MEGA CAPITAL FUNDING, INC.

SILVER JUMBO

- **PRIMARY RESIDENCE**

Primary Residence: 1-2 Unit, including PUDs, Condos						
Transaction Type	**Max Loan Amt**	**LTV/CLTV/HCLTV**	**FICO**	**Max Cash-Out**	**Max DTI**	**Reserves**
Purchase & Rate Term Refinance	$1,000,000	80% / 80% / 80%	720	NA	43%	12
	$2,000,000	75% / 75% / 75%	720		41%	18
	$3,000,000	70% / 70% / 70%	760		41%	24
		75% / 75% / 75%				36
Cash-Out Refinance	$1,000,000	70% / 70% / 70%	740	$350,000	43%	18
	$1,500,000	65% / 65% / 65%				

Primary Residence: 3-4 Unit, including PUDs						
Transaction Type	**Max Loan Amt**	**LTV/CLTV/HCLTV**	**FICO**	**Max Cash-Out**	**Max DTI**	**Reserves**
Purchase & Rate Term Refinance	$2,000,000	70% / 70% /70%	720	NA	43%	18
	$3,000,000	65% / 65% / 65%	760		41%	36
Cash-Out Refinance	NOT ALLOWED					

- The minimum loan amount is $1 over agency conforming loans size, including properties in high-cost areas. No AUS is required.
- Loans must meet Continuity of Obligation.
- The above maximum LTV/CLTV/HCLTV should be reduced by 5% if the subject property is located in a depreciating market by the appraisal report and MCFI's Depreciating Markets List (Exhibit 1).

- **SECOND HOME**

Second Home: 1-unit, including PUDs, Condos						
Transaction Type	**Max Loan Amt**	**LTV/CLTV/HCLTV**	**FICO**	**Max Cash-Out**	**Max DTI**	**Reserves**
Purchase & Rate Term Refinance	$1,500,000	70% / 70% / 70%	740	NA	43%	18
Cash-Out Refinance	NOT ALLOWED					

*PUDs are only allowed on 1-unit properties.

- The minimum loan amount is $1 over agency conforming loans size, including properties in high-cost areas. No AUS is required.
- Loans must meet the Continuity of Obligation policy.

- The above maximum LTV/CLTV/HCLTV should be reduced by 5% if the subject property is located in a depreciating market by the appraisal report and MCFI's Depreciating Markets List (Exhibit 1).

Second Home: 2-4 Units, including PUDs—Not Permitted

- **INVESTMENT PROPERTIES**

Investment Property: 1-Unit, including Condos* and PUDs**						
Transaction Type	**Max Loan Amt**	**LTV/CLTV/HCLTV**	**FICO**	**Max Cash-Out**	**Max DTI**	**Reserves**
Purchase & Rate Term Refinance	$1,500,000	65% / 65% / 65%	760	NA	40%	36
Cash-Out Refinance	NOT ALLOWED					

*Florida and Georgia Condominiums secured as investment property are not permitted.
**PUDs are only allowed on 1-unit properties.

- The minimum loan amount is $1 over agency conforming loans size, including properties in high-cost areas. No AUS is required.
- Loans must meet the Continuity of Obligation policy.
- The above maximum LTV/CLTV/HCLTV should be reduced by 5% if the subject property is located in a depreciating market by the appraisal report and MCFI's Depreciating Markets List (Exhibit 1).

Investment Property: Co-op and 2-4 Unit, including PUDs – NOT PERMITTED

FIXED RATE

Product provides for a fixed interest rate for the life of the loan. Loans may only be originated in first lien position.

Product

Product	Term
15-Year	15 years
30-Year	30 years

All loans must be in 12-month increments; they may not have an odd number of months.

Only loans that meet QM Safe Harbor requirements are eligible.

Loan Plans:

- 15 yr FRM Non-Agency
- >15yr FRM Non-Agency

Note: Plan Codes are combination of the individual product and program

Note Rate Limitations

Not Applicable

Qualifying Rate

Occupancy	Qualifying Rate
Primary Residence	Note Rate
Second Home	Note Rate
Investment Property	Note Rate

No AUS required

Adjustment Caps & Margin
Not Applicable

Assumable
Not Permitted

Convertible
Not Permitted

Buy Downs
Temporary buy downs not permitted.

Prepayment Feature
Not Available

Mortgage Insurance
Not Required

Eligible Loan Purpose/ Transaction Types

- Purchase
- Rate/Term Refinance
- Cash-Out Refinance

Property Type

- 1-Unit, including condominiums, PUDs
- 2-4 Unit

Manufactured homes are not permitted.

Occupancy/ Property Usage

- Primary Residence
- Second Home
- Investment Property

Loan Amount

Minimum: Must be at least $1 over the conforming loan sizes listed below.

Units	Contiguous States and District of Columbia	Alaska and Hawaii
One	$766,550	$1,149,825
Two	$981,500	$1,472,250
Three	$1,186,350	$1,779,525
Four	$1,474,400	$2,211,600

Maximum: As per LTV matrix in 1st page.

SOFR ARM

The Secured Overnight Financing Rate (SOFR) is based on actual transactions in the Treasury repurchase (repo) market, one of the largest markets in the world. This is the market where investors offer borrowers overnight loans backed by their U.S. Treasury bond assets.

Note The index used for the 3yr/6m, 5yr/6m, 7yr/6m & 10yr/6m SOFR products is the 30-day average of the SOFR index as published by the Federal Reserve Bank of New York.

Variable rate mortgage product—without negative amortization—whereby the interest rate and payment is adjusted in accordance with a specified index as agreed to at inception.

- 5 Year (5yr/6m), 7 Year (7yr/6m), & 10 Year (10yr/6m): A fixed-to-adjustable-rate product that provides for an initial fixed rate period based on the product selected with a variable interest rate and payment adjustments every 6 months thereafter.

Loans may only be originated in first lien position.

Note: The above products will be abbreviated as 5yr/6m, 7yr/6m & 10yr/6m SOFR ARMs throughout the MPM to simplify listing.

Product

Product	Term	Initial Fixed Rate Period
5 Year (5yr/6m) SOFR	30 years	60 Months
7 Year (7yr/6m) SOFR	30 years	84 Months
10 Year (10yr/6m) SOFR	30 years	120 Months

All loans must be in 12-month increments; they may not have an odd number of months.

Only loans that meet QM Safe Harbor requirements are eligible.

Loan Plans:

- 5 Year (5yr/6m) SOFR ARM Non-Agency
- 7 Year (7yr/6m) SOFR ARM Non-Agency
- 10 Year (10yr/6m) SOFR ARM Non-Agency

Note: Loan Plans are combination of the individual product and program.

Note Rate Limitations

- 5yr/6m SOFR: Note rates may not be lower than 3% below the Fully Indexed Rate (FIR).
- 7yr/6m & 10yr/6m SOFR: Note rates may not be lower than 3% below the Fully Indexed Rate (FIR).

Qualifying Rate

Product	Qualifying Rate
5yr/6m SOFR	Higher of Note Rate + 2% or the FIR*
7yr/6m SOFR	Higher of Note Rate or FIR*
10yr/6m SOFR	Higher of Note Rate or FIR*

*Fully Indexed Rate (FIR)

Adjustment Caps & Margin

	Initial	Sub	Life	Margin
5yr/6m SOFR	2%	1%	5%	2.75%
7yr/6m SOFR	5%	1%	5%	2.75%
10yr/6m SOFR	5%	1%	5%	2.75%

The floor rate is the margin

Assumable

	Y/N	When
5yr/6m SOFR	Yes	Following fixed period
7yr/6m SOFR	Yes	Following fixed period
10yr/6m SOFR	Yes	Following fixed period

Note: Non-assumable ARMs are not available

Convertible
Not Permitted

Buy Downs
Temporary buy downs not permitted.

Prepayment Feature
Not Available

Mortgage Insurance
Not Required

Eligible Loan Purpose/ Transaction Types

- Purchase
- Rate/Term Refinance
- Cash-Out Refinance

Property Type

- 1-Unit, including condominiums, PUDs
- 2-4 Unit

Manufactured homes are not permitted.

Occupancy/ Property Usage

- Primary Residence
- Second Home
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Loan Amount

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Maximum: As per LTV matrix in 1st page.

PROGRAM SPECIFIC APPLICABILITIES AND REQUIREMENTS

Credit report	• MCFI will pull Credco credit report if a broker's credit report submitted is not on approved credit vendors list. • Broker credit report is allowed if within 60 days from submission date. Credit Reports are good up to 90 days at time of CTC
Ineligible Transactions & Scenarios	*All Deed Restricted Properties, including Age Only *Delayed Financing *Higher Priced Mortgage Loans *Industrial, Commercial or Agricultural Zoned Properties *Income sources listed in Section Employment and Income/Introduction/Ineligible Sources of Income topic *Mixed Use Properties *Non-Arm's Length Transactions *Non-occupant Co-borrowers *Non-resident Applicants *Partial Release *Technical Refinance *Texas Cash-Out *Texas Section 50(a)(6) *Texas Section 50(f)(2) *Work Completion Escrow
Borrower Eligibility	**U.S. Citizens **Permanent resident borrowers: A copy of the Permanent Resident card (front and back) must be provided. ** Non-Permanent Resident Applicants: Allowed **Non-Resident Aliens: Not permitted.
Non-Borrowing Spouse	When a married applicant applies for a mortgage in their name alone, without involving the applicant's spouse, the spouse is referred to as a non-borrower spouse. A non-borrower spouse may have rights in the property, either as a co-owner of the property or because state community property or marital rights laws. MCFI's lien must always be superior to that of the non-borrower spouse. • If the non-borrower spouse is to be listed on the title as a co-owner, MCFI requires the non-borrower spouse to sign the security instrument—in all states. Note: We cannot require a non-borrower spouse who is a co-owner of the property to sign a quitclaim deed. • If the non-borrower spouse is not listed on the title, MCFI does not require the non-borrower spouse's signature on the Security Instrument, unless it is necessary under state law to obtain a valid security interest.

INCOME	

Wage Earner Income Documentation	**REGULAR INCOME**
	• Most recent YTD paystub or salary voucher documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained.
	
	• W-2: W-2s for the most recent 2 years regardless of how long the borrower has been on their current job. An IRS Wage and Income Transcript (W-2 transcripts) may be used in lieu of the actual W-2 forms. Note: Income used to qualify must have a history of receipt and be expected to continue. A calculation worksheet must be documented in the loan file to show how the income being used to qualify was calculated.
	
	• If either the borrower or co-borrower is self-employed, in addition to the required wage earner income documentation, complete tax returns for the most recent 2 years must be provided even if the income is not being used to qualify. The personal tax returns must be reviewed to determine if there is a "meaningful" business loss that may have an impact on the stable monthly income being used to qualify. Additional documentation may be needed to fully evaluate the impact of the business loss on the borrower's ability to repay.
	
	Future Income
	If the borrower is scheduled to begin employment after the loan closes, their Future Income may be considered as qualifying income following the guidelines below.
	Examples of this type of scenario are teachers whose contracts begin with the new school year, physicians beginning a residency or an employee relocating for a new job.
	Future income is limited to loans that meet the following criteria:
	• Purchase transaction
	• Primary residence or 2nd home occupancy
	• The borrower is not employed by a family member or by an interested party to the transaction.
	• Borrowers must document a minimum 2 year work / student history.
	• Start date of employment must be within 90 days of the note date.
	
	The following documentation must be obtained:
	• An offer letter or contract for future employment that meets all of the following:
	    o Clearly identifies the employer and the borrower, is signed by the employer, and is accepted and signed by the borrower
	    o Clearly identifies the terms of employment, including position, type and rate of pay, and borrower's start date
	    o Is non-contingent. Note: If conditions of employment exist, all conditions of employment must be satisfied either by verbal verification or written documentation prior to closing. This confirmation must be documented in the mortgage loan file.

	• In addition to the funds required for the transaction, the borrower must have verified sufficient reserves to cover all monthly liabilities (the subject PITIA payment and all monthly liabilities included in the DTI) for 3 months. **Note**: A verbal verification is not required as the borrower will begin employment after closing **<u>Employment Stability</u>** A 2-year employment history must be reflected on the application. The purpose of reviewing employment history is to assure that the borrower has a history of receiving stable income from employment (and other sources) and that there is reasonable expectation that the income will continue to be received in the foreseeable future. If documentation indicates that the income will end within the next 3 years the income should not be used to qualify. • **Frequent Job Changes** Frequent employment changes within the same line of work while continuing to advance in income or benefits is acceptable. Income stability takes precedence over job stability. However, there may be occasions that warrant a closer examination of employment and income. Example: Frequent changes in employment for reasons other than advancement (e.g., changing careers) or extended periods of unemployment may be indicative of an unsteady work history and income. o Borrowers with questionable employment histories must have financial strengths in order to be considered for maximum financing. Negative comments received from an employer may or may not be reason to decline the application, but circumstances must be investigated thoroughly before doing so. o Borrowers who work in certain industries may experience frequent job changes due to the nature of the work (e.g., seasonal or unskilled labor). In these instances borrowers should not be penalized provided they have demonstrated the ability to maintain a steady income and the changes have not affected the borrower's ability to pay their obligations. Note: Often due to the nature of the work, LMI (Low to Moderate Income) borrowers may change jobs frequently and still be able to demonstrate the ability to earn consistent and predictable income. In these instances, emphasize the continuous flow of income. Borrowers who have held the same position during their entire tenure should not be penalized. However, their potential for future increases may need to be taken into consideration in determining the type of mortgage that best meets their needs. • **Re-entering the Workforce** A borrower's income may be considered effective and stable when recently returning to work after an extended absence if s/he: • Is employed in their current job for six months or longer; and • Can document a two-year work history prior to an absence from employment using: o Traditional employment verifications; and/or

	○ W-2s or paystubs. Note: An acceptable employment situation includes individuals who took some time off from employment to raise children, then returned to the workforce. Situations not meeting the criteria listed above may not be used in qualifying. Extended absence is defined as six months. • **Newly Employed** Borrowers who are newly employed and have an employment and income history that covers less than the 2 most recent years may be eligible for a mortgage loan as long as the borrower was attending school, in a training program related to the new position, or in the military immediately prior to their current employment. Supporting evidence such as College transcripts or discharge papers are required to verify. Note: When the borrower has less than a two-year history of receiving income, the underwriter must also provide a written analysis to justify the determination that the income used to qualify the borrower is stable. **<u>EVALUATING WAGE INCOME</u>** Wage earner income is best defined as compensation for services paid by a person, business or organization at specified intervals and is commonly referred to as salary or wage earner income. The pay schedules of wage earners can be classified into 4 general categories. • Full Time: The borrower is a permanent employee of a company and works a standard workweek, usually totalling 35 to 40 hours a week. Hours and number of days may or may not vary. • Part Time: The borrower is a permanent employee of a company, but the number of hours is not standardized, usually totalling less than 30 hours a week. • Temporary: The borrower is not a permanent employee of the company and therefore is not part of the company's permanent staff. Temporary employees usually work for a contracted, or "as needed" period of time only. • Occasional/Seasonal: The borrower works for a specified period of time on a specific job or project. Once completed, the borrower is on "standby" until they receive their next assignment. Examples of this type of worker include roofers, landscapers, union construction workers, and migrant farm workers. The type of pay schedule directly impacts how monthly qualifying income is calculated. Common types of stable wage earner income may include regular base earnings plus consistent and documented secondary income, such as overtime, commission, and bonus, and additional part-time or seasonal employment. **<u>BONUS INCOME</u>** A bonus is money paid in addition to regular wages. Sometimes bonuses are paid on a regular basis throughout the year. Some employees also receive a guaranteed bonus—a promise or contract made by the employer as part of an incentive plan paid regardless of the company's profitability or the employee's performance. The nature of the bonus must be determined up front in order to include in qualifying income. The borrower must have a 2-year history of receipt to use as qualifying income and it must be likely to continue for the next three years. Earnings

	must be level or increasing; compensating factors must exist if decreases in the last year. **<u>Required Documentation</u>**: • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; **and** • 2 years most recent W-2s and/or 1099s; **and** • There is no evidence from the employer that the income will no longer be received; and • It is determined that the income is likely to continue based on an established earnings trend. o If the trend is stable or increasing, income can be averaged over the two-year period. o If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used. o If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline. **and** • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing. **<u>COMMISSION INCOME</u>** Commission income is a fee or percentage paid to the employee for performing a service or is based on the dollar amount of the goods and/or the number of units a person sells. Some borrowers are paid a salary plus commission while others receive only commission pay. The borrower must have a two-year consecutive history of receiving commission income and the commission income must be likely to continue for the next three years in order to use the income to qualify. Income may be subject to fluctuations from year-to-year. If there are large fluctuations, the borrower must provide a written explanation to support the increase or decrease in income and the appropriate adjustments made to average income used to qualify. All letters of explanation must be signed by the Borrower prior to close. **<u>Required Documentation</u>** • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and • 2 years most recent W-2s; and • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing. **Note**: If the file contains tax returns or tax transcripts they cannot be ignored. **<u>Employees of a School District</u>** Employees of a school district may be paid on a 9-month, 10-month, or 12-month basis. As such, a current year-to-date pay stub dated within 30 days of application may not be available. Income structure must be determined

	before calculating qualifying income. Although every effort should be made to obtain a copy of the borrower's most recent pay stub, if the borrower is on a pay schedule of less than 12 months, a copy of their employment contract with the school district may be used in lieu of a current pay stub or it may be verbally verified directly with the school district HR department (conversation must be documented in the file). Contract must be valid and non-expired. Note: Requirements to verify income remain as noted below. Required Documentation: • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained, or a copy of the Employment contract with the School District; and • 2 years most recent W-2s; and • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing. **<u>Individual Employed by an Interested Party in the Transaction</u>** Tax returns must be obtained even if the borrower does not meet the definition of self-employed. However, they do not have to be treated or registered as a self-employed borrower. • Carefully examine loans with borrowers who are employed by interested parties to the property sale, purchase or financing of the transaction. • Borrowers who are employed by an interested party in the transaction must also provide 2-years tax returns, regardless of the percentage of ownership or type of income. **Required Documentation:** • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and • 2 years most recent personal tax returns with all W-2s; and • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing. **<u>Individual Employed in a Family-Owned Business</u>** Tax returns must be obtained even if the borrower does not meet the definition of self-employed. However, they do not have to be treated or registered as a self-employed borrower unless they have 25% or more ownership in the business. • Carefully examine loans with borrowers who are employed in a family-owned business, or whose employer is an interested party to the sale of the property. • Ownership in a family business must be established and verified, regardless of the percentage of ownership; therefore, the most recent 2-years tax returns are required. **Required Documentation:** • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the

paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and
- 2 years most recent personal tax returns and all W-2s; and
- Verbal Verification of Employment performed no more than 10 business days prior to the loan closing.

OVERTIME

Overtime is money paid to individuals who earn additional wages for time worked above and beyond the normal workday or workweek.
The borrower must have a 2-year history of receipt to use as qualifying income and it must be likely to continue for the next three years. Earnings must be level or increasing; compensating factors must exist if decreases in the last year.

Required Documentation:

- Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and
- 2 years most recent W-2s and/or 1099s; and
- There is no evidence from the employer that the income will no longer be received; and
- It is determined that the income is likely to continue based on an established earnings trend.
  - If the trend is stable or increasing, income can be averaged over the two-year period.
  - If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used.
  - If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline. and
- Verbal Verification of Employment performed no more than 10 business days prior to the loan closing.

PART TIME, SEASONAL & SECONDARY INCOME

Part-time, seasonal, or second-job income may be used to qualify if it can be verified as having been received for the previous 2-years and if it has a strong likelihood of continuation. This income is considered uninterrupted if the borrower has held the same position for at least 2-years and employment is expected to continue for the next 3 years. (For example, someone who works at a department store only during the Christmas season, or who works summers in an amusement park demonstrate a consistency that is likely to continue.) Income is averaged over 2 years.
For secondary income, it is acceptable for a borrower to have a history that includes different employers as long as the income has been consistently received. In no instance may the borrower have any gap in employment greater than one month in the most recent 12-month period unless the secondary employment is considered seasonal income. Occasionally, with extraordinary circumstances less than a 2-year history may be considered—but no less than 12-months—provided there is a strong likelihood income will continue. When the income used to qualify has less than a 2-year history the file must contain a written explanation and justification from the underwriter as to why the income was used to qualify.

	Required Documentation: • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and • 2 years most recent W-2s; and • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing **<u>TIPS & GRATUITIES</u>** Tips or gratuity income is compensation received in addition to the employee's straight salary or hourly wage. The borrower must have a 2-year history of receipt to use as qualifying income and it must be likely to continue for the next three years. Gratuities and tips can only be included in qualifying income if they are included in two years of taxable income. This income source is usually found on W-2s or 1040s. The income should be reported to the IRS. The employer must also indicate that the tip income will in all probability continue. **Required Documentation:** • Most recent YTD pay stub documenting at least 30 days of income. Paystub must be dated no earlier than 30 days prior to the application date and must include all year-to-date income. If the paystub does not include sufficient information to appropriately calculate income, additional documentation must be obtained; and • 2 years most recent tax returns with all W-2s; and **Note:** The borrower may report additional tip income to the IRS using Form 4137, Social Security and Medicare Tax on unreported tip income, when filing his/her tax returns. This income may be used in qualifying if the most recent two years federal income tax returns with Form 4137 are obtained. • Determine that the income is likely to continue based on an established earnings trend. o If the trend is stable or increasing, income can be averaged over the two-year period. o If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used. o If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline; And • Verbal Verification of Employment performed no more than 10 business days prior to the loan closing; and • For First Mortgage transactions, either verbal or written confirmation with borrower's employer that tip income is likely to continue. (Written VOE may be required. If confirmation cannot be obtained, the income may not be used to qualify.) **<u>Union Worker</u>** Union workers are members of a specific trade union and are often skilled tradesperson (e.g., electricians, plumbers, roofers, etc.). Workers can work for a single employer on a long-term basis or for more than one employer throughout the year. At the completion of a job, the Union will then refer the individual to a new employer. During the individuals' course of employment with the assigned employer, they are paid directly by the

	employer, not the Union. Their jobs may be seasonal, and it is not uncommon for individuals to receive unemployment during down time. If the borrower is in a line of work that is deemed seasonal (e.g., roofing) and is not working at the time of loan application or closing, they may still be eligible for financing. Verify that the borrower is a member of the union and in good standing. It is not necessary to verify the union dues or count them as a liability. If the borrower is a member of a local trade union and obtains employment via these means, income can be verified by the following: **Required Documentation:** • 2 years tax returns; or • 2 years of W-2s and/or 1099s, or • A VOE from the Union for earnings from all employers during the current year and a W-2 from prior year. If the union work is paid with a 1099 and have expenses that may be deducted from the income used to qualify, s/he should be treated as a self-employed borrower, averaging the income over a 2-year period. Note: This policy does not apply to borrowers who are employed by a traditional employer (e.g., GM, Ford, etc.), but rather are members of a trade union such as a carpenter's union. Borrowers who are employed by a traditional employer would be considered wage-earner employees. **<u>Variable Income</u>** Certain types of income fluctuate and must be averaged in order to arrive at income that is used to qualify. Examples of variable income sources include hourly workers with fluctuating hours, or income that includes commission, bonus or overtime. Typically two years or more of receipt of the variable income is recommended; however, a shorter time period of 12 to 24 months may be considered as acceptable. Refer to the requirements for each individual source of income for additional details. It is also important to establish an earnings trend. The earnings trend must be evaluated and the amount that is most likely to continue for the next 3 years must be used to qualify. A borrower who has had different types of employment in the past may be considered to have stable income if the amount has remained at a consistent level (at a minimum), and changes have not affected the borrower's ability to pay their obligations. The frequency of the payment (weekly, biweekly, monthly, quarterly, or annually) must be determined in order to accurately calculate the monthly income to be used. The monthly year to date income calculation should be compared to prior year's earnings using the borrower's W-2's or signed federal income tax returns, as determined by the documentation required under the source of income.
Self-Employed Income Documentation	• Individual: Complete tax returns for the most recent 2 years, including all W-2s and Schedules. • Corp. S-Corp. & Partnerships: The most recent 2 years' business tax returns including all Schedules. • Corp, S-Corp & Partnership: The YTD (year-to-date) P&L (profit and loss) and balance sheet are required when the application is dated more than

90 days after the end of the business' fiscal or calendar year end. YTD unaudited P&L statement and balance sheet for the business either:

- Completed by the business's tax preparer; or
- Completed by the borrower in addition to the following:
  - Evidence provided that the document has been viewed by the business's tax preparer, or
  - Evidence provided that the document has been viewed by an appropriate third party who is not affiliated with the loan transaction, or
  - Two months business bank statements to support the income on the P&L statement and balance sheet.
  - The year-to-date P&L and balance sheet are required when the application is dated more than 90 days after the end of the business' fiscal or calendar year end.

