

PMI  
**UNDERWRITING  
GUIDELINES** 2011

MANUAL

UPDATED 8.15.2011



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Topic	Section	Change/Clarification/New Policy
<p>The Underwriting Manual has been updated. Some Sections have been renamed and policies updated</p> <p>All changes are shown in <b>“blue text”</b> in the Underwriting Manual. The date of the change is detailed in the header for the topic within the manual.</p>		
Ineligible Loan Features	3.1	Removed reference to HomeStyle® Mortgages
Ready Refinance Program	3.4.5	Added new program guidelines and criteria
Remaining Programs	3.4.6 – 3.4.15	Renumbered remaining programs

## SECTION 1 - PMI UNDERWRITING POLICY

### 1.1 OVERVIEW (12/06)

PMI Mortgage Insurance Co. was founded in 1972 to serve the needs of mortgage lenders, and to facilitate homeownership. PMI's insurance programs and services help lenders expand their lending opportunities to serve more homebuyers through the sharing of default risk. Ultimately, this risk-sharing partnership enables both lenders and investors to profit from the increased availability of capital, as well as, to generate a larger volume of business. This, in turn, creates more opportunities for potential homebuyers.

The ***Underwriting Guidelines Manual*** provides comprehensive information on PMI's loan documentation requirements; loan, borrower, and property eligibility; PMI programs and products; PMI's risk philosophy; and other general underwriting issues. PMI's more flexible underwriting guidelines for low- and moderate-income borrowers, developed to meet the needs of as many qualified borrowers as possible, are also contained in this manual.

Underwriting mortgage loans requires a sensitive analysis of the many elements necessary to finance a home. This manual describes PMI's general underwriting approach; it does not set forth all-inclusive underwriting standards. In discussing this general approach, minimum guidelines considered necessary for prudent mortgage insurance underwriting are identified; the most essential requirement is that the terms of the loan, property value, creditworthiness of the borrower(s), and the appropriate documentation to support the underwriter's judgment that it is probable the borrower will repay the mortgage debt.

Each loan should be individually evaluated with emphasis placed on the overall quality of the loan. Although multiple risk factors are assessed, the underwriter must attempt to balance the evaluation between the borrower and the property. Generally, no one single characteristic will lead to ineligibility of an insurance application.

### 1.2 UNDERWRITING STANDARDS (12/06)

PMI provides products and programs to the mortgage lending industry, which assists potential borrowers in realizing their goal for homeownership. Our objective is to help lenders expand their lending programs to meet the needs of as many qualified borrowers as possible. This "partnership" allows lenders, investors, and PMI to profit from increased availability of capital, as well as, to generate a larger volume of business; and borrowers benefit from the creation of more opportunities for homeownership.

The principal responsibility of underwriters, in support of the PMI Group's mission, is to build and maintain a quality book of business. This is achieved by balancing goals for growth with long-term profitability, and is achieved with (1) an understanding of past performance, (2) evaluation of present conditions, and (3) anticipation of future developments. PMI Underwriters are committed to superior customer service, a display of professionalism, and the maintenance of operational excellence.

### 1.3 UNDERWRITING POLICY (6/15/11)

PMI's underwriting policy is developed in support of corporate Risk Management objectives and for compliance with laws and regulations, including those of state Insurance Commissions, Fannie Mae® and Freddie Mac® mortgage insurer eligibility criteria, Fair Lending, and the Equal Credit Opportunities Act.

#### **Fair Lending**

PMI is committed to the use of underwriting standards and risk management techniques that are consistent, equitable, and adhere to fair lending principles and state and federal regulations. PMI reviews

applications for insurance to determine the applicant's ability and willingness to repay the mortgage obligation and to ensure that the property sufficiently secures the debt. Each application is given an in-depth and sensitive analysis of its individual circumstances in order to fully evaluate the risk.

It is PMI's policy to provide creditworthy borrower's with underwriting decisions made without regard to race, color, national origin, religion, gender, sex, or marital status of the borrower; or because income is derived from a public assistance program; or based on trends, characteristics, or conditions in the neighborhood or geographic area or any other prohibited basis as defined by state and federal law.

### **Predatory Lending**

PMI is committed to insuring loans made in a responsible and equitable manner. Providing mortgage insurance that would facilitate abusive lending practices is in violation of the Federal Home Ownership and Equity Protection Act (HOEPA); and is not, and will never be, a part of PMI's business strategy.

PMI, along with other industry participants, agree the following practices are potentially predatory and/or abusive. Some of these practices cannot be readily identified by the documents that are submitted for mortgage insurance purposes; however, to the extent possible, PMI's underwriters will review each file for the evidence of potentially abusive practices.

- Product steering, which occurs when a borrower who could qualify for a lower cost mortgage is instead "steered" to a higher cost product
- Charging an interest rate that is not representative of the borrower's risk profile
- Approving a mortgage loan without regard to the borrower's ability to repay the obligation
- Charging excessive points and fees
- Successive refinancing of the same loan with no real economic benefit to the borrower
- Mandatory prepayment penalties that offer no benefit to the borrower (such as lower rate or fee)
- Requiring credit life insurance as a condition of loan approval

### **Privacy Policy**

PMI is committed to complying with applicable information, privacy and security laws. In the process of underwriting loans for mortgage insurance, PMI underwriters have access to nonpublic personal information relating to individual consumers. Each PMI employee exercises a high degree of care to protect the security, integrity, and confidentiality of nonpublic personal information in our possession. Access to consumer nonpublic personal information is restricted to those employees or contract employees who need to know the information in order to provide mortgage insurance.

### **OFAC Blocked Persons List**

Borrowers who are confirmed on the OFAC List are not eligible for insurance.

## **SECTION 2 - SUBMISSION, DOCUMENTATION, COVERAGE AND PREMIUM PLANS**

### **2.1 SUBMISSION (6/15/11)**

There are several ways to apply for mortgage insurance; you can submit a traditional paper application or use our electronic delivery method.

- e-PMI® is PMI's online channel for products and services on the Internet. It provides fast access to MI origination and policy servicing and works with a variety of loan origination systems and requires no special training. This system is used by lenders to:
  - Originate delegated and non-delegated MI certificates
  - Update information on existing MI certificates
  - Upload document images for non-delegated transactions
  - View and/or print existing MI certificates
- pmiPAPERLESS® – a dedicated, secure fax line used to submit loans for delegated and non-delegated MI transactions.
- The receipt of a Commitment/Certificate of Insurance when submitting a request through one of PMI Origination Systems does not guarantee that the request meets all underwriting guidelines. The lender is still responsible for ensuring that the loan information provided within the insurance application is true and accurate and meets PMI's eligibility requirements as set forth in this Guide.

### **2.2 DOCUMENTATION**

#### **2.2.1 AGE OF DOCUMENTS (4/15/11)**

Credit Documents should be no more than 120 days old on the date that PMI approves the loan.

For Construction-Permanent loans the credit documents can be no more than 120 days old at underwriting, and at the time the mortgage insurance is activated.

Credit Documents are defined as the documents used to underwrite the loan and include, but are not limited to, income, asset, credit, and appraisal documents.

Appraisals can be no more than 120 days old. An appraisal update and/or completion report (Form 442/1004D) is required after 120 days for existing construction and for new construction, including construction-to-permanent; a new appraisal is required after 12 months.

#### **2.2.2 STANDARD/FULL DOC (11/09)**

Loans submitted on a non-delegated basis, and loans underwritten and retained by the lender for a delegated submission, would typically contain the following documentation to be considered as fully documented:

- Fully completed PMI Application for Insurance, signed and dated by an authorized representative of the Master Policyholder
- Uniform Residential Loan Application (Fannie Mae 1003/Freddie Mac 65). The loan application should be signed and dated by all borrowers; underwriter discretion will be used to determine if an unsigned loan application is accepted
- Uniform Underwriting and Transmittal Summary (Fannie Mae 1008/Freddie Mac 1077)
- Residential Mortgage Credit Report (RMCR), or tri-merged report (alternate credit requirements may

be applicable based on DU/LP findings)

- Loan payment history, if not included in credit report
- Verification of Employment and Income (which would include a verbal verification obtained by the lender prior to closing)
- Verification of cash needed to close, plus reserves
- Residential Appraisal Report
- Purchase contract/escrow instructions
- Fannie Mae DU/ Freddie Mac LP Feedback
- Lender's Loan Approval Letter

Additional documentation as applicable:

- Gift letters and source of gift funds
- Divorce decrees
- Lease agreements
- Borrower's explanation of derogatory credit
- Verification of source of funds deposited into the borrower's account within the past 60-90 days
- Occupancy statements
- Details of borrower's employment history
- Form 4506 -- Borrower's written authorization to obtain copies of the past two years' federal income tax returns from the Internal Revenue Service

## 2.3 PARTNER DELIVERED QUALITY® (PDQ) - DELEGATED (6/10)

PMI's Partner Delivered Quality® (PDQ<sup>SM</sup>) program was designed to give quality-conscious customers who share PMI's risk management and underwriting philosophies more control over the mortgage insurance process. PDQ provides customers with the authority to approve loans for mortgage insurance without prior PMI review.

PMI expects PDQ lenders to use their delegated underwriting authority as granted under the terms of their delegated underwriting agreement and to exercise prudent judgment when exercising this authority. Delegated lenders do have the option to submit loans to PMI's National Underwriting Center for non-delegated underwriting. If, after the underwriting review, PMI rejects the loan for insurance or issues a conditional approval, the lender may not exercise its delegated authority to resubmit the loan.

### 2.3.1 DELEGATED SUBMISSION REQUIREMENTS

Delegated loans are typically submitted via ePMI or edi. These loans should be underwritten by the lender and the lender's loan file should be fully documented and must be provided to PMI on request.

## 2.4 PRE-QUALIFICATION (6/10)

PMI's Pre-Qualification program is designed to help both lenders and their borrowers determine creditworthiness and the maximum eligible mortgage amount before or after selecting a home.

The risk associated with a pre-qualification is no different from a standard submission; PMI's standard underwriting guidelines apply.

## 2.5 INSURANCE COVERAGE (9/08)

Standard coverage, the basic mortgage insurance coverage plan limits the lender's initial exposure on a mortgage loan. Standard Coverage is available for all loan types that PMI insures.

Under Standard Coverage, a lender selects a specific percentage of coverage (i.e., 20%, 25%, etc.), called the optional settlement percentage. Should a claim occur under Standard Coverage, PMI will apply the optional settlement percentage to the sum of the outstanding loan balance, delinquent interest, and other claimable expenses. PMI also has the right to acquire the property by paying the total

claimable expense rather than the optional settlement percentage.

Although the actual rates may differ, the products listed below are available on all of the insurable loan types.

### **2.6 PREMIUM PLANS (5/5/11)**

#### **2.6.1 MONTHLY / PMINU MONTHLY<sup>SM</sup> (12/06)**

These plan rates are annualized and are for first year and renewals through year ten.

The MONTHLY plan allows the MI premium to be remitted to PMI on a monthly basis instead of an annual premium amount up-front. This assists in reducing the initial closing costs for the loan. The actual premium amount due is calculated by multiplying the annualized premium by the loan amount and dividing the result by 12. Please note that, because the monthly premium payments are made in arrears, additional premium will likely be due at policy termination.

Monthly refunds are based on unearned premium. Annual plan refunds are pro rata.

