



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

FEDERAL HOUSING ADMINISTRATION

SINGLE FAMILY HOUSING



Welcome to...

Single Family Housing Policy Handbook Lender Training – Mortgage Credit

Today's webinar begins
at 11:00 AM (Eastern)

We will be underway shortly...

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- The presentation team will answer questions submitted in advance.
- Questions will be addressed following the presentation.
- Due to time limitations, not all submitted questions will be answered; however, a Q&A document will be emailed to all registrants several days after the webinar.



Contact FHA Resource Center

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Santa Ana Homeownership Center

Single Family Housing Policy Handbook Lender Training Mortgage Credit

June 30, 2020

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Last Update: April 2020



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Welcome



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Welcome and Housekeeping

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Disclaimer

The purpose of this presentation is to provide an overview and summation of recent changes to the Federal Housing Administration (FHA) policy. It introduces and explains official policy issued in Department of Housing and Urban Development (HUD) Handbooks and Mortgagee Letters. If you find a discrepancy between the presentation and Handbooks, Mortgagee Letters, etc., the official policies prevail. Please note the information provided in this training is subject to change.

Please consult HUD Handbooks and Mortgagee Letters through HUDClips for the most recent updates and current policy.



Agenda

Welcome

Recent Updates

Underwriting the Credit Package

Endorsement



COVID-19



FHA's Response

Given these extraordinary times and the nature of the COVID-19 emergency and pandemic, the Federal Housing Administration (FHA) issued several Mortgagee Letters to address the Lending Industry's concerns.

Most relevant to the Single Family loan origination community are:

- Mortgagee Letter (ML) 2020-05 – Re-verification of Employment and Exterior-Only and Desktop-Only Appraisal Scope of Work Options
- Mortgagee Letter (ML) 2020-07- FHA Catalyst: Case Binder Module-Single Family Forward and Home Equity Conversion (HECM) Electronic Endorsement Submission

Mortgagee Letter 2020-05

- FHA Single Family's modification to the re-verification of employment requirements due to the Presidentially-Declared COVID-19 National Declaration
- FHA Single Family's Exterior-Only or Desktop-Only Appraisal inspection option, which limits face-to-face contact for certain transactions affected by the Presidentially-Declared COVID-19 National Emergency Declaration
- Guidance was issued on March 27, 2020 and effective immediately. Subsequently extended by ML 2020-14.
- Guidance applied to loans closed on/before June 30, 2020



Mortgagee Letter 2020-07

- In response to the declaration of a National Emergency concerning the COVID-19 outbreak, Homeownership Centers moved to a full telework platform to protect the health and safety of staff and contractors.
- These steps hampered Mortgagees' ability to submit and HUD's ability to review physical case binders.
- FHA accelerated the deployment of a system to securely deliver case binder electronically for endorsement.
- FHA Catalyst allows Mortgagees to securely transmit Forward and HECM case binders for mortgage endorsement.

Additional COVID-19 Guidance

- Mortgagee Letter 2020-06 FHA's Loss Mitigation Options for Single Family Borrowers Affected by the Presidentially-Declared COVID-19 National Emergency in Accordance with the CARES Act
- Mortgagee Letter 2020-08 FHA Catalyst: Claims Module-Single Family Forward Supplemental Claims Digital Submission
- Mortgagee Letter 2020-09 Implementation of the Coronavirus Aid, Relief, and Economic Security (CARES) Act Forbearance
- Mortgagee Letter 2020-14 Extension of the Effective Date of ML 2020-05



Recent Updates



Recent Updates

Sections of the *Single Family Housing Handbook 4000.1*, last revised 10/24/2019 (*SF Handbook*) referenced in this training presentation provide standards for Single Family (1 to 4 units) mortgages to be insured under the National Housing Act.



SF Handbook Updates:
10/24/2019



Cash-Out Refinances: Maximum LTV/CLTV

- Reduced the Maximum LTV and CLTV percentages from 85% to 80% of the Adjusted Value on Cash-out Refinance Mortgages.
- Announced in Mortgagee Letter 2019-11
- Effective with case numbers assigned on/after 9/1/2019
- This policy change seeks to mitigate risks to the FHA Insurance Fund associated with increasing levels of insured loan balances on cash-out refinance mortgages.

Condominiums

FHA issued comprehensive revisions to Condominium Project Approval Requirements which include the Final Rule and SF Housing Policy Handbook updates.

- The condominium Final Rule became effective on 10/15/2019
- Loan Level/Single Unit Approval
- Please refer to pages 477-496 and 510-537 of the SF Handbook.



SF Handbook Updates:
8/14/2019



Conditional and Unconditional DELRAP Authority

Added a new section that defines the scope of authority, eligibility requirements, application and approval process, and post-approval requirements to obtain Conditional and Unconditional Direct Endorsement Lender Review and Approval Process (DELRAP) Authority.

Please refer to pages 37-41 of the SF Handbook.



Site Condominiums

Updated definition to align with new Site Condominium definition.

A Site Condominium refers to:

- a Condominium Project that consists entirely of single family detached dwellings that have no shared garages, or any other attached buildings; or
- a Condominium Project that:
 - consists of single family detached or horizontally attached (townhouse) dwellings where the unit consists of the dwelling and land;
 - does not contain any Manufactured Housing units; and
 - is encumbered by a declaration of condominium covenants or a condominium form of ownership.

Please refer to page 590 of the SF Handbook.

Condominiums

Added a new Condominium section that includes requirements for:

- Units Not Requiring Approval;
- Units in Approved Condominium Projects;
- Single-Unit Approval; and
- Site Condominiums

Please refer to pages 477-496 of the SF Handbook.

Condominium Project Approval and Project Definitions

- Added a new condominium Project Approval section with updated eligibility requirements to obtain FHA Condominium Project Approval and the Project Approval Submission process for the HUD Review and Approval Process (HRAP) and DELRAP.
- Updated definitions to align with new Condominium Project, Common Elements, and Site condominium definitions.

SF Handbook 4000.1 Updates **7/10/2019**



Use of TOTAL Mortgage Scorecard

All transactions must be scored through TOTAL Mortgage Scorecard, except Streamline Refinance transactions, Reverse Mortgages, assumptions, and Mortgages made to nonprofit/Governmental Entity Borrowers.

SF Handbook 4000.1, Page 182



TOTAL/Manual Income Requirements

General Income Requirements:

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

SF Handbook Page 203/278



Overtime, Bonus or Tip Income

(C) Calculation of Effective Income:

- For employees with Overtime, Bonus or Tip Income, the Mortgagee must calculate the Effective Income by using the lesser of:
 - The average Overtime, Bonus or Tip Income earned over the previous two years or, if less than two years, the length of time Overtime, Bonus or Tip Income has been earned; or
 - The average Overtime, Bonus or Tip Income earned over the previous year.

SF Handbook Page 206/281

Commission Income

(D) Calculation of Effective Income:

- The Mortgagee must calculate Effective Income for commission by using the lesser of:
 - Either, (i) the average Commission Income earned over the previous two years for Commission Income earned for two years or more, or (ii) the length of time Commission Income has been earned if less than two years; or
 - The average Commission Income earned over the previous year.

SF Handbook Page 208/284



Automobile Allowances

(3) Calculation of Effective Income:

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

SF Handbook Page 216/292



Cash to Close

(h) Premium Pricing on FHA-Insured Mortgages:

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

SF Handbook Page 229/304



Interested Party Contributions

Definition:

Interested Parties refer to sellers, real estate agents, builders, developers, Mortgagees, **Third Party Originators (TPO)**, or other parties with an interest in the transaction.

Exceptions:

Premium Pricing credits from the Mortgagee or TPO are excluded from the six percent limit, provided the Mortgagee or TPO is not the seller, real estate agent, builder, or developer.

SF Handbook Page 237/312



Interested Party Contributions (cont.)

(3) Required Documentation

The Mortgagee must document the total Interested Party Contributions on the sales contract or applicable legally binding document, form HUD-92900-LT, and Closing Disclosure or similar legal document. When a legally binding document other than the sales contract is used to document the Interested Party Contributions, the Mortgagee must provide a copy of this document to the assigned Appraiser.

SF Handbook Page 238/313



Interested Party Contributions (cont.)