- Income Analysis Form
- Verification that borrower's business remains open and in existence performed no more than 10 calendar days prior to the loan closing.
- Note: Corporate income may not be used unless the borrower owns 100% of the business. (W-2 and 1099 earnings are eligible)

EVALUATING SELF-EMPLOYED INCOME

A self-Employed Income Analysis Form must be completed on every transaction and retained in the permanent loan file. Examples of this form include Freddie Mac Form 91 or Fannie Mae Form 1084.

An individual receiving income from any of the following sources must be qualified as self-employed:

- Borrower has an ownership interest of 25% or more in a business. The business may be a sole proprietorship, a general partnership, limited partnership, corporation, or S-corporation. Loans must be coded as self-employed
- Borrower relies on investments for income (e.g., interests, dividends, capital gains, or real estate).
- Borrower is a member of the clergy and files taxes as self-employed. (Additional guidelines apply if a portion of their income is for housing, which may be tax exempt—federal and state.
- Borrower is a contract worker (1099 income)
- Borrower receives income from the subject property seller or broker

A 2-year self-employment history, which includes verifying the borrower has ownership in the business, is required to ensure that the income is stable. Less than 2-years may be considered provided the borrower has a recent 2-year history of successful employment in the same occupation (or a related field) and they have been self-employed for at least 1 full tax year.

The borrower's most recent 2 years signed federal income tax returns, including all schedules, must reflect the receipt of income at the same or greater level in a line of business that provides the same products or services as the current business or in an occupation in which s/he had similar responsibilities to those undertaken in connection with the current business.

Individual tax returns and business tax returns (when applicable) must be signed by the borrower unless using an acceptable alternative defined in Tax Forms.

For individual tax returns, the underwriter may accept one of the following alternatives to the Borrower's signature on the tax returns:

- Documentation confirming that the tax returns were filed electronically (e.g., signed Form 8879, IRS e-file Signature Authorization or equivalent);
- A completed IRS form 4506-C (signed by the borrower) for the year in question; or
- IRS transcripts that validate the information on the unsigned tax returns.

Notes: There are some self-employed borrowers who, although classified as such, may not own their own business per se. E.g., 1099 contract workers, borrowers relying on investments for income, borrowers who receive commission income, etc. In these instances, verifying the borrower has ownership in the business is not necessary.

A self-employed individual's income is calculated based on the tax returns. Business tax returns are analysed to assess the likelihood of continued personal income to the borrower. The cash flow of the corporation and an analysis of the trends experienced by the business are used to determine its viability. The inclusion of projected gross or net business income, retained earnings, or capital withdrawal generally may not be used when calculating qualifying income. This restriction applies to all businesses, including closely held corporations.

If any of the borrowers are self-employed, their personal tax returns must be reviewed to determine if there is a business loss that may have an impact on the total qualifying income even if the income from the self-employed business is not being used to qualify.

Note: If personal or business tax returns are included in the loan file for a borrower or co-borrower(s), the underwriter must review and consider in their credit evaluation. The underwriter may not disregard data in tax returns just because they are not required.

BUSINESS RESTRUCTURING

It is not unusual for a business to change their structure to take advantage of various tax or business laws. Although the most common business conversion is from a sole proprietorship to something else, other conversions also occur. A conversion provides the business owner with more protection and less liability. A change like this doesn't necessarily mean the borrower is starting a new business. For example, a business begins as a sole proprietorship and then switches to a partnership, corporation, or S-corporation.

The total length of the business' existence must be at least 2-years. Average income should be calculated using income from both business structures—the current as well as the previous—as long as it can be confirmed that the nature of the business remains the same. Additional adjustments may be required if the restructure occurred. Nevertheless, the result should be the same.

CALCULATING CASH FLOW: PARTNERSHIP & S-CORPORATIONS

Ordinary income, net rental income, and other net rental income reported on Schedule K-1 may be included in the borrower's cash flow provided:

- The borrower can document ownership share (may use Schedule K-1);
- The borrower can document access to the income; and
- The business has adequate liquidity to support the withdrawal of earnings.

Note: Borrowers, who have less than 25% ownership, refer Other Income section for requirements.

If…	Then…

The Schedule K-1 reflects a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify…	No further documentation of access to the income or adequate business liquidity is required. The Schedule K-1 income may then be included in the borrower's cash flow.
The Schedule K-1 does not reflect a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify…	Must confirm the following to include the income in the borrower's cash flow: • The borrower can document access to the income (such as a partnership agreement or corporate resolution)—unless the borrower(s) own 100% of the business, in which case confirmation of access to the income is not required; and • The business has adequate liquidity to support the withdrawal of earnings.
The borrower has a two-year history of receiving "guaranteed payments to the partner" from a partnership or an LLC…	These payments can be added to the borrower's cash flow.
Business tax returns are required…	The type of business structure and analysis of the business returns as indicated in this section of Policy must be considered in accordance with requirements.

Business income may be used to qualify only if the following is documented and verified:

- The income was distributed to the borrower, or
- The business has adequate liquidity to support the withdrawal of earnings. If the Schedule K-1 provides this confirmation, no further documentation of business liquidity is required.

It is important to select a business liquidity formula based on how the business operates. For example:

- The Quick Ratio (also known as the Acid Test Ratio) is appropriated for businesses that rely heavily on inventory to generate income. This test excludes inventory from assets in calculating the proportion of current assets available to meet current liabilities.

Quick Ratio = (current assets – inventory) / current liabilities

- The Current Ratio (also known as the Working Capital Ratio) may be more appropriate for businesses not relying on inventory to generate income). Current Ratio = current assets / current liabilities

For either ratio, a result of one or greater is generally sufficient to confirm adequate business liquidity to support the withdrawal of earnings.

CONTRACT EMPLOYEES

Individuals who work on a contractual basis rather than as an employee, are treated as self-employed and must have a 2-year history in the same line of work. Because the individual may be released from employment at any time, or as specified in their contract, employment history is key in establishing income stability and the likelihood that it will continue.

Required Documentation:

- 2 years most recent personal tax returns with all W-2s or 1099's; and
- Verification that borrower's business remains open and in existence

performed no more than 30 calendar days prior to the loan closing.

CORPORATION

One or a group of individuals establishes a corporation for various tax and liability purposes. Documentation with original signatures of the borrower must be prepared in accordance with standard accounting procedures. Cash flow is determined by taking taxable income minus total tax and adding back: depreciation, depletion, pension, or net operating loss deductions listed on the return.

The corporation must report income and losses on IRS Form 1120 and individual owners may be paid by W-2 or 1099. Complete personal tax returns and corporate returns for the most recent two years must be included in the loan file.

Required Documentation:

- 2 years most recent personal and business tax returns with all Schedules and W-2s or 1099s (tax returns must reflect at least 12 months of self-employed income); and
- Year-to-date unaudited profit and loss (P&L) statement and balance sheet for the business either:
  - Completed by the business's tax preparer; or
  - Completed by the borrower in addition to the following:
    - Evidence provided that the document has been viewed by the business's tax preparer, or
    - Evidence provided that the document has been viewed by an appropriate third party who is not affiliated with the loan transaction, or
    - Two months business bank statements to support the income on the P&L statement and balance sheet.
  - Year-to-date P&L and balance sheet are required when the application is dated more than 90 days after the end of the business' fiscal or calendar year end; and
- Income Analysis Form; and
- Verification that borrower's business remains open and in existence performed no more than 30 calendar days prior to the loan closing.

Note: Corporate income may not be used unless the borrower owns 100% of the business. (Note: W-2/1099 earnings are eligible.)

PARTNERSHIP

There are 2 types of partnerships—a general partner and a limited partner.

- A general partnership indicates that the individual has full ownership interest and is totally liable for the business.
- A limited partner's liability is limited to the amount of their investment only.

The partnership must report its profit or loss on IRS Form 1065 and each partner's share of the profit or loss is reported on Schedule K-1 of the 1065. Complete signed and dated personal tax returns and partnership returns for the most recent two years must be included in the loan file.

The cash flow of the partnership must be analyzed to assess the stability of the borrower's personal cash flow. This provides a snapshot of the business' ability to meet its short-term obligations. Analyzing the 1065 tax return and giving credit for ordinary income, depreciation, depletion, and pension expenses determine cash flow. Discretionary losses should be excluded from the cash flow analysis if the business is a limited partnership, and the borrower provides a copy of the partnership agreement stating that all subsequent contributions are voluntary.

	Required Documentation: • 2 years most recent personal & business tax returns with all Schedules including Partnership return and K-1s (tax returns must reflect at least 12 months of self-employed income); and • Year-to-date unaudited profit and loss (P&L) statement and balance sheet for the business either: o Completed by the business's tax preparer; or o Completed by the borrower in addition to the following ▪ Evidence provided that the document has been viewed by the business's tax preparer, or ▪ Evidence provided that the document has been viewed by an appropriate third party who is not affiliated with the loan transaction, or ▪ Two months business bank statements to support the income on the P&L statement and balance sheet. o Year-to-date P&L and balance sheet are required when the application is dated more than 90 days after the end of the business' fiscal or calendar year end; and • Income Analysis Form; and • Verification that borrower's business remains open and in existence performed no more than 30 calendar days prior to the loan closing. **S-CORPORATION** An S-corporation has the same legal characteristics as a corporation except income and/or losses pass through to the owners/shareholders in the corporation. It may be either the borrower's primary employment or an investment vehicle. Depreciation and depletion can be proportionately added back to the borrower's income since they are considered non-cash expenses. The S-Corporation must report income and losses on IRS Form 1120S and each partner share of the profit or loss is reported on Schedule K-1 of the 1120S. Complete personal tax returns and corporate returns for the most recent two years must be included in the loan file. **Required Documentation:** • 2 years most recent personal and business tax returns with all Schedules and K-1s (tax returns must reflect at least 12 months of self-employed income); and • Year-to-date unaudited profit and loss (P&L) statement and balance sheet for the business either: o Completed by the business's tax preparer; or o Completed by the borrower in addition to the following: ▪ Evidence provided that the document has been viewed by the business's tax preparer, or ▪ Evidence provided that the document has been viewed by an appropriate third party who is not affiliated with the loan transaction, or ▪ Two months business bank statements to support the income on the P&L statement and balance sheet. o Year-to-date P&L and balance sheet are required when the application is dated more than 90 days after the end of the business' fiscal or calendar year end; and • Income Analysis Form; and • Verification that borrower's business remains open and in existence performed no more than 30 calendar days prior to the loan closing.

	<u>SOLE PROPRIETOR</u>
	As an individual owner of a business, the sole proprietor has unlimited personal liability for the debts of the business. There is no distinction between the owner's personal assets and the assets used in the business. The success of this type of organization is solely dependent on the individual who owns it.
	The income, expenses and taxable profits are reported on the owner's personal tax returns, Schedule C. Complete personal tax returns for the most recent two years must be included in the loan file.
	When there is evidence of a large increase in net profits from the prior year, and the income is needed to qualify, additional information may be required to substantiate the income. The borrower must provide a detailed letter from their CPA explaining the cause of the increase along with an audited year-to-date Profit and Loss Statement.
	Required Documentation:
	• 2 years most recent tax returns with all Schedules (tax returns must reflect at least 12 months of self-employed income); and
	• Income Analysis Form; and
	• Verification that borrower's business remains open and in existence performed no more than 30 calendar days prior to the loan closing.
	Note: Third party vendors may be used as an alternative method for verifying self-employed Schedule C income. The verification must provide the same level of documentation defined in this fact sheet. If it does not, additional supplements must be obtained to meet documentation requirements.
	
	<u>VERIFYING THE EXISTENCE OF THE BUSINESS</u>
	Confirmation that the borrower's business remains open and in existence must be verified within 30 calendar days prior to the loan closing when a borrower(s) has 25% or greater ownership in the business. Confirmation is not required if the business income is not used to qualify or if there is a business loss.
	
	Verification should include:
	
	• Documentation prepared/issued by from a third party, such as a CPA, regulatory agency, or applicable licensing bureau, if possible; OR
	• Obtaining a phone listing and address for the borrower's business using telephone book, the Internet or directory assistance. Internet sites such as 411.com, Chamber of Commerce sites and Manta.com where they allow the business owner to add their own information are not acceptable.
	• If the above items are not obtainable, the following alternative methods may be used:
	  o A current statement of bond insurance (the insurance policy must be a minimum of 2 yrs. old); or
	  o Evidence of workers compensation/liability insurance.
	The underwriting rationale must clearly state why the alternative method was used and how the verification confirms the existence of the business.
	
	• For all of the methods of verification, the lender must document the source of the information obtained as follows:
	  o Name and address of the business, and
	  o The entity contacted (if applicable), and
	  o The date the information is verified, and

	○ The name and title of the person who obtained the verification. Note: At the underwriter's discretion, on a case-by-case basis, other sources may be used to verify employment but must be thoroughly explained and documented.
Unacceptable Sources of Income	Income derived from any of the following may not be used in calculating qualifying income. • Any income derived from transactions in or related to the sale or production of marijuana, hemp or any cannabis products or derivatives, such as CBD products. • Any income that cannot be documented and verified • Capital withdrawals • Draw Income • Gambling Income • Gifts, including Gift of Equity • Illegal Income/Income not listed on Tax Returns • Income from Foreign / Non-U.S. Sources • Retirement assets used as qualifying income • Room/boarder rent • ADU rental income • Trade Equity • Trailing Co-Borrower • Any income derived from owning or controlling a VASP (Virtual Asset Service Provider), as defined in the VASP standard. Income that is paid in cryptocurrency
Evaluating Non-Employment Income	If the borrower intends to use income from other non-employed/non-self-employed sources to qualify, the income may be considered stable to the extent that it is consistent, and it is likely to continue for the next 3 years based on the documentation received and the following: • There is no evidence from the employer that the income will no longer be received; and • It is determined that the income is likely to continue based on an established earnings trend. o If the trend is stable or increasing, income can be averaged over the two-year period. o If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used. o If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline. **Note**: Income that is paid to the borrower in cryptocurrency may not be used for qualification. Factors that should be considered in determining the likelihood of consistent payments include, but are not limited to the following: • Whether the payments are received pursuant to a written agreement, court decree, or law; • The length of time the payments have been received; • Eligibility criteria governing the continued receipt of the income, such as age of dependents or accumulation of assets.

	The purpose of this section is to address the various types of other non-employed income that may be used to qualify the borrower, the documentation used to verify the source and the principle methods of validating its authenticity. The Documentation Process used to process the loan will determine if income must be verified and what income documentation is required. As always, additional documentation may be requested if deemed necessary. **Note**: The determination of income stability and its continuance for all sources is based on the required documentation as defined in this section. There should be no evidence that the income will no longer be received to be assumed that it will continue.
Other income	**Alimony/Separate Maintenance** Alimony/separate maintenance/spousal support can be considered a stable source of income provided the borrower has received the income for at least 6 months and the income will continue for at least 3 years. Alimony/separate maintenance/spousal support may be non-taxable. See the Tax Exempt/Non-Taxable Income guidelines in this section for additional information. **Documentation Requirements:** • Deposit slips and/or bank statements/cancelled checks, court records or tax returns evidencing regular deposit of the funds covering 6 consecutive months; and • Final divorce decree, legal separation agreement or court order evidencing amount, frequency, and 3 years continuance **Annuity** Annuity income is similar to pension and Social Security income except that it may not be payable for life. **Documentation Requirements:** Copy of the most recent updated annuity renewal statement showing the effective date, amount, frequency, and 3 years continuance. **Auto Allowance / Expense Account Reimbursement** Auto and expense account reimbursement are paid by the employer to cover expenses incurred related to conducting business. MCFI will consider using a portion of this income to qualify if the borrower has a 1-year history of receiving it and it can be reasonably expected to continue for 3-years. If the borrower reports automobile expenses on Form 2106 or personal tax returns, schedule C: • The amount of the auto allowance that exceeds the amount of monthly expenses is added to the monthly income; or • The amount of the expenses that exceeds the allowance should be included in the borrower's total monthly obligations. Note: If the borrower uses IRS Form 2106 with "actual expenses" instead of the "standard mileage rate," MCFI must look at the "actual expenses" section to identify the borrower's actual lease payments, and then make the appropriate adjustments.

	If the borrower does not report the allowance on either Form 2106 or Schedule C: • The full amount of the allowance should be added to the borrower's monthly income; and • The full amount of the lease or monthly payment for the automobile must be added to the borrower's total monthly obligations and included in the total debt to income ratio. Typically, auto allowance and expense account reimbursements are included with the W-2 earnings; therefore it is very important to make certain the income is not included twice. Refer to Employee Business Expenses (2106) in Employment & Income/ Tax Returns for additional information. **Documentation Requirements:** Most recent pay stubs covering past 30 days; and 2 years most recent W-2s; or 2 years most recent tax returns with all Schedules when auto allowances and/or expenses are reported on IRS Form 2106 or Schedule C. **Boarder Income** Boarder income may not be used to qualify. **Capital Gains/Losses** If a capital gain/loss appears to be a one-time occurrence, it does not have to be considered when calculating available income. However, gains/losses that are recurring may be considered. For example, an asset sold during the year might be income producing and could result in a reduction of future income. If income from this source represents a substantial portion of the borrower's income, review the tax returns along with the Schedule D and average it over 2- years. If earnings are consistent, a 2-year average will suffice. However, if income fluctuates substantially, a 3-year average will be necessary. Capital gain income should only be considered if there is evidence of sufficient assets remaining after closing to support continuance of the income, at the level used for qualifying, for at least the next 3 years. **Exercising Stock Options** Although not typically used as qualifying income, stock options may be considered as qualifying income on occasion if the loan warrants. Only profits received from exercised stock options may be considered. The borrower must have a verified history of receiving income from executed stock options for at least 2-years and the likelihood of its continuance must be verified. **Documentation Requirements** • 2 years most recent tax returns with Schedule D and W-2s or 1099's; and • Proof of ownership of the asset (e.g., statements) evidencing sufficient value to support the continuance of capital gains; and • It is determined that the income is likely to continue based on an established earnings trend. o If the trend is stable or increasing, income can be averaged over the two-year period. o If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used.

- If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline.

Note: Assets may not be in the form of cryptocurrency.

Child Support

Child support can be considered a stable source of income provided the borrower has received the income for at least 6 months and the income will continue for at least 3 years.

Child support is non-taxable and can be grossed up. Follow the Tax Exempt/Non-Taxable Income guidelines in this section for applicable adjustments.

Documentation Requirements:

- 6 months court records, deposits slips, bank statements or cancelled checks evidencing regular deposit of the funds; and
- Proof of ages of the children for which the child support is received; and
- Final divorce decree, legal separation agreement or court order evidencing amount, frequency, and 3 years continuance

Disability – Workers Compensation

Disability and workers compensation varies and must be verified by obtaining a copy of the borrowers' disability policy or benefits statement. A statement from the insurance company or employer must confirm the borrowers' current eligibility for the disability benefit must also be obtained. If the benefits have an expiration date, the remaining term must continue at least 3 years from the date of the mortgage application. Generally, long term disability will not have a defined expiration date and it must be expected to continue. The requirement for re-evaluation is not considered an expiration date.

If the payments will not continue for at least 3 years, refer to the Temporary Leave Income topic in this section for additional guidance.

If the borrower is currently receiving short-term disability payments that will convert to long-term benefits within the next three years, the borrower must be qualified on the lesser amount of either the long-term or short-term disability payments.

Disability and/or workers compensation benefits must be stable and expected to continue for at least 3 years. Non-taxable benefits can be grossed up provided it is verified as non-taxable.

Note: When the income is verified to be non-taxable, and its tax-exempt status is determined likely to continue, the underwriter must develop an "adjusted gross income" for the borrower if the additional income is needed to qualify for the product, program or loan amount applied for. The previous year's tax rate must be used to calculate grossed up percentage. If the borrower was not required to file a tax return or they didn't have any tax liability on their tax return, a 25% tax rate must be used in the calculation. Refer to the Tax-Exempt Income/ Non-Taxable Income topic in this section

	for documentation requirements that must be obtained to determine if a particular source of income is non-taxable. **Documentation Requirements:** • Copy of Disability policy or Benefits Statement • A statement from the benefits' payer (insurance company, employer, or other qualified and disinterested third party) confirming the borrower's current eligibility. • 2-months deposit slips and/or bank statements/cancelled checks evidencing regular deposit. **Foster Care** Foster care income is received from a state-or county-sponsored organization for the temporary care of one or more children. This income may be considered provided the borrower has a 2-year history of providing foster-care services under a recognized program and is likely to continue for the next 3 years at a level that supports the amount of income needed for qualifying for the mortgage. **Documentation Requirements:** • Letters from the organization providing the income showing a 2-year payment history; and • 2 years most recent personal tax returns; or • 24-months deposit slips or bank statements/cancelled checks confirming regular deposit of the payments. **Gambling Winnings** Funds are usually considered as a lump sum distribution and therefore not considered income. However, if the borrower is a professional gambler and the earnings are from his/her self-employed business the income may be used for qualifying. The income must be documented and analyzed per the requirements outlined in Employment & Income/Self Employed Income section. Lottery winners will be considered on a case-by-case basis. **Documentation Requirements:** • 2 years most recent tax returns with all Schedules **Gift Income** Not Permitted. **Inheritance & Other Guaranteed Income** Ongoing income received from inheritance or other guaranteed sources—such as prize earnings, or lottery winnings—may be used to qualify provided it can be verified that the income is regular and recurring. Typically, the borrower should have a documented history of receiving it for at least 2-years and verify that it will continue for at least 3 more years. A copy of the award letter confirming the amount, frequency, duration of payments, and evidence of receipt for the previous 2 years is required. Borrowers who do not have a 2-year history of receiving the income may still be considered contingent upon the terms of the payout. Example: The income is guaranteed to continue for the next 20 years but the borrower has only received one payment/installment. **Documentation Requirements:** • Copy of Award letter confirming amount, frequency, and duration of payments; and • 2 years most recent tax returns with all Schedules. **Interest & Dividends**

Interest and dividend income are reported on personal tax returns, Schedule B.
In order for interest or dividend income to be used as qualifying income the borrower must have a 2-year history of receiving the interest or dividend income and the income must be expected to continue for the next 3 years. The assets from which the interest and dividend income was earned must also be verified via most recent bank statements. Any taxable interest or dividend income that is not recurring must not be used to qualify.
Average interest and dividend income received for the last 2 years to calculate the qualifying income. If funds are used for the down payment and closing costs, the value of the assets should be reduced accordingly, and the interest and dividends recalculated based on the reduced value.
Documentation Requirements:
- 2 years most recent tax returns with Schedule B; and
- Two month's asset account statements showing sufficient assets available to continue generating dividends and interest after closing; and
- Determine that the income is likely to continue based on an established earnings trend.
    - If the trend is stable or increasing, income can be averaged over the two-year period.
    - If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used.
    - If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline.

Note: Assets may not be in the form of cryptocurrency.

K-1 Income w/ <25% Ownership
When a borrower receives K-1 income but has <25% ownership of a partnership, S corporation, or LLC, ordinary income, net rental real estate income and other net rental income reported on IRS Form 1065 or IRS Form 1120S, the income may be used to qualify the borrower provided:
- The borrower can document ownership share (may use Schedule K-1);
- The borrower can document access to the income; and
- The business has adequate liquidity to support the withdrawal of the earnings.

K-1 Cash Distributions
If the Schedule K-1 reflects a stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify, the Schedule K-1 income may be used to qualify, no additional documentation of access to the income or adequate liquidity is required.
If the Schedule K-1 does not reflect a stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify, additional review is required. In addition to the documentation requirements as listed below, the following must be documented and reviewed:
- Evidence that the borrower has access to the income such as partnership agreement or corporate resolution confirming access to the income.

- Evidence that the business has adequate liquidity to support the withdrawal of the earnings. The underwriter needs to determine what documentation is acceptable to determine that the business has the capacity to continue making cash distributions at the level of business income being used to qualify.

Schedule K-1 Guaranteed Payments to Partner
If the borrower has a 2-year history of receiving "guaranteed payments" from a partnership or an LLC, the payments can be used to qualify.

Note: If the borrower has less than a 2-year history of receiving "guaranteed payments" it may only be used to qualify IF the borrower has recently acquired a minimal ownership in a professional services partnership (i.e., medical practice or law firm) after having an established employment history with the partnership. The borrower's partnership agreement and evidence of year-to-date income must also be obtained.
Documentation Requirements:
- 2 years most recent tax returns with Schedule E; **and**
- 2 years most recent Schedule K-1.
- Verification of the existence of the business is required as outlined in the Verifying the Existence of the Business topic in Section Employment and Income/Self-Employed.

Military Benefits
Military personnel may be entitled to different types of pay in addition to their base pay. The following may be considered stable income provided there is documentation verifying the income will continue for at least 3 years.
- Flight Pay
- Hazardous Duty Pay
- Rations
- Clothing Allowance (usually paid yearly)
- Housing Allowances

Education benefits may not be used to calculate qualifying income.
Obtain a copy of the borrower's last Leave and Earnings Statement (LES) to verify allotments, allowances, estimated time in service, and the amount net and gross pay. Also, obtain and verify the following information from the borrower's latest Leave and Earnings Statement (LES):
Military Rank, Social Security Number, Length of active service to date, Estimated remaining time at present location
The tax-free income from housing (BAQ), rations, uniforms, food, flight pay, etc., can be used as income to qualify for the loan as long the income will continue for at least 3 years.
Documentation Requirements:
- YTD LES documenting at least 30 days of income
- W-2's for the most recent two years
- In lieu of a verbal VOE, a Military Leave and Earnings Statement dated within 120 calendar days prior to the note date is required or verification through the online Defense Manpower Data Center.

Military Reserve: Income paid to military reservists may be used to qualify as long as the borrower has a 2-year history or receipt, and the income is expected to continue for the next 3 years.

Minister / Clergy Income

Ministers and other clergy members are typically paid a monthly base pay plus “other” income. The amount of “other” income may vary widely and may or may not be taxable income. Often, ministers are self-employed and/or have unreimbursed business expenses. Housing allowance is typical and may be considered with acceptable verification and documentation.

- Review YTD paystubs and W-2s/1099s and personal tax returns to determine income. Review personal federal tax returns/IRS transcripts to determine unreimbursed business expenses which must be deducted from qualifying income if the tax returns reflect “other” income >25% of the borrower’s annual employment income.
- Documentation provided must show income has been received for most recent 12 months and likely to continue for the next 3 years.
- If there is any indication that all or part of the income is not likely to continue, it should not be used to qualify the borrower.

Notes Receivable

Income from notes receivable may be used to qualify provided the income is regular and recurring. The borrower should have a documented history of receiving the income for at least 1-year and can verify that the income will continue for at least 3 years.

Documentation Requirements:

- A copy of the Note confirming the amount, frequency, and 3 years continuance; and
- Most recent 2 years’ tax returns with Schedule B; or
- 12-months deposit slips and/or bank statements/cancelled checks evidencing regular deposit of the fund.

Notes receivable income on newly executed notes, that do not have at least a 12-month history of receipt but has a minimum duration of 3 years, may not be used to qualify.

Public Assistance

Types of Public Assistance income include but are not limited to Social Security, Section 8 Housing Voucher, Food Stamps and SNAP. Public Assistance income may not be discounted or treated differently than wage income.

It may be considered if the income is properly documented by letters or exhibits from the paying agency. The amount and frequency must be stated in the letters/exhibits and there is no statement that the income will not continue.

Documentation Requirements:

- 2 months deposit slips and/or bank statements/cancelled checks evidencing regular deposit of the fund; and
- Receipt of Letters or Exhibits from paying agency showing amount, frequency, and 3 years continuance.

Restricted Stock

Restricted stock plans award an employee shares of stock as a form of additional compensation. However, the employee cannot take possession of the shares until vesting restrictions are met. Most commonly, the vesting restriction is met if the employee continues to work for the company for a certain number of years. Time-based restrictions may lapse all at once or gradually. If the recipient does not meet the conditions the company set forth prior to the end of the vesting period, the shares are typically forfeited.

	Note: To avoid counting the income/asset twice, if restricted stock is used as income, any unvested shares of restricted stock cannot be used as an asset, nor can dividend interest or capital gains income from the same restricted stock be used. Restricted stock may be considered as qualifying income if the loan documentation supports. The borrower must have a verified history of receiving income from restricted stock for at least 24 months and the likelihood of its continuance must be verified. **Documentation Requirements:** • Documentation of receipt of restricted stock income for the most recent 2 years. E.g., 2 most recent year-end paystubs, W-2's that provide a breakdown of base pay and restricted stock, etc. and • Documentation of the most recent 2 years of restricted stock awards. E.g., compensation awards letters, vesting schedule etc. • Printout/screenshot verifying company is publicly traded and verifying the stock price on the date of application. Note: Restricted stock received from a sign-on type award can be used towards establishing the history of receipt of RSU income, but those shares cannot be considered in the income calculation. Determine that the income is likely to continue based on an established earnings trend. • If the trend is stable or increasing, follow income calculation below. • If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income Calculation Typically, restricted stock income is calculated using the lower of: • An average of the prior 2 years RSU earnings or • The number of performance-based shares/units awarded over the last 2 years at the current employer multiplied by the current stock price on the application date at 70% and averaged over 24 months. See below for example. Example: - 2020 performance/refresh award of 100 shares - 2021 performance/refresh award of 90 shares - Stock price of publicly traded company on date of application $200/share 100 shares + 90 shares = 190 shares x $140 (share price at 70%) = $26,600 / 24 months = $1,108/month qualifying income. **Retirement Assets Used as Qualifying Income** Not permitted. **Retirement Pension** Retirement/pension income may be considered as long as the amount makes sense based on the information provided and time limits of its receipt seem reasonable. Pension income is reported via a 1099. This income can be either taxable or non-taxable and must be expected to continue for the next 3 years. Non-taxable benefits can be grossed up provided it is verified as non-taxable. **Note**: When the income is verified to be non-taxable, and its tax-exempt status is determined likely to continue, the underwriter must develop an

	"adjusted gross income" for the borrower if the additional income is needed to qualify for the product, program or loan amount applied for. The previous year's tax rate must be used to calculate grossed up percentage. If the borrower was not required to file a tax return or they didn't have any tax liability on their tax return, a 25% tax rate must be used in the calculation.
	
	Lump Sum Distributions
	Borrowers who have recently retired and opted to take a lump sum distribution are eligible to use the income as qualifying provided the borrower has transferred funds to an annuity or similar account that allows for regular withdrawals and the account is set up for regular withdrawals. A letter from the borrower's financial advisor is required to verify the terms of the withdrawal.
	If funds are not set up in an account allowing for regular withdrawals, income may not be used to qualify.
	Documentation Requirements
	• Copies of most recent 1 years' 1099 or IRS W-2; or
	• 2-months financial statements or bank statements evidencing regular deposit of the fund; or
	• Statement from the organization providing the income; or
	• Most recent 1 years' Federal Tax Return
	If retirement income is paid as a monthly distribution from a 401(k), IRA or Keogh retirement account, the income must continue for the next 3 years. The retirement accounts (IRAs, 401k or Keogh) may be combined to determine the 3 years continuance. In addition, the following apply:
	• Borrower must have unrestricted access without penalty to the accounts; and
	• If the assets are in the form of stocks, bonds or mutual funds, 70% of the value must be used to determine the number of distributions remaining to account for the nature of the assets.
	Note: Unrestricted access is obtained by borrower arranging under Internal Revenue Code Section 72(t) for distributions and if the distributions are in a series of substantially equal periodic payments (not less frequently than annually) there shall be no associated income tax increase.
	
	Royalty Payments
	Royalty payments may be used to qualify if they have been received on a regular basis for the most recent 12 months and are likely to continue for the next 3 years.
	The income is verified by the most recent 2 years' personal tax returns, including Schedule E.
	Documentation Requirements:
	• 2 years' most recent tax returns with all Schedules, and
	• Documentation that the income will continue for 3 years, and
	• Obtain copies of the royalty contract, agreement or statement confirming amount, frequency & duration of the income.
	  o Determine that the income is likely to continue based on an established earnings trend.
	  o If the trend is stable or increasing, income can be averaged over the two-year period.
	  o If the trend was declining but has since stabilized and there is no reason to believe that the borrower will not continue to receive the income at the current level, the current, but lower stabilized amount must be used.

- If the trend is declining, the income may not be stable and additional analysis must be performed to determine if the income should be used. Income should not be averaged over the period of decline.

Social Security
Social Security income, a type of public assistance, may not be discounted or treated differently than wage income. Social Security benefits or award statements are normally issued each year by the Social Security Administration to reflect cost of living adjustments. This income can be either taxable or non-taxable. The portion that is non-taxable can be grossed up provided it is verified as non-taxable income.
Note: Social Security may be non-taxable. See the Tax Exempt/Non-Taxable Income topic in this section for guidelines and additional information.

Social Security income for retirement or long-term disability that the borrower is receiving from his/her own account/work record will not have a defined expiration date and must be treated as though income is "expected to continue".
If Social Security benefits are being paid as a benefit for a family member of the benefit owner and the income has a defined expiration date due to recipient's age, the income may be used in qualifying; however, you must obtain evidence that the income will continue for at least three years from the date of the mortgage application.

Documentation Requirements
Document regular receipt of payments, as verified by the following, depending on the type of benefit and the relationship of the beneficiary (self or other) as shown in the table below.

<table>
<tr><th>Type of Social Security Benefit</th><th>Borrower is drawing Social Security benefits from own account/work record</th><th>Borrower is drawing Social Security benefits from another person's account/ work record</th></tr>
<tr><td>Retirement</td><td rowspan="2">• Most recent Social Security Administrator's (SSA) Award Letter OR
• SSA-1099 OR
• Most recent signed federal tax returns OR
• Proof of current receipt</td><td rowspan="3">• Most recent SSA Award Letter;
• Proof of current Receipt; AND
• If Social Security income has a defined expiration date due to recipient's age, you must obtain evidence that income will continue for at least three years.</td></tr>
<tr><td>Disability</td></tr>
<tr><td>Survivor Benefits</td><td>N/A</td></tr>
<tr><td>Supplement Security Income (SSI)</td><td>• Most recent Social Security Administrator's (SSA) Award Letter, and
• Proof of current receipt</td><td>N/A</td></tr>
</table>

Note: If the borrower is presently employed but is anticipating retirement within the next 12 months, anticipated retirement income should also be taken into consideration. For newly established SSI benefits, a recently issued Social Security award letter reflecting the finalized terms may be used to document the income if the borrower will begin receiving payments on or before the first payment date of the subject mortgage as confirmed by the award letter. Verification of receipt is not required.

Tax Exempt / Non-Taxable Income
A borrower with tax-exempt/non-taxable income should be evaluated in the same manner as a borrower who has a higher gross taxable income. Tax-exempt sources may include

	• Child support payments, • Social Security benefits, • Disability retirement payments, • Workers' compensation benefits, • Supplemental Nutrition Assistance Program (SNAP) • Public Assistance Payments • Section 8 Housing Payments • Tax Free Municipal Bonds • Section 8 Income may be considered. The payments may not be used to offset the monthly housing payment. The public agency that provides the payment must provide documentation that shows the amount and terms of the monthly payment received and if the income is nontaxable. Refer to Public Assistance topic in this section to determine if able to use Grossed Up income to qualify. The documentation must show that the payments are made directly to the borrower. If the Section 8 income is determined to be nontaxable it may be grossed up as described below. • Tax-exempt trust and inheritance income may be considered provided there is sufficient documentation to support the tax-exempt status. • Verify that the particular source of income is tax-exempt and that both the income and its tax-exempt status are likely to continue. Acceptable forms of documentation include award letter, policy agreements, and account statements. • If the income is verified to be non-taxable, and its tax exempt status is determined likely to continue, the underwriter must develop an "adjusted gross income" for the borrower if the additional income is needed to qualify for the product, program or loan amount applied for. The previous year's tax rate must be used to calculate grossed up percentage. If the borrower was not required to file a tax return or they didn't have any tax liability on their tax return, a 25% tax rate must be used in the calculation. Refer to the specific income types in this section to determine if the income may be grossed up. **Documentation Requirements:** • 1 year's most recent tax returns with all Schedules; or • Other documents show that the income, or a portion is nontaxable. **Note:** If the borrower indicates in any way that s/he did not file a tax return and the 4506-C transcript confirms there is no filing, no additional documentation is required. **Temporary Leave** Temporary leave from work is generally short in duration and may be for family, medical, maternity, short-term disability, or other temporary leave that is acceptable by law or the borrower's employer. During a temporary leave the borrower's income may or may not be reduced or the borrower may not be paid during their absence from work. Leave is no longer considered temporary when the borrower does not intend to return to their current employer, or they do not have a commitment from their current employer to return to work. The requirements and guidance for income while on temporary leave do not extend to employer-initiated actions such as furloughs and layoffs.

	Note: Refer to the Legal section 2201 of this manual for information regarding Medical Information Privacy in the Fair Credit Reporting Act, including details regarding medical information that can or cannot be collected. Income used to qualify is determined by when the borrower will be returning to work: • If the borrower will return to work prior to the first mortgage payment being due, the borrower's regular employment income that will be received upon their return to employment can be used to qualify. • If the borrower will not return to work prior to the first mortgage payment being due, the lesser of the borrower's temporary leave income (if any) or their regular employment income may be used to qualify. Supplemental Income If the borrower will not return to work prior to the first mortgage payment being due and the borrower's temporary income is less than their regular pay, liquid assets may be used to supplement the temporary leave income. However, the total qualifying income (temporary leave income plus supplemental income) may not exceed the borrower's gross monthly income that will be received upon their return to their current employer. Supplemental Income=Available liquid reserves* ÷ the number of months of supplemental income** *Available liquid reserves: Total liquid assets reduced by the amount of funds needed to complete the transaction (down payment, closing costs, prepaids, other debt payoff, required reserves, etc.). **Number of months of supplemental income: The number of months from the first mortgage payment date to the date the borrower will begin receiving his/her regular employment income, rounded up to the next whole number. Qualifying Income Total Qualifying Income = Temporary Leave Income + Supplemental Income Note: Total qualifying income may not exceed the borrower's regular employment income. Example: Regular income amount: $6,000 per month Temporary leave income: $2,000 per month Total verified liquid assets: $30,000 Funds needed to complete the transaction: $18,000 Available liquid reserves: $12,000 First payment date: July 1 Date borrower will begin receiving regular employment income: November 1 Supplemental income $12,000 ÷ 4= $3,000 Total qualifying income: $3,000 + $2,000 = $5,000 **Documentation Requirements:** • Borrower must provide written confirmation of his/her intent to return to work and the agreed upon date of their return as evidenced by

documentation provided either from the borrower, directly from the employer, or a third party as designated by the employer. There must not be any evidence or information from the employer indicating that the borrower does not have the right to return to work after the leave period; and

- Documentation from the current employer confirming the borrower's statutory right to return to work (or the employer's commitment to permit the borrower to return to work), containing the date of return, and the borrowers post-leave employment and income; and
- Documentation of the amount and duration of the borrower's temporary leave income, which may require multiple documents or sources depending on the type and duration of the leave period; and
- Documentation of the amount of the regular employment income that the borrower received prior to the temporary leave. This should include all eligible sources of income that could be used to qualify under normal circumstances (i.e., base pay, commissions, bonus, overtime, etc.); and
- Verbal verification of employment. If the employer confirms the borrower is currently on temporary leave, the borrower must be considered employed; and
- If supplemental income is being used to qualify, the liquid assets must be verified according to the documentation process type selected; and
- Underwriter's rationale must include how qualifying income was calculated.

Trust Income
Income from a trust may be used provided it is properly documented. The trust must have sufficient assets to maintain the same level of payments for the next 3 years. A copy of the trust agreement is generally required.
Note: Assets may not be in the form of cryptocurrency.
Acceptable forms of verification include a copy of the trust agreement or the trustee's statement confirming the amount, frequency, duration of payments and what portion if any is tax-free. Income must continue for at least 3 years.
Lump-sum distributions made before the loan closing may be used for the down payment or closing costs if they are verified by a copy of the check or the trustee's letter showing the distribution amount. The lump-sum amount must be subtracted from the total funds to determine income requirements.
Estates & Trusts
Income from estates and trusts can be very complex in nature; therefore, there must be documented evidence of the amount, frequency of receipt, and continuance for the next 3 years. Losses from estates and trusts must be analyzed for disallowed losses.
Documentation Requirements:

- Copy of Trust Agreement or trustee's statement that verifies the amount, frequency, and 3 years continuance; and
- Proof of receipt of income verified with a bank statement or equivalent documentation; and
- Evidence of sufficient assets to support the qualifying income for at least 3 years (e.g., letter from trustee, bank statements).

In addition to the above the following must be obtained:

- For Variable Trust Payments
    - History of receipt showing 24 months payments documented with 2 years most recent tax returns with all Schedules.
    - Income to be calculated using 24-month average.

	• For Fixed Trust Payments
	  ○ 12-month history of receipt with a bank statement or equivalent documentation; or
	  ○ If unable to document a 12-month history, the trust documentation must reflect fixed payments and
	    the borrower is not the grantor of trust, and
	    at least one payment must be received prior to closing shown in bank statement or equivalent documentation.
	  ○ Income to be calculated using the fixed payment amount documented.
	
	VA Benefits
	Borrowers receiving VA benefits can use the income with proof the benefits will continue for at least three years from the date of loan application. Income must be documented with a letter or distribution from the VA. Education benefits may not be used to calculate qualifying income.
	Documentation Requirements:
	• Document the borrowers' receipt of VA benefits with a letter of distribution from the VA.
	• Verify that the income can be expected to continue for a minimum of three years from the date of the mortgage application. (Verification is not required for VA retirement or long-term disability benefits.)

Rental Income	Rental income can be used as qualifying income provided the transaction meets all of the documentation requirements outlined in this section. Rental income may be generated from the following sources:
	  • Subject property being financed is an owner-occupied 2-4 unit primary residence;
	  • Subject property being financed is a single-family investment property
	  • Other investment property that the borrower currently owns that is not part of loan transaction
	Rental income generated from a second home or single-family primary residence is not considered stable monthly income, may not be used to qualify the borrower, and may not be considered as a compensating factor to offset the total debt-to-income ratios.
	If rental income is not used to qualify the subject investment property, the full PITIA must be included in the debt-to-income ratio.
	Income Calculation for all categories:
	• If the amount is positive, it is added to the qualifying income.
	• If the amount is negative, it is added to the recurring debts.
	The income from rental / investment properties is determined based on if the borrower has a history of renting the subject and/or another property. The rental income will be reported on the IRS for 2 years of 1040, Schedule E of the borrower's personal tax returns, or on Rental Real Estate Income and Expenses of 2 years Partnership or 2 years S Corporation form (IRS Form 8825) of a business tax return.
	Signed leases may be used to determine the net rental income for an investment property not owned during the previous tax year. (Income/loss should be calculated by using 75% of the gross income and verified by current leases.)
	
	Calculating Rental Income on Non-Subject Property
	If the borrower is qualified using the full housing expense (rental income is not considered), documentation of net rental income is not required.

Refer to the table below for all Non-Subject Property income verification requirements.

Does the Borrower Have a History of Receiving Rental Income from the Non-Subject Property?	Documentation Requirements
Yes	The two most recent federal tax returns with Schedule E; and If the property generating income does not appear on the most recently filed tax return, a current lease is required. Rental income must be documented based on requirements for Partial or No Rental Income on Tax Returns reflected below. Income should be calculated using 75% of the gross income.
No	Income/loss should be calculated by using 75% of the gross income and verified by current leases.

Signed leases may be used to determine the net rental income for an investment property not owned during the previous tax year. Refer to Partial or No Rental History on Tax Returns section for additional eligibility options.

When using a lease agreement, the lease agreement amount must be supported by

- Form 1007 or Form 1025, as applicable, or
- Evidence the terms of the lease have gone into effect. Evidence may include:
    - Two months consecutive bank statements or electronic transfers of rental payments for existing lease agreements, or
    - Copies of the security deposit and first month's rent check with proof of deposit for newly executed agreements.

Schedule E - Supplemental Income and Loss

Net Rental Income/Loss should be calculated as follows:

Gross Rents and Royalties Received (from the schedule E)

(-) Total Expenses (from the schedule E)

(+) Amortization/Casualty Loss/Non-recurring Expenses

(+) Insurance

(+) Mortgage Interest

(+) Taxes

(+) HOA fees

(+) Depreciation

= Total ÷ 12 to 24 (# of months based on the tax return review above) – monthly PITIA* payment = Net rental income/loss per month

*If there is a HELOC secured by the property, the payment per the credit report may be used to calculate the monthly net rental income/loss.

- If positive add to income, if a loss add to the liabilities. (Do not include the PITIA in the total obligations, as adding the loss is already taking it into consideration and we don't want to count it against the borrower twice)
- This calculation should be documented in the loan file.

If the current residence is being converted to a second home or investment property, refer to Section Liabilities-Recurring Debt/Real Estate Obligations: Departure Property for additional guidelines.

Calculating Rental Income on Subject Property

Rental/Investment Property Income/Loss – Subject Property

If the borrower is qualified using the full housing expense (rental income is not considered), documentation of rental income is not required.

When the subject property will generate rental income, one of the following forms must be used to support the income-earnings potential of the property:

- Small Residential Income Property Appraisal Report (Fannie Mae form #1025 or Freddie form # 72)
- Single Family Comparable Rent Schedule (Fannie form #1007 or Freddie form #1000)

Note: Leases must be current and fully executed, with a minimum original term of one year.

Refer to the table below for all Subject Property income verification requirements.

Does the Borrower Have a History of Receiving Rental Income from the Subject Property? Yes/No		Documentation Requirements
Yes	Refinance	Average the income/loss unless declining. Verify by use of form 1025/72 or 1007/1000 as applicable and either: • The two most recent federal tax returns with schedule E; or • Current lease agreements that reflect consistent gross rental income if the borrower can document a qualifying exception (see Partial or No Rental History on Tax Returns below).
No	Purchase	Verify by use of form 1025/72 or 1007/1000 as applicable. • Copies of the current lease agreement(s), if property is currently rented. • To calculate the monthly rental income amount for qualifying use 75% of the gross rental income reflected on the lease agreement or verified on form 1007, 1025.
No	Refinance	Verify by use of form 1025/72 or 1007/1000 as applicable. • Copies of the current lease agreements(s), if property is currently rented. • To calculate the monthly rental income amount for qualifying, use 75% of the gross rental income reflected on the lease agreement or verified on form 1025/72 or 1007/1000.

Note: The income approach on the appraisal and copies of the present lease(s), if applicable, must support the rental income used to qualify the borrower.

If the borrower does not have a documented history of receiving rental income as noted above, refer to Partial or No Rental History section for additional eligibility options.

Partial or No rental History on Tax Return

This policy may be applied to refinance of a subject rental property or to other rental properties owned by the borrower.

If the borrower is able to document (per the table below) that the rental property was not in service the previous tax year, or for only a portion of the year, qualifying rental income may be determined by using the following:

- Schedule E Income and expenses, and annualizing the income (or loss) calculation; or
- Lease agreement(s) to 75% of the gross rental income to be used in the net rental income (or loss) calculation.

Note: Leases must be current and fully executed, with a minimum original term of one year. The rental payment on the lease must be in U.S. dollars (cannot be in cryptocurrency)

If the property was acquired during or subsequent to the most recent tax filing year,	Then confirm the purchase date using the Closing Disclosure or other documentation • If acquired during the year, Schedule E (Fair Rental Days) must confirm a partial year rental income and expenses (depending on when the unit was in service as a rental). • If acquired after the last tax filing year, Schedule E will not reflect rental income or expenses for this property.
If the rental property was out of service for an extended period,	• Schedule E will reflect the costs for renovation or rehabilitation as repair expenses. Additional documentation may be required to ensure that the expenses support a significant renovation that supports the amount of time that the rental property was out of service. • Schedule E (Fair Rental Days) will confirm the number of days that the rental unit was in service, which must support the unit being out of service for all or a portion of the year.
It is determined that some other situation warrants an exception to use a lease agreement,	The loan file must contain an explanation and justification to support using a lease agreement.

Rental Income Reported Through a Partnership or S-Corporation

If the borrower is personally obligated on a mortgage debt (as evidenced by the credit report) and gross rents and related expenses are reported through a Partnership or an S-Corp, Form 8825 may be used to calculate net rental income or loss for the property.

The Partnership or S-Corp must be documented and analyzed according to the Employment & Income/Self-Employed Income/Partnership or Employment & Income/Self-Employed Income/S-Corp section.

- Obtain Partnership or S-Corp business tax returns, including IRS Form 8825.
- Analyze each property listed on Form 8825
- If the net cash flow is positive, exclude the property PITIA from the borrower's monthly obligations.
- If the net cash flow is negative (not sufficient to offset the properties PITIA) the negative amount must be included in the DTI calculation.

APPRAISAL

Appraisal

**A full interior/exterior appraisal is required.

**A recertification is required if the appraisal will be more than 120 days old as of the date of the Note/Mortgage. In addition, the recertification of value cannot be more than 90 days old at the time of closing.

Note: No more than two recertifications of value may be obtained on a transaction when the appraisal is more than 120 days old as of the Note/Mortgage.

**High Value Zip Code Areas and Depreciating Market policies apply.

When the subject property is in a depreciating market. The maximum LTV/CLTV/HCLTV is reduced by 5%. If the subject property is not in a depreciating market per the appraisal report, but the subject property is in MCFI depreciating market list (Exhibit 1 can be provided per request), there will be a 5% LTV/CLTV/HCLTV mandatory reduction applied.

**Clear Capital CDA (Collateral Desktop Analysis) appraisal review is required. If CDA produces a value more than a 10% negative variance to the appraisal value, a field review is required. If there are two appraisal reports, CDA is not required.

Additional Appraisals

	MCFI determines the number of appraisals required and the type of appraisal reviews required based on loan size.
	
	• If the loan amount is > $2.0MM, 2 appraisals are required.
	   ➢ Ordering both reports from the same company, vendor, or agent is expressly forbidden. If two appraisal reports are required, MCFI requires the two reports to be ordered from two different Appraisal Management Companies (AMC). Note: In some circumstances, that may not be possible, including in cases where a Correspondent Lender may only work with one AMC. In those instances, it may be necessary for one AMC to order the two appraisal reports. However, the independence of the appraiser/ appraisal process must be maintained at all times by all parties.
	   ➢ If two appraisals are required, the lesser of the two values should be used to underwrite the transaction and determine LTV/CLTV/HCLTV.
	
	All appraisal reports that are more than 120 days old as of the Note/Mortgage require a recertification of value/update that includes an exterior inspection of the property and a review of current market data to confirm that the property has not declined in value since the date of the original appraisal.

Condo Project Approval	**For Delegated transactions: Limited Review Condominium Projects: The condominium project must meet Fannie Mae's guidelines for limited review. Full Review Condominium Projects: The condominium project must meet Fannie Mae's guidelines for full review. The following documentation must be provided to MCFI in the loan package: Condominium Project Questionnaire Current Condominium Project Budget Master Insurance Policy CC&R By-laws HO6 policy if applicable **Note**: Non-warrantable condo/co-ops are not permitted.
Flood Insurance	For Condominiums, private flood insurance policies are permitted only if reviewed and approved by MCFI. For single-family loans, any private insurance policy is subject to review. The flood insurance coverage must be at least as broad as a comparable standard NFIP flood policy and must meet the rating requirements for property insurers as defined – Hazard Insurance. Evaluation of the review of the private policy requirements below must be documented in the file. Deductible limits should not exceed the NFIP policy deductibles for comparable coverage amounts. Deductibles may be higher than NFIP deductibles when coverage amounts exceed NFIP coverages; however, the borrower must have two times that deductible in liquid reserves/assets. Pooled risk policies (covering multiple condominium associations) are not acceptable to primary investors or consistent with this policy. Flood Insurance must be impounded on all Flood Zone Area properties (SFR, Multi-Units, Detached Condo/PUD)

Chain of Title	All purchase and refinance transactions on existing properties will require a 12 month "chain of title" from the title insurer that does not evidence any previous flipping activity for the property (i.e., multiple property transfers).

OCCUPANCY	
Primary Residence	A primary residence is the borrower's main residence, where they live the majority of the year. It may be a 1-unit, condominium, PUD, or 2-4 unit property. Characteristics that may indicate the property is the borrower's primary residence include: • It is occupied by the primary wage-earner for the major portion of the year; • It is in a location relatively convenient to the owner's principal place of employment; • It is the address of record for such activities as federal income tax reporting, voter registration, occupational licensing, and similar functions. The borrower must occupy the property within 60 days of closing. At least one of the borrowers must occupy and take title to the property and execute the note and mortgage. Exceptions (e.g., active military personnel) will be considered on a case-by-case basis.

Second Home	A second home is defined as 1-unit property (including condominiums, and PUDs), unless otherwise indicated in a process or program fact sheet, that the borrower occupies for some portion of the year in addition to their principal residence. A borrower may have more than one second home. While second homes are often located in a vacation/resort area although not always, the property must be suitable for year-round occupancy. A second home should not be in the same market as the borrower's primary residence. However, there are exceptions, such as: • Property located in a recreational area which is part of a metropolitan area (e.g., beach house), or • Property used to minimize commuting problems (e.g., a Manhattan condominium owned by a Connecticut resident working in New York City). There are no specific mileage requirements with regards to the distance between the primary and second home. Good judgment must prevail, and all of the following criteria must be considered for second homes: • Rental income received from the second home may not be used to offset the expense of a second home and cannot be used as qualifying income. • 2-4 unit properties are not eligible as a second home. • The property must be occupied by the borrower for some portion of the year • The borrower must retain exclusive control over the property. • The sales contract or appraisal must not reflect that there are timeshare arrangements or any other rental agreements that require the property to be rented.
Investment Property	An investment property is an income-producing property that the borrower or co-borrower does not occupy. The subject property may be a 1-4 unit, condominium, or PUD. Rental income may be used to qualify. Rent Loss Insurance required. Occupying Tenant: For Purchase transactions, if the subject property is currently being rented, the rental agreement/lease must be reviewed to ensure that it does not contain any provisions that could affect our position as mortgagee. In some jurisdictions, a lease that pre-dates the mortgage has a superior claim to the mortgage, even if it has not been recorded. However, the tenant's rights will usually remain intact under the pre-existing lease. If the lease is not subordinated to the mortgage, each lease must be reviewed to ensure that any "rights to purchase"—and any other rights that could adversely affect the mortgagee's interest—have been formally waived by the tenant. Additional Requirements for Subject Investment Properties: • If rental income is not used to qualify, PITIA must be used in calculating the debt ratios. • When the subject property is an investment property and the borrower(s) own multiple investment properties, the borrower(s) must provide evidence of a minimum of 2 years' experience managing multiple investment properties • Co-op properties are not eligible as investment properties.

Multiple Properties	**Subject is Primary Residence:** For loans secured by primary residences, borrowers may not own or be obligated on a combined total of more than 5 financed residential properties, including the subject property. (Refer to the section below to determine if "other properties owned" should be included in limitation.) **Subject is Second Home or Investment Property:** If the subject property is a second home or investment property, typically each borrower individually and all borrowers collectively may not own or be obligated on a combined total of more than 4 financed residential properties (including the subject property) at the time of application (applies to either a single lender or several different lenders, including MCFI). **Other properties owned should be included in limitation.** • Joint ownership of residential real estate. (This is considered to be the same as total ownership of an individual property.) • Joint or total ownership of a property that is held in the name of a corporation or S-corporation even if the borrower is the owner of the corporation. however, the financing is in the name of the borrower. • Obligation on a mortgage debt for a residential property (regardless of whether or not the borrower is an owner of the property on title). • Joint or total ownership of a property that is held in the name of an LLC or partnership where the borrower(s) have an individual or combined ownership in the LLC or partnership of 25% or more, regardless of the entity (or borrower) that is the obligor on the mortgage. • Ownership of a manufactured home and the land on which it is situated that is titled as real property. • Joint or total ownership of a property that is held in the name of an LLC or partnership where the borrower(s) have an individual or combined ownership in the LLC or partnership of less than 25% and the financing is in the name of the borrower. **Other properties owned should not be included in limitation.** • Ownership of commercial real estate. • Ownership of multifamily property consisting of more than four dwelling units. • Joint or total ownership of a property that is held in the name of a corporation or S-corporation even if the borrower is the owner of the corporation and the financing is in the name of the corporation or S-corporation. • Ownership in a timeshare. • Ownership of a vacant (residential) lot. • Joint or total ownership of a property that is held in the name of an LLC or partnership where the borrower(s) have an individual or combined ownership in the LLC or partnership of less than 25% and the financing is in the name of the LLC or partnership. • Ownership of a manufactured home on a leasehold estate not titled as real property.

TRANSACTION TYPE	
Buyout of Spouse, Domestic Partner, or Affianced Interest	A refinance that results from a divorce settlement in which one of the spouses is required to buy out the other's interest in a property is considered a rate/term refinance provided the borrower who acquires sole ownership of the property does not receive any cash back. We may also consider a buyout of the interests of a domestic partner, fiancée, or fiancé as a rate/term refinance transaction if all of the following conditions are satisfied: • Both parties owned the subject property jointly for at least 12 months preceding the date of the mortgage application. An individual who inherits an interest in the property does not have to satisfy this requirement. • Both parties are able to demonstrate that they occupied the property as their principal residence by providing an acceptable source of verification (e.g., driver's license, bank statement, credit card bill, utility bill, etc. that was mailed to the individual at the address of the mortgaged property). • Both parties must sign a written agreement that states the terms of the property transfer and the proposed disposition of the proceeds from the refinance transaction. The borrower who acquires sole ownership of the property must not receive any cash back from the proceeds of the refinance. • The party who is buying out the other party's interest must be able to qualify for the mortgage under our standard underwriting guidelines. • Texas Property: The division of the homestead property pursuant to a court order or an award in a divorce proceeding is considered a Texas Non Equity Loan that may be processed as a rate/term refinance. The borrower may not receive any cash back at closing. • Transaction Type: All transactions may be originated as rate/term refinances, regardless of process type.

Continuity of Obligation	When an existing Mortgage on the subject property will be satisfied as a result of a refinance transaction (rate/term and cash out), one of the following requirements must be met: • At least one Borrower on the refinance mortgage was a Borrower on the mortgage being refinanced; or • At least one Borrower on the refinance Mortgage held title to and resided in the mortgaged premises as a primary residence for the most recent 12-month period and the mortgage file contains documentation evidencing that the borrower, either: o Has been making timely mortgage payment, including the payments for any secondary financing, for the most recent 12-month period; or • At least one Borrower on the refinance mortgage inherited or was legally awarded the mortgaged premises (for example), in the case of divorce, separation, or dissolution of a domestic partnership. • The property was previously owned by an inter vivos revocable trust and the borrower is the primary beneficiary of the trust. **Note**: Continuity of Obligation requirements do not apply when there is no existing mortgage on the subject property. Refer to the Rate/Term Refinance: Other Purpose topic below for additional requirements for adding or removing a borrower from a transaction, or the Buyout of Spouse, Domestic Partner, or Affianced Interest topic for additional requirements.
Non-Arm's Length Transaction	**Non-arm's length transactions are not permitted.** A non-arm's length transaction is one in which there is a relationship or business affiliation between the seller and the buyer of the property (e.g., family sale, property in an estate, employee and employer, renter and landlord, or flip transactions). Common risks associated with this type of loan include: absence of equity or down payment; a purchase price that does not represent the actual property value; financial bailouts or attempts to hide poor credit; occupancy concerns; and financing of unsold builders inventory, especially in soft real estate markets.
Properties Listed for Sale	If the subject property is currently listed for sale the loan is not eligible for a rate/term refinance or a cash-out refinance. Properties that were listed for sale and taken off the market within the past 180 days are eligible for a rate/term refinance only on a primary or second home. These loans are not eligible for a cash out refinance. Documentation evidencing the listing was cancelled, along with a letter of explanation from the borrower detailing the rationale for cancelling the listing, must be provided. Every effort should be made to verify the property is no longer listed for sale and the underwriter should give additional scrutiny to these transactions to ensure that refinancing the loan provides a benefit to borrower. This policy does not apply to the refinance of a property that was recently purchased within the past 180 days.

<table>
<tr><td>Purchase</td><td>A purchase transaction allows proceeds to be used to:
Finance the purchase of a property.
Payoff an outstanding balance on an installment land contract, including any costs the borrower incurred for rehabilitation, renovation, or energy conservation improvements. If the financing exceeds the liens, the transaction must be considered a refinance.
Convert a lease option to purchase into permanent financing, as long as the borrower receives no cash back from the transaction.
Note: The borrower may not be on title prior to the loan closing. The seller that is on title (the vested owner of record) must be the individual who executes the sales contract. Additionally, the seller must be on title prior to when the Closing Disclosure and closing docs are executed.
Exceptions:
Corporate relocation transactions are excluded from this requirement. For a corporate relocation loan only, a third-party relocation company may sign the sales contract and the Closing Disclosure as the seller. A copy of the fully executed Relocation Agreement is required.
If the transaction is a purchase transaction of a repossessed property where the seller is FNMA, FHLMC, bank, etc., it is acceptable for an individual representative of the “seller” to sign the sales contract and Closing Disclosure. For this type of transaction, we would rely on the title company to ensure that the individual is an authorized signer.
LTV Calculations:
Calculate the LTV by dividing the loan amount by the lower of the sales price or the current appraised value.
Purchase Transactions for Existing Properties: The cost of a separate contract or bid for improvements to be made may not be added to the contract purchase price to calculate the LTV.</td></tr>
<tr><td>Refinance: Cash-Out</td><td>A cash-out refinance transaction enables a borrower to pay off his or her existing mortgage by obtaining a new first mortgage that is secured by the same property, or enables the property owner to obtain a mortgage on a property that does not already have a mortgage lien against it.
A transaction that does not meet all of the criteria listed for a Rate/Term Refinance section above must be treated as a cash-out refinance and must meet all the LTV/loan amount restrictions.
Cash out transactions must meet the following requirements:
At least one borrower must have owned the subject property for a minimum of 6 months prior to the application date. (Note: There are no seasoning restrictions for doing two consecutive cash-out transactions.):
Borrower acquired the property through an inheritance or was legally awarded the property (divorce, separation, or dissolution of a domestic partnership there are no other seasoning requirements. Refer to “Inherited Property” requirements below.
If prior to closing the property is owned and held in a Limited Liability Corporation (LLC) that is majority-owned or controlled by the borrower, the time it was</td></tr>
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	held in the LLC may be counted towards meeting the borrower's six-month ownership requirement. (Reminder: In order to close the new refinance transaction, ownership must be transferred out of the LLC and into the name of the individual borrower.) o For properties in a leasehold estate, at least one borrower must have been a lessee on the ground lease or lease agreement of the subject leasehold estate for at least 6 months. • Continuity of Obligation must be met. Refer to the Continuity of Obligation topic for complete information. • The existing loan being refinanced may not be a restructured mortgage as defined in "Restructured Loans" section. • Refer to the "Properties Listed for Sale" topic in this section for information if the subject property has been listed for sale in the six months preceding the application date. • Except as required by applicable law, a Power of Attorney may not be utilized to sign a security instrument or note if the transaction is cash-out refinance. • Financing the payment of closing cost, points, and prepaid items is allowed. However, if real estate taxes are more than 60 days past due and are included in the new loan amount an escrow account must be established, unless prohibited by state law or regulation. In those instances, only, when the particular state law prohibits the lender from requiring an escrow account, the loan is still eligible as a cash-out refinance without an escrow account. • This includes the payoff of any second mortgage, that is not permitted as outlined in the Rate/Term Refinance section, and transactions in which the loan proceeds exceed the maximum amount of funds that can be disbursed to the borrower per the rate/term refinance guidelines can be done as a cash out refinance. **Inherited Properties** If a mortgaged property was inherited within the last 6 months, the following restrictions apply: • The owner must have clear title; • Title cannot be held in probate; and • Percentage of ownership by heirs must be demonstrated. • Documentation evidencing the inheritance must be obtained.
Refinance: Other Purposes	Proceeds from a rate/term refinance may also be used for the following purposes, as long as all other rate/term refinance guidelines and policies as defined in the referenced sections are met: • Buy out a divorced spouse, domestic partner's ownership interest in the subject property as defined in Buyout of Domestic Partner or Affianced Interest. **Existing HELOC/Fixed Rate Second Being Paid Off** Refer to the Rate/Term Refinance Loan Amount Calculation topic in this section for details. **Adding a Borrower to the New Transaction** All borrowers listed on the new loan must be the same as those listed on the original loan. A new borrower may be added, and the transaction still will be eligible under the terms of a rate/term refinance

	provided at least one of the original borrowers remains on the loan. However, all credit parameters (e.g., minimum score) must be met for the product/program selected. **Removing a Borrower from the Transaction** The loan may still be eligible for a rate/term refinance if the borrowers have been divorced for 6 months or more and the remaining borrower has demonstrated the ability to manage the payments without the "absent" borrower's income. Verification of timely payments for 6 months is required.

Rate/Term Refinance	**Eligibility Criteria**
	The policies outlined in this section apply only to the following conventional rate/term refinance transactions.
	There must be an existing mortgage secured by the property that will be paid off.
	The transaction is not eligible as a rate/term refinance if the borrower completed a cash-out refinance transaction with a note date 30 days or less prior to the application date of a new refinance on the same property.
	Loan Amount Calculation
	The new loan amount is limited to:
	• Payoff the outstanding unpaid principal balance of the existing first lien, regardless of the loan originate date; and
	• Pay off any remaining balance due under a repayment plan, payment deferral or other loss mitigation program, as long as the funds are not subordinate financing; and
	• Financing of related closing costs and prepaid items*;*Prepaid Real Estate Taxes: The loan must be treated as a cash-out refinance and is subject to all cash-out policies, LTV's, etc. if:
	  o If the borrower finances the payment of real estate taxes for the subject property in the loan amount, but does not establish an escrow account; OR
	  o The borrower finances the payment of real estate taxes for the subject property in the loan amount and the real estate taxes are more than 60 days delinquent (with or without establishing an escrow account).
	  However, if a particular state law prohibits a lender from requiring an escrow account, the loan is still eligible as a rate/term refinance without the escrow account.
	Note: Properties with transfer fees that are identified as exceptions on the title commitment may not be included.
	• Payoff of a subordinate loan that meets one of the following scenarios:
	  o The subordinate lien was made within the last 12 months and all proceeds were used to purchase the property.
	    ✓ A copy of the HUD-1/Closing Disclosure signed by the borrower from the original sale must be obtained to verify that the entire amount being paid off was used to purchase the subject property.
	    ✓ The payoff may also include any prepayment penalty that may be associated with the subordinate lien.
	    ✓ If the subordinate lien is a home equity line of credit, the total amount of additional draws within the past 12 months may not

	exceed $2000 (as documented by copies of home equity line statements). OR ○ The subordinate lien was made more than 12 months ago: ✓ The payoff may also include any prepayment penalty that may be associated with the subordinate lien; and ✓ If the subordinate lien is a home equity line of credit, the total amount of draws against the line during the past 12 months does not exceed $2,000 (as documented by copies of home equity line statements); or • Cash back to the borrower may not exceed 1% of the principal amount of the new mortgage or $5,000 whichever is less, as noted on the Closing Disclosure. Cash back on the Closing Disclosure may only exceed this amount by the amount that was paid outside of closing by the borrower, or due to refunds that may be required in accordance with federal laws or regulations as documented in the loan file. The Closing Disclosure must clearly indicate the refund with a notation for the reason, and the loan file must include documentation to support the amount and reason for the refund. **Note**: For Texas properties, a new refinance transaction that includes the payoff of an equity line of credit, the payoff of any loan that is a Texas Section 50(a)(6) loan, or provides any cash to the borrower at closing makes the new loan subject to Texas Section 50(a)(6) requirements and is not eligible. **Inherited Properties** If a mortgaged property was inherited within the last twelve (12) months, the following restrictions apply: • The owner must have clear title; • Title cannot be held in probate; and • Percentage of ownership by heirs must be demonstrated. A five percent (5%) LTV/CLTV reduction must be applied to LTV/CLTV /HCLTV. • Documented evidence of the inheritance must be obtained.
Refinances: Restrictions	• At-Close Principal Curtailments are not permitted. If cash proceeds to the borrower exceed the maximum amount permitted for a rate/term refinance, the loan amount must be adjusted accordingly before the loan closes. The excess amount must not be handled as an at-close principal curtailment. Exception: Principal Curtailments are only allowed as a result of at closing excess premium rate credits. The amount must be identified on the Closing Disclosure and is limited to the amount of the excess premium rate credit.
Construction-to-Permanent Financing	MCFI provides end-loan financing on a proposed property, subject to completion, per plans and specifications after a construction loan is obtained. To be considered for construction to permanent financing, the borrower must be the primary obligor on the construction loan as well as the owner of the lot. Any other combination (e.g., the borrower owns the lot, but is not the primary obligor on the construction loan) must be considered a traditional purchase transaction.

	A newly constructed home is eligible for construction to permanent financing once the construction is complete. All construction work must be completed and paid for, and all mechanics' liens, materialmen's liens, and any other liens and claims that could become a lien relating to the construction must be satisfied before the mortgage loan is closed. The conversion of an interim loan or term note into permanent financing may be considered a purchase money transaction or a refinance transaction. While a purchase transaction may allow a higher LTV, the borrower may wish to opt for a refinance transaction that requires less documentation to establish the value of the mortgaged property and offers the possibility for cash-out. **Note:** The right to rescind will not apply to a loan to finance the acquisition or construction of a dwelling, but the right to rescind will apply to a loan to rehabilitate or improve the borrower's principal dwelling. If you have any questions about whether the right to rescind applies to a particular loan transaction, consult with Legal or Compliance. The loan classification is determined on the length of time the borrower has held legal title to the lot, and in some cases, how title was acquired. A copy of the purchase contract or HUD-1/Closing Disclosure signed by the borrower may be used to document the cost of the lot. **Ineligible Property Types**: Units in a condo or co-op project are not eligible. **Required Documentation:** • Uniform mortgage instruments are required, and they may not be altered to include any reference to construction of the property. A construction loan rider is used to modify the uniform instruments. The rider must state the construction loan terms, and the construction-related provisions of the rider must become null and void at the end of the construction period, when the construction loan is modified into the permanent financing. • When the construction-to-permanent loan provides funds for acquisition or refinancing of an unimproved lot and the construction of a residence on the lot, a certificate of occupancy must be obtained from the applicable government authority. **New Construction** • New construction properties are properties that are proposed or under construction at the time of loan application. • A full interior/exterior appraisal is required. **Note:** Transactions that allow a borrower to make a single disbursement to a builder/contractor for the purchase of a newly completed site-built property (including an existing home that has never been occupied), where the borrower acquires title to both the lot and the improvements at the same time, are not considered new construction or a conversion of a construction loan; however, a full interior/exterior appraisal is required if the property has never been occupied.

Converting an Interim Construction Loan to a Permanent Loan
The conversion of an interim construction loan to a permanent loan may be handled as:

1. A Single-Close Transaction: (Not Permitted), where one loan is used for both the interim construction loan and the permanent long-term mortgage. Upon completion of construction, the construction loan is either automatically converted to the permanent loan, as outlined in the construction rider to the note, or the construction loan terms are modified to match the final terms of the permanent loan, as outlined in the Modification Agreement. If required, the Modification Agreement must be recorded.
2. A Two-Close Transaction, where a new long-term mortgage replaces the interim short-term construction loan that was used to fund the construction of the new residence. There is one closing for the construction loan and another closing for the new permanent loan. Two-Close Transactions may be rate/term or cash out refinance transactions.

Purchase Money Guidelines
Purchase money guidelines (including required minimum borrower contribution requirements) apply to transactions where the borrower is not the owner of record prior to closing the construction financing.

The cost of the lot and total construction costs must be fully documented with receipts identifying the subject property along with cancelled checks.

The borrower may not receive any cash back on a purchase transaction, unless the amount represents:

- Reimbursement for overpayment of fees, transaction costs paid by the borrower in advance (e.g., earnest money deposit, appraisal, credit report fees, etc.), or pro-rated real-estate tax credit in locales where real estate taxes are paid in arrears. The underwriter must confirm that the minimum down payment or required borrower contribution has been met. Pro-rated real estate tax credits cannot be considered when determining if the borrower has enough funds for the transaction.
- Verify that Borrower Contribution Requirements have been met.

Rate/Term Refinance Guidelines:
For the transaction to be treated as a refinance, the borrower must have acquired title to the lot before applying for construction financing and must be named as the borrower on the construction loan.

LTV Calculation for Single-Closing Transactions

Transaction Type	Lot Ownership Requirement	LTV Ratio Calculation
Purchase	The borrower is the owner of record to the lot after or in connection with the first advance of the	Divide the loan amount of the construction-to-permanent financing by the lesser of:

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<td>construction financing.</td>
<td>The purchase price (sum of the cost of construction and the sales price of the lot); or
The “as completed” appraised value of the property (the lot and improvements).</td>
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<tr>
<td>Limited Cash-out Refinance</td>
<td>The borrower is the owner of record to the lot prior to the first advance of interim construction financing.</td>
<td>Divide the loan amount of the construction-to-permanent financing by the “as completed” appraised value of the property (the lot and improvements).</td>
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Cash-Out Refinance Guidelines
If the borrower receives cash back at the construction loan closing or pays off unsecured liens or construction costs paid by the borrower outside of the interim construction loan, the loan must be treated as cash-out refinance. In addition, the borrower must have acquired title to the lot before applying for the construction financing and must be named as the borrower on the construction loan.
LTV Calculation:
The LTV is determined by dividing the loan amount by the current appraised value of the lot and improvements.
Note: To be eligible for a cash-out refinance, the borrower must have held legal title to the lot for at least six months prior the closing of the permanent mortgage. All other cash-out refinance parameters—including the maximum LTV and loan amount, must be met. It is not necessary to ask the borrower to provide evidence of the funds invested into the transaction.
Modified/One-Time Close Transactions
This feature is not available.
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<td>Tangible Benefits</td>
<td>The net tangible benefit is the financial advantage that a borrower gains by completing a refinance transaction. The existence of at least one benefit of the refinance for every refinance transaction must be existed, which may include but is not limited to the following;

Cash-out refinances
Refinancing an existing Home Equity line of credit into a fixed-rate, closed-end mortgage loan
Reduction in principal and interest payment
Reduction in term
Reduction in interest rate
Refinancing an ARM to a fixed rate mortgage
Refinancing an interest only product to a fully amortized product

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	• Refinancing a balloon/reset product to a fixed rate mortgage • Refinancing to buy out another party's equity position • Refinancing to comply with court order (e.g., divorce or other court ordered separation of title) • Refinancing to complete inheritance buyout • Refinancing to eliminate mortgage insurance • Refinancing to extend draw period on a HELOC NOTE: Curing a default or delinquency on a mortgage is not a valid NTB

CREDIT	
Age of Credit Documents	MCFI credit report must be pulled upon loan submission. Third party originator credit report is not acceptable. Credit documents may not be more than 90 days old at time of loan closing for existing and new construction. Credit documents include credit reports and employment, income, and asset documentation. The age of the documents is measured from the date of the document to the date the note is signed. For properties located in an "escrow state" only, the printed note date and actual closing/signing date may differ. In these instances, the Closing Disclosure should be used to determine the actual closing date for determining the age of credit documents.
Minimum Tradelines	**Traditional Credit** The cumulative established credit history of all borrowers on the transaction needs to consist of a minimum of 4 trade lines (installment, revolving accounts, mortgages, etc.), one of which is open and has a minimum of 24 months history, the other 3 may be open or closed but must be rated for at least 12 months. Non-traditional credit history is not permitted. **Note**: If there are less than 4 trade lines, or the trade lines do not meet the required payment history requirements as outlined or if there is no credit, there is insufficient data to determine credit behavior—even if the report includes a credit score.
Credit History	The credit history reflects the manner in which a borrower manages their financial responsibility, current obligations, and monthly payments. Good credit must not be considered a compensating factor. It must be expected of each borrower applying for a mortgage. Changes in Credit Usage Recent changes in the borrower's use of credit may indicate they are having difficulty in maintaining accounts. Review is required for the age of all obligations to determine whether there has been a recent, significant increase in the number of open accounts and/or the number of outstanding balances. Authorized Users of Credit – All Loan Transactions Credit report trade lines that list a borrower as an "Authorized User" may only be considered as part of the borrower's credit history to meet minimum credit requirements if: • Another borrower in the current loan transaction is the owner of the trade line; or • The borrower can provide written documentation (i.e., cancelled checks) that s/he has been the actual and sole payer on the

	account for at least twelve months preceding the date of the loan application. If an authorized user's account is used to meet the minimum credit requirements, then both the payment history, including any late payments and the monthly obligation must be considered in the credit analysis and included in the DTI ratios.
Evaluating the Credit Score	If using an external credit score, the underwriter should review the score in conjunction with the borrower's credit history requirements, keeping in mind that: • A high score does not mean the loan should automatically be approved. Rather, it means that the underwriter must determine that the mortgage satisfies our eligibility criteria and the borrower meets our overall underwriting standards. • A low score does not mean the loan will go into default (although statistically there is a higher likelihood of this occurring). However, the loan must have strengths to compensate for the low credit score. • A lack of a score due to little or no credit does not constitute a high credit risk. Rather, it means that the borrower has insufficient credit from the type of credit providers that generally report to credit bureaus.

Consumer Credit Counseling Agencies (CCCA)/Debt Management Services (DMS)	Consumer Credit Counseling Agencies (CCCA) and Debt Management Services (DMS) assist borrowers who may have had difficulties in managing their debt; it is often demonstrated by a history of delinquent accounts. Debt management plans may be administered by a not-for-profit agency such as consumer credit counseling agency (CCCA) or a non-affiliated for-profit debt prorating service.
	
	Note: Homeownership Counseling, which is designed to help first time homebuyers prepare for the financial responsibilities associated with home ownership, should not be confused with Consumer Credit Counseling. This section addresses Consumer Credit Counseling Agencies (CCCA)/Debt Management Services (DMS) only.
	
	The following scenarios ARE NOT considered added risk and should not be held against the borrower when considering them for a mortgage loan.
	
	• The borrower is/has participated in Homeownership Counseling in preparation for purchasing a home.
	• The borrower is/has participated in consumer credit counseling or debt management program but continues to manage their own finances.
	• The borrower participated in consumer credit counseling or debt management program during which time the counseling agency made payments to creditors on the borrower's behalf. The following conditions must be met:
	  o A minimum of 12 months must have passed since the borrower participated in the program.
	  o The borrower has demonstrated the ability to manage credit since then.
	  o The borrower has a satisfactory pay history on all accounts.

	The following conditions ARE considered adverse risk factors and must be considered accordingly: • The borrower is currently participating in credit counseling and making monthly payments to the Consumer Credit Counseling Agency or other debt pro-rating service instead of paying creditors directly. • The borrower has recently completed credit counseling or other debt service counseling program (less than one year has passed) during which time the counseling agency made payments to creditors on the borrower's behalf.
Bankruptcy	To be considered for a mortgage loan, the borrower's bankruptcy must have been dismissed or discharged (as defined below) and s/he must have re-established a satisfactory credit history and demonstrated the ability to manage financial affairs prudently. ("Satisfactory" means that the most recent rating has a rating of "1".) The bankruptcy should be fully discharged or dismissed as specified below. The mortgage application may not be approved before the following time periods have elapsed from the date of the application: • 4 years from the date the Chapter 7 or 11 bankruptcy was discharged or dismissed; • 4 years from the date a Chapter 12 or 13 repayment plan was dismissed or 2 years from discharge date. A letter of explanation for the bankruptcy is required. **Bankruptcy on the Same Mortgage** If a mortgage debt was discharged through a bankruptcy, the bankruptcy waiting periods may be applied if the appropriate documentation to verify that the mortgage obligation that was discharged in the bankruptcy is obtained. Otherwise, the greater of the applicable bankruptcy or foreclosure waiting periods must be applied. **Multiple Bankruptcy Filings** A 5-year time period must have elapsed from most recent dismissal or discharge date for borrowers with more than one bankruptcy filing within the A 5-year time period must have elapsed from most recent dismissal or discharge date for borrowers with more than one bankruptcy filing within the past 7 years. A satisfactory credit record must be re-established. All bankruptcies must be either dismissed or discharged. **Note**: Two or more borrowers with individual bankruptcies should not be considered cumulative. For example, if the borrower has one bankruptcy and the co-borrower has one bankruptcy, this is not considered a multiple bankruptcy. Documentation Requirements Borrowers who have had a bankruptcy closed within the past 7 years must provide the following: • Copies of the bankruptcy petition, schedule of debts, discharge or dismissal order and the document issued by the court showing the bankruptcy estate is closed.

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Evidence to indicate that all debts not satisfied by the bankruptcy have been paid or are being paid.
Any other evidence necessary to support the determination that the borrower has re-established and maintained an acceptable credit reputation (see Re-establishing Credit).

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<tr><td>Forbearance/repayment Plan</td><td>

Forbearance
A Forbearance plan suspends or reduces the amount of the regular monthly mortgage payment. At the end of the forbearance term, the borrower(s) is responsible for the balloon payment.

Repayment Plan
A repayment plan is an arrangement in which a borrower(s) agrees to repay past due amounts while still making regularly scheduled payments.
Borrower(s) who have been accepted into a Payment Deferral are considered current upon completion of the Payment Deferral.
Borrowers(s) are eligible for new financing upon completion of the payment deferral under a Forbearance or Repayment Plan and if the following criteria are met:
All transactions:

At least 6 months have elapsed since the Forbearance or Repayment Plan was completed; and
Borrower(s) must have made the payments as agreed per the loan forbearance or repayment plan, and
Mortgage history must meet the mortgage history requirements per the product, program and/or process applied, and
Borrower(s) must meet all other requirements per the product, program and/or process applied.

</td></tr>
<tr><td>Foreclosure</td><td>

After 7 years have elapsed, the borrower may obtain a purchase mortgage pursuant to the eligibility requirements in effect at that time. A letter of explanation is required.
When both a bankruptcy and foreclosure are disclosed on the loan application, or when both appear on the credit report, the bankruptcy waiting period may be applied if the borrower provides appropriate documentation to verify that the mortgage loan in question was discharged in the bankruptcy. Otherwise, the greater of the applicable bankruptcy or foreclosure waiting period must be applied.
Note: This topic does not apply to deeded Timeshares.

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<tr><td>Restructured Loan & Modification</td><td>

Restructured Loan
Restructuring a loan is a process where the terms of a mortgage are modified outside the original terms of the contract agreed to by the lender and borrower. It may involve:

A reduction in the interest rate
An extension of the length of time for repayment
Forgiveness of a portion of the principal and/or interest on either the first or second mortgage
Conversion of any portion of the original mortgage debt to a “soft” subordinate mortgage; or
Conversion of any portion of the original mortgage debt from secured-to-unsecured
A different type of loan
Any combination of the above.

Modification

</td></tr>
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	A Modification is a written agreement between a financial institution and a borrower that changes one or more terms of an existing mortgage such as: • Interest Rate • Number of years allowed for repayment • Amount of monthly payment. The goal of the program is to help borrowers who, due to a hardship, are struggling to make their mortgage payments. If the transaction involves the refinancing of a mortgage that has been previously Restructured or Modified, or if the borrower(s) were obligated on a prior mortgage that was restructured or modified, the borrower(s) are eligible for new financing as long as the following criteria are met: All transactions: • At least 6 months have elapsed since the Restructure or Modification was completed; and • Mortgage history and all other requirements per the product, program and/or process selected must be met.
Deed-In-Lieu/Short Sale/ Pre-Foreclosure or Charge-Off of A Mortgage Account	The waiting period (i.e., the amount of time that must pass before the borrower is eligible for mortgage financing), which commences on the completion date of the events, is a minimum of four years with the maximum LTV/CLTV/HCLTV permitted as defined by the product/program selected. • A deed-in-lieu is a transfer of title from a delinquent borrower to the lender in satisfaction of the mortgage debt to avoid foreclosure; also called a voluntary conveyance or typically identified on the credit report through Remarks Codes such as “Forfeit Deed-in-Lieu of Foreclosure.” • A short sale, pre-foreclosure sale or charge-off of a mortgage account is a transaction where the mortgage lender agrees to accept a lower amount than is owed on the property. These are typically identified on the credit report through Remarks Codes such as “Settled for less than full balance and “Foreclosure Initiated.” The loan may or may not be delinquent. Examples of how short sales/pre-foreclosures or charge-off of a mortgage account may be identified on the credit report: • Special Comment Code AU (Account Paid-in-Full for Less than Full Amount Due) • $0.00 Current Balance • Payment rating applicable to the contractual status of the loan at time short sale is processed (i.e., current, 30 days’ delinquent, 60 days’ delinquent, etc.).
Purchase of a Pre-Foreclosure or Short Sale Property	Allowable Fees and Payments Borrowers may pay additional fees or payments in connection with acquiring a property that is a pre-foreclosure or short sale that are typically the responsibility of the seller or another party. Examples of additional fees or payments include, but are not limited to the following: • Short sale processing (also referred to as short sale negation fees, buyer discount fees, short buyer fees);Note: This fee does not represent a common and customer charge and therefore must be treated as a sales concession if any portion is reimbursed by an interested party to the transaction. • Payment to a subordinate lien holder; and

	• Payment of delinquent taxes or delinquent HOA fees. The following requirements apply: • The borrower (buyer) must be provided with written details of the additional fees or payments and the additional necessary funds to complete the transaction must be documented. • The servicer that is agreeing to the pre-foreclosure or short sale must be provided with written details of the fees or payments and has the option of renegotiating the payoff amount to release its lien. • All parties (buyer, seller, and servicer) must provide their written agreement of the final details of the transaction which must include the additional fees or payments. This can be accomplished by using the "Request for Approval of Short Sale" or "Alternative Request for the Approval of Short Sale" forms published by the U.S. Treasury Supplemental Directive 09-09 or any alternative form or addendum. The Closing Disclosure must include all fees and payments included in the transaction.
Credit Inquiries	When reviewing borrower credit history, new accounts and inquiries should always be considered. There may be red flags for multiple liens or other fraud schemes, or an indication that the customer's repayment ability is being compromised by new debt. Inquiries on the credit report generally reflect the borrower's requests for new or additional credit. Inquiries made for other purposes, such as general solicitations not initiated by the borrower or monitoring inquiries by current creditors, typically are not shown on the credit report. The presence of many recent inquiries in combination with a significant number of recently opened accounts, high balance credit utilization, and/or delinquent accounts represent a high credit risk. If the credit report indicates that a creditor has made an inquiry within the previous 90-day period, then MCFI must determine whether additional credit was granted as a result of the borrower's request. A letter from the creditor OR a signed statement from the borrower OR a conversation with the borrower (which must be documented in the loan file) may be used to determine whether additional credit was obtained. **Note:** Letters of explanation that are e-mailed are not required to be signed, refer to the Borrowers Letters of Explanation topic in this section for additional requirements. Inquiries from a source that would not result in a debt included in the DTI calculation do not require written explanation from the borrower. MCFI must verify the unpaid balance, the terms of repayment and the payment history (if applicable). The final loan application signed by the borrower(s) must include all debts that were verified, disclosed, or identified during the loan application process. If new credit was obtained and there is a balance on the new account, the debt must be included in the list of debts and the calculation of DTI ratios, even if the account does not appear on the credit report. **Note**: If new credit is obtained after the loan has been approved, re-underwriting will be required.

<table>
<tr><td>Credit Report Alerts</td><td>Pursuant to the provisions of the Fair and Accurate Credit Transactions Act (FACT Act), consumers have certain rights to protect themselves from the risk of identity theft. Consumers who are victims of identity theft, or who believe they may become victims, or who are on active duty in the military may request that a credit reporting agency pass a fraud or active duty flag to users who request their credit report.

The underwriter is responsible for reviewing each credit bureau report carefully to ensure there are no alerts or “red flags” which would require special attention.

Fraud or Active Duty
A consumer has the right to place a fraud or active duty alert on their credit bureau by following a procedure established by the bureaus. An alert means that someone may have used the consumer’s identity without his or her consent.
MCFI prohibits loans to applicants who have a security alert in their credit file unless reasonable steps have been taken to verify the applicant’s identity. MCFI must follow the instructions provided by the consumer located in the consumer’s credit report before an application can receive further processing, or the borrower may contact the consumer reporting agency and provide the appropriate instructions and identifying information to the credit reporting agency allowing the lender to re-pull a consumer report clear of fraud or active duty alerts. In some instances the consumer will need to be contacted by phone to verify identity.
Reminder: The borrower may not be automatically declined due to the presence of such alerts.

Address Indicators
The credit reporting agencies indicate when the applicant’s address provided by a creditor differs, or is a variation, from the address on the credit report.
Often there is a simple and logical explanation. However, such discrepancies may be red flags for fraudulent activity.
Address Discrepancy Alert - This alert occurs when the applicant’s address is a variation of the address the credit bureau has on file, or the credit bureau address history reflects other addresses reported during the same time period as the inquiry address.
Address Mismatch Alert - This alert occurs when the applicant’s address does not show up on the credit bureau report. This indicates the inquiry address is a new address for the applicant’s credit profile, as the address does not match or has never been reported to the credit bureau before.
All discrepancies/mismatch addresses must be reviewed and resolved.
Frozen/Locked Credit must be unfrozen, and credit files must be released.</td></tr>
<tr><td>Derogatory Credit</td><td>The presence of significant derogatory credit information dramatically increases the likelihood of a future default and represents a significantly higher level of default risk. Examples of significant derogatory credit events include bankruptcies, foreclosures, deeds-in-lieu of foreclosure, pre-foreclosure sales, short sales, and charge-offs of mortgage accounts.</td></tr>
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	MCFI must determine the cause and significance of the derogatory information, verify that sufficient time has elapsed since the date of the last derogatory information, and confirm that the borrower has re-established acceptable credit history. A written explanation for significant derogatory credit must be documented along with supporting exhibits as defined throughout this section. All letters of explanation must be signed by the Borrower prior to close. The underwriter should determine if a letter of explanation is required for minor derogatory credit or an isolated incident that is not representative of the borrower's overall credit history/ profile. The underwriter should explain in their rationale if a letter is not being required. Note: Mortgage payments missed during the time of a COVID-19 related Forbearance do not have to be considered as mortgage lates and do not have to be considered significant derogatory credit as outlined below. Significant Derogatory Credit The following scenarios are examples of what may be considered "Significant Derogatory Credit" and, therefore, require a written explanation from the borrower. • There are several accounts showing recent late payments; • There is multiple 60- or 90-day late payments; • There is more than one 30-day late housing payment in the last 12 months; • There are more than two 30-day or more than one 60-day late housing payments within the most recent two years; • The number and size of the delinquent accounts are large in relation to the overall credit; • There are multiple episodes of late payments extending over a period of time; • The credit history shows derogatory credit information within the two most recent years combined with multiple revolving accounts with high balances-to-limits; • The public record information reveals several occurrences of derogatory credit information, including judgments, tax liens and/or collection accounts; • There is a bankruptcy filing, foreclosure, pre-foreclosure sales, mortgage charge-offs, deed-in lieu of foreclosure, short sale within the last seven years, or accounts that have been turned over to a collection agency.
Discrepancies	When a credit report does not include a reference of a debt the borrower reported on the loan application, separate written verification for each unreported debt is required. Accounts listed on the credit report as "will rate by mail only" or "need written verification" also require separate verification. If debt shows up on the credit bureau that was not on the application, no explanation is required. However, it should be included on the application and included in the debt ratios.

	Written explanation may be required depending on the documentation process selected. All letters of explanation must be signed by the Borrower prior to close.
Disputed Credit Obligations	Disputed trade lines or public records adverse to the credit profile require a written explanation from the borrower including evidence to support the dispute. If the account in question adds risk, such as stolen/fraudulent use of the account, the evidence must include documentation and verification of the account status (i.e., current balance, delinquency, etc.) from the creditor or credit bureau. All written letters of explanation must be signed by the borrower prior to close. Refer to the Borrower Letters of Explanation topic in this section for more information. **Note:** If the account or public record is medical, a letter of explanation and evidence is not required, as dictated in FCRA - Regulation V: Medical Information Privacy Act. Past Due Accounts An explanation is required, and all past due accounts must be paid prior to closing. Incorrect Information If a borrower states the information on the credit report is incorrect or does not belong to the borrower and the information reflected is deemed to be of material significance (e.g., delinquent credit obligation, public records or trade lines that do not belong to the borrower), the borrower must provide documentation from the creditor or the credit bureau evidencing that a dispute has been initiated for the identified account(s). All written letters of explanation must be signed by the Borrower prior to close. Refer to the Borrower Letters of Explanation topic in this section for more information. A subjective review must be performed as part of the underwriter's risk analysis.
Borrower Explanations (LOX)	A written explanation from the borrower is required for the following: • All Significant Derogatory Information. The purpose for requiring a written explanation is to assist the underwriter in determining whether the Borrower's credit problems were due to extenuating circumstances (factors clearly beyond the control of the Borrower) or whether they reflect financial mismanagement (the Borrower's disregard for the payment of obligations when due). • Temporary Leave: The borrower must provide written confirmation of their intent to return to work and the agreed upon date of their return. • Gap in Employment: The borrower must provide a written explanation when there is a gap in employment of 30 days or more.
Credit Utilization	MCFI must review the borrower's credit report to evaluate his/her use of revolving credit by comparing the current balance on each open account to the amount of credit that is available to determine whether the borrower has a pattern of using revolving accounts up to (or approaching) the credit limit. The higher the borrower's overall utilization of revolving credit the higher the amount of risk. (Note: The lack of adverse or derogatory

	credit information may not be used as an offset for high balance-to-limits or high overall utilization of revolving credit.)
Garnishments/Judgements & Tax Liens / Public Records /Lawsuits	**Garnishments** • A garnishment occurs when an employer or other asset holder is required to send/ apply borrower monies, wage, or property directly to a specific debt or creditor. This is often, but not always, brought about by the non-payment of a debt. The underwriter should find out the reason for the garnishment, document explanation (in writing or verified via telephone) and continue processing. If the borrower has a garnishment, the monthly debt should be included in the total debt ratio. **Note**: Garnishments do not need to be paid off prior to or at close. **Judgements & Tax Liens/Public Records** • Borrower must pay off all delinquent credit—including delinquent taxes, judgments, charged-off accounts, tax liens and mechanics or materialmen's liens—that have the potential to affect lien position or diminish the borrower's equity. • Borrowers with previous judgments must provide evidence of payment in full or evidence the judgment no longer represents a claim against the borrower. The borrower must provide satisfactory written explanation along with any supporting documentation, as needed. All letters of explanation must be signed by the Borrower prior to close. Loan proceeds may be used to pay off judgments or tax liens at closing by the title company; pay off must be documented on the Closing Disclosure. **Lawsuits** • The fact that there is a lawsuit pending does not mean that the borrower is guilty of the claim. Until the court has made a ruling on the case, there is no judgment or lien. However, the type and extent of the lawsuit and whether it could impact our first lien position, may increase the risk, therefore the loan should be evaluated carefully before rendering a decision. A written explanation and a copy of the filed complaint pertaining to the lawsuit are required. All letters of explanation must be signed by the Borrower prior to close. Refer to the Borrower Letters of Explanation topic in this section for more information. Additional documentation may be required depending on the type of lawsuit and the borrower's involvement.
Unpaid Charge-offs & Collection	The unpaid charge-off and/or collection is required to be satisfied as defined below. An explanation from the borrower is required. Proceeds from a cash-out refinance transaction may be used to satisfy the unpaid charge-off and/or collection at closing. An account may be paid at closing, for a purchase or rate/term refinance transaction, if all of the following requirements are met: • The payoff should be documented on the Closing Disclosure And match documentation in the loan file; and • The loan must contain documentation as to why the account(s) could not be satisfied prior to the loan closing; and

	• Under no circumstances may the proceeds of the loan be used to pay the unpaid charge-off or collection account unless the transaction is a cash-out refinance. The total balance of all outstanding collections is ≤$2,000; or • If the total outstanding balance of all collections is >$2,000, Then 5% of the balance of each outstanding collection account for all borrowers must be included in the calculation of the total debt ratio. • The charge off has not reached a judgment or lien status; and • The borrower has documented evidence of the dispute if it is a disputed account. If none of the above criteria are met, then the collection/charge-off must be paid prior to or at loan closing.
Payment Of Past Mortgages / Rent	How the borrower has handled present and prior mortgage/ rent payments provides useful insight as to how the new mortgage will be managed. In addition to the new mortgage payment, the underwriter should also examine the payment history and the amount/ percentage the monthly payment will increase. • The credit report must contain the entire mortgage payment history. If the report covers activity for the previous 12 months or longer, we may rely on the credit report for the verification. If it does not, we must obtain the history directly from the mortgage servicer or get 12 months cancelled checks (front and back). **Verification of Rental Payments:** A verification of rental history is required on all transactions via: • Copies (front & back) of twelve (12) months consecutive (one (1) payment per month) rental payment cancelled checks; or • Bank statements or direct payment records showing one (1) payment per month; or. • A professional management company must provide verification in writing (VOR); or • Residential mortgage credit report ("RMCR") or merged in-file report. • The rental payments must be current on the date of the loan application. Borrowers unable to provide a complete twelve-month (12) mortgage/rental history are limited to owner occupied primary residences only. If the landlord is related to the borrower, twelve months of cancelled checks must be provided. The rental history must reflect 0 x 30 in the previous twelve (12) months. **Note:** Verifications performed by a party other than a professional management company are not permitted. The management company must be listed in the local telephone directory and the file must contain a copy of the list. If the listing is not available, 12 months cancelled checks must be provided. Existing Mortgage Payment Requirements A verification of mortgage history is required on all transactions and must contain current balance, status and payment amount verified via:

	• A third party or credit bureau; or • Verification of mortgage completed by the holder of the mortgage is acceptable. • On the date of the loan application, the borrower's mortgage payments (first and second) on the subject property must be current. • On the date of the loan application, the mortgage history must reflect 0 x 30 in the previous twelve (12) months. "Rolling" Mortgage late pays are not permitted. • In case of a recent refinance or account transfer, a combination of payment performance from multiple lenders for the same collateral may be used to complete the twelve-month (12) history requirement. • For a recent purchase, a combination of payment performance from a prior property or rental payments may be used to complete the twelve-month (12) history. A gap in mortgage/rental payment history of up to six (6) months is allowed by obtaining the most recent eighteen-month (18) history and providing written documentation explaining the reason for the gap. • ~~For each mortgage liability where the borrower is currently an obligor on the note secured by real estate debt, a verification of mortgage must be obtained if the mortgage is not verified on the credit report.~~ **Note**: If there is a new debt being incurred from a pending purchase transaction, the TIL, GFE, Loan Estimate or other alternative documentation from the lender should be obtained to verify the new monthly payment amount.
Purchase of a Pre-Foreclosure or Short Sale Property	Allowable Fees and Payments Borrowers may pay additional fees or payments in connection with acquiring a property that is a pre-foreclosure or short sale that are typically the responsibility of the seller or another party. Examples of additional fees or payments include, but are not limited to the following: • Short sale processing (also referred to as short sale negation fees, buyer discount fees, short buyer fees); Note: This fee does not represent a common and customer charge and therefore must be treated as a sales concession if any portion is reimbursed by an interested party to the transaction. • Payment to a subordinate lien holder; and • Payment of delinquent taxes or delinquent HOA fees. The following requirements apply: • The borrower (buyer) must be provided with written details of the additional fees or payments and the additional necessary funds to complete the transaction must be documented. • The servicer that is agreeing to the pre-foreclosure or short sale must be provided with written details of the fees or

	payments and has the option of renegotiating the payoff amount to release its lien. • All parties (buyer, seller, and servicer) must provide their written agreement of the final details of the transaction which must include the additional fees or payments. This can be accomplished by using the "Request for Approval of Short Sale" or "Alternative Request for the Approval of Short Sale" forms published by the U.S. Treasury Supplemental Directive 09-09 or any alternative form or addendum. The Closing Disclosure must include all fees and payments included in the transaction.
Re-Establishing Credit	Following are the requirements that the borrower must meet to re-establish credit after a significant derogatory event. Note: After a bankruptcy, foreclosure, deed-in-lieu of foreclosure, pre-foreclosure sale or charge-off of a mortgage account, the borrower's credit will be considered re-established if all the following are met. • The waiting period for the event along with related requirements have been met. • The borrower has met traditional credit as defined in Credit History/Minimum Trade Lines topic above. • Non-traditional credit or "thin files" are not permitted.

LIABILITIES	
Types of Recurring Debt	Debt is defined as borrowed money, the repayment of which may be either secured or unsecured, with various possible repayment schedules. The following items are examples of recurring debt. It is important to note that the debt may or may not need to be included in the borrower's debt-to-income ratios. • Alimony / Maintenance • Borrowed Funds Against Financial Asset • Business Debt • Child Support • Contingent Liabilities (Co-Signed Debt) • Court Ordered Assignment of Debt • Deferred Loans • Demand Loans • Installment Loans • Leased Obligations • Mortgage Assumption • Net Rental Loss • Non-Reimbursed Business Expense • Overdraft Protection Account • Payroll Deductions • Real Estate Obligations: Departure Property • Real Estate Obligations: Verification of Mortgage Debt • Revolving Debt

	• Special Assessment • Student Loans • Subordinate Financing • Unsecured Loans Note: The recurring debts above must be verified on all purchase and refinance transactions.
Debt Payoff / Consolidation	• Installment loans that are being paid off do not have to be included in the borrower's long-term debt. • Payoff of revolving debt to qualify is not permitted. The debt listed on the credit report must be used to calculate the DTI. If all or any portion of the proceeds of the Mortgage is used to pay off or pay down existing debts (installment) in order to qualify for the Mortgage, payoff must be documented. Cancelled checks, paid receipts and/or a copy of the Closing Disclosure form or other closing statement may be used to document the repayment. When the borrower pays off or pays down an existing debt in order to qualify, the source of funds used must be verified, and meet eligibility requirements for both purchases and refinances. See Asset Verification Requirements for additional information.
Alimony & Maintenance	Monthly alimony obligation should be treated as a recurring debt. Acceptable sources of documentation include a copy of: • Applicable page(s) and signature page of the divorce decree, or • Signed court order, or • Property settlement, or • Separation agreement. If payments are being paid through the court, a letter from the court verifying the dollar amount is sufficient. Obligations that will end within the next 10 months do not need to be considered. However, the size and number of remaining payments should not impact the borrower's ability to handle the new mortgage payment during the early period of the loan.
Borrowed Funds Against Financial Asset	The borrower may take a loan against a liquid asset that is secured by stocks, bonds, or any other investment account, life insurance policies, 401(k) accounts, CDs, or other financial assets. Although information regarding the amount of the loan must be provided, the debt is not generally counted in the borrower's qualifying ratios if the loan instrument shows the asset as collateral for the loan, since the loan may be repaid by liquidating the asset. Financial institution must have made the loan. The borrower may only use assets in the account that exceed the loan balance to satisfy cash reserve requirements. Payments on installment debts secured by cryptocurrency must be included in the monthly debt ratio.
Business Debt	A business debt is a financial obligation of a business and can be the sole responsibility of the business or personally secured by the business owner, which makes that person also liable for the debt. If the debt is reflected on the borrower's personal credit report, the borrower is personally liable for the debt, and it must be included in the debt-to-income ratios. Debts paid by the borrower's business do not have to be included in the debt-to-income ratios if: • The borrower provides 12 months cancelled checks drawn against the business account; and • The account in question does not have a history of

	delinquency; and • Two years' personal, partnership, and/or corporate tax returns evidencing that business expenses associated with the debt support that the debt has been paid by the business must be obtained; and • The underwriter's cash flow analysis of the business took into consideration the payment of the obligation (included interest expenses, and taxes and insurance, if applicable, that one would reasonably expect to see based on the loan balance and age of the loan). **Note**: The debt must be included in the borrower's debt ratios, if the tax return analysis of the business does not reflect any business expense (including taxes and insurance, if applicable), equal to or greater than the amount of interest that one would reasonably expect to see given the amount of financing shown on the credit report and the age of the loan. If the debt is not included in the borrower's debt ratio, the loan must be reviewed to confirm income is independent of the borrower and the business can continue to cover the debt for the next three years. If the above requirements are not met, the payment needs to be included in the total debt ratio. In lieu of cancelled checks, a letter from a CPA providing specific account number(s) and verification that the business has paid the debt for the past 12 months is acceptable.
Child Support	Payments of child support are counted as recurring debts. Acceptable sources of documentation include a copy of: • Applicable page(s) and signature page of the divorce decree, or • Property settlement, or • Separation agreement. If payments are being paid through the court, a letter from the court verifying the dollar amount is sufficient. Obligations that will end within the next 10 months do not need to be counted in debt-to-income ratio. However, the size and number of remaining payments should not impact the borrower's ability to handle the new mortgage payment during the early period of the loan. Borrowers with current or previous past due child support must provide evidence that all past due payments are current unless the borrower is making the payments according to a court approved plan. In this case, the borrower must demonstrate that payments are current according to the plan.
Contingent Liabilities: Paid by Others	A contingent liability being paid by others may be excluded from the monthly debt payment ratio when meeting the following requirements: **INSTALLMENT DEBT (not including mortgages), REVOLVING, OR MONTHLY LEASE PAYMENT:** • The most recent 12 months' cancelled checks or bank statements from the party making the payments, • There must be no delinquencies in the most recent 12 months, and

	• The party making the payments cannot be an interested party to the subject real estate or mortgage transaction **<u>MORTGAGE PAYMENT OR OTHER PROPERTY RELATED EXPENSES (taxes, insurance, homeowners association dues):</u>** • The party making the payments must be obligated on the note, • The most recent 12 months' cancelled checks or bank statements from the party making the payments, • There must be no delinquencies in the most recent 12 months, • The borrower is not using rental income from the property to quality, and • The party making the payments cannot be an interested party to the subject real estate or mortgage transaction. **<u>COURT-ORDERED ASSIGNMENT OF DEBT:</u>** When a borrower has outstanding debt that was assigned to another party by court order (such as under a divorce decree or separation agreement), regardless of whether the creditor has not released the borrower from liability, the lender is not required to count this contingent liability as part of the borrower's recurring debt obligations. • Lender must document the order with a copy of the appropriate pages from the divorce decree or separation agreement. Note: The above policy for court ordered assignments of debt and property settlement buyouts should never apply to debt secured against the subject property. In these instances, debt must ALWAYS be counted in the debt ratio calculation.
Deferred Loans	Installment debts with deferred payments include debts on furniture, household items, and automobiles for which the initial payment is delayed for a period of time as part of a merchant's promotional campaign. For student loans refer to the Student Loans topic later in this section. For deferred installment debts, the payment amount that will be required once the deferment or forbearance period has ended must always be included as part of the borrower's recurring monthly obligations. If the credit report does not indicate a monthly payment at the end of the deferment period, the following documentation should be requested: • A direct verification from the creditor; or • A copy of the installment loan agreement obtained from the borrower.
Demand Loans	A demand loan has no monthly payment; it becomes due and is payable in full on a particular date. This type of debt may or may not be secured. • If the notice is due within the next 2-years and the borrower does not have adequate reserves available to repay the obligation in full, the transaction should be treated as an installment loan. A minimum payment of 5% of the unpaid balance must be included in the debt-to-income ratio.

	• If the borrower does have adequate reserves available to pay the obligation in full, the debt should not be included in the debt-to-income ratio.
Installment Debt	Installment debt is borrowed money that is repaid in several successive payments, usually at regular intervals, for a specific amount and for a specified term (e.g., an automobile or furniture loan). • Installment debts with monthly payments that extend beyond 10 months (and debts that are in a period of either deferment or forbearance for agency loans) must be included in the debt-to-income ratio for qualification purposes. • Even if the debt does not extend beyond 10 months, it must be noted whether the size and/or number of remaining payments will impact the borrower's ability to handle the new mortgage payment during the early period of the loan. • If debt is paid by the borrower's business, it does not need to be included as a liability if it meets the requirements in the Business Debt topic above.
Leased Obligations	A lease is a written document containing the conditions under which property (most often an automobile or land) is given to an individual for a specific period of time (term). • The monthly payment for the leased item should always be counted as a recurring debt regardless of the remaining term. • If lease is paid by the borrower's business, the debt does not need to be included as a liability if it meets the requirements in the Business Debt topic above. Pre-Paid Leases - If the borrower fully pre-paid the terms of their lease at the original time the Lease Agreement was executed, the monthly payment for the lease does not have to be included in his/her recurring debt obligations provided the borrower's assets are reviewed and no undisclosed obligations are reflected. The file should be documented with the terms of the lease and the Underwriters rationale for not including a monthly payment in the DTI.
Mortgage Assumptions	For a contingent liability on a Mortgage Assumption, the liability must be included in the DTI when the borrower has sold a property as an assumption without a release of liability being obtained.
Net Rental Loss / Negative Rent Income	If real estate is owned free and clear, only current real estate taxes, hazard insurance premiums, and homeowners' association fees must be included in the borrower's monthly expenses. The borrower must supply a copy of the homeowner's insurance policy declaration page or other documentation that clearly evidences the current property is free of encumbrance. If any documents in the file indicate that the property has a mortgage, it must be verified, and the payment history supplied. The amount of the negative cash flow calculated from the tax return must be included in the borrower's debt-to-income ratio.
Non-Reimbursed Business Expenses	When a borrower has non-reimbursed business expenses that are being analyzed, such as meals, gasoline, auto insurance and/or taxes, a recurring monthly debt obligation should be developed based on a 24-month average of the expenses (from Schedule A and IRS Form 2106 from the tax returns).

	Automobile depreciation may be netted out. Union dues shown as an expense on the 2106 do not need to be treated as a reduction to total income. The 24-month average should be deducted from the borrower's stable monthly income. Automobile loan payments and automobile lease payments that are included as non-reimbursed expenses on the tax returns may not be deducted from income. They must be included as recurring debts in the total debt ratio. • If the borrower claims a "standard mileage" deduction, multiply the business miles driven by the depreciation factor for the appropriate year as published by the IRS, and add that figure back to the calculation. • If the borrower claims an "actual depreciation expense" deduction, the amount the borrower claimed should be added back. Note: Non-reimbursed expenses should be deducted from the income that is being used to qualify and should not be considered in the 20% tolerance between the income documentation provided by the borrower and the income documented on the IRS Transcript
Overdraft Protection Account	Overdraft protection is considered a revolving line of credit (given without the benefit of security) that is attached to a checking account. If there is a balance, count a minimum payment in the debt-to-income ratios.
Payroll Deductions	Any time a payroll deduction appears on the borrower's pay stub, the underwriter must determine if the deduction represents a debt that must be included in the debt ratio. Examples of such debts include, but are not limited to: Credit Union or employer loans, garnishments, child support, etc. The following information may assist in making the determination: • Monthly payment of the debt • Balance of the debt • Reason the debt is being deducted from payroll • All guidelines regarding the debt
Revolving Debt	Revolving debt is an arrangement for credit in which the borrower is granted a credit limit and can use any amount up to the limit. Repayment is usually at regular intervals but not for a specified amount or term. Credit cards are an example of revolving debt. The following must be included in the debt-to-income ratio: • Minimum payment (from statement or credit report); or • The greater of 5% of the current balance, or $10, if no payment Is stated on the credit report. If multiple account payments are not reported, and/or the borrower's ratios are at the maximum permitted for the process selected, MCFI should obtain actual minimum payments from the borrower's account statements to qualify the borrower. **Open 30-Day Charge Accounts**: On all 30-day accounts, also referred to as open accounts (e.g., Diners Club, American Express), the full amount of the outstanding balance must be included in the debt payment ratio, or verification that the borrower has sufficient funds to pay off the outstanding account balance must be provided. The funds must be in addition to any funds needed for cash to close.

	"**Authorized User of Credit" Accounts**: Payments on "Authorized User" accounts should always be included in the debt-to-income ratio unless written documentation (i.e., 12 months cancelled checks) is provided proving that the owner of the account is making the payments. **Fees Paid Outside of Closing (POC)** The applicant may charge the total fees due on a credit card, regardless of the amount. When more than 1% is charged and the borrower does not have sufficient liquid funds to cover the charge, then the credit card payment must be re-calculated and the new payment included in the DTI. To recalculate the new POC debt one of the following is required: • Credit Card Receipt: Obtain credit card receipt and use 5% of the POC amount in addition to the payment on the credit report for any current balance; or • Card Statement with the POC Charge: Obtain a copy of the credit card statement showing the amount charged, the outstanding balance and the terms of repayment. Fees POC include lock-in fees, origination fees, commitment fees, credit report fees, and appraisal fees. Borrowers are not required to pay off these credit card charges on or before closing. Under no circumstances may credit card financing be used for the down payment.
Special Assessments	If the property is located in a special assessment district, the locality has the right to assess homeowners for the cost of developing utilities and various infrastructure facilities such as roads, sewers, etc. (e.g., "Mello Roos" school tax.) Any special assessment amounts indicated on the appraisal or in the title work must be included in the borrower's total debt ratio. If the underwriter learns that the special assessment district may be having financial difficulties, the underwriter should evaluate the borrower's ability to repay the mortgage in the event additional assessments are imposed. If special assessments are in arrears, documentation must be obtained to show they have been paid, or that sufficient deposits to cover such amounts are being collected. **MCFI requires an escrow account for the payment of special assessments.**
Student Loans	Repayment of all student loans must be included in the debt-to-income ratio, unless 10 months or fewer payments remain. See Installment Debt section for requirements when not including the payment in the debt to income ratios, if 10 months or fewer payments remain. For deferred student loans, the payment amount that will be required once the deferment or forbearance period has ended must be included as part of the borrower's recurring monthly obligations. To calculate the payment used for qualification. In all cases, an amount greater than zero must be included in the monthly debt payment-to-income ratio for all student loans. • Use the greater of the payment showing on the credit report or 1% of the outstanding balance of all of the loans reported, or • When student loan documentation is received use the monthly payment reflected on the student loan documentation as long as the payment reflected is greater than $0, which should include all loans

	showing on the credit bureau (i.e., a copy of the installment loan agreement or the most recent student loan statement). o For Income Driven Repayment Plans: If documentation is received in the loan file and shows the payment will increase the higher payment must be used to qualify.
Subordinate Financing	If the subject property has an existing subordinate lien, the existing lien may be subordinated to the new "refinance" transaction. **Note:** Subordinate financing may not contain negative amortization financing structure and may not have any special servicing requirements. **Eligibility** Subordinate financing is any type of financing which creates a subordinate lien on the same property for which we are originating a first mortgage. Funds from subordinate financing may be used for a variety of reasons, including: • Supplementing the down payment • Payment of closing costs • Setting up a Permanent Buy Down • Repairing/improving the subject property If the loan is secured by the subject property, subordinate financing, and LTV parameters for the first mortgage must be enforced. Any lien against the subject property other than the first mortgage must be acceptable to MCFI, clearly subordinated to the first mortgage lien, and properly recorded. The monthly payment on the subordinate lien should be included with the PITIA on the subject property, if applicable, when calculating the monthly housing ratio. **Note:** Small Business Administration (SBA) subordinate financing is not allowed. If funds are from a subordinate lien that is secured by another property, we need not be concerned with the type of financing or combined LTV parameters, but we must include the monthly payment in the back end qualifying ratio. All terms of the note and the security instrument for the subordinate financing must be acceptable. **Documentation Requirements** • For purchase transactions, and refinance transactions where subordinate financing is originated concurrently with the first mortgage (either new subordinate financing or refinance of an existing subordinate lien), all the following subordinate financing documentation must be included in the loan file as applicable for each loan: o Note or other evidence of subordinate lien terms; and o Closing Disclosure or other closing statement; and o For HELOCs, the HELOC agreement indicating all fees and costs paid by the borrower at closing, and the maximum permitted credit advance. • For refinance transactions, if an existing subordinate lien is not paid off, it must be re-subordinated to the new first lien, and a copy of the recorded subordination agreement must be maintained in the loan file. The note or other evidence of subordinate lien terms must be included in the loan file, so terms can be appropriately disclosed as indicated below.

	Underwriter must review the terms of the note and the security instrument for the subordinate financing to make sure the terms are acceptable. **The subordinate financing must provide for the following:** • Regular payments of principal and interest, OR regular payments of interest only so that negative amortization does not occur. • If the repayment terms provide for a variable interest rate, the monthly payment must remain constant for each 12-month period over the term of the subordinate lien mortgage. • Interest rate should be at market rate. • If the subordinate lien contains a maturity date or balloon or call provision within the five-year period after the note date of the first lien, it must be fully amortizing under a level monthly payment. (May be less than 5 years if the subordinate debt is minimal in comparison to the borrower's financial assets and/or credit profile. E.g., borrower's financial situation supports ability to pay off or refinance within the balloon period.) • Be recorded and subordinate to the first mortgage lien. **Disclosure Requirements** Lender must disclose the existence of subordinate financing and the terms of repayment (including note rate, repayment terms, and the institution providing the financing) to the appraiser, the mortgage insurer, and the investor. Lender may not indicate to the appraiser a value or loan-to-value needed to support the transaction. **Maximum Combined Loan Amount** There are no restrictions on the combined loan amount. The first mortgage transaction must meet LTV/CLTV/HCLTV and loan amount guidelines for the program selected. **Calculations** • CLTV: Calculate the CLTV by adding the first mortgage loan amount plus the current balances of all subordinate financing, divided by the lower of the appraised value or purchase price. • HCLTV: Calculate the HCLTV by adding the first mortgage loan amount, plus the total amount of all subordinate financing, including the entire available home equity line amount, divided by the lower of appraised value or purchase price. If the HELOC has been modified, a copy of the modification agreement must be obtained in order for the lower, modified total line amount to be used in the HCLTV calculation. The amount on the modification agreement and the subordination agreement should also match. **Minimum Down Payment Requirements**: The minimum down payment requirement for a transaction is based on the CLTV, not the HCLTV, so if the CLTV is 80%, a 10% down payment would be required, regardless of what the HCLTV is. **Note**: Borrowers must use their own funds to meet the minimum borrower down payment or contribution requirement for the loan transaction. **Note**: Subordinate financing may be paid off or paid down by the title company at closing; the amount paid off/down must be shown on the HUD-1/Closing Disclosure. Additional evidence of payoff/pay down is not required.

	Subordinate financing may not have the following: • Negative amortization • Have special Servicing requirements. • Terms that restrict prepayments or provide for a prepayment penalty, except as indicated above. • Does not fully amortize under a level monthly payment plan when the maturity or balloon payment date is less than five years after the note date of the new first mortgage.
Real Estate Obligations: Departure Property	The reserve requirements for the subject property must be applied in addition to the Departure Property policies defined below: **Current principal residence is pending sale or up for sale but the transaction will not be closed (with title transfer to a new owner) prior to the new transaction (evidence that property is up for sale or pending sale is required):** The following reserve requirements must be met for all loans: • If the borrower can qualify with both properties in DTI, count both payments plus two months PITIA reserves for the departure property. • If the borrower cannot qualify with both properties in DTI: • If there is an accepted contract, a minimum of 6 months PITIA reserves on the departure property in addition to the reserves required for the transaction is required and payment on the departure property does not have to be included in the DTI. • If there is no contract on the departure property, a minimum of 24 months PITIA reserves for the departure property in addition to the reserves required for the transaction is required and the payment on the departure property does not have to be included in the DTI. **The current principal residence is being converted to a second home:** • The PITIA for the current and proposed mortgage payments must be used to qualify the borrower for the new mortgage loan; and • Minimum of 6 months of PITIA reserves are required for the departure property in addition to the reserves required for the transaction. **The current principal residence is being converted to an Investment Property:** If the borrower qualifies with the PITIA for the departing property and the PITIA for the new proposed mortgage payment, the borrower must have six months PITIA reserves for the departure property in addition to the reserves required for the transaction. To determine if rental income may be used to qualify, equity must be documented with one of the following: • A current appraisal (2055 or better), minus any liens. The appraisal may not be dated more than 180 days prior to the note date; or • By comparing the original sales price of the departure property to the current unpaid principal balance. • If 25% or more equity is in the departure property:

	○ 75% of the rental income can be used to calculate rental income. Refer to Calculating Rental Income on Non-Subject Property for complete information, and the following must be obtained: ✓ A copy of the fully executed lease agreement; and ✓ Twelve months of PITIA for the departure property is required to be in reserves in addition to the reserves required for the transaction, and ✓ If the borrower does not have a 2-year history of managing an investment property a minimum 760 FICO is required. • If less than 25% equity in the departure property: rental income may not be used to qualify. ○ Both the current and the proposed mortgage payments must be used to qualify the borrower for the new transaction; and ○ 6 months of PITIA for are required for the departure property in addition to the reserves required for the transaction.
Real Estate Obligations: Verification of Mortgage Debt	For each mortgage liability where the borrower is currently an obligor on the note secured by real estate debt, a verification of mortgage must be obtained if the mortgage is not verified on the credit report. Note: If there is a new debt being incurred from a pending purchase transaction, the TIL, GFE, Loan Estimate or other alternative documentation from the lender should be obtained to verify the new monthly payment amount. If there are any mortgage interest deductions or payments on the borrower's personal tax returns (if tax returns are in the file) it must be determined if the borrower is obligated on an undisclosed mortgage, and if so, the mortgage must be verified. **Real Estate obligations that do not meet the criteria for utilizing rental income as stated in the Rental Income section:** The PITIA must be included in the debt ratio for qualifying. Standard with Bridge Loans – refer to the Bridge Loans topic. Note: "Current mortgage payments" as used below includes payments for bridge loan financing secured by the current residence. Reserve requirements must also include payments on the bridge loan, if applicable.
Minimum Reserve Requirements	If a borrower has multiple properties, the following reserve requirement must be satisfied for all of the borrower's Mortgage Loans: In addition to the reserve requirements specified in the LTV Matrices and Program fact sheets for the subject property, 2 months PITIA is required on each additional residential property with a lien (i.e., primary residence, second home, and investment property). Cash-out amount to be received at closing may not be used to satisfy reserve requirements.

	Reserves must be cash or marketable securities. Retirement assets can be used if it meets Fannie Mae guidelines.

ASSETS	

Asset Verification Requirements	Assets must be verified to ensure the borrower has sufficient funds to complete the mortgage transaction and if required, adequate reserves after closing. Assets must be liquid, calculated, and documented.
	The source of funds for all large deposits made into accounts that will be used to fund the down payment, closing costs, or to establish required reserves.
	When the borrower is required to make a down payment, the source of assets must be seasoned for at least sixty (60) days before the date of the loan application.
	The two most recent consecutive months' bank statements and/or other documents are required to verify assets to close.
	Verifications must be no more than 45 days old at the time of application AND no more than 90 days old at closing for existing or new construction.
	The most recent statement date should be used to determine the documentation expiration date. (E.g., May and April statements required. The May statement would be used to determine the document expiration date.) Quarterly asset statements must be dated within 90 days of the initial loan application. The underwriter should also make certain that qualifying assets used from the quarterly statement are not counted twice (e.g., funds from the quarterly asset account transferred to a more recent/current verified account).
	
	Documentation Methods
	• Written Verification of Deposit (VOD) Form: A written VOD may be used to verify deposits. The VOD must be faxed or mailed to/from Lender directly to/from the borrower's deposit institution. It may not be hand delivered by the borrower or loan officer.
	• Account Statements: Copies of bank statements or investment portfolio statements that cover activity in the borrower's account(s) and, if applicable, copies of the most recent retirement account statement that is available, which may be obtained directly from the borrower. The statements must:
	  ○ Clearly identify the borrower as the account holder;
	  ○ Include at least the last four digits of the account number;
	  ○ Include the time period covered by the statement/printout;
	  ○ Include all deposits and withdrawals transactions (for depository accounts);
	  ○ Include all purchase and sale transactions (for financial portfolio accounts); and
	  ○ Include the ending account balance.
	• Internet Downloads: Documents that are faxed or downloaded from the Internet must clearly identify the name of the institution and the source of information…for example, by including that information in the Internet or fax banner at the top of the document.

	• Letters: A letter statement is usually generated when an attorney or trustee, insurance company, or employer manages the asset. The most frequent types of accounts that make use of letter statements include: trust funds for the benefit of the customer, cash value of life insurance, present value of an annuity or current value of a 401k. • Printouts: Printouts obtained from a depository institution are acceptable. However, if the printouts do not contain all the information that is found on account statements (e.g., bank name, logo, account number, etc.). The printouts are only acceptable if they are signed and dated by a representative of the deposit institution. • Faxed Documents: If MCFI has not viewed or copied the original documents directly, the source of the information should be verified via telephone with the borrower's financial institution. The documents must clearly identify the institution and the source of the information must be included in the "fax" banner that is at the top of the document. • E-Mail: If MCFI has not viewed or copied the original documents directly, verify the source of the information via telephone. • Third-Party Verification Service Providers: The borrower must provide the proper authorization for MCFI to use this verification method. The verification must contain the same information and meet the same requirements as reflected on a Verification of Deposit or Account Statements as noted above. If any required information is missing, additional documentation to supplement the third-party verification must be obtained.
1031 Like Property Exchange	1031 Exchange—Tax Deferred or Like Property Exchange—is an exchange of real property in which no taxable gain or loss is recognized at the time of sale. Section 1031 of the Internal Revenue Code allows investors to defer the payment of state and federal capital gains taxes by exchanging one investment property with another, rather than selling it. A 1031 exchange is an investment property exchange therefore primary residences and second home transactions are not permitted. We will permit a 1031 tax deferred exchange to be used as the down payment for the purchase of an investment property with the following restrictions: • The 1031 exchange is properly documented and is in compliance with Internal Revenue Code Section 1031. • There is no subordinate financing. • A qualified intermediary must handle the loan closing. A qualified intermediary is an entity (usually a subsidiary of a title company) who enters into a written agreement with the taxpayer. The qualified intermediary cannot be an agent, attorney, accountant, investment banker or broker. This exchange agreement requires the qualified intermediary to acquire and transfer the relinquished property and to acquire and transfer the replacement property. The relinquished property is the property "sold" and the replacement property is the property "acquired". • Copies of all closing documents—including the 1031 exchange agreement, settlement statement, and title transfer—and the

	purchase agreement on the relinquished property must be obtained. • Both purchase agreements on the relinquished and replacement properties must contain appropriate language to identify the 1031 exchange. Seller Accommodation If the borrower is purchasing a seller's 1031 investment property to occupy as a primary residence, the borrower is accommodating the seller. Therefore, the transaction is not considered a 1031 Tax Deferred Exchange and is eligible for normal financing. The borrower's down payment less the equity from the exchange can be used for all or part of the down payment.
529 Savings Plan	Typically, a 529 College Savings Plan designed to help families pay for future expenses associated with college or other qualified post-secondary training is an eligible source of funds provided that the borrower is the owner of the account, and the account is revocable. However, because there are penalties for early withdrawal or not being used for educational purposes, only the net value, after any withdrawal and/or tax penalties are deducted, may be considered. 529 Accounts must be verified by the following: • Most recent two months Statements • If the assets are required for closing, proof of liquidation is required. It must be determined where the money is invested (stocks, bonds, mutual funds, etc.) to evaluate the effective net balance – see Stocks & Other Securities topic in this section.

Annuities	An annuity is an investment that is typically managed by a life insurance company. Regular or lump sum deposits are put into an annuity and the asset grows tax-deferred until the owner starts taking withdrawals.
	The amount available for liquidation depends on the owner's age at distribution and whether or not the annuity is in the accumulation phase or distribution phase. The company managing the annuity may also charge various penalties, fees, etc. for withdrawals as well as tax implications.
	If the annuity is being used as income, it cannot be used for reserves, down payment, etc.
	The annuity asset may be used for closing costs, down payment and reserves as follows:
	    • 70% of the current cash value, less any outstanding loans, should be used to calculate the amount of funds available; or
	    • 100% of the current cash value can be used if it can be verified that the borrower is not subject to penalties, surrender charges, or taxes.
	If the asset is used for closing and/or down payment, proof of liquidation is required. Surrender Charges, penalties and fees imposed by the managing company as well as any outstanding loans should be deducted from the cash value prior to calculating the amount available for closing. If the asset is being used for reserves only, proof of liquidation does not need to be obtained; however, verification of the asset is still required.

	A computer generated statement must always be obtained to verify the following: • The name of the company managing the annuity; • The name of the annuity owner; • The period covered and the current cash value; • Outstanding loans; and • Penalties, surrender charges and or fees.
Large Deposits/New Accounts	For both refinance and purchase transactions deposits into accounts may be an indication of recently opened liabilities resulting from borrowed funds or an indication that funds used to cover closing costs, pre-paids, the down payment for purchase transactions, or reserves may be from an unacceptable source. Any liabilities resulting from borrowed funds must be considered when qualifying the borrower. A large deposit may be from cryptocurrency that was exchanged into U.S. dollars. MCFI must obtain sufficient documentation to verify the funds originated from the borrower's cryptocurrency account. **Refinance Transactions:** • Except as specified below, documentation or explanation for large deposits is not required; however, any liabilities resulting from all borrowed funds must be considered when qualifying the borrower. • When the borrower pays off or pays down an existing debt in order to qualify, the source of funds used must be verified. If the funds verified include a large deposit as defined above, the source of that deposit must be verified, unless the borrower has sufficient funds to pay off/down the debt without the large deposit. **Purchase Transactions:** The Source of funds must be explained and documented if the deposit is needed to meet requirements for Borrower's cash to close and or reserves for the following: • A single deposit on the account statements that exceeds 50% of the total monthly qualifying income. If the source of a large deposit is readily identifiable on the account statement where the source of the deposit is printed on the statement, the underwriter does not need to obtain further explanation or documentation. If the source of the deposit is printed on the statement, but the Underwriter still has questions as to whether the funds may have been borrowed, the underwriter should obtain additional documentation. **Note:** When a single deposit includes both verified and unverified funds as defined above, only the unverified funds are used to determine the 50% requirement. (Example: The borrower has a monthly income of $4,000 and an account at ABC Bank with a balance of $20,000. A deposit of $3,000 is identified, but only $2,500 is documented as coming from the borrower's federal income tax refund, leaving $500 unverified [the deposit of $3,000 minus $2,500], which is 12.5% of the borrower's $4,000 monthly income, falling short of the 50% definition of a large deposit. Therefore, in this example the full $20,000 can be used to qualify.) The Underwriter should review the source of funds for all large deposits made into accounts that will be used to fund the down payment, closing costs, establishing required reserves, or if a

	borrower is paying off or paying down an existing debt to qualify. The purpose of this review is to determine if any deposits demonstrate the existence of debt that may not have been captured on the borrower's credit report or application or if the funds may have been acquired from an unacceptable source. If the large deposit is from another account belonging to the borrower, that account must also be verified to ensure that the funds into the account were properly sourced and in compliance with this Policy. To source a large deposit from another account belonging to the borrower, the complete one month's statement from the source account must be obtained for the month the withdrawal of the funds occurred. This does not change the number of months that are required per the AUS or documentation process. If the large deposit is from another account being verified for the loan, that account must also be verified after the withdrawal to assure that the funds are not counted twice.
Borrowed Funds	Borrowed funds include subordinate financing, as well as any monies borrowed from other sources, obtained for the specific intention of paying the down payment and/or closing costs. Borrowed funds that are secured by an asset represent a return of equity. Therefore, they may be used for the transaction. Assets that may be used to secure funds include certificates of deposit, stocks, bonds, automobiles, real estate, and life insurance policies. The underwriter must verify the value and ownership of the secured asset, the terms of the loan and the fact that it is a secured loan. Monthly payments for the loan must be considered as debt when qualifying the borrower. When the loan does not require monthly payments, MCFI should calculate an equivalent amount and consider it as debt. Borrowed funds are subject to the following restrictions: • Funds must not be borrowed from the broker, developer, real estate professional, or a lender who is otherwise connected with the subject transaction. • Funds from a loan secured by real property owned by the borrower (other than the subject property) may be used as a source of the down payment. The debt must be included as a liability on the application. • Payments for loans secured by the borrower's personal financial assets (such as life insurance policies, 401(k) accounts, CDs, stocks, bonds, etc.), in which repayment may be accomplished by liquidating the asset, do not have to be included in the debt ratio calculations if the loan instrument shows the asset as collateral for the loan. The loan secured by the financial asset must have been made by a financial institution. The borrower may not use the same asset to satisfy cash reserve requirements. However, they may use the portion of the asset remaining after the value of the asset plus any related fees have been reduced by the amount of the secured loan. • Unsecured loans are not permitted, except when available in conjunction with an Employer-Provided Subordinate Financing as outlined below.

	The above applies to primary residences, second homes and investment properties. Unacceptable Borrowed Funds: • Signature loans • Lines of credit on credit cards, • Overdraft protection on checking accounts. • Energy-efficient loan program, the cost of which is added to the property tax assessment and secured by a lien on the property that takes precedence over the first mortgage. Such programs include Energy Loan Tax Assessment Programs (ELTAP) and Property Assessed Clean Energy (PACE), Home Energy Renovation Opportunity (HERO) programs.
Borrower Contribution Requirements / Minimum Down Payment	A minimum down payment from borrower's own funds is required as indicated below: Primary home - 70% LTV or less:5% minimum contribution from his/her own funds Primary home – above 70% LTV:10% minimum contribution from his/her own funds 2nd home/Investment – All LTVs: Borrower must make full down payment. Gift funds are not permitted. **Note:** If the borrower has the 5% or 10% minimum contribution in a non-liquid asset account (stocks, bonds, etc.), but is also receiving a gift for the transaction, the borrower may use the gift funds for their 5% or 10% minimum contribution in lieu of liquidating the assets. The non-liquid asset account must be verified per policy as evidence that the borrower has the 5% or 10% minimum contribution available.
Borrowers Real Estate Commissions	**Earned Real Estate Commission** Earned real estate commission refers to the borrower's portion of a real estate commission earned from the sale of the subject property being purchased when the borrower is acting as their own real estate agent. Lenders may use the borrower's earned real estate commission as an eligible source of funds for down payment and closing costs provided the borrower is a licensed real estate agent and will receive a sales commission from the purchase of the subject property. **Documentation Requirements** MCFI must document the following: • the settlement statement must reflect the commission earned by the borrower, and • the earned commission amount must be credited towards the mortgage loan.
Bridge Loans	A bridge (or swing) loan is a form of second trust that is collateralized by the borrower's present home, which is usually for sale. By using funds from a bridge loan, the borrower can close on a new house before selling his/her existing home. There is not a specific limitation on the terms of the bridge loan. Generally, financing is acceptable if: • Borrower has the ability to carry the payment on the new home, the payment on other obligations, the payment on the current home and the payment on the bridge loan. If the

	repayment schedule for the bridge loan is not monthly, it must be converted to a monthly amount for qualifying purposes; and • Bridge loan may not be cross-collateralized against the new property. For additional information regarding how to treat the debt on the "departure property" refer to Real Estate Obligations: Departure Property.
Business Funds	If Business Funds are used for down payment, closing costs and/or reserves, all of the following conditions must be met: • Borrowers must provide verification from the other owners of the business that they have access to the funds UNLESS the Borrower is the sole proprietor or 100% owner of the business. • Regardless of the documentation required for the process type, two years' personal, partnership and/or corporate tax returns must be obtained, and the underwriter must perform a cash flow analysis to determine that the withdrawal of funds will not have a detrimental effect on the business. • The file must contain the underwriter's written analysis and conclusions. **Note**: Forms 1084/91, which are used to calculate income, not assets, do not satisfy this requirement. • Verification of funds in the account is required. (**Note**: Large deposits that are not in line with business revenue/income stream should be explained and verified.)
Checking, Savings & CD Accounts	Money retained in bank (including credit unions, savings and loan associations, and savings banks) checking and savings accounts are the most common method of accumulating assets, but it may also be in the form of a Certificate of Deposit (CD). Verification Bank statements serve to present a snapshot of the borrower's account of deposits, withdrawals, transaction activity and bank services. Although bank statements are typically generated on a monthly cycle, they may also be generated on a quarterly, semi-annual, or annual basis. Statements must clearly identify the borrower as the account holder and include the name of the issuing institution, account number, the period covered by the statement, and all deposits and withdrawals made during the period covered. CD's typically contain a forfeiture provision whereby a portion of the accumulated interest and possibly an early withdrawal fee are applied if the CD is liquidated early. The forfeiture of interest and/or withdrawal fee should be considered when using the asset for closing and/or reserves.
Corporate Relocation Buyout & Closing Cost Assistance	Corporate Buyout: If funds from a Corporate Relocation Buyout are being used for closing, a copy of an executed buyout agreement along with the equity advance statement should be obtained. Closing Costs Assistance:

<table>
<tr><td></td><td>Most employers provide their transferring employees a benefit which covers normal and customary closing costs. This benefit is reflected on the HUD-1/Closing Disclosure. This reduces the out of pocket costs for the employee and eliminates the need to get reimbursed for an expense after closing. The specific benefit is determined by the relocation agreement/corporate relocation package which should be obtained to verify the terms, etc.</td></tr>
<tr><td>Credit Card Reward Points</td><td>Credit card reward points that have been converted to cash prior to closing are acceptable funds for use towards closing costs, down payment, and financial reserves. The following requirements apply:
If the reward points are converted to cash and deposited into the borrower’s depository account (checking or savings), no additional documentation is required unless the deposit is considered a large deposit. In that event, follow the requirements for evaluating large deposits.
If the reward points are converted to cash, but not deposited into the borrower’s depository account, the lender must provide the evidence the reward points were:
Available to the borrower prior to the conversion, including verification of the cash value (for example, credit card reward statement prior to conversion); AND
Converted to cash prior to the closing of the loan.</td></tr>
<tr><td>Cryptocurrency</td><td>Cryptocurrency (e.g., Bitcoin, Dash, Etherium, Litecoin, etc.) is a worldwide digital payment system. As a decentralized digital currency, the system works without a central bank or single administrator. Instead, the network is peer-to-peer and transactions take place between users directly, without an intermediary.
Cryptocurrency may not be used to meet MCFI asset requirements (i.e., down payment, earnest money, closing costs, reserves, or other investable assets).
However, if the borrower liquidates the asset, s/he may use the funds” received from the liquidation provided they meet “Sale of Asset” and “Large Deposit” requirements.</td></tr>
<tr><td>Earnest Money</td><td>If the deposit is being used as part of the borrower’s minimum contribution requirement, MCFI must verify that the funds are from an acceptable source. Admissible verification includes:
Copy of the cancelled check and bank statement showing that the check has cleared; or
Copy of the cancelled check and Verification of Deposit (VOD). The VOD must indicate that the average balance for past two months was large enough to cover the amount of the earnest money deposit.
Note: If the borrower has sufficient verified assets to cover earnest money deposit, the above verification is not required. Receipt of funds on the Closing Disclosure is sufficient evidence that funds have been received.
If the earnest money deposit is a gift and has been provided directly to the builder or real estate agent, verification of transfer of funds from the donor’s account in a financial institution to the earnest money deposit holder is required.
If it cannot be determined that the earnest money deposit was withdrawn from the borrowers account, additional documentation,</td></tr>
</table>

	and evidence that the funds have actually changed hands should be provided. **Note**: Large earnest money deposits and deposits that exceed the amount customary for the area should be closely evaluated.
Foreign Assets	Funds that are currently held or sourced from an account outside of a U.S. Banking Institution may be allowed under the following circumstances: • All assets must be verified prior to the transfer and the funds must be seasoned and sourced per Assets/Source of Funds/ Verifying Assets topic. • All assets being used for down, payment, closing costs, pre-paids and reserves currently held in an account outside of a U.S. Banking Institution must be translated into English, transferred into an account in the United States and verified in U.S. dollars prior to closing of the mortgage transaction. • Donor gift funds, given at closing, that are currently held in an account outside of a U.S. Banking Institution must be transferred into an Escrow/Closing Agent account in the United States. The funds must be verified in U.S. dollars at the time the funds are transferred and received in the U.S. and meet all the requirements of the Gift Funds topic below. Documents of foreign origin must be translated to English. • It is important to look for patterns of behaviour particularly when gift funds are involved. Some of the scenarios may include multiple transfers for smaller amounts and from various individuals instead of one wire transfer for the entire gift amount. It is important to pay attention to the amounts, account owner, etc. • China: Funds coming from the Republic of China (including but not limited to Hong Kong and Taiwan) are ineligible to be used in a mortgage transaction. This applies to the assets required for the transaction, including gift funds as well as the qualifying income.
Gift Funds	Gift funds cannot satisfy the minimum down payment from the borrower's own funds. Gifts are permitted in connection with a purchase or refinance of a primary residence. Gift funds must not be used to satisfy the reserve requirements. Gift funds are not permitted on a second home or investment property transactions. **Down Payment** Refer to the Borrower Contribution Requirements/ Minimum Down Payment topic above for requirements unless specified otherwise in the program parameters. The gift can be provided by the following: • Relative, which is defined as a borrower's spouse, child, or other dependent, or an individual who is related by blood, legal proceedings, marriage, or adoption; or • Fiancé, fiancée, or domestic partner; or • Former relative, Godparent, or relative of a domestic partner. If gift funds are coming from outside of the U.S., refer to the Foreign Assets topic above for additional information. Acceptable Sources of Gift Funds

	Large financial gifts from close family members can be considered if properly documented. Substantial cash gifts ($1000 or more) from one individual must comply with standard gift documentation.
	
	Gift funds may come from the following sources.
	• Wedding Gifts: The following documentation must be obtained to verify funds:
	  ○ A copy of a marriage license or certificate, and
	  ○ Verification that gift funds were deposited within 90 days of the date of the marriage license or certificate.
	• Graduation Gifts: The following documentation must be obtained to verify funds:
	  ○ Evidence of graduation from an educational institution, such as diploma or transcripts that supports the date of graduation, and
	  ○ Verification that gift funds were deposited within 90 days of the date of the graduation.
	• Funds Pooled From a Relative or Domestic Partner residing with the Borrower: Can not be used to meet the borrower's minimum required down payment. However, funds from a relative or domestic partner may be used as outlined in the above gift policy.
	• Gift of Equity: Not permitted.
	• Gift or Grant from a Non-Profit Organization: Not permitted.
	Gift Letters
	The following information must be completed on a fully executed gift letter:
	• The actual or the maximum dollar amount of the gift
	• The donor's name, address, telephone number, his/her relationship to the borrower.
	• Indicate that funds are a gift that does not have to be repaid.
	Verification of Funds
	The transfer of the gift funds to the borrower must be documented in one of the following ways:
	• Funds Received prior to closing: Transfer of funds from the donor's account in a financial institution to the borrower's account via either:
	  ○ copies of bank statements from both the donor and the borrower's accounts OR
	  ○ copy of a cancelled gift check OR
	  ○ copy of the donor's withdrawal slip and the borrower's deposit receipt.
	  ○ Evidence of electronic transfer
	• Funds Received at Closing: If the donor does not intend to provide gift funds until closing, the following documentation must be obtained at the closing table:
	  ○ Transfer of the funds from the donor's account in a financial institution to the settlement or closing agent via either
	    ✓ copy of a cashier's check
	    ✓ wire transfer confirmation
	Funds transferred using a third-party money transfer application or service are acceptable only when the documentation evidence that the funds were transferred using the application or service directly

	from the donor's bank account to the borrower's bank account or to the settlement or closing agent.
Government / U.S. Savings Bonds	US Savings/Government Bonds must be verified by the following: • A statement from a financial institution or the loan originator confirming review of the actual bonds and listing the serial numbers, date of maturity, type, amount and verifying that the borrower is the owner; • Proof of value from the U.S. Treasury Table; • Evidence of liquidation if the assets are required for closing.
Ineligible Source of Funds	The following sources of funds may not be used in the calculation of assets: • Borrowed Funds from the following sources: o Signature Loans o Lines of Credit on Credit Cards o Overdraft Protection on Checking Accounts • Cash-on-Hand • Cash advances from a credit card or other revolving account. • Community Assistance or Down Payment Assistance Programs • Corporate Sponsored Loans • Cryptocurrency • Disaster Relief Grant or Loan • Employer Assisted Housing (Secured & Unsecured) • Funds from Individual Development Accounts (IDA) • Gift of equity • Gifts which must be repaid in full or partially. • Gift/Grant from Non-Profit • Individual Development Account (IDA) (Including funds from an IDA) • Lender Paid Assistance • Non-Traditional Savings Plan • Pledged Assets • Pooled Funds • Proceeds from unsecured loans or personal loans (except as permitted with an approved Employer-Assisted Housing program.) • Salary / bonus advances received against future earnings • Seller Carrybacks • Seller Derived Assistance Programs • Subordinate Financing which contains any of the following: o Negative Amortization o Contains special Servicing requirements for MCFI o Terms that restrict prepayments or provide for a prepayment penalty, except as indicated in Subordinate Financing o Does not fully amortize under a level monthly payment plan when the maturity or balloon payment date is less than five years after the note date of the new first mortgage. • Sweat Equity (includes donated goods and/or materials): Contribution to the construction or rehabilitation of a property in the form of labor or services rather than cash is considered sweat equity. Sweat equity may not be deducted from the construction costs, nor may it be used to offset the borrower's minimum down payment. • Trade Equity
Inheritance	An inheritance, if appropriately documented, can serve as the borrower's down payment. The borrower must provide a copy of the will or a letter from the Trustee detailing the distribution of the estate. Borrower's receipt of funds must be verified prior to closing.

	Because the inheritance is considered the borrower’s money, funds can be used for the borrower’s minimum down payment. Gift letter policy does not apply.
Life Insurance net Cash Value	The amount available for liquidation should be calculated using 60% of the cash/surrender value, less any outstanding loans or fees. If asset is required for closing proof of liquidation is required, regardless of the Documentation Process. Proof must be verified by the following: • Computer generated statement identifying the life insurance company • Identify the policy owner. Policy owner must be a borrower. • Evidence the period covered, and the current cash/surrender value • Identify any outstanding loans and deduct them from the cash value/surrender value.
Margin Loan	There are times when the borrower does not want to liquidate their stocks. Although it can be for a number of reasons, it is often because it’s not financially advantageous at that particular time. The borrower may use funds received from a margin loan secured by their stock portfolio to pay down payment and closing costs. Margin loans typically do not have a monthly payment therefore it is generally not included in the debt ratios. Repayment of the loan does not have to be considered.
Pooled Funds	Pooled funds are not permitted.
Proceeds from Sale of Home	The proceeds from the sale of a currently owned home are a common and acceptable source for the down payment and closing costs on a new house. Funds escrowed at the time of contract/agreement and verified as paid may be considered as earnest money. If the contract calls for an additional deposit to be made within a certain period of time, an escrow letter verifying the date and payment of the additional funds is required. Remaining Down Payment: The Closing Disclosure or Seller’s Closing Disclosure from the sale of the home showing sufficient net cash proceeds to consummate the purchase of the new home should be obtained before, or simultaneously with, the closing on the new home. (**Note:** The Closing Disclosure or Seller’s Closing Disclosure does not need to be executed; however, it must reflect sufficient funds to complete the required funds needed to cover required costs.) Photocopies of sales contracts or listing agreements may not be used as an alternative form of verification. **Calculating Proceeds** If the borrower’s current home is listed for sale—but has not yet been sold—s/he can be qualified on the basis of the anticipated equity. The following formula should be used to determine the amount of equity a borrower has in the house that is being sold: • (Sales Price* x 90%) - all Mortgage Balances = Equity *If the sales price has not yet been established, the listing price should be used. Funds for down payment, closing costs, and reserves (if applicable) may come from an equity advance or buyout from the borrower’s employer.

Retirement Accounts	Funds from an individual retirement account (IRA/Keogh) and/or an employer sponsored tax-favored retirement savings account (401k), the vested balance less any outstanding loans secured by the account may be used for the down payment, closing costs, and reserves provided the borrower has access to the fund(s). The underwriter must verify the ownership of the account and confirm that the account is vested and allows withdrawals regardless of current employment status. However, because there are severe penalties for early withdrawal (before retirement age), only the net value, after any withdrawal and/or tax penalties are deducted, may be considered. Retirement Accounts must be verified by the following: • Most recent two months statements (For 401k accounts the statements must reflect the vested balance or percentage of vesting, any outstanding loans, the ending balance of the account and terms of withdrawals/loans. If the 401k account is used for reserves the terms of the retirement plan must show that the borrower is vested and that the plan will allow withdrawals regardless of the current employment status) • Any outstanding loans must be subtracted prior to determining the vested balance; • If the assets are required for closing, proof of liquidation is required.
Sale of Assets	Proceeds received from the sale of the borrower's personal assets may be considered as long as the borrower can provide evidence that s/he: • Owned the asset, for all asset types that are titled assets, for example automobile title; • Has documentation to support the value of the asset, as determined by an independent source, if the proceeds represent more than 50% of the total monthly income used in qualifying. The lesser of the estimated value (as determined by the independent source) or actual sales price must be used when determining the amount of funds for the transaction. For example, a borrower plans to sell their vehicle. The value as determined by an independent source is $10,000; the sales price of the vehicle is $12,000. Only $10,000 can be added to the borrower's available funds, even if the sale has already occurred. • Can prove the transfer of ownership (a copy of a bill of sale or a statement from the purchaser); and • Provides the receipt of the purchase proceeds (deposit slips or bank statement)
Savings Bonds / U.S. Savings Bonds	U.S. Savings / Government Bonds must be verified by the following: • A statement from a financial institution or the loan originator confirming review of the actual bonds and listing the serial numbers, date of maturity, type, amount and verifying that the borrower is the owner. • Proof of value from the U.S. Treasury Table. • Evidence of liquidation if the assets are required for closing.
Stocks & Other Securities	The net value of the stock (which includes mutual fund or other publicly traded security, restricted stock and non-vested stock), should be calculated using 70% of the current market rate. Value is established using a current statement from the stockbroker, a

	photocopy of the stock certificate, accompanied by a dated newspaper, or Internet stock list. (Because value is difficult to establish, we do not accept securities that are not publicly traded.) If assets are liquidated, the actual amount of documented liquidated assets may be used. **Note:** Stock options and non-vested restricted stock options are not eligible for use as reserves. Pledged stocks and/or bonds used as loan security or to offset a margin account are not considered liquid assets. The broker statement is an investor's account of all transactions and asset values within a set period. They list dividends received, interest earned or due, assets purchased and sold, and the value of assets owned during the period. Stocks/Securities statements must identify the following: • The institution or administrator • The account owner • The account number • All transactions, the period covered, any outstanding loans and the ending balance • For securities accounts, identify the stocks/securities • If the assets are needed for closing, proof of liquidation is required • If there is a margin account secured by stock/securities, the borrower's total assets must be reduced by the margin account's outstanding balance amount, plus any overdrawn amount. If the borrower does not receive a statement, the following must be provided: • Photocopy of the stock certificate that identifies the ownership of the stocks by the borrower, number of shares/units owned, and identification numbers of the stock certificate, type, and entity name • Current stock prices from a published source
Trust Accounts	Funds from a Trust may be used with a copy of the Trust Agreement or a letter from the Trustee confirming the following information: • Identify the trustee's name, address, and telephone number. The trustee must be an independent third party that would typically handle trust accounts. • Identify the borrower as the beneficiary. • Verify that the borrower has access to all or a specific amount of the funds. • Verify that the funds are available for disbursement to the borrower. • Proof that funds have been received is required if assets from the trust are being used for closing.
Interested Party Contributions	Interested Party Contributions (IPCs) are funds provided by someone other than the borrower(s) to pay costs associated with obtaining a mortgage that are normally the responsibility of the property purchaser. They may be paid by the seller, lender, or by any other third party who has an interest in the property sale or purchase transaction. IPCs are defined as Financing Concessions or Sales Concessions, as discussed later in this section.

	Interested Parties An interested party is defined as anyone other than the borrower who has a financial interest in, or can influence the terms and sale or transfer of, the property including: the property seller, builder/ developer, real estate agent, or broker (or an affiliate who may benefit from the sale of the property and/or the sale of the property at the highest possible price). A relative, domestic partner, fiancé, fiancée, municipality, non-profit organization, or employer is not considered an interested party unless s/he is the property seller or is affiliated with the property seller. A lender is not considered an interested party unless it is the property seller, or is affiliated with the property seller or another interested party to the sales transaction. For example, MCFI would be considered an interested party on a MCFI real-estate-owned (REO) property transaction. An affiliation exists if there is direct common ownership or control by the lender over the interested party or vice versa or if there is direct common ownership or control by a third party over both the lender and the interested party. A relationship between a builder and a lender that serves as its financial institution is not an affiliation. **Appraisal Requirements** Appraisers must be provided with information relating to all interested party contributions for the subject property granted by anyone associated with the transaction, including both financing and sales concessions that have been, or will be, granted. The appraiser must also be provided with information associated with a permanent interest rate buy down funded through a standby commitment provided by the lender or the builder. Positive adjustments for sales or financing concessions are not acceptable. **File Document Requirements** When there is an IPC in a transaction, all loan and sales contract documents, including the sales contract, Loan Estimate (LE), the loan application, appraisal report and Closing Disclosure must include or address all financing arrangements that have been negotiated between the buyers and sellers. **Items That Are Subject to IPC Limits** Financing Concessions are IPCs that are payments or credits related to acquiring the property or paying for financing terms (including prepaids). Financing concessions are items that are subject to IPC limits. • Origination fees, Discount points, Commitment fees • Cost for Interest Rate Shortfalls • Appraisal Costs • Transfer taxes • Stamps • Attorney fees • Survey charges • Title insurance premiums or charges

	• Real estate tax service fees • Real estate taxes covering any period after the settlement date. • Funds to subsidize a permanent interest rate buy down. • Funds that flow from an interested party to a non-profit and then to the buyer for payment of closing costs. These plans may not be used for to fund down payment or reserves. Prepaid items: • Interim interest charges (limited to no more than 30 days of interest) • Escrow Fees (may not be paid by MCFI) • Real estate taxes covering any period after the settlement date (if the taxes are being escrowed by the servicer for future payments) • Hazard* insurance premiums (limited to no more than 14 months); and • Initial or renewal mortgage insurance premiums and any escrows required for renewal of borrower-purchased mortgage insurance coverage. • Homeowner association (HOA) dues covering any period after the closing date (limited to no more than 12 months);*Includes flood insurance, where applicable. Lender Paid Assistance programs where the lender is the property seller or is affiliated with the property seller or another interested party to the sales transaction. Fees for standby commitments that a builder obtains for blanket coverage before it enters into a contract with a borrower are contributions, but they are not subject to limitations because they are not attributable to the specific mortgage transaction. Items paid by the property seller that are the responsibility of the seller—such as real estate sales commissions, charges for pest inspections, deed release fees, or costs that the property seller is required to pay under state or local law—are not contributions. This includes pro-rated real estate tax credits provided by the seller at closing in those jurisdictions in which property taxes are paid in arrears. This credit represents property tax amounts assessed but not yet due and payable, for the period when the seller still owned the property, and it is not considered to be a contribution. Pro-rated real estate taxes cannot be considered when determining the funds required for the transaction. Although a pro-rated tax credit from the property seller can offset that portion of the charge for the establishment of the escrow account, the borrower must still verify sufficient funds for down payment, closing costs, prepaids and reserves, including the payment of pro-rated real estate taxes prior to closing. (Example: Borrowers closing costs and prepaids are $5,000. The seller's portion of the pro-rated real estate tax credit to the borrower is $2,000. This reduces the borrower's cash to close to $3,000. The borrower must still verify the entire $5,000 prior to closing). Pro-rated real estate tax credits cannot be used to meet the borrowers minimum required investment or down payment. **Items Not Subject to IPC Limits**

- Buyer-broker fees paid by the seller as part of the real estate sales commission, as long as the commission being paid is typical of the commission usually paid in that real estate market.
- Gift funds received from a donor that complies with gift policy.
- Gifts or grants from a non-profit that do not obtain funding from the seller or any other interested party to the transaction.
- Funds the lender provides for closing costs and borrower prepaid fees as long as the lender is not the property seller or affiliated with an interested party to the transaction. Refer to the Lender Paid Assistance topic below for further information.
- Sales Concessions

IPC Contribution Limits

IPC contribution limits are based on occupancy type. They are measured using the lesser of the sales price and appraised value. The contribution limits are as follows:

Loan Process & Products:

Occupancy	Maximum Contribution
Primary & Second Home	6%
Investment Property	2%

The total dollar amount of the Financing Concessions may not exceed the actual total dollar amount of the allowable closing costs.

Items Not Permitted as IPCs

- Contributions may not be used to meet the borrower's down payment or minimum borrower contribution requirements, or to meet reserve requirements for the transaction.
- Payment Abatements. Monthly payment abatements to pay for or reimburse the borrower for payments of principal, interest, taxes, insurance, and more than 12 months of homeowner association fees for units in condominium, PUD or cooperative projects are not permitted, regardless of whether they are disclosed on the Closing Disclosure. This applies to transactions where the interested party is directly funding the abatement and/or if the funding for the abatement is flowing through another entity, such as a non-profit down payment assistance program (DAP). Note: The payment of HOA fees is not considered abatement unless the payment of the fee extends for more than 12 months. The payment of HOA fees for 12 months or less is considered an interested party contribution.
- Undisclosed IPCs, including "Silent" second mortgages held by the property seller. Seller contributions that are not disclosed on the Closing Disclosure are often given to homebuyers outside of loan closing. These undisclosed contributions tend to reduce the effective sales price of a property and may compromise the loan-to-value ratio for a mortgage. Consequently, a mortgage with undisclosed seller contributions is not eligible for origination or purchase.

Sales Concessions

- IPCs that exceed allowable Financing Concession limits are considered Sales Concessions. In addition to contributions that exceed those limits, additional inducements may come in the form of cash or personal property such as furniture, automobiles,

	securities, and/or other "giveaways" granted by any interested party to the transaction. Often they are used as an incentive to the buyer and may or may not be disclosed on the Closing Disclosure. Other inducements to purchase that are not disclosed on the Closing Disclosure are not permitted. The cost of items that are in the form of personal property (i.e., furniture, decorator items, automobiles, or other “giveaways”) are also considered Sales Concessions.
	• Sales Concessions are not subject to IPC contribution limits, but their value must always be deducted from the sales price of the property. For underwriting purposes, the sales price must be reduced to reflect the amount of all Sales Concessions. The LTV ratio should then be calculated based on the lesser of the reduced sales price or the appraised value.
	• Sales Concessions include, but are not limited to:
	  o Payment of various fees on the borrower's behalf that are not considered allowable Financing Concessions
	  o Pre-foreclosure or short sale processing fees that are charged to the borrower (also referred to as short sale negotiation fees, buyer discount fees, short sale buyer fees, etc) must be treated as a sales concession if any portion is reimbursed by the seller or an interested party to the transaction.
	  o Financing Concessions that exceed allowable IPC Financing Concession limits, or that exceed the dollar amount of actual costs
	  o Cash, Furniture, Automobiles, Decorator allowances, Repair allowances*, Moving expenses
	  * Money received for repairs will not be considered contributions provided the property is new construction, repairs are complete prior to close, or if funds have been escrowed for work to be completed. Note: Escrows for repairs on existing properties are not permitted.
	For underwriting purposes, the value of Sales Concessions must be deducted from the sales price. The LTV and CLTV ratios should then be calculated based on the lesser of the reduced sales price or the appraised value.
	
	Lender Contributions
	The lender may provide the borrower with a contribution to fund borrower paid closing costs and prepaid fees in the following cases:
	• The lender credit is derived from premium pricing.
	• The funds are sourced directly from lender with no expectation for repayment or financial obligation apart from the subject mortgage. Funds passed to the lender from a third party for the purpose of providing a lender credit are not eligible as a lender contribution.
	The amount of the lender contribution cannot exceed the amount of the borrower-paid closing costs and prepaid fees and may not be used to fund any portion of the down payment or reserve requirements.
	Lender Incentives for Borrowers
	Cash or Cash-like Incentives for all Transactions Types: The Lender may provide the borrower with a cash or cash-like incentive (e.g., a gift card) that is not reflected on the Closing Disclosure provided that

	the amount of the incentive does not exceed $500, and no repayment is required. These types of lender incentives are not considered IPCs and, as a result, are not included in the IPC limit calculation. Furthermore, these incentives are not considered cash out to the borrower and do not have to be included in the cash back to borrower at closing calculation.
Paycheck protection Plan	Loan proceeds from the SBA Payroll Protection Plan (PPP) and/or any other similar COVID-19 related programs are not considered business assets for the purposes of eligible funds to qualify for the Borrower for the Mortgage transaction, including but not limited to, funds for down payment, closing costs, and reserves
Escrow Account	Mandatory Impounds on all HPML and Higher-Priced QM loans MCFI requires an escrow account for the payment of special assessments.