#### **2.6.2 SUPER SINGLE<sup>SM</sup> (12/06)**

This plan allows greater flexibility for both lenders and borrowers. The Super Single premium plan offers borrowers the option to pay the premium in full, or to finance their mortgage insurance into the loan amount at closing. Super Single refunds are calculated using a schedule available at [pmi-us.com](http://pmi-us.com).

#### **2.6.3 FINANCED PREMIUM (4/09)**

Loans which include financed mortgage insurance premium will be underwritten, and premium will be determined, using the net LTV (before premium added). The premium to be financed is not considered in the net LTV.

The net LTV is defined as the loan amount (not including the MI premium amount) divided by the lesser of the sales price or appraised value.

Rates for the loan are based on the LTV band where the loan falls prior to adding the financed mortgage insurance. For example, if the LTV is 95% and the rate for 35% coverage with a 680 credit score is 3.77%; this would yield a gross LTV of 99%.

The premium is calculated using the loan amount multiplied by the premium rate, which is then added to the loan amount.

The gross LTV, including the financed mortgage insurance, cannot exceed 103%.



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### SECTION 3 – MATRICES, PRODUCTS AND PROGRAMS

#### 3.1 INELIGIBLE LOAN FEATURES (8/15/11)

Loans with the following features are ineligible for mortgage insurance:

- |   |  |
|---|--|
| <ul style="list-style-type: none"> <li>▪ Manufactured Housing</li> <li>▪ 2-to-4 Units</li> <li>▪ Third Party Originations</li> <li>▪ Borrowers with Nontraditional Credit</li> <li>▪ Investment Properties</li> <li>▪ Condotels</li> <li>▪ Kiddie Condos and SFDs</li> <li>▪ Time-Share, Fractional or Incremental Ownership</li> <li>▪ A-Minus Loans</li> <li>▪ Interest-only Loans</li> <li>▪ Limited Documentation Loan</li> </ul> | <ul style="list-style-type: none"> <li>▪ Option Payment Mortgages</li> <li>▪ Negative Amortization – Potential and Schedules</li> <li>▪ PMI-to-PMI Streamlined (Instant) Refinance</li> <li>▪ Bridge (Swing) Loans</li> <li>▪ Vacant Land</li> <li>▪ Pioneering designs – log cabins, dome homes, etc.</li> <li>▪ Home Improvement and Rehab loans</li> <li>▪ Model Home Leasebacks</li> </ul> |
|---|--|

#### 3.2 LOAN MATRICES (UPDATED 7/15/11)

#### PMI Eligibility Matrix (7/11/11)

		Full Doc								
		Standard				Jumbo Loans*				
		Loan Amount	Min Credit Score	Distressed Market Credit Score	Max DTI	Loan Amount	Min Credit Score	Distressed Market Credit Score	Max DTI	
<b>Owner-Occupied</b> Purchase only	1 Unit (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	97/97	\$417,000	720	N/A	45%	Not Eligible			
<b>Owner-Occupied</b> Purchase or Rate/ Term Refinance	1 Unit (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	95/95	\$417,000	660	720	45%	Not Eligible			
		90/90	\$417,000	660	680	45%	\$625,500	700	740	45%
		85/85	\$417,000	660	680	45%	\$625,500	700	740	45%
	Co-ops <sup>1</sup>	95/95	\$417,000	660	N/A	45%	Not Eligible			
		90/90	\$417,000	660	N/A	45%	\$625,500	700	N/A	45%
		85/85	\$417,000	660	680	45%	\$625,500	700	740	45%
<b>Owner-Occupied</b> Purchase or Rate/ Term Refinance	2 Units	95/95	\$533,850	680	720	45%	Not Eligible			
		90/90	\$533,850	680	680	45%				
		85/85	\$533,850	680	680	45%				
<b>Owner-Occupied</b> Cash-Out Refinance <sup>2</sup> Maximum cash-out \$150,000	1 Unit (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	90/90	Not Eligible				<b>NOTE:</b> * Maximum \$625,500 in all markets; \$729,750 in specific FHFA high-cost areas only 1. Attached housing is not eligible in Florida 2. Not eligible in Distressed Markets			
		85/85	\$417,000	720	N/A	45%				
<b>Second Home<sup>2</sup></b> Purchase or Rate/ Term Refinance	1 Unit (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	95/95	Not Eligible							
		90/90	\$417,000	720	N/A	45%				
		85/85	\$417,000	720	N/A	45%				



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	Co-ops	95/95	Not Eligible			
		90/90	\$417,000	720	N/A	45%
		85/85	\$417,000	720	N/A	45%
Cash-Out Refinance			Not Eligible			

### pmiAFFORDABLE (5/23/11)

		Full Doc				
		Standard & Distressed Markets				
		LTV / CLTV	Loan Amount	Min Credit Score	Distressed Markets Min Credit Score	Max DTI
<b>Owner-Occupied</b> Purchase or Rate/ Term Refinance	1 Unit (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	95/95	Conforming	660	720	45%
		90/90	Conforming	660	680	45%
		85/85	Conforming	660	680	45%
	2 units	95/95	Conforming	680	720	45%
		90/90	Conforming	680	680	45%
		85/85	Conforming	680	680	45%

**NOTE:** 1. Attached housing is not eligible in Florida

### 3.3 LOAN PRODUCTS

#### 3.3.1 FIXED-RATE/FIXED PAYMENT LOANS (12/06)

Fixed-rate/fixed-payment loans are fully amortizing and do not contain any provisions for rate adjustments.

#### 3.3.2 BALLOON PAYMENT MORTGAGES (12/06)

Balloon payment loans have periodic, level installments of principal and interest that do not fully amortize the loan over the loan term. The balance of the mortgage is due in lump sum at the end of the term. PMI will insure loans with balloon payments based on the following:

- Balloon loans with terms of five years or more are priced using the fixed-rate category
- Unless the lender offers either a new loan or modification of the existing loan, mortgage insurance coverage will terminate at the end of the loan term

At the end of the loan term, coverage may only be renewed if the loan has been modified or extended. Unless prior-approved under Fannie Mae or Freddie Mac's Balloon Reset Eligibility Criteria, PMI reserves the right to approve any extension or modification of the loan terms. Notification, which includes the terms of the extension or modification, must be sent to the local PMI Regional Operations Center for approval.

If the loan is not modified or extended, and coverage is terminated, coverage will be offered only if a new loan is written for the borrower(s) and a new insurance application package is approved.

PMI is not liable for failure of the borrower to pay any "balloon" or non-level payment. PMI does not insure against the inability to refinance the balloon, but only against the inability of the borrower to make the installment payments. PMI will not cover default of the balloon payment unless the lender offers to renew the loan or offers new financing.

### 3.3.3 ADJUSTABLE RATE MORTGAGES (ARMS) (4/15/11)

ARMs provide for a variable interest rate which is tied to an index and will adjust at specified periods of time and in an amount which is based on movement of the index. Payments adjust either concurrent with the interest rate adjustments or at other intervals, as specified in the Note. Lenders frequently offer initial interest rate discounts (“teaser rates”) in order to attract borrowers. A discount or teaser rate exists when the initial rate is less than the program rate, which is determined by the current index value plus the margin (i.e., the Fully Indexed Accrual Rate/FIAR).

Following is a description of features and an overview of PMI’s philosophy for ARM loans:

- The ARM index used must be beyond the control of the lender, easily verifiable by the borrower, and published on a regular basis. The most common indices are treasury-related indexes, which include indexes based on 1 year Constant Maturity Treasury (CMT) securities and the 12 Month Treasury Average (MTA); the 11th District Cost of Funds Index (COFI), and the London Interbank Offered Rate (LIBOR) index.
- The Fully Indexed Accrual Rate (FIAR) is the index value plus maximum margin applied during the life of the loan.
- Annual payment increases are limited to 15% or a 2% interest rate change, whichever is greater. A maximum six percentage point (6%) increase over the initial payment rate (or 5% over the FIAR) during the life of the loan is allowed. If the initial payment rate is less than the FIAR on an ARM, the maximum allowable discount, or rate concession is as outlined below:
  - Positively Amortizing ARM – 300 bp below FIAR
  - Potential Negatively Amortizing – Not Eligible
- Payment increases for 3/3 and 5/5 year ARMS are limited to an aggregate interest adjustment equivalent to 1% per year.
- Short Term ARMs are defined as loans with a three year or less fixed-rate period
- The Hybrid ARM starts with an initial fixed-rate period; commonly 5, 7 or 10 years -- before they turn into a traditional one-year ARM for the remainder of a 30-year term
- Qualifying Rates
  - Short term ARMs (3 years or less fixed rate period) qualify using the greater of the note rate plus 2% or the Fully Indexed Accrual Rate (FIAR)
  - 5/1 ARMS - qualify using the greater of the note rate plus 2% or the Fully Indexed Accrual Rate (FIAR)
  - Hybrid ARMs (fixed rate periods of 7 years or greater) qualify the note rate

### 3.3.4 TEMPORARY BUYDOWNS (2/11)

Loans with temporary buydowns feature money advanced to the lender (often by the builder or seller) to reduce the monthly payments for the initial years of the loan (i.e., temporary interest rate discount). The maximum acceptable temporary annual buydown plans are:

- 2, 1 on FRM, 3/1 and 5/1 ARM up to 95% LTV
- 3, 2, 1 on FRM, 5/1, 7/1 and 10/1 ARMs up to 95% LTV
- 1, 0 on 1-year ARMs up to 95% LTV

The source of buydown funds is a critical factor in the evaluation of risk. For example, borrower funds derived from savings should be given more favorable consideration than seller-funded buydowns, which pose potential payment shock and generally impact property value.

Borrower- or lender-funded buydown loans can be underwritten at the bought-down rate. Seller-funded buydowns should be underwritten at the contract note rate. Compressed buydowns provide for payment adjustments more frequent than annually. Borrower- or lender-funded compressed temporary buydowns are eligible subject to the following:

- Fixed-rate mortgage
- Maximum 1% interest rate increase every six months
- Owner-occupied, primary residence
- Maximum 2-1 interest rate adjustments on 95% LTVs and 3-2-1 interest rate adjustments on 90% LTVs

Temporary buydowns are not eligible for the following:

- 97% LTV loans
- Cash-out refinances
- Second home properties
- Investment properties
- Interest Only mortgages
- High Balance Loans
- Balloon Mortgages

Any portion of the buydown paid by the builder/seller must be included in the maximum allowable third-party contribution.

### 3.4 PROGRAMS

#### 3.4.1 PMI'S DESKTOP UNDERWRITER® (DU®) AND LOAN PROSPECTOR® (LP) PROGRAM (7/11/11)

When underwriting loans using DU or LP, PMI expects the lender will:

- Employ prudent underwriting judgment when determining if a loan should be underwritten using DU or LP
- Confirm that all the information provided to DU or LP is accurate
- Assess the appraisal for accuracy and determine that the value is well-supported
- Use due diligence for red flags when reviewing the documentation provided
- Meet the credit report validation requirements
- Determine if there is any derogatory or contradictory information in the loan that could not be analyzed by DU or LP and take action regarding that information
- For DU loans – ensure that the loan meets all the verification messages and approval conditions detailed in the findings, and the observations have been reviewed and addressed in the file
- For LP loans – ensure that the loan meets the credit and loan processing information detailed on the feedback certificate

Loans must receive one of the following recommendations:

- Desktop Underwriter
  - Approve
  - Expanded Approval
- Loan Prospector
  - Accept

The loan must comply with the PMI Eligibility matrix.

Lenders must confirm that the loan meets these additional requirements:

- Minimum 3% borrower's own funds verified for down payment (5% for high balance and second homes)
- Borrowers must have a minimum 2 months of verified reserves
- Credit score is valid (i.e., at least three trade lines are evaluated for 12 months)
- Full interior / exterior appraisal
  - Ineligible: 2055, 2070 and 2075
- If the property is located in an area on PMI's Distressed List, or the appraiser checks the declining property value box, the loan must meet the PMI Distressed Markets matrix, policy and guidelines
- Meet PMI's Condominium Project Criteria
  - Limited and Streamlined Reviews allowed with maximum 30% investor concentration
  - All other condominiums must meet PMI Condominium Project Criteria
- Meet PMI's Property Flipping Policy

Ineligible for DU/LP program:

- Non-traditional credit\*
- Loans with a non-occupant co-borrower\*
- Construction-Permanent\*

- DU recommendations: Refer, Refer with Caution, Out of Scope
- LP Risk Classifications: A-Minus or Caution
- Document efficiency of only a Verbal Verification of Employment

\* Eligible using standard guidelines

### **3.4.2 HIGH LTV LOAN PROGRAM (95.01% TO 97.0%) (4/15/11)**

- Purchase only transactions
- Minimum 720 credit scores
- Maximum loan amount is \$417,000 (\$625,500 for Alaska/Hawaii)
- Maximum DTI of 45%
- Non-distressed markets
- Minimum 3% down payment from the borrowers own funds
- 1 unit Owner Occupied SFD, attached or detached, Condos and PUDs
- Retail only
- Fixed Rate or Hybrid ARMs (5/1, 7/1, 10/1)
- Ineligible
  - Rate/Term or Cash-out Refinance
  - Construction-Permanent loans
  - Second Homes or Co-ops
  - High Balance Loans
  - Properties in Distressed Markets
  - Short-Term ARMs
  - Buydowns
  - Balloons

### **3.4.3 JUMBO LOAN PROGRAM (7/11/11)**

- Meet PMI Eligibility Matrix
- Maximum loan amount is \$625,500 in all markets (\$938,250 for Alaska/Hawaii); \$729,750 in specific high-cost areas
- Purchase or rate/term refinance one-unit, condos and co-ops only
- Minimum 700 credit score in non distressed markets; 740 credit score in distressed markets
- ARM loans must have a minimum 5 year initial fixed period
- Maximum 5% down payment from borrower's own funds
- Maximum interested party contributions
  - Non-distressed markets      6%
  - Distressed markets              3%
- Loans over \$625,500 eligible in FHFA designated high-cost areas only
- For non-DU/LP loans, the loans must meet PMI eligibility and underwriting guidelines
- Regardless of the AUS decision, the loan must meet PMI eligibility and underwriting guidelines
- Ineligible:
  - Non-traditional credit
  - Manufactured housing
  - 2- to 4- units
  - Second homes
  - Cash-out refinance
  - Interest-only loans
  - Loans with temporary buydowns
  - Balloon mortgages
  - Short-term ARMs
  - Affordable housing, i.e. MyCommunityMortgage® and Home Possible®
  - Fannie Mae's Flex Mortgage and HomeStyle® programs
  - Freddie Mac's Newly Built Home and Alt 97 programs
  - Properties in Guam and the U.S. Virgin Islands

### 3.4.4 FANNIE MAE HOMESTYLE® RENOVATION MORTGAGE (5/23/11)

The Fannie May HomeStyle Renovation mortgage enables a borrower to obtain a purchase transaction mortgage or a rate/term refinance mortgage and receive funds to cover the cost of repairs, remodeling, or renovations to the property. Lenders must obtain special approval from Fannie Mae to deliver this type of mortgage to Fannie Mae,

#### Eligibility Criteria

- Lenders must receive special approval to deliver this program to Fannie Mae
- The lender must meet all Fannie Mae guidelines
  - Loans may be approved DU®
  - All other automated underwriting systems decisions require underwriting to PMI's current eligibility and guidelines
- Ineligible:
  - DU® Refer, Refer with Caution IV, Out of Scope, and EA Recommendation from version 5.7 or earlier
- Renovation work must be completed no later than 12 months from the date the mortgage loan is closed
- All renovation work must be performed by a licensed contractor

#### Loan Purpose

- Loans may be a Purchase Rehabilitation or a Refinance Rehabilitation transaction

#### Loan-to-Value Calculations

- Follow Fannie Mae Guidelines

#### Jumbo Loan Program

- All loans must be in specific high-cost areas
- Minimum 700 credit score - non-distressed markets
- ARM loans must have a minimum 5 year initial fixed period
- Minimum 5% down payment from borrower's own funds
- Maximum allowable Interested Party Contributions
  - Properties in Non-Distressed Markets 6%
- For non-DU® loans, the loan must meet PMI eligibility and underwriting guidelines
- Loans approved through DU® may utilize the PMI DU® program

#### Income Documentation Requirements

- Acceptable full documentation and document efficiencies are allowed
- 2 years' income verification may be required
- A documentation efficiency of only a Verbal Verification of Employment is not permitted

#### Other Documentation Requirements

- Assets required to close the transaction must be verified for all loans, regardless of any documentation efficiency provided
- Standard appraisal with an interior and exterior review
- The appraised report must provide an "as completed" appraised value that estimates the value of the property after completion
- Ineligible:
  - 2055 exterior review only
  - Drive-by inspections
  - Property Inspection Waivers (PIW)/Alternatives (PIA)
- A final inspection must be provided by the appraiser to indicate renovation is complete
- Appraisals more than 120 days old up to 12 months old must be recertified
- A copy of the original HUD-1 from the original purchase transaction is required for the refinance transaction when the property has been owned for less than 12 months
- A copy of the contract for cost of improvements must be provided

#### Escrow Accounts

- At closing, the lender must deposit all of the renovation costs, including the contingency reserve and,

if applicable, any escrowed mortgage payments or funds that the borrower provides from his or her own funds, into an interest-bearing renovation escrow account for the benefit of the borrower.

- Unused contingency funds and/or escrow funds, unless they are received directly from the borrower, must be used to reduce the outstanding balance of the renovation mortgage after all of the renovation work has been completed and certification has been obtained. Reimbursement of any excess funds to the borrower is considered cash-out and is not permitted.

#### Minimum Down Payment

- Borrower must contribute a minimum equity or down payment from their own funds as follows:
  - Conforming 3%
  - Jumbo or Second home 5%

#### Maximum Interested Party Contributions

- Maximum 3% of the lesser of the property's sales price or appraiser value on:
  - LTVs greater than 90%
- Maximum 6% of the lesser of the property's sales price or appraised value on:
  - LTVs of 90% or less

#### Minimum Reserves

- Minimum reserves
  - Minimum 2 months' PITI
- For conversion of primary residences, 6 months reserves are required per property

#### Qualifying Rate

- 3 & 5 year ARMs (5 years or less fixed-rate period) qualify using the greater of the note rate +2% or the Fully Indexed Accrual Rate (FIAR)
- 7/1 and 10/1 ARMs qualify at the note rate

#### Qualifying Ratios

- Maximum 45% DTI

#### Valid Credit Score and Credit History

- Although a credit score can be generated with one trade line, PMI does not consider the credit score valid unless at least three trade lines are evaluated for at minimum of 12 months, regardless of AUS decision. (Trade lines can be open or closed). Authorized user accounts generally do not belong to the borrower, therefore cannot be used to validate the credit score.
- Minimum 660 credit score
- Judgments, liens, collections, voluntary or involuntary repossessions, and charge-offs should generally be paid in full at loan closing
- If the credit report does not contain a mortgage rating, a separate VOM should be obtained
- The borrower's credit history must reflect:
  - 0x30 mortgage late payments in the last 12 months (non DU® loans)
  - 0x60 mortgage late payments in the last 12 months (DU® loans)
  - 0x60 installment or revolving account late payments in the last 12 months
- Minimum 4 years' reestablished traditional credit after discharge of a bankruptcy; 2 years with documented extenuating circumstances
- Borrower with a prior foreclosure/short-sale/deed-in-lieu is generally not acceptable
- For credit score-based programs and pricing, the qualifying credit score will be determined using the lower-middle method; the lowest borrower credit score will be used
- Comparable credit characteristics may be used in lieu of credit score to determine eligibility for NY properties or if the credit score is unusable due to invalid credit information on the credit report
  - Refer to PMI's Comparable Credit Criteria for a summary of attributes equivalent to PMI's credit score tiers at [www.pmi-us.com](http://www.pmi-us.com)

#### Mortgage Insurance Information

- The insurance may be activated prior to the completion of the renovations at the time of loan closing.
- If the subject loan defaults prior to completion of renovations, PMI may choose to acquire the property minus any costs of renovations not completed or the lender may choose to complete the renovations prior to submitting a claim to PMI.

- Condition of approval - no claims will be paid until the repairs/renovations are completed per the plans and specs and a final inspection by the appraiser has been completed and the value recertified.

### 3.4.5 Ready Refinance (8/10/11)

Ready Refi provides refinance opportunities for lenders that sell directly to Fannie Mae and/or Freddie Mac, or portfolio their loans.

Seasoned PMI-insured loans can be refinanced by meeting the following:

- Confirm the loan is currently insured by PMI
- The new loan must do one of the following:
  - Reduce the borrower's payment
  - Reduce the interest rate
  - Replace an ARM loan with a fixed rate mortgage
- The existing loan has a minimum of 12 payments with no delinquency and is current
- The new loan is to the original borrowers and same property as the current loan
- The new loan must be a fixed rate/fixed payment or 5/1, 7/1, 10/1 ARM
- The new loan's LTV is calculated using a new appraisal (Distressed Markets Policy does not apply)

While PMI will insure all occupancy and property types, this does not guarantee a secondary market exists.

Confirm that PMI insures the loan by contacting the Policy Servicing @ 800.366.1143

#### LENDER EXPECTATIONS

PMI expects that the lender will:

- Process and underwrite the loan as fully documented, with all income, employment and assets verified as required
- Employ prudent underwriting judgment and assess the appraisal for accuracy and determine that the value is well-supported
- All loan documents will not be reviewed by PMI. We expect the income, employment and assets presented on the loan application and transmittal summary (1003/1008) have been verified and can be provided upon request

#### RATE/TERM REFINANCE DEFINITION

- Payoff of the existing lien, including the related closing costs and prepaid items
- Up to 5% of the customary closing costs may be included in the new loan amount
- No more than 2% of the loan amount or \$2000, whichever is less, cash back to the borrower

#### BORROWERS

The new loan is for the original borrowers on the currently insured loan; no assumptions

#### LOAN TYPE

The new loan must be a fixed rate/fixed payment or 5/1, 7/1, 10/1 ARM

#### CREDIT REPORT/CREDIT SCORE

- A new credit report with a current credit score is required
- 0x30 mortgage lates in past 12 months

#### PROPERTY VALUATION

- A new appraisal with an interior and exterior inspection is required
- The Distressed Markets Policy does not apply



# 2011 Underwriting Guidelines Manual

## ELIGIBILITY MATRIX

			Full Doc		
			Standard		
			Loan Amount	Min Credit Score	Max DTI
<b>Owner-Occupied Rate/Term Refinance</b>	1 Unit SFD (attached & detached, condos & PUD's); Co-ops; Manuf.Housing	97/97	\$625,500	620	45%
		95/97	\$625,500	620	45%
		90/97	\$625,500	620	45%
		85/97	\$625,500	620	45%
	2 Units*	97/97	\$533,850	620	45%
		95/97	\$533,850	620	45%
		90/97	\$533,850	620	45%
		85/97	\$533,850	620	45%
	3 Units*	97/97	\$645,300	620	45%
		95/97	\$645,300	620	45%
		90/97	\$645,300	620	45%
		85/97	\$645,300	620	45%
	4 Units*	97/97	\$801,950	620	45%
		95/97	\$801,950	620	45%
		90/97	\$801,950	620	45%
		85/97	\$801,950	620	45%
<b>Second Home Rate/Term Refinance</b>	1 Unit SFD (attached & detached, condos & PUD's); Co-ops; Manuf.Housing	97/97*	\$625,500	620	45%
		95/97*	\$625,500	620	45%
		90/97	\$625,500	620	45%
		85/97	\$625,500	620	45%
<b>Investment Property* Rate/Term Refinance</b>	1-4 Units, Condos, PUDs, Co-ops; Manuf.Housing	97/97	\$625,500	620	45%
		95/97	\$625,500	620	45%
		90/97	\$625,500	620	45%
		85/97	\$625,500	620	45%

\* Check with Investor for saleability

### SUBORDINATE FINANCING

- Junior liens must be either paid off with the borrower's own funds or resubordinated, provided the maximum CLTV requirements are met
- No new subordinate financing permitted

### MORTGAGE INSURANCE

- A new Certificate will be issued
- The mortgage insurance coverage percentage can change
- The new loan is subject to the premium rates in effect at the time of the new loan
- If the loan exceeds any of these parameters, please contact the National Underwriting Center (NUC) for consideration.

### DELEGATED SUBMISSION

- Delegated loans should be submitted via e-PMI, no additional documentation is required

- **If manually submitted, the lender should include the following:**
  1. MI Application
  2. New 1003/1008

**NON-DELEGATED SUBMISSION**

**Lenders should also use e-PMI and electronically submit the following documents:**

1. MI Application (manual submissions only)
2. New 1003/1008
3. New credit report
4. Appraisal

**3.4.6 PMI-TO-PMI REFINANCE-TO-MODIFICATION PROGRAM HARP-ELIGIBLE ONLY – SAME LENDER/SERVICER (4/25/11)**

This program offers flexible refinances for existing PMI insured mortgages via HARP-Eligible GSE-owned loans. The existing loan must meet the following criteria:

- The loan was originated on or before May 31, 2009 and the new note date is on or before June 30, 2012 and the loan is purchased by Fannie Mae or Freddie Mac no later than October 2012.
- PMI is the current insurer
- The originating lender must be the current servicer of the existing mortgage
- The originating lender must be in possession of the original underwriting file
- The coverage percentage and premium rate remain unchanged
- The borrower and property are the same as on the existing loan (Borrower changes are permitted as GSE policies allow)
- The loan is current
- The new loan improves the borrower's ability to repay the loan by at least one of the following:
  - A reduction in the mortgage payment, interest rate or principal balance; or
  - An extension of the ARM fixed-payment period; or
  - An extension of the loan or amortization term; or
  - A more stable payment product

**Loan Purpose and program**

- PMI-to-PMI Refi-to-Mod Program
  - Fannie Mae HARP Same Servicer
  - Freddie Mac Relief Refi Same Servicer
- Refinance allows:
  - Payoff of existing lien
  - Payoff of accrued interest through the date the loan will be paid off
  - Related closing costs and prepaid items (see maximum financed closing costs)
  - Existing subordinate liens must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted
  - The borrower may receive no more than \$250 cash back at closing; all other funds must be applied as a principal curtailment on the new loan

**Maximum Financed Closing Costs**

- Reasonable and customary closing costs to be financed in the new loan amount are limited to:
  - 5% of the existing loan's unpaid principal balance plus accrued interest

**Fannie Mae Refi Plus and DU® Refi Plus /Freddie Mac Relief Refinance Mortgage**

- The lender is responsible to determine that the specific requirements for Fannie Mae and Freddie Mac are met

**Loan Types**

- Fully amortizing Fixed-rate/Fixed-payment loan with a term up to 40 years
- Fully amortizing ARM with an initial fixed period of at least five years, with a term up to 40 years

**LTV / CLTV Maximums**

- No maximum LTV
- No maximum CLTV

- Existing subordinate financing must be re-subordinated or paid off with the borrowers own funds

#### Other requirements:

- All original occupancy types are eligible; occupancy changes are permitted
- The property type is the same as the original loan

#### Mortgage Payment History

- Loan must be current
- No more than 0x60 mortgage late in the last twelve months, or the life of the loan if less than twelve months old

#### Property Valuation

- No property valuation is required as PMI will rely on the value provided with the original loan

#### Seasoning Requirements

- None

#### Mortgage Insurance

- The mortgage insurance premium rate and the coverage percentage will not change for PMI Monthly, pmiNu Monthly™ and annual premium plans:
  - The premium payment amount may change if the new unpaid principal balance of the refinanced loan has increased or decreased from the original loan amount, and this new payment amount will be determined by applying the existing premium rate to the new loan amount
  - If the existing loan had single premium coverage, no additional premium will be due even if the loan or insured amount changes
- The PMI certificate of insurance will be modified to reflect the new loan terms, and the existing certificate number; percentage level of coverage and the premium rate will remain unchanged
- The mortgage insurance premium amount will be updated if the new unpaid principal balance of the refinanced loan is different from the original loan amount
- Once PMI's review of the loan is complete, one of the following will be faxed:
  - Refi-to-Mod Certificate Amendment Request – Confirmation; or
  - Refi-to-Mod Certificate Amendment Request – Ineligible

#### Electronic Submission

Delegated and Non-delegated loans should be submitted via e-PMI®

For Non-delegated loans only, upload the following documents:

- New 1003 and 1008
- New Credit Report (for current mortgage payment history)

#### Manual Submission

Fax the following documentation to the National Underwriting Center at 888.444.9792:

- Modification Request
- New 1003 and 1008
- A new Credit Report (for current mortgage payment history)

#### Current Certificate

- To determine if the borrower's loan is insured by PMI:
  - Fannie Mae DU Refi Plus Messaging will indicate that PMI is the Mortgage Insurer
  - Call Customer Service at 800-366-1143

### **3.4.7 PMI-TO-PMI REFINANCE-TO-MODIFICATION PROGRAM GSE HARP-ELIGIBLE ONLY – NEW LENDER/SERVICER (4/25/11)**

This program offers flexible refinances for existing PMI insured mortgages via HARP-Eligible GSE-owned loans. The existing loan must meet the following criteria:

- The loan was originated on or before May 31, 2009 and the new note date is on or before June 30, 2012 and the loan is purchased by Fannie Mae or Freddie Mac no later than October 2012.
- PMI is the current insurer

- The coverage percentage and premium rate remain unchanged
- The borrower and property are the same as on the existing loan (Borrower changes are permitted as GSE policies allow)
- The maximum financed closing costs meet the requirements detailed below
- The loan is current
- The new loan improves the borrower's ability to repay the loan by at least one of the following:
  - A reduction in the mortgage payment, interest rate or principal balance; or
  - An extension of the ARM fixed-payment period; or
  - An extension of the loan or amortization term; or
  - A more stable payment product

#### Loan Purpose and program

- PMI-to-PMI Refi-to-Mod Program
  - Fannie Mae HARP New Servicer
  - Freddie Mac Open Access New Servicer
- Refinance allows:
  - Payoff of existing lien
  - Payoff of accrued interest through the date the loan will be paid off
  - Related closing costs and prepaid items (see maximum financed closing costs)
  - Existing subordinate liens must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted
  - The borrower may receive no more than \$250 cash back at closing; all other funds must be applied as a principal curtailment on the new loan

#### Maximum Financed Closing Costs

- Reasonable and customary closing costs to be financed in the new loan amount are limited to:
  - 5% of the existing loan's unpaid principal balance plus accrued interest

#### Fannie Mae Refi Plus or DU® Refi Plus /Freddie Mac Open Access Mortgage

- The lender is responsible to determine that the specific requirements for Fannie Mae and Freddie Mac are met

#### Loan Types

- Fully amortizing Fixed-rate/Fixed-payment loan with a term up to 40 years
- Fully amortizing ARM with an initial fixed period of at least five years, with a term up to 40 years

#### LTV / CLTV Maximums

- No maximum LTV
- No maximum CLTV
- Existing subordinate financing must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted

#### Other requirements:

- All original occupancy types are eligible; occupancy changes are permitted
- The property type is the same as the original loan

#### Mortgage Payment History

- Loan must be current
- No more than 0x60 mortgage late in the last twelve months

#### Property Valuation

- No property valuation is required as PMI will rely on the value provided with the original loan

#### Seasoning Requirements

- None

#### Mortgage Insurance

- The mortgage insurance premium rate and the coverage percentage will not change for PMI Monthly, pmiNu Monthly™ and annual premium plans:
  - The premium payment amount may change if the new unpaid principal balance of the refinanced loan has increased or decreased from the original loan amount, and this new

payment amount will be determined by applying the existing premium rate to the new loan amount.

- If the existing loan had single premium coverage, no additional premium will be due even if the loan or insured amount changes
- Any outstanding premiums on the existing loan must be paid prior to the activation of the modification
- The PMI certificate of insurance will be modified to reflect the new loan terms, and the existing certificate number; percentage level of coverage and the premium rate will remain unchanged
- The mortgage insurance premium amount will be updated if the new unpaid principal balance of the refinanced loan is different from the original loan amount.
- Once PMI's review of the loan is complete, one of the following will be faxed:
  - Refi-to-Mod Certificate Amendment Request – Confirmation; or
  - Refi-to-Mod Certificate Amendment Request – Ineligible

### Electronic Submission

Delegated and Non-delegated loans should be submitted via e-PMI®

For Non-delegated loans only, upload the following documents:

- New 1003 and 1008
- New Credit Report (for current mortgage payment history)

### Manual Submission

Fax the following documentation to the National Underwriting Center at 888.444.9792:

- Modification Request
- New 1003 and 1008
- A new Credit Report (for current mortgage payment history)

### Current Certificate

- To determine if the borrower's loan is insured by PMI:
  - Call Customer Service at 800-366-1143
  - If the existing loan is owned by Fannie Mae, DU Refi Plus messaging will indicate that PMI is the Mortgage Insurer

### **3.4.8 PMI-TO-PMI REFINANCE-TO-MODIFICATION PROGRAM (NON-HARP-ELIGIBLE) – SAME LENDER/ SERVICER (4-18-11)**

This program offers flexible refinances for existing PMI insured mortgages, for loans owned by portfolio lenders, other investors and GSE loans that are not HARP-Eligible. The existing loan must meet the following criteria:

- PMI is the current insurer
- The originating lender must be the current servicer of the existing mortgage
- The originating lender must be in possession of the original underwriting file
- The coverage percentage and premium rate remain unchanged
- The borrower and property are the same as on the existing loan (Borrower changes are permitted as GSE policies allow)
- The loan is current
- The new loan improves the borrower's ability to repay the loan by at least one of the following:
  - A reduction in the mortgage payment, interest rate or principal balance; or
  - An extension of the ARM fixed-payment period; or
  - An extension of the loan or amortization term; or
  - A more stable payment product

### Loan Purpose and program

- PMI-to-PMI Refi-to-Mod Program
  - PMI Refi to Mod Same Servicer
- Refinance allows:
  - Payoff of existing lien
  - Payoff of accrued interest through the date the loan will be paid off

- Related closing costs and prepaid items (see maximum financed closing costs)
- Existing subordinate liens must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted
- The borrower may receive no more than \$250 cash back at closing; all other funds must be applied as a principal curtailment on the new loan

### Maximum Financed Closing Costs

- Reasonable and customary closing costs to be financed in the new loan amount are limited to:
  - 5% of the existing loan's unpaid principal balance plus accrued interest

### Loan Types

- Fully amortizing Fixed-rate/Fixed-payment loan with a term up to 40 years
- Fully amortizing ARM with an initial fixed period of at least five years, with a term up to 40 years

### LTV / CLTV Maximums

- No maximum LTV
- No maximum CLTV
- Existing subordinate financing must be re-subordinated or paid off with the borrowers own funds

### Other requirements:

- All original occupancy types are eligible; occupancy changes are permitted
- The property type is the same as the original loan

### Mortgage Payment History

- Loan must be current
- No more than 0x60 mortgage late in the last twelve months, or the life of the loan

### Property Valuation

- No property valuation is required as PMI will rely on the value provided with the original loan

### Seasoning Requirements

- None

### Mortgage Insurance

- The mortgage insurance premium rate and the coverage percentage will not change for PMI Monthly, pmiNu Monthly™ and annual premium plans:
  - The premium payment amount may change if the new unpaid principal balance of the refinanced loan has increased or decreased from the original loan amount, and this new payment amount will be determined by applying the existing premium rate to the new loan amount
  - If the existing loan had single premium coverage, no additional premium will be due even if the loan or insured amount changes
- The PMI certificate of insurance will be modified to reflect the new loan terms, and the existing certificate number; percentage level of coverage and the premium rate will remain unchanged
- The mortgage insurance premium amount will be updated if the new unpaid principal balance of the refinanced loan is different from the original loan amount
- Once PMI's review of the loan is complete, one of the following will be faxed:
  - Refi-to-Mod Certificate Amendment Request – Confirmation; or
  - Refi-to-Mod Certificate Amendment Request – Ineligible

### Electronic Submission

Delegated and Non-delegated loans should be submitted via e-PMI®

For Non-delegated loans only, upload the following documents:

- New 1003 and 1008
- New Credit Report (for current mortgage payment history)

### Manual Submission

Fax the following documentation to the National Underwriting Center at 888.444.9792:

- Modification Request
- New 1003 and 1008
- A new Credit Report (for current mortgage payment history)

- Income verification when the P&I payment is increasing over 20% of the current payment

### Current Certificate

- To determine if the borrower's loan is insured by PMI:
  - Fannie Mae DU Refi Plus Messaging will indicate that PMI is the Mortgage Insurer
  - Call Customer Service at 800-366-1143

### **3.4.9 PMI-TO-PMI REFINANCE-TO-MODIFICATION PROGRAM (NON-HARP-ELIGIBLE) – NEW LENDER/SERVICER (8/1/09)**

This program offers flexible refinances options to allow a different Lender/Servicer to refinance an existing PMI insured loan, for loans owned by portfolio lenders, other investors and GSE loans that are not HARP-eligible. The existing loan must meet the following criteria:

- PMI is the current insurer
- The existing mortgage has been seasoned for twelve months
- The coverage percentage and premium rate remain unchanged
- The borrower and property are the same as on the existing loan (Borrower changes are permitted as GSE policies allow)
- The maximum financed closing costs meet the requirements detailed below
- The loan is current
- The new loan improves the borrower's ability to repay the loan by at least one of the following:
  - A reduction in the mortgage payment, interest rate or principal balance; or
  - An extension of the ARM fixed-payment period; or
  - An extension of the loan or amortization term; or
  - A more stable payment product

### Loan Purpose and program

- PMI-to-PMI Refinance-to-Modification Program
  - PMI Refi to Mod New Servicer
- Refinance allows:
  - Payoff of existing lien
  - Payoff of accrued interest through the date the loan will be paid off
  - Related closing costs and prepaid items (see maximum financed closing costs)
  - Existing subordinate liens must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted
  - The borrower may receive no more than \$250 cash back at closing; all other funds must be applied as a principal curtailment on the new loan

### Maximum Financed Closing Costs

- Reasonable and customary closing costs to be financed in the new loan amount are limited to:
  - For loan amounts up to \$417,000 – 4% of the existing loan's unpaid principal balance plus accrued interest, or \$5,000, whichever is less; or
  - For loan amounts greater than \$417,000 – 4% of the existing loan's unpaid principal balance plus accrued interest, or \$10,000, whichever is less

### Increased Mortgage Payments

- If the new principal and interest payment increases by more than 20% of the existing principal and interest payment, the income and employment must be verified and the maximum DTI is limited to 55%. Required income documentation:
  - Salaried borrowers – minimum of one paystub indicating the most recent 30 days' earnings and year-to-date earnings, and a verbal Verification of Employment (VOE)
  - Self-employed or other non-salaried borrowers – minimum of one year's tax return and a verbal VOE

### Loan Types

- Fully amortizing Fixed-rate/Fixed-payment loan with a term up to 40 years
- Fully amortizing ARM with an initial fixed period of at least five years, with a term up to 40 years

### LTV / CLTV Maximums

- No maximum LTV

- No maximum CLTV
- Existing subordinate financing must be re-subordinated or paid off with the borrowers own funds; no new subordinate financing is permitted

Other requirements:

- All original occupancy types are eligible; occupancy changes are permitted
- The property type is the same as the original loan

Mortgage Payment History

- Loan must be current with no 30 day late payments in the last 90 days
- No more than 1x30 mortgage late in the last twelve months

Property Valuation

- No property valuation is required as PMI will rely on the value provided with the original loan

Seasoning Requirements

- Existing loan must be seasoned for a minimum of twelve months
- Multiple mortgages cannot be used to meet this requirement

Mortgage Insurance

- The mortgage insurance premium rate and the coverage percentage will not change for PMI Monthly, pmiNu Monthly™ and annual premium plans:
  - The premium payment amount may change if the new unpaid principal balance of the refinanced loan has increased or decreased from the original loan amount, and this new payment amount will be determined by applying the existing premium rate to the new loan amount.
  - If the existing loan had single premium coverage, no additional premium will be due even if the loan or insured amount changes
- The PMI certificate of insurance will be modified to reflect the new loan terms, and the existing certificate number; percentage level of coverage and the premium rate will remain unchanged
- The mortgage insurance premium amount will be updated if the new unpaid principal balance of the refinanced loan is different from the original loan amount.
- Once PMI's review of the loan is complete, one of the following will be faxed:
  - Refi-to-Mod Certificate Amendment Request – Confirmation; or
  - Refi-to-Mod Certificate Amendment Request – Ineligible

Electronic Submission

Delegated and Non-delegated loans should be submitted via e-PMI®

For Non-delegated loans only, upload the following documents:

- New 1003 and 1008
- New Credit Report (for current mortgage payment history)

Manual Submission

Fax the following documentation to the National Underwriting Center at 888.444.9792:

- Modification Request
- New 1003 and 1008
- A new Credit Report (for current mortgage payment history)
- Income verification when the P&I payment is increasing over 20% of the current payment

Current Certificate

To determine if the borrower's loan is insured by PMI:

- Fannie Mae DU Refi Plus Messaging will indicate that PMI is the Mortgage Insurer
- Call Customer Service at 800-366-1143

### 3.4.10 PMIAFFORDABLE (7/11/11)

#### PMI'S Affordable Housing Initiative Policy Summary

To facilitate homeownership by the broadest possible group of borrowers, PMI has worked with lenders, housing finance agencies, and non-profit organizations to design products and programs which

encourage lending in underserved low- and moderate-income communities and to targeted populations. Based on our experience, we believe that insuring affordable housing loans, using a prudent but flexible underwriting approach, can expand a borrower's financing options while providing PMI with profitable business opportunities.

PMI has developed national eligibility and underwriting requirements for affordable housing programs and endorses various agency- and lender-specific programs to address the needs in diverse markets across the country. As with our standard underwriting guidelines, PMI underwriters will undertake an in-depth and sensitive analysis of the individual applicant's circumstances in order to fully evaluate the risk. Recognition will be given to the borrower's motivation for safe and decent shelter, instead of speculation, appreciation, and long-term investment in the property. These positive attributes will be considered in offsetting other risk elements that may be present such as frequent job changes, employment gaps, limited savings, and collateral variances.

### **Program Eligibility**

This is an affordable housing product for the low-to moderate-income borrower who can demonstrate the willingness and capacity yet lack the cash typically needed for the down payment and/or closing costs.

#### **Automated Underwriting Systems**

- Allows Fannie Mae's MyCommunityMortgage® (MCM) or Freddie Mac's Home Possible.
- All other automated underwriting systems require underwriting to PMI's standard eligibility and guidelines

#### **Eligibility Criteria**

- Maximum 95% LTV/CLTV
- Minimum credit score required is 660 for traditional credit
- Non-traditional credit is eligible
- Owner-occupied Purchase and rate/term refinance only
- One and two unit properties including single-family attached & detached, condominiums, and PUDs (Attached properties are not eligible in Florida)
- Fixed-rate, fixed payment fully amortizing mortgages or 5/1, 7/1 and 10/1 ARMs

#### **Income limitations**

- Maximum 115% of area median income except in high-cost areas or special programs determined by Fannie Mae and Freddie Mac

#### **Subordinate financing must have grant-like features including:**

- No payments due during the term of the loan
- No interest charged
- The principal becomes due if the property is no longer owner-occupied or the first mortgage is paid off due to sale, transfer of title, or cash-out refinance

#### **Minimum Down Payment**

- No minimum contribution from the borrower required unless program directed
- Funds for down payment, closing costs, and prepaid escrow may be from any of the following:
  - Borrower's own funds
  - Gift, grant, or down payment assistance from a family member not related to the transaction, a nonprofit charitable organization (non Nehemiah-like), government agency, or borrower's employer
  - Unsecured installment loans may only be from an extended family member who is not a party to the transactions (maximum 2% of purchase price)
  - Non-real estate secured loan; terms of the note must be verified and should reflect the borrower's assets used as security (maximum 2% of purchase price)
  - Subordinate financing with grant-like features
- Down payment funds are not permitted from a Nehemiah-like structured program
- A minimum one month PITI reserve of borrower's own funds is required

#### **Closing costs may be:**

- Gifts from family members
- Grant or unsecured loan from a non-profit organization, public agency, church, municipality, or

employer

- Paid by the lender through premium pricing

### Maximum Interested Party/Seller Contributions and Concessions

- Maximum 3% of the lesser of the property sales price or appraised value on:
  - LTVs greater than 90%
  - Properties in distressed markets
- Maximum 6% of the lesser of the property sales price or appraised value on:
  - LTVs of 90% or less

### Eligible Borrowers

- U.S. Citizen
- Permanent Resident Alien
- Non-permanent resident aliens are eligible, except those with Visa status types of A (Diplomatic) or B-1 (temporary business use); must have a minimum of 2 years' history of residence, employment, and credit in the United States
- Foreign Nationals are ineligible

### Qualifying Ratios

- Maximum 45% DTI

### Credit History

- Minimum 660 credit score
- Comparable credit characteristics may be used in lieu of credit score to determine eligibility for NY properties or if the credit score is unusable due to invalid credit information on the credit report:
  - Refer to PMI's comparable credit criteria for a summary of attributes equivalent to PMI's credit score tiers at [www.pmi-us.com/underwriting/](http://www.pmi-us.com/underwriting/)
- Demonstrated willingness to repay debt
- For credit score-based programs and pricing, the qualifying credit score will be determined using the lower-middle method; the lowest borrower credit score will be used—the minimum credit score is 660

### Non-traditional credit

- All loans must be underwritten by PMI; PDQ delegated submission not eligible
- A minimum of 4 sources of non-traditional credit with at least 12 months history required:
  - one housing-related;
  - one a utility company; and
  - two from other sources.
- Credit references must be provided either by a credit reporting agency creating a non-traditional credit report or:
  - Twelve (12) months of consecutive account statements; or
  - A current account statement with 12 months of cancelled checks or paid receipts; or
  - Lender direct-written verification which must include all of the information required on a non-traditional credit report and a current statement provided by the creditor.
- 0x30 housing lates in the past 12 months;
- 0x60 late payments in past 12 months for all other credit references
- Borrowers with a Bankruptcy/Foreclosure/Deed-in-Lieu/Short sale are not eligible
- No collections or judgments (except medical) in past 24 months; judgments must be satisfied

### Homebuyer Education

- Prepurchase homebuyer education is not required, MCM or LP program may have requirements
- Early delinquency intervention counseling is required, borrower must execute the Borrower Authorization for Counseling form

### Ineligible:

- Florida attached housing (condominiums, PUDs, co-ops, townhomes and rowhouses)
- Third Party Originations
- Jumbo loans

- Interest-only loans
- Construction-Permanent loans
- Reduced Appraisal forms
- Manufactured Housing
- 3- to 4-unit property
- Second homes
- Investment property

### 3.4.11 MODIFICATION REQUESTS (8/09)

PMI's Modification request offers our customers an easy way to modify PMI-insured loans that are:

- ARM conversions
- Balloon Resets; or
- PMI-to-PMI Refinance-to-Modifications (RTM)

PMI will provide an amendment to the policy or a signed copy of the Modification Form as verification that the modification has been processed and approved.

The following transactions are **NOT** considered modifications:

- Removing the name of an existing borrower
- Adding a new borrower
- Property address change, i.e. releasing a portion of the property (this is considered a partial release/reconveyance)

### 3.4.12 HOME PRESERVATION LOAN MODIFICATIONS (4/09)

PMI strongly supports the Treasury's Making Home Affordable program, offering homeowner's assistance by making their mortgages more affordable and helping to curb the rate of foreclosure. We offer the following:

Home Affordable Modification (HMP): Loan modification program to reduce the monthly mortgage payments of at-risk homeowners whose existing mortgage is owned by Fannie Mae, Freddie Mac or other investors.

Loan Modifications and Workouts: For loans insured by PMI, we make it easy and efficient to promptly and accurately assist your customers with a range of programs for both performing and non-performing loans, including PMI's SHARP program, a claim advance for eligible loans.

Detailed information on all the Loan Modifications offered by PMI is available at [www.pmi-us.com](http://www.pmi-us.com) ; click on the Home to Stay banner.

### 3.4.13 ASSUMPTIONS (11/10)

PMI will continue to insure a mortgage assumption, provided that the assuming borrower generally meets current PMI underwriting criteria. PMI must approve the assumption in writing. Under the terms of the PMI First Lien Master Policy, PMI reserves the right to re-underwrite the risk whenever there is a change in borrowers.

The lender must submit the following:

- Notice of Assumption Form
- Completed and signed Residential Application Form
- Credit Report
- Income and Employment Verification
- Verification of Funds for Closing
- Signed Property Purchase/Sale Agreement

#### ASSUMPTION TYPES

##### Release of Financial Liability

The assuming borrower must qualify for mortgage insurance using the current pricing and guidelines.

PMI-approval must be granted prior to transfer of title or addition of borrower to promissory note.

### **Due-on-Sale Clause - Exempt Transactions**

Certain notes/mortgages contain a due-on-sale clause which does not allow assumption. Certain transactions are exempt from enforcement of the due-on-sale clause. They are as follows:

- Assumption without release of financial liability of current borrower
- Surviving party on the death of a joint tenant
- Transfer to a junior lien holder as the result of foreclosure or deed-in-lieu of foreclosure of a subordinate lien
- Transfer of the property (or beneficial interest in a trust) to the relative of a deceased borrower, as long as the transferee will occupy the property
- Transfer of the property (or beneficial interest in a trust) to an immediate family member, as long as the transferee will occupy the property
- Transfer of the property (or beneficial interest in a trust) to the spouse of the borrower under a divorce decree, legal separation agreement or incidental property settlement, as long as the transferee will occupy the property
- Transfer to an unrelated co-borrower who has owned the property under joint tenancy or tenancy in common, as long as the transfer occurs more than 12 months after the mortgage closed and transferee will occupy the property
- Transfer of the property (or beneficial interest in a trust) into an Intervivos Revocable Trust, so long as the borrower is the individual who established the trust, will be the beneficiary of the trust and will occupy the property

If the assumption is the result of a due-on-sale clause and complies with the requirements listed above and there is no release of liability, the lender is required to only submit a completed and signed PMI Notice of Assumption (Form #UW2104.01). If a release of liability is requested, the remaining borrower must qualify

### **Declined Transactions**

The lender must be made aware that if the property transfers without PMI approval, coverage will be terminated on the date of transfer.

In the event of termination, a short rate or prorated cancellation (depending on product type) and a refund of appropriate premium are coordinated with the Policy Servicing Department.

### **3.4.14 PARTIAL RELEASE OF COLLATERAL (12/06)**

PMI requires that lenders have a valid first lien on each secured property. The PMI Commitment and Certificate of Insurance may be invalidated if PMI has not been notified and approved an easement or encroachment on the property or if a partial release of collateral has been granted without PMI's prior written approval. All Partial Release requests will be completed by the Credit Risk Management (Quality Control) Department.

A partial release may be requested due to division of the property (a lot split) or condemnation of a portion of the property through eminent domain. Subject to receipt and satisfactory review of all of the following documentation, PMI may approve a partial release and process the transaction as a request for a modification.

- New appraisal report showing value of the property before and after the release
- The appraiser's statement that the remaining secured property is suitable for residential occupancy
- Copy of the survey of the land
- Contract of Sale of the released portion of the land
- A detail of the distribution of any cash consideration paid for the release, including the amount that will be applied to the outstanding balance of the loan (or that will be applied to cure any delinquency)
- Mortgage payment history
- Re-calculation of the loan-to-value ratio to determine that, after release of the property and any paydown of the outstanding debt, the new LTV does not exceed the original insured loan-to-value ratio

When the loan amount is reduced as a result of a pay down, and a premium adjustment is required, the

lender will be notified. At that time PMI will provide a new Certificate of Insurance and a bill or refund for the adjusted premium amount.

### **3.4.15 SEASONED/CLOSED LOANS (11/09)**

Not eligible for insurance.

Seasoned/closed loans are defined as a loan that has been closed and has past the first payment due date.

## **3.5 LOAN PURPOSES (6/10)**

### **3.5.1 Purchase (12/06)**

Also known as a purchase money transaction, the funds are used to finance the purchase of the subject property. The proceeds may be used for the following:

- Finance the purchase of a property – both the land and improvements
- Payoff an installment land contract, including documented costs to improve the property. If the new loan exceeds the liens, this transaction must be considered a refinance
- Payoff recorded interim financing from the construction lender, for the permanent financing, as long as no cash is paid to the borrower
- Convert a lease option to purchase into permanent financing, as long as the borrower receives no cash from the new loan

The property seller in a purchase transaction must be confirmed as the Owner of Record for the subject property.

### **3.5.2 Refinance Transactions (4/15/11)**

A refinance transaction is defined as repayment of a debt from the proceeds of a new mortgage to the same borrower and that uses the same property as security. In some instances refinance transactions may have cash out.

If a subordinate lien to be paid off was not used for purchase of the subject property the loan will be considered a cash-out refinance transaction.

If the borrower has taken equity from the property (not a loan for home improvements) within the past 12 months through a new first deed of trust (cash-out refinance) the loan will be considered a cash-out refinance transaction.

If the borrower has taken equity from the property through a second lien, the loan will be considered a cash-out refinance transaction.

If the subordinate lien is not being repaid but will re-subordinate and there is no cash extracted from the transaction, the loan will be considered a rate/term refinance despite the age of the subordinate lien.

If the borrower has completed multiple transactions in the past 12 months, the value used to calculate the LTV must be the lowest appraised value determined during the 12 month period. The value can be increased based on documented improvements.

It must be confirmed and documented that the property Seller is the Owner of Record for the subject property for all transactions.

### **Continuity of Mortgage (4/15/11)**

All Refinance transactions must have a continuity of obligation for an existing lien, i.e., there must be at least one borrower on the new loan who was also obligated on the loan being refinanced.

### **Property Listed for Sale (4/15/11)**

For Rate/Term Refinance transactions, the subject property cannot be currently listed for sale; it must be removed from the market on or before the application date and the borrowers must confirm their intent to

occupy.

For Cash-out Refinances, Properties that have been listed for sale in the past 90 days are not eligible.

### **Rate/Term Refinance (4/15/11)**

The proceeds of a rate/term refinance may be used for the following:

- Payoff of the existing lien, including the related closing costs and prepaid items
- Payoff of a subordinate lien, (including prepayment penalty), provided a copy of the HUD1 from the original sale is obtained to verify the entire amount being paid off was used to purchase the property. The subordinate lien can be a second mortgage or HELOC (with no subsequent draws) that was used entirely for the subject purchase.
- Incidental funds not exceeding 2% of the loan amount or \$2,000, whichever is less

### **Cash-Out Refinance (4/15/11)**

Cash-out refinance transaction is defined as repayment of a debt from the proceeds for a new mortgage to the same borrower that uses the same property as security, providing cash to the borrower. The proceeds may be used for the following:

- Payoff of existing mortgage(s) and closing costs, greater than 2% of the loan proceeds, will be distributed to the borrower
- Payoff obligations of the borrower that are not secured by the subject property (i.e., a debt consolidation loan)
- Place a new loan on a property that is owned by the borrower free and clear of any mortgage
- Payoff or re-subordinate a junior lien that was not used entirely to purchase the property

The maximum cash-out to the borrower is \$150,000.

### **Special Purpose Cash-Out Refinance**

A loan being refinanced as part of a divorce settlement in which one spouse is required to “buy-out” the interests of the other spouse or any other refinancing in which an owner “buys-out” the interests of another owner is considered a rate/term refinance – as long as the following conditions are satisfied:

- The property must have been jointly owned by all parties for at least 12 months preceding the date of the loan application. (Parties who inherit an interest in the property do not have to satisfy this requirement)
- All parties must be able to demonstrate that they occupied the subject property as their principal residence, by providing an acceptable source of verification – drivers’ license, bank statement, credit card bill, etc., that was mailed to the individual at the address of the security property. (Parties who inherit an interest in the property do not have to satisfy this requirement).
- All parties must sign a written agreement that states the terms of the property transfer and the proposed disposition of the proceeds from the refinancing transaction (The borrower who acquires sole ownership of the property may not receive any of the proceeds of the refinancing).
- The party who is “buying out” the other party’s interest must be able to qualify for the mortgage under our standard underwriting guidelines

### **3.5.3 CONSTRUCTION-PERMANENT LOANS (7/11/11)**

A construction-to-permanent loan can be structured as a one- or two-time close may be considered a purchase or refinance loan.

A One-time Close is when the loan finances the construction phase and permanent loan in one instrument then, when the construction is complete, converts to the terms for the permanent financing. PMI will not insure the construction phase.

A Two-time Close is when the initial closed loan finances the construction costs; then a second loan is originated and closed as the permanent financing.

Both loans are subject to the standard underwriting guidelines and the following additional criteria:

- The long-term permanent financing, known as “permanent” or “end loan”, to replace the interim financing upon completion of the proposed home’s construction is eligible for insurance
- Maximum 95% LTV for conforming loans; maximum 90% LTV for jumbo loans

- Minimum 660 credit score for conforming loans; minimum 700 credit score for jumbo loans
- Purchase and Rate/Term Refinance only; Cash-out Refinance is not eligible. Reimbursement of borrower expenses in excess of the construction loan is considered cash-out and is not permitted
- Properties in Distressed Markets are not eligible
- Maximum term is 40 years
- The permanent loan can be a Fixed-rate Mortgage or Positively Amortizing ARM
- The borrower for the permanent financing must be the same as the borrower for the construction loan
- The loan must meet all other PMI underwriting guidelines

### Construction-Purchase Definition

- The borrower does not own the lot and is not currently the owner of record at the same time the construction loan is being obtained; or
- A Builder is the owner of the lot and construction has not started or is in the initial stages of construction at the time the property is sold.

### Loan-to-Value Calculations

- Construction-Purchase transaction the LTV will be based on:
  - The lot purchase price plus the documented cost of improvements, or the appraised value, whichever is less
  - When the lot is builder owned, the lesser of the appraised value or sales price
- Construction-Refinance transaction the LTV will be based on:
  - Property lot owned less than 12 months – The LTV is based on the original purchase price of the lot plus the documented cost of improvements; or the appraised value, whichever is less
  - Property lot owned 12 months or more - The LTV is based on the current appraised value
- A copy of the HUD1 from the original purchase transaction must be provided for the lot, when the lot has been owned for less than 12 months
- If the land is acquired by gift or inheritance, use the appraised value of the land; document the acquisition and transfer of the land
- Cost of Improvements is defined as the documented costs to build the home, the costs to obtain the construction and /or the permanent financing and the cost of the land, or value of the lot depending on when the lot was acquired
  - Construction costs may include building permits and architectural, survey, and loan fees
  - All acquisition costs must be verified by the construction lender and with a HUD1 for the purchase of the land
  - Reimbursement of borrower expenses in excess of the construction loan is considered cash-out and is not permitted

### Documentation

- All loans are required to have credit documents that are no more than 120 days old at the time of the underwriting and at the time the mortgage insurance is activated. Credit documents are defined as the documents used for income, assets, credit and appraisal
- All loans must be fully documented; document efficiencies are acceptable for DU/LP approved loans

### Appraisal Documentation

- Standard appraisal with an interior and exterior review is required
- A final inspection must be provided by the appraiser to indicate construction is complete
- Appraisals more than 120 days old up to 12 months old must be recertified. A new appraisal is required if the existing appraisal is more than 12 months old
- Ineligible:
  - 2055 Exterior review only
  - Drive-by inspections
  - Property Inspection Waivers (PIW) or Property Inspection Alternatives (PIA)

### Qualifying Ratios

- Maximum 45% DTI
- The PITI for the new home will be determined using the interest rate established for the permanent mortgage
- The borrower's current housing expense must be considered. The underwriter must evaluate the

borrower's ability to sustain payments on both the current residence and the new home during the construction period and after completion

- If documentation in the loan indicates that the borrower's current residence will be sold upon completion of construction, but is not under a non-contingent sales agreement, the borrower must qualify with both mortgage payments

### Mortgage Insurance

PMI will not insure loans during the construction phase. Loans that have a delinquency during the construction phase are not eligible for insurance. When the construction phase is complete and the permanent loan begins, prior to the commitment expiration date, the commitment must be put in-force by providing the certificate effective date for the loan, which can not be sooner than the permanent loan closing.

- The loan must be current at the time the commitment is put in-force
- Mortgage insurance coverage may be placed in-force once the property is complete per the specs and plans, final inspections have been made and certified by the appraiser with a Recertification of Value provided
- The Commitment/Certificate will be issued for a period of 12 months. Reinstatement/Extension is not permitted. To obtain mortgage insurance on a property where the commitment has expired, the loan must be resubmitted and meet PMI's current guidelines
- Mortgage Insurance on the permanent loan is ineligible if the borrower has any 30 day delinquencies during the construction phase
- For loans that are not delegated, a conditional commitment will be issued with the following conditions:
  - Appraisal and Credit Documents, including income and asset documentation and credit report, must be dated 120 days or less prior to MI effective date
  - Property must be completed at the time the mortgage insurance is placed in-force
  - Payment history for the construction loan or construction phase is required
- The lender must submit all conditions to the ROC for review and approval prior to the activation of the mortgage insurance
- When the documents are updated, the borrower must still qualify using the guidelines in place at the time of the original commitment
- Ineligible:
  - The construction phase of the loan
  - Properties located in a MSA/MSAD on PMI's Distressed Markets List, or identified on the lenders' list, or identified by the appraiser who has checked the "declining box" for property values
  - Non-traditional credit
  - Third party originations
  - Cash-out Refinance
  - Second Homes
  - 2-to-4 Unit Properties
  - Manufactured Housing
  - Cooperative Housing
  - Condominiums
  - Rehabilitation Loans
  - Investment properties
  - Potential Negative Amortizing ARMs
  - Option Payment Mortgages
  - Temporary buydowns
  - Limited documentation Loans

Losses are not covered for the borrower's inability to obtain a permanent loan or the lenders' failure to roll over or convert the construction loan to a permanent loan.

### 3.5.4 RELOCATION LOANS (4/15/11)

Relocation loans are those where an employer is relocating an employee to a new job location. The borrower must meet minimum down payment requirements and qualify with their prior home unless it is

being purchased by a relocation firm. The terms of the relocation must be specified by contract or letter to qualify the borrower. Relocation loans should generally conform to the following criteria:

- The mortgage loan is made to a transferred employee or to a newly hired employee, including military personnel - to finance the purchase of his or her primary residence at a new job location
- The employer normally transfers employees in the course of business
- The loan has been originated pursuant to a corporate employee relocation program administered by the corporate employer or its agent
- Mortgage financing may involve an employer contribution of the original principal balance of the new mortgage loan. Employer contributions may be applied toward any one or more of the following:
  - Closing costs
  - Buydowns or interest rate subsidies
  - Bridge loans
  - Payment differentials

### **3.5.5 LAND CONTRACT/CONTRACT OF SALE (12/06)**

If the land contract or contract for deed was executed more than 12 months preceding the mortgage application date, the transaction is considered a rate/term refinance transaction. Proceeds from the refinance transaction may include the sum of the outstanding balance of the installment sales contract and the costs incurred for rehabilitation, renovation, or energy improvements. A new appraisal is required and the LTV must be calculated using the appraised value for the new first mortgage transaction.

**SECTION 4 – ELIGIBILITY****4.1 OVERVIEW (12/06)**

PMI Mortgage Insurance Co. is limited by regulation to insuring indebtedness secured by first mortgage liens or Deeds of Trust on residential one- to four-unit properties. Loan eligibility requirements are maintained that are in compliance with Fannie Mae and Freddie Mac mortgage insurer eligibility criteria, Fair Lending, the Equal Credit Opportunity Act, and the State Insurance Departments' laws and regulations.

Due to our mortgage insurance charter, licensing, and states insurance laws or regulations, loans with the following characteristics, or secured by properties with these characteristics, will not be insured by PMI:

- Property which includes more than 4 residential units
- Property that is not located in the 50 United States, District of Columbia, Guam, or Puerto Rico
- Non-residential use of property, including vacant land, commercial or business activity on premises (except for incidental business use)
- Manufactured housing unit that is less than 22 feet wide
- Loan instruments which include scheduled negative amortization
- Property is located in New York and the loan includes negative amortization
- Property is located in New York or Washington state and loan-to-value ratio is less than or equal to 80%
- Property is located in Puerto Rico and loan-to-value ratio exceeds 100%
- Property located in Illinois, not a fixed-rate-fixed payment mortgage, secured by an owner-occupied, primary residence, and the loan to value exceeds 100%
- Property is located in Arizona, California, Idaho, Montana, New Jersey, New York or Ohio and the loan-to-value exceeds 103%
- Property is located in Kansas or Oregon, or is a fixed rate-fixed payment mortgage in Illinois, and the loan-to-value exceeds 105%
- Loans with a credit grade lower than "B"

**4.2 BORROWER ELIGIBILITY****4.2.1 BORROWER (12/06)**

PMI will only insure loans made to natural persons. Loans to borrowers that are other types of legal entities, such as corporations, general or limited partnerships, real estate syndications, or a trust (other than an Inter Vivos Revocable Trust) are not eligible for insurance.

**4.2.2 PERMANENT RESIDENT ALIEN (6/10)**

A permanent resident alien has the right to live and work permanently in the United States. Evidence of occupancy status for a permanent resident alien will be validated by one of the following documents:

- U.S. Citizenship & Immigration Services (USCIS) issues a United States of America Permanent Resident "Green Card" (I-151 or I-551)
- Un-expired foreign Passport with an un-expired stamp reading "Processed for I-551. Temporary evidence of lawful admission for permanent residence. Valid until (MM/DD/YY). Employment authorized".

### 4.2.3 NON-PERMANENT RESIDENT ALIENS (4/15/11)

A non-permanent resident alien has the right to live and work in the United States on a temporary basis and is eligible for mortgage insurance, except those with VISA status types for Diplomatic Immunity or temporary business use. USCIS approval will include valid dates of the stay. The employer or alien must petition the USCIS for an extension. Evidence of occupancy status for a non-permanent resident alien will be validated by one of the following documents:

- Unexpired foreign passport containing INS form I-94 stamped "Employment Authorized"
- Unexpired Visa that allows borrower to work
- I-797 Notice of Action/Notice of Approval form with valid extension dates and the I-94 Arrival/Departure Receipt

#### Additional Underwriting Consideration for Non-Permanent Resident Alien Borrowers

The following consideration should be given when underwriting loans to non-permanent resident alien borrowers:

- Employee information on the Petition for Nonimmigrant Worker (form I-140) must correspond to the borrower's *Residential Loan Application*
- Loans to non-permanent resident aliens will be considered for coverage subject to the following criteria
  - Borrower must evidence a two-year history of residency, employment, and established credit within the U.S.
  - Funds for down payment, closing costs, and reserves should be verified on deposit in a U.S. financial institution
  - The visa status should provide for a remaining duration of at least three years
  - Heavy emphasis will be placed on employment history and its likelihood of continuation

Non Resident Aliens do not reside continuously in the United States and do not have authorization to work here. Loans to non resident aliens are not eligible for insurance with PMI.

### 4.2.4 NON-OCCUPANT CO-BORROWERS (4/15/11)

Non-occupant co-borrowers will be considered if:

- The Non-occupant co-borrower is not a party to the transaction (i.e., builder/developer, seller, Realtor®, escrow agent, etc.)
- The property is Owner-occupied to a maximum LTV of 95%
- Occupant borrower contributes a minimum 5% cash down payment to the transaction
- Occupant borrower has verified reserves from their own funds
- Occupying borrower's ratios, without consideration of non-occupying co-borrower's income and obligations, should not exceed the ratio guidelines

### 4.2.5 NON-BORROWING SPOUSE (8/08)

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 of state community property or marital rights laws.

- If the non-borrower spouse is to be included on the deed as a co-owner, the non-borrower spouse must sign the security instrument
- If the non-borrower spouse is not included on the deed, they are not required to sign the security instrument. A quitclaim deed may be required to ensure a valid security instrument is established for the borrower.
- Pursuant to the California Domestic Partner Rights and Responsibilities Act of 2003, a domestic partner may have community property and homestead rights in property owned by their partner. In

Vermont, a party to a civil union may have homestead rights in property owned by their partner. In New Jersey, civil union couples shall have all the same benefits, protections, and responsibilities under the law. Non-borrower spouse signature requirements will apply to non-borrower domestic and civil union partners on loans secured by California, Vermont and New Jersey property.

Debts and income from the non-borrower spouse cannot be considered in qualifying the loan.

### 4.2.6 CO-SIGNERS / GUARANTORS (12/06)

A guarantor or co-signer is an applicant who will not have an ownership in the mortgaged property, but will sign the Note and Deed of Trust/Mortgage. A party who has an interest in the property sales transaction – such as the property seller, the builder, the real estate broker, etc – is not eligible to be a co-signed/guarantor. PMI will insure a loan with a Co-signer/Guarantor; however, their income and assets cannot be used for qualifying purposes.

### 4.2.7 ADDING/REMOVING BORROWERS ON APPLICATION (12/06)

To remove a borrower from a transaction, a new application and credit report must be provided for the remaining borrower only. Additional borrowers may be added during the application process without the need to resubmit as a new transaction.

### 4.2.8 MAXIMUM PMI INSURED LOANS PER BORROWER (11/09)

PMI will insure up to **3** loans to a borrower or borrowing entity or \$300,000 in risk exposure (aggregate of original loan amount x percent of MI coverage) to a borrower or borrowing entity.

Within the 3 loans to a borrower, PMI limits the loans by product/program as follows:

- Primary Residence - 1 loan maximum
- Second Home – 1 loan maximum
- Investment Property – 1 loan maximum (currently insured)
- Limited Doc – 1 loan maximum (currently insured)
- Interest Only – 1 loan maximum (currently insured)

## 4.3 OCCUPANCY

### 4.3.1 PRIMARY RESIDENCE (5/16/11)

A primary residence is defined as single family property which is the borrower's main residence, where they live a majority of the year. Owner-occupied 3-4 unit properties are not eligible for insurance.

PMI will also insure a loan:

- when parents want to provide housing for their physically handicapped or developmentally disabled adult child who is unable to work or does not have sufficient income to qualify for a mortgage on his or her own, the parent is considered the owner/occupant; or
- when children want to provide housing for elderly parents if the parent is unable to work or does not have sufficient income to qualify for a mortgage on his or her own, the child is considered the owner/occupant.
- Lenders' must document the file to support the circumstances, i.e. the elder parents can't afford the home.

### 4.3.2 SECOND HOME (4/25/11)

A second home is a single-family property which generates no rental income and is occupied by the borrower in addition to his or her primary residence. A minimum 5% down payment is required from the borrowers own funds. Second homes must meet the following:

- Property is a one unit property, single family, attached or detached, condominiums or cooperative
- Property is located a reasonable distance from the borrower's primary residence; it can not be in the same location as the borrower's primary residence
- Property can be located in a resort area, recreation area or urban area; as long as it can be reasonably considered a location where most people would want a second home
- The property is suitable for year round occupancy, and will be occupied by the borrower for some portion of the year
- Agreements that require the property to be rented are prohibited, i.e. must not be a rental property or timeshare
- The property may not be a part of a rental pool, have a management firm control the occupancy of the property and can not be a timeshare

**Ineligible:**

- 2-4 unit property

### 4.4 PRIMARY RESIDENCE CONVERSION (OWNER CONVERSION) (3/1/11)

PMI requires the following when a borrower is purchasing a new home that requires insurance and has an existing primary residence which will then be converted to a second home or investment property instead of being sold. The borrower must have sufficient equity and/or reserves verified to support both the existing financing and the new mortgage being originated.

**All Intended Uses of the Current Primary Home**

- The borrower must qualify using both the current PITI payment as a debt and the new PITI payment for the new property
- The borrower must have six months' verified PITI reserves for both properties
- The current residence has been owned for a minimum of twelve months, with no cash out transactions with in the prior six months
- If the current residence is a pending sale, but the sale will not be completed prior to the new property closing, the reserves can be reduced to two months provided there is a documented minimum 30% equity in the property (via an appraisal, AVM, or BPO, or executed sales contract). When the executed contract is provided it is not necessary to count the PITI in the debt qualification if the financing contingencies have been removed.

**Primary Home Converts to a Second Home**

- Both the current and proposed mortgage payment must be used to qualify the borrower for the new transaction; and
- Six months' PITI for both properties is required to be verified in reserves. Reduced reserves of no less than two months for both properties may be considered, if there is documented evidence (via an appraisal, AVM, or BPO) of at least 30% equity in the existing property
- Normal second home requirements must be met, i.e., property is in a resort-like area, etc. The home cannot be considered a second home just because the borrower decides to purchase a new primary residence. If the existing primary home location does not meet second home guidelines, it can be considered using the investment property guidelines stated below

**Primary Home Converts to an Investment Property**

- Up to 75% of rental income can be used to offset the mortgage payment IF there is documented evidence (via an appraisal, AVM, or BPO) of 30% equity in the existing property
- The rental income must be documented with:
  - A copy of the fully executed lease agreement; and
  - The receipt of a security deposit from the tenant AND verified deposit into the borrower's account
- Six months' PITI for both properties is required to be verified in reserves. Reduced reserves of no less than two months for both properties are permitted if there is documented evidence (via an

appraisal, AVM or BPO) of at least 30% equity.

- If 30% equity in the property cannot be documented, rental income may not be used to offset the mortgage payments
  - Both the current and proposed mortgage payments must be used to qualify the borrower for the new transaction; and
  - Six months' PITI for BOTH properties is required to be verified in reserves

These guidelines are applicable to manually underwritten loans not approved through DU® or LP.

Properties not eligible to be converted:

- If the borrower indicates that the primary residence was previously listed for sale in the past 90 days, and now indicates that it will be a rental or second home, this could be considered a red flag; therefore PMI will not offer insurance on the new property.
- If the borrower has not owned their current residence for 12 months and is purchasing a new home in the same town with a same or lesser value than their existing home, and indicate that the existing home will be a rental or second home, this could be considered a red flag; therefore PMI will not offer insurance on the new property.
- If there is documented evidence of a job transfer, the 90-day listing and ownership of 12 months restrictions will not apply.

Additional Issues:

- If the borrower's current residence is owned free and clear, appropriate documentation for the state should be provided to document there are no liens and to document the current taxes and insurance costs. The TI would be used to qualify the borrower.
- Common sense should be utilized when the borrower is purchase a new residence but has not owned their current residence for more than twelve months; the borrower may have genuine reasons for the move, such as living in a duplex and moving to a single family, or living in a condo and purchase a single-family. These situations must be considered on a case-by-case basis.

### 4.5 SECONDARY FINANCING (12/06)

Secondary financing may be accepted provided that it is fully disclosed in the mortgage insurance application and the maximum combined loan-to-value ("CLTV") does not exceed the CLTV criteria for the borrower's occupancy, loan type, and property type. The loan will be underwritten using the eligibility criteria applicable to the LTV; distressed markets policy will apply. For example:

Total financing which includes an 85% LTV first mortgage and a 10% second (95% CLTV) on a 1 unit property will be eligible for coverage since 1 unit properties are limited to 95% CLTV.

#### Underwriting Criteria for loans with Subordinate Financing

The mortgage insurance premium rate and premium amount will be will be determined by the insured first lien amount. The underwriter should confirm that the terms of the subordinate financing meet the following minimum requirements:

- The second mortgage is recorded and subordinate to the insured first lien
- The second mortgage is either fully amortizing or interest only and payments are no less frequent than annual
- If the second lien calls for a balloon payment, the term of the second lien is no less than five years.
- The second lien will not negatively amortize
- Payment for the second lien is added to the monthly housing expense and included in the borrower's housing-to-income ratio. If payments are made quarterly, semi-annually, or annually, the monthly equivalent payment should be used.
- If the secondary financing is an Equity Line of Credit, the following criteria apply:
  - Terms of the equity line of credit are disclosed in the mortgage insurance application package
  - The equity line of credit will be recorded and subordinate to the insured first mortgage

- The property is an owner-occupied, primary residence
- The CLTV ratio is calculated using the maximum amount of the equity line of credit

Repayment terms will include regular payments that cover, at minimum, interest due on the outstanding balance (Negative amortization is not allowed)

### 4.6 SEASONING OF EXISTING LIENS (11/09)

A first lien need not be seasoned to be eligible for a rate/term refinance. If, however, the property was purchased within the past 12 months, the loan-to-value ratio will be determined using the lesser of the purchase price plus value of documented improvements or current appraised value.

If the borrower has taken equity from the property within the past 12 months through a new first deed of trust (cash-out refinance) the loan will be considered a cash-out refinance transaction.

If the borrower has taken equity from the property through a second lien, the loan will be considered a cash-out refinance transaction.

### 4.7 Other Eligibility

#### 4.7.1 PROPERTY FLIPPING (3/1/11)

It is critical for all transactions that the property seller be the owner of record for the subject property on publically available documents. The lender should confirm that the seller on a purchase, or the borrower on a refinance, show as the owner of record when a new appraisal is required. Examples of acceptable documentation include:

- The appraiser's analysis and conclusions in the appraisal report
- A copy of a recorded deed or mortgage
- A recent property tax bill or tax assessment notice
- A title report
- A title commitment or binder
- A property sale history report

This documentation is especially important for transactions involving a purchase contract that has an assignment (or sale) and /or "back-to-back", "simultaneous", or double escrows to support the property acquisition, financing and closing.

It is critical for the lender to analyze and review the sales of the subject property, and the sales price trend in relation to the appraiser's opinion of value, to confirm that they are reasonable and representative of the market.

If the seller acquired the subject property less than 90 days from the date of the purchase contract, the loan is generally not eligible for mortgage insurance. However, it can be considered by submitting the non-delegated loan to the National Underwriting Center for a full underwrite.

We expect that the lender will review the appraisal on any property flips over 90 days prudently, determining that the property value has increased due to value-added improvements, not just cosmetic improvements, insuring that the value increase is appropriate for the marketplace.

The following property sales/transfers are not required to meet this policy. The seller is:

- A lender, mortgage investor, or a mortgage insurance company that acquired the property as a result of a foreclosure, or a deed in lieu of foreclosure
- