortgage received directly from the Servicer; or
- a review of canceled checks that cover the most recent 12-month period.

The Mortgagee must verify and document the previous 12 months' housing history. For Borrowers who indicate they are living rent-free, the Mortgagee must obtain verification from the property owner where they are residing that the Borrower has been living rent-free and the amount of time the Borrower has been living rent free.

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.

(D) Collection Accounts (Manual)

(1) Definition

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

(2) Standard

The Mortgagee must determine if collection accounts were a result of:

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

(3) Required Documentation

The Mortgagee must document reasons for approving a Mortgage when the Borrower has any collection accounts.

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

(E) Charge Off Accounts (Manual)

(1) Definition

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

(2) Standard

The Mortgagee must determine if Charge Off Accounts were a result of:

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

(3) Required Documentation

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

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

(F) Disputed Derogatory Credit Accounts (Manual)

(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

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

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

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

(3) Required Documentation

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

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

(G) Judgments (Manual)

(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.

Regardless of the amount of outstanding Judgments, the Mortgagee must determine if the Judgment was a result of:

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

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 calculation of the Borrower's Debt-to-Income (DTI) ratio.

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.

(H) Bankruptcy (Manual)

(1) Standard: Chapter 7

A Chapter 7 bankruptcy (liquidation) does not disqualify a Borrower from obtaining an FHA-insured Mortgage if, at the time of case number assignment, at least two years have elapsed since the date of the bankruptcy discharge. During this time, the Borrower must have:

- re-established good credit; or
- chosen not to incur new credit obligations.

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

- can show that the bankruptcy was caused by extenuating circumstances beyond the Borrower's control; and
- has since exhibited a documented ability to manage their financial affairs in a responsible manner.

(2) Standard: Chapter 13

A Chapter 13 bankruptcy does not disqualify a Borrower from obtaining an FHA-insured Mortgage, if at the time of case number assignment at least 12 months of the pay-out period under the bankruptcy has elapsed.

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

(3) 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.

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

(I) Foreclosure and Deed-in-Lieu of Foreclosure (Manual)

(1) Standard

A Borrower is generally not eligible for a new FHA-insured Mortgage if the Borrower had a foreclosure or a DIL of foreclosure in the three-year period prior to the date of case number assignment.

This three-year period begins on the date of the DIL or the date that the Borrower transferred ownership of the Property to the foreclosing Entity/designee.

Exceptions

The Mortgagee may grant an exception to the three-year requirement if the foreclosure was the result of documented extenuating circumstances that were beyond the control of the Borrower, such as a serious illness or death of a wage earner, and the Borrower has re-established good credit since the foreclosure.

Divorce is not considered an extenuating circumstance. An exception may, however, be granted where a Borrower's Mortgage was current at the time of the Borrower's divorce, the ex-spouse received the Property, and the Mortgage was later foreclosed.

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

(2) Required Documentation

If the credit report does not indicate the date of the foreclosure or DIL of foreclosure, the Mortgagee must obtain the Closing Disclosure, deed or other legal documents evidencing the date of property transfer.

If the foreclosure or DIL of foreclosure was the result of a circumstance beyond the Borrower's control, the Mortgagee must obtain an explanation of the circumstance and document that the circumstance was beyond the Borrower's control.

(J) Pre-Foreclosure Sales (Short Sales) (Manual)

(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

A Borrower is generally not eligible for a new FHA-insured Mortgage if they relinquished a Property through a Short Sale within three years from the date of case number assignment.

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

(a) Exception for Borrower Current at the Time of Short Sale

A Borrower is considered eligible for a new FHA-insured Mortgage if, from the date of case number assignment for the new Mortgage:

- all Mortgage Payments on the prior Mortgage were made within the month due for the 12-month period preceding the Short Sale; and
- installment debt payments for the same time period were also made within the month due.

(b) Exception for Extenuating Circumstances

The Mortgagee may grant an exception to the three-year requirement if the Short Sale was the result of documented extenuating circumstances that were beyond the control of the Borrower, such as a serious illness or death of a wage earner, and the Borrower has re-established good credit since the Short Sale.

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

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

(3) Required Documentation

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

If the Short Sale was the result of a circumstance beyond the Borrower's control, the Mortgagee must obtain an explanation of the circumstance and document that the circumstance was beyond the Borrower's control.

(K) Credit Counseling/Payment Plan

Participating in a consumer credit counseling program does not disqualify a Borrower from obtaining an FHA-insured Mortgage, provided the Mortgagee documents that:

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

iv. Evaluating Liabilities and Debts (Manual)

(A) General Liabilities and Debts (Manual)

(1) Standard

The Mortgagee must determine the Borrower's monthly liabilities by reviewing all debts listed on the credit report, *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 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.

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

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

(2) Required Documentation

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.

(B) Undisclosed Debt and Inquiries (Manual)

(1) Standard

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

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

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

(2) Required Documentation

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

(C) Federal Debt (Manual)

(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.

(D) Alimony, Child Support, and Maintenance (Manual)

(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 verify and include the monthly obligation in its calculation of the Borrower’s debt.

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

(3) Required Documentation

The Mortgagee must obtain 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.

(E) Non-Borrowing Spouse Debt in Community Property States (Manual)

(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 counted in the DTI ratio.

(F) Deferred Obligations (Manual)

(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 verify and include deferred obligations in the calculation of 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.

(G) Student Loans (Manual)

(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 1 percent of the outstanding balance reported on the Borrower's credit report; and
- 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.

(4) Calculation of Monthly Obligation

Regardless of the payment status, the Mortgagee must use either:

- the greater of:
    - 1 percent of the outstanding balance on the loan; or
    - the actual documented payment; or
- if the actual documented payment is less than 1 percent of the outstanding balance, the Mortgagee may use the lower payment only if it will fully amortize the loan over its term.

(H) Installment Loans (Manual)

(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.

(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 obtain a copy of the loan agreement or payment statement documenting the amount of the monthly payment. If the credit report, loan agreement or payment statement shows a deferred payment arrangement for an Installment Loan, refer to the Deferred Obligations section.

(I) Revolving Charge Accounts (Manual)

(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.

(J) 30-Day Accounts (Manual)

(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.

(K) Business Debt in Borrower's Name (Manual)

(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.

(L) Disputed Derogatory Credit Accounts (Manual)

(1) Definition

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

(2) Standard

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

The following items are excluded from the cumulative balance:

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

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

(M) Non-derogatory Disputed Account and Disputed Accounts Not Indicated on the Credit Report (Manual)

(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; or
- disputed accounts that are current and paid as agreed.

(2) 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 must analyze the effect of the disputed accounts on the Borrower's ability to repay the loan. If the dispute results in the Borrower's monthly debt payments utilized in computing the DTI ratio being less than the amount indicated on the credit report, the Borrower must provide documentation of the lower payments.

(N) Contingent Liabilities (Manual)

(1) Definition

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

(2) Standard

The Mortgagee must include monthly payments on contingent liabilities in the calculation of the Borrower's monthly obligations unless the Mortgagee verifies that there is no possibility that the debt holder will pursue debt collection against the Borrower should the other party default or the other legally obligated party has made 12 months of timely payments.

(3) 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, and does not have a history of delinquent payments on the loan.

(c) Court Ordered Divorce Decree

The Mortgagee must obtain a copy of the divorce decree ordering the spouse to make payments.

(4) 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.

(O) Collection Accounts (Manual)

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

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

(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.

(P) Charge Off Accounts (Manual)

(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.

(Q) Private Savings Clubs (Manual)

(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 Borrowers' 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.

(R) Obligations Not Considered Debt

Obligations not considered debt include:

- medical collections
- federal, state, and local taxes, if not delinquent and no payments required
- automatic deductions from savings, when not associated with another type of obligation
- Federal Insurance Contributions Act (FICA) and other retirement contributions, such as 401(k) accounts
- collateralized loans secured by depository accounts
- utilities
- 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

b. Income Requirements (Manual)

Effective Income Definition

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

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.

ii. Employment Related Income (Manual)

(A) Definition

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

(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 using one of the following methods.

(1) Traditional Current Employment Documentation

The Mortgagee must obtain the most recent pay stubs covering a minimum of 30 consecutive Days (if paid weekly or bi-weekly, pay stubs must cover a minimum of 28 consecutive Days) that show the Borrower's year-to-date earnings, and one of the following to verify current employment:

- a written Verification of Employment (VOE) covering two years; or
- an electronic verification acceptable to FHA.

Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.

(2) Alternative Current Employment Documentation

If using alternative documentation, the Mortgagee must:

- obtain copies of the pay stubs covering the most recent 30 consecutive Days (if paid weekly or bi-weekly, pay stubs must cover a minimum of 28 consecutive Days) that show the Borrower's year-to-date earnings;
- obtain copies of the original IRS W-2 forms 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.

Re-verification of employment must be completed within 10 Days prior to the date of the Note. Verbal re-verification of employment is acceptable.

(3) Past Employment Documentation

Direct verification of the Borrower's employment 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 or Bonus Income).
- The Borrower executes IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-T, 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:

- W-2(s)
- VOE(s)
- electronic verification acceptable to FHA
- evidence supporting enrollment in school or the military during the most recent two full years

iii. Primary Employment (Manual)

(A) Definition

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

(B) Standard

The Mortgagee may use primary Employment Income as Effective Income.

(C) Calculation of Effective Income

(1) Salary

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.

(2) Hourly

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.

iv. Part-Time Employment (Manual)

(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.

v. Overtime and Bonus Income (Manual)

(A) Definition

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

(B) Standard

The Mortgagee may use Overtime and Bonus 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 and Bonus Income less than two years may be considered Effective Income if the Mortgagee documents that the Overtime and Bonus 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

For employees with Overtime or Bonus Income, the Mortgagee must average the income earned over the previous two years to calculate Effective Income. However, if the Overtime or Bonus Income from the current year decreases by 20 percent or more from the previous year, the Mortgagee must use the current year's income.

vi. Seasonal Employment (Manual)

(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 (Manual)

(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 (Manual)

(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

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.

(2) Hourly

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.

ix. Commission Income (Manual)

(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 Commission Income less than or equal to 25 percent of the Borrower's total earnings, the Mortgagee must use traditional or alternative employment documentation.

For Commission Income greater than 25 percent of the Borrower's total earnings, the Mortgagee must obtain signed tax returns, including all applicable schedules, for the last two years. In lieu of signed tax returns from the Borrower, the Mortgagee may obtain a signed IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-T, *Request for Transcript of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, and tax transcripts directly from the IRS.

(D) Calculation of Effective Income

The Mortgagee must calculate Effective Income for commission by using the lesser of (a) the average net Commission Income earned over the previous two years, or the length of time Commission Income has been earned if less than two years; or (b) the average net Commission Income earned over the previous one year. The Mortgagee must calculate net Commission Income by subtracting the unreimbursed business expenses from the gross Commission Income.

The Mortgagee must reduce the Effective Income by the amount of any unreimbursed employee business expenses, as shown on the Borrower's Schedule A. For information on analyzing the Borrower's 1040, review Analyzing IRS Forms.

x. Self-Employment Income (Manual)

(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 proprietorship;
- 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 document that the business income is now stable.

A Mortgagee may consider income as stable after a 20 percent reduction if the Mortgagee can document the reduction in income was the result of an extenuating circumstance, the Borrower can demonstrate the income has been stable or increasing for a minimum of 12 months, and the Borrower qualifies utilizing the reduced income.

(C) Required Documentation

(1) Individual and Business Tax Returns

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

In lieu of signed individual or business tax returns from the Borrower, the Mortgagee may obtain a signed IRS Form 4506, *Request for Copy of Tax Return*, IRS Form 4506-T, *Request for Transcript of Tax Return*, or IRS Form 8821, *Tax Information Authorization*, 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 date of most recent calendar or fiscal year-end tax return was filed by the Borrower. A balance sheet is not required for self-employed Borrowers filing Schedule C income.

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

(3) Business Credit Reports

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

(D) Calculation of Effective Income

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 the previous two years; or
- the average gross Self-Employment Income earned over the previous one year.

xi. Additional Required Analysis of Stability of Employment Income

(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 job 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 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.

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. 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.

xii. Other Sources of Effective Income (Manual)

(A) Disability Benefits (Manual)

(1) Definition

Disability Benefits refer to benefits received from the Social Security Administration (SSA), Department of Veterans Affairs (VA), 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 (Manual)

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) VA 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 (Manual)

(1) Definition

Alimony, Child Support, and Maintenance Income refers to income received from a former spouse or partner or from a non-custodial 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 six months, 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 (Manual)

(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 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 (Manual)

(1) Definition

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

(2) Required Documentation

The Mortgagee must verify and document that the Governmental Entity subsidizes the Borrower's Mortgage Payments either through direct payments or tax rebates.

(3) Calculating Effective Income

Mortgage Credit Certificate income that is not used to directly offset the Mortgage Payment before calculating the qualifying ratios may be included as Effective Income. The Mortgagee must use the current subsidy rate to calculate the Effective Income.

(E) Section 8 Homeownership Vouchers (Manual)

(1) Definition

Section 8 Homeownership 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 Homeownership 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 (Manual)

(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 (Manual)

(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.

The Mortgagee must also obtain IRS Form 2106, *Employee Business Expenses*, for the previous two years.

(3) Calculation of Effective Income

The Mortgagee must determine the portion of the allowance that can be considered Effective Income.

The Mortgagee must subtract automobile expenses as shown on IRS Form 2106 from the Automobile Allowance before calculating Effective Income based on the current amount of the allowance received.

If the Borrower uses the standard per-mile rate in calculating automobile expenses, as opposed to the actual cost method, the portion that the IRS considers depreciation may be added back to income. Expenses that must be treated as recurring debt include:

- the Borrower's monthly car payment; and
- any loss resulting from the calculation of the difference between the actual expenditures and the expense account allowance.

Automobile Allowance refers to the amount of the Automobile Allowance that exceeds the Borrower's actual automobile expenditures.

(H) Retirement Income (Manual)

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

(1) Social Security Income (Manual)

(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 SSA Form-1099/1042S, *Social Security Benefit Statement*.

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) equivalent documentation 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 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 (Manual)

(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) (Manual)

(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 (Manual)

(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 (Manual)

(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.

(b) Required Documentation

Required 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 the prospective leases if available.

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*, 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 existing lease, rental history over the previous 24 months that is free of unexplained gaps greater than three months (such gaps could be explained by student, seasonal or military renters, or property rehabilitation), and the Borrower's most recent tax returns, including Schedule E, from the previous two years.

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 other legal document.

(c) Calculation of Effective Income

The Mortgagee must add the net subject property Rental Income to the Borrower's gross 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 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 the 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 (Manual)

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

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*, 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 PITI from the lesser of:

- the monthly operating income reported on 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 with less than two years of Rental Income history, the Mortgagee must document the date of acquisition by providing the deed, Closing Disclosure or other 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 (Manual)

(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 (Manual)

(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 (Manual)

(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 (Manual)

(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 Accounts (Manual)

(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 (Manual)

(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 (Manual)

(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) Non-Taxable Income (Grossing Up) (Manual)

(1) Definition

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

- some portion of Social Security Income;
- some federal government employee Retirement Income;
- Railroad Retirement benefits;
- some state government Retirement Income;
- certain types of disability and Public Assistance payments;
- Child Support;
- military allowances; 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 Non-Taxable 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 Non-Taxable Income may be added to the Borrower's gross income.

The percentage of Non-Taxable 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 Non-Taxable Income by 15 percent.

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

c. Asset Requirements (Manual)

i. General Asset Requirements (Manual)

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 towards the Borrower's MRI.

(A) Earnest Money Deposit (Manual)

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; or
- 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.

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).

(B) Cash to Close (Manual)

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 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 are 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, MIP, 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 a credit from a Mortgagee for the interest rate chosen.

Premium Pricing may be used to pay a Borrower's actual closing costs and/or prepaid items. Closing costs paid in this manner do not need to be included as part of the Interested Party limitation.

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 expenses; 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 to the origination fees, other closing costs and discount points including any items Paid Outside Closing (POC).

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 at the time of underwriting.

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 (Manual)

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

Reserves do not include:

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

(1) Reserves for One- to Two-Unit Properties

The Mortgagee must verify and document Reserves equivalent to one month's PITI after closing for one- to two-unit Properties.

(2) 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 (Manual)

(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 source of funds 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 towards 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 towards 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 towards the Borrower's MRI;
- the Governmental Entity has, at or before closing, incurred a legally enforceable obligation to provide the funds towards the Borrower's MRI; or
- the Governmental Entity has, at or before closing, authorized a draw on its account to provide the funds towards 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 (Manual)

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

(A) Checking and Savings Accounts (Manual)

(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

If the Borrower does not hold the deposit account solely, all non-Borrower parties on the account must provide a written statement that the Borrower has full access and use of the funds.

(a) Traditional Documentation

The Mortgagee must obtain a written VOD and the Borrower's most recent statement for each account.

(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 (Manual)

(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 (Manual)

(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 (Manual)

(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 third party verification. 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 (Manual)

(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) (Manual)

(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 MRI.

(b) Reserves

Surplus gift funds may not be considered as cash Reserves.

(c) 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, 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 gift funds from the donor to the Borrower in accordance with the requirements below.

a. 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.

b. 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, and a bank statement showing the withdrawal from the donor's account.

If the gift funds are paid directly to the settlement agent, the Mortgagee must verify that the settlement agent received the funds from the donor for the amount of the gift, and that the funds were from an acceptable source.

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 a party to the transaction.

The Mortgagee and its Affiliates are prohibited from providing the loan of gift funds to the donor 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, 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, 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 (Manual)

(1) Definition

Interested Parties refer to sellers, real estate agents, builders, developers 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 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 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, 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.

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 form HUD-92900-LT, Closing Disclosure or similar legal document, and the sales contract.

(H) Inducements to Purchase (Manual)

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 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 (Manual)

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 (Manual)

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 (Manual)

Rent may be an inducement to purchase when the sales agreement reveals that the Borrower has been living in the Property rent-free or has an agreement to occupy the Property at a rental amount considerably below fair market rent.

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 (Manual)

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 (Manual)

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 (Manual)

(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 MRI;
- 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:

- the functions performed are limited to the Governmental Entity's secondary financing program; and
- the secondary financing legal documents (Note and Deed of Trust) name the Governmental Entity as the Mortgagee.

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 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 MRI.

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 loan instruments; 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.

Where a nonprofit assisting a Governmental Entity with its secondary financing programs is not a HUD-approved Nonprofit, a documented agreement must be provided that:

- the functions performed by the nonprofit are limited to the Governmental Entity's secondary financing program; and
- the secondary financing legal documents (Note and Deed of Trust) name the Governmental Entity as the Mortgagee.

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

(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.

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 loan instruments.

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 (Manual)

(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 loan instruments.

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 (Manual)

(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 loan instruments.

(K)Loans (Manual)

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 (Manual)

(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 MRI.

(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 (Manual)

(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 (Manual)

(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.

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

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 (Manual)

(1) Disaster Relief Grants (Manual)

(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 MRI.

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

(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 MRI.

(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 (Manual)

(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, 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 (Manual)

(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 Housing (Manual)

(1) Definition

Trade-In of Manufactured Housing 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 (Manual)

(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 the transaction was arms-length, and that the Borrower is entitled to the Net Sale Proceeds.

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

(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 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 the sale of the Property being purchased.

(R) Sweat Equity (Manual)

(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 MRI.

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 Proposed Construction, the Mortgagee must also obtain the sales contract indicating the tasks to be performed by the Borrower during construction.

(S) Trade Equity (Manual)

(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 (Manual)

(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 towards 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.

d. Final Underwriting Decision (Manual)

The Direct Endorsement (DE) underwriter is ultimately responsible for making an underwriting decision on behalf of their DE Mortgagee in compliance with HUD requirements.

i. Duty of Care/Due Diligence (Manual)

The underwriter must exercise the same level of care that would be used in underwriting a Mortgage entirely dependent on the Property as security. Compliance with FHA requirements is deemed to be the minimum standard of due diligence required in originating and underwriting an FHA-insured Mortgage.

ii. Specific Underwriter Responsibilities (Manual)

The underwriter must review each Mortgage as a separate and unique transaction, recognizing that there may be multiple factors that demonstrate a Borrower's ability and willingness to make timely Mortgage Payments to make an underwriting decision on behalf of their DE Mortgagee in compliance with HUD requirements. The underwriter must evaluate the totality of the Borrower's circumstances and the impact of layering risks on the probability that a Borrower will be able to repay the mortgage obligation according to the terms of the Mortgage.

As the responsible party, the underwriter must:

- review appraisal reports, compliance inspections, and credit analyses to ensure reasonable conclusions, sound reports, and compliance with HUD requirements regardless of who prepared the documentation;
- determine the acceptability of the appraisal, the inspections, the Borrower's capacity to repay the Mortgage, and the overall acceptability of the Mortgage for FHA insurance;