(3) Rent Below Fair Market (TOTAL)

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

SF Handbook Page 239/315



Closing

ii. Required Documentation for Disbursement of Mortgage Proceeds

The Mortgagee must obtain the final Closing Disclosure or similar legal document from the settlement agent. **If the seller's Closing Disclosure or similar legal document is provided separately, the Mortgagee must obtain from the Closing Agent a copy of the final disclosure provided to the seller to keep in the case binder.**

SF Handbook Page 354



Post Closing and Endorsement

v. Closing Disclosure and Settlement Certification

Confirm that the Closing Disclosure or similar legal document is complete and signed by all required parties, and the Settlement Certification is complete and signed by the Borrower, seller (as applicable, except in case of HUD Real Estate Owned (REO) Sales), and settlement agent. The Settlement Certification is not required for refinance transactions. If the seller's Closing Disclosure or similar legal document is provided separately, the Mortgagee must obtain from the Closing Agent a copy of the final disclosure provided to the seller to keep in the case binder.

SF Handbook Page 356



Inspection Requirements-PDMDA

(c) All Properties with pending Mortgages or endorsements in areas under a Presidentially-Declared Major Disaster Areas (PDMDA) designated for individual assistance must have a damage inspection report that identifies and quantifies any dwelling damage. The damage inspection report must be completed by an FHA Roster Appraiser even if the inspection shows no damage to the Property, and the report must be dated after the Incident Period (as defined by FEMA) or 14 Days from the Incident Period start date, whichever is earlier. If the effective date of the appraisal is on or after the date required above for an inspection, a separate damage inspection report is not necessary.

SF Handbook Page 358



Net Tangible Benefit-Streamline Refinance

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

SF Handbook Page 426-427



Origination/Processing



General Requirements



Maximum Age of Documents

General Document Age

Documents used in origination and underwriting a mortgage may not be more than **120 days old at the Disbursement Date**.

- The **Disbursement Date** refers to the date the proceeds of the mortgage are made available to the borrower.

Mortgage Loan Application

- Uniform Residential Loan Application (URLA) and HUD/VA Addendum to the URLA.
- The Mortgagee **must** obtain **the Borrower's initial completed *signed* URLA** (Fannie Mae Form 1003/Freddie Mac Form 65) and Page 2 of form HUD-92900-A ***before underwriting*** the mortgage application.

Mortgage Loan Application (cont.)

Government-Issued Photo ID:

- The Mortgagee **must** include a statement that they have verified the borrower's identity using a valid government-issued photo identification prior to endorsement of the mortgage; **or**
- The Mortgagee may choose to include a copy of such photo identification in the case binder.

Non-Borrowing Spouse Community Property State: Consent and Authorization

The Mortgagee **must** obtain a non-Borrowing spouse's consent and authorization when necessary to:

Verify specific information required to process the mortgage application, including the consent to verify their SSN with the Social Security Administration (SSA).

Chain of Title

- The Mortgagee **must** obtain evidence of prior ownership when a property was sold within 12 months of the case number assignment date.
- The Mortgagee **must** review the evidence of prior ownership to determine any undisclosed Identity-of-Interest transactions.

Identity-of-Interest – Tenant/Landlord

- The maximum LTV percentage for a transaction where a tenant-landlord relationship exists at the time of contract execution is restricted to 85 percent.
- Exception to the Maximum LTV: The 85 percent LTV restriction may be exceeded if the current tenant purchases the Property where the tenant has rented the Property for at least six months immediately predating the Sales Contract. A lease or other written evidence to verify occupancy is required.

Borrower Eligibility



Borrower Minimum Decision Credit Score

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

Multiple Borrowers MDCS

- Where the mortgage involves multiple Borrowers, the Mortgagee must determine the MDCS for each Borrower, and then select the lowest MDCS for all Borrowers.
- Where the mortgage involves multiple Borrowers and one or more of the Borrowers do not have a credit score (non-traditional or insufficient credit), the Mortgagee must select the lowest MDCS of the Borrower(s) with credit score(s).
- Where the mortgage involves multiple Borrowers and **none of the Borrowers report a credit score** (non-traditional or insufficient credit), the borrowers may **still be eligible for FHA-insured financing.**

Eligibility Requirement Minimum Decision Credit Score

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



Non-occupying Co-borrowers or Co-signers

Non-occupying co-Borrowers or co-Signers must either be:

- United States (U.S.) citizens; or
- Have a Principal Residence in the U.S.

Borrower Ineligibility

Borrower Ineligibility Due to Delinquent Federal Non-Tax Debt

- Mortgagees are prohibited from processing an application for a FHA-insured mortgage for Borrowers with delinquent federal non-tax debt, including deficiencies and other debt associated with past FHA-insured mortgages.
- Mortgagees are required to determine whether the Borrowers have **delinquent federal non-tax debt**.
- Mortgagees may obtain information on delinquent Federal Debts from public records, credit reports or equivalent, and must check all Borrowers against the **Credit Alert Verification Reporting System (CAIVRS)**.
- **Resolution**-In order for a Borrower with verified delinquent Federal Debt to become eligible, the Borrower must resolve their federal non-tax debt in accordance with the Debt Collection Improvement Act.

Allowable Mortgage Parameters



LTV Limitations Based on Borrower's Credit Score

- The **Minimum Decision Credit Score (MDCS)** will be used to determine the maximum insured financing available to a Borrower with traditional credit.
- The Mortgagee must determine the Borrower's MDCS, except for mortgages to be insured under Section 247-Hawaiian Home Lands, Section 248-Mortgages on Indian Land, Streamline Refinances, and Assumptions.

Adjusted Value: Purchase

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

- Purchase price less any Inducements to Purchase; or
- Property Value:
 - The value as determined by the FHA Roster Appraiser.

Adjusted Value: Refinance

- For properties acquired by the Borrower within 12 months of the case number assignment date, the Adjusted Value is the lesser of:
 - The Borrower's purchase price, plus any documented improvements made after the purchase; **or**
 - The Property Value.
- This policy applies to all FHA refinance transactions which require appraisals including FHA to FHA refinance transactions.

Adjusted Value: Refinance (cont.)

- For properties acquired by the Borrower within 12 months of the case number assignment by inheritance or through a gift from a family member may:
 - Utilize the calculation of Adjusted Value for properties purchased 12 months of greater.
- For properties acquired by the Borrower greater than or equal to 12 months prior to the case assignment date: the Adjusted Value is the Property Value.

TOTAL vs. Manual



When to Downgrade



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When to Downgrade

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

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

When to Downgrade (cont.)

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

Mortgage Payment Downgrade

Obligations/Mortgage Payment History-Purchase and No Cash-Out Refinance Transactions

Purchase and No Cash-Out Refinance Transactions

Downgraded to a **REFER** if any mortgage trade line reflects:

Most recent 12 months

$\geq 3 \times 30$ days –

Three or more late payments of greater than 30 days

$\geq 1 \times 60 + > 1 \times 30$

One or more late payments of 60 Days plus one or more 30-day late payments.

$\geq 1 \times 90$

One payment greater than 90 Days late.

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

**Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



Mortgage Payment Downgrade (cont.)

Obligations/Mortgage Payment History Cash-Out Refinance Transactions

Cash-Out Refinance Transactions

Downgraded to a **REFER** if any mortgage trade line reflects:

- Any Delinquency within 12 months of the case assignments date; or
- A current delinquency.

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

**Modified Mortgage utilize the payment history in accordance with the modification agreement for the time period of modification in determining late housing payments.



Applicability of Automated Underwriting System Rules

If the mortgage application must be manually downgraded, the Mortgagee must cease its use of the AUS and **comply with all requirements for manual underwriting** when underwriting a downgraded mortgage.

Inconsistencies: Credit Report and Mortgage File

- **TOTAL**: The Mortgagee **must** obtain a new credit report **and** rescore the mortgage through TOTAL if the underwriter identifies inconsistencies between any information in the mortgage file and the original credit report.
- **MANUAL**: The Mortgagee **must** obtain an updated credit report or supplement if the underwriter identified inconsistencies between any information in the mortgage file and original credit report.

