WesLend Select USDA – Guaranteed Rural Housing (GRH)

WesLend FINANCIAL

Transaction	*FICO*	*Number of Units*	*Maximum LTV/CLTV*
Primary Residence – Owner Occupied			
Purchase / Rate Term	640	1 - Unit	100%
Refinance (existing GRH Loan only)	640	1 - Unit	100

WesLend Select USDA – (GRH) Product Code:	
30 Year Fixed	7000-00

Highlights

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Minimum Loan Amounts	• Min loan amount $60,000. • Min loan amount $75,000 for properties located in NY and TX.
4506 Transcripts	Full 1040 transcripts for the most recent two years for all adult household members regardless of whether or not they are obligated on the loan are required. ***Note: This requirement has been suspended by USDA. Tax return transcripts for household members must not be ordered until further notice. Household members' income must be documented with traditional income documentation.***
Appraisals	An Environment Property Inspection is required when the property is exposed to the environmental hazard of sulfur-containing drywall. A recertification of value dated within 30 days of the purchase date and supporting the original appraised value is required for loans purchased more than 60 days after the close dated. (Note date to purchase date) **Transferred appraisals are not permitted.**
Appraisers	Appraisers must be FHA approved appraisers.
Assets	Suspicious Activity Related to Deposits or Payments: • All asset documentation will be reviewed for patterns of unusual payments, deposits, and/or gift funds, regardless of when they were provided to the borrower that may be indicative of structuring to avoid compliance with the laws and regulatory reporting requirements of the United States or foreign countries. Unusual patterns can include, but are not limited to, large cash deposits, large and numerous gifts and any other unexplained activity not typical for the borrower. **Red Flags:** Transactions which include any of the following characteristics will be given additional scrutiny: • A borrower receives multiple gifts of similar amounts wired from outside the U.S. • A borrower receives gift funds in the form of a wire transfer from an individual with no ties to the borrower or the transaction. • A borrower receives a wire from a business not associated with the transaction and it is explained as payment for services rendered or products provided. • A borrower receives large deposits listed as tuition expenses comingled with funds for down payment from the same account. • A borrower receives gift funds from a donor that transferred the funds through multiple financial institutions prior to the deposit into the borrower's account. Cryptocurrency, such as Bitcoin and Ethereum, may NOT be used for down payment funds or closing funds. These types of assets must be backed out of the borrower's assets.
AUS	Must use GUS (Guaranteed Underwriting System)
Community Property States	• Arizona • California

	• Idaho • Louisiana • Nevada • New Mexico • Texas • Washington • Wisconsin
Condominium	Must meet Fannie, Mae, Freddie Mac, FHA or VA project standards. • Current financials and a budget are required. • The underwriter must certify the project on the USDA Condominium Certification Form.
Construction to Permanent	Not Allowed.
Credit Report	• A new credit report may not be pulled once the file has been submitted for underwriting. • A new credit report is allowed only after the existing credit report has expired.
Credit Score	**640** - At least one borrower must meet the minimum loan score requirement. If other borrowers do not have credit scores, follow USDA requirements for borrowers who do not have a credit score.
Deed Restrictions	Not Allowed
DTI	If fees associated with the transaction have been paid outside of closing (POC) and are charged to the borrower's credit card but are not reflected on the credit report, then the updated payment must be documented and included in the DTI.
Escrow / Impound	Required. Waivers are not allowed.
Flip Transactions	Flip transactions are not eligible. • A flip transaction is defined as a purchase transaction for a property that has recently been acquired by the seller and is being sold for a quick project. • A flip transaction exists if the title reveals several changes in ownership in the course of a few months.
Illegal Activity	All sources of income must be legal in accordance with all applicable federal, state and local laws, rules and regulations without conflict. Indication of income obtained from illegal sources makes the transaction ineligible. All assets must be legal in accordance with all applicable federal, state and local laws, rules and regulations without conflict. If there is an indication of illegal activity occurring on the subject property that does not comply with federal, state, and local laws, rules and regulations the loan is ineligible. **Note:** Income or assets derived from a marijuana business or a marijuana producing property are ineligible regardless of state law. Marijuana income, assets and income producing property are illegal at the federal level.
Ineligible	Interest only Flip transactions Properties outside the US or in US territories, provinces or commonwealths including Guam, Puerto Rico and the Virgin Islands USDA Streamline Refinance USDA Rural Refinance Pilot Texas 50(a)(6) Loans to borrowers with diplomatic immunity
LTV/CLTV	100%/100%
Manual Underwriting	Allowed
Manufactured Homes	***Not Allowed***.
Non-traditional Credit	Not Allowed.
Refinance	Rate/term refinance of an existing USDA loan is eligible per USDA guidelines. Loan amounts may not exceed the current appraised value including the amount of the financed guarantee fee.

Sales Contract	Re-negotiated purchase agreements that increase the sales price **after** the original appraisal has been completed are acceptable only if one or more of the following applies: • Renegotiation includes seller-paid closing costs that do not exceed allowable guidelines and are customary for the market as supported by the appraisal. • Renegotiation represents changes to the improvements (features, finishes, or other property characteristics) not included in the appraisal and/or original sales contract; an updated appraisal must be obtained to verify value of the changes. • Sale of subject property is between family members where the increase represents additional gift of equity; higher sales price must be supported and not exceed the appraised value. • Original sales contract included a provision that provides for the sales price to be increased as a result of a higher appraised value. • A missed contingency or other unsatisfied contract demand voids the original contract.
Section 8 Housing Vouchers	Section 8 Homeownership Vouchers are an acceptable source of qualifying income. The monthly subsidy must be treated as income in determining the borrower's DTI and may not be used to offset the mortgage payment.
Temporary Buydown	Not Allowed.
Third Party Originated Loans (TPO)	TPOs with lender paid broker compensation where the broker charges third party processing fees as a separate fee paid by the borrower, property seller, or other third party are not allowed.

Credit Philosophy

The Lenox/WesLend philosophy is to offer the Rural Housing Guaranteed Program with minimal overlays to our clients. All loans are evaluated in accordance with the following principals:

- All loans must be submitted to GUS.
- Each loan is evaluated in accordance with:
  - Rural Housing policies as defined in the *"SFH Guaranteed Loan Program Technical Handbook",* HB 1-3555;
  - GUS recommendation; and
  - Policies as outlined within this Program Guide.
- Each loan applicant is underwritten individually and all credit standards are applied consistently to each borrower.
- All factors are considered when evaluating a loan file. The underwriting decision is not based on any single item or factor.

Origination Overview

Introduction

Preliminary Determination of Applicant Eligibility

- Always review the following items to make a preliminary determination of the borrower's eligibility:
  - **Income**. Does the combined annual adjusted income of all members of the borrower's household, not just the borrowers on the note, fall within the program's income limits? **Annual and adjusted incomes (eligibility income) are distinct from repayment (stable and dependable) income.**
  - **Ratios**. Do the borrower's PITI and total debt ratios fall at or below the program's maximum allowable ratios?
    - o Ratios are calculated using repayment income from the borrowers who will be parties to the transaction.
  - **Credit.** Does the credit record appear to meet the program guidelines?

        - The borrower must have a credit history that demonstrates their ability and willingness to repay the loan.
        - **Note:** GUS is unable to accept supplemental credit reports – all errors must be corrected at the bureau level and a new credit report obtained through GUS.
    - **Loan Amount.** Is the loan amount supported by the appraisal's fair market value?
    - **Rural Area.** Does the property appear to be in an eligible rural area?
        - A property's eligibility can be verified at the following website: http://eligibility.sc.egov.usda.gov/eligibility or by using GUS.
    - **Qualified Alien/U.S. Citizen.** Is the borrower a qualified alien or a United States citizen?
        - If the borrower is not a U.S. citizen they must produce evidence that they are qualified to received federal assistance and establish that they are a qualified alien.
    - **Need for Guarantee.** Has a preliminary determination been made regarding the borrower's ability to obtain traditional credit?
        - Both the underwriter and the borrower must certify that the borrower is unable to secure traditional credit from conventional loan sources upon terms and conditions which the borrower can reasonably fulfill.

Loan Purposes

Purchase Loans

- Rural Housing loans can be used to acquire new or existing housing that will be the borrower's principal residence and to pay costs associated with such a purchase.
- Properties must be residential in use, character and appearance. Loan funds may be used for the following purposes:
    - The purchase of a new or existing dwelling; and
    - Reasonable and customary expenses associated with purchasing a dwelling.
- The Guaranteed Underwriting System (GUS) must be used including when the loan is manually underwritten.

Refinance Loans

Rate/term refinances are permissible under the following conditions:

- The existing loan must be a Rural Housing guaranteed loan.
    - The payoff of any other loan type is not permitted.
- The new loan must be a 30 year fixed loan.
- The interest rate of the new loan must be fixed and must not exceed the interest rate of the existing loan that will be refinanced.
- Borrowers must meet all Rural Housing eligibility requirements.
- Total adjusted annual income for the household cannot exceed the moderate level for the area.
- The subject property must be the same property securing the original deed of trust.
    - Properties located in areas since determined by Rural Housing to be non-rural are eligible.
- The subject property must be occupied by the borrowers as their principal residence.
- Additional borrowers may be added to the new Rural Housing loan.
- Existing borrowers on the current mortgage note may be removed, however at least one of the original borrowers must be a borrower for the new refinance loan.
- A new appraisal is required.
- The maximum loan amount may not exceed the new appraised value with the exception of the up-front guarantee fee. The following items are eligible to be financed up to the new appraised value:
    - The principal and interest balance of the existing loan;
    - Reasonable and customary closing costs;
    - Funds necessary to establish a new tax and insurance escrow account; and
    - Discount points that reduce the effective interest rate and that are reasonable and customary for the area.
        - Discount points may not exceed 2%.
- Unpaid fees, past-due interest, and late fees/penalties cannot be included in the new loan amount.
- Borrowers are not eligible to receive cash out from the refinance transaction.

  - Borrowers may receive reimbursement from loan proceeds at closing for their personal funds advanced for eligible loan purposes that are part of the refinance transaction such as the appraisal fee or credit report fee.
  - At closing a nominal amount of "cash out" may occasionally result due to final escrow and interest calculations.
- Subordinate financing such as home equity seconds and down payment assistance "silent" seconds cannot be included in the new loan amount.
  - Any existing secondary financing must be subordinate to the new first lien.
- The existing loan must have closed 12 months prior to a request for a refinance and must be current for the 180 day period prior to Rural Housing's receipt of a Conditional Commitment request.
- The Guaranteed Underwriting System (GUS) must be used including when the loan is manually underwritten.

Prohibited Loan Purposes

- Purchase of income producing land or buildings that will be used principally for income producing purposes is not allowed.
- Vacant land or properties used primarily for agricultural, farming, or commercial enterprise are ineligible.
  - A minimal income producing activity, such as maintaining a garden that generates a small amount of additional income, does not violate this requirement
- Payment on any lease agreement associated with the subject property is not permitted.

Loan Terms and Conditions

Maximum Loan Amount

- The borrower is permitted to finance reasonable and customary expenses associated with purchasing a home as long as the total amount financed does not exceed any of the following limits:
  - The maximum loan amount for which the borrower qualifies as determined by their income and repayment ability.
  - The fair market value of the property as determined by a current appraisal; and
  - A 100% loan-to-value ratio.
    - Loans may exceed 100% LTV only to the extent of the financed up-front guarantee fee.
- The purchase price of the property is permitted to exceed these limits for borrowers with sufficient cash reserves to pay the difference.
- A newly constructed dwelling that does not meet the definition of an existing dwelling and cannot meet the requirements for a newly constructed dwelling is limited to a loan-to-value of 90% of the present market value.
  - Regardless of the LTV, the dwelling must meet or exceed the International Energy Conservation Code (IECC) in effect at the time of construction.

Loan Term

- Consideration must be given as to whether or not the loan could be made without a guarantee.
- If the borrower is able to qualify without the guarantee at the same rate and terms, the loan is not eligible for the Rural Housing guaranteed program.
- The loan term must be 30 years and the loan must fully amortize in that period.

Unacceptable Loan Terms

- Adjustable rate mortgages (ARMS);
- Balloon mortgages;
- Mortgages with terms other than 30 years;
- Interest on interest or negative amortization or any non-fully amortizing loans; and
- Prepayment penalties.

Reasonable and Customary Expenses

Loan Acquisition Expenses

- These include:
  - Legal, architectural and engineering fees;
  - Title clearance costs;
  - Insurance costs;
  - Guarantee fees;
  - Appraisal fees;
  - Surveys; and
  - Homeownership counseling expenses
- **Reasonable Lender Fees.** Lender fees may include an origination fee and other fees and charges.
  - Lender fees and charges must meet the points and fees limits published by the Consumer Financial Protection Bureau (CFPB) and cannot exceed those charged other borrowers for similar transactions such as FHA-insured or VA-guaranteed first mortgage loans.
  - Payment of other fees, charges, or commissions, such as finder's fees or placement fees for referral of a prospective borrower to the lender or administrative fees charged to the buyer by the realtor is prohibited.
  - Discount points that reduce the effective interest rate.
  - **Note,** the Rural Housing up-front guarantee and annual fee are not included in the lender fees and charges calculation.

- **Closing Costs.** Closing costs that are reasonable and customary for the area can be paid for with loan funds.
  - Closing costs cannot exceed those charged other borrowers by the lender for similar transactions such as FHA-insured or VA-guaranteed first mortgage loans.
  - Seller contributions, or other interested parties, are limited to 6% of the loan amount and must represent an eligible loan purpose.
  - Closing costs and/or prepaid items paid by the lender through premium pricing are not included in the seller contribution limitation.
  - Closing costs, including lender fees, may not exceed the total loan amount.

Borrower Characteristics

Borrower Eligibility Requirements

- **Owning a Dwelling** – The borrowers may not own any other real property.
- **Ability to Obtain a Conventional Loan** – Rural Housing loans are only available to borrowers who are unable to secure conventional credit from other sources upon terms and conditions which the borrowers cannot reasonably fulfill. Traditional conventional credit is defined for Rural Housing purposes as:
  - The borrower has available personal non-retirement liquid verifiable asset funds of at least 20% of the purchase price that can be used as a down payment;
  - The borrower can, in addition to the 20% down payment, pay all closing costs associated with the loan;
  - The borrower can meet qualifying ratios of no more than 28% PITI and 36% DTI when applying the 20% down payment.
  - The borrower demonstrates qualifying credit for such a loan and the conventional mortgage loan term is for a 30-year fixed rate loan term that does not require private mortgage insurance.
  - If the borrower meets the cumulative criteria of traditional conventional credit as defined above, the borrower is ineligible for a Rural Housing loan. It is the underwriter's responsibility to support the ineligibility for conventional credit.
  - Liquid assets for conventional credit down payment purposes typically consist of cash equivalents which include:
    - Funds in the borrower's checking or savings accounts;
    - Investments in stocks, bonds, mutual funds, certificates of deposit; and
    - Money market funds.
  - Cash equivalents do not include:
    - Individual Retirement Accounts (IRA);
    - 401k Accounts;

    - KEOUGH Accounts; or
    - Other retirement accounts that are restricted and may not be accessed without incurring substantial monetary penalties.
- **Occupying the Property** – The Borrower must agree to personally occupy the dwelling as a principal residence **throughout the term of the loan**. The borrower must occupy the home within 60 days of closing.
    - Active duty military borrowers may be eligible for a Rural Housing loan. They must occupy the property as their principal residence.
    - The military borrower must express intent to meet occupancy requirements upon his/her discharge from the service.
    - A military service person who cannot physically reside in the property because they are on active duty will be considered to meet occupancy requirement if the service person's family will continue to occupy the property as their principal residence.
- Due to the probability of relocation after graduation, full-time students cannot obtain a Rural Housing loan unless they intend to make the home a permanent residence and there are reasonable prospects of securing employment in the area after graduation.
- **Legal Capacity** – the borrower must be considered an adult under state law and must have the legal capacity to incur the loan obligation. A borrower with a court-appointed guardian or conservator, who is empowered to obligate the borrower in real estate matters, is eligible for a Rural Housing loan.
- **Not Suspended or Debarred** – Individuals who have been suspended or debarred from participation in federal programs are not eligible for a Rural Housing guaranteed loan.
    - The underwriter is responsible for screening the borrower and other parties to the transaction in the DataVerify system accessed through Lending QB.
- **Having Acceptable Citizenship or Immigration Status** – The borrower must be a U.S. citizen or a qualified alien.
    - Aliens must provide evidence that they are qualified aliens.
    - Examples of supporting documentation required for submission to Rural Housing to validate alien status are:
        - I-327 (Re-entry Permit)
        - I-551 (Permanent Resident Card)
        - I-571 (Refugee Travel Document)
        - I-766 (Employment Authorization Card)
        - Certificate of Citizenship
        - Naturalization Certificate
        - Machine Readable Immigrant Visa (with Temporary I-551 language)
        - Temporary I-551 Stamp (on passport or I-94)
        - I-94 (Arrival/Departure Record)
        - I-94 (Arrival/Departure Record) in Unexpired Foreign Passport
        - Unexpired Foreign Passport
        - I-20 (Certificate of Eligibility for Non-Immigrant (F-1) Student Status)
        - DS2019 (Certificate of Eligibility for Exchange Visitor (J-1) Status)
- From the above list(s) obtain proof of identity and evidence that non-citizens who apply for a guaranteed loan are qualified aliens.
    - Prior to requesting a Conditional Commitment, send the alien documentation information to the Rural Housing office that has jurisdiction in the subject property's state.
    - Rural Housing personnel will submit the information to their SAFE system and will provide evidence indicating whether or not the borrower is a qualified alien.

