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NMLS# 629700

FHA Underwriting Guidelines

Version 09.01.2019

STANDARD 203(b)

CREDIT-QUALIFYING STREAMLINE REFINANCE

NON CREDIT-QUALIFYING STREAMLINE REFINANCE

DISASTER RELIEF 203(h)

HIGH BALANCE

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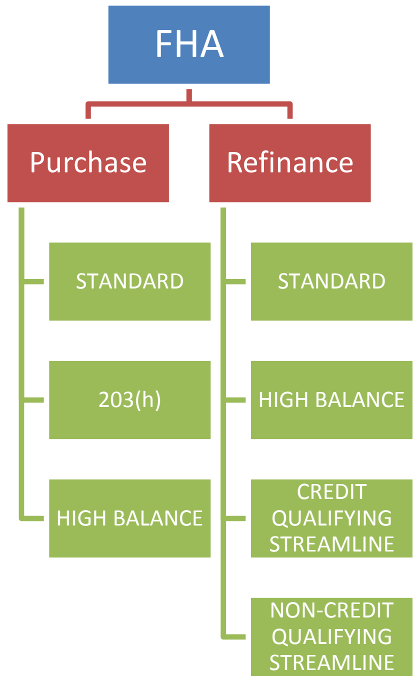
1.02 Program Overview

The Federal Housing Administration (FHA) provides mortgage insurance on loans made by FHA-approved lenders throughout the U.S. FHA mortgage insurance provides lenders with protection against loss as the result of homeowners defaulting on their mortgage loans.



1.02.01 Multiple Risk Layering

Underwriters must take into account the file as a whole when evaluating any file for approval. Although the AUS findings and TOTAL Scorecard are essential tools in today's mortgage underwriting marketplace, in the end they are just that, tools to be used by the underwriter to help evaluate the overall risk tolerance for any given file. It will always fall back to the underwriter's experience and seasoned real-world skills in order to determine a file's creditworthiness and viability in the secondary marketplace.

That said, our underwriters are trained to assess the transaction for multiple layers of risk on any given file. Past performance has shown that individual risks and blemishes on a borrower's application may not pose a large potential for lack of repayment, however when multiple layers of risk are combined the performance levels drop significantly.

Some examples of these types of risks are:

- High Debt-To-Income Ratios
- Payment Shock
- Serious Adverse Credit
- Duration of Employment
- ARM Loans

1.03 Program Terms

1.03.01 Program Code

- FHA30: FHA Purchase or Cash Out (Regular) Refinance 30, 25 & 20-Year Terms
- FHA15: FHA Purchase or Cash Out (Regular) Refinance 15-Year Term
- FHAS30: FHA Streamline 30, 25 & 20-Year Terms
- FHAS15: FHA Streamline 15-Year Term
- FHA5/1ARM: FHA 5/1 Adjustable Rate Mortgage
- FHA203K15 FHA Purchase or Refinance with Renovation and Repair 15-year term
- FHA203K30 FHA Purchase or Refinance with Renovation and Repair 30-year term

1.03.02 Term

- Purchase: 15/20/25/30 Year Terms Available
- Cash Out (Regular) Refinance: 15/20/25/30 Year Terms Available
- Streamline Refinance: 15/20/25/30 Year Terms Available

1.03.03 Loan Type

- Purchase: Fixed Rate, 5/1 ARM
- Cash Out (Regular) Refinance: Fixed Rate, 5/1 ARM
- Streamline Refinance: Fixed Rate Only

1.03.04 Occupancy Type

- Purchase: Primary Residence Only
- Cash Out (Regular) Refinance: Primary Residence Only
- Streamline Refinance: Primary Residence, Investment Property

1.03.05 Loan-To-Value

Maximum Loan-To-Values (LTVs) are determined by using the base loan amount. The base loan amount is the maximum loan amount prior to the addition of the financed mortgage insurance premium.

The most recent FCM Credit Score/Loan-To-Value Matrix can be found by referencing the link below:

FCM CREDIT SCORE/LTV MATRIX

1.03.06 Mortgage Insurance

FHA requires both a Monthly Mortgage Insurance Premium (MIP) and an Up-Front Mortgage Insurance Premium (UFMIP). For information on the latest MIP factors please reference the following document:

FHA MIP CHART

Partial financing of the UFMIP is not allowed. The UFMIP must be 100% financed into the mortgage or paid entirely in cash.

1.03.07 Maximum Loan Amount

The Maximum Base Loan Amount cannot exceed the FHA Statutory Mortgage Limit for each county or the "ceiling" amount listed in the chart below, whichever is less:

- 1-unit: $484,350
- 2-unit: $620,200
- 3-unit: $749,650
- 4-unit: $931,600

The FHA Statutory Mortgage Limits can be found at the following website:

FHA STATUTORY MORTGAGE LIMITS

Please reference High Balance Transactions for Base Loan Amounts which exceed the FHA Statutory Mortgage Limit ceilings listed above.

For Refinances:

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.

For Streamline Refinances: Please reference the Maximum Loan Amount subsection in the Streamline Refinance section.

For HUD REO $100 Down: The maximum loan amount on the HUD $100 down program is limited to 100% of the as-is appraised value. For more information on the HUD $100 down program please reference the section on HUD REO Purchases.

1.03.08 FHA Case Numbers

FHA Case Numbers should be requested through FHA Connection as soon as a property has been identified by the customer. Proof of validation for all case numbers must be requested after case number assignment and retained in the file. FHA case numbers should reflect a clear CAIVRS, if it does not reflect a clear CAIVRS, a separate CAIVRS request should be initiated. Case numbers are to be requested prior to ordering an appraisal.

1.03.08.01 Case Number Transfers

Request/approval for case number transfer should be received by the customer either verbally or in writing. The new lender must request the transfer and provide their Lender/Institution ID. If the application is being denied by FCM, a credit reject must be filed in FHA Connection prior to transfer of the case number.

1.03.09 Acceptable AUS Findings

The following AUS findings are acceptable. Refer findings are subject to manual underwriting, see Manual Underwriting 1.03.10

- DU Approve/Eligible
- DU Refer/Eligible
- LP Accept/Accept/Eligible
- LP Refer

Note that streamline transactions should not be run through TOTAL Scorecard. Streamline transactions inadvertently run through TOTAL Scorecard are permitted, and documentation of values is not required.

1.03.09.01 AUS Tolerance

The loan does not have to be re-run in AUS if the changes are within the following tolerance levels:

- Cash Reserves: Cash Reserves are not less than 10% below the previous AUS Approval
- Income: Income verified is not less than 5% below the previous AUS approval
- Tax and Insurance Escrow: The change in escrows does not result in more than a 2% increase in the Front-End DTI (Total Mortgage payment vs. Income)

1.03.10 Manual Underwriting

The following guidelines are specific to manually underwritten loans and are in addition to the other requirements in this guide:

Manually underwritten loans include:

- Loans involving borrowers without a credit score which were not scored against FHA's Total Scorecard/AUS
- Loans receiving a REFER scoring recommendation from AUS
- Loans receiving an ACCEPT scoring recommendation from AUS but which have been manually downgraded to a refer by the underwriter **see Automatic Downgrade to Manual Underwrite 1.03.09.04

1.03.10.01 Credit Score Requirement for Manually Underwritten Loans:

- Traditional Tradeline Credit Score Minimum: 640
- Non-Traditional Credit: Zero Credit Scores only.

1.03.10.02 Non-Traditional Credit

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
- Any utility not included in the payment of rent, including, but not limited to:
  - telephone service
  - gas
  - electricity
  - water

- television service
- Internet service

If three credit references from the list above cannot be obtained, the following sources of unreported recurring debt may be used to:

- 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 not reporting on credit report
- 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;
  - are 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
- a documented 12-month history of payment by the Borrower on an account for which the Borrower is an authorized user

1.03.10.03 Evaluating Credit History (Traditional and Non-Traditional)

(1) Housing History

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 mortgage servicer or
- A review of cancelled 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.

(2) Satisfactory Credit

- Borrower has made all housing and installment payments on time in the last 12 months and has no more than 2x30 day lates in last 24 months
- Borrower has no major derogatory credit on revolving accounts: 90 day late payments or 3x 60 day lates

1.03.10.04 Asset & Reserve Requirement

- 1-2 Unit – Reserves must equal or exceed one total monthly mortgage payment
- 3-4 Unit – Reserves must equal or exceed three total monthly mortgage payments.

Reserve requirements stated above are in addition to any compensating factors that may be applied.

(1) Unacceptable Reserves Sources

- 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.

1.03.10.05 Compensating Factors for Manual Underwrite

Manual Underwriting Matrix	
Maximum Qualifying Ratios	Acceptable Compensating Factors
31/43 (EE** 33/45)	Non Traditional Credit Files Maximum Ratio regardless of compensating factors.
31/43 (EE** 33/45)	No Compensating factors required
37/47	**One** of the following: • Verified and documented cash reserves • Minimal increase in housing payment • Residual income
40/40	• No discretionary debt

40/50	**Two** of the following: • Verified and documented cash reserves • Minimal increase in housing payment • Significant additional income not reflected in effective income and/or • Residual income

* See Maximum Debt Ratio 1.07.06 **EE = Energy Efficient

1.03.10.06 Automatic Downgrade to Manual Underwrite

Mortgages must be downgraded and manually underwrite any time a file receives 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.

1.03.11 AUS Reduced Documentation

Reduced documentation as specifically addressed by properly submitted AUS findings is acceptable at the discretion of the underwriter. However, Property Inspection Waivers are only allowed for certain Streamline Refinances. Please reference sections on Streamline Refinance and Appraisal Requirements for further information.

1.03.12 FHA Credit Rejects

For any FHA loan that is denied in underwriting, all requirements of the FCRA and ECOA must be met. In addition, the underwriter must complete the Mortgage Credit Reject screen in FHA Connection and follow all internal FCM Credit Denial procedures. A copy of the credit reject must be maintained in the file.

1.03.13 Secondary Financing

1.03.13.01 Purchases

The borrower may receive secondary financing to cover the entire cash investment requirement from the following sources:

- Federal, state or local government agencies
- FHA Approved Non-Profit agencies that are considered instrumentalities of government
- Borrower may also receive secondary financing from FHA Approved non-profit agencies NOT considered instrumentalities of government provided the borrower makes a cash down payment of at least 3.5% of the sales price. A list of these HUD-approved non-profit agencies is maintained here:

  HUD-Approved Non-Profit Agencies

- 100% of funds for down payment, closing costs, prepaid expenses and discount points may be from an unsecured loan from a family member

All FHA loans using Down Payment Assistance require:

- A cancelled check, or evidence of wire transfer, or other draw request showing that prior to or at the time of closing the Government Entity had authorized a draw of the funds on its account provided towards the borrower's required Minimum Cash Investment from the Government Entity's account;
  -OR-
- A letter from the Government Entity, signed by an authorized official establishing that the funds provided towards the borrower's required Minimum Cash Investment were funds legally belonging to the Government Entity at or before closing.

1.03.13.02 Rate/Term Refinances

Existing subordinate financing not used to purchase the property must be seasoned twelve months to be included in the loan amount. If disbursements from an equity line exceed a total of $1,000 within the past twelve-month period and the funds were used for purposes other than repairs and rehabilitation of the property, the amount in excess of the $1000 cannot be included in the new mortgage.

New subordinate financing is allowed subject to CLTV restrictions listed in the Credit Score/LTV Matrix.

1.03.13.03 Cash Out Refinances

Effective with Case numbers ordered on or after September 1, 2019: Existing subordinate financing must be seasoned 6 months for Cash Out Refinances. When the LTV of the proposed first mortgage is 80%, no subordinate financing may remain on the loan regardless of the length of ownership.

New subordinate financing is not allowed on any Cash Out Transaction.

1.03.13.04 Streamline Refinances

Existing secondary financing which is seasoned 6 months prior to the date of the new FHA case number assignment with 0x30 day late payments is allowed to be re-subordinated up to CLTV restrictions. CLTV restrictions can be found in the Credit Score/LTV Matrix.

New Subordinate Financing is not allowed on Streamline Refinances.

1.03.14 Escrows

Tax and Insurance Escrows are required on all FHA loans.

Homestead taxes may be used for qualifying and escrow purposes if the amount is verified by the title company and there is a reasonable belief the borrower will qualify for, or continue to qualify for, the exemption based on local and state qualification standards.

1.03.15 Repair Escrows

Repair Escrows are reviewed on a case-by-case basis but as a general guideline must satisfy at least all of the stipulations below:

- Cash-Out transactions are ineligible for repair escrows.
- Repairs must be required by the appraiser on the appraisal report.
- Repair Escrows may not cover any repair that would be considered a structural issue or could affect the liability of the subject. In addition, the repairs cannot be for an item that could be safety hazard (i.e. Roof Replacement, Mold removal and mitigation)
- For HUD/REO Properties:
    - Maximum Repair Amount: $10,000 plus a 10% contingency not to exceed $11,000 total.

- Use repair escrow amount shown on the HUD purchase contract
- 30 day standard escrow timeframe
- Up to 90 days escrow may be allowed if weather related items cannot be completed in time due to inclement weather
- A Final inspection is required and an Inspection Fee must be added
- The repair amount can be financed into the loan amount and can also exceed the appraised value up to 110%

- Standard FHA:
  - Maximum Repair Amount: $5,000
  - Two Contractor/Professional estimates are required.
  - 150% of the highest contractor estimate must be escrowed.
  - 30-day standard escrow timeframe
  - Up to 90 days escrow may be allowed if weather related items cannot be completed in time due to inclement weather
  - A Final inspection is required, and an Inspection Fee must be added
  - No amount of the repair escrow may be financed into the loan amount.

1.03.16 Ineligible Transactions

- Any property listed for sale at the time of application.
- Transactions where one or more borrowers have entered into a short refinance or restricted debt on the subject property.
- Texas 50(a)(6) Refinances

1.03.17 FHA High Balance Transactions

FCM offers a High Balance Transaction program for loan amounts above the standard loan limit "Ceiling" and where the FHA Statutory Mortgage Limit for the particular county allows. These transactions require the following stipulations be verified before submission to FCM:

- Two months reserves required
- Non-occupant co-borrowers are not permitted
- Twelve-month mortgage and/or rental history is required
- No Bankruptcy or Foreclosures allowed in the most recent 3 years
- AUS Approve only, AUS Refer is not allowed
- Owner-Occupied Only
- Maximum loan amount is limited to the FHA Statutory Mortgage Limit by County
- 30 year fixed only

- Seller-funded down payment assistance programs are not allowed

Loan amounts greater than $1,000,000 require a full appraisal and desk review. The lesser of the two values will be used to determine the LTV.

1.03.18 203(h) Disaster Victim Loans

A program designed to assist victims of presidentially-declared disasters. Program must be utilized within 1 year of declaration. FCM offers the 203h loan to allow the borrower to purchase another 1 unit primary residence with an FHA Loan. FCM Does not offer the rehabilitation/renovation loan.

  - New Residence must be 1 unit primary residence (FHA Approved Condo, PUD Or SFR)
  - Need not be located in same area as previous home
  - 100% Financing is available – no secondary financing is permitted
- A list of presidentially-declared disaster areas can be found at the following website:

http://www.fema.gov/hazard/index.shtm

1.03.19 FHA EEM Loans

1.03.19.01 Eligible Property Types

- New Construction 1-4
- Existing Construction 1-4
- Condos
- Manufactured Housing

1.03.19.02 Eligible Programs

- 203B – Purchase, NCOR
- 203K
- 203H

1.03.19.03 Energy Package (Set of Improvements to be done)

- Must be based on an analysis and recommendations of a qualified home energy rater
- Must meet a cost-effective test (the requirements of the 2006 International Energy Conservation Code was revised to the latest energy code adopted by HUD through a Federal Register notice).

1.03.19.04 Home Energy Assessment/Report

- Must be by a qualified person (guides state qualified persons)
- Makes energy improvement recommendations based on cost vs. savings.
- Can't be greater than 120 days old

1.03.19.05 Max Loan Amount

Lesser of

- Dollar amount of a cost-effective energy package (can include the cost of an EE< Facilitator (project manager)
- Lesser of 5% of: Adjusted Value, 115% of Median area price for an SFR or 150% of the National Conforming mortgage limit

There is a calculator on FHA Connection to determine this loan amount. Streamlines are based on the prior appraised value in lieu of Adjusted value.

1.03.19.06 Underwriting

- AUS is ran before the energy package is included in the loan amount. There will be 2 FHA LT forms – one without the package and one reflecting final loan terms with package. FHA recognized base Loan Transmittal for borrower approval.
- Manual works the same – just no AUS – but you need two FHA LT's – one based on base loan amount and one reflecting energy package.

1.03.19.07 Appraisals

- Do not need to reflect the energy package

1.03.19.08 Cash Back to Borrower/Cash Out

- None allowed

1.03.19.09 Escrows

- Treated the same as repair completion escrow requirements
- Borrower's may not ESCROW for work performed by the borrower
- Must be completed within 90 days
- Must be inspected by FHA Roster Inspector or the initial rater – borrower may be charged the fee.

1.03.20 FHA Amendatory Clause / Real Estate Certification

The FHA Amendatory Clause and Real Estate Certification is required as part of the sales contract in each FHA purchase transaction with the exception of the following:

- A transaction in which the borrower was provided the Appraisal and Conditional Commitment/DE Statement of Appraised value PRIOR to signing the sales contract.
- HUD REO sales
- FHA's 203(k) loan program
- Sales in which the seller is, Fannie Mae, Freddie Mac, the Department of Veterans Affairs (VA), Rural Housing Services or any other federal, state, and local government agency

- A lender disposing of REO assets
- A seller at a foreclosure sale
- Those sales in which the borrower will not be an owner-occupant (for example, sales to nonprofit agencies).

In all other cases a FHA Amendatory Clause and RE Certification is required. When required, this amendment must be included as part of the sales contract; however, they may be executed at different times so long as the FHA Amendatory clause is included as part of the sales contract by closing.

1.03.21 HUD REO Purchases

1.03.21.01 Overview

A HUD home is a 1-to-4 unit residential property acquired by HUD as a result of a foreclosure action on an FHA-insured mortgage. HUD becomes the property owner and offers it for sale to recover the loss on the foreclosure claim.

Note that the borrower's name on the HUD REO sales contract must match all other documents exactly, including but not limited to: FHA Case Number request, initial and final 1003, initial disclosures, flood certification, etc.

1.03.21.02 Seller Contributions

HUD may contribute up to three percent (3.00%) of the property's gross purchase price towards the borrower's allowable closing costs, including up to one percent (1.00%) of the loan origination fee.

If the borrower's total closing costs reflected on the HUD-1 Settlement Statement are less than the amount indicated as being paid by HUD on the sales contract, HUD will credit ONLY the actual costs charged and will not credit the purchaser with any difference, either in cash or through a reduced purchase price.

1.03.21.03 Loan Amount

The UFMIP can be financed into the total loan amount.

The maximum mortgage amount will be based on the adjusted value (appraised value).

Closing costs and prepaids may not be included in the mortgage.

1.03.21.04 Appraisal

Effective July 1, 2014 HUD asset managers will no longer provide the HUD Appraisal to borrowers and lenders. An appraisal should be ordered via standard FHA procedure. If the sales contract has a repair escrow listed, the appraiser should be provided with the Property Condition Summary (PCS) and the Property Condition Report (PCR). These can be obtained by going through www.hudhomestore.com or directly through the websites of HUDs asset managers:

www.hometelosfirst.com

www.hudpemco.com

www.oforireo.com

1.03.21.05 Repair Escrows

See Repair Escrow section.

1.03.22 Manufactured Homes Requirements and Restrictions

Manufactured Homes are eligible for financing under the FHA program. The following list of restrictions and requirements are in addition to regular program underwriting requirements:

- 640 minimum Credit Score
- Greater than 400 square feet
- Fixed Rate Only
- 30 Year Amortization only
- No FHA Jumbo
- Non-Occupant Co-Borrowers allowed at LTVs $\leq$ 80%
- Purchase, Rate and Term, Cash Out and Streamlines
- On Cash Out Refinances, the manufactured home must have been onsite for 12 months prior to the case number assignment.
- Approve/Accept/Eligible only (Exceptions: Streamlines are manually underwritten)
- There is no specific acreage limit, however, generally the land-to-value should not exceed 30% of total value.
- Structural engineer report meeting HUD guidelines must be provided prior to closing.
- Properties with an unexpired right of redemption
- Singlewide homes are not eligible.
- Repair escrows are ineligible.

Property Requirements:

- Home must have been manufactured in 1994 or newer.
- Appraiser must be able to verify that the subject has not been removed from original installation site. Verification of wheels, axles, tongue and running lights have been removed.
- If the manufactured home is de-titled prior to underwriting, nothing further is required.
- If the manufactured home is not de-titled, a copy of the original certificate of title will be required for underwriting approval; the original certificate of title must be delivered to the title company on or before the date of closing to de-title the manufactured home. The title company instructions will include collecting the original certificate and de-titling the manufactured home to be classified as real estate except when the loan is in conjunction with a THDA loan. For THDA, the title company will need to send us the original certificate of title so we can send it to THDA for de-titling.
- New construction is eligible if the manufactured home will be sold as real estate (de-titled and classified as Real Estate by dealer/seller) and vested in fee simple ownership prior to closing and reflected as real property on title commitment.

1.04 Borrower Eligibility

1.04.01 Eligible Borrowers

All purchasers listed on the sales contract must be Borrowers on the loan. All borrower must sign the sales contract. A family member of the purchaser, who is not a borrower, may be listed on the sales contract.

1.04.01.01 Total Number of Borrowers

The total number of borrowers on an FHA loan is limited to 4 regardless of AUS type.

1.04.01.02 Valid Social Security number (U.S. Citizens and Non-U.S. Citizens)

Each borrower on the loan transaction must have a valid Social Security number. In addition, any borrower who is not a U.S. citizen must meet the requirements in the following section.

1.04.01.03 Permanent Resident Aliens

A copy of the Green Card is required for all permanent resident aliens whose income and/or assets are being used to qualify for a loan. A copy of the front and back of the card is required and must be included in the loan file.

While the Green Card itself states "Do Not Duplicate" for the purpose of replacing the original card, U.S. Citizenship and Immigration Services (USCIS) allows photocopying of the Green Card. Making an enlarged copy or copying on colored paper may alleviate any concerns the borrower may have with photocopying.

1.04.01.04 Non-Permanent Resident Aliens

For all non-us Citizens and Non-Permanent Resident Aliens, please submit all citizenship status paperwork to citizenshipdocs@fcmhomeloans.com for review and approval. VISA, EAD and/or Social Security Card should be submitted if applicable.

1.04.01.05 Borrowers Not Yet Divorced/Divorce Not Final

Borrowers who are separated/legally separated and not yet divorced may be eligible to purchase a primary residence prior to finalizing their divorce provided specific documentation is provided:

- Recorded Legal Separation Agreement: In states where legal separations are recorded the agreement may be provided to determine assignment of credit obligations, current real estate holding disposition and future alimony/child support obligations. If there are minor children a child support worksheet provided by the court or attorneys must be provided.

- Marital Dissolution Agreement: In states where MDAs are prepared, the agreement may be provided to determine assignment of credit obligations, current real estate holding disposition and future alimony/child support obligations. If there are minor children a child support worksheet provided by the court or attorneys must be provided.
- Notarized Letter from Borrowers and Attorneys: In states where legal separation is not recognized and Marital Dissolution Agreements are not prepared, the borrower may provide a written separation plan signed by both parties and notarized. The attorneys representing each spouse must also submit letters stating this plan has been agreed upon and is likely to be accepted as is by the courts. If there are minor children, a child support worksheet completed by each attorney must be included.

NOTE: Please see Alimony, Child Support or Separate Maintenance section to determine if payments being received may be included in qualifying income.

1.04.02 Ineligible Borrowers

1.04.02.01 Non-natural Borrowers

Non-natural Borrowers including LLC's, Corporations, Trusts, Inter-vivo revocable trust.

1.04.02.02 Foreign Nationals

Foreign nationals who have no lawful residency status in the U.S. are not considered to be non-permanent resident aliens and are not eligible for financing.

1.04.02.03 Diplomatic Immunity

Due to the inability to compel payment or seek judgment, transactions with individuals who are not subject to United States jurisdiction are not eligible. This includes embassy personnel with diplomatic immunity. Verification the borrower does not have diplomatic immunity can be determined by reviewing the visa, passport or the U.S. Department of State's Diplomatic List at http://www.state.gov/s/cpr/rls/.

1.04.03 Non-Occupant Co-Borrowers

1.04.03.01 Overview

Non-occupant co-borrowers may be added to the transaction in certain situations in order to improve the debt ratios, however they may not be added to overcome any borrower's derogatory credit history.

- All non-occupant co-borrowers must have a principal residence in the United States unless one of the following exceptions applies:
    - Non-occupant co-borrower is in the military and stationed overseas
    - Non-occupant co-borrower is a United States citizen living abroad
- Non-occupant co-borrowers are not allowed on loans where the borrowers do not have credit scores.
- Non-occupant co-borrowers must take title at closing.
- Non-occupant co-borrowers are not allowed on manufactured/mobile home transactions.

1.04.03.02 Purchases & Fully qualifying rate/term refinances

Non-occupant Co-Borrowers are permitted on purchases and rate/term refinances with the following restrictions for loans over 75% LTV:

- Must be a family member.
- 1-unit properties only

1.04.03.03 Cash Out & Streamline Refinances

Non-occupant co-borrowers are not permitted on cash out or streamline transactions

1.04.04 Power of Attorney (POA)

All POA's used by the borrower(s) on the loan must be pre-approved by the Underwriter and may not be allowed to close without underwriter approval. POA's must be reviewed by all departments involved for accuracy up to and including Processing, Underwriting and Closing.

POA's used by the seller, realtor or other parties to the transaction may be requested but do not need approval by FCM. Other POA Requirements are listed below:

- Date of POA cannot be dated more than 180 days from the closing date.
- POA must be fully-executed.
- POA must not be expired on the date of the closing.
- POA must be specific to the transaction with the subject property address and authorization for attorney in fact to be able to execute all documents necessary to purchase or refinance the property/mortgage.
- Grantor's Names must be as they will appear on closing documents.
- A separate POA must be used for each borrower unless the borrowers are married.
- The Attorney in Fact cannot have a financial interest in the transaction (i.e. Realtor, Broker, LO, Closing Attorney)

- When using a POA for closing, the borrower's signature must be on the Uniform Residential Loan Application (1003), the initial disclosures and the sales contract/purchase agreement.

1.04.05 Identity of Interest

Identity of Interest Transactions are sales transactions between family members, business partners or other business affiliates. These transactions are restricted to a maximum LTV of 85%. However, maximum financing above 85% is permissible under the following circumstances:

- Borrower purchasing a family member's primary residence, or another property owned by a family member if the borrower has been a tenant for the previous 6 months and written evidence of their occupancy is obtained.
- Employee of a builder, who is not a family member, purchases one of the builder's new houses or models as a Principal Residence
- Current tenant purchasing home they have rented for at least six months predating the sales contract, (with lease or other written evidence).
- Sales by corporations purchasing an employee's home and reselling to another employee.

Additional Notations:

- For identity-of-interest transactions, a family member includes a child, parent, grandparent (biological, foster or step), sister, step-sister, brother, step-brother, aunt, uncle, legally adopted son or daughter, or a child who is a member of the borrower's household due to placement by an authorized agency for legal adoption.
- A full appraisal is required and must include verification of the purchase price, last sale date, and recent listing of the subject property regardless of the feedback provided in the AUS Messaging.

NOTE: Identity of Interest transactions involving originator principals, employees, and spouses are not eligible.

1.04.06 Multiple FHA Loans

FHA generally will not insure more than one principal residence mortgage for any borrower. Any person individually or jointly owning a home covered by an FHA-insured mortgage in which ownership is maintained may not purchase another principal residence with FHA insurance, except in certain situations described below:

1.04.06.01 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 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.

1.04.06.02 Increase in Family Size

Borrowers are permitted to obtain a second FHA insured primary residence loan when the existing home no longer meets the family's needs due to increase in the number of legal dependents. The following documentation is required to substantiate the familial increase and spatial needs:

- Satisfactory evidence of the increase in dependents
- Explanation of why the property no longer meets the needs of the family

In addition, the outstanding mortgage balance on the present home must be paid down to a maximum LTV of 75% (excluding financed MIP) and documented with a residential appraisal. Methods other than a residential appraisal to determine the LTV are unacceptable.

1.04.06.03 Vacating a Jointly-Owned Property

If the borrower is vacating a primary residence that will remain occupied by a co-borrower, the borrower may obtain another FHA-insured primary residence loan.

1.04.06.04 Co-Borrower for Family Member

If the borrower will be a non-occupying co-borrower on a property being purchased as a FHA-insured primary residence by other family members then they may have a joint interest in that property as well as their own FHA-insured primary residence.

A Borrower with an existing FHA-insured Mortgage on their own Principal Residence may qualify as a non-occupying co-Borrower on other FHA insured Mortgages.

1.04.07 FHA Screening

Borrowers must pass screening through federal Credit Alert Verification Report System (CAIVRS).

In addition, all of the following parties to the transaction must be checked on the HUD Limited Denial of Participation (LDP) and Excluded Parties List System (EPLS/GSA) lists:

- Borrower(s)
- Seller(s)
- Buyers' and Sellers' agents
- Builders
- Closing Agents
- Brokers
- Loan Originators
- Gift Donors
- Power of Attorney
- Processor (Broker side of Business)

1.04.08 Social Security Number Verification

All borrowers, including United States citizens, must have a valid Social Security Number (SSN) and must provide evidence of that SSN to the lender. Tax ID numbers issued by the Social Security Office are unacceptable. Any credit report used in the file must indicate that a Social Security validation vendor has validated the borrower's Social Security Number.

Social Security Number verification may be documented using any of the following:

- W-2, paystub, passport, etc.
- Copies of social security cards
- Direct verification through the Social Security Administration (SSA)
- Tax Transcripts (this is not a viable option on Streamline refinances)

Note: These requirements apply to purchase money loans and all refinances, including streamline refinances.

1.05 Employment & Income

1.05.01 Overview

Income may not be used in calculating the borrower's debt-to-income ratios if it comes from any source that cannot be verified, is not stable, or will not continue.

Loans that receive a TOTAL Scorecard *Accept* or *Approve* can generally follow the documentation requirements found in the Automated Underwriting System's (AUS) findings. It falls to the underwriter to determine if the AUS is correctly reading and accounting for the particular income situation on any given file.

1.05.02 Length of Employment

All borrowers with qualifying income must have an acceptable and stable employment history to be considered effective income for qualifying purposes. Borrowers do not need to be in their current job for two years but must be able to show a verifiable two year work history.

1.05.02.01 Gaps in Employment

A letter of explanation is required on all gaps of employment exceeding 30 days. Allowances for seasonal employment, where applicable, may be documented.

1.05.02.02 College Transcripts

College transcripts may be used in some circumstances to meet the 2 year employment history requirement for wage earners. Diplomas are not necessary and will not satisfy the condition.

1.05.02.03 Extended Absences

An extended absence is defined as any job gap greater than 6 months. If the borrower is just returning to the work force following an extended absence, the borrower's income may be considered only if the following conditions are met:

- Borrower has been employed at his/her current job for at least 6 months at the time of case number assignment; and
- Borrower can document 2-year work history prior to absence from work force

1.05.03 Primary Employment Salaried or Hourly Wage Earner

Primary employment is generally defined as a full-time employee who earns either a salary or is paid hourly.

- Salary: Use Current Salary for effective income
- Hourly (hours do not vary) – Current hourly rate is used for effective income.

- Hourly (hours vary) – Use average of previous 2 years of income. If an increase in hourly rate is documented, an average of the previous 12 months may be used.

1.05.03.01 Documentation Requirements

Minimum income documentation required for salaried or hourly wage earners is determined by AUS Total Scorecard findings unless the loan is being manually underwritten. Generally, the AUS findings for salaried or hourly wage earner income is as follows:

Traditional Current Employment Documentation, must obtain all the following:

- Most recent paystub
- A written VOE covering two years (or electronic version acceptable to FCM); or
- direct electronic verification of employment by a TPV vendor covering two years, subject to the following requirements:
  - the Borrower has authorized the lender to verify income and employment; and
  - the date of the data contained in the completed verification conforms with FHA requirements in Maximum Age of Mortgage Documents.

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

Alternative Current Employment Documentation, must obtain all the following:

- Most Recent paystubs showing YTD earnings
- W-2 Forms for previous two years
- Verbal VOE

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

Handwritten paystubs are allowed provided a copy of the cancelled checks covering a 30-day period is reviewed by underwriting along with a full Verification of Employment.

1.05.03.02 Additional Notations

Teachers must have a full VOE completed to determine the proper pay schedule unless the pay schedule can be deduced from existing documentation.

Salaried or Hourly Wage Earners cannot own 25.00% or more interest in the business.

1.05.04 Self-Employed

A borrower is considered self-employed if they own 25.00% or more interest in a business. The four basic types of business structures are: sole proprietorships, corporations, limited liability or "S" corporations, and partnerships.

1.05.04.01 Documentation Requirements

Generally, standard FHA guidelines apply with some exceptions on documentation requirements.

- The borrower must provide two years of individual federal tax returns and corporate partnership federal tax returns (if applicable to business). In certain situations where the AUS is only requiring one-year tax return the underwriter has the discretion in determining the need for the additional tax year's documentation.
- If "Approve/Eligible" or "Accept/Eligible," the borrower is not required to provide business tax returns if **ALL** of the following can be met:
    - Individual Federal tax returns show increasing self-employed income over the past two years,
    - Funds to close are not coming from business accounts,
    - The loan is not a cash out refinance.

Note: A business credit report is not required for a corporation or "S" corporation if the TOTAL Scorecard response is *Accept* or *Approve*.

- A profit and loss statement (P&L) and a balance sheet***** is required if more than a calendar quarter has elapsed since date of most recent calendar year or fiscal-year end tax return was filed by the borrower. If income used to qualify the borrower exceeds the two-year average of tax returns, an audited P&L or signed quarterly tax returns obtained from the IRS are required.
- For additional requirements regarding Tax Transcripts and returns please see the IRS Tax Transcript Requirements section.

*****Balance Sheet is not required for Sole Proprietor/Schedule C Income

FCM Verbal VOE requirements for Self-employed Borrowers:

- The existence of the borrower's business must be verified by a third party, such as a CPA, regulatory agency, or the applicable licensing bureau if possible.
- The borrower's business address and phone listing must be verified by using a telephone book, the internet or directory assistance.

- If the contact is made verbally, then a Verbal Verification of Employment must be completed to document the source of the information. The VVOE form must indicate the title of the individual verifying the employment.
- CPA letters must be dated within 30 days of the NOTE date

1.05.04.02 History

Self-employed borrowers are required to have a minimum of 2 years consecutive self-employment in the same business and geographic area.

1.05.04.03 Analysis

FCM requires self-employed income to be calculated using Fannie Mae Cash Flow Analysis Form 1084.

Business income is averaged over a two-year period using Federal Tax Returns. If there are 2106 unreimbursed expenses, they must be factored into the income as they are true expenses.

In the case of declining income, significant compensating factors must exist to consider the income in the qualifying ratios. A significant decline in income is not acceptable, even if the current income and debt ratios meet HUD guidelines.

(1) Business Types for Self-Employed Borrowers

Sole Proprietorships: the total net profit of the business with depreciation or depletion added back to the adjusted gross income.

Partnerships: the amount of the draw or bonus taken from the capital account plus the borrower's share of the net profit.

Corporations: the amount of wages or salary as shown on the W-2 plus any bonus or other compensation, deducting any spousal income.

1.05.05 Rental Income

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

1.05.05.01 Rental Income Received from the Subject Property

FCM 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. Required

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

(1) 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 underwriter 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.

Calculation of Effective 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 underwriter must use the lesser of:

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

(2) History of Rental Income

Where the Borrower has a history of Rental Income from the subject since the previous tax filing, the underwriter 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 underwriter must document the date of acquisition by providing the deed, Settlement Statement or similar legal document.

Calculation of Effective Income The underwriter 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 underwriter must annualize the Rental Income for the length of time the Property has been owned. The underwriter must add the net subject property Rental Income to the Borrower's gross income. The underwriter may not reduce the Borrower's total Mortgage Payment by the net subject property Rental Income.

1.05.05.02 Rental Income from Other Real Estate Holdings

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 underwriter 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.

(1) 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, FCM 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 underwriter 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 underwriter 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.

Calculation of Effective Income: 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 underwriter 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.

(2) History of Rental Income

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

Calculation of Effective Net Rental Income: The underwriter 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 underwriter 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 underwriter must document the date of acquisition by providing the deed, Settlement Statement 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.

1.05.06 Other Types of Income

1.05.06.01 Alimony, Child Support or Separate Maintenance

Alimony, Child Support, or Maintenance income may be documented by obtaining the appropriate master document and evidence of payment history as listed below:

Master Document	Evidence of Payments and Effective Income
Final Divorce Decree/Parenting Plan	3 months cancelled checks, deposit slips or bank statements showing ACH deposits
Legal Separation Agreement	3 months cancelled checks, deposit slips or bank statements showing ACH deposits
Court Order	3 months cancelled checks, deposit slips or bank statements showing ACH deposits
Voluntary Payment Agreement	12 months cancelled checks, deposit slips or bank statements showing ACH deposits

To be considered effective income:

Final Divorce Decree/Legal Separation/Court Order: borrower must have consistently received the amount used for qualifying for the most recent 3 months

Voluntary Payment Agreement: borrower must have consistently received the amount used for qualifying for the most recent 6 months. If the income has not been consistently received, a 2 year average must be documented and used; if the income has been received for less than 2 years, the average must be used from when the income started.

In all cases above, the documentation must show that the payments will continue for the first 3 years of the mortgage. Non-taxable child support income may be grossed up under the same provisions as other non-taxable sources.

1.05.06.02 Capital Gains

Capital gains or losses generally occur only one time, and should not be considered when determining effective income.

However, if the individual has a constant turnover of assets resulting in gains or losses, the capital gain or loss must be considered when determining the income. Two 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.

The lender must document anticipated continuation of income through verified assets.

Example: A lender can consider the capital gains as income for an individual who purchases old houses, remodels them, and sells them for profit.

1.05.06.03 Car Allowances

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

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

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

1.05.06.04 Employer Differential Payments

If the employer subsidizes a borrower's mortgage payment through direct payments, the amount:

- Is considered gross income, and
- Cannot be used to offset the mortgage payment directly, even if the employer pays the servicing lender directly.

1.05.06.05 Employment by Family-Owned Business

In addition to normal employment verification, a borrower employed by a family-owned business is required to provide evidence that he/she is not an owner of the business. This evidence may include one of the following:

- a copy Federal personal tax returns, and/or
- a signed copy of the Federal corporate tax return showing ownership percentages (usually evidenced on the Schedule K-1), if applicable

1.05.06.06 Government Assistance Programs

Government assistance in the form of workman's compensation, welfare programs, payments for foster children, unemployment income, etc. may be used to qualify the borrower.

- Documentation must be provided from the agency paying benefits to verify that the benefits are likely to continue for at least three years after closing. If continuance of such income is not expected for three years, it may be considered as a compensating factor.
- Past receipt of unemployment income must be documented for two years. Reasonable assurance of its continuance is also required. This applies to individuals employed on a seasonal basis, such as farm workers, resort employees, etc.

1.05.06.07 Interest and Dividend Income

Interest and Dividend Income are acceptable sources of income subject to the following conditions:

- Evidence required showing that the borrower still owns the assets generating the income used to qualify.
- Interest and dividend income must be documented as received for the past two years.
- A two year average is required to use such income to qualify for the mortgage.
- Two years Federal tax returns or account statements must be provided. Funds used for down payment and/or closing costs must be subtracted before the interest is calculated.
- Income cannot be counted if the borrower is using the interest-bearing or dividend-producing asset as the source of the down payment or closing costs.

1.05.06.08 Long-Term Disability Income

Long-term disability income applies to income received from long-term disability insurance or benefits and does not include income received from the Social Security Administration. Long-Term Disability income must be verified from the third-party source (insurance company, employer, or other qualified disinterested party) to determine:

- The borrower's current eligibility for the disability benefits,
- The amount and frequency of the disability payments, and
- If there is a contractually established termination or modification date.

Generally, long-term disability will not have a defined expiration date and must be expected to continue. The requirement for re-evaluation of benefits is not considered a defined expiration date.

If a borrower is currently receiving short-term disability payments that will decrease to a lesser amount within the next three years because they are being converted to long-term benefits, the amount of the long-term benefits must be used as income to qualify the borrower.

Non-taxable disability income may be grossed up under the same provisions as other non-taxable sources.

1.05.06.09 Military Income

In addition to base pay, military personnel may be entitled to additional forms of pay provided its continuance is verified in writing:

- flight or hazard pay,
- BAS, Basic Allowance for subsistence (rations),
- clothing allowance,
- proficiency pay, and
- BAH, Basic Allowance for housing.

Allowances are non-taxable may be grossed up under the same provisions as other non-taxable sources.

Additional pay, such as pro-pay, hazard pay, etc. is taxable and may not be grossed up.

1.05.06.10 Overtime, Bonus & Tip

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

Periods of Overtime, Bonus or Tip Income less than two years may be considered Effective Income if it can be documented that the Overtime, Bonus or Tip Income has been consistently earned over a period of not less than one year and is reasonably likely to continue

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

- the average Overtime, Bonus or Tip Income earned over the previous two years or, if less than two years, the length of time Overtime, Bonus or Tip Income has been earned; or
- the average Overtime, Bonus or Tip Income earned over the previous year
- A full VOE showing the probability of continuance is required.

1.05.06.11 Commission Income

Commission income may be considered effective income if received for at least one year in the same or similar line of work (job) and it is documented that it is likely to continue.

Calculation should be based on the lesser of:

- The average net Commission income earned over the previous 2 years or length of time commission income has been earned OR
- The average net commission income earned over the previous year

1.05.06.12 New Employment

Income from a new job the borrower has already started must be documented with a paystub and a written Verification of Employment. Documentation for the previous 2-year history of employment follows standard documentation requirements.

1.05.06.13 Expected Income

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. Expected Income may be considered effective income except when expected income is to be derived from a family-owned business or an interested party to the transaction.

The amount of expected Income must be documented with the employer in writing and that it is guaranteed to begin within 60 Days of mortgage closing. The borrower should supply an offer letter with a salary and a start date. The letter must not be subject to conditions.

For expected Retirement Income, the amount and start date within 60 days must be verified in writing through an awards letter or benefits letter.

Income is calculated in accordance with the standards for the type of income being received. 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 must be documented.

A final Verbal VOE must be completed confirming start date is still valid prior to closing.

1.05.06.14 Part-Time/Second Job Income

Part-Time employment refers to employment that is NOT the borrower's primary employment and generally is less than 40 hours per week. It may be considered effective if the borrower has worked a part-time job uninterrupted for the prior two years and continuance is likely.

Calculation: Income must be averaged over the previous 2 years. If an increase in pay rate can be documented a 12 month average of hours at the current pay rate may be used.

1.05.06.15 Seasonal Employment Income

Seasonal employment refers to employment that is not year-round and is not dependent on the number of hours per week the borrower works on the job. In order to be considered effective, the seasonal income must have been received for the prior 2 years and continuance is likely.

Calculation: Income must be averaged over the previous 2 full years.

1.05.06.16 Retirement Income

Retirement income refers to income derived from a privately-held retirement account or an employer-sponsored pension. For information on Social Security Retirement Income please refer to that particular section.

Retirement must be verified from the third-party source (former employer) or from the most recent two years' Federal tax returns. The income must continue for at least three years after closing; otherwise, it will be used only as a compensating factor.

If the income is paid in the form of a monthly distribution from a 401(k), IRA, or Keogh retirement account, determine whether the income is expected to continue for at least three years after the date of the mortgage application. In addition, the borrower must have unrestricted access without penalty to the accounts and if the assets are in the form of stocks, bonds, or mutual funds, 70% of the value must be used to determine the number of distributions remaining to account for the volatile nature of these assets.

1.05.06.17 Section 8 Home Ownership Vouchers

A monthly subsidy may be treated as income if a borrower is receiving subsidies under the housing choice voucher home ownership option from a public Housing Agency. Continuation of the home ownership voucher subsidy beyond the first year is subject to Congressional appropriation, however, FHA has agreed that it will assume, for the purposes of underwriting, that the subsidy will continue for at least three years.

Procedures for loan applications where the homebuyer receives a monthly homeownership assistance payment under the housing choice voucher homeownership program (Section 8) are shown below.

- The homeownership assistance payment must be paid directly to the homeowner/borrower.
- The amount of the non-taxable subsidy that is received directly by the homeowner may be grossed up by 25% and added to the borrower's income from employment and/or other sources in calculating the qualifying ratios.

- All Section 8 subsidized mortgage loans must have “88” entered as the program identification code in FHA Connection.

Note: Although HUD allows the homeownership assistance payments to be made directly to the servicing lender to offset the mortgage payment, First Community Mortgage is unable to facilitate the procedure for receiving or allocating these funds. Therefore, the requirements shown above must be adhered to for eligibility purposes, without exception.

1.05.06.18 Social Security Income

ALL income from the Social Security Administration (SSA) including, but not limited to Supplemental Security Income (SSI), Social Security Disability Insurance (SSDI), and Social Security Income can be used to qualify the borrower if the income has been verified, and is likely to continue for at least a three-year period from the date of mortgage application. This income can be documented by 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 “Benefit Letter” that
- evidences income from SSA (Please visit www.ssa.gov for an explanation of types of letters issued by the SSA): or
- A copy of the borrower’s Social Security Benefit Statement, SSA-1099/1042S.

In addition to verification of income, the lender must document the continuance of this income by obtaining from the borrower

- a copy of the last Notice of Award letter which states the SSA’s determination on the borrower’s eligibility for SSA income, or
- 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 mortgage application, that income may *only* be considered as a compensating factor.

If the Notice of Award or equivalent document does not have a defined expiration date, the income shall be considered effective and likely to continue. Additional documentation should not be requested from the borrower to demonstrate continuance of Social Security Administration income. Under no circumstance may originators inquire into or request documentation concerning the nature of the disability or the medical condition of the borrower.

Note: Pending or current re-evaluation of medical eligibility for benefit payments is not considered an indication that the benefit payment is not likely to continue.

Note: An initial Notice of Award letter (or its equivalent) may specify a start date for receipt of income in the future. Income may be considered as effective income as of the start date specified in the Notice of Award Letter. The borrower must have other income to qualify for the mortgage until the start date for receipt of income.

Note: Other forms of long-term disability income (such as worker's compensation or private insurance) may be considered qualifying income with a reasonable expectation of continuance. Lenders should use procedures similar to those noted above to verify such income

1.05.06.19 Trust Income

A copy of the Trust Agreement or the Trustee's statement confirming the amount, frequency and duration of payments must be provided.

- The income must continue for at least three years after closing.
- Lump sum distributions made before loan closing may be used for down payment or closing costs if they are verified by a copy of the check or the Trustee's letter that shows the distribution amount. If a distribution was made that reduces the Trust income, the reduction must be taken into consideration in computing the income.

1.05.06.20 VA Benefits

Income received in the form of VA benefits must be documented by a letter or distribution form from the Veterans Administration.

- Education benefits are not acceptable income, as it offsets education expenses

1.05.07 Non-Taxable Income

Non-taxable income (or any portion of) may be "grossed-up" by using the greater of 15% or the tax rate based on the borrower's tax rate for the previous year. If the borrower is not required to file a federal income tax return, the tax rate to use is fifteen percent (15.00%).

1.05.08 Temporary Leave/Short Term Disability

Temporary leave from an employer may encompass various circumstances (e.g., family and medical, short-term disability, maternity, other temporary leaves with or without pay). Temporary leave is generally short in duration. The period of time that a borrower is on temporary leave may be determined by various factors such as applicable law, employer policies and short-term insurance policy and/or benefit terms. Leave ceases being considered temporary when the borrower does not intend to return to the current employer or does not have a commitment from the current employer to return to employment. A loan should not be denied specifically because a borrower is on temporary leave or short-term disability.

1.05.08.01 Documentation Requirements for Temporary Leave/Short Term Disability

Documentation must be provided from the current employer confirming the following:

- Borrower's statutory right to return to work (or the employer's commitment to permit the borrower to return to work) and
- Borrower's confirmed date of return, and
- Borrower's post-leave employment and income and
- Written statement signed by the borrower confirming that the borrower will return to current employer and stating the confirmed date of return that has been agreed upon between the borrower and the employer.

In addition, if the borrower is returning to the current employer AFTER the first mortgage payment is due the following additional documentation is required:

- Documentation evidencing amount, duration and consistency of all temporary leave income sources being used to qualify the borrower (e.g., short-term disability benefits or insurance, sick leave benefits, temporarily reduced income from employer) that are being received during the temporary leave and
- All available liquid assets used to supplement the reduced income for the duration of the temporary leave must meet the requirements found below and be verified and
- Written rationale explaining the analysis used to determine the qualifying income.

1.05.08.02 Determining Qualifying Income for Temporary Leave/Short Term Disability

(1) Borrowers returning to their current employer PRIOR to the first mortgage payment due date:

Qualifying income from the borrower's gross monthly income amount that will be received upon the borrower's return to the current employer may be used.

(2) Borrowers returning to their current employer AFTER the first mortgage payment due date:

Qualifying income used must be the lesser of the qualifying income amount that will be received upon the borrower's return to the current employer or the borrower's gross monthly income being received for the duration of the temporary leave. In the event that the income has been reduced or interrupted, available liquid assets may be used as a partial or complete income supplement up to the amount of the income reduction.

Assets that are required for the transaction (e.g., down payment, Closing Costs, Financing Costs, Prepaids/Escrows and reserves) may not be considered as available assets in determining the supplemental income amount.

Total qualifying income = lesser of (supplemental income + temporary leave income) or (qualifying income received after borrower's return to work)

Supplemental income = available liquid reserves divided by the number of months from the first mortgage payment due date to the date the borrower will begin receiving his or her regular employment income, rounded up to the next whole number.

1.05.09 Income Types Not Addressed

Income types not specifically addressed in this guide will be evaluated on a case-by-case basis by underwriting management.

1.05.10 Unacceptable Sources of Income

The following types of income are unacceptable for qualifying purposes:

- Trailing Spouse Income
- Education Benefits
- Per Diem Income
- Gambling Income
- Temporary Income
- Temporary Leave Income
- Short-Term Disability Income
- Non-verifiable Income
- Unstable Income
- Projected Income
- Reverse Mortgage Income
- Income from Foreign Employers not included on US Federal Tax Returns
- Mortgage Credit Certificate Income: Mortgage credit certificates may be included in the file for the borrower's tax benefit – but may not be included in qualifying income.

1.05.11 4506-T Requirements

A fully executed IRS Form 4506-T must be included in all loan files.

1.05.12 IRS Tax Transcript Requirements

Transcripts may be ordered according to the income received by the borrower:

Income Type	Transcript Type
Borrower is qualified based on W-2 income (Salary, Bonus, Overtime and Commission less than 25%). Borrower has no rental income, alimony or other evidence taxes would be required to accurately assess income or liabilities.	NONE
1099 Income for Pension or Social Security Income	NONE
Income inclusive of Commission greater than 25%	Full IRS 1040 Transcripts
Self Employed Income (Schedule C, K-1, W-2 where borrower owns more than 25%)	Full IRS 1040 Transcripts
Rental Income Capital Gains Dividend Income	Full IRS 1040 Transcripts

If tax transcripts are obtained the borrower is not required to sign the tax returns.

Tax Transcript requirements can change based on the application date and whether an extension has been filed.

Note that Tax Transcripts are not an adequate substitute for Tax Return Schedules and should only be used to support the validity of the actual Tax Returns. In instances in these guidelines where it is specified that Tax Returns are required, actual Tax Returns including all schedules should be provided.

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1.05.12.01 Documentation requirements for Self-Employed income when an extension has been filed:

Self Employed borrowers will need P&L 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 – with no exceptions.

Additionally, if income used to qualify self-employed borrower exceeds a two-year average, an audited Profit and Loss Statement or signed quarterly tax returns obtained from the IRS are required. Additional requirements are determined by the application date.

Application Date between Jan 1st – June 14th:

- Most recent year(s) available tax transcripts for the number of years required
- Prior calendar year W-2s for a corporation

- Prior calendar year 1099s for commission income
- After April 17th, copy of filed extension for prior calendar year with any tax payment made, if applicable. Must also have IRS notification of "no record found"

Application Date between June 15th to October 14th:

- Most recent year(s) available tax transcripts for the number of years required
- Copy of the filed extension for the prior calendar year with any tax payments made
- Prior calendar year year-end profit and loss statement
- IRS notification of "no record found" for prior calendar year
- Prior calendar year W-2s for corporations
- Prior calendar year 1099s for commission income

Application Date between October 15th to November 14th:

- Most recent year(s) available tax transcripts for the number of years required
- Copy of the filed extension for prior calendar year with any tax payments made
- Copy of the prior calendar year tax returns
- IRS notification of "no record found" for prior calendar year

Application Date after November 15th:

- Most recent year(s) available tax transcripts for the number of years required
- Copy of the filed extension for prior calendar year with any tax payments made
- Copy of the prior calendar year tax returns
- Transcripts from the IRS to verify the prior calendar year tax returns (regardless of the type of income used to qualify)

1.05.12.02 Documentation requirements for Self-Employed income when tax returns have been filed

Application Date between Jan 1st – June 14th:

- Most recent year(s) available tax transcripts for the number of years required by AUS
- Copy of the prior calendar year tax returns
- Must have IRS transcripts of prior calendar year tax returns if using income to qualify

Application date on and after June 15th:

- Must have IRS transcripts of prior calendar year tax returns

1.05.12.03 SSN Misuse For Tax Filing Purposes

IRS tax transcripts may not match loan documentation due a borrower's SSN being used fraudulently by another individual for tax filing purposes.

If IRS tax transcripts cannot be obtained or do not agree with income documentation, FCM advises the following action steps:

- Obtain 6C Record of Account
- Obtain and execute a Social Security Consent form to validate the borrower's SSN.
- If the borrower is a wage earner, order W-2s transcripts from the IRS to support the income documentation received. If there is 1099 income, order the 1099 transcripts.
- If the borrower is a non-wage earner, request prior year 1040s to compare against current income documentation received. This is used to see if the borrower's current income is consistent with the prior year. If the borrower's SSN misuse has occurred over multiple tax filing years, this action step will not work.
- The borrower should be advised that there is a discrepancy with their tax information and the IRS. Once the borrower has gone to the IRS documentation should be requested. The IRS or a tax advocate will issue a letter acknowledging the case and at that point the IRS will most likely explain to them they have been a victim of identity theft. This letter must be validated by the party which completed it. There is usually a contact phone number in the letter. The phone number should be reverse searched prior to calling to verify the number goes to the IRS or tax advocate.
- The IRS should confirm that revised returns are not being accepted for the borrower until the conclusion of the identity theft case. If the IRS is accepting the borrowers' modified tax returns then a copy of the revised returns, stamped by the IRS, should be provided in addition to the information outlined above.

It should be noted that FCM must still have a reasonable and verifiable justification for all income calculations used to determine the final qualifying income. If sufficient valid documentation is not available and an income determination cannot be made the income may not be used to qualify the borrower.

1.05.13 Amended Tax Returns

For Borrowers who have recently amended their tax returns, the following will apply:

- If the borrower qualified based on the original return filed and/or the amendment was clerical in nature the income is acceptable on the amended tax returns.

OR

- If the borrower would not have qualified based on the original return filed and the income increased such that the borrower will qualify based on amendment, the borrower must wait 6 months prior to loan application from the date of the amendment.

1.06 Assets & Reserves

All assets entered in DU or LP must be verified regardless of their use as cash to close or to fulfill reserve requirements.

- Reserves are defined as:
  - The sum of verified and documented borrower funds;
    minus
  - The sum the borrower is required to pay at closing, including the cash investment, closing costs, prepaid expenses, any payoffs that are a condition of loan approval and any other expense required to close the loan;
- Items not to be included in reserves:
  - Cash back as a result from a cash out transaction
  - Incidental cash back from settlement of other loan transactions
  - Gift funds in excess of the amount required for the cash investment
  - Equity in another property
  - Borrowed funds from any other source

1.06.01 Cash on Hand

Cash on hand is not an acceptable source of funds for reserves or closing costs.

1.06.02 Checking and Savings Accounts and Certificates of Deposit

Checking, Savings, and Certificate of Deposits must be verified with one of the following:

- Verification of Deposit (VOD) and the borrower's most recent statement for each account
  OR
- A statement showing the previous month's ending balance for the most recent month, If the previous month's balance is not shown, statements covering 2 months most be obtained.
  OR
- Most recent quarterly statement, if received quarterly
  OR
- Online printouts covering 60 days must show all of the information on a normal bank statement as well as the http web address at the bottom or top of the page.

OR

- direct verification by a TPV vendor of the Borrower's account covering activity for a minimum of the most recent available month, subject to the following requirements:
  - the Borrower has authorized the Mortgagee to use a TPV vendor to verify assets; and
  - the date of the data contained in the completed verification is current within 30 days of the date of the verification.

In addition to cash to close and required reserves, bank statements will be reviewed for undisclosed debt, overdraft/nsf activity and large deposits. Any indication of undisclosed debt (ie. IRS Tax payments, child support/alimony) will require documentation and explanation of the payments made on the bank statement. Overdraft/NSF activity can be an indicator of financial mismanagement and credit risk; Overdrafts/NSF activity may require explanation and if severe, could warrant a decline. See the Large Deposit section for documentation requirements.

Bank Statements are required to contain, at a minimum, the following information:

- Account Number
- Account Holder Name
- Account Holder Address
- Beginning and Ending Balance
- All pages
- Blacked-out information is not acceptable
- Bank printouts must cover at least 60 days and must be signed and stamped by a Bank Representative.

Note that when the account is held jointly by any non-borrowing party, including a non-borrowing spouse, a letter from the non-borrowing party must be provided which states the borrower has 100% unrestricted access to the account.

1.06.03 Stocks, Bonds, and Mutual Funds

Stocks, Bonds, and Mutual Funds must be verified with all of the following:

- The most recent monthly or quarterly statement provided by the stockbroker or financial institution managing the portfolio to verify the value of stocks and bonds.
- The borrower's actual receipt of funds must be verified and documented.

Note: If the loan receives an Accept/Approve recommendation, proof of liquidation is not necessary.

1.06.04 Retirement Accounts (Employer Held)

Retirement funds must be verified with all of the following:

- Copy of the most recent retirement account statement.
- Evidence that the account allows for withdrawals for conditions other than those related to the borrower's employment or death.
- Evidence of liquidation is required if the funds are being used for down payment or closing costs.

When calculating the asset value of retirement accounts, 60% of the borrower's vested interest in the account may be used unless the borrower provides documentation that a higher percentage may be withdrawn after subtracting any federal income tax and withdrawal penalties.

Any outstanding loans on the retirement account must be subtracted from the principal balance before using them as an asset.

1.06.05 Retirement Accounts (Privately Held)

Retirement funds must be verified with all of the following:

- Copy of the most recent retirement account statement.
- Evidence of liquidation is required if the funds are being used for down payment or closing costs.

When calculating the asset value of retirement accounts, 60% of the value of the account may be used unless the borrower provides documentation that a higher percentage may be withdrawn after subtracting any federal income tax and withdrawal penalties.

1.06.06 Gift Funds

1.06.06.01 Overview

Gift funds from an eligible donor may be used for 100% of the borrower's closing costs and down payment. Gift funds may not be used as reserves. Gift funds in excess of the required amount to close cannot be used as reserves. A sample gift letter can be found by clicking the hyperlink. The source of the donor's gift funds must be verifiable.

1.06.06.02 Eligible Donors

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.

The gift funds may not be provided, either directly or indirectly, by a person or entity with an interest in the transaction, such as a realtor, seller, or builder. Gifts from these entities are considered inducements to purchase and must be subtracted from the contract sales price.

If a gift is being provided by a nonprofit, government entity or other business entity, the following is required:

- Employer Identification Number (EIN) must be noted in the appropriate line(s) of the "Mortgage Information" section of the FHA Loan Underwriting and Transmittal Summary (HUD-92900-LT).
- The correct provider box must be marked below the space where the EIN is entered.
- When the "Other" box is marked as the provider of secondary financing, the type of provider (i.e. employer, labor union) must also be identified.

1.06.06.03 Documentation Requirements

The following documentation is required to document gift funds:

Gift Funds have been verified in Borrower's Account:

- Gift Letter meeting requirements below
- Donor's Bank Statement showing the withdrawal
- Evidence of the deposit into Borrower's account (updated statement)

Gift funds are not verified in borrower's account (at closing):

- Gift Letter meeting requirements below
- Obtain Certified Check, Money Order, Wire Transfer or Official Check evidencing payment to the borrower or settlement agent
- Copy of Donor's Bank Statement evidencing sufficient funds for the amount of the gift

- A gift letter with donor's and borrower's signature that specifically states the following information:
  - The donor's name, address, telephone number, and relationship to the borrower
  - The exact dollar amount of the gift funds
  - The address of the subject property
  - No repayment is necessary

- The donor's signature
- The statement: "Our signatures above indicate that we fully understand that it is a Federal Crime punishable by fine, imprisonment, or both to knowingly make any false statement concerning any of the above facts as applicable under the provision of Title 18, United States Code, Section 1012 and 1014."

1.06.07 Gift of Equity

Only family members may provide equity credit as a gift on a property being sold to other family members.

The equity credit must be reflected on the HUD-1 and all other stipulations regarding gift funds must be satisfied. Please see the aforementioned Gift Funds and Identity of Interest sections for more information.

1.06.08 Trade Equity

The borrower may agree to trade his/her real property to the seller as part of the cash investment. 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.

In order to establish the property value an independently ordered appraisal is required along with documentation confirming the certification of independence. In addition, the borrower must provide evidence of ownership.

1.06.09 Proceeds from the Sale of Property

Proceeds from the sale of other property may be used to fulfill cash to close requirements if the sale occurs on or before the closing of the subject loan transaction.

The borrower must provide verification and documentation of the actual sale and the net sale proceeds by obtaining a fully executed Closing Disclosure, it must be signed by the borrower/owner even if it was not signed at the time of closing. Dating at the time of submission to FCM is acceptable as certification the document is accurate.

FCM must also verify and document that the transaction was arms-length, and that the Borrower is entitled to the net sale proceeds.

1.06.10 Borrowed Funds

Borrowed funds may only be used to fulfill cash to close and down payment requirements if satisfactory evidence is provided that the funds are fully secured by financial institution investment accounts (bitcoin is ineligible) or real property (real estate) and the borrower can qualify with the repayment. This payment must be included in the borrower's debt ratio.

Loans secured by automobiles, recreational vehicles, furniture and other household goods are not an acceptable source of funds.

1.06.11 Earnest Money Deposit

The earnest money deposit amount and source of funds must be verified if it exceeds 1 percent of the sales price or is excessive based on the borrower's savings ability. The following documentation is required in order to document earnest money:

- A copy of the canceled check (front and back).
- Certification from the deposit holder acknowledging receipt of the funds; or
- A VOD or bank statement reflecting showing that the average balance was sufficient to cover the amount of EM at the time of the deposit.
- direct electronic verification by a TPV vendor, subject to the following requirements:
  - the Borrower has authorized the Mortgagee to verify assets;
  - the date of the completed verification conforms with FHA requirements in Maximum Age of Mortgage Documents; and
  - the information shows that the average balance was sufficient to cover the amount of the earnest money deposit at the time of the deposit.

1.06.12 Contributions by Interested Parties

Sellers or other interested third parties such as real estate agents, builders, developers, sellers, Mortgagees, Third Party Originators or other parties with an interest in the transaction may contribute up to a total of 6% of the sales price towards actual closing costs, prepaid expenses, discount points and other financing concessions allowable by HUD.

Contributions from these parties in excess of 6% of the sales price are treated as inducements to purchase and must be subtracted from the sales price.

Premium Pricing refers to the aggregate credits from a Mortgagee or TPO at the interest rate chosen. Premium Pricing may be used to pay a Borrower's actual closing costs and prepaid items. Premium Pricing is not included as part of the Interested Party limitation unless the Mortgagee or TPO is the property seller, real estate agent, builder or developer.

Items typically paid by the seller are not considered contributions. Examples of these items are; real estate commissions, pest inspections, and fees paid to release a deed of trust.

1.06.13 Down Payment Assistance

Seller-Funded Down Payment Assistance is not permitted. Currently FCM accepts a variety of FHA approved down payment assistance programs. These programs can be found on the FCM Knowledge Center State Housing and DPA Program Resource Tab. Other FHA approved DPA programs may be acceptable with prior underwriting approval. FCM's Welcome Home funds may be used in conjunction with one other Down Payment Assistance Program.

1.06.14 Ineligible Funds

All of the following are unacceptable source of funds:

- Foreign Assets
- Unsecured Borrowed Funds
- Seller Funded Down Payment Assistance
- Sweat Equity
- Undocumented funds
- Cash on hand
- Illegally obtained funds

1.06.15 Large Deposits

A large deposit is defined as any single deposit non-payroll deposits or VOD variances that represent amounts in excess of 1% of the adjusted value. All deposits exceeding this threshold are subject to explanation and source documentation. Underwriting reserves the right to request documentation on a deposit of any size if there is suspicion the funds are from an ineligible source or there is evidence deposits were structured in order to avoid documentation.

1.06.16 Reserve Requirements

Note that although there is no reserve requirement for 1-2 unit properties, cash reserves may be needed as a compensating factor in certain circumstances as determined by the underwriter.

All 3-4-unit property transactions require the borrower to have 3 months PITI reserves.

1.07 Credit

1.07.01 Credit Report Requirements

A credit report submitted with a loan application must contain all credit information available in the accessed repositories. Additionally, for each borrower responsible for the debt, the report must contain all of the information available in the credit repositories pertaining to

- credit
- residence history, and
- public records information

Note: One report is required for each borrower. The lender may obtain a joint report for individuals applying jointly.

The accepted traditional credit report is the three-repository merged credit report, also known as a "tri-merged" credit report (TRMCR).

A corrected credit report *must* supplement the TRMCR if the report *does not* verify legal actions such as bankruptcies, judgments, lawsuits, foreclosures, and tax liens.

For any open debt listed on the loan application, but not referenced on the TRMCR, credit information must be developed separately.

Incorrect Social Security Numbers and dates of birth will require a new credit report to be pulled with the correct data. Major address inconsistencies, and name extensions (Jr., III, etc.) must match throughout the file and may require a re-pulled credit report. Common shortening of names does not require a re-pulled credit report (e.g. Matt for Matthew).

1.07.02 Age of Credit Documents

- Credit reports cannot be older than 120 days from the Note Date
- Credit documents, such as income and asset documentation, cannot be older than 120 days from the Note Date subject to underwriter discretion. New Construction is limited to 120 days.

1.07.03 Credit Score Requirements

- All borrowers must have at least one valid credit score to use AUS/Traditional Credit Underwriting.
- When three scores exist, the middle of the three will be used as the qualifying credit score.

- When only two scores exist, the lower of the two will be used as the qualifying credit score.
- A borrower may have a “no score” credit report – the file may be considered for manual underwriting provided the borrower can provide non-traditional trade lines to be verified and borrower meets all manual underwriting requirements.
- Additional restrictions for credit scores between 600-639 apply:
  - AUS Approval-no manual underwrites

1.07.04 Inquiries

All credit reports used for underwriting must include all inquiries for a minimum of the most recent 120 days. Most credit reporting agencies (CRA) already contain a 120-day history, but some are limited to 90 days. If the credit inquiry history is limited to 90 days, the CRA must be contacted to update the credit report to include a full 120-day history.

Any inquiry that is found within the most recent 90 days must be addressed with a specific explanation letter from the borrower. The explanation letter must address the individual inquiry, the date, the reason for the inquiry, and the result. If a new debt was opened, the borrower must provide documentation to verify the payment and balance. The debt must then be added to the 1003, AUS and included in the DTI.

Inquires resulting from the subject mortgage application, for primary or secondary financing, do not require explanation. Should the customer have multiple applications for multiple properties an explanation will be required.

NOTE: FCM recommends the specific inquiry letter located on the FCM Knowledge Center be used to satisfy any credit inquiry explanations.

1.07.05 Maximum Debt Ratio

The maximum debt-to-income (DTI) ratio for AUS Approve/Eligible loans is determined by AUS risk assessment. Maximum Debt to Income ratio for manually underwritten loans is 43% with an underwriting exception up to 50%, acceptable compensating factors must be present.

1.07.06 Housing History

All loans must contain a 24-month history of residence. See Manual Underwriting for manually underwritten housing history verification requirements.

1.07.06.01 Purchases:

- AUS Approval - loans are ineligible if there is one or more housing delinquency that is 1x60 or greater within 12 months of the date of the credit report

- AUS Refer - loans are ineligible if there is one or more housing delinquency that is 1x30 or greater within 12 months of the date of the credit report

1.07.06.02 Rate/Term Refinances:

- Loans are ineligible if there is one or more housing delinquency that is 1x60 or greater within 12 months of the date of the credit report
- All mortgages must have been paid within the month due for the previous 12 months. In addition, the payments for all Mortgages secured by the subject Property must have been paid within the month due for the month prior to mortgage disbursement.

1.07.06.03 Cash Out Refinances:

- Loans are ineligible if there is one or more housing delinquency that is 1x30 or greater within 12 months of the date of the credit report
- All mortgages must have been paid within the month due for the previous 12 months. In addition, the payments for all Mortgages secured by the subject Property must have been paid within the month due for the month prior to mortgage disbursement.
- 6-month mortgage seasoning is required for all cash out refinances.

1.07.07 Open Charge Accounts

Open charge accounts, also known as Revolving Accounts, must have their payments included in the DTI calculation regardless of the number of payments remaining to pay off the debt.

If the credit report shows a revolving account with an outstanding balance but no specific minimum monthly payment, the payment must be calculated as the greater of:

- 5% of the outstanding balance, or
- $10

Note: If the actual monthly payment is documented from the creditor or a copy of the current statement reflecting the monthly payment is obtained, that amount may be used for qualifying purposes.

1.07.07.01 30 Day Accounts

30-day accounts may be excluded from the borrower's DTI if verification is obtained that the borrower paid the account in full every month for the prior 12 months and the borrower has verified funds in addition to MRI and Reserves to pay off the current balance.

If the account was not paid in full for the prior 12 months or a late payment in the last 12 months is indicated on the credit report, 5% of the outstanding balance must be used to calculate a payment and include in the debt-to-income ratio.

1.07.08 Lease Payments

Lease payments must be included in the borrower's recurring monthly debt obligations, regardless of the number of months remaining on the lease.

1.07.09 Alimony, Child Support or Separate Maintenance

When the borrower is required to pay alimony, child support, or maintenance payments under a divorce decree, separation agreement, or any other written legal agreement, and those payments will continue for more than ten months, the payments must be considered in the debt-to-income ratio. The alimony payments may be deducted from income or added as a monthly obligation. Child support and maintenance payments may not be deducted from income and must be added as a liability. Voluntary payments do not need to be taken into consideration.

The following is required to document the payment and the number of remaining payments:

- A copy of a written legal agreement or court decree describing the payment terms for the obligation, the amount of the award and the period of time over which it will be received **OR**
- Any applicable state law that mandates the obligation document, which must specify the conditions under which payments must be made **AND**
- Borrower's pay stubs covering no less than 28 consecutive days to verify the borrower does/does not have an order for garnishment relating to the Alimony/CS/Maintenance.

Alimony, Child Support, or Separate Maintenance debts with less than 10 remaining payments may be excluded from the borrower's debt ratio under certain circumstances. These payments may still be required by the underwriter if they deem the existing payment could have an adverse effect on the borrower's repayment ability.

Generally underwriting will require the borrower have sufficient funds in reserves to pay off the debt in full. Note that it is not a requirement to pay off this debt but the existence of reserves adds a level of assurance that the borrower's repayment ability would not be hindered by the existing debt.

1.07.10 Contingent Liabilities / Co-Signed Loans

When a borrower co-signs for a loan to enable another party (the primary obligor) to obtain credit, but is not actually repaying the debt, the borrower has a contingent liability.

The contingent liability must be included in the debt-to-income ratio, unless there is documentation to evidence the primary debtor has been making satisfactory payments for a minimum of 12 consecutive months and the account is current with no history of delinquency.

Evidence such as cancelled checks or automated savings withdrawals will be accepted.

If joint obligations are listed in the final divorce decree and/or separation agreement as being the responsibility of the ex-spouse then they can be omitted from the qualifying DTI calculation. The divorce decree or separation agreement must be finalized by the court and recorded.

Borrower is still liable for any adverse payment history or outstanding debt associated with these joint accounts that are dated prior to the divorce or separation agreement.

A debt must be included in the debt-to-income ratios if the party making the payment is not co-obligated on the loan.

1.07.11 Business Debt

When a self-employed borrower claims that a monthly obligation that appears on his or her personal credit report is being paid by the borrower's business, the lender must confirm that it verified that the obligation was actually paid out of company funds and that this was considered in its cash flow analysis of the borrower's business tax returns. A sole proprietor may not exclude business debts from personal liability if shown on their personal credit report.

The account payment does not need to be considered as part of the borrower's individual recurring monthly debt obligations if:

- the account in question does not have a history of delinquency,
- the business provides acceptable evidence that the obligation was paid out of company funds (such as 12 months of canceled company checks), and
- the lender's cash flow analysis of the business took payment of the obligation into consideration.

The account payment does need to be considered as part of the borrower's individual recurring monthly debt obligations in any of the following situations:

- The borrower's business is a sole proprietorship.
- If the business does not provide sufficient evidence that the obligation was paid out of company funds.
- If the business provides acceptable evidence of its payment of the obligation, but the lender's cash flow analysis of the business does not reflect any business expense related to the obligation (such as an interest expense—and taxes and insurance, if applicable—equal to or greater than the amount of interest that one would reasonably expect to see given the amount of financing shown on the credit report and the age of the loan). It is reasonable to assume that the obligation has not been accounted for in the cash flow analysis.

- If the account in question has a history of delinquency, to ensure that the obligation is counted only once, the lender should adjust the net income of the business by the amount.

1.07.12 Financed Properties

FCM limits the maximum number of properties financed for FHA borrowers with all lenders at four. The total maximum financed properties referenced above includes the subject property along with any other financed mortgages, conventional or government. This limitation includes joint or total ownership and is cumulative across all borrowers on the loan.

The following property types are included in the maximum number of financed properties:

- Residential properties including single-family, 2-4 units, condominium, lot, land, PUD (attached and detached), manufactured housing, row house, and townhouse.
- Residential properties that have a commercial lien against them are included.
- Residential properties that the borrowers purchased for elderly parents or a disabled child.

The following property types are excluded from the maximum number of financed properties:

- Commercial, franchises, multi-family (i.e. greater than four units), and timeshares.

In addition, borrowers may not own more than a total of seven "units". As an example, a borrower could own three 2-unit properties and still qualify but owning four 2-unit properties would exceed the unit maximum of seven.

1.07.13 Installment Debt

Installment debts with less than 10 remaining payments may be excluded from the borrower's debt ratio under certain circumstances. These payments may still be required by the underwriter if they deem the existing payment could have an adverse effect on the borrower's repayment ability.

Generally underwriting will require the borrower have sufficient funds in reserves to pay off the debt in full. Note that it is not a requirement to pay off this debt but the existence of reserves adds a level of assurance that the borrower's repayment ability would not be hindered by the existing debt.

Debts with less than 10 remaining payments may be excluded from the borrower's debt ratios and the payments do not exceed 5% of the borrower's gross monthly income. If multiple accounts are excluded, the cumulative of all excluded payments may not exceed the 5% limitation.

Installment debt which does not list a payment on the credit report must have verification of the actual payment along with the term of the loan. Using percentages of outstanding balances to determine an estimated payment is not acceptable.

1.07.13.01 IRS Installment Agreements

Borrowers with approved IRS installment agreements are eligible for financing. The installment agreement must be in writing and have a determined payment amount included in the borrower's qualifying DTI. The following documentation is required:

- Letter from IRS stating terms and approval of Installment Agreement
- Evidence 3 payments have been paid under the agreed terms
- If a payment plan was established for the prior tax year and it is not a tax lien, 3 months payment verification is not required.
- If the payment plan is established to pay an existing recorded IRS lien, 3 months will be required.

1.07.14 Deferred Installment Debt

All deferred installment debt (student and non-student) must be included in the borrower's DTI regardless of length of deferment.

Non-Student Installment Debt

The actual verified monthly payment may be used in qualifying. If a payment cannot be verified, 5% of the outstanding balance must be used as a payment for qualifying purposes.

Student Installment Debt

All Student Loans must be included in the Borrower's liabilities, regardless of the payment type or status of payments. Regardless of payment status, the borrower's payment will be calculated as:

- the greater of:
  - 1% 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 over the loan term.

1.07.15 "Paying Down" Accounts

Paying down debt to qualify for the loan is not acceptable.

Paying off debt at or prior to closing, either installment or revolving, is acceptable if:

- Funds used to pay off the debt are documented, sourced, and received from either the borrower's own funds or other acceptable party.
- Revolving accounts paid to zero are not required to be closed.

1.07.16 Loans Secured by Liquid Assets

Payments on a loan secured by liquid assets (i.e., 401k/IRA accounts, CDs, stocks, bonds, marketable securities, etc.) may be excluded from the DTI.

1.07.17 Disputed Accounts

Applications with credit reports showing less than $1000 in disputed derogatory accounts do not require manual downgrade and can follow FHA Total Scorecard recommendation. Medical accounts and non-derogatory accounts are not included in the $1000 limit. Disputed accounts with outstanding balances must include a payment and the payment must be included in the borrower's DTI.

Derogatory Accounts: disputed accounts that are Charge off accounts, collections accounts and accounts with late payments in the last 24 months.

Non-Derogatory Accounts: disputed accounts with zero balance, with late payments aged 24 months or greater and accounts that are current and paid as agreed.

1.07.18 Past Due Accounts

For loans receiving a TOTAL Scorecard Accept/Approve, delinquencies on consumer credit accounts is evaluated by the AUS system. The underwriter must still take these delinquencies into consideration when evaluating the entire file as a whole.

Past due or delinquencies within the previous 12 months on consumer credit accounts are generally not permitted on manually underwritten files.

Note that Collection accounts and Past Due accounts are two separate classifications of debt. A collection account, by definition, is always past due and follows specific guidance found in the Collection/Charge-offs section below instead of the Past Due Account section.

1.07.19 Collections/Charge-offs

If	And	Then
The Automated Underwriting System using the TOTAL Mortgage Scorecard rates the mortgage as an Accept,	The cumulative outstanding balance of all collections of all borrowers is less than $2,000	The lender is not required to consider or evaluate collection accounts.
	The cumulative outstanding balance of all collections of all borrowers is equal to or greater than $2,000	The lender must include monthly payments in the borrower's debt-to-income ratio based on written

		payment agreement letters provided by the creditor including documentation which indicates that payments have been made according to the agreement for all accounts that will remain open subsequent to closing. If evidence of a payment arrangement is not available, 5% of the outstanding balance of each collection can be used to calculate the monthly payment.

Note: Medical collections and charge offs are excluded from this guidance. Non-Medical charge offs are also excluded from this guidance unless they have been sent to collection or disputed per the credit report. If disputed, follow the disputed guidelines.

1.07.20 Outstanding Federally Insured or Guaranteed Debt

A borrower is not eligible for a HUD insured loan if they have any outstanding Federal debt until the delinquent account is brought current, paid, or satisfied.

Federal debts include direct loans, HUD-insured mortgage loans, VA-insured mortgages, student loans, Small Business Administration loans, or judgments/liens against property for a debt owed the Federal Government.

The only exception to the above guidelines are for Federal IRS Tax Liens against the property where the IRS has agreed to subordinate the lien.

Prior Federal defaults or claims must be documented with:

- A letter of explanation from the borrower regarding the circumstances surrounding the default or claim.
- A letter on letterhead from the affected agency, signed by an officer and stating that the delinquent debt is now current, paid, or that a satisfactory agreement for repayment has been reached.
- Underwriter or Processor’s reason for recommendation of the borrower

1.07.21 Judgments/Liens

All judgments, garnishments and/or liens must be paid in full at or prior to closing for purchase and cash out transactions. For rate/term refinance transactions the debt must be paid prior to closing.

Documentation of payoff must be provided and a letter of explanation from the borrower is required.

Exceptions can be made on a case by case basis if the borrower has been making regular and timely payments on the judgment and the creditor is willing to subordinate that judgment to the insured first lien mortgage. (Federal tax liens must be subordinate to the FHA-insured Mortgage)

1.07.22 Chapter 7 Bankruptcy

Loans where the borrower has field Chapter 7 bankruptcy which was discharged within the previous 2 years require manual downgrade and must be underwritten manually. In all instances:

- The borrower must have re-established good credit since the bankruptcy or chosen not to incur new credit obligations, and
- The borrower must document that their situation and the events that led to the bankruptcy are not likely to reoccur.
- If the bankruptcy included a mortgage that was not re-affirmed in bankruptcy it will be treated as a foreclosure, date of deed transfer will be used to determine eligibility, please refer to section 1.07.27 Foreclosures to determine eligibility.

In ALL manual underwrite cases and some AUS-approved cases the following documentation is required:

- Copy of the bankruptcy petition
- Schedule of Debts and Discharge
- Written explanation from the borrower

The Discharge date and AUS findings both play an important role in determining the viability and future repayment of the new loan. As such, the following timeline requirements must be met regardless of AUS findings:

- Chapter 7 bankruptcy discharged more than 24 months prior to the application date may be allowed.
- Chapter 7 bankruptcy discharged between 12 and 24 months prior to the application date requires satisfactorily established credit and documentation showing the circumstances which caused the bankruptcy were beyond the borrower's control (i.e. unemployment, medical bills not covered by insurance). In these instances, the file must be manually downgraded to a refer and manually underwritten. It falls upon the underwriter to make a final determination as to the overall quality of the file.
- Chapter 7 bankruptcy discharged less than 12 months prior to the application date is not allowed.

Note that for High Balance Transactions a minimum of 3 years must have elapsed since the discharge date regardless of AUS findings. For bankruptcies which included a Foreclosure, the more restrictive requirement for foreclosures applies in that there is a 3 year waiting period from the date the claim is paid until the application date.

1.07.23 Chapter 13 Bankruptcy

Loans where the borrower is currently in a Chapter 13 bankruptcy or had a Chapter 13 bankruptcy which was discharged within the previous 2 years require manual downgrade and must be underwritten manually.

In ALL manual underwrite cases and some AUS-approved cases the following documentation is required:

- Copy of the bankruptcy petition
- Schedule of Debts and Discharge
- Written explanation from the borrower

A borrower who is currently in a Chapter 13 bankruptcy may be eligible for FHA financing provided all of the following conditions are met in addition to standard manual underwriting requirements:

- At least 12 months of payments have been made satisfactorily
- The Trustee or bankruptcy judge's approval to enter into the mortgage transaction is documented
- Bankruptcy payments are included in the borrower's debt ratio

Regardless of the current status or discharge date of the Chapter 13, all of the below requirements must be met for all files which contain a history of a Chapter 13 bankruptcy:

- The borrower must have re-established good credit since the bankruptcy or chosen not to incur new credit obligations, and
- The borrower must document that their situation and the events that led to the bankruptcy are not likely to reoccur.

Note that for High Balance Transactions a minimum of 3 years must have elapsed since the discharge date until the application date regardless of AUS findings. For bankruptcies which included a Foreclosure, the more restrictive requirement for foreclosures applies in that there is a 3 year waiting period from the date the claim is paid until the application date.

1.07.24 Consumer Credit Counseling (CCC)

Participating in a consumer credit counseling program does not disqualify a borrower from obtaining an FHA-insured mortgage. If the file receives an Accept/Approve recommendation then the borrower's decision to participate in consumer credit counseling does not trigger a requirement for additional documentation, as the credit scores already reflect the degradation in credit history. No additional explanation is necessary in this case.

However, if the file is being underwritten manually then the following documentation is required:

- 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.

1.07.25 Multiple Bankruptcy Filings

All bankruptcies must meet the requirements listed in the Chapter 7 Bankruptcy and Chapter 13 Bankruptcy sections. Generally manually underwritten loans with multiple bankruptcies are not acceptable.

1.07.26 Foreclosure

In all instances, the "date of foreclosure" is considered the date of the foreclosure deed. The end date of the timeframe is determined by the case assignment date.

The borrower's credit history since the foreclosure, the circumstances behind the foreclosure, and the foreclosure date all factor in to the final determination by the underwriter.

In all instances:

- The borrower must have re-established good credit since the foreclosure or chosen not to incur new credit obligations, and
- The borrower must document that their situation and the events that led to the foreclosure are not likely to reoccur.

In ALL manual underwrite cases and some AUS-approved cases the following documentation is required:

- Written explanation from the borrower

The foreclosure date and AUS findings both play an important role in determining the viability and future repayment of the new loan. As such, the following timeline requirements must be met regardless of AUS findings:

- A foreclosure less than 3 years ago is not allowed.

1.07.27 Deed-In-Lieu of Foreclosure

See previous Foreclosure section and follow the same guidance.

1.07.28 Short Sales

See previous Foreclosure section and follow the same guidance. It should be noted that Short Sales which were current at the time of transfer are treated the same as Short Sales which were delinquent at the time of transfer.

1.07.29 Community Property States

Purchase and refinance transactions for properties located in a Community Property State have additional underwriting and closing requirements when a non-purchasing spouse exists. The following states are Community Property states, please check Retail Standard Lending Footprint or Wholesale/NDC Lending Footprint to verify loan availability in each state:

Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin.

1.07.29.01 Underwriting Requirements

- Debts and obligations from a non-purchasing spouse must be counted in the qualifying ratios.
- Credit from a non-purchasing spouse must be reviewed in order to determine outstanding debts to be factored into the qualifying ratios.
- Non-purchasing spouse credit history and performance is not to be considered a reason for credit denial. The non-purchasing spouse's credit score is not a factor.
- The non-purchasing spouse's collections and/or judgment totals must be included in the aggregate amount when determining program-specific payoff and/or payment amounts regarding these types of accounts.
- CAIVRS is not required on the non-purchasing spouse.

1.07.29.02 Closing Requirements

ALL SPOUSES OF:	ARE REQUIRED TO SIGN THE:
• Borrowers • Non-borrowing title holders, and • Trustees	• Security Instrument • Truth In Lending Disclosure, and • Notice of Right to Cancel

1.07.30 Authorized User Accounts

Credit report trade lines designated as authorized user trade lines are automatically taken into consideration in the AUS findings. However, the underwriter is still required to review credit report trade lines which the applicant has been designated as an authorized user in order to ensure the trade lines are an accurate reflection of the borrower's credit history. If the underwriter believes the authorized user trade lines are not an accurate reflection of the borrower's credit history, the underwriter should evaluate the borrower's credit history without the benefit of these trade lines and use prudent underwriting judgment when making its final underwriting decision. In order to assist the underwriter in its review of authorized user trade lines, DU issues a message providing the name of the creditor and account number for each authorized user trade line identified.

When ensuring trade lines are an accurate reflection of the borrower's credit history, as a general rule, if the borrower has several authorized user accounts but only has a few accounts of his/her own, the following should be established:

- The relationship of the borrower to the owner of the account,
- If the borrower uses the account, and
- If the borrower makes the payments on the account.

If the authorized user trade-lines belongs to another borrower on the mortgage loan, no additional investigation is needed. On the other hand, if the borrower has several trade lines in good standing and only a minor number of authorized user accounts, the underwriter could make the determination that:

- The authorized user accounts had minimal, if any, impact on the borrower's overall credit profile; and
- The information reported on the credit report is an accurate reflection of the borrower's credit history.

The underwriter is not required to review an authorized user trade line that belongs to the borrower's spouse when the spouse is not on the mortgage transaction.

The authorized user account must be included in the borrower's DTI unless the borrower can document the primary account holder has made all required payments in the previous 12 months. If less than 3 payments have been required on the account in the past 12 months the payment amount must be included in the borrower's DTI.

1.07.31 Undisclosed/New Debt

Undisclosed or new debt (other than a mortgage obligation) not listed on the credit report and not considered in AUS must be documented accordingly:

- Payment of new debt must be verified
- Resubmission to AUS/Total is required if the monthly obligation added to the borrower's DTI is greater than $100
- If funds were received, as a result of the debt it must be verified they are not part of the borrower RMI.

1.07.32 Compensating Factors

Manually underwritten loans must document compensating factors which influence the approval of the loan. A list of common compensating factors can be found below.

- **Housing Expense Payments** – The borrower has successfully demonstrated the ability to pay housing expenses greater than or equal to the proposed monthly housing expenses for the new mortgage over the past 12-24 months.
- **Down Payment** – The borrower makes a large down payment of 10% or higher toward the purchase of the property.
- **Accumulated Savings** – The borrower has demonstrated an ability to accumulate savings and a conservative attitude toward using credit.
- **Previous Credit History** – A borrower's previous credit history shows that they have the ability to devote a greater portion of income to housing expenses.
- **Compensation or Income Not Reflected in Effective Income** – The borrower receives documented compensation or income that is not reflected in effective income, but directly affects their ability to pay the mortgage. This type of income includes food stamps and similar public benefits.
- **Minimal Housing Expense Increase** – There is only a minimal increase in the borrower's housing expense.
- **Substantial Cash Reserves** – The borrower has substantial documented cash reserves (at least three months) after closing.
- **Substantial Non-Taxable Income** – The borrower has substantial non-taxable income. (applies if no adjustment was previously made when computing debt ratios)
- **Potential for Increased Earnings** – The borrower has a potential for increased earnings, as indicated by job training or education in their profession.

1.08 Property

1.08.01 Geographical Restrictions

The FHA product at First Community Mortgage is only restricted by the most recent standard lending footprint for each division.

Retail Standard Lending Footprint

Wholesale Standard Lending Footprint

Note that additional products used in conjunction with FHA products, such as THDA or Georgia Dream, may have their own proprietary lending territories.

1.08.01.01 State-Specific Restrictions

STATE	GUIDANCE

Illinois	• The following guidelines apply for primary residence and second homes:
	  ○ Fully amortizing ARM loans will be acceptable ONLY if the following credit overlays are applied:
	    ▪ For all AUS processed fully amortizing ARMs, the greater of the product qualifying rate or the fully amortizing, fully indexed rate must be input into DU and LP as the note rate for qualifying purposes.
	    ▪ For traditionally underwritten fully amortizing ARMs, the borrower must be qualified at the greater of the product qualifying rate or the fully amortizing, fully indexed rate.

Maryland	• The following guidelines apply for primary residence and second homes:
	  ○ Fully amortizing ARM loans will be acceptable ONLY if the following credit overlays are applied:
	    ▪ For all AUS processed fully amortizing ARMs, the greater of the product qualifying rate or the fully amortizing, fully indexed rate must be input into DU and LP as the note rate for qualifying purposes.
	    ▪ For traditionally underwritten fully amortizing ARMs, the borrower must be qualified at the greater of the product qualifying rate or the fully amortizing, fully indexed rate.

Minnesota	• The following guidelines apply for primary residence and second homes:
	  ○ Fully amortizing 7/1 and 10/1 ARM loans will be acceptable ONLY if the following credit overlays are applied:
	    ▪ For all AUS processed fully amortizing 7/1 and 10/1 ARMs, the fully amortizing, fully indexed rate must be input into DU and LP as the note rate for qualifying purposes.

	• For traditionally underwritten fully amortizing 7/1 and 10/1 ARMs, the borrower must be qualified at the fully amortizing, fully indexed rate.
Texas	• Texas 50(a)(6) transactions are ineligible. • All Texas transactions require a survey.
Wisconsin	• Please see the subsequent section on Community Property States for additional restrictions in the state of Wisconsin.

1.08.02 Title Commitment

- Amount of policy may not be less than the original principal balance of the mortgage.
- Named Insured must be: First Community Mortgage, Inc., ISAOA/ATIMA
- ICL/CPL must be loan specific and include the subject property address or borrower name.
- Final Title Policy Requirements:
- ALTA standard (1990 ALTA policies are not permitted) or ALTA Expanded Coverage Residential Policy is acceptable in all states. The modified ALTA Short Form Residential loan policy approved by the State of Florida is acceptable on Florida properties only.
- ALTA Endorsement 4 (condominium) – required on all condominium properties.
- ALTA Endorsement 5 (PUD's) – required on all PUD properties.
- ALTA Endorsement 6 (ARM's) – required on all ARM transactions.
- ALTA Endorsement 8.1 (environmental hazards) – required on all properties.
- ALTA Endorsement 9 (restrictions, encroachments, minerals) – required on all properties.
- Title policy must include, as an informational note, (a) the recorded plat number(s), if any, and (b) the property parcel number(s), or tax identifying number(s), as applicable, if available.
- Any Survey Exception must be deleted.
- The legal description on the policy must conform to the legal description contained in the Security Instrument.
- Tax information including next due and amount to be included on the title commitment.
- Florida properties require Florida Endorsement Form 9 (aka ALTA 9-06) as well as a property survey. If an existing survey is being utilized a Survey Affidavit must be completed.

1.08.03 Hazard, Flood and Condo Insurance

Please see FCM's Insurance Policies and Requirements document for all insurance related information.

1.08.04 Occupancy Types

1.08.04.01 Overview

FHA loans are limited to owner-occupied principal residences only.

1.08.04.02 Primary Residence

A primary residence is defined as a property that will be occupied by the borrower for the majority of the calendar year.

At least one borrower must occupy the property and sign the security instrument and the mortgage note in order for the property to be considered owner-occupied.

FHA security instruments require a borrower to establish bona fide occupancy in a home as the borrower's principal residence within 60 days of signing the security instrument, with continued occupancy for at least one year.

When a borrower has re-occupied their existing investment property the duration of time they have re-occupied the property determines what level of financing is available:

- If the borrower has occupied the property 12 months or more prior to the loan application date of the refinancing mortgage the maximum financing is treated at the same level as an owner-occupant loans.
- If the borrower has occupied the property less than 12 months prior to the loan application date of the refinancing mortgage only a fully qualifying standard rate/term refinance is allowed and the loan-to-value cannot exceed 85%.

Generally, FHA will only insure one principal residence mortgage for any borrower. For more information regarding exceptions to this rule please see the section on Multiple FHA Loans.

1.08.04.03 Secondary Residence

A secondary residence is defined as a property that a borrower occupies in addition to his/her principal residence.

Second homes are not eligible for FHA loans at First Community Mortgage.

1.08.04.04 Investment Property

An investment property is defined as a property that is not occupied by the borrower as a principal or secondary residence.

Investment properties are not eligible for FHA loans at First Community Mortgage. Investment properties **are** allowed on FHA Streamline Mortgage transactions.

1.08.05 Property Evaluation

1.08.05.01 Eligible Properties

First Community Mortgage accepts the following property types for FHA loans:

- One-to-four family detached
- Townhomes/PUDs
- Condominiums on FHA-approved list
- Modular homes
- Manufactured Homes (see additional requirements and restrictions)

1.08.05.02 Ineligible Properties

First Community Mortgage does not accept the following property types for FHA loans:

- Co-ops
- Mixed-Use Properties
- Commercial Enterprises
- Boarding Houses
- Tourist Houses
- Private Clubs
- Bed and Breakfast Establishments
- Fraternity or Sorority Houses
- Sinkhole Homes
- Leasehold Estates
- Berm Homes
- Condo Projects not appearing on FHA Approved Project List with an unexpired approval
- Life Estate
- Working Farms
- Hotel or Motel Condominium Conversions (or conversions of other similar transient properties)
- Land Trust

1.08.05.03 Appraisal Requirements

- A full appraisal must be completed for all FHA loans (except where noted for streamline refinances without appraisals) by an FHA approved appraiser with State Certification.
- The following appraisal forms are required based on property type:

- 1 unit single family dwellings: Uniform Residential Appraisal Report (Fannie Mae Form 1004)
- 2-4 unit dwellings: Small Residential Income Property Appraisal Report (Fannie Mae Form 1025)
- Condominium units: Individual Condominium Unit Appraisal Report (Fannie Mae Form 1073)

- Appraisals on existing, proposed, and under construction properties are valid for 120 days from the date of inspection to the Note date.
- All appraisals must have an FHA case number assigned to the subject property. Case numbers are specific to the subject property and a new case number must be ordered if the borrower changes properties.
- The effective date of appraisal cannot be before the FHA case number assignment unless the appraisal was originally completed for a conventional underwrite or government guaranteed loan but was performed by an FHA Roster Appraiser and is being converted to an FHA insured mortgage.
- Legal Non-Conforming Properties: If the property is legal non-conforming, the appraiser must report that the property may be legally rebuilt in the case of total loss. If the property cannot be rebuilt, it is ineligible for FHA financing.
- All property conditions, including repairs, alterations and/or required inspections must be reported within the appropriate section of the applicable Fannie Mae appraisal reporting form. Note: FHA does not require any home to have any appliances to be eligible for FHA financing
- Underwriting reserves the right to request the Property Inspection report when mentioned in the Sales Contract but is not required to request said document unless they feel it is necessary or items are specifically mentioned in the appraisal report which would warrant a property inspection be completed.
- If the utilities are off at the time of the inspection, the Appraiser must ask to have them turned on and complete all requirements under Mechanical Components. However, if it is not feasible to have the utilities turned on, then the appraisal must be completed without the utilities turned on or the mechanical systems functioning.
- If the utilities are not on at the time of observation and the systems could not be operated, the Appraiser must: 1. render the appraisal as subject to re-observation; 2. condition the appraisal upon further observation to determine if the systems are in proper working order once the utilities are restored; and 3. complete the appraisal under the extraordinary assumption that utilities and mechanical systems, and appliances are in working order.

- Upon receipt of a completed appraisal report prepared on one of the revised Fannie Mae forms, the underwriter/processor must note any physical deficiency or adverse condition requiring repair, alteration or further inspection on *Conditional Commitment Direct Endorsement Statement of Appraised Value*
- See the New Construction, Identity of Interest, and HUD REO Purchase sections for information regarding property inspections on these types of loans.

1.08.05.04 Appraisal Extension Requirements

FHA has two different types of appraisal "extensions" for normal FHA transactions, a standard 30 day extension and an Appraisal Update And/Or Completion Report. The two are mutually exclusive, that is, can never both be used on the same file.

(1) Standard 30-Day Extension

In order to use this option all of the following conditions must be met:

- Appraisal must not be expired.
- Appraisal has not been updated using an appraisal update and/or completion report.
- Sales contract must be signed OR loan must be approved prior to expiration. Note that approval of the borrower occurs when the underwriter signs the HUD-92900-LT.

The appraisal validity period is then equal to 120 days plus an additional 30 days.

(2) Appraisal Update And/Or Completion Report

In order to use this option all of the following conditions must be met:

- Appraisal must not be expired.
- Appraisal has not been extended using the standard 30 day extension.
- Sales contract must be signed OR loan must be approved prior to expiration. Note that approval of the borrower occurs when the underwriter signs the HUD-92900-LT.

When using an Appraisal Update And/Or Completion Report the appraiser who completed the original report is responsible for completion of the update, performing an exterior inspection, researching and commenting on current market data, and determining if the value of the property has declined or stayed the same. This report extends the appraisal validity period to 120 days plus an additional 120 days.

1.08.05.05 Property Flipping

Property flipping refers to a practice whereby a recently acquired property is resold for a considerable profit with an artificially inflated value, often accomplished with the help of the appraiser. Most flipping occurs within a matter of days after acquisition and usually with only minor cosmetic improvements made to the subject property.

(1) Resale Restrictions

A purchase transaction is eligible when the current seller is the owner of record and acquired subject property at least 90 days prior to the execution of the current sales agreement. The seller's acquisition date is the date when the seller acquired legal ownership of that Property.

(2) Owner of Record

- The property must be purchased from the owner of record
- The transaction may not involve any sale or assignment of the sales contract
- Must have documentation verifying that the seller if the owner of record, which includes, but is not limited to:
  - A property sales history report
  - A copy of the recorded deed from the seller
  - A copy of the property tax bill, title commitment or binder demonstrating the seller's ownership and the date of acquisition
- The appraisal report describing the date, price and data for prior sales for the subject property within the last three years

(3) Seller Acquisition Date

- 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.
- If the appraisal report shows the most recent sales date for the subject property occurred at least one year prior to the sales contract (to include the actual acquisition date and sales price), no additional documentation is required
- If conflicting information exits, it must be resolved and documented accordingly
- Foreclosure Sales:

- If the seller purchased the property at a foreclosure sale, but the deed transferring the property was not recorded until several months later, use the date of warranty deed conveying subject property to seller as the acquisition date and document the file with an explanation.
- Obtain a copy of the seller's winning bid for the property and the other documents from the sheriff showing the property was sold to the seller at the auction.
- Example:
  - Date of foreclosure sale is April
  - Date deed recorded is July
  - Acquisition date is April

(4) Resale Within 90 Days

Properties sold 90 days or fewer following the date of acquisition by the seller, are not eligible unless, one of the following applies:

- The property is acquired by an employer or relocation agency in connection with the relocation of an employee. A relocation agency does not include individual real estate agents that advertise themselves as relocation experts and who purchase properties.
- A builder is selling a newly built home or building a home for a borrower.
- Property re-sales by HUD and other Federal agencies of their REO properties
  - Federal agencies that acquire properties as a result of a function of their programs and quickly market and sell these acquired properties. (Agencies such as the Department of Veterans Affairs (VA), the Rural Housing Service of the Department of Agriculture (Farm Home) and the Federal Deposit Insurance Corporation (FDIC)
- The transaction involves a property that has been inherited.
- The transaction involves the sale of the property by a nonprofit approved to purchase HUD-owned single-family properties at a discount with resale restriction
- Property resales by State and Federally chartered financial institutions (e.g., banks and Savings & Loans)
- Government-Sponsored Enterprises (GSE) (e.g., Fannie Mae and Freddie Mac)
- Sale of properties by Local and State Government agencies
- Sale of properties by non-profit organizations approved to purchase HUD Real Estate Owned (REO) properties at a discount

- Sale of properties within Presidentially Declared Disaster Areas

A second appraisal is required by another FHA Roster appraiser if the resale value is 100% or more over the purchase price.

The re-execution of a sales contract in order to circumvent 90 day requirements is not an acceptable practice. In addition, FHA case numbers assigned prior to the executed contract date may require additional documentation as warranted by underwriting.

(5) Resales Between 91 and 180 Days

- Properties sold between 91 days and 180 days after acquisition by the seller are eligible. A second appraisal is required by another appraiser if the resale value is 100% or more over the purchase price.
- In addition, compliance with 24 CFR Part 203 Form may also be attached to document the cost and extent of rehabilitation that went into the property resulting in the increased value. This form is not mandatory.

(6) Second Appraisals

- When a second appraisal is required, the appraisal must be completed by an FHA Roster appraiser.
- When two appraisals are obtained, the required information for both appraisals must be entered into FHA Connection. FHA will identify the appraisals as “First Appraisal” and “Second Appraisal.”
- In addition, the following requirements must be met:
    - Do not reveal to the appraiser that this is a second request
    - The second appraisal fee may not be charged to the borrower
    - A new FHA case number is not required
    - Use of the lower of the two appraised values as the appraised value when determining maximum mortgage
    - All repairs and conditions from both appraisals must be addressed and resolved even if the conditions are different
    - Both appraisals must be included in the loan file and submitted for FHA insurance
    - The DE underwriter must comment on the FHA Loan Underwriting and Transmittal Summary Form HUD 92900-LT that a second appraisal was obtained and state which value was used in the calculation of the maximum loan amount

1.08.05.06 Access to Property

There must be vehicular access to the property via an all-weather public or private street. If a private street is the only form of access there must be a permanent recorded easement and provisions for permanent maintenance of the street.

1.08.05.07 Pest Inspections

Termite inspections are not required unless one of the following conditions apply:

- Appraiser notes a termite infestation (current or previous)
- Mandated by a local or state jurisdiction
- New construction (see New Construction section for more information)

If a termite letter shows there are any current infestations then treatment is required.

If a termite letter or appraisal notates any damage due to termites, FCM will require proof the damage was repaired or a licensed inspector, contractor, or structural engineer will need to verify the damage is minor. Also, the letter must clearly state the evidence observed has not affected the structural soundness of the home.

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.

Termite inspection letters must be dated within 90 days of closing. Soil treatment letters must be dated within 12 months of the day of closing.

1.08.05.08 Wells & Septic Systems

(1) Community Wells & Septic Systems

Community well and/or septic systems must be owned, operated, and maintained by a private corporation or a non-profit property owners association.

If the Property is on a Community Water System, the Appraiser must note the name of the water company on the appraisal report.

Properties located within a reasonable distance from public water or sewer systems may be required to connect to public utilities if the cost to connect is less than 3% of the value used to determine LTV.

(2) Shared Wells

A test of the well water is required for, but not limited to, properties:

- that are newly constructed;
- where an Appraiser has reported deficiencies with a well or the well water;

- where water is reported to be unsafe or known to be unsafe;
- located in close proximity to dumps, landfills, industrial sites, farms (pesticides) or other sites that could contain hazardous wastes; or
- where the distance between the well and septic system is less than 100 feet.

All testing must be performed by a disinterested third party. This includes the collection and transport of the water sample collected at the water supply source. The sample must be collected and tested by the local health authority, a commercial testing laboratory, a licensed sanitary engineer, or other party that is acceptable to the local health authority. At no time will the Borrower/owner or other Interested Party collect and/or transport the sample.

Properties located within a reasonable distance from public water or sewer systems may be required to connect to public utilities if the cost to connect is less than 3% of the value used to determine LTV

(3) Private Septic Systems

Waste water systems must be determined to be free of observable evidence of system failure. Certification can be provided by the local health department, a septic system professional, a qualified home inspector, or can be evidenced on the appraisal if completed by a FHA roster appraiser. If the appraiser does not make mention of any issues with the septic, it can be deemed acceptable. A septic system test is only required when:

- Evidence of system failure is present,
- If mandated by local or state jurisdiction,
- If customary to area, or;
- If required by lender.

All new systems must be accompanied by a permit and local health department approval.

Properties located within a reasonable distance from public, or community, water or sewer systems may be required to connect to public utilities if the cost to connect is less than 3% of the value used to determine LTV

(4) Private Wells

A test of the well water is required for, but not limited to, properties:

- that are newly constructed;
- where an Appraiser has reported deficiencies with a well or the well water;

- where water is reported to be unsafe or known to be unsafe;
- located in close proximity to dumps, landfills, industrial sites, farms (pesticides) or other sites that could contain hazardous wastes; or
- where the distance between the well and septic system is less than 100 feet.

All testing must be performed by a disinterested third party. This includes the collection and transport of the water sample collected at the water supply source. The sample must be collected and tested by the local health authority, a commercial testing laboratory, a licensed sanitary engineer, or other party that is acceptable to the local health authority. At no time will the Borrower/owner or other Interested Party collect and/or transport the sample.

Properties located within a reasonable distance from public, or community, water or sewer systems may be required to connect to public utilities if the cost to connect is less than 3% of the value used to determine LTV.

1.08.05.09 Easements

If any part of the residential structure lies within utility or drainage easement boundaries, the property is ineligible for financing. The residential structure includes attached improvements such as decks or patios.

1.08.05.10 Garage Conversions

Appraisers must notate any garage conversion. They must notate the impact on marketability for not having a garage and whether that is common in the subject property's comparable market. The appraiser must address the legal use of any garage conversion and whether permits were required and obtained. If they were required and permits were not obtained the appraiser must require the garage to be put back it its original use before FHA Financing can be obtained.

1.08.05.11 FEMA Disaster Areas

FEMA announces major disaster areas for specific counties after a significant event has occurred which the President of the United States has declared a disaster area. The [FEMA website] lists these disaster areas and has a searchable feature to determine the Incident Begin and End dates. The following procedures will be followed for any properties located in a county declared a disaster by the President of the United States.

To pass along the cost of the re-inspection to the borrower a Change In Circumstance form must be completed and submitted to FCM for approval within 3 days of the announcement by FEMA.

(1) If the original appraisal was performed ON or Before the Incident Period End Date:

- Property must be re-inspected by the original appraiser or, if not available, another licensed appraiser. The appraiser must provide the following commentary/evidence:
    - Property is free from damage and the disaster had no effect on value or marketability.
    - Photos provided of exterior only.
- If the re-inspection indicates damage, the extent of the damage must be addressed along with the following:
    - Completion of repairs is required as evidenced by Form 1004D/442, Appraisal Update and/or Completion Report prior to closing.
    - Photos are provided of interior, exterior and neighborhood.

(2) If the appraisal is performed after the Incident Period End Date:

- Appraisal must include written certification by the appraiser that:
    - Property is free from damage and the disaster has no effect on value or marketability.
    - All Comparables should be post-disaster; however, if sufficient comparables are not available, the appraiser must provide current photos of the subject property and comparables. MLS photos or photos used for previous appraisals are not acceptable.
- If appraisal indicates damage, the extent of the damage must be addressed, along with the following:
    - Completion of repairs is required as evidenced by Form 1004D/442, Appraisal Update and/or Completion Report, with photos, prior to closing.
    - Photos are provided of interior, exterior and neighborhood.

Additional Considerations:

All loans with a property inspection waiver including FHA Streamlines, that are located in a FEMA Declared Disaster Area will require a disaster inspection with exterior photos for a period of 90 days after the Incident Period End Date declared by FEMA.

1.08.05.12 Condominiums

A condominium is a multi-unit project that has individually-owned units, which may be either attached in one or more structures or detached from and each other and is essentially residential in use.

All condominiums must be on HUD's approved list except in the case of an FHA streamline refinance without an appraisal or HUD REO purchases.

The FCM underwriter is required to sign and authenticate all information referenced in the Lender Certification for Individual Unit Financing form.

Please see the previous section on insurance requirements for specific insurance guidelines on condominiums.

1.08.05.13 Three and Four Unit Properties

For three and four unit properties, the borrower must have personal reserves equivalent to three months' PITI after closing on a purchase transaction. Reserves cannot be derived from a gift.

The maximum mortgage amount for three and four unit properties is limited so that the ratio of the monthly mortgage payment divided by the monthly net rental income does not exceed 100%, regardless of the occupancy status. Form HUD 92561, *Borrower's Contract with Respect to Hotel and Transient Use of Property* is required at application for all multi-unit properties.

The monthly mortgage calculation referred to in the paragraph above can be calculated by adding the properties principal, interest, taxes, insurance, and homeowner's association dues.

The monthly net rental income referred to in the paragraph above can be 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 or the vacancy factor used by the jurisdictional Homeownership Center.

The calculation above does not alleviate the borrower from qualifying for the mortgage based on standard income, credit, cash to close or any other standard FHA guidelines.

1.08.05.14 Planned Unit Developments (PUDs)

A PUD is a mixed-use residential development of single-family dwellings in conjunction with rental, condominium, cooperative or town house properties. A residential development should be processed as a PUD if it has the following minimum characteristics:

- a homeowner association that holds either title in fee or a lease of prescribed length on the common area,

- mandatory membership of all unit owners (or units) in the association,
- the right of all unit owners to participate by vote in the operation of the association,
- lien supported assessment of the members to meet the association's budgeted operating costs (special assessments may be handled differently), and
- the appraisal for a detached PUD must be ordered as a detached PUD, not as a single-family residence.

Homeowner's assessments must be subordinate to the FHA mortgage. Provide one of the following items as documentation of HOA assessment subordination (required for all loans except Streamline refinances):

- PUD by-laws indicating all homeowner's association assessments are subordinate to mortgage liens (At minimum, First Community Mortgage must review the title page, table of contents and corresponding HOA lien subordination section reflecting the page(s) indicated in the table of contents) or
- Subordination agreement executed by a representative of the homeowner's association or
- Title commitment stating that the title company will insure over any homeowner's association assessment liens or
- Letter on letterhead from the title company indicating that PUD liens cannot take first lien position in the state in which the property is located or
- ALTA 9 or ALTA 5 title endorsement
- 60-Day letters may not be provided in lieu of one of the documents above

Please see the previous section on insurance requirements for specific insurance guidelines on attached PUDs.

1.08.06 New Construction

1.08.06.01 Overview - New Construction

New Construction refers to Proposed Construction, Properties Under Construction, and Properties Existing Less than One Year as defined below:

• Proposed Construction refers to a Property where no concrete or permanent material has been placed. Digging of footing is not considered permanent.

• Under Construction refers to the period from the first placement of permanent material to 100 percent completion with no Certificate of Occupancy (CO) or equivalent.

• Existing Less than One Year refers to a Property that is 100 percent complete and has been completed less than one year from the date of the issuance of the CO or equivalent. The Property must have never been occupied.

FHA treats the sale of an occupied Property that has been completed less than one year from the issuance of the CO or equivalent as an existing Property.

1.08.06.02 Re-sales of New Construction Properties

The re-sale of a property less than one year old, one sold from a builder to an owner-occupant and then subsequently to another borrower, is generally exempt from the new construction documentation requirements listed below when both of the following conditions are met:

- Property is 100% complete, including all on and offsite improvements and
- Re-sale is not an identity of interest transaction

1.08.06.03 Documentation Requirements for New Construction

The following documents are required on new construction loans:

- Site built housing and Condominiums
    - Under-Construction:
        - Obtain:
            - Copies of the building permit and CO (or equivalent); or
            - A final inspection issued by the local authority with jurisdiction over the Property or ICC, RCI or CI.
    - Existing for Less than One Year (100% Complete)
        - Obtain:
            - A copy or the CO (or equivalent); or
            - A final inspection issued by the local authority with jurisdiction over the Property or an ICC, RCU or CI; and
            - An appraisal evidencing the Property is 100% complete
- Required documentation for maximum financing:
    - Obtain and include the following documents in the case binder:
        - Form HUD-92541, Builders Certification of Plans, Specs and Site;
        - Form HUD-92544, Warranty of Completion of Construction;

- Copy of building permit issued by local authority prior to start of construction;
- Required inspections;
- Wood Infestation Report, unless the property is located in an area of no to slight infestation as indicated on HUD's "Termite Treatment Exception Areas" list:
  - Form HUD-NPMA-99-A Subterranean Termite Protection Builder's Guarantee, is required for all New Construction. If the building is constructed with steel, masonry, or concrete building components with only minor interior wood trim and roof sheathing, no treatment is needed. The underwriter muse ensure the builder notes on the form that the construction is such.
  - Form HUD-NPMA-99B, New Construction Subterranean Termite Service Record, is required when the proposed Property is treated with a soil chemical termiticide. The underwriter must reject the use of the post construction soil treatment when the termiticide is applied only around the perimeter of the foundation.
- A well water test is required for all newly constructed Properties. All testing must be performed by a disinterested third party. This includes the collection and transport of the water sample collected at the water supply source. The sample must be collected and tested by the local health authority, a commercial testing laboratory, a licensed sanitary engineer, or other party that is acceptable to the local health authority. At no time will the Borrower/owner or other Interested Party collect and/or transport the sample.

- Financing LTV Limit:
  - Properties that are Under Construction or Existing for Less than One Year are limited to a 90%LTV unless they have a building permit or its equivalent has been issued by a local jurisdiction (not applicable to Manufactured Housing) and the Required documentation for Maximum Financing.
  - For a Mortgage with an LTV of 90% or less, obtain:
    - Form HUD-92541, Builders Certification of Plans, Specs and Site;
    - Final inspection or appraisal if the Property is 100% complete;

- Wood Infestation Report, unless the property is located in an area of no to slight infestation as indicated on HUD's "Termite Treatment Exception Areas" list:
  - Form HUD-NPMA-99-A Subterranean Termite Protection Builder's Guarantee, is required for all New Construction. If the building is constructed with steel, masonry, or concrete building components with only minor interior wood trim and roof sheathing, no treatment is needed. The underwriter muse ensure the builder notes on the form that the construction is such.
  - Form HUD-NPMA-99B, New Construction Subterranean Termite Service Record, is required when the proposed Property is treated with a soil chemical termiticide. The underwriter must reject the use of the post construction soil treatment when the termiticide is applied only around the perimeter of the foundation.
- A well water test is required for all newly constructed Properties. All testing must be performed by a disinterested third party. This includes the collection and transport of the water sample collected at the water supply source. The sample must be collected and tested by the local health authority, a commercial testing laboratory, a licensed sanitary engineer, or other party that is acceptable to the local health authority. At no time will the Borrower/owner or other Interested Party collect and/or transport the sample.

1.08.06.04 Appraisal Requirements for New Construction

- Appraisals are valid for 120 days from the date of inspection to the Note date.
- Appraiser must be provided with a fully executed Builder Certification form dated no more than 30 days prior to appraisal order date.
- New construction properties must have at least one comparable from outside the subdivision. All builder sales must not be used in the same subdivision.
- New construction properties that are less than 90% complete: Appraiser must be provided a copy of the floor plan, plot plan and any other exhibits necessary to allow appraiser to determine the size and level of finish for the house they are appraising.
- New construction properties that are 90%- 99.9% complete: Appraiser must be provided a list of components to be installed or completed after the inspection.
- For new construction where the house is 100% complete at the time of the appraisal, the appraiser must take a clear photograph (in addition to the standard appraisal

photos) of each diagonally opposite front and rear corner of the house to record adequate grading and drainage of the site.

Notes:

- "Complete" means everything is complete including the installation of buyer preferences (flooring, appliances, etc.), utilities are on and fully functioning and all site improvements completed at the time of appraisal (Ready for Occupancy).
- If the appraiser makes no repair or correction conditions, the appraisal serves as the final inspection.

- If the appraisal is ordered as "proposed construction" and is fully completed, a final inspection is still required regardless if property is 100% complete.
- If the appraisal is ordered as "new construction, existing" and is 100% complete, a final inspection is not required providing the appraiser states that "the dwelling was built in accordance with the submitted plans and specifications and drainage and grading are adequate."

1.08.06.05 Calculating Tax Estimates for New Construction

The borrower must qualify with the monthly payment based on improved property taxes, not on the vacant land.

Realistic estimates for the improved property taxes used for loan qualification purposes as well as setup of monthly escrow accounts must come from a reliable source such as:

- The Appraiser
- Comparable Sales Data
- The Title Company as determined by the Assessor's Office

1.08.06.06 Building On Own Land

- Building on Own Land refers to the permanent financing of a newly constructed dwelling on land owned by the Borrower and may include the extinguishing of any construction loans.

- **Eligibility**

    - The Borrower must have contracted with a builder to construct the dwelling. The builder must be a licensed general contractor.

- **Calculating Maximum Mortgage Amount**

The Mortgagee must use the lesser of the appraised value or the documented Acquisition Cost to determine the Adjusted Value.

The maximum mortgage amount is calculated using the appropriate purchase Loan-to-Value (LTV) percentage of the lesser of the appraised value or the documented Acquisition Cost.

The documented Acquisition Cost of the Property includes:

- the builder's price or the sum of all subcontractor bids and materials;
- Borrower-paid options and construction costs not included in the builder's price to build;
- interest and other costs associated with a construction loan obtained by the Borrower to fund construction, if applicable; and
- either of the following:
  - the lesser of the cost of the land, or appraised value of the land, if the land is owned six months or less at case number assignment;
    OR
  - the appraised value of the land if the land has been owned for greater than six months at case number assignment or was received as an acceptable gift.

For Manufactured Housing, the builder's price to build includes the sum of the cost of the unit(s), the cost to transport the unit from the dealer's lot to the installation site, and all on-site installation costs.

Minimum Required Investment

- **Standard**
  - The Borrower may utilize any cash investment in the Acquisition Cost of the Property or land equity to satisfy the MRI in accordance with Calculating Maximum Mortgage Amount.
- **Required Documentation**
  - The Mortgagee must document that the cash investment was from an acceptable source of funds in accordance with TOTAL or Manual Underwriting requirements as applicable.

If the land was given as a gift to the Borrower, the Mortgagee must verify that the donor was not a prohibited source.

The Mortgagee must obtain standard gift documentation for any gift of land.

- **Borrower's Additional Equity in the Property**

  The Borrower may not receive cash back from the additional equity in the Property, but the Borrower may replenish their own cash expenditures for any Borrower-paid extras over and above the contract specifications and any out-of-pocket expenses not included in the builder's price. The Mortgagee must obtain an itemization of the extras and expenses and the cost of each item.

- **Required Documentation**

  The Mortgagee must document the date of purchase of the land by obtaining the Closing Disclosure or similar legal document.

  The Mortgagee must obtain evidence that the funds used to pay Borrower paid options were derived from an acceptable source. The Mortgagee must obtain an itemization of the options, expenses, and cost of each item.

  The Mortgagee must comply with New Construction requirements.

1.08.07 Declining Markets

If the appraisal indicates that the property is located within a declining market a detailed explanation by the appraiser on the effect of the declining market on the subject neighborhood values and how the appraiser determined the property to be in a declining market are required. Additional comparables may be required by the underwriter on a case-by-case basis.

1.08.08 Right of Redemption Transactions

1.08.08.01 Overview

Certain state laws provide a "redemption period" after a foreclosure or tax sale has occurred, during which time the property may be reclaimed by the prior mortgagor or other party upon payment of all amounts owed. The length of the redemption period varies by state and does not expire automatically upon sale of the property to a new owner.

1.08.08.02 Transaction Restrictions

- No Manufactured Homes

- A Surety Bond may be required depending upon the subject property's state – consult with your title company for further details

1.09 Refinance Transactions

Below are general guidelines specific to FHA refinance transactions. Please note that all of the previous guidance in the above sections apply to refinance transactions as well unless specifically stated.

First Community Mortgage offers the following types of refinance programs:

- Rate/Term Refinance
- Simple Refinance – FHA to FHA R/T Refinanced
- Cash Out Refinance
- Streamline Refinances (both credit and non-credit qualifying)

1.09.01 General Overview

- The payment due in the month the loan is closing must be paid either prior to closing or included in the payoff amount at closing.
- Payoff statements that have credited the existing escrow balance to the balance due are not acceptable. (netted out escrows)
- The mortgage must be current for the month prior to the month in which they close and the month they close. Note: The borrower has the option to make the current payment at the beginning of the month or include it in the payoff amount at closing, when closing within the month the payment is due.
- On existing FHA loans, often there is a refund of a portion of the upfront MIP. This refund is applied as a credit to the new loan when determining the loan amount and can be found using the Refinance Credit Query page on the FHA Connection website.
- All 3-4 unit properties must have 3 months PITI reserves.
- Non-traditional credit is not allowed.
- Refinances of previously modified mortgages are allowed provided the current mortgage has a 24-month 0x30 payment history.

1.09.01.01 Determining Value

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.

1.09.02 Rate/Term Refinance

1.09.02.01 Overview

- Rate/Term Refinances consist of loans originated with the intent of paying off a first and/or second mortgage. See Subordinate Financing section for details regarding existing and new secondary financing.
- The buyout of a spouse's equity per a divorce decree or to pay off heirs to settle an estate is permitted as a rate/term refinance.
- The borrower may not receive more than $500 cash at closing.

1.09.02.02 Maximum Mortgage Amount

The maximum mortgage amount may not exceed the Nationwide Mortgage limit for the property area.

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 after 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.

(1) Calculation of Maximum Mortgage Amount

the lesser of:

- the Nationwide Mortgage Limit;
- the maximum LTV based on the Maximum LTV Ratio; or
- the existing debt and costs associated with the transaction as follows:
  - the unpaid principal balance of the first Mortgage as of the month prior to mortgage Disbursement;
  - the unpaid principal balance of any purchase money junior Mortgage as of the month prior to mortgage Disbursement;
  - the unpaid principal balance of any junior liens over 12 months old as of the date of mortgage Disbursement. If the balance or any portion of an equity line of credit in excess of $1,000 was advanced within the past 12 months and was for purposes other than repairs and rehabilitation of the Property, that portion above and beyond $1,000 of the line of credit is not eligible for inclusion in the new Mortgage;
  - ex-spouse or co-Borrower equity, as described in "Refinancing to Buy out Title Holder Equity" below;
  - interest due on the existing Mortgage(s);
  - the unpaid principal balance of any unpaid PACE obligation;
  - Mortgage Insurance Premium (MIP) due on existing Mortgage;
  - any prepayment penalties assessed;
  - late charges; and
  - escrow shortages;
  - allowed costs include all Borrower paid costs associated with the new Mortgage; and
  - any Borrower-paid repairs required by the appraisal;
- less any refund of the Upfront Mortgage Insurance Premium (UFMIP).

1.09.02.03 Maximum LTV

The maximum LTV for a Rate and Term refinance is:

- 97.75 percent for Principal Residences that have been owner-occupied for previous 12 months, or owner-occupied since acquisition if acquired within 12 months, at case number assignment;
- 85 percent for a Borrower who has occupied the subject Property as their Principal Residence for fewer than 12 months prior to the case number assignment date; or if

owned less than 12 months, has not occupied the Property for that entire period of ownership.

1.09.02.04 Credit

- Borrower can have no 30 day or greater mortgage delinquencies in the most recent 6 months. If mortgage has less than 6 months history, payments must have been made in month due. If mortgage is not reflected on credit report, a 12-month VOM is required. This applies to all mortgages on all properties.

1.09.02.05 Occupancy

- Determination of length of occupancy in subject property is required. Requirement can be met with employment documentation; in case of discrepancies or uncertainty, underwriter may ask for recent utility bills in the borrower's name to further document occupancy.

1.09.02.06 Subordinate Financing

- The maximum CLTV on a rate/term refinance is 97.75%.
- Existing subordinate financing not used to purchase the property must be seasoned twelve months to be included in the loan amount on a rate/term refinance. If disbursements from an equity line exceed a total of $1,000 within the past twelve-month period and the funds were used for purposes other than repairs and rehabilitation of the property, the amount in excess of the $1000 cannot be included in the new mortgage.

1.09.02.07 Borrowers

- Non-occupant Co-Borrowers are permitted on purchases and rate/term refinances with the following restrictions for loans over 75% LTV:
    - Must be a family member.
    - 1-unit properties only
- When a borrower is not currently on the note or title and the current note holder will not be on the new loan, the new borrower must be seasoned on title for a minimum of 12 months and a 12-month documented pay history coming from the new borrower's funds is required with no 30 day or greater lates.

1.09.02.08 Properties Listed for Sale

- Properties currently listed for sale are eligible for a Rate and Term Refinance. The listing must be removed/cancelled prior to closing.

1.09.03 Cash-Out Refinance

1.09.03.01 Overview

- Effective with Case numbers ordered on or after September 1, 2019: Cash-Out Refinances are limited to 80% LTV and CLTV. See Acquisition section below for additional restrictions.
- Texas 50 (a)(6) transactions are ineligible.

1.09.03.02 Credit

- A mortgage history with a minimum of 6 months is always required. See below for acquisition seasoning requirements.
- The Borrower has made all payments for all their Mortgages within the month due for the previous 12 months or since the Borrower obtained the Mortgages, whichever is less. Additionally, the payments for all Mortgages secured by the subject Property must have been paid within the month due for the month prior to mortgage Disbursement.

1.09.03.03 Occupancy

- 12-month occupancy history is required. Requirement can be met with employment documentation; in case of discrepancies or uncertainty, underwriter may ask for recent utility bills in the borrower's name to further document occupancy.

1.09.03.04 Acquisition Seasoning

- There is a 12-month acquisition seasoning requirement for all cash out refinances. The property must have been owned and occupied as a primary residence for the last 12 months.
- The borrower must have made at least six consecutive monthly payments on the existing loan. The first payment due date of the new loan must be at least 210 days after the first payment due date of the loan being refinanced.
- Note: A sales price need not be considered if the property was acquired as the result of inheritance and is, or will become, the borrower's primary residence.
- Properties owned free and clear must be treated as a cash out refinance.

1.09.03.05 Subordinate Financing

- New subordinate financing is not allowed on cash out refinances.
- Effective with Case numbers ordered on or after September 1, 2019: Existing secondary financing may be subordinated up to 80% CLTV.
- All existing liens, including subordinate financing, must be seasoned at least six months and have an acceptable payment history (i.e., no late payments of 30 days or greater).

- If the secondary financing is an equity line, the maximum amount of the equity line is used in the CLTV calculation.

1.09.03.06 Borrowers

- Non-occupant co-borrowers are not permitted on cash out transactions.
- Any co-borrower being added to the note must be an occupant of the property.

1.09.03.07 Properties Listed for Sale

- Cash-Out Refinances are not allowed if the property is currently listed for sale. The property must have been taken off the market or the listing must have expired at least 1 day prior to the application date to be eligible.

1.09.04 Streamline Refinance

1.09.04.01 Overview

- Streamline refinances are designed to lower the monthly payment on current FHA mortgages to put the borrowers in a better financial position.
- First Community Mortgage offers the following types of Streamline Refinances:
    - Non-Credit Qualifying Streamline without Appraisal
    - Credit Qualifying Streamline with Appraisal
    - Credit Qualifying Streamline without Appraisal
- All Streamline refinances must contain a Net Tangible Benefit to the borrower. A transaction solely for the purpose of reducing the mortgage term must be underwritten and closed as a standard rate/term refinance transaction unless the requirements of the Net Tangible Benefit test are met.
- The tolerance level for cash back at closing is $500 and must only include minor adjustments. The loan must not be structured to facilitate the maximum of $500 cash back at closing to the borrower.
- FHA streamlines are manually underwritten and should not be run through an AUS system.
- The following underwriting sections/requirements do not apply:

For Credit Qualifying Streamline	For Non-Credit Qualifying Streamlines
• Ordering Appraisal • Transferring Existing Appraisal • Ordering Second Appraisal • Ordering an Update to an Appraisal	• Ordering Appraisal • Transferring Existing Appraisal • Ordering Second Appraisal • Ordering an Update to an Appraisal

• Borrower Ineligibility Due to Delinquent Federal Non-Tax Debt • Delinquent Federal Tax Debt • Property Eligibility and Acceptability Criteria • National Housing Act's Statutory Limits • Nationwide Mortgage Limits • LTV Limitations Based on Borrower's Credit Score • Underwriting the Property • Underwriting the Borrower Using the TOTAL Mortgage Scorecard	• Borrower and Co-Borrower Ownership and Obligation Requirements • Cosigner Requirements • Principal Residence in the United States • Military Personnel Eligibility • Citizenship and Immigration Status • Residency Requirements • Borrower Ineligibility Due to Delinquent Federal Non-Tax Debt • Delinquent Federal Tax Debt • Property Eligibility and Acceptability Criteria • National Housing Act's Statutory Limits • Nationwide Mortgage Limits • Underwriting the Property • Underwriting the Borrower Using the TOTAL Mortgage Scorecard/AUS • Credit Requirements • Income Requirements • Asset Requirements • Underwriting of Credit and Debt • Underwriting of Income • Underwriting of Assets • Calculating Qualifying Ratios • Approvable Ratio Requirements • Documenting Acceptable Compensating Factors

1.09.04.02 Maximum Term

- All streamline refinances without an appraisal require the maximum term to be no greater than the remaining term plus twelve years.

1.09.04.03 Determining the Maximum Loan Amount

The maximum base loan amount calculation for streamline refinances is the lesser of:

A) Outstanding principal balance of the existing mortgage as of the month prior to mortgage disbursement **+** Interest due on the existing mortgage **+** MIP due on the existing mortgage **–** any refund of the UFMIP.

OR

B) Original principal balance of the existing mortgage **–** any refund of UFMIP.

Note: Nothing other than the existing principal balance and the current interest charged by the servicing lender may be included in the principal balance. No other fees or charges showing on the payoff may be financed in the loan amount. Therefore, do not include delinquent interest, escrow shortages, late fees, fax or courier fees or any other fees. Also note that escrow shortages may not be paid through premium pricing, so the borrower must bring funds to closing that are equal to or exceed the amount of escrow shortages listed on the payoff statement.

1.09.04.04 Acquisition/Seasoning

- On the date of the new FHA case number assignment:
    - the Borrower must have made at least six payments on the FHA insured Mortgage that is being refinanced;
    - at least six full months must have passed since the first payment due date of the Mortgage that is being refinanced;
    - at least 210 Days must have passed from the Closing Date of the Mortgage that is being refinanced; and
    - if the Borrower assumed the Mortgage that is being refinanced, they must have made six payments since the time of assumption.
- In addition to these seasoning requirements, the loan must also meet GNMA requirements:
    - the borrower made at least six consecutive monthly payments on the loan being refinanced, referred to hereinafter as the Initial Loan, beginning with the payment made on the first payment due date; and
    - the first payment due date of the refinance loan occurs no earlier than 210 days after the first payment due date of the Initial Loan

Mortgage Payment History Requirement for a Streamline Refinance.

The borrower must exhibit an acceptable payment history as described in the table below.

If the outstanding mortgage has…	Then the borrower must have…
fewer than 12 months payment history	made all mortgage payment within the month due
12 months payment history or more	0x30 late payments

1.09.04.05 Subordinate Financing

- New subordinate financing is not allowed on streamline refinances.
- Existing secondary financing may be subordinated.
- All existing liens, including subordinate financing, must be seasoned at least six months and have an acceptable payment history (i.e., no late payments of 30 days or greater).
- If the secondary financing is an equity line, the maximum amount of the equity line is used in the CLTV calculation.

1.09.04.06 Adding or Removing Borrowers on a Streamline Refinance

- Borrowers may be added to the loan without credit qualification, provided all of the original borrower(s) also remain on the loan.
- Non-occupant co-borrowers are not permitted on streamline transactions unless they have been on title and the mortgage note as a non-occupant co-borrower since the original financing of the purchase mortgage.
- Borrowers may only be deleted from the existing loan without credit qualifying in cases of divorce, legal separation or death when:
  - The divorce decree or legal separation agreement awarded the property and responsibility for payment to the remaining borrower and
  - The borrower can demonstrate that they have made the mortgage payments for a minimum of six months prior to case number assignment.
- If deleting a borrower from the loan causes any of the following, the borrower must be credit qualified:
  - Deletion of the borrower will trigger a due-on-sale clause or
  - The borrower assumed a mortgage that did not contain a due-on-sale clause but limited assumptions only to creditworthy borrowers and the assumption occurred less than six months previously or
  - The borrower assumed a mortgage that did not contain a due-on-sale clause but the property was assumed less than six months prior to application as the result of a divorce, devise or descent

1.09.04.07 Non-Credit Qualifying Streamline Documentation Requirements

Documentation	Requirement
1003	Abbreviated 1003: Borrower Information, Employer and Mortgage Liability. Assets only if cash is required to close, and only the subject property in the REO section. Declarations and HMDA need to be completed. (Income, other debts and other REO schedule should not be completed)
Credit Report	Should be a mortgage only credit report with scores and should be updated to show payment received through month of closing. Mortgage history must reflect 0x30 late payments in the last 12 months.
VOE	A Verbal Verification of Employment needs to be obtained, no income information should be provided.
Assets to Close	Cash to close exceeding the new mortgage payment must be verified using Manual Underwriting Requirements: 2 months bank statements OR VOD and 1 Month Bank Statement OR Quarterly Asset Statement Large Deposits must be sourced and documented
FHA Connection	A New Case # needs to be assigned and validated. A refinance authorization will need to be obtained as part of the case # assignment.
WORKSHEETS	**FHA Loan Amount Worksheet** should be completed prior to underwriting. Closing Costs cannot be included in loan amount. **Net Tangible Benefit** worksheet should be completed and signed by borrower prior to underwriting.
Other Documents	Copy of Social Security Card Current Mortgage Statement HUD-1 from Loan being refinanced Current Note Payoff good through Funding Copy of current utility bill or employment documentation (Ie Current paystub) to confirm subject property occupancy – if borrower cannot provide documentation of occupancy the loan must be processed as an investment property.
NOT Required	Appraisal Tax Transcripts Paystubs W2

1.09.04.08 Credit Qualifying Streamlines

- Credit-qualifying streamlines contain all of the normal features of a streamline refinance, but provide a level of assurance for continued performance on the mortgage. A credit-qualifying streamline refinance must be considered when:
    - A change in the mortgage term will result in an increase in the mortgage payment of more than 20%. Note that this would only apply in the case of refinancing an existing one-year ARM to a new fixed rate, all other scenarios require a reduction in payment in order to meet the *Net Tangible Benefit*.
    - Under certain scenarios involving deletion of a borrower or an assumption. See Adding or Removing a Borrower on a Streamline Refinance section.
- Credit-qualifying streamlines require the underwriter to evaluate the borrower's income and credit to determine the overall file quality and approval. The following items are evaluated in the same fashion as a standard FHA refinance:
    - Income documentation
    - Credit history/liabilities
    - Debt-to-income ratios
- The maximum debt-to-income ratio on credit-qualifying streamlines is 31%/43% with no exceptions.
- Tax transcripts are required on all Credit Qualifying Streamlines according to the tax transcript policy/income type.
- All of the standard FHA streamline requirements in the sections above apply.

1.09.04.09 Net Tangible Benefit Test

A Net Tangible Benefit is a reduced Combined Rate, a reduced term, and/or a change from an ARM to a fixed rate Mortgage that results in a financial benefit to the Borrower.

Combined Rate refers to the interest rate on the Mortgage plus the Mortgage Insurance Premium (MIP) rate.

Reduction in Term refers to the reduction of the remaining amortization period of the existing Mortgage.

- **Standard for Refinances without a Term Reduction**

	TO		
FROM	Fixed Rate New Combined Rate	One-Year ARM New Combined Rate	Hybrid Arm New Combined Rate

Fixed Rate	At least .5 percentage points below the prior combined rate.	At least 2 percentage points below the prior combined rate.	At least 2 percentage points below the prior combined rate.
Any ARM with less than 15 months to next payment date change	No more than 2 percentage points above the prior combined rate.	At least 1 percentage point below the prior combined rate.	At least 1 percentage point below the prior combined rate.
Any ARM with greater than or equal to 15 months to next payment change	No more than 2 percentage points above the prior combined rate.	At least 2 percentage points below the prior combined rate.	At least 1 percentage point below the prior combined rate

**Combined Rate refers to the interest rate on the mortgage plus the MIP rate.

- **Standard for Refinances with a Term Reduction**
  Must determine that there is a net tangible benefit to the Borrower meeting the standards in the chart below for all Streamline Refinance transactions with a reduction in term.
  Additionally, the combined principal, interest, and MIP payment of the new Mortgage must not exceed the combined principal, interest, and MIP payment of the refinanced Mortgage by more than $50.

	To		
From	Fixed Rate New Combined Rate	One-Year ARM New Combined Rate	Hybrid ARM New Combined Rate
Fixed Rate	Below the prior Combined Rate.	N/A	N/A
Any ARM with Less than 15 Months to Next Payment Change Date	No more than 2 percentage points above the prior Combined Rate	N/A	N/A
Any Arm with Greater Than or Equal to 15 Months to Next Payment Change Date	No more than 2 percentage points above prior Combined Rate	N/A	N/A

1.09.05 Adjustable Rate Mortgage (ARM) Transactions

First Community Mortgage offers two different types of adjustable rate mortgages for FHA products. Each has unique properties as outlined below but all are based off the One-Year Treasury Index and all should be run through the Desktop Underwriting (DU) AUS. Loan Prospector (LP) should never be used for ARM loans. ARMs are not allowed in combination with credit scores below 640.

1.09.05.01 FHA ARMs

Program Code	ARM Type	Margins	First Adjustment Cap	Annual Cap after First Adjustment	Lifetime Cap	Qualifying Rate	INDEX
FHA3/1ARM	3 Year ARM	2.00	1	1	5	Note Rate	CMT
FHA5/1ARM	5 Year ARM	2.00	1	1	5	Note Rate	CMT

1.10 Definitions

Automated Underwriting System (AUS): General term for automated underwriting tools acceptable to First Community Mortgage, that includes:

- Fannie Mae's Desktop Underwriter® and
- Freddie Mac's Loan Prospector®

Combined Loan-To-Value or CLTV: The ratio calculated by adding the HELOC credit line limit to the mortgage amount plus any secondary financing and dividing that total by the value of the mortgaged premises.

Co-op or Cooperative Project: A structure of two or more Cooperative Units in which a borrower obtains the right to occupy one of the Cooperative Units by purchasing stock in the Corporation that owns the structure and by executing a Proprietary Lease for the Cooperative Unit.

Debt to Income or DTI ratio: A borrower's DTI generally includes a "front-end" and "back-end" ratio. The front-end ratio, also known as a mortgage payment expense to effective income ratio, is calculated by taking the total mortgage payment and dividing it by the gross effective income. The back-end ratio, also known as the total fixed payments to effective income ratio, is calculated by taking the total obligations and dividing it by the gross effective income.

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. (Fiancé's parents will be eligible if Fiancé will be on title and certifies occupancy).

Fannie Mae: The Federal National Mortgage Association, a federally chartered and privately owned corporation, organized and existing under the Federal National Mortgage Association Charter Act, or any successor thereto.

Federal Debt: A Federal debt is defined as

- a Veterans Affairs guaranteed mortgage
- a Title I loan
- a Federal Student loan
- a Small Business Administration (SBA) loan
- delinquent Federal taxes, or
- a lien, including taxes, placed against the borrower's property for a debt owed to the U.S.

FHA: The Federal Housing Administration

First Time Homebuyer: An individual who has had no ownership in a principal residence in the three years prior to the closing date of the loan OR an individual who, though having owned a home in the previous three years, owned a home with a former spouse while married and is no longer living in the property as evidenced by the divorce decree and/or separation agreement.

Freddie Mac: The Federal Home Loan Mortgage Corporation, a corporate instrumentality of the United States created and existing under Title III of the Emergency Home Finance Act of 1970, as amended, or any successor thereto.

Gift Funds: Gift funds are assets provided by a non-interested third party to the borrower.

Identity-of-Interest: An identity-of-interest transaction is a transaction for the purchase of a principal residence between either parties with familial or business relationship, or business affiliates.

Interested Party: Interested parties include real estate agents, builders, developers, or anyone with an interest in the sale or refinance of the property.

Loan-to-Value or LTV: The loan-to-value of a mortgage loan at the time of its origination, which shall be the ratio, expressed as a percentage, that the mortgage loan bears to the lesser of (i) the appraised value of the mortgaged property at origination (as determined by a true and accurate appraisal that satisfies the procedural and substantive requirements of the underwriting guidelines) or (ii) if the mortgage loan was made to finance the acquisition of the mortgaged property, the sales price of the mortgaged property.

Manufactured Home: A manufactured home, including all accessions thereto, that is legally classified as real property under applicable state law.

Monthly Payment: The scheduled monthly payment of principal and/or interest, and any escrow payment, that is due each month on a mortgage loan.

Mortgage: The mortgage, deed of trust or other security instrument creating a first lien on an estate in real property.

Mortgage Loan: An individual Loan that is evidenced by a Mortgage Note and secured by a Mortgage and made in connection with the other documents included in the Mortgage Loan file (all of which are deemed included in the definition of "Mortgage Loan").

Mortgaged Property: The property pledged as security for the debt evidenced by a Mortgage Note.

Mortgagee: The originator of any Mortgage Loan, as lender thereunder, together with its successors and assigns, as mortgagee thereunder.

Mortgagor: The obligor on a Mortgage Note.

Non-occupying borrower transaction: A non-occupying borrower transaction is a transaction involving two or more borrowers where one or more borrower will not occupy the property as the principal residence.

Note: Document signed by a borrower as acknowledgment of the debt, and is, by inference, a promise to pay.

Self-employed borrower: For FHA mortgage loan underwriting purposes, a self-employed borrower is a borrower with a 25 percent or greater ownership interest in a business.

Third party contribution: A third party contribution is a payment by an interested third party, or a combination of parties, toward the borrower's

- Closing costs, per ML 06-04
- Prepaid expenses
- Discount points, and
- Other financing concessions