TOTAL vs. Manual Credit



Judgments

TOTAL and MANUAL

- **Judgment** refers to any debt or monetary liability of the Borrower, and the Borrower's spouse in a community property state unless excluded by state law, created by a court, or other adjudicating body.
- The Mortgagee must verify that court-ordered Judgments are resolved or paid off prior to or at closing.
- Judgments of a non-borrowing spouse in a community property state must be resolved or paid in full, with the exception of obligations excluded by state law.

Judgments: Exception Policy Clarification

TOTAL and MANUAL:

A Judgment is considered resolved if the Borrower has:

- Entered into a valid agreement with the creditor to make regular payments on the debt;
- Has made timely payments for at least **three months** of scheduled payments; **and**
- The Judgment will not supersede the FHA-insured mortgage lien. The Borrower **cannot prepay** scheduled payments in order to meet the required minimum of three months of payments.

Judgments: Additional Requirement

MANUAL

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

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

Credit Counseling/Payment Plan

TOTAL

- No explanation or other documentation is needed.

MANUAL

- The Mortgagee must document:
 - One year of the pay-out period has elapsed under the plan;
 - 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.

Mortgage Modifications

TOTAL and MANUAL

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



TOTAL vs. MANUAL Liabilities and Debts



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Inquiries - Manual

Material Inquiries

- Refers to inquiries that may potentially result in obligations incurred by the Borrower for other mortgages, auto loans, leases, or other Installment Loans.
- Inquiries from department stores, credit bureaus, and insurance companies are not considered material inquiries.
- The Mortgagee must document all undisclosed debt and support for its analysis of the Borrower's debt.

Borrower's Total Mortgage Payment

TOTAL and MANUAL

- The Mortgagee must use accurate estimates of monthly tax escrows when calculating the total Mortgage Payment.
- In New Construction cases **and** Manufactured Homes converting to real estate, property tax estimates **must** be based on both the land and improvements.
- Where real estate taxes are **abated**, Mortgagees **may** use the abated amount provided that:
 - The Mortgagee can document the abated amount with the taxing authority; and
 - The abatement will remain in place for at least the first three years of the Mortgage.

Closed-end Debts Paid Off Within 10 Months

TOTAL and MANUAL

- Closed-end debts do not have to be included if:
 - They will be paid off within 10 months; **and**
 - The cumulative payments of all such debts are less than or equal to five percent of the Borrower's gross monthly income.
- The Borrower **may not pay down** the balance in order to meet the 10 months requirement.

Undisclosed Debt *Other* Than a Mortgage

TOTAL and MANUAL

- When a debt or obligation (other than a mortgage) is not listed on the application and/or credit report, the Mortgagee must:
 - Verify the actual monthly payment amount; **and**
 - Determine that any funds borrowed were not/will not be used for the Borrower's MRI (Minimum Required Investment).

TOTAL

- If the debt was not considered by the AUS, the Mortgagee must:
 - Re-submit the Mortgage for evaluation by TOTAL if the cumulative change in the amount of the Borrower's liabilities increases by more than \$100 per month. Enter the debt into TOTAL.

Alimony, Child Support, or Other Maintenance

- The Mortgagee must calculate the Borrower's monthly obligation from the greater of:
 - The amount shown on the most recent decree or agreement establishing the Borrower's payment obligation; or
 - The monthly amount of the garnishment.
- The Mortgagee must obtain the official signed divorce decree, separation agreement, maintenance agreement, or other legal order.
- The Mortgagee must also obtain the Borrower's pay stubs covering no less than **28 consecutive Days** to verify whether the Borrower is subject to any order of garnishment relating to the alimony, child support, or other maintenance.

Installment Loan Monthly Payment Clarification

TOTAL and MANUAL

- If the monthly payment shown on the credit report is utilized to calculate the monthly debts, no further documentation is required.
- If the credit report does not include a monthly payment for the loan, the Mortgagee **must** obtain a copy of the loan agreement or payment statement documenting the amount of the monthly payment and enter it into TOTAL Mortgage Scorecard.
- If the payment cannot be documented the Mortgagee **must** calculate the payment at five percent of the balance.

Deferred Obligations: Clarification (Excluding Student Loans)

TOTAL and MANUAL

- Deferred Obligations refer to liabilities that have been incurred but where payment is deferred or has not yet commenced, including accounts in forbearance.
- The Mortgagee **must** verify and **include deferred obligations** in the calculation of the Borrower's debt.
- Mortgagee **must** use the actual monthly payment to be paid on a deferred liability whenever available.
- If the actual monthly payment is not available:
 - **Installment Debt (not including student loans)**, the Mortgagee **must** utilize five percent of the outstanding balance to establish the monthly payment.

Deferred Obligations: Clarification (cont.)

If the actual monthly payment is not available:

Student Loan:

- If the payment used for the monthly obligation is:
 - Less than one percent of the outstanding balance reported on the Borrower's credit report, **and**
 - Less than the monthly payment reported on the Borrower's credit report:
 - the Mortgagee **must** obtain written documentation of the actual monthly payment, the payment status, and evidence of the outstanding balance and terms from the creditor.

Deferred Obligations: Clarification (cont.)

Student Loans (cont.)

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

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

Business Debt in Borrower's Name

TOTAL and MANUAL

When a self-employed Borrower states debt appearing on their personal credit report is being paid by their business, the Mortgagee **must** obtain documentation to evidence the following:

- The company has been making regular on-time payments during the previous **12 months without delinquency**;
- The debt is paid out of company funds; **and**
- The debt was considered in the **cash-flow analysis** of the Borrower's business.

Business Debt Considered in Cash Flow Analysis

When the Borrower's personal debt being paid by the Borrower's business is considered in the cash flow analysis, then the Borrower's business tax returns must reflect:

- A business expense related to the obligation, equal to or greater than the amount of payments documented as paid out of company funds, and may be added back to the net income; **and/or**
- An interest expense related to the obligation;
 - **Only** the interest portion of the debt may be considered in the cash flow analysis and added back to the net income.

TOTAL vs. Manual Income Requirements



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GENERAL Income Requirements

- **Effective Income** refers to income that may be used to qualify a Borrower for a mortgage.
- **Effective Income** must:
 - Be likely to continue through at least the first three years of the mortgage;
 - Be documentable;
 - Be legally derived;
 - Be reported to the IRS when required; and
 - Subtract negative income from the Borrower's gross monthly income.
- If FHA requires tax returns for any type of Effective Income, the Mortgagee must also analyze the tax returns in accordance with Appendix 2.0-Analyzing IRS Forms.

Re-verification of Employment

TOTAL and MANUAL

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

Calculation of Effective Income: Hourly

TOTAL and MANUAL

- Hourly Wages which:
 - **Do not vary:** the Mortgagee must consider the Borrower's current hourly rate to calculate Effective Income.
 - **Vary:** the Mortgagee **must** average the income over the previous two years.
- If the Mortgagee can **document an increase in pay rate**, the Mortgagee **may** use the most recent 12 month average of hours at the current pay rate.

Overtime, Bonus or Tip Income

TOTAL and MANUAL

- The Mortgagee may use Overtime, Bonus or Tip Income as Effective Income if the Borrower has received this income for the **past two years** and it is **reasonably likely to continue**.
- Periods of Overtime, Bonus or Tip Income **less than two years** may be considered Effective Income if the Mortgagee documents that the Overtime, Bonus or Tip Income has been consistently earned over a period of **not less than one year and is reasonably likely to continue**.

Overtime, Bonus or Tip Income: Calculation

TOTAL and MANUAL

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

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

Seasonal Employment

TOTAL and MANUAL

- The Mortgagee may consider Seasonal Employment income as Effective Income if the Borrower:
 - Has worked in the same line of work for the past two years; **and**
 - Is reasonably likely to be rehired for the next season.
- The Mortgagee **may** consider unemployment income as Effective Income for those with effective Seasonal Employment income.

Seasonal Employment

TOTAL and MANUAL

Calculation of Effective Income:

- For employees with Seasonal Employment income, the Mortgagee **must** average the income earned over the previous two full years to calculate Effective Income.
- For seasonal employees with unemployment income, the Mortgagee **must** document the **unemployment income for two full years** and there must be reasonable assurance that this income will continue.

Commission Income

TOTAL and MANUAL

The Mortgagee may use Commission Income as Effective Income if:

- The Borrower earned the **income for at least one year in the same or similar line of work; and**
- It is reasonably likely to continue.

Commission Income: Effective Income

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

- Either, (i) the average Commission Income earned over the previous two years for Commission Income earned for two years or more, or (ii) the length of time Commission Income has been earned if less than two years; or
- The average Commission Income earned over the previous year.

Self-Employment Income

TOTAL and MANUAL

- Self-Employment Income refers to income generated by a business in which the Borrower has a 25 percent or greater ownership interest.
- The Mortgagee may consider Self-Employment Income if the Borrower has been self-employed **for at least two years**.

Self-Employment Income: Stability

TOTAL and MANUAL

- If the Borrower has been self-employed between **one and two years**, the Mortgagee may only consider the income as Effective Income if the Borrower was previously employed in the same line of work in which the Borrower is self-employed or in a related occupation for at least two years.
- Income obtained from businesses with **annual earnings that are stable or increasing is acceptable.**

Self-Employment Income: Stability (cont.)

TOTAL

If the income from businesses show a **decline** in Effective Income of **20 percent or more** over the analysis period, the Mortgagee **must downgrade** the transaction to a Refer and manually underwrite the transaction.

Self-Employment Income: Stability (cont.)

MANUAL

Mortgagee may consider income as stable after a 20 percent reduction if:

- The Mortgagee can document the reduction in income was the result of an extenuating circumstance;
- The Borrower can demonstrate the income has been stable or increasing for a minimum of 12 months; **and**
- The Borrower qualifies utilizing the reduced income.

Self-Employment Income: Documentation

TOTAL

- The Mortgagee **must** obtain completed individual federal tax returns for the most recent two years, including all schedules.
- The Mortgagee **must** obtain the Borrower's business federal tax returns, including all schedules, for the most recent two years unless the following criteria are met:
 - Individual federal income tax returns show increasing Self-Employment Income over the past two years;
 - Funds to close are **not** coming from business account; **and**
 - The mortgage to be insured is **not a cash-out refinance**.

Self-Employment Income: Documentation (cont.)

MANUAL

- The Mortgagee must obtain signed, completed individual and business federal tax returns for the most recent two years, including all schedules.
- The Mortgagee must obtain a business credit report for all corporations and 'S' corporations.

Self-Employment Income: Documentation (cont.)

- The Mortgagee must obtain a year-to-date Profit and Loss (P&L) statement and balance sheet if:
 - More than a calendar quarter has elapsed since date when the most recent calendar or fiscal year-end tax return was filed by the Borrower.
- A balance sheet is not required for self-employed Borrowers filing Schedule-C income.
- If income used to qualify the Borrower exceeds the two year average of tax returns, an audited P&L or signed quarterly tax return must be obtained from the IRS.

Self-Employment Income: Documentation (cont.)

TOTAL and MANUAL

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

- A signed IRS Form 4506, Request for Copy of Tax Return;
- IRS Form 4506-T, Request for Transcript of Tax Return; or
- IRS Form 8821, Tax Information Authorization, and obtain tax transcripts directly from the IRS.



Self-Employment Income: Calculation

TOTAL and MANUAL

The Mortgagee **must** calculate gross Self-Employment Income by using the lesser of:

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

Frequent Changes in Employment

TOTAL and MANUAL

- If the Borrower has changed jobs more than **three times** in the **previous 12 month period**, **or has changed lines of work**, the Mortgagee **must** take additional steps to verify and document the stability of the Borrower's Employment Income.
- The Mortgagee **must** obtain:
 - Transcripts of training and education demonstrating qualification for a new position, **or**
 - Employment documentation evidencing continual increases in income and/or benefits.

Gaps in Employment

TOTAL and MANUAL

- For Borrowers with gaps in employment of **six months or more** (an extended absence), the Mortgagee may consider the Borrower's current income as Effective Income if it can verify and document the Borrower:
 - Has been employed in the current job for at least six months at the time of case number assignment; **and**
 - Had a two year work history prior to the absence from employment using standard or alternative employment verification.

Temporary Reduction in Income

TOTAL and MANUAL

- For Borrowers with a temporary reduction of income due to a short-term disability or similar temporary leave, the Mortgagee may consider the Borrower's current income as Effective Income if it can verify and document that the Borrower:
 - **Intends** to return to work;
 - **Has the right** to return to work, **and**
 - **Qualifies** for the mortgage taking into account any **reduction of income** due to the circumstance.
- For Borrowers returning to work before or at the time of the first Mortgage Payment due date, the Mortgagee may use the Borrower's pre-leave income.

Temporary Reduction in Income: Calculation (cont.)

TOTAL and MANUAL

For Borrowers returning to work after the first Mortgage Payment due date:

- The Mortgagee may use the Borrower's current income plus available surplus liquid asset Reserves, above and beyond any required Reserves, as an income supplement up to the amount of the Borrower's pre-leave income.
- The amount of the monthly income supplement is:
 - The total amount of **surplus liquid asset Reserves** divided by the number of months between the first payment due date and the Borrower's intended date of return to work.
- **Surplus Liquid Asset Reserves:** Liquid asset reserves above and beyond the program requirements.

Alimony, Child Support, or Maintenance Income

TOTAL and MANUAL

- The Mortgagee **must** obtain a fully executed copy of the Borrower's final divorce decree, legal separation agreement, court order, or voluntary payment agreement with documented receipt.
- The Mortgagee **may** use the front and pertinent pages of the divorce decree/settlement agreement and/or court order showing the financial details.

Alimony, Child Support or Maintenance Income: Legal Record - Documentation

- When using a final divorce decree, legal separation agreement, or court order, the Mortgagee must obtain evidence of receipt using the following documentation for the **most recent three months** that supports the amount used in qualifying:
 - Deposits on bank statements;
 - Canceled checks; or
 - Documentation from the child support agency.

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

Alimony, Child Support, or Maintenance Income: Voluntary – Effective Income

TOTAL and MANUAL

When using evidence of voluntary payments, if the Borrower has received consistent alimony, child support or other maintenance payments for the most recent **six months**, the Mortgagee may use the current payment to calculate Effective Income.

The Mortgagee **must** provide evidence that the claimed income will continue for at least three years.

Alimony, Child Support, or Maintenance Income: Inconsistent Payments – Effective Income

TOTAL and MANUAL

- If legal record or voluntary payment alimony, child support, or other maintenance payments **have not been consistently received** for the **most recent six months**, the Mortgagee **must** use the **average of the income received over the previous two years** to calculate Effective Income.
- If Alimony, Child Support, or Maintenance Income has been received for **less than two years**, the Mortgagee **must use the average over the time of receipt**.

Automobile Allowances

- Automobile Allowance refers to the funds provided by the Borrower's employer for automobile expenses.
- The Mortgagee must verify and document the Automobile Allowance received from the employer for the previous two years.
- The Mortgagee must use the full amount of the Automobile Allowance to calculate Effective Income.

Expected Income

TOTAL and MANUAL

- **Expected Income** refers to income from cost-of-living adjustments, performance raises, a new job, or retirement that has not been, but will be received within 60 Days of mortgage closing.
- The Mortgagee may consider Expected Income as Effective Income **except** when the Expected Income is to be derived from a family-owned business.

Expected Income: Verification

TOTAL and MANUAL

- The Mortgagee must verify and document that the Borrower will have sufficient income or cash reserves to support the mortgage payment **and** any other obligations between the mortgage closing and the start of the Expected Income.
- For expected Employment Income, the Mortgagee must verify the existence and the amount of the Expected Income with the employer in writing and that it is guaranteed to begin within **60 Days** of mortgage closing.
- For expected Retirement Income, the Mortgagee must verify the amount and that it is **guaranteed** to begin within **60 Days** of the mortgage closing.

Non-Taxable Income (Grossing Up)

TOTAL and MANUAL

- Non-Taxable Income refers to types of income not subject to federal taxes.
- The Mortgagee **must** document and support:
 - The amount of income to be Grossed Up for any non-taxable income source; **and**
 - The current tax rate applicable to the Borrower's income that is being Grossed Up.

Non-Taxable Income (Grossing Up): Calculation

TOTAL and MANUAL

- Non-Taxable Income that may be added **cannot exceed the greater of 15 percent or the appropriate tax rate for the income amount**, based on the Borrower's tax rate for the previous year.
- If the Borrower was **not required** to file a federal tax return for the previous tax reporting period, the Mortgagee may Gross Up the Non-Taxable Income by **15 percent**.
- The Mortgagee **may not** make any additional adjustments or allowances based on the number of the Borrower's dependents.

TOTAL vs. Manual Rental Income



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Evaluating Rental Income

TOTAL and MANUAL

- How to evaluate Rental Income:
 - How long has the Borrower owned the property?
 - Is the rental income being received from the subject property?
 - Does the Borrower have a history of receiving rental income from the subject since the previous tax filing?

Limited/No History of Rental Income Received: Subject Property (TOTAL and Manual)

Borrower Does Not Have a History of Rental Income from the Subject :	One Unit	Two-to-Four Units
	<p>Fannie Mae Form 1004/Freddie Mac Form 70, Uniform Residential Appraisal Report, Fannie Mae Form 1007/Freddie Mac Form 1000I, Single Family Comparable Rent Schedule, and Fannie Mae Form 216/Freddie Mac Form 998, Operating Income Statement, showing fair market rent.</p>	<p>Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Max Form 72, Small Residential Income Property Appraisal Report)</p>
	<p>The prospective executed lease, if available</p>	<p>The prospective executed leases, if available</p>
	<p>Document the date of acquisition by provided the deed, Settlement Statement or other legal document.</p>	

History of Rental Income Received Subject Property (TOTAL and Manual)

The Borrower has a history or Rental Income from the subject since the previous tax filing:	One Unit	Two-to-Four Units
	Executed lease	Executed leases
	24 month rental history free of unexplained gaps > 3 months	24 month rental history free of unexplained gap > 3 months
	Borrower's most recent 2 years Tax Returns including Schedule E	Borrowers most recent 3 years Tax Returns including Schedule E
Properties with less than 2 years of Rental Income history, the date of acquisition must be documented by providing the deed, Settlement Statement or other legal document.		

Note: If rental history over the previous 24 months reflects gaps greater than 3 months, an explanation is required.

History of Rental Income Received Subject Property: Calculation (cont.)

TOTAL and MANUAL

The following items shown on the Schedule E may be added back to the income or loss:

- Depreciation;
- Mortgage interest;
- Taxes;
- Insurance; and
- Any HOA Dues.

Rental Income: Property Being Vacated by the Borrower (TOTAL and Manual)

Rental Income from the Property being Vacated by the Borrower:	One Unit	Two – Four Units
	<p>Fannie Mae Form 1004/Freddie Mac Form 70, Uniform Residential Appraisal Report, Fannie Mae Form 1007/Freddie Mac Form 10001</p> <p>Single Family Comparable Rent Schedule, and Fannie Mae Form 216/Freddie Mac Form 998, Operating Income Statement, showing fair market rent.</p>	<p>Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, Small Residential Income Property Appraisal Report)</p>
	<p>Minimum 25 percent equity in vacated property</p>	<p>Minimum 25 percent equity in vacated property</p>
	<p>Executed 1-year lease agreement, commencing after the closing</p>	<p>Executed 1-year lease agreement, commencing after the closing</p>
	<p>Evidence of payment of the security deposit or first month's rent of lease agreement</p>	<p>Evidence of payment of the security deposit or first month's rent of lease agreement</p>
	<p>Evidence that the Borrower is relocating to an area more than 100 miles from the Borrower's current Principal Residence.</p>	

Rental Income: Limited or No History-Other Real Estate (TOTAL and Manual)

Rental Income Limited or No History by the Borrower:

One Unit	Two-to-Four Units
<p>Fannie Mae Form 1004/Freddie Mac Form 70, Uniform Residential Appraisal Report, Fannie Mae Form 1007/Freddie Mac Form 1000I</p> <p>Single Family Comparable Rent Schedule, and Fannie Mae Form 216/Freddie Mac Form 998, Operating Income Statement, showing fair market rent.</p>	<p>Appraisal showing fair market rent (use Fannie Mae Form 1025/Freddie Mac Form 72, Small Residential Income Property Appraisal Report)</p>
<p>Investment property must support a minimum 25 percent equity position</p>	<p>Investment property must support a minimum 25 percent equity position</p>
<p>Executed 1-year lease agreement</p>	<p>Executed 1-year lease agreement</p>
<p>Properties with less than 2 years of Rental Income history, the date of acquisition must be document by providing the deed, Settlement Statement or other legal document.</p>	

Rental Income: History Other Real Estate (TOTAL and Manual)

The Borrower has a History of Rental Income Since the Previous Tax Filing:

One Unit

Borrower's most recent 2 years executed Tax Returns including Schedule E

Two-to-Four Units

Borrower's most recent two years executed Tax Returns including Schedule E

Properties with less than 2 years of Rental Income history, the date of acquisition must be documented by providing the deed, Settlement Statement or other legal document.



Self-Sufficiency Rental Income Eligibility (Three-to-Four Unit Properties)

TOTAL and MANUAL

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

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

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



TOTAL vs. Manual Assets



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General Asset Requirements

TOTAL and MANUAL

- The Mortgagee may only consider assets derived from acceptable sources in accordance with FHA Single Family Housing Policy.
- Closing costs, prepaid items, and other fees may not be applied towards the Borrower's minimum required investment (MRI).

Earnest Money Deposit (EMD)

TOTAL and MANUAL

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

- A copy of the Borrower's cancelled check; **or**
- Certification from the deposit-holder acknowledging receipt of funds; **or**
- A Verification of Deposit (VOD) or bank statement showing that the **average balance** was sufficient to cover the amount of the EMD at the time of the deposit.

Real Estate Tax Credits

TOTAL and MANUAL

- Where real estate taxes are paid in arrears, the seller's real estate tax credit may be used to meet the MRI, **if** the Mortgagee documents that the Borrower had **sufficient assets to meet the MRI and the Borrower paid closing costs at the time of underwriting.**
- This permits the Borrower to bring a portion of their MRI to the closing and combine that portion with the real estate tax credit for their total MRI.

Reserves

TOTAL and MANUAL

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

MANUAL Only:

- Reserves do not include:
 - The amount of cash taken at settlement in cash-out transactions;
 - Incidental cash received at settlement in other loan transactions;
 - Gift funds;
 - Equity in another Property; or
 - Borrowed funds from any source.

Reserves (cont.)

MANUAL

The Mortgagee must verify and document Reserves after closing equivalent to:

- One month PITI for one-to two-unit properties.
- Three months PITI for three-to four-unit properties.

Source Requirements for the Borrower's Minimum Required Investment (MRI)

TOTAL and MANUAL

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

Source Requirements for the Borrower's Minimum Required Investment (MRI) (cont.)

TOTAL and MANUAL

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

- The seller of the property; **or**
- Any other person or Entity who financially benefits from the transaction (directly or indirectly); **or**
- Anyone who is or will be reimbursed, directly or indirectly, by any party included in (1) or (2) above.

Source Requirements for the Borrower's Minimum Required Investment (MRI) (cont.)

TOTAL and MANUAL

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

Checking and Savings Accounts

TOTAL and MANUAL

For recently opened accounts and recent individual deposits of more than **one percent of the Adjusted Value**, the Mortgagee **must**:

- Obtain documentation of the deposits; **and**
- Verify that no debts were incurred to obtain part, or all, of the MRI.

Standards for Gifts

TOTAL and MANUAL

Gifts may be provided by:

- The Borrower's **Family Member**;
- The Borrower's employer or labor union;
- A close friend with a clearly defined and documented interest in the Borrower;
- A charitable organization;
- A governmental agency or Public Entity that has a program providing homeownership assistance to:
 - Low or moderate income families
 - First-time homebuyers

Family Member

TOTAL and MANUAL

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

- Child, parent, or grandparent;
 - A child is defined as a son, stepson, daughter, or stepdaughter.
 - Parent or grandparent includes a step-parent/grandparent or foster parent/grandparent.
- Spouse or domestic partner; and
- Legally adopted son or daughter, including a child who is placed with the Borrower by an authorized agency for legal adoption;

Family Member (cont.)

TOTAL and MANUAL

- Foster child;
- Brother, stepbrother;
- Sister, stepsister;
- Uncle;
- Aunt; **or**
- Son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, sister-in-law of the Borrower.

Documenting the Transfer of Gifts

TOTAL and MANUAL

- The Mortgagee **must** verify and document the transfer of gift funds from the donor to the Borrower.
- Regardless of when gift funds are made available to a Borrower, the Mortgagee **must** be able to make a reasonable determination that the gift funds were not provided by an unacceptable source and were the donor's own funds.

Documenting the Transfer of Gifts (cont.)

TOTAL and MANUAL

If the gift funds:

- Have been verified in the Borrower's account, obtain the donor's bank statement showing the withdrawal **and** evidence of the deposit into the Borrower's account.
- Are not verified in the Borrower's account:
 - Obtain the certified check, money order, cashier's check, wire transfer **or** other official check evidencing payment to the Borrower or settlement agent; **and**
 - The donor's bank statement evidencing sufficient funds for the amount of the gift.

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

Documenting the Transfer of Gifts (cont.)

TOTAL and MANUAL

- If the gift funds are being borrowed by the donor and documentation from the bank or other savings account is not available, the Mortgagee **must** have the donor provide written evidence that the funds were borrowed from an acceptable source, not from a party to the transaction.
- The Mortgagee and its Affiliates are prohibited from providing the loan of gift funds to the donor unless the terms of the loan are equivalent to those available to the general public.

Interested Party Contributions (TOTAL and Manual)

- Interested Parties refer to sellers, real estate agents, builders, developers, Mortgagees, Third Party Originators (TPO), or other parties with an interest in the transaction.
- Interested Party Contribution refers to a payment by an Interested Party, or combination of parties, toward the Borrower's origination fees, other closing costs, prepaid items and/or discount points.

Interested Party Contributions (TOTAL and Manual)

- Interested Parties may contribute up to six percent of the sales price toward the Borrower's origination fees, other closing costs, prepaid items and discount points. The six percent limit also includes:
 - Interested Party payment for permanent and temporary interest rate buydowns, and other payment supplements;
 - Payments of mortgage interest for fixed rate Mortgages;
 - Mortgage Payment protection insurance; and
 - Payment of the UFMIP.
- Interested Party Contributions that exceed actual costs/fees are considered an inducement to purchase. Interested Party Contributions exceeding six percent are considered an inducement to purchase.

Interested Party Contributions (TOTAL and Manual)

Exception -

- Premium Pricing credits from the Mortgagee or TPO are excluded from the six percent limit provided the Mortgagee or TPO is not the seller, real estate agent, builder or developer.

Required Documentation –

- The Mortgagee must document the total contribution on the sales contract, HUD 92900-LT and Closing Disclosure. When a legally binding document other than the sales contract is used, the Mortgagee must provide a copy of the document to the assigned Appraiser.

Inducement to Purchase

Rent Below Fair Market

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

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

Secondary Financing

TOTAL and MANUAL

- Secondary Financing is any financing other than the first mortgage that creates a lien against the property.
- Any such financing that creates a lien against the property is not considered a gift or a grant **even if it does not require regular payments or has other features forgiving the debt.**

Secondary Financing-Quick Reference

	Governmental Entities and HOPE Grantees	HUD-Approved Non Profits	Family Members	Private Individuals and Other Organizations
Nationwide Mortgage Limits	The insured 1 st mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The insured 1 st mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The insured 1 st mortgage cannot exceed the FHA Nationwide Mortgage Limit for the area in which the property is located.	The Base Loan and secondary financing amounts must not exceed the Nationwide Mortgage Limits for the area in which the property is located.
Secondary Financing for Borrower's MRI	Any secondary financing of the Borrower's MRI must fully comply with the additional requirements in <u>Source Requirements</u> for the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.	The secondary financing may not be used to meet the Borrower's MRI.
CLTV Limitations	No maximum Combined Loan-to-Value (CLTV)	No maximum Combined Loan-to-Value (CLTV)	CLTV ratio of the Base Loan Amount and the secondary financing amount must not exceed 100 percent of the Adjusted Value.	The CLTV ratio of the Base Loan Amount and the secondary financing amount must not exceed the applicable FHA LTV limit.

Manual Underwriting of the Borrower



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Introduction

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

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

Non-Traditional and Insufficient Credit

For Borrowers without a credit score, the Mortgagee must either:

- Obtain a Non-Traditional Mortgage Credit Report (NTMCR); or
- Independently develop the Borrower's credit history.
 - Non-traditional and alternative credit may not be used to off-set or overcome derogatory credit.

Independent Verification of Non-Traditional Credit Providers

- Mortgagees may independently verify the Borrower's non-traditional credit providers.
- The Mortgagee **must** verify through public records:
 - The existence of each credit provider;
 - A published address or telephone number for the credit provider;
and
- Obtain the most recent 12 months cancelled checks or equivalent proof of payment.

Non-Tradition Mortgage Credit Report

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

- Creditor’s name;
- Date of opening;
- High credit;
- Current status of the account;
- 12-month history of the account;
- Required monthly payment;
- Unpaid balance; and
- Payment history in the delinquency categories (for example, 0x30 and 0x60).

Sufficiency of Credit References

To be sufficient to establish the Borrower's credit, the credit history **must** include **three credit references**, including at **least one** or more from the list below:

- Rental housing payments;
- Telephone service (cellphone is acceptable); and
- Utilities (not included in rent)
 - Gas; Electric; Water; Television service; and
 - Internet.

Sufficiency of Credit References (cont.)

Two credit references can be used from list provided below:

- Insurance premiums not payroll deducted;
- Payment to child-care providers (business);
- School tuition;
- Retail store credit cards;
- Rent-to-own;
- Patient obligation for medical bills;
- Savings history for 12 month evidence by regular deposits--not payroll deducte--resulting in an increased balance to the account that were made at least quarterly without insufficient funds (NSF) reflecting for checking;
- Automobile lease; or
- Personal loan from an individual with repayment terms in writing and payments made supported by cancelled checks

Sufficiency of Credit References: Authorized User Accounts

The Mortgagee may use Borrower Authorized User Accounts as a credit reference. The Mortgagee must obtain documentation to evidence that the Borrower:

- Has been making regular on-time payments during the previous 12 months;
- Does not have a history of delinquent payments on the loan;
and
- The debt payment is be included in a Borrower's debt-to-income (DTI) ratio.

Evaluating Credit History

- The underwriter must examine the borrower's overall pattern of credit behavior, not just isolated unsatisfactory or slow payments, to determine the Borrower's creditworthiness.
- The underwriter must evaluate the Borrower's payment histories in the following order:
 - Previous housing expenses and related expenses, including utilities;
 - Installment debts; and
 - Revolving accounts.

Satisfactory Credit

Under the following circumstances, the underwriter may consider a Borrower to have an acceptable payment history:

	0-12 months	12-24 months
Housing and Installment	0x30 days or more	2x30 days; 0x60 days or more
Revolving	2x60 days; 0x90 days	-

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

Payment History on Housing Obligation

- The Mortgagee must determine the Borrower's Housing payment history through:
 - The credit report;
 - Verification of rent received directly from the landlord;*
 - Verification of Mortgage or;**
 - A review of canceled checks – most recent 12 months.
- Borrower's living rent-free must be verified by the property owner that the borrower is living rent-free and for how long.
- Modified mortgage must utilize the payment history in accordance with the modification agreement for the time period of modification.

Collection Accounts

- The Mortgagee must determine if Collection accounts were a result of:
 - The Borrower’s disregard for financial obligations;
 - The Borrower’s inability to manage debt; or
 - Extenuating circumstances.
- The Mortgagee must document reasons for approving a Mortgage when the Borrower has any Collection accounts.
- The Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account.

Charge Off Accounts

- The Mortgagee must determine if Charge Off accounts were a result of:
 - the Borrower’s disregard for financial obligations;
 - the Borrower’s inability to manage debt; or
 - extenuating circumstances.
- The Mortgagee must document reasons for approving a Mortgage when the Borrower has any Charge Off accounts.
- The Borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account.

Disputed Derogatory Credit Accounts

Definition

Disputed Derogatory Credit Accounts refer to:

- Disputed Charge Off Accounts;
- Disputed Collection Accounts; or
- Disputed accounts with Late Payments in the last 24 months.

Disputed Derogatory Credit Accounts (cont.)

Standard

- The Mortgagee must analyze the documentation provided for consistency with other credit information to determine if the derogatory credit account should be considered in the underwriting analysis.
- The following items may be excluded from consideration in the underwriting analysis:
 - Disputed medical accounts; and
 - Disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use provide the Mortgagee includes a copy of the police report or other documentation from the creditor to support the status of the account.

Disputed Derogatory Credit Accounts (cont.)

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

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

Chapter 13 Bankruptcy: Pay-out Period

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

The Mortgagee must determine that during this time:

- The Borrower's payment performance has been satisfactory; all required payments have been made on time; **and**
- The Borrower has received written permission from bankruptcy court to enter into the mortgage transaction.

Refinance Transactions



Adjusted Value

- For properties acquired by the Borrower within 12 months of the case number assignment date, the Adjusted Value is the lesser of:
 - The Borrower’s purchase price, plus any documented improvements made after the purchase; or
 - The Property Value.
- For properties acquired by the Borrower within 12 months of application by inheritance or through a gift from a family member may utilize:
 - The Adjusted Value

Maximum Loan-to-Value Ratio

Maximum LTV	Maximum CLTV	Principal/Secondary Residence	Occupancy since Acquisition	Occupancy @ Case Number Assignment
97.75%	97.75%	Principal	Owner for minimum 12 months	Acquired within 12 months
85%	97.75%	Principal	Owner for less than 12 months	Occupies as Principal Residence fewer than 12 months or if owned less than 12 months, has not occupied the property for that entire period of ownership
85%	97.75%	Secondary*		

*for all HUD-approved Secondary Residences



Maximum Loan-to-Value Ratio Simple Refinance

Maximum LTV	Maximum CLTV	Principal/Secondary Residence
97.75%	97.75%	Principal Residence
97.75%	97.75%	Principal Residence
85%	85%	Required for all HUD-approved Secondary Residences



Documenting Occupancy

Required Documentation

The Mortgagee must review the Borrower's employment documentation or obtain utility bills to evidence the Borrower has occupied the subject Property as their Principal Residence for the 12 months prior to case number assignment.



Payment History Requirements: Streamline Refinance

Non-Credit Qualifying

- The Borrower **must** have made all Mortgage Payments for all Mortgages on the subject Property within the month due for the six months prior to case number assignment and have no more than one 30-Day late payment for the previous six months for all Mortgages on the subject Property.
- The Borrower **must** have made the payments for all Mortgages secured by the subject Property within the month due for the month prior to mortgage Disbursement.

Payment History Requirements: Streamline Refinance

Credit Qualifying

- The Borrower **must** have made all Mortgage Payments for all Mortgages on the subject Property within the month due for the six months prior to case number assignment.
- The Borrower **must** have made the payments for all Mortgages secured by the subject Property within the month due for the month prior to mortgage Disbursement. For all Mortgages on all other Properties, the Borrower **must** have no more than one 30-Day late payment for the previous six months.

Net Tangible Benefit: Streamline Refinance

From	To Fixed Rate	To One-Year ARM	To Hybrid ARM
	New Combined Rate	New Combined Rate	New Combined Rate
Fixed Rate	At least 0.5 percentage points below the prior Combined Rate.	At least 2 percentage points below the prior Combined Rate	At least 2 percentage points below the prior Combined Rate
Any ARM With Less than 15 Months to Next Payment Change Date	No more than 2 percentage points above the prior Combined Rate	At least 1 percentage point below the prior Combined Rate	At least 1 percentage point below the prior Combined Rate
Any ARM With Greater Than or Equal to 15 Months to Next Payment Change Date	No more than 2 percentage points above the prior Combined Rate.	At least 2 percentage points below the prior Combined Rate	At least 1 percentage point below the prior Combined Rate

If the mortgage term is reduced, the new interest rate does not exceed the current interest rate and the payment does not increase by more than \$50. This alone meets the test.



Net Tangible Benefit: Streamline Refinance

Standard for Refinances with a Term Reduction

The Mortgagee must determine that there is a net tangible benefit to the Borrower meeting the standards in the chart that follows for all Streamline Refinance transaction with a reduction in term.

Additionally, the combined principal, interest, and MIP payment of the new Mortgage must not exceed the combined principal, interest, and MIP payment of the refinance Mortgage by more than \$50.



Net Tangible Benefit: Streamline Refinance

Standard for Refinances with a Term Reduction

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



Cash Out: Qualifying

Income from a non-occupant co-Borrower may not be used to qualify for a cash-out refinance.



Cash Out: Occupancy Requirements

- Cash-out refinance transactions are only permitted on owner-occupied Principal Residences.
- The property securing the cash-out refinance must have been owned and occupied by the Borrower as their Principal Residence for the 12 months prior to the date of case number assignment.

Cash Out: Occupancy Requirements Documentation

The Mortgagee **must** review the Borrower's employment documentation or obtain utility bills to evidence the Borrower has occupied the subject property as their Principal Residence for the 12 months prior to case number assignment.

Cash Out: Occupancy Requirements Exception

Inheritance: A Borrower is not required to occupy the property for a minimum period of time before applying for a cash-out refinance, provided the Borrower has not treated the subject property as an Investment Property at any point since inheritance of the property:

- If the Borrower rents the property following inheritance, the Borrower is not eligible for cash-out refinance until the Borrower has occupied the property as a Principal Residence for at least 12 months.

Cash Out: Payment History

The Mortgagee must document that the Borrower:

- Has made all payments for all their mortgages within the month due for the previous 12 months or since the Borrower obtained the mortgages, whichever is less.
- The payments for all mortgages secured by the subject property must have been paid within the month due for the month prior to mortgage Disbursement.
- Properties with mortgages must have a minimum of six months of Mortgage Payments.
- Properties owned free and clear may be refinanced as cash-out transactions.

Final Underwriting Decision



Final Underwriting Decision (TOTAL)

The Mortgagee may approve the mortgage as eligible for FHA insurance endorsement if:

- TOTAL rated the mortgage application as Accept;
- The Mortgagee reviewed the TOTAL Mortgage Scorecard findings and verified that all information entered into TOTAL Mortgage Scorecard is consistent with mortgage documentation, and is true, complete, and accurate;
- The mortgage meets all FHA requirements applicable to mortgages receiving a rating of Accept from TOTAL Mortgage Scorecard;
- A Direct Endorsement (DE) underwriter underwrote the appraisal according to standard FHA requirements; **and**
- A DE underwriter approved the property as acceptable for FHA single family insurability.

Final Underwriting Decision (Manual)

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

Duty of Care/Due Diligence

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

Endorsement



Common Missing Documents

- HUD 92800.5b
- Closing Disclosure
- 1004D Completion Cert
- HUD 92900-LT Addendums
- Flood Cert and/or Insurance
- Acceptable Evidence of Occupancy
- Secondary Financing Documents
- Engineer's Certification
- New Construction Documents
- Loan Estimate
- Settlement Certification
- Gift Letter Documentation
- Chain of Title
- Complete Bank Statements-All Pages
- 203k Documents
- Condo Cert for Individual Unit Financing

Last, but not least, a contact sheet on top of the right or left side of the binder listing the name, phone number and/or email of someone we can contact for a limited number of missing documents to avoid sending the case binder back to you.



FHA Catalyst

Mortgagee Letter 2020-07 announced the implementation of FHA Catalyst, a new web-based platform, in response to the National Emergency declaration due to the COVID-19 outbreak.

This declaration, while in the interest of public health, hampered the ability of Mortgagees to fully comply with FHA requirements for delivery of Single Family Forward and HECM paper case binders.

In response, FHA accelerated the deployment of a system to securely deliver case binders electronically for endorsement.

Who uses FHA Catalyst?

- Non-Lender Insurance (non-LI) Mortgagees may use the system for initial submission and to re-submit binders which have been rejected by a Notice of Reject (NOR).
- Lender Insurance (LI) Mortgagees, not approved for electronic Case Binder (eCB) submission, may use the system for submission of case binders to address Severe Case Warnings.
- Lenders currently in the Test Case process may also use the system to submit their Case Binder for review.

How to submit a binder to FHA Catalyst

- Non-LI Mortgagees must comply with current guidance found in Handbook 4000.0 II.A.7.d.iii Case Binder Submission-Direct Endorsement Non-Lender Insurance.
- LI Mortgagees must comply with current guidance found in Handbook 4000.1 II.A.7.d.vi Case Warnings-Lender Insurance (LI).
- Test Case Lenders must comply with current guidance found in Handbook 4000.1 I.A.5.a.iii. (A)(3) Test Case Phase and II.A.7.d.vii, Mortgagees with Conditional Direct Endorsement Approval (Test Case).

Late Submission

If the Mortgage is submitted for endorsement more than 60 Days after the Disbursement Date, the Mortgagee must complete a late endorsement certification stating:

- No Mortgage Payment is currently unpaid;
- All escrow accounts for taxes, hazard insurance and MIPs are current and intact, except for Disbursements that may have been made to cover payments for which the accounts were specifically established; and
- Neither the Mortgagee nor its agents provided the funds to bring and/or keep the Mortgage current or to bring about the appearance of an acceptable payment history.

Late Submission (cont.)

Each late endorsement certification must:

- List the FHA case number;
- List the Borrower's name;
- Be dated and signed by the Mortgagee's representative; and
- Be printed on company letterhead with the Mortgagee's address and telephone number.



Inspections-PDMDA Presidentially Declared Major Disaster Areas

All Properties with pending Mortgages or endorsements in a Presidentially-Declared Major Disaster Areas (PDMDA) designated for individual assistance must have a damage inspection report that identifies and quantifies any dwelling damage. The damage inspection report must be completed by an FHA Roster Appraiser even if the inspection shows no damage to the Property, and the report must be dated after the Incident Period (as defined by FEMA) or 14 Days from the Incident Period start date, whichever is earlier. If the effective date of the appraisal is on or after the date required above for an inspection, a separate damage inspection report is not necessary.



Case Warnings

- Case warnings are issued by FHAC system edits.
- They identify issues that must be addressed before the Mortgage can be insured.
- There are two kinds of case warnings:
 1. Non-Severe
 2. Severe

Case Warnings: Non-Severe

Non-Severe case warnings:

- Non-severe case warnings are warnings to provide guidance to the Mortgagee that conditions have been detected and must be researched before the Mortgage can be endorsed.
- If, after researching the matter, the Mortgagee determines that HUD requirements have not been violated, the Mortgagee may re-submit the Mortgage for insurance.
- By re-submitting the mortgage, the Mortgagee is representing that the warning has been reviewed and the Mortgage is eligible for insurance endorsement. FHAC will then allow the Mortgage to be insured by the Mortgagee.

Case Warnings: Non-Severe (cont.)

Common examples of non-severe warnings include:

- Mortgage Credit Reject related to Subject Case Number;
- Credit Alert Sanction related to borrower's social security number; and
- Multiple Loans related to borrower's social security number.

Case Warnings: Non-Severe (cont.)

Excessive Mortgage Amount:

- An excessive mortgage amount occurs when the Mortgagee closes a Mortgage in an amount higher than what is permitted by FHA requirements. The Mortgage is not eligible for insurance until the amount is reduced to within permissible limits.

The Mortgagee may choose to either:

- Pay down the principal balance, or
- Re-close the Mortgage to an insurable amount.

Case Warnings: Non-Severe (cont.)

“Loan Rescored as Refer. Manual Underwriting Required”

FHAC insuring screen and TOTAL (AUS) input do not match including, but not limited to:

- Name;
- Address;
- Required investment amount;
- Gift is missing or amounts are discrepant; and
- Verified assets are less than required funds.

Case Warnings: Non-Severe (cont.)

Prior to submitting or re-submitting for insuring, the Mortgagee **MUST RECONCILE AND RESOLVE ALL DISCREPANCIES.**

Case binder must support and document all resolutions.

Case Warnings: Severe

Severe case warnings make the Mortgage ineligible for Lender Insurance (LI).



Case Warnings: Severe (cont.)

Severe Case Warning Examples (LI Cases Only):

- Borrower failed or is pending SSN validation
 - Name and/or birth date do not match SSA records
- Borrower has a record in CAIVRS
- Pre-Endorsement delinquency status
- Deficiency exists causing unacceptable risk to HUD-Loan has a known uncorrectable violation including but not limited to:
 - Owner-occupancy;
 - Non-permanent resident alien whose income is required to qualify and lacks an Employment Authorization Document (EAD); and
 - Eligibility requirements for a 2nd FHA-insured mortgage are not met.

What is a Notice of Return (NOR) and Where Can I View an NOR?

- Notice of Return (NOR) refers to a notification to the Mortgagee specifying the reason a Mortgage is not currently eligible for endorsement. These reasons may include but are not limited to:
 - Late submission without a late endorsement certification;
 - Missing documentation;
 - FHAC input errors; and/or
 - Unresolved policy issues.
- The NOR can be viewed in the FHA Connection Case Processing Notice of Return screen.

After Receipt of a Notice of Return

If the Jurisdictional HOC issues a NOR, the Mortgagee may request reconsideration for insurance endorsement. All requests for reconsideration must be received by the Jurisdictional HOC within the 60-Day endorsement submission period or within 30 Days of the issuance of the NOR, whichever is longer. If the request for reconsideration is submitted after this time period, the Mortgagee must follow the guidelines for late submission.

Mortgagees submitting paper case binders must submit the original case binder with any request for reconsideration. *



Ineligible for Endorsement

- If the Mortgage is not eligible for endorsement, FHAC issues an electronic NOR which states the deficiencies and any corrective actions that the Mortgagee must take.
- If the Mortgage is permanently rejected for insurance endorsement, the Mortgagee **must notify the Borrower** that they do not have an FHA-insured mortgage and of the circumstances that made the mortgage ineligible for FHA insurance.

Ineligible for Endorsement (cont.)

Additional Requirements of Permanently Rejected Mortgages

The Mortgagee must obtain a refund of both the UFMIP and any periodic MIP paid by or on behalf of the Borrower and apply the refund to the principal balance of the Mortgage.

[Lenders Refunds@hud.gov](mailto:LendersRefunds@hud.gov)



Endorsement

Upon successful completion of a pre-endorsement review, either by FHA or the Lender Insurance (LI) Mortgagee, the electronic Mortgage Insurance Certificate will be issued.



Post Endorsement

- **Confirming Status of the Mortgage Insurance Certificate (MIC)**-The Mortgage can confirm the endorsement status of a Mortgage using the FHAC or FHA Connection Business to Government application.
- **Obtaining the Mortgage Insurance Certificate**-When requesting the MIC, the Mortgagee must specify whether it is to be prepared in the name of the originator (principal), or authorized agent, as it appears in HUD Systems. The MIC will be issued electronically. The Mortgagee can download and print copies of the MIC as needed.

Post Endorsement (cont.)

- **Corrections to the Mortgage Insurance Certificate-** To obtain a correction to the MIC, the Mortgagee must submit the MIC Correction Request Template to the FHA Resource Center. This form may be used to correct the property address, Borrower name, ADP Code, maturity and first payments dates, P&I, interest rate, SSN, FHA case number, mortgage amount or other information contained in the MIC, or to add a co-Borrower.
- **Corrections to Original Instruments-** The Mortgagee must follow applicable local law when making corrections to the original instruments. If new instruments are executed as required by local law, the Mortgagee must submit the new instruments prior to insurance endorsement.

Endorsement Deficiencies

When submitting the case binder to the jurisdictional HOC, please include contact information for the Endorsement Department:

- Name
- Phone Number
- E-Mail Address



Helpful Links

- SF Handbook Information:

https://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/handbook_4000-1

- Upcoming Single Family Housing Events and Training :

https://www.hud.gov/program_offices/housing/sfh/events

- Subscribe to FHA INFO:

https://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/FHA_INFO_subscribe



FHA Resource Center

	Option	Point of Contact	Hours Available	Comments
1	FHA Knowledge Base – FAQs	www.hud.gov/answers	24/7/365	Knowledge Base web page includes option to email questions.
2	Email	answers@hud.gov	24/7/365	
3	Telephone	1-800-CALL-FHA (1-800-225-5342) Persons with hearing or speech impairments may reach this number by calling the Federal Relay Service at 1-800-877-8339.	8:00 AM to 8:00 PM Eastern M-F	Voicemail is available after hours or during extended wait periods.

FHA INFO emails: Frequent email notifications of new policies and training opportunities for anyone who signs up. Subscribe at: https://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/FHA_INFO_subscribe



Thank You!

For joining us today