Income Analysis

Income Definition

- Four income definitions are used:
    - **Annual Income**. The income of **all adult household members**;
    - **Adjusted Annual Income**. The household's annual income minus certain qualified household deductions;
    - **Eligibility Income**. Adjusted annual income compared to established income limits, which is used to determine eligibility of the household for Rural Housing guaranteed loans. The moderate income limits must be met.
    - **Repayment Income**. The stable and dependable income used to calculate debt ratios and determine whether the borrower can afford the home.

Validation of Household Income

As of December 21, 2017 Rural Housing has suspended the requirement of signed IRS *Form 4506-T* for all household members until further notice. This applies to all GUS and manually underwritten loan submissions. The requirements listed below do not apply at this time. They will be re-instated upon notification from Rural Housing that the suspension has been lifted

- Each adult member of the household regardless of income source must complete and sign IRS Form 4506-T for the previous two tax years **at the time of the loan application.**
    - Tax transcripts must be received **prior to submission to Rural Housing for a request for Conditional Commitment.** This would include a "no record" result when a member of the household did not file a tax return for the years requested.
    - If tax transcripts are not able to be obtained, the following alternative method to validate household income is permitted in limited situations. This method is typically used when the automated return message from the IRS is due to "limitations". This type of message usually indicates the tax payer's tax return transcript has been flagged by the IRS due to possible identity theft.
        - Provide evidence in the file that the IRS could not fulfill the online order request.
        - The borrower(s) may order their own transcripts.
        - All schedules must be requested by the borrower for the previous two tax years. If the borrower has not filed the previous tax year, request the two years previous to the most recent tax filing year and support the most recent tax filing year with verification of previous year's earnings together with current income verifications.
- Determine which transcripts are necessary to validate the household's income such as:
    - W2 transcripts
    - 1040 transcripts
    - 1099 transcripts
    - Government payment transcripts
    - Cancellation of debt transcripts
- Transcripts provide an excellent quality control check to ensure all income and asset earnings reported to the IRS from all adult household members has been disclosed.
- If the IRS transcripts reveal additional income or asset sources that were not previously disclosed, follow up and verify these income sources. Resolve any discrepancies noted in the IRS transcripts.

Underwriters are still required to perform their due diligence in reviewing income and asset documentation for all household members.

Temporary Guidance for Validating Household Income

- *Determine which type of documentation is necessary to validate the household's income and obtain:*
    - *W2 Forms;*
    - *Federal Income Tax Returns;*
    - *1099 Forms (including 1099 Forms reporting any cancellation of debt);*
    - *Award Letters;*
    - *Or any other necessary documentation to verify all adult household members' income from all sources.*

Projected Annual Income

- Current income and family circumstances should be used to estimate the household's annual income over the coming twelve months unless there is verifiable evidence of a likely change in circumstances. For annual income consider income that is attributable to any household member.
- For annual income count only the first $480 of earned income from adult full-time students who are not the borrower, co-borrower, or spouse.
    - The income of a borrower's spouse, unless the spouse has been living apart from the borrower for at least three months (for reasons other than military or work assignment), or court proceedings for divorce or legal separation have been commenced must be included in the calculation of annual income.

Income that Must be Included in the Annual Income Calculation:

- **Employment Related Income:** For base wages/salaries, overtime pay, commissions, fees, tips, bonuses, housing allowances, and other compensation for personal services use the gross amount before any payroll deductions.
    - If a cost of living allowance or a proposed increase in income has been verified to take place on or before loan approval it will be included in the annual income calculation.
    - A deduction is allowed for verified business expenses (2106 unreimbursed expenses).
- **Business, Farm, and Professional Net Income:** The following provisions apply:
    - Farm and non-farm business losses (negative income) are considered "0" in determining annual income. A negative amount must **not** be used to offset other family income.
    - A deduction, based on straight line depreciation, is allowed for the exhaustion, wear and tear, and obsolescence of depreciable property used in the operation of a farm, business or profession by a member of the household.
    - For home-based operations such as child care, product sales, and the production of crafts, housing related expenses for the property being financed such as mortgage interest, real estate taxes, and insurance, which may be claimed as business expense deductions for income tax purposes**, will not be deducted** from annual income.
- **Withdrawals of Salaries, Cash or Assets from a Business, Farm or Profession:** Distributions to family members from the farm, business or profession will be included in income.
- **Assets:** The assets of all household members are considered. Many types of assets generate income that must be included in the calculation of annual income. Borrowers must provide information about household assets at the time of loan application.
- **Interest and Dividend Income:** Interest, dividends and other net income of any kind from real or personal property including:
    - The share received by adult members of the household from income distributed from a trust fund.
    - Any withdrawal of cash or assets from an investment.
    - Where the household has net family assets in excess of $5,000, the greater of the actual income derived from all net family assets or a percentage of the value of assets based on the current interest rate attributable to the account.
- **Periodic Payments:** The full amount of periodic payments received from social security (including social security received by adults on behalf of minors or by minors intended for their own support), annuities, insurance policies, retirement funds, pensions, disability or death benefits, and other similar types of periodic receipts.

- **Payments in Lieu of Earnings:** Such as unemployment and disability compensation, worker's compensation, and severance pay.
- **Public Assistance:** Unless excluded by law.
- **Periodic Allowances:** Such as:
  - Alimony and child support awarded by the court in a divorce decree or separation agreement unless the borrower certifies the payments are not received and the borrower provides documentation that he or she has taken all reasonable legal actions to collect the amounts due, including filing with the appropriate courts or agencies responsible for enforcing payment; or
  - Recurring monetary gifts or contributions from an organization or person who is not a member of the household.
- **Other:** All regular pay, special pay (except for persons exposed to hostile fire), and allowances of a member of the armed forces who is the borrower or spouse, whether or not that family member lives in the home.

Calculation of Income

- Historical data may be utilized to project annual income in certain circumstances. For example, if a household member works overtime in winter, but the income is being verified in the summer, historical overtime may be used to determine annual income.
- Historical information may also be used to estimate annual income that is anticipated to be received for less than twelve months. If a household member is a seasonal worker, the income attributable to that worker should be based upon past history rather than annualizing the current income.
  - For example, for a family member, who currently does not have income but historically has seasonal income during the summer months, confirm with the borrower and employer that the same seasonable pattern is expected and use historical data to project the annual income for the coming twelve months.
- If any adult member of the household is not presently employed but there is a recent history of such employment, that person's income **will be** considered in the calculation of annual household income.
  - If the person involved is not presently employed and does not intend to resume employment in the foreseeable future, the borrower and person involved must sign a statement to such.
- Once the income source is verified, project the expected income from the source for the next twelve months.
  - This calculation is used only to determine the household eligibility for a Rural Housing guaranteed loan.
  - This calculation does not necessarily represent stable and dependable income for calculating repayment income.
  - This projection should be based on a comparison and analysis of the figures derived to establish earning trends and avoid underestimating annual income for the household.
  - The calculation of annual income must be the most representative of income likely to be received during the next twelve months.
    - **Conservatively selecting the lowest projected income figure without analysis is not acceptable.**

Temporary Income of Absent Family Members

- Household members may be temporarily absent from the household for a variety of reasons such as temporary employment or students who live away from home during the school year.
- A student is considered a member of the household if either of the following conditions is met:
  - The student lives or proposes to live in the dwelling at any time during the coming twelve months; or
  - The property is listed as the student's permanent address.
- If the absent person is not considered a member of the household and is not a party to the transaction, do not count that individual's income when calculating annual income, do not consider that person when determining deductions for adjusted annual income, and do not consider the individual as a family member when determining which income limit to use.

Verification Requirements – Eligibility Income

- The borrower must provide the income, expense and household information needed to enable the underwriter to make income determinations.
- Facsimiles, photocopies, computer images and computer-generated documents may be used instead of original forms.
- Income documentation cannot be greater than 120 days old at time of loan closing.
- The documents must be legible and free of any alterations, erasures, "white-outs", or similar indications that changes have been made.
- Eligibility for a Rural Housing guaranteed loan is **based upon all income received in the household regardless of whether or not the adult household is a party to the transaction.**

Full Documentation

- When using full documentation the file must contain the following as applicable:
  - **Employment Income** – A written VOE to verify the borrower's or household member's YTD and previous year's employment earnings and the most recent paycheck stub to support the information on the written VOE. Employment income may include base income, overtime, bonus, commissions or other employment income earned.
  - Overtime, Bonus or Commission Income: Consider the previous history of these income types from the same employer or same line of work together with the employment verification of continuance when calculating annual income.
    - Employee Differential Payments/Housing Allowances: Include these types of payments as gross income when calculating annual income.
    - Automobile/Expense Allowance/Per Diem: If the allowance/reimbursement is shown on the earnings statement as "gross earnings" it must be included in the annual income calculation.
    - Unreimbursed Employee Expenses: The amount of unreimbursed employee expenses will be deducted from the calculation of annual income when supported on IRS Form 2106.
  - **Military Income** – Pay allowances and other types of income should be included in the calculation of annual income when there is a history of receipt and it will continue to be paid. The hazardous duty pay to a service person exposed to hostile fire (combat pay) will not be included in the calculation of annual income.
  - **Self-Employed Income** – Self-employed income is to be verified with two consecutive years of signed federal income tax returns. Signed business tax returns for the most recent two years, year-to-date profit and loss and balance statements are required but do not need to be audited. Fannie Mae Form 1084, *"Cash Flow Analysis"* and Fannie Mae Form 1088, *"Comparative Income Analysis"* should be used to document a trend analysis for the borrower's or household member's business. **A business with a loss will be considered zero for the annual income calculation.**
  - **Non-Employed Income** – Examples of other income types are alimony/child support, pension/retirement income, social security/disability income, trust income, notes receivable, etc. Obtain a copy of the most recent award letter, pension statement, 1099, federal income tax returns for the most recent tax year or other appropriate documents for other types of non-employed income. Documentation must be dated within the last twelve months.
  - **Unemployment Income**: Unemployment compensation must be computed as the estimated amount for the upcoming 12 months with consideration to the history of this income type for the previous twelve months.
    - Retirement Income: Retirement payments that have a history of receipt and will continue for the next 12 months will be included in the annual income calculation.
    - Public Assistance Income: Obtain a copy of the most recent award or benefit letter for public assistance. Documentation must be dated within the last twelve months.
    - Child Support or Alimony Income: Obtain a copy of the recorded divorce decree, separation agreement or other recorded documents indicating the amount of required alimony or child support payments. Obtain proof of receipt of payments from one of the following:
      - ✓ Court payment records, cancelled checks or bank statements clearly showing the deposit for the subject income.

- ✓ If a borrower or household member who is separated does not have a separation agreement that specifies alimony or child support payments, consider any voluntary payment that is reoccurring in the annual income calculation.
- **Seasonal Employment Income** – Seasonal employment must be supported with the most recent two year history of federal income tax returns, W2s and/or 1099 statements.
- **Rental Income** – Rental income must be considered in the annual income analysis regardless of its duration. Rental income, for annual income purposes, is considered the total rental real estate income amount reported on the most recent Schedule E for the previous twelve months.
  - In the absence of a Schedule E, cancelled checks, money order receipts, bank statements or other documentation may be used to support the amount of rent received for annual income purposes. Any negative net rental income is treated as **zero** for the purposes of calculating annual income.
- **Other Income** – Unemployment benefits, disability and worker's compensation must be supported with the most recent award or benefit letter prepared and signed by the authorizing agency to verify the non-employment income. Computed annual income will be the estimated amount for the upcoming 12 months with consideration to the history of this type of income for the previous 12 months.

Alternative Documentation

- When using alternative documentation for employed borrowers and/or adult household members obtain the following:
  - W2s for the previous two years that clearly identify the borrower or household member and the employer;
  - Paycheck stubs or payroll earnings statements covering the most recent 30 day period which reflects the borrower's or household member's gross earnings for both the most recent pay period and for year-to-date. The document must clearly identify the employee by name and/or social security number, the employer's name and source of information; and
  - A verbal VOE from the current employer.
- Employers may provide electronic access to employment and income verification information. When using this form of documentation the automated verification must provide essentially the same detailed employment and income information that is obtained using the written verification form including year-to-date and previous year's pay history. The file must contain the following:
  - Electronic verification or other computer generated documents accessed and printed from an intranet or internet.
  - The electronic verification or other computer generated document accessed must cover the most recent pay period as of the date of the initial loan application.

Calculating Income from Assets

- **For the purpose of computing annual income, the assets of all household members are considered**.
  - Many types of assets generate income that must be included in the calculation of annual income.
  - Borrowers and household members must provide information about assets at the time of loan application.
- **Interest Income from Liquid Assets** – Examples of liquid assets could include checking accounts, savings accounts, certificates of deposit, and money market accounts. Verify assets by obtaining the most recent two consecutive monthly bank statements.
- Banks calculate the average monthly balance by adding together each daily closing account balance throughout the month. The sum of the daily account balances are divided by the number of days in the month. For example, if the daily account balance is $1,345, which is divided by 30 for the number of days in April, the average monthly balance is $48.33.
- **Net Family Assets Income** – Documentation of income from net family assets must be included in the calculation of annual income. Verify and document assets as part of the annual income calculation.

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Assets Not Considered in Income Calculations

- Retirement savings are not included in the calculation of assets when determining annual income. The following assets are not to be considered in the annual income calculation:
  - Amounts in retirement and pension plans;
  - Individual retirement accounts (IRA);
  - 401(k) plans;
  - KEOUGH accounts;
  - Cash value of life insurance policies;
  - The value of personal property;
  - Assets that are part of any business, trade or farming operation.
  - The value of an irrevocable trust fund or the value of any trust over which no member of the household has control;
  - Interests in American Indian restricted land; and
  - Any asset on hand that will be used to purchase the property or pay for closing costs.

Market Value, Cash Value and Methods of Calculation

- The market value of an asset is simply its dollar value on the open market.
  - For example, the market value of $2,000 in a savings account is $2,000 and the market value of real estate is its appraised value.
- The cash value of an asset is the market value less reasonable expenses to convert the asset to cash.
  - The cash value of stock worth $5,000 would be $5,000 less any broker's fee. For example, a Certificate of Deposit with a $10,000 balance has a market value of $10,000. However, in order to withdraw funds from the account a withdrawal penalty of $200 is charged. Therefore the cash value of the CD is $9,800.
- There are two ways to calculate the contribution that household assets make toward annual income. The method used depends on whether the cash value of the asset is greater than or less than $5,000.
  - **Cash Value of $5,000 or Less**: The amount of asset income included in the annual income calculation is the actual income that the household derives from these assets.
  - **Cash Value over $5,000**: The amount of the asset income included in the annual income calculation is the greater of:
    - The actual income to be derived from the assets; or
    - An imputed income from assets that is calculated by multiplying the total cash value of assets by a documented local passbook savings rate.
  - For example, the borrowers have the following assets:
    - A Certificate of Deposit with a balance of $2,000 which earned 6.8% ($136) of interest last year. The estimated cash value after paying penalties is $1,750 ($250 in withdrawal penalties and federal tax).
    - A savings account with a $4,000 balance earning 4% annually. $1,000 of these funds will be used for closing. The net value of the savings account is $3,000.
    - A two-month average balance of $300 in a non-interest bearing checking account.
  - The cash value of the assets is $5,050 ($1,750 + $3,000 + $300). Since the total is greater than $5,000 the greater of the actual income or the imputed income must be included in the annual income calculation.
    - In this case the actual income is $256 ($136 from the CD ($2,000 X 6.8%) + $120 from the savings account interest ($3,000 X 4%). The actual income is greater than the imputed income of $202 which is the cash value of the assets ($5,050 X 4% = $202).
    - The income to be used for annual income calculation purposes is $256.

Assets Disposed of for Less than Fair Market Value

- Imputed income from assets disposed of for less than fair market value during the two years preceding the loan closing must be included in the annual income calculation.
  - The amount to be included in the annual income is the imputed income from the difference between the market value of the asset and the amount that was actually received, if any, in the disposal of the asset.

- Assets disposed of for less than fair market value as a result of foreclosure, bankruptcy, divorce, and separation are not to be included in this income calculation.

Adjusted Annual Income

Adjusted Income Calculation

- Adjusted annual income is calculated by subtracting any of the five deductions below that apply to the household from the annual income calculated per the above.
- Not all households are eligible for all deductions. These deductions, household eligibility and documentation requirements are listed below:
  - **Dependent Deduction** – a deduction from annual income of $480 is made for each household member who qualifies as a dependent and will make the home their principal residence. Dependents are:
    - Members of the family who are not the head of household or spouse;
    - Members of the family who are ages 17 or younger;
    - Members of the family with a disability;
    - Children of divorced parents even if the child lives with the family only part of the time; and
    - A full-time student.
    - A divorce decree, custody agreement and/or federal income tax returns are acceptable documentation to evidence the borrower is authorized to claim the dependent.
    - Documentation from the school indicating that the individual is enrolled on a full-time basis is required for students who are 18 years of age or older.
    - A foster child, an unborn child, a child who has not yet joined the family or a live-in aid may never be counted as a dependent.
  - **Child Care Expenses** – Reasonable unreimbursed child care expenses for the care of children age 12 and under are deducted from the annual income if the care enables a family member to work, actively seek employment, or go to school and if no other adult household member is available to care of the children.
    - If the child care enables a household member to work, the expenses deducted cannot exceed the income earned by that household member. If the child care provider is a household member, the cost of the child(ren)'s care cannot be deducted.
    - To qualify for the deduction the borrower must:
      - ✓ Identify the child(ren) who is/are receiving child care and the family member who can work, seek employment or go to school as a result of the care;
      - ✓ Demonstrate that there is no adult household member available to care for the child(ren);
      - ✓ Demonstrate that the child care hours parallel the hours the family member works or goes to school;
      - ✓ Identify the child care provider, the hours of child care provided, the costs; and
      - ✓ If the child care provided enables a family member to go to school, identify the educational institution. The family member need not be a full-time student but the child care hours must parallel the hours the family member goes to school.
  - **Elderly Household Deduction** – A single $400 deduction is subtracted from the annual income for any elderly household member. To be considered an elderly household, the head of household, spouse, or sole member of a family who is party to the note, must be 62 years of age or older or a person with a disability.
  - **Deduction for the Care of Household Members with Disabilities** – Reasonable expenses for the care of a person with disabilities in excess of 3% of the annual income may be deducted from the annual income if the expenses:
    - Enable the individual with disabilities or another family member to work;
    - Are not reimbursable from insurance or any other source; and
    - Do not exceed the amount of earned income included in the annual income by the person who is able to work as a result of the care provided.
    - To qualify for this deduction, borrowers must identify the person with a disability. Obtain verification of the individual's disability from the state review board in the state where the borrower resides, the social security administration or a physician or other medical professional.
    - Typical disability expenses include attendant care to assist an individual with disabilities with the activities of daily living directly related to permitting the individual or another family member

to work, or special apparatus such as wheelchairs, ramps, adaptations to vehicles or work place equipment, if directly related to permitting the person with disabilities or another family member to work.

- **Deduction for Medical Expenses (for Elderly Families Only)** – Medical expenses may be deducted from annual income for elderly households if the expenses will not be reimbursed by insurance or another source, and when combined with any disability assistance expenses, are in excess of 3% of the household annual income. Typical medical expenses include:
    - Services of physicians or other health care providers;
    - Services in hospitals or other health care facilities;
    - Medical insurance premiums or Medicare premiums;
    - Prescription and non-prescription medicine;
    - Dental expenses;
    - Eyeglasses and eye examinations;
    - Medical or health products or apparatus (hearing aids, wheel chairs, etc.);
    - Live-in or periodic medical care (visiting nurses or care attendants); and
    - Periodic payments on accumulated medical bills.
        - ✓ If the elderly household qualifies for the medical expense deduction, expenses of the entire family are considered. For example, if a household included the head (grandmother age 64), her son (age 37) and her granddaughter (age 6) the medical expenses of all three family members would be considered.
        - ✓ While some anticipated expenses can be documented easily, for example, Medicare or other health insurance premiums and on-going prescriptions, others need to be estimated. Use historical information about medical bills to estimate future expenses. However, the estimates should be realistic. For example, if the household has a significant medical bill, count only that portion of the bill that is likely to be paid during the coming year.

Income that is Never Counted

- The following income is never counted as annual income:
    - Income received by live-in aides, regardless of whether the live-in aide is paid by the family or a social service program. Family members cannot be considered live-in aides unless they are being paid by a health agency and have an address, other than a post office box, elsewhere.
    - Employment income of a minor.
    - Employer provided fringe benefit packages, even if displayed on the borrower's pay statements, are not considered in annual income unless reported as taxable income to the IRS.
    - Amounts granted for, or in reimbursement of, the cost of medical expenses.
    - Earnings of full-time students 18 years of age or older in excess of $480 unless the student is a spouse or head of household.
    - Temporary, nonrecurring, or sporadic income including gifts.
    - Lump sum additions to family assets such as inheritance; capital gains; insurance payments under health, accident, or worker's compensation policies; settlements for personal or property losses; and deferred periodic payments of supplemental social security income and social security benefits received in a lump sum.
    - Any earned income tax credit.
    - Adoption assistance payments in excess of $480 per adopted child.
    - Amounts received by the family in the form of refunds or rebates under state or local law for property taxes paid on the dwelling.
    - Amounts paid by a state agency to a family with a developmentally disabled family member living at home to offset the cost of services and equipment needed to keep the developmentally disabled family member at home.
    - The full amount of any student financial aid received by household members.
    - The amount of Section 8 housing vouchers.
    - Payments received on reverse amortization mortgages.

Repayment Income

Stable and Reliable Income

- Repayment income is calculated to determine whether the borrower has sufficient income to repay the mortgage in addition to other recurring debts.
- **Repayment income often differs from the calculation of annual income and the adjusted annual income used to determine if the household is eligible for a Rural Housing loan.**
- To calculate repayment income, count only the stable and dependable income of persons who will be parties to the transaction.
  - **Co-signers are not permitted on a Rural Housing transaction and are not an acceptable source when considering repayment income.**
- The anticipated amount of income and likelihood of its continuance must be established to determine the borrower's capacity to repay the loan.
- The determination of stable and dependable income remains the underwriter's responsibility. **GUS does not evaluate the stability and dependability of repayment income** in the overall risk evaluation. The underwriter must determine the history and stability of earnings prior to entering repayment income into GUS.
- Income from any source that cannot be verified, is not stable, or will not continue must not be used in calculating the borrower's repayment income.
- Stable monthly income is the borrower's verified gross monthly income from all acceptable and verifiable sources that can reasonably be expected to continue for at least the next three years.
- For each income source used to qualify the borrower determine that both the source and the amount of the income are stable.
- There is no minimum length of time a borrower must have held a position to consider employment income as dependable.
  - Many low and moderate income borrowers change jobs frequently due to the nature of employment that is available.
  - Borrowers in this situation should not be penalized for frequent changes in jobs within the same line of work if income continuity has been maintained and the income amount has remained at a consistent level.
- Verify the borrower's employment for the most recent two full years and verify the borrower's income has been stable.
  - If a borrower indicates he/she was in school or in the military during any of this time, the borrower must provide evidence supporting this such as college transcripts or discharge papers.
  - If the borrower has recently re-entered the workforce after an absence to care for a family member or minor child, extended illness, or other reasonable circumstance the borrower must provide documentation to support the reason for the absence from the workforce.
- Analyze the gaps in employment as it relates to the probability of continued income.
- Allowances may be made for seasonal employment as it is typical in several trades such as agriculture and building.
- In most instances a two year history of receiving income is required in order for the income to be considered stable and used for qualifying. Focus on the borrower's occupation, tenure, past employment history and probability of consistent receipt of income.
- Borrowers that have not been employed for twelve months with their current employer or have experienced a significant earnings increase are considered high risk.
  - Ensure the borrower will have the required stable and dependable income to carry the mortgage debt.
  - Caution must be used when the borrower's employment includes a probationary period.
- Reasonable allowances may be made for borrowers with less than twelve months' time on the job with their current employer under the following circumstances:
  - The borrower has recently changed jobs but remains in the same line of work;
  - The borrower frequently changes jobs but demonstrates income continuity;
  - The borrower is a recent graduate as evidenced by college transcripts or a recent member of the military as evidenced by discharge papers who is now entering the civilian workforce.
  - The borrower has recently re-entered the workforce after an absence to care for a family member or minor child, has had an extended illness or other reasonable circumstance; and

  - A borrower will begin a new job with a firm offer letter from the employer indicating a start date within 60 days of loan closing.
    - Verify the borrower will have sufficient income or cash reserves to support mortgage payments and other obligations during the time between loan closing and the start of employment.
- Many income sources such as commission, bonus, overtime, tips and income from a second job require a two year history and two years of income documentation.
  - In some instances less than two years of income receipt may be acceptable with a documented thorough analysis of the borrower's income and a determination that the income is stable and likely to continue for the next three years.
  - If less than two years documentation is used for qualifying the borrower the underwriter must explain on the 1008 their basis for determining the income used and the probability of continuance.
- Other non-employed or non-self-employment income sources such as child support, alimony, public assistance payments, social security (including social security received by adults on behalf of minors), retirement, etc. can be considered stable to the extent that they are likely to be consistently made by the payer and can reasonably be expected to continue for at least the next three years.
- Generally income from self-employment is considered stable and dependable if the borrower has been self-employed for two or more years.
- Projected or hypothetical income from any source is typically not acceptable for repayment purposes.

Salaries, Wages and Other Forms of Repayment Income

- The income of each party to the transaction must be analyzed to determine whether it can reasonably be expected to continue.
- If a borrower's regular employment is less than a typical 40 hour work week, the stability of that income should be evaluated as any other regular, on-going primary employment. This would include, for example, a registered nurse that has been working 24 hours per week for the last year.
- If the borrower intends to retire within the next twelve months, the repayment income will be the amount of retirement benefits, social security payments, and other retirement income.
- **Employed Income** – Stable income may be income from primary or secondary employment, including base earnings plus consistent and documented secondary income such as bonuses, commissions, overtime, additional part-time employment or seasonal employment.
- **Newly Employed** – Income for a borrower who has less than a two year employment and income history can be considered when supportive documentation is obtained indicating that the borrower was either attending school or a training program immediately prior to their current employment.
- **Significant Increases or Decreases in Income Level** – When a borrower has experienced a significant decrease in income, the previous higher income level cannot be averaged for repayment purposes unless there is documentation of a one-time occurrence (such as an injury) that prevented the borrower from working or earning full income for a period of time. Documentation must be obtained to show that the borrower is back to the income level previously earned.
  - When a borrower has experienced a significant increase in income and is to be qualified at the higher amount, sufficient documentation to confirm the increased income is stable and likely to continue must be obtained.

Income Calculation

Calculation of Monthly Repayment Income from Primary Employment

- The following table is to assist in calculating base earnings from primary employment paid on an hourly, weekly, bi-weekly, semi-monthly or monthly basis to qualify the borrower.

Calculation of Monthly Repayment Income – Base Earnings	
Frequency	***Calculation of Repayment Income***
Hourly	Multiply the hourly pay rate by the average number of hours worked per week; multiply by 52 weeks; divide by 12 months.
Weekly	Multiply the weekly income by 52 weeks; divide by 12 months.
Bi-Weekly (Every Two Weeks)	Multiply the bi-weekly income by 26 pay periods; divide by 12 months.

Semi-Monthly	Multiply the semi-monthly income by 24 pay periods; divide by 12 months.
Monthly	Use the monthly income from the paystub. Multiply by 12 months.
Paid Less Than 12 Months Per Year	Annual salaries may be received over a period of less than 12 months. Determine how often and how long the borrower is paid. Use the monthly income based upon calculations above. Example, divide an annual salary paid 10 months of the year by 12 to arrive at the average monthly income.

Calculation of Overtime and Bonus Income

- If the amount of the bonus and/or overtime is consistent in the most recent two years, the amount used for repayment income will be the total of the most recent two years divided by 24 months.
    - Unreimbursed business expenses, if applicable are to be deducted.
- If the borrower has experienced a decrease in overtime or bonus income determine the amount of income, if any, which can be justified as stable and document the reason for the decrease.

Calculation of Commission Income

- The borrower must have a two year consecutive history of receiving commission income and it must be likely to continue for the next three years.
- Commission income from the current employer should be averaged over the previous two years.
- Obtain two years' tax returns and W2s along with the most recent year-to-date paystub.
    - Unreimbursed expenses, if any, must be subtracted from the commission income.
- Commission income received for less than two years, or a decrease in commission income from one year to the next generally cannot be included in repayment income unless there are significant documented reasons to do so.

Part-Time, Second Job, Seasonal Income, and Unemployment

- To use part-time, second job, seasonal, or unemployment income the income must be reported on the borrower's individual federal income tax return for the most recent two year period.
- **Income from a Second Job or Part-Time Job -** May be counted for repayment income if the borrower has worked this position **uninterrupted** for the past two years and will continue to do so for at least the next three years.
    - Second or part-time income refers to jobs taken in addition to regular employment to supplement the borrower's income.
    - Income from a part-time position that has been received for less than two years may be counted if the employer verifies that the income continuance is likely at the level of receipt verified in the past.
- **Seasonal Employment** – Is considered uninterrupted and may be counted if the borrower has worked the **same type of job** for the past two years.
    - Unemployment compensation associated with seasonal employment may be considered repayment income if the borrower has a two year history of receipt and the unemployment compensation is likely to continue for the next three years.

Tax Exempt Income

- If a particular source of income is not subject to federal taxes, for example, certain types of disability payments or military allowances, the amount of continued tax savings attributable to the non-taxable income source may be added to the borrower's repayment income.
    - Income that has been verified to be tax exempt may be "grossed up" by 25%. No other adjustments for tax exempt income are authorized. **Tax exempt income should not be grossed up when calculating annual income.**

Military Income

- In addition to military base pay, military personnel may be entitled to additional forms of pay. Income from variable housing allowances, clothing allowances, flight or hazard pay, rations and proficiency pay is acceptable provided it is verified as continuous, regular and likely to continue.
  - An additional consideration may be the tax-exempt nature of some of these payments.
  - If the borrower is a member of the Reserves or National Guard the reserve duty income may be used for qualifying.

Retirement and Social Security Income

- Obtain verification from the source such as the former employer or the Social Security Administration with a copy of the current award letter or federal tax returns.
- If any benefits expire within the first three years of the loan, the income source may only be considered as a compensating factor in lieu of repayment income.
  - The Social Security Administration benefit verification letter or equivalent document will specifically state benefits will expire if applicable. Otherwise, treat social security income as likely to continue.

Alimony and Child Support

- Income from alimony and child support may be counted if such payments are likely to continue for the first three years of the loan.
- The borrower must provide a copy of the divorce decree/court order, legal separation agreement, or voluntary payment agreement and evidence that payments have been received for the past twelve months.
  - Acceptable evidence of payments received includes the most recent, consecutive twelve months' cancelled checks, deposit slips, or court records.

Interest and Dividend Income

- Obtain tax returns or account statements supporting a two year history of receipt of interest and dividend income.
- This income must be averaged over two years.
  - Any funds derived from these sources that are required for closing must be subtracted before the interest or dividend income is calculated.
  - Documentation of sufficient assets remaining after closing to support continuance of the dividend and interest income at the level used for qualification for the next three years is required.

Employer Differential Payments/Housing Allowances

- If the borrower's employer subsidizes the mortgage payments through direct payments (housing allowance), the amount of the payments are to be considered gross income when calculating repayment ratios.
- These payments may not be used to offset the mortgage payment even if the employer pays the servicing lender directly.
- Obtain documentation to demonstrate that the payments are pursuant to an established, ongoing and documented employer program.
  - The employer must not be an interested party to the transaction and the payments must continue for the next three years.

VA Benefits

- Direct compensation from the U.S. Department of Veterans Affairs paid for a service related disability can be counted if verification is obtained from the Department.
- **A VA education benefit is not an acceptable source of income.**
  - Any amount provided for living expenses may be counted as repayment income.
  - Any student financial aid received for tuition, fees, books, equipment, materials, and transportation **will not** be considered in the repayment income.

Government Assistance Programs

- Income received from a welfare program, unemployment income, worker's compensation, or similar government assistance programs can be used for repayment income. The paying agency must verify the income has been received for the most recent two years and can be expected to continue for three years.
  - If this income is not expected to last three years it may be considered as a compensating factor.
- Unemployment income requires a two year documentation of its receipt and reasonable assurance of its continuance.
  - Unemployment income used for repayment income is generally appropriate for individuals employed on a seasonal basis such as farm workers or resort area employees.
  - Borrowers with a sole source of unemployment benefits as their earnings are ineligible for a Rural Housing guaranteed loan.
- Documentation from the applicable agency that indicates the amount, frequency and the length of time the benefit payment will be received is required.

Automobile Allowance and Expense Account Payments

- The borrower must have a two year consecutive history of receiving an automobile allowance and the allowance must be likely to continue for three years in order to consider the income for repayment purposes.
- The amount by which the borrower's auto allowance or expense account payments exceed actual expenditures may be considered as income. The borrower must provide IRS Form 2106, "*Employee Business Expenses*" for the previous two years to establish the amount of the income that may be added to the repayment income along with verification from the employer that these payments will continue.
- The monthly debt amount must be treated as a recurring debt. If the borrower uses the standard per-mile rate in calculating auto expenses, depreciation may be added back to the repayment income. The borrower's monthly auto payment must be treated as a recurring debt and must not be offset by the auto allowance.

Trust Income

- Income from trusts may be counted for repayment income if it is guaranteed that constant payments will continue for at least the first three years of the mortgage term and if it is adequately documented.
- Documentation requirements include a copy of the Trust Agreement or other trustee's statement confirming the amount, frequency of distribution, and duration of the payments.

Projected Income

- Projected or hypothetical income is not acceptable for repayment purposes.
  - Exceptions are permitted for cost-of-living adjustments, performance raises, bonuses, etc. that are both verified by the employer in writing and scheduled to begin within 60 days of loan closing.
    - If the loan will close more than 60 days before the employment begins, the income cannot be counted for repayment purposes.
    - Use full documentation for this type of income. In the absence of a payroll statement to support income earned for new jobs, a copy of the contract with the employer that validates the amount of income to be earned should be obtained.

Tip Income

- The borrower must have a two year consecutive history of receiving income from tips in order to consider the income for repayment. For tip income that fluctuates, evaluate the income trend and use the amount that is likely to continue for the next three years.

Unreimbursed Employee Expenses

- Unreimbursed employee expenses reported on *IRS Form 2106* must be deducted from the repayment income.

Employed by a Family Owned Business

- A borrower employed by a family owned business is required to provide additional income documentation. These borrowers must provide the usual verification of employment and pay stubs as well as evidence that he or she is not an owner of the business.
  - This may include copies of the borrower's signed personal tax returns, current paystubs, or a payroll ledger signed by the business accountant or payroll administrator or a signed copy of the corporate tax return showing ownership names and percentages.

Self-Employment

- A borrower with a 25% or greater ownership interest in a business is considered self-employed for the purpose of calculating repayment income.
- The business may be a sole proprietorship, a partnership (limited or general), or a corporation.
- A self-employed borrower introduces additional layers of risk to a mortgage loan due to the uncertain nature of future income
  - GUS will not take this additional risk into consideration in the overall risk evaluation.
  - The underwriter is responsible to determine the income source used for qualifying is a stable, consistent source that will continue to be received at the level used for repayment income.
- **Minimum Length of Self-Employment** – Income from self-employment is considered stable and dependable if the borrower has been self-employed for two or more years.
  - Because of the high incidence of failure during the first few years of a new business, income from borrowers self-employed for between one and two years can only be counted if the borrower has at least two years previous successful employment (or a combination of one year of employment and formal education or training) in a related occupation or profession at the same or greater level in the same or a similar occupation.
- When additional income the borrower draws from his/her corporation, partnership or S-corporation is used for repayment income, additional documentation is required to verify the borrower has a legal right to the additional income.
  - Obtain a corporate resolution or other comparable document that establishes that right. Also confirm the borrower's percentage of ownership of the business entity from a review of business tax returns, letter from the accountant for the business, or similar documents. The underwriter's analysis must support that the business is clearly capable of providing the borrower with the additional income used to qualify.
  - As part of the analysis any increase or decrease in business income must be documented and justified to support a determination that the income used to qualify the borrower is stable and likely to continue for the next three years. It may be necessary to obtain additional years' tax returns when the borrower's self-employment income fluctuates to determine the stability of income.
  - If the borrower's self-employment income is not used to qualify the borrower for repayment, the individual federal tax return is required to determine if there is a business loss that may have an impact on the stable monthly income.
  - If a business loss is reported additional documentation may be necessary to evaluate the impact of a business loss on the income used for qualifying.
    - For the purposes of computing annual income to qualify the household, business losses will be treated as zero in the calculation.
    - Business losses when calculating repayment income will be deducted from the repayment income prior to calculating debt ratios.
- **Documentation** – The following documentation for self-employed borrowers is required to establish capacity to repay the loan:
  - Signed and dated individual tax returns for the most recent two years. If the borrower has been self-employed for less than two years, the individual federal tax returns must reflect at least one full year of self-employment income.
  - A year-to-date Profit and Loss (P&L) statement and Balance Sheet.
  - Signed copies of federal business income tax returns for the last two years if the business is a corporation, an S-corporation, a partnership, or a limited liability corporation.

Analyzing Self-Employment Income

- The borrower's earning trend over the previous two years must be established. A three year average of the business income may be used for repayment purposes if all three years' tax returns are provided.
- If the borrower provides quarterly tax returns, the analysis can include income through the period covered by the tax filings.
- If the borrower does not file quarterly returns, the income shown on the P&L may be included in the analysis provided the income stream based on the P&L is consistent with the previous years' earnings. If the P&L statements submitted for the current year shows an income stream considerably greater than what is supported by the previous two years' tax returns, the analysis of income must be based solely on the income verified through the tax returns.
- Carefully analyze the business' financial strength, the source of its income, and the general economic outlook for similar businesses in that area to determine if the business can be expected to continue to generate sufficient income for the borrower's needs. Annual earnings that are stable or increasing are acceptable. Income from a borrower whose business shows a significant decline in income over the period analyzed may not be considered adequate, dependable, and stable.

Calculating Self-Employment Income

- The borrower's average monthly income must be based on a review of the borrower's complete individual federal tax returns, including W2s and K-1s, if applicable, and the borrower's complete business tax returns (Forms 1120, 1120s, and 1065) as applicable.
- Non-cash items such as depreciation and depletion may be added back to adjusted gross income for the purpose of determining qualifying income.
- **Schedule C Business Income or Loss** – Depreciation or depletion may be added back to net income.
  - Business related debts are often paid with business funds.
  - If a debt such as a car loan is paid through the business, the debt does not need to be included in debt ratio calculations as long as documentation is provided that the debt is being paid by the business with copies of the most recent, consecutive 12 months' cancelled checks.
- **Corporate Income Tax Returns Form 1120** – Compensation of a corporation's officers is shown on the corporate tax returns and will appear on the individual tax returns. If the borrower's percentage of ownership is not shown, it must be separately obtained from the corporations' accountant with evidence the borrower has the right to those funds. Once the adjusted business income is determined it is to be multiplied by the borrower's percentage of ownership in the business. In analyzing the corporate tax return, adjust for the following:
  - Depreciation and depletion may be added back to the after-tax income.
  - Taxable income is the corporation's net income before federal taxes. It must be reduced by the tax liability.
  - Fiscal year vs Calendar year. If the corporation operates on a fiscal year that is different from the calendar year, an adjustment must be made to relate corporate income to the individual tax return.
  - Cash withdrawals. The borrower's withdrawal of cash from the corporation may have a severe negative impact on the corporation's ability to continue operating which must be considered in the analysis of the borrower's business.
- **"S" Corporation Tax Returns** – Both depreciation and depletion may be added back to income in proportion to the borrower's percentage of ownership. However, income must also be deducted proportionately by the total obligations payable by the corporation in less than one year. The borrower's withdrawal of cash from the corporation may have a severe negative impact on the corporation's ability to continue operating which must be considered in the analysis.
- **Partnership Tax Returns** – Both general and limited partnerships report income on *IRS Form 1065*. It must be reviewed to assess the viability of the business. The partner's share of income is carried over to Schedule E of the partner's individual tax return. Both depreciation and depletion may be added back to income in proportion to the borrower's share of income. However, income must also be deducted proportionately by the total obligations payable by the partnership in less than one year.
  - The borrower's withdrawal of cash from the partnership may have a severe impact on the partnership's ability to continue operating that must be considered in the analysis.

Documentation Requirements

Electronic Verification of Employment

- Employers may provide electronic access to employment and income verification information.
  - When using this form of documentation, the automated verification must provide essentially the same detailed employment and income information that is obtained using the full documentation employment verification form including year-to-date and previous years' pay history.
  - All verifications must pass directly between the lender and the employer.
  - The file must contain the following:
    - Electronic verification or other computer generated documents accessed and printed from the Intranet or Internet.
    - The electronic verification or other computer generated document accessed and printed must cover the most recent pay period as of the date of the initial loan application; clearly identify the borrower as the employee by name and/or social security number and show the borrower's gross earnings for the most recent 30-day period and year-to date; and
    - W2 forms for the previous two years that clearly identify the borrower as the employee.

Expiration of Credit Documents

- Credit documents must be no more than 120 days old on the date the Note is signed.
- When the age of documents is greater than allowed, obtain updated verifications that support the borrower's continued eligibility. Credit documents that require updating are:
  - The loan application;
  - The credit report;
  - Employment verification forms;
  - Pay stubs; and
  - Bank statements.

Verbal Verification of Employment

- A verbal verification of employment for all salaried borrowers must be done within ten business days prior to the Note date.
- Confirm with a third party source the existence of a borrower's business no more than 30 calendar days prior to the Note date for self-employed borrowers.
- Acceptable third party sources include, but are not limited to:
  - A regulatory agency,
  - The phone directory,
  - The internet directory assistance or the applicable licensing bureau.

Documents Handled by Third Parties

- Documents relating to credit, employment, or income of borrowers that have been handled by, or transmitted from or through the equipment of interested third parties **may not** be used. Interested third parties are:
  - Real estate agents;
  - Builders; or
  - Sellers

Ratio Analysis

The Ratios

- Ratios are calculated by using the repayment income. To qualify for a Rural Housing guaranteed loan the borrower must meet Rural Housing's requirements for both PITI and DTI ratios.

PITI Ratio

- Borrowers are considered to have repayment ability if their proposed monthly housing expense does not exceed 29% (manual underwriting) of their repayment income or per the GUS "Accept" underwriting recommendation. Monthly housing expenses include the following:
  - Principal and interest payment;

- Hazard insurance premiums;
- Real estate taxes;
- Monthly amount paid for the Rural Housing annual fee;
- Homeowners' association dues and regular assessments;
- Flood insurance premiums; and
- Special assessments, if applicable.

DTI Ratio

- Borrowers are considered to have repayment ability when their total debts do not exceed 41% (manual underwriting) of their repayment income or per the GUS "Accept" underwriting recommendation.
- Total debt includes monthly housing expense PITI plus any other monthly credit obligations incurred by the borrower.
- All of the borrower's open debts/accounts, including collection accounts and judgments, incurred through the **Note date** must be included in the total debt calculation and be listed under the liabilities section of the loan application. Monthly obligation expenses include:
  - PITI.
  - Long term obligations with more than ten months repayment remaining which include all installment loans, alimony, child support or separate maintenance payments, student loans and other continuing obligations.
  - Revolving accounts. The minimum monthly payment is required for all revolving credit card debts. If the credit report shows an outstanding balance, but no specific minimum monthly payment, the payment will be calculated at 5% of the balance as reported on the credit report.
    - A copy of a current statement reflecting the actual monthly payment may be used to determine the payment for repayment purposes.
    - Revolving accounts with no outstanding balance do not require an estimated payment to be included in the debt ratio.
    - Revolving accounts that will be paid in full prior to loan closing are not required to be closed.
  - 30-Day Accounts. Use the credit report to document the borrower has paid the outstanding balance in full for each of the previous twelve months.
    - 30-day accounts that are paid in full monthly are not included in the total debt ratio.
    - If the credit report reflects any late payments in the last twelve months, a monthly payment calculated at 5% of the outstanding balance is to be included in the total debt ratio.
  - Child Support and Alimony. Borrowers obligated to pay child support, alimony, garnishments or other court ordered debts must have the payment included in the total debt ratio. If the borrower has a release of liability from the court/creditor, and acceptable evidence is obtained, the debt can be excluded.
    - For GUS transactions manually enter the obligation in the "Additional Expenses" section of the "Assets and Liabilities" page. The manual entry of these types of obligations does not require an underwriting recommendation of "Accept" to be downgraded to a "Refer". Ensure repayment agreements are current.
  - Child care expenses are not required to be considered as a recurring liability when calculating the total debt ratio.
  - Student loan payments must be included as follows:
    - <u>Fixed Payment Loans</u> - A permanent amortized, fixed payment may be used in the debt ratio when documentation is provided to verify the payment is fixed, the interest rate is fixed and the repayment term is fixed.
    - <u>Non-Fixed Payment Loans</u> - Payments for deferred loans, income based repayment (IBR), graduated, adjustable and other types of repayment agreements which are not fixed cannot be used in the debt ratio calculation. One percent (1%) of the loan balance must be used as the monthly payment. No additional documentation is required.
  - Previous Mortgages. Previous mortgage liabilities disposed of through a sale, trade or transfer without a release of liability will be included in the total debt ratio unless evidence can be obtained to confirm the remaining party or new owner has successfully made the payment for the previous twelve months prior to the loan application.

    - In the case of divorce obtain a copy of the divorce decree to document the remaining party is responsible to pay all mortgage debts from the effective date of decree forward.
    - If the loan was assumed, sold or traded without a release of liability, a copy of the assumption agreement and deed showing transfer of title out of the borrower's name must be obtained.
        - ✓ In both of the above cases documented evidence the remaining party or new owner has been making regular payments during the previous twelve months with no history of delinquent payment must be obtained.
- Co-signed Obligations. Co-signed debts must be considered in the total debt ratio unless the borrower provides evidence another **obligor** has made the payment on time in the previous twelve months prior to the loan application.
    - Acceptable evidence that demonstrates the remaining co-obligor's history of making regular payments during the previous twelve months include cancelled checks, money order receipts, and bank statements. If the co-obligor has made any late payments in the previous twelve months the debt must be included in the borrower's total debt ratio.
    - **Debts identified as "individual" on a credit report will always be considered in the debt ratio regardless of what party is making the monthly payments**. For example, when parents make car payments on behalf of the borrower but the loan is in the borrower's name only, the payment must be included in the borrower's total debt ratio.
- **Business Debt**. Business debt reported on the borrower's personal credit report may be excluded from the debt ratio if the debt is paid through a business account. Twelve months' cancelled business checks are required to document the business makes the payment.
- **401(k) Loans/Personal Asset Loans**. Loans pledging assets such as a 401(k) account, retirement funds, savings account or other liquid assets are not considered in the total debt ratio.
- **Debts of a Non-Purchasing Spouse**. For borrowers who reside in or are purchasing in a community property state, the debts of their spouse must be included in the borrower's total debt ratio.
- **Collection Accounts**. If a repayment agreement has been established with the creditor the payment must be included in the total debt ratio.
- **Judgment Accounts**. Judgment accounts with a repayment plan already established with a history of consistent repayment will be included in the borrower's total debt ratio.
- **Charged-Off Accounts**. Charged off accounts are not required to be included in the borrower's total debt ratio.
- **Automobile Allowances and Expense Account Payments**. The amount of actual expenditures exceeding the amount of automobile allowance or expense account payments will be treated as recurring debt. Use *IRS Form 2106*, "*Employee Business Expenses*", for the previous two years and employer verification that the payments will continue as documentation to support the calculation.
    - The borrower's monthly car payment will be treated as a recurring debt and may not be offset by any car allowance.
- **Short term obligations**. If a short term obligation has a significant impact on repayment ability it must be included in the total debt ratio. A significant impact on repayment is defined as 5% or greater of the monthly repayment income of the borrower. Installment debt may be paid down to a repayment balance of ten months or less, however, underwriters must include any debt that, in their underwriting analysis, is considered a significant impact to the borrower's ability to repay the debt.
- **Balloon/Deferred Payments/Payments Due in the Next 24 Months**. These include personal loans with deferred installments and balloon payments. If the actual payment on a deferred loan is unknown, estimate the monthly payment using 5% of the outstanding balance.
    - This does not include deferred student loans. Refer to the "Credit Analysis" section for direction on deferred student loans.
- Obligations for child care, voluntary contributions to a retirement account and open accounts with zero balances are not considered a debt.

Debt Ratio Waivers and Compensating Factors

- A borrower's PITI ratio may exceed 29% and the DTI ratio may exceed 41% if the underwriter determines that strong compensating factors demonstrate the borrower has the ability to repay the mortgage.
- GUS Underwritten Loans Receiving an "Accept" – GUS files that receive an "Accept" underwriting recommendation do not require a debt ratio waiver request.
- Debt Ratio Waiver Request and Rural Housing Approval - The underwriter must send debt ratio waiver requests to Rural Housing along with supporting documentation at the time the loan is submitted to Rural Housing for a Conditional Commitment. A request for a ratio waiver is done by submitting a signed underwriting analysis that cites one or more acceptable compensating factors. *Form Fannie Mae 1008*, *"Uniform Underwriting and Transmittal Summary"* may be used when requesting the waiver.
  - Written approval of the debt ratio waiver request by Rural Housing is confirmed if a Conditional Commitment is issued.
- Debt Ratio Waivers for Purchase Transactions – For manually underwritten loans, Rural Housing approval of an underwriter's request for a debt ratio waiver may be granted if the following conditions are met:
  - The PITI ratio is greater than 29% but less than or equal to 32% with a DTI ratio that does not exceed 44%; Or
  - The DTI ratio is greater than 41% but less than or equal to 44% with a PITI ratio that does not exceed 32%; and
  - The credit score of all applicants is 680 or greater; and
  - At least one of the acceptable compensating factors listed below is identified and supporting documentation is provided to Rural Housing.
- Debt Ratio Waivers for Refinance Transactions – For manually underwritten full refinances the underwriter must fully document the compensating factors that justify a debt ratio waiver. Debt ratio waivers can be approved when acceptable compensating factors are present.

Acceptable Compensating Factors and Documentation

- **Purchase Transactions**
  - The proposed PITI is equal to or less than the borrower's current verified housing expense for the twelve month period preceding the loan application.
    - Verification of housing expenses may be documented on a Verification of Rent (VOR) or credit report. The VOR or credit report must include the actual payment amount due and report there have been no late payments for the previous twelve months.
    - Rent or mortgage payment histories from an individual or from a family member will not be considered unless twelve months of cancelled checks, money order receipts, or bank statements are provided.
    - A history of less than twelve months will not be considered an acceptable compensating factor.
  - Accumulated savings or cash reserves available are equal to or greater than three months' PITI payments. Two months most recent consecutive bank statements documenting the average balance held by the borrower are required. **Cash on hand is not eligible for consideration as a compensating factor.**
- **Refinance Transactions**
  - Credit scores of 680 and higher can be used as a stand-alone compensating factor for a debt ratio waiver request if no additional risk layers are present such as adverse credit or payment shock.
  - The borrower has successfully made, for the past twelve months, the existing mortgage payment in an amount that is equal or greater than the new proposed monthly mortgage payment.
  - The borrower has demonstrated a conservative attitude toward the use of credit.
  - The borrower has demonstrated the ability to accumulate savings comparable to the difference between current housing costs and projected costs.
    - The use of retirement accounts as compensating factors and as cash reserves is limited to 60% of the vested amount of the retirement asset.
    - Retirement accounts that restrict withdrawals to termination of employment, retirement or death may not be considered as a compensating factor for cash reserves.
  - Continuous employment with the current primary employer.

Obligations Not Included in Debt-to-Income Ratios

- Medical Collections;
- Federal, State and Local Taxes;
- Social Security/Medicare Withholding;
- Other Retirement Contributions such as 401(k) Accounts;
- Automatic Deductions for Savings Accounts, Mutual Funds, Stocks, Bonds, and Certificates of Deposit;
- Collateralized Loans Secured by Depository Accounts;
- Utilities;
- Insurance (other than property insurance);
- Commuting Costs;
- Union Dues;
- Open Accounts with Zero Balances;
- Child Care; and
- Voluntary Deductions.

Assets

Checking/Savings Accounts

- Obtain **the average two month balance of accounts** of the two most recent consecutive monthly bank statements reflecting the previous month's balance.
- Review the bank statements for evidence of any additional household income.
  - Large deposits may indicate additional income as well as the incurrence of recent debt by the borrower to obtain funds to complete the purchase of the subject property.
  - Review unusual deposits that are not consistent with previous history and document the source of the funds.

Earnest Money Deposit

- The earnest money deposit on the sales contract can be considered an asset if the deposit is not already reflected in a liquid asset account.
- If the funds have cleared the borrower's account, place the amount as an "other credit" in the Details of Transaction section of the loan application.
  - For GUS only enter the earnest money one time on either the "Asset and Liabilities" section or on the "Transaction Details" page.

Gifts

- Gift funds may be from the following types of donors:
  - A relative;
  - An employer or labor union;
  - A charitable organization; or
  - A government agency/public entity that has a program to provide homeownership assistance to low and moderate income borrowers.
    - Funds received from non-profit entities may not be used to pay installment loans, credit cards, collections, judgments or other similar borrower debts.
- The donor must be able to furnish conclusive evidence that the funds given to the homebuyer came from the donor's own funds and were not provided directly or indirectly by the seller, real estate agent, builder or any other entity with an interest in the sales transaction.
- Gifts must be documented with a gift donor letter signed by the donor and borrower. The gift letter must indicate that the gift does not have to be repaid.
  - Obtain proof of transfer from the donor to the borrower by obtaining a copy of the cancelled check or other withdrawal document showing the withdrawal is from the donor's personal account; and
  - A copy of the borrower's deposit slip or bank statement showing the gift funds have been deposited to the borrower's account.
- If the gift funds are in the borrower's bank account at the time of the loan application obtain the following:

   - Document the transfer of the funds from the donor to the borrower by obtaining a copy of the cancelled check or other withdrawal document showing that the funds are from the donor's account; and
   - Evidence that the borrower deposited the gift into their personal account.
- If the gift funds are not verified in the borrower's account at the time of application and the transfer occurs at closing, obtain verification that the closing agent received funds from the donor for the amount of the gift and that the funds came from an acceptable source. Acceptable documentation includes:
   - If the transfer of funds is by certified check obtain a copy of the certified check showing the donor is the "remitter" and a bank statement to document the withdrawal from the donor's account.
   - If the transfer of gift funds is from a donor purchased cashier's check, money order, official check or bank check obtain a withdrawal document or cancelled check for the amount of the gift to evidence the funds came from the donor's personal account.
   - If the transfer of funds was via a wire transfer, obtain a wire transfer confirmation to verify the settlement agent received the funds from the donor for the amount of the gift.
- **Cash on hand is not an acceptable source of the donor's gift funds.**
- Gift funds should be reflected on the application as a separate entry to the borrower's depository accounts.
   - Gift funds should not be reflected in the borrower's depository account balances.
- Gift funds will not be considered as cash reserves or as a compensating factor in the underwriting decision.
- Once gift funds are documented, verified and received, for purposes of loan settlement, gift funds are considered the borrower's personal funds. Any excess funds at settlement that represent gift funds contributed may be returned to the borrower.

Sale of Real Estate
- Obtain the final CD or equivalent closing statement to indicate cash sales proceeds to the borrower.
- Proceeds from the sale of real estate should be included in the borrower's liquid assets.
- For GUS enter the information regarding the real property sold or pending on the "REO Property Information" page.
   - For properties with a disposition of "Pending Sale" the calculation of net equity will automatically populate on the "Assets and Liabilities" page.
   - For properties with a disposition of "Sold" on the "REO Property Information" section, manually enter the net equity on the "Assets and Liabilities" page.

Trust Funds
- Obtain a copy of the Trust Agreement or other Trustee statement confirming the amount of funds in the trust and the conditions under which the funds may be withdrawn.

Stocks, Bonds, Savings Certificates, Certificates of Deposit, Money Market Funds and Other Investment Accounts
- The monthly or quarterly statement provided by the stock broker or financial institution managing the portfolio may be used to verify the value of these securities.
- Government issued bonds such as savings bonds are counted at the original purchase price unless eligibility for redemption and redemption value is verified.

Credit Analysis
Credit Eligibility Requirements
- It is the borrower's overall credit management skill such as repayment patterns, credit utilization and level of experience using credit, not only the existence of delinquent credit accounts that has an effect on the eventual default risk of a mortgage.
- Evaluate the credit history for each borrower who will be a party to the note. The borrower's credit record does not have to be perfect to be eligible for a Rural Housing guaranteed loan as long as any isolated instance is fully explained and supported with documentation.
- A few instances of credit problems can be acceptable if the underwriter determines that a borrower's overall credit record demonstrates an ability and willingness to repay obligations.

- An “Accept” underwriting recommendation from GUS eliminates the need to document the credit qualification decision provided the borrower’s credit score has been validated.
- Verify that the borrower has no delinquent federal debt through the Credit Alert Verification Reporting System (CAIVRS). CAIVRS is a federal government-wide repository of information on those individuals with delinquent or defaulted federal debt and those for whom a payment of an insurance claim or guarantee loss has occurred.
  - The GUS automated underwriting system automatically generates a CAIVRS confirmation.

Credit Report Requirements

- Lenox/WesLend requires the use of the automated merged credit report that is generated within the GUS automated underwriting system at the time of loan setup.
- Credit reports must:
  - Be no more than 120 days old when the loan is closed;
  - Be accurate and complete;
  - Provide an account of the credit, residence history, and public record information for each borrower;
  - Be an original document, either the original electronic version or the printed report delivered by the credit reporting agency;
  - Have no whiteouts, erasures or alterations;
  - Indicate the name and address of the consumer reporting agency;
  - Show the primary repository from which the particular information was pulled for each account listed; and
  - Show the name of the party ordering the report.

Credit Scores

- **Credit Score over 680** – Perform a basic level of underwriting to confirm the borrower has an acceptable credit reputation. Perform additional analysis if the borrower’s credit history has indicators of unacceptable credit.
- **Credit Score 679 – 640** – Perform a comprehensive level of underwriting. Underwrite all aspects of the borrower’s credit history to establish the borrower has an acceptable credit reputation. Credit scores in this range indicate the borrower’s reputation is uncertain and will require a thorough analysis by the underwriter to draw a logical conclusion about the borrower’s commitment to making payments on the new mortgage obligation. The borrower’s credit history should demonstrate past willingness and ability to meet credit obligations.
- **A borrower with an *outstanding* judgment obtained by the United States in a federal court, other than the United States Tax Court, is *not* eligible for a Rural Housing loan.**

Acceptable Credit Scores for Automated Underwriting (GUS)

- GUS will determine the applicable score when developing an underwriting recommendation.
- The credit score used by GUS represents the overall credit reputation risk for the loan.
  - **The minimum allowable credit score for this program is 640.**
- Indicators of unacceptable credit are already considered in the risk evaluation considered by GUS when rendering an underwriting recommendation.
- The underwriting score is located in the “Credit Report” section of the GUS recommendation report.

Validating the Credit Score

- Credit scores are an integral part of the risk assessment. Credit scores are used to underwrite a borrower’s credit reputation. Too little information, or information that is significantly inaccurate makes the credit score unusable for underwriting.
- A usable score ensures that the credit score adequately indicates the borrower’s credit reputation and ensures a fair evaluation of borrowers in using credit scores to evaluate their overall credit reputation.
- For borrowers with usable credit scores the loan can be underwritten with the GUS automated underwriting system.
  - **GUS does not validate the credit score used for the underwriting recommendation. It remains the underwriter’s responsibility to ensure the credit score is valid.**

- Even if the score exceeds the credit score requirement the credit score must be validated and the underwriter must determine that the borrowers have satisfactorily established the willingness and ability to manage and repay obligations as agreed.
- Two or more eligible trade lines are necessary to validate a borrower's credit report score.
  - Eligible trade lines consist of credit accounts (revolving, installment, etc.) with at least 12 months of repayment history reported on the credit report.
  - At least one borrower whose income or assets are used for qualification must have a valid credit score.
  - Confirm the borrower has at least two eligible trade lines reported to the credit bureau. The trade line may be open, closed and/or paid in full. Eligible trade lines include:
    - Secured or unsecured loans;
    - Revolving accounts;
    - Installment accounts;
    - Credit cards;
    - Collections accounts;
    - Charged off accounts; and
    - Authorized user accounts. **These accounts may not be considered in the credit score and credit reputation analysis unless the borrower provides documentation that they have made payments on the account for the previous 12 months.**
  - The following are not considered an eligible trade line to validate the credit score:
    - Public Records such as bankruptcies, tax liens, and judgments;
    - Disputed accounts; and
    - Deferred loans such as deferred student loans without 12 months of repayment history.
  - A credit score may be generated if a repository's file includes only one trade line, however, **the underwriter must not use any score based on fewer than two trade lines.**
  - Loans underwritten with the assistance of the GUS Automated Underwriting System that receive an "Accept" recommendation ***are also*** subject to the credit score validation.
    - GUS applications receiving an "Accept" underwriting recommendation that fail to meet the credit score validation test using a traditional credit report must be downgraded to a "Refer".

Downgrading an "Accept" Underwriting Recommendation

- The following represent examples of when an underwriter will downgrade an "Accept" underwriting recommendation to a "Refer".
  - The underwriting score located in the Credit Report section of the GUS underwriting findings report cannot be validated.
  - Accounts have been manually input into the liabilities section of GUS and do not appear on the credit report and have not been considered in the credit evaluation by GUS.
  - The presence of disputed accounts on the credit report.
  - Trade lines that are authorized user accounts may require a downgrade.
  - When the underwriter is aware of any potential derogatory or contradictory information that is not any part of the data submitted to GUS or if there is any erroneous information in the data submitted to GUS.
  - GUS will evaluate credit for significant credit indicators such as bankruptcies, foreclosure sales, deeds-in-lieu of foreclosure and late mortgage payments.
    - **GUS does not evaluate pre-foreclosure sales, therefore, the underwriter must independently review information regarding pre-foreclosure (short) sales that occurred within the past three years.**

Credit Exceptions

- Credit history problems do not always reflect an unwillingness to meet financial obligations. If the underwriter believes that the borrower is creditworthy, the underwriter should document on the underwriter's analysis the reasons that an exception is justified.
- Exceptions should be made only in the following types of situations:
  - **Temporary Situations** – The circumstances that caused the credit problems were temporary in nature, beyond the borrower's control and the circumstances have been removed and resolved for the 12 months prior to the application. Examples are:

        - Temporary loss of job;
        - Delays or reduction in benefits;
        - Illness; or
        - Disputes over payment for defective goods or services.
    - **Reduced Housing Expenses** – The new loan will significantly reduce the borrower's housing expenses which will result in improved debt repayment ability. A significant reduction in housing expenses would be 50% or more.
- The loan file should contain clear evidence that the underwriter evaluated the credit history and arrived at a conclusion that the borrower's credit history demonstrates an ability to handle financial obligations successfully.
- Rural Housing concurrence is not required for credit exceptions.
- The underwriter **is not** authorized to make an exception in the case of a borrower with a delinquency on a federal debt, or with an outstanding judgment obtained by the United States in a federal court, other than the United States Tax Court.
    - Evidence of payment arrangements is acceptable for an IRS federal tax judgment.
    - A borrower who has made delinquent payments during the payment arrangement term is ineligible for a Rural Housing guaranteed loan.

Prudent Underwriting

- Rural Housing expects that underwriters will act responsibly when originating and underwriting loans. Rural Housing does not re-underwrite the loan. This remains the underwriter's responsibility.
- Underwriters are expected to use professional judgment and rely upon prudent underwriting practices to determine the likelihood of successful homeownership. The use of GUS does not replace the judgment of experienced underwriters. GUS is merely a tool that helps evaluate the credit risk of the loan.

Order and Importance of the Credit Review

- Borrowers are expected to have acceptable credit, a stable income and no recent unsupported debt problems. To meet these requirements borrowers must prove they are creditworthy and unlikely to default on the loan.
- **Previous Rental or Mortgage Payment History** – The borrower's housing obligation payment history holds significant importance when evaluating credit. It is an indicator of the borrower's ability to pay the mortgage payments in the future.
    - Borrowers who make rental or mortgage payments that are the same or more than the anticipated mortgage payment have demonstrated the ability to make future mortgage payments.
    - Unless there is major derogatory credit noted in the credit file, a borrower is considered to have an acceptable credit history if he/she does not have late housing payments.
    - Borrowers who live rent free prior to purchasing a home may require the underwriter to cautiously approach a loan decision. Living rent free and proposing to exceed the required repayment ratios may represent a high risk when unsupported. Approach this type of borrower prudently if approving the application.
    - Loans underwritten with GUS that receive an "Accept" underwriting recommendation are not subject to additional rental or mortgage payment history documentation.
    - Loans that have been underwritten with GUS and receive an "Accept" underwriting recommendation require no further documentation with the presence of late mortgage payments as they have already been considered by the scorecard.
- **Recent and/or Undisclosed Debt and Inquiries** – Determine the purpose of any recent inquiries as indebtedness may have been incurred to obtain funds to close the loan. Any new debt and payment must be included in the final underwriting analysis. A borrow must provide a satisfactory explanation for any significant debt noted on the credit report but not included on the loan application.
    - <u>Automated Underwriting System – GUS "Accept"</u> - Confirm and include any monthly payment amount for debts not considered in the automated underwriting system recommendation. Resubmit the loan for an updated underwriting recommendation.
        - If the debt was not reported on the credit report uploaded into GUS it must be manually added to the "Assets and Liabilities" page in GUS, downgrade to "Refer" and manually underwrite the file. **Exception:** The manual entry of child support, alimony, garnishments and other debts that are not typically reflected on a credit report will not require a downgrade.

- A debt may be added to the credit report and a new credit report obtained that includes the previously recent or undisclosed debt. The new credit report must be re-associated with GUS and GUS must be re-run with the new credit report.
- **Credit supplements obtained outside of GUS *may not* be used to verify debts to retain an "Accept" recommendation.**

- Apply due diligence when reviewing the documentation in the loan file to determine if there is any potentially derogatory or contradictory information that is not part of the data submitted to GUS or if there is erroneous information in the data submitted to GUS. If there are debts, late payments, or derogatory information that has not been made available to the data submitted to GUS, or if there is a federal judgment, a risk analysis decision of "Accept" must be downgraded and the file manually underwritten
- Manually Underwritten Loans – Add recent undisclosed debts to the loan application. Consider these debts in the credit underwriting analysis.

Non-Purchasing Spouse Credit History

- In community property states, the non-purchasing spouse's obligations must be considered in the debt-to-income ratio. The non-purchasing spouse's (NPS) credit history is not considered a reason to deny a loan application.
- Obtain a credit report that meets Rural Housing's requirements for the non-purchasing spouse in order to determine the debts that must be counted in the debt-to-income ratio.
  - GUS will retrieve credit reports for borrowers only. **Obtain an acceptable credit report for the borrower's spouse outside of the GUS system.**
  - Liabilities for a non-purchasing spouse should be entered on the "Assets and Liabilities" page.
  - When recording the debt, reference the liability as a non-purchasing spouse debt in the "notes" data field of the Liability page.
  - Submit a copy of the non-purchasing spouse's credit report to Rural Housing when requesting the Conditional Commitment.
- Community property states are: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin..
- Alaska is an opt-in community property state. Property is separate unless both parties agree to make it community property through a community property agreement or community property trust.

Payment Shock

- The term "payment shock" signifies the increase in housing expenses experienced by a borrower. Payment shock is defined as a percentage under the following formula: New Principal Interest Taxes and Insurance (PITI) divided by Previous Housing Expense. Examples:

A. The borrower's new PITI is \$187.00 and their former rent was \$100.00. B. \$187.00/\$100.00 = 1.87; 1.87 – 1 = .87; .87 = 87% C. The payment shock in this example is 87 percent.
A. The borrower's new PITI is \$345.00 and their former rent was \$150.00 B. \$345.00/\$150 = 2.30; 2.30 – 1 = 1.30; 1.30 = 130% C. The payment shock in this example is 130 percent.
A. The borrower's new PITI is \$2,000.00 and their former rent was \$1,000.00 B. \$2,000/\$1,000 = 2.00; 2.00 – 1 = 1.00; 1.00 = 100% C. the payment shock in this example is 100%.

- In cases where the borrower did not have a housing expense prior to purchasing a home, such as if the borrower was living with relatives, payment shock cannot be measured as a percentage.
- **GUS "Accept"** – Payment shock is a part of the underwriting risk evaluation and is not subject to further evaluation or documentation unless required by the GUS Underwriting and Findings Analysis report.
- **Manually Underwritten Loans** – Payment shock by itself, without the presence of other risks, is not an additional risk layer.

- Payment shock is a risk layer for underwriters to consider when the PITI ratio exceeds 29% and the proposed mortgage payment is 100% or greater than the current housing expense.
- Payment shock is not a risk layer and requires no further supportive documentation if the PITI ratio is 29% or less.
- In cases where payment shock is 100% or higher and qualifying PITI ratios are exceeded, as well as in cases where the borrower did not have a housing payment history, no additional risk layering such as adverse credit waivers, debt ratio waivers, or temporary buy downs should be allowed without strong compensating factors. Acceptable compensating factors include, but are not limited to:
  - The borrower has an ability to accumulate savings or cash reserves.
  - The borrower has demonstrated a conservative attitude towards using credit.
  - The borrower has the potential for increased earnings as indicated by job training or education in the borrower's profession.
  - The borrower has a representative credit score of 680 or higher.

Indicators of Unacceptable Credit

Authorized User Accounts

- Review credit report trade lines in which the borrower has been designated as an authorized user in order to ensure that any open trade lines are an accurate reflection of the borrower's credit history.
- Closed authorized trade lines do not require consideration. An authorized user account that is classified as "terminated" on the credit report is equal to a closed trade line.
- Automated Underwriting System – GUS "Accept" – For GUS decisions supported by credit reports that designate the borrower as an authorized user on **open** trade lines, obtain evidence of one of the following:
  - The trade line in question is owned by another borrower on the mortgage loan application.
  - The owner of the trade line is the borrower's spouse.
  - The borrower has made payments on the account for the previous 12 months prior to loan application.
  - There are two or more other trade lines listed on the credit report, which are not authorized user accounts, with at least 12 months of payment history listed to validate the credit score.
- In the event one of the conditions cannot be met an underwriting recommendation of "Accept" must be downgraded to a "Refer" and the file must be manually underwritten.
- Manually Underwritten Loans - Ensure open authorized trade lines reported on the credit report are an accurate reflection of the borrower's independent approach to credit repayment and credit history.

Collection Accounts

- Collection accounts are factored into the credit score. Collection accounts will be considered in the analysis of credit and capacity. Paying an outstanding collection account is not justification, in itself, that would establish a borrower's willingness to meet obligations in an acceptable manner. Payment of the collection account may cause the depletion of cash resources that may otherwise be available as reserves or for closing costs.
  - The underwriter is responsible for determining which collection accounts, if any, should be paid in full by the borrower prior to or at loan closing. The repayment in full of unpaid collections does not always need to be a condition of loan approval.
- Whether a collection account represents a greater risk is entirely the underwriter's decision regardless of the credit score. The decision should be based upon several factors including the credit profile of the borrower, the amount of meaningful financial reserves available, the unpaid balance of the collection accounts, and whether they pose a threat to the first mortgage lien and are likely to affect the borrower's equity or ability to repay the loan.
- The underwriter must conclude that the borrower did not disregard his or her financial obligations. Outside factors such as disputes, illness, or loss of job may have contributed to the cause of the collection account. Underwriters must evaluate all outstanding collection accounts. Perform additional analysis when making credit determinations if collection accounts are encountered that have:
  - A record of irregular payments; or
  - No satisfactory arrangements for repayment; or
  - Payment in full within the last six months just prior to application unless the borrower had been previously making regular payments.

- Automated Underwriting System – GUS "Accept" - Underwriters remain responsible for considering the existence of unpaid collections and the history of the collection account in the final credit analysis (see capacity analysis section below).
  - A letter of explanation or documentation supporting the presence of unpaid collections is not required when the underwriting recommendation is an "Accept".
  - The underwriter will document reasons for approving a loan request when collection accounts remain unpaid.
  - Ensure all open collections are listed on the loan application and on the "Assets and Liabilities" page in GUS. Omit any collections that are eligible to be omitted (see capacity analysis section below).
- Manually Underwritten Loans - Document mitigating circumstances subject to the capacity analysis described below for approving a loan when collection accounts are present and remain unpaid.
  - For each outstanding collection account the borrower must provide a letter of explanation together with documentation to support the explanation. The supporting documentation and explanation must be consistent with other credit information in the file.
  - Refer to the capacity analysis below when the outstanding balances of all collection accounts collectively exceed $2,000.
  - Ensure all open collections are listed on the loan application in the liabilities section.

Capacity Analysis when Collections are reported (GUS and Manual)

- Collections meeting the omission policy noted below can be omitted from the total debt-to-income ratio. Additional documentation is not required to omit those collections meeting these criteria:
  - Remove all medical collections and all types of charged off accounts.
    - Medical collections and charged off accounts must be clearly identifiable on the credit report.
- In an effort to minimize future risk of open collections left unpaid, the underwriter will consider the following during the capacity analysis of the loan **regardless of the whether the loan is manually underwritten or approved by GUS**:
  - Determine if the total outstanding balance of all collection accounts of all borrowers is equal to or greater than $2,000. Collection accounts of a non-purchasing spouse in a community property state **are** included in the cumulative balance of all collections.
  - If the outstanding balance of collection accounts are equal to or greater than $2,000 one of the following will be required:
    - Payment in full of all collection accounts at or prior to closing;
    - Payment arrangements must be made with each creditor for each collection account remaining outstanding. A letter from the creditor or evidence on the credit report is required to validate the payment arrangements. The agreed upon monthly payment for each outstanding collection account will be included in the borrower's debt-to-income ratio; or
    - In the absence of a repayment arrangement, the underwriter will use in the debt-to-income ratio a calculated monthly payment. For each collection use 5% of the outstanding balance to represent the monthly payment.

Chapter 7 Bankruptcy

- Automated Underwriting System – GUS "Accept" - No further documentation regarding the bankruptcy is required.
- Manually Underwritten Loans - A Chapter 7 bankruptcy does not disqualify a borrower from obtaining a loan if at least three years have elapsed since the date of the discharge of the bankruptcy. During this time the borrower must have re-established good credit or chosen not to incur new credit obligations.
  - An elapsed period of less than three years may be acceptable if the borrower can show the bankruptcy was caused by extenuating circumstances beyond their control and has since exhibited a documented ability to manage their financial affairs in a responsible manner for a reasonable period of time following discharge. A borrower whose bankruptcy has been discharged less than one year is ineligible.
  - Document that the borrower's current situation indicates the events that led to the bankruptcy are not likely to recur.
  - When a Chapter 7 bankruptcy absolved the mortgage debt for the borrower, any foreclosure is an action against the property, not the borrower. The foreclosure action is not considered an indicator of

unacceptable credit in the borrower's evaluation. A loan underwritten with the assistance of GUS will not be required to be manually downgraded when the bankruptcy discharge included the mortgage debt and foreclosure proceedings have been completed.
    - If a borrower has a real estate mortgage discharged in a Chapter 7 bankruptcy, however a foreclosure action is not completed, the borrower remains in ownership of the property. Title must be transferred to the lender of the pending foreclosure in order to remove the borrower from ownership and from the responsibility of real estate taxes and homeownership dues, if any, of the property.

Chapter 13 Bankruptcy

- A Chapter 13 bankruptcy plan in progress (not yet discharged) does not disqualify a borrower from obtaining a loan provided the following criteria, applicable to all underwriting methods, can be met:
    - Twelve months of the debt restructuring plan has elapsed;
        - The borrower's payment performance has been satisfactory;
        - All required payments have been made on time; and
        - The borrower receives written permission from the bankruptcy court/trustee to enter into a mortgage transaction.
    - Automated Underwriting System – GUS "Accept" – When a plan is in progress and GUS has rendered an "Accept" underwriting recommendation a credit exception by the underwriter is not required. Include the required Chapter 13 bankruptcy payment on the "Assets and Liabilities" page in GUS.
    - Manually Underwritten Loans – In addition to the requirements listed above, a credit exception by the underwriter will be required in accordance with the credit exception guidelines.

Chapter 13 Bankruptcy Plan Completed

- Automated Underwriting System – GUS "Accept"– The discharge date of the completed plan has been considered by GUS and is reflected in the overall credit score. No additional documentation is required.
- Manually Underwritten Loans – A completed Chapter 13 bankruptcy plan will not require a credit exception provided the borrower has demonstrated a willingness to meet obligations when due for the full 12 months prior to the date of the loan application.

Charged Off Accounts

- The presence of a charge off is already reflected in the credit score and does not need to be included in the borrower's long-term liabilities or debt. If the borrower has entered into an agreed upon repayment plan with the creditor, the payment must be included in the long-term liabilities.

Consumer Credit Counseling

- A borrower who has experienced credit or financial management problems in the past may have elected to participate in consumer counseling sessions to learn how to correct or avoid such problems in the future. Participation in a consumer credit counseling program does not disqualify a borrower from obtaining a loan provided:
    - One year of the payout period has elapsed;
    - The borrower's payment performance has been satisfactory and all required payments have been made on time; and
    - Written permission from the counseling agency to enter into the mortgage transaction along with the counselor's recommendation of the borrower as a good credit risk is obtained.
- Automated Underwriting System – GUS "Accept" – GUS does not trigger a requirement for additional documentation since the credit score already reflects the counseling in the credit history. No further explanation or other documentation is required. Include the payment for the repayment plan in the "Assets and Liabilities" page of GUS.
- Manually Underwritten Loans – Evaluate the borrower's credit. Some creditors may still report the borrower as delinquent even though they have agreed to accept a lesser payment. This must be considered in the analysis of the borrower's overall credit. Include the repayment plan payment in the debt-to-income ratio.

Delinquent Federal Non-Tax Debt

- Determine if the borrowers have delinquent federal non-tax debt. Information may be obtained from public records, credit reports, or equivalent and all borrowers must be checked against the Credit Alert Verification Reporting System (CAIVRS).
  - **Delinquent federal non-tax debts are ineligible for Rural Housing guaranteed loans unless the delinquency is resolved.**
  - Delinquent federal non-tax debt also refers to a borrower who has had a previous Rural Housing debt which was settled, or is subject to settlement, or whether Rural Housing otherwise suffered a loss on a loan to one or more of the borrowers. The borrower is ineligible unless the borrower qualifies for an exception granted by Rural Housing.
    - If Rural Housing suffered any loss related to a previous loan, a loan guarantee shall not be issued unless Rural Housing determines the loss was beyond the borrower's control and any identifiable reason for the loss no longer exists.

Delinquent Federal Tax Debt

- Borrowers with delinquent federal tax debt are ineligible.
  - Tax liens may remain unpaid if the borrower has entered into a valid repayment agreement with the federal agency owed to make regular payments on the debt and the borrower has made timely payments for at least three months. The borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments.
  - Document the payments with a copy of the IRS repayment agreement and verification that the payments have been made. Payments will be included in the debt-to-income ratio.

Disputed Accounts

- Disputed accounts on a borrower's credit report are not considered in the credit score.
- Automated Underwriting System – GUS "Accept" – When disputed accounts are present, downgrade to a "Refer" and manually underwrite the loan unless the following conditions are met:
  - The disputed trade line has a zero dollar balance.
  - The disputed trade line is marked "paid in full" or "resolved".
  - The disputed trade line has a balance owed of less than $500 and is more than 24 months old.
- Loans downgraded for failure to meet any of these conditions are subject to a manual review and require the submission to Rural Housing of the complete underwriting file at the time the Conditional Commitment is requested.
- Manually Underwritten Loans - All disputed accounts with outstanding balances/payments must have a letter of explanation and documentation supporting the basis of the dispute.
  - Those debts that have been excluded from the debt ratios must have evidence in the loan file to support a justifiable dispute. Evidence may include correspondence to the creditor from the borrower or from their attorney.
  - The underwriter is responsible for analyzing the documentation presented and confirming that the explanation and documentation are consistent with the credit record.

- **Foreclosure and Deed-in-Lieu of Foreclosure** – A borrower is generally not eligible for a Rural Housing guaranteed loan, if during the prior three years, the borrower's previous real property was foreclosed on or they have given a deed-in-lieu of foreclosure.
  - An exception may be granted if there are extenuating circumstances.
    - The inability to sell the property due to a job transfer or relocation to another area does not qualify as an extenuating circumstance.
    - Divorce is not considered an extenuating circumstance. However, a borrower whose loan was current at the time of a divorce in which the ex-spouse received the property and the loan was later foreclosed may qualify as an exception.

Judgments

- The presence of court-ordered judgments must be considered in the credit analysis. Unpaid judgments may represent a borrower's disregard for credit obligations. Underwriters must document reasons for approving a loan when the borrower has judgments.
- The following is applicable to all underwriting types, manually and GUS approved:
  - **Borrowers who have open and unpaid judgments are ineligible for a Rural Housing guaranteed loan.**
  - Court ordered judgments ***MUST*** be paid off before the loan is eligible for Rural Housing guarantee unless the borrower provides documentation indicating that regular payments have been made on time in accordance with a documented agreement with a creditor.
    - The borrower must have made regular and timely payments for the three months prior to loan application.
    - Prepaying scheduled payments as a means of meeting minimum requirements is unacceptable.
    - Obtain a copy of the payment agreement and validate payments have been made in accordance with the payment agreement.
    - The payment will be included in the debt-to-income ratio.
  - Judgments of a non-purchasing spouse in a community property state must be paid in full or meet the requirements for repayment arrangements.
- If a loan is underwritten with the assistance of GUS, then regardless of the underwriting recommendation, the findings report will require evidence of payoff for any outstanding judgments shown on the credit report.

Short Sales

- A short sale is considered a pre-foreclosure activity or event.
- A borrower is not eligible for a Rural Housing guaranteed loan if they pursued a short sale agreement on their principal residence to take advantage of declining market conditions and subsequently purchased, at a reduced price, a similar or superior property within a reasonable commuting distance.
- If a borrower was current at the time of short sale, or in the case of divorce at time of the divorce, they may be eligible for a new loan. The prior mortgage payment history must reflect all mortgage payments due were made on time for the 12 month period preceding the short sale, or time of divorce, and all installment debt payments for the same period were also made within the month due.
- A borrower in default on their mortgage at the time of the short sale is not eligible for a new mortgage loan for three years from the date the short sale was completed.

Property and Appraisal Requirements

Underwriting the Property

Overview

- Ensure the subject property meets Rural Housing's site guidelines. The site must be developed according to state or local government standards.
- Sites must be in rural areas; meet community standards regarding utilities, including water and wastewater systems; meet street and road access and maintenance requirements; and contain other amenities essential to the continued marketability of the home.
- The use of the property must comply with zoning and use restrictions. If the existing property does not comply with current zoning regulations, but is accepted by the zoning authority, it is considered legal non-conforming property. **The property is not eligible for a Rural Housing guarantee when the use is not legal.**
- The economic life of a property must meet or exceed the term of the proposed loan. The appraiser may reject the property if the future economic life of the property is shortened by obvious and compelling pressure to a higher use, making a long-term mortgage impractical.

Rural Area Designation

- Only loans secured by properties located in areas designated by Rural Housing as rural are eligible to receive a loan guarantee.
- An area's rural designation is determined by Rural Housing and may be changed as a result of periodic review or after the decennial census of a population. Rural Housing conducts reviews every five years to identify areas that no longer qualify as rural. In areas experiencing rapid growth in eligible communities within Metropolitan Statistical Areas (MSAs), reviews take place every three years.
- In general rural areas are defined as:
  - Open country that is not part of or associated with an urban area.
  - Any town, village, city or place including the immediately adjacent densely settled area, which is not part of or associated with an urban area and which:
    - Is rural in characteristic with a population of less than 10,000; or
    - Is not contained within an MSA and has a population above 10,000 but below 20,000 and has a serious lack of mortgage credit for lower and moderate-income families.
  - Two or more towns, villages, cities or places that are contiguous may be considered separately for a rural designation if they are not otherwise associated with each other and their densely settled areas are not contiguous.
- Use the following Internet site to determine whether a specific site is in an eligible area: http://eligibility.sc.egov.usda.gov/eligibility

Making Loans in Areas Changed to Non-Rural

- If an area's designation changes from rural to non-rural, loans that meet the following criteria may be approved in that area:
  - The application and purchase contract was complete, the loan was underwritten by an approved lender and a complete application for loan note guarantee was submitted to Rural Housing prior to the area designation change.
  - Existing Conditional Commitments that have been issued will be honored provided the commitment was issued prior to the area designation change.
  - Rural Housing REO property sales and transfers with assumption may be processed in areas that have changed to non-rural.

Site Requirements

- Sites must be modest and developed in accordance with any standards imposed by a state or local government. Verify that the following requirements are met at the time of the loan application:
  - **Site Size**. The site size must be typical for the area.
  - **Income Producing Buildings**. The property must not include buildings designed to be used principally for income producing purposes such as barns, silos, greenhouses, or livestock facilities. Properties used primarily for income producing agricultural, farming or commercial enterprise are ineligible.
    - Barns, silos, livestock facilities or greenhouses no longer in use for commercial operation used for storage and outbuildings such as storage sheds are permitted if they are not used primarily for income producing agricultural, farming, or commercial enterprise.
    - A minimal income producing activity, such as maintaining a garden that generates a small amount of additional income, does not violate this requirement.
    - Home based operations such as child care, product sales, or craft production that do not require specific features are not restricted.
    - A qualified property must be predominantly residential in use, character and appearance.
  - **Income Producing Land.** The site must not have income producing land that will be used principally for income producing purposes. Vacant land or properties used primarily for agricultural, farming or commercial enterprise are ineligible.
    - **Sites that have income producing characteristics such as large tracts of arable land ready for planting are considered income producing property.**
    - A minimal income producing activity such as a garden that could generate a small amount of additional income is acceptable.
    - A qualified property must be predominantly residential in use, character and appearance.

- **Site Specifications**. The site must be contiguous to and have direct access from a street, road, or driveway. Streets and roads must be hard surfaced or all weather surfaced and legally enforceable arrangements must be in place to ensure that needed maintenance will be provided.
- **Utilities**. The site must be supported by adequate utilities, water and wastewater disposal systems.

Appraisals

Residential Appraisal Reports

- All appraisal reports must comply with the reporting requirements of USPAP.
- The appraisal report for both existing and new construction properties must not be more than 120 days old at loan closing.
- Appraiser/client confidentiality under USPAP Ethics Rules does not permit the appraiser to discuss the appraisal with anyone other than the lender.
- All appraisal reports must include a Market Condition Addendum (1004MC) and meet the Uniform Appraisal Dataset (UAD) requirements set forth by Fannie Mae and Freddie Mac.
- The appraisal forms currently applicable are:
  - *"Uniform Residential Appraisal Report* "(FNMA Form 1004) for one unit single family dwellings
  - *"Individual Condominium Unit Appraisal Report* "(FNMA Form 1073) for all individual condominium units.
- The market or sales comparison report is required in all cases. At least three comparable sales must be used unless the appraiser provides documentation that such comparable sales are not available.
- If the appraiser considers the property to be unique, has specialized improvements or the underwriter requires a cost approach to be completed, then the appraisal report will be completed using the sales comparison approach and the cost approach to value. The appraiser will identify the source of the cost estimates and will comment on the methodology used to estimate depreciation, effective age and remaining economic life.
- The income approach is only needed if the appraiser determines that it is necessary.
- An appraisal prepared for REO purposes, or for any other purpose other than for a purchase transaction, is not acceptable. A new appraisal must be obtained.

Photographs

- Photographs must be clear and descriptive so that the property's condition and quality are reflected. Acceptable photographs include color original images from actual photographs or electronic images.
- Photographs must clearly represent the improvements, any physical deterioration of the property, amenities, and conditions and external influences that may have a material effect on the market value or marketability of the subject property.
- The appraisal report must include, at a minimum, the following photographs:
  - A front view of the subject property;
  - A rear view of the subject property;
  - A street scene identifying the location of the subject property and showing neighboring improvements;
  - The kitchen, main living area, bathrooms, and bedrooms;
  - Any other rooms representing overall condition and recent updates such as restoration, remodeling and renovation;
  - Basement, attic and crawl space;
  - The front view of all comparable sales and listings and/or pending sales used in the valuation analysis; and
  - The common areas and shared amenities of condominium projects.

Property Flipping

- It is the underwriter's responsibility to ensure any recently sold property's value is strongly supported when a significant increase between sales occur.
- Perform a thorough review of the appraisal report to validate and support the property's value.

Rural Housing Review

- Rural Housing will review appraisals for all guarantee loan requests.
- If Rural Housing's reviewer detects concerns, the appraisal will be referred to a Rural Housing licensed appraiser for a technical desk or technical field review.
  - Should the Rural Housing appraiser determine the appraisal inadequate, the underwriter will be informed of corrections needed prior to issuance of the Conditional Commitment.
  - The corrected appraisal will be subject to the same review process.
  - Rural Housing retains the right to determine if an appraiser is ineligible based upon the appraiser's failure to comply with Rural Housing's requirements.

Water and Wastewater Disposal Systems

Water

- The site must have an acceptable water system to ensure the property is decent, safe, and sanitary meeting community standards.
- Public water systems are presumed to meet state and local requirements with no additional documentation or inspections.
- Private well systems require inspections or documentation as discussed below.
- Water systems, for existing or new construction, that require continuous or repetitive treatment to be safe bacterially or chemically **are not acceptable.**
- Individual dwelling water purification units are not an acceptable alternative however they may be used if the individual water system with purification meets the requirements of the State Department of Health or other comparable regulatory authority.

Individual Privately Owned Water Systems

- Individual water systems are owned and maintained by the homeowner and are subject to compliance with all requirements of the local and/or state health authority codes. Individual water supply systems may be acceptable when the cost to connect to a public or community water system is not reasonable as defined by the underwriter. The underwriter is responsible for determining if connection is feasible. Water quality tests are required as follows:
  - The water quality of the well must meet the requirements of the state or local authority. If the state or local authority does not have specific requirements, the maximum contaminant levels established by the Environmental Protection Agency (EPA) will apply.
  - The local health authority or a state certified laboratory must perform a water quality analysis.
  - The water analysis must be no greater than 120 days old at loan closing. If Rural Housing is aware of any recent environmental impacts that may render the previous analysis invalid such as chemical spills, natural disasters, etc. a new report may be required.
  - The well located for individual water supply systems must be measured to establish the distance from the septic system. Distances must meet the local and/or state health authority codes or the requirements of HUD Handbook 4000.1.
  - Individual wells should be located on the subject property site. If located on an adjacent property, evidence of water rights and recorded maintenance agreements must be obtained.
  - **Properties served by cisterns are not acceptable.**

Shared Wells

- If the property is served by a shared well or off-site facility, ensure the private system will provide a continuous and adequate supply of safe and potable water. The following requirements must be met:
  - The well must serve properties that cannot be feasibly connected to an acceptable public or community water supply system. It is the underwriter's responsibility to make this determination.
  - A shared well must have a valve on each dwelling.
  - The water supply must be adequate for all families served. A shared well must service no more than four living units or properties.

- The water quality of the shared well must meet the requirements of state or local authorities. If the state or local authority does not have specific requirements, the maximum contaminant levels established by the Environmental Protection Agency (EPA) will apply.

- The shared well must have an agreement that meets the following requirements:
  - The agreement must be binding upon all signatory parties and their successors in title.
  - The agreement must be recorded or will be recorded no later than the closing date.
  - The agreement must make provision for maintenance and repair of the system and the sharing of costs to do so. These provisions must include a permanent easement that allows access for maintenance and repair.

Community Wells

- If the property is served by a community water system operated by a private corporation or non-profit property owners' association, ensure the following conditions are met:
  - The system and the water supply must meet all applicable federal, state and local requirements.
  - The system must have the capacity to provide a sufficient water supply during periods of peak demand.
  - The system must be operated under a legally binding agreement that allows interested third parties to enforce the obligation of the operator to provide satisfactory service.
- Obtain documentation to demonstrate that the water quality meets state and local standards.

Wastewater

- The site must have an acceptable wastewater disposal system to ensure the property is safe and sanitary meeting community standards.
- Public sewer systems are presumed to meet state and local requirements with no additional documentation or inspection.
- Private wastewater systems require inspections or documentation as discussed below.
- Individual sewage systems may be acceptable when the cost to connect to a public or community sewage system is not reasonable as determined by the underwriter. The underwriter is required to obtain a septic inspection.
  - An FHA roster appraiser who certifies the property meets HUD's Single Family Housing Policy Handbook, a government health authority, a licensed septic system professional or a qualified home inspector may perform the septic evaluation.
  - The inspector may require additional inspections as a result of the inspection.
  - The separation distances between a well and septic tank, and the property line, must comply with HUD guidelines or state codes.
  - The septic system must be free of observable evidence of failure.
  - Existing dwellings appraised by a HUD roster appraiser, who has indicated the dwelling meets the required HUD handbook policy, does not require further septic certification.
- If the property is served by an individual sewage disposal system ensure the system:
  - Meets any applicable requirements of the state or local health authority with jurisdiction.
  - Is located entirely on the subject property. If any part of the system is located on an adjacent property (for example, leach lines), a perpetual encroachment easement must be recorded to establish the rights of the property owner's permitted use.
  - Is operating properly and has the capacity to dispose of all domestic wastes in a manner that will not create a nuisance or endanger public health.

Community Owned Wastewater Systems

- If the property is served by a community wastewater system operated by a private corporation or non-profit property owners' association, ensure that the system:
  - Meets any applicable requirements of the state or local health authority with jurisdiction.
  - Is licensed, operating properly and has the capacity to dispose of all domestic wastes in a manner that will not create a nuisance or endanger public health.
  - Is subject to a legally binding agreement that allows interested third parties to enforce the obligation of the operator to provide satisfactory service.
  - Obtain documentation the wastewater system meets state and/or local standards.

Street Access and Road Maintenance

Access

- The site must be contiguous to, and have direct access from, a public or private street, road, or driveway.
- Private roads or streets must be protected by a permanent recorded easement (non-exclusive and non-revocable easement without trespass from the property to a public street) or the street must be maintained by a homeowners' association.
- Shared driveways must also meet these requirements requiring a permanently recorded easement for ingress and egress. This agreement must be binding to successors and title.
- A copy of a title report may be used to evidence the easement.
- Private streets must have a permanently recorded easement or be owned and maintained by a Homeowners' Association.

Maintenance

- Streets and roads must be hard surfaced or all-weather surfaced.
- An all-weather surface is a road surface over which emergency and the area's typical passenger vehicles can pass at all times.
    - A publically maintained road is automatically assumed to meet this requirement.
    - If a homeowners' association is responsible for maintaining streets and roads, it must meet the criteria set forth by Fannie Mae, Freddie Mac, FHA or VA.

Dwelling Requirements

Modest Housing

- Rural Housing will not guarantee loans to purchase a building designed to accommodate a business or an income producing enterprise.
    - Homebased operations such as child care, product sales, or craft productions that do not require specific features are not restricted.

Existing Dwellings

- The objective of Rural Housing is to assist eligible rural households in obtaining adequate, safe and sanitary homes.
- An existing dwelling may be attached, detached, or semi-detached dwellings and must be inspected to determine that the dwelling meets the current requirements of:
    - FHA's "Single Family Housing Policy Handbook" (HUD Handbook 4000.1).
    - Only licensed or certified appraisers who are on FHA's roster of approved appraisers can certify the HUD Handbook standards have been met.
    - The appraiser may certify that HUD requirements have been met on page three of the appraisal report in the "comments" section.
- An existing dwelling is a dwelling that has been completed for more than 12 months or has been completed less than 12 months but has been previously occupied.
- Required repairs are limited to those repairs necessary to preserve the continued marketability of the property and to protect the health and safety of the occupants.
- The responsibility for enforcing code rests with the local municipalities.
- All repair items required by the appraiser or underwriter must be inspected and the clearance documented on Form 1004D.
- Termite/pest inspections are not required unless the lender, appraiser, inspector, or state law requires the inspection to confirm the property is free of active infestation.
- An inspection to confirm thermal standards is not required for existing dwellings.
- Dwellings with in-ground swimming pools are generally eligible.
- A property which an FHA roster appraiser indicates is in average or good condition may be considered in good repair, though repairs may still be required by the underwriter.

- The appraiser must report all readily observable property deficiencies as well as any adverse conditions discovered when performing the research involved in completing the appraisal.
- Underwriters are expected to use professional judgment and rely upon prudent underwriting practices in determining when a property condition requires additional inspections or repairs.
- Conditions that would warrant additional repairs include those that pose a threat to the safety of the occupants, jeopardize the soundness and structural integrity of the property, or adversely affect the likelihood of a low-to-moderate income borrower from becoming a successful homeowner.

New Dwellings

- New dwellings must be designed and constructed in accordance with certified plans and specifications. Obtain copies of the documents described in one of the following options:
  - 1. Three construction inspections (footing, framing and final):
    - Footing inspection to be done when footings and foundation are ready to be poured and prior to back-filling.
    - Framing inspection to be done when shell is complete but plumbing, electrical and mechanical work is still exposed.
    - Final inspection to be done when the work is completed.
  - Certificate of Occupancy issued by the local jurisdiction.
  - A one year insured builder warranty plan on HUD Form 92544; OR
  - 2. Final inspection and a ten year insured warranty plan acceptable to Rural Housing.
- Obtain evidence the plans and specifications comply with all development standards applicable to the new construction. Applicable development standards are the current International Code Council (ICC) standards or current state adopted ICC code(s) for residential construction.
- Acceptable evidence is a copy of the certification form from a qualified individual or organization that the reviewed documents comply with applicable development standards.
  - Certifications from individuals or organizations trained and experienced in the compliance, interpretation or enforcement of the applicable development standards for drawings and specifications may be obtained. Plan certifiers may be any of the following:
    - Licensed architects;
    - Professional engineers;
    - Plan reviewers certified by a national model code organization;
    - Local building officials authorized to review and approve building plans and specifications; or
    - National codes organizations.
- Obtain evidence thermal standards meet or exceed the International Energy Conservation Code (IECC) in effect at the time of construction. Documentation of conformance may be by one of the following options:
  - The builder may certify confirmation with IECC standards.
  - A qualified, registered architect or a qualified, registered engineer may certify confirmation with IECC standards.

Environmental Requirements

Hazard Identification

- Use due diligence with regard to potential environmental hazards to ensure the property is decent, safe and sanitary, and has sufficient value to adequately secure the loan.
  - The property must be free of known hazards that may have adverse effects on the health and safety of the occupants.
  - The structural soundness of the dwelling must ensure customary use and enjoyment of the property by the occupants.
- Appraisers play an important role in identifying potential environmental hazards by reporting any concerns identified during their visit to the property. The appraiser is required to note readily observable conditions.
  - If the any party to the transaction knows or is informed by another party of a potential hazard, the information must be disclosed to the appraiser.
  - Underwriters must follow up on all potential environmental hazards identified by an appraiser to determine the nature and scope of the problem and the impact the problem is likely to have on the property's value.

- If potential environmental hazards are noted, the underwriter should carefully document the suspected problem and the findings of his/her investigation.
- If the investigation reveals an environmental hazard does exist, ensure the hazard is mitigated before requesting the loan guarantee.

Flood Hazards

- Existing dwellings are eligible only if flood insurance, through FEMA's National Flood Insurance Program (NFIP) is purchased by the borrower.
- Flood insurance must be obtained and maintained for the life of the loan for existing residential structures when any portion of the structure is determined to be located in a Special Flood Hazard Area including decks, carports, etc.
    - Flood insurance is not required for any additional structures that are located on the property but are detached from the primary residential structure and do not serve as a residence such as sheds, garages or other ancillary structures.
- **New or proposed construction in a special flood hazard area (SFHA) is ineligible for a Rural Housing loan unless:**
    - A final letter of Map Amendment (LOMA) or final Letter of Map Revision (LOMR) removing the property from the SFHA is obtained from FEMA; or
    - A FEMA National Flood Insurance Program Elevation Certificate (FEMA Form 086-0-33) is obtained. The flood elevation certificate must document that the lowest floor, including the basement, of the residential building and all related improvements/equipment essential to the value of the property are built at or above the 100 year flood elevation in compliance with the National Flood Insurance Program (NFIP) criteria. The flood elevation certificate must be prepared by a licensed engineer or surveyor.
    - **NOTE:** Part of the site may be located in the SFHA without triggering these requirements as long as no part of the dwelling is located in an SFHA. At the underwriter's discretion flood insurance may be required even if the residential building and related improvements to the property are not located within the SFHA but the underwriter has reason to believe that the building and related improvements to the property may be vulnerable to damage from flooding.
- Flood insurance must cover the lesser of the outstanding principal balance of the loan or the maximum amount of coverage allowed under FEMA's National Flood Insurance Program. Unless a higher amount is required by state or federal law, the maximum deductible clause for a flood insurance policy should not exceed the greater of $1,000 or 1% of the face amount of the policy.
- Existing dwellings and newly constructed dwellings located with the SFHA which are not served by public sewer systems and have on-site septic or sewage treatment systems must have a drinking water supply which is protected from cross contamination from the on-site septic/sewage treatment during flooding. A property serviced by an on-site septic or sewage treatment system is eligible provided one of the following can be met:
    - The property is served by a publically provided water supply;
    - The property is serviced by a private drinking water well/supply with a fitted sanitary well cap which prevents backflow floodwater from entering the drinking supply well; or
    - The property is served by a private drinking water well/supply whose opening is located above the base flood elevation of the SFHA. Additional documentation such as an elevation certificate will be required to verify this type of property.

Condominiums and Planned Unit Developments

Condominiums

- Units in a condo project are eligible for Rural Housing if the condo has been approved by FHA, VA, Fannie Mae or Freddie Mac.
- Underwriters must supply evidence they have reviewed the condominium documentation that supports the project's approval or acceptance by FHA, VA, Fannie Mae or Freddie Mac.

Ineligible Condominiums

- Certain types of condo projects are not eligible. They are:
  - Condominium hotels;
  - Timeshares;
  - Houseboat projects;
  - Multi-dwelling unit condos that permit an owner to hold title to more than one dwelling by a single deed and mortgage;
  - Any project for which the owners' association is named a party to current litigation or for a project that has not been turned over to the association for which the project sponsor or developer is named a party to current litigation.
  - Condominiums that represent a legal, but non-conforming use of the land, if zoning regulations prohibit rebuilding the improvements to current density in the event of their full or partial destruction.
  - Investment Securities – a project in which ownership is characterized or promoted as an investment opportunity and/or projects that have documents on file with the Securities and Exchange Commission.
  - Common interest apartments or community apartment projects – Any project or building that is owned by several owners as tenants-in-common or by a homeowners' association in which individuals have an undivided interest in a residential apartment building and land, and have the right of exclusive occupancy of a specific apartment in the building.
  - A project with non-incidental business operations owned or operated by the owners' association such as, but not limited to, a restaurant, spa, health club, etc.

Site Condominiums

- Project approval are not be required for site condominiums if they meet the following criteria:
  - Single family totally detached dwellings encumbered by a declaration of condominium covenant or condominium form of ownership.
  - The unit has no shared garage or any other attached buildings such as archways and breezeways.
  - The condominium unit consists of the entire structure, site and air space and is not considered to be common area or limited common area.
- Appraisals will be completed on the *"Individual Condominium Unit Appraisal Report"*, FNMA Form 1073.
- A Condominium Rider must supplement the mortgage or deed of trust.
- Insurance and maintenance costs will be the responsibility of the unit owner.

Planned Unit Developments

- PUDs are eligible for the Rural Housing Program the same as for single family dwellings that are not located in a PUD.

Modular Homes

Modular Homes

- Modular homes are sectional pre-fabricated houses that consist of multiple modules or sections which are typically manufactured in a remote facility and delivered to their site of intended use. They differ from manufactured homes largely in their absence of axles or frames.
- Modular dwellings are commonly transported to their site by means of flatbed trucks and set in place with the assistance of a crane.
  - Permanent on-frame homes do not meet the definition of modular homes.
- Modular homes are to be treated as stick built housing.
  - For new modular homes follow the requirements for the "new construction" requirements above.

Submitting the File to Rural Housing

Contents of the Loan Application Package

Automated Underwriting System – GUS "Accept"

- Loans underwritten with the assistance of GUS receiving an underwriting recommendation of "Accept" may allow the underwriter to submit abbreviated documentation when compared to manually underwritten loans when requesting the Conditional Commitment. The underwriter certifies upon final submission that the loan has been reviewed, underwritten and the data entered into GUS is true, complete and accurate. Pre-Conditional Commitment conditions identified on the final GUS underwriting analysis must be met prior to submitting the loan to Rural Housing.
- Unless a quality control message requires the submission of a fully documented file, submit the following completed documents when ordering the Conditional Commitment:
    - All pages of the current version of Form RD 3555-21 signed/dated by the borrower(s) and the underwriter.
    - A summary of the calculation of annual income, adjusted income and repayment income calculation.
    - Include the credit report of a non-purchasing spouse if the property is located in a community property state.
    - The appraisal.
    - The final GUS underwriting and findings analysis.
    - FEMA Form 086-0-32 (flood certification).
    - If the borrower is not a United States citizen, evidence the borrower meets the qualified non-resident alien criteria.
- If a quality control message for a GUS "Accept" underwriting recommendation requires a fully documented file to be submitted to Rural Housing, the extent of the review by Rural Housing is to determine the data entered into GUS is true, complete and accurately represented. Ratio waiver requests will not be required.

Manually underwritten Loans

- Manually underwritten loans are those applications reviewed and approved by the underwriter or applications underwritten with the assistance of GUS that receive an underwriting recommendation of "Refer" or "Refer with Caution".
- For manually underwritten loans, submit a fully documented loan application package to Rural Housing.
- The following information must be provided for the application to be considered complete:
    - All pages of the current version of Form RD 3555-21 signed and dated by the borrower(s) and the approving underwriter who is submitting the request.
    - A signed copy of the *"Uniform Residential Loan Application",* (URLA). The loan amount must match the loan request on Form RD 3555-21.
        - If the borrower is not a United States citizen, evidence the borrower meets the qualified alien criteria is required.
    - The CAIVRS number must be indicated on Form RD 3555-21.
    - The underwriter's conformation they have checked the SAM lists and have confirmed the borrower and all parties participating in the loan transaction are not debarred from doing business with the federal government. Certification of this action is recorded on Form RD 3555-21.
    - Summary of the calculation of annual income, adjusted income and repayment income calculations. Include documentation for all adult members of the household. Documentation to include IRS 4506 tax transcripts, verifications of employment and other income verification documentation such as asset documentation.
    - Credit reports. Include the credit report of a non-purchasing spouse if the property is located in a community property state. Include any credit supplements.
    - Verification of rental. Include documentation to support rental history in the previous 12 months prior to application, as applicable, for all manually underwritten loans.
    - The appraisal.
    - Purchase/sales agreement/contract.

  - Underwriting analysis (Form 1008). This may include evidence the underwriter reviewed and approved the loan, documentation of a credit waiver granted by the underwriter, if applicable, or a request for repayment ratio waiver with documented compensating factors listed (as applicable).
  - FEMA Form 086-0-32 (flood certification).

Agency Review of the Application Package

Standard Review

- Rural Housing will review the application to determine that all program requirements have been met. The lender's underwriter has the sole responsibility for properly underwriting the loan. Rural Housing's review of the application does not relieve the underwriter of that responsibility.
- Rural Housing's staff have the responsibility for determining if the borrower is income eligible and meets the established qualifying ratios, if the property is located in an eligible rural area, that the loan is for eligible purposes, and that the appraised market value supports the requested loan amount.
- Rural Housing staff must review the documentation to ensure that loans meet program requirements. The following summarizes the criteria used to ensure that each program requirement has been met:
  - **Household Income at or below 115% of Median for the Area** – Rural Housing must review the underwriter's program eligible income. This calculation is arrived at from eligible adjustments made to the annual income. This calculation is used one time to determine program eligible income. Eligibility income often differs from repayment income which represents the stable and dependable portion of income.
  - **PITI Ratio of 29% or Less/DTI Ratio of 41% or Less** – Rural Housing must review the underwriter's ratio calculation and any ratio applicable waiver requests for manually underwritten loans.
    - If the loan was underwritten with GUS and received an "Accept" underwriting recommendation, a ratio waiver request is not required.
  - **Appraisal** – Rural Housing will review the appraisal. If the Rural Housing reviewer detects concerns, the appraisal will be referred to a Rural Housing licensed appraiser for a technical desk or technical field review. Should the review appraiser determine the appraisal is unsatisfactory the underwriter will be informed of the corrections needed prior to issuance of the Conditional Commitment.
  - **Rural Area Designation** – Rural Housing staff must review the maps of ineligible areas to determine if the property is located in an eligible rural area. Rural Housing will make the final property eligibility determination.
  - **Environmental Review** – Rural Housing staff will perform an environmental review.
    - **Rural Housing will be unable to guarantee loans for new or proposed construction located in the flood zone** unless a Letter or Map Amendment (LOMA) that removes the property from the flood zone or a Letter of Map Revision (LOMR) that removes the property from the flood zone is obtained.
    - As an alternative, a FEMA elevation certificate that shows the lowest floor, including the basement, of the dwelling and all related building improvements are built at or above the 100 year flood plain elevation in compliance with the National Flood Insurance Program may be obtained.
    - All requirements for properties that are served by private water and/or wastewater systems have been met.

Notification Regarding Request for a Loan Guarantee

Approval of the Request

- If Rural Housing's review indicates the loan meets all program requirements, Rural Housing will agree to guarantee the loan subject to the conditions on the Conditional Commitment. The commitment will expire in 90 days from the issuance unless new construction is involved. The new construction expiration date will correspond with the projected completion of the construction, however, the expiration date for new construction should not exceed one year from the issuance of the Conditional Commitment.

Return of Incomplete Applications

- Ensure that complete application requests are submitted. Ensure that the documents are submitted in the correct stacking order required by Rural Housing.
    - An exception to the stacking order is the appraisal report. When GUS is used the appraisal will be uploaded separately from all other documents.
- If the application request is missing any required information the application request will be deemed incomplete and will be returned.
- Complete applications are processed in order by the date received. Only complete applications requests will be considered for processing by Rural Housing.

Denial of the Request

- The application request will be denied if the proposed loan fails to meet any Rural Housing program requirement or if a requested ratio waiver cannot be granted.
- Rural Housing will provide written notification to the underwriter of the reason for denial and will provide review and appeal rights.

Requesting Changes

- If changes to the loan amount or interest rate need to be made or if there are reasons that the conditions and requirements specified on the Conditional Commitment should be altered, the underwriter can contact Rural Housing and propose an alternative.
    - The request must be writing and must not affect the eligibility of the loan. If the change will increase the interest rate or loan amount, the request must include documentation as follows:
        - A newly executed 1003 reflecting the corrections;
        - A newly executed Form RD 3555-21 with the modifications; and
        - An updated 1008.
    - If the loan was underwritten with the assistance of GUS, contact Rural Housing to release the GUS system so that modifications can be made and a new GUS underwriting recommendation obtained. The new GUS findings must be re-submitted with the above documents.
- If Rural Housing accepts the change, attach the written modification to the existing Conditional Commitment and proceed to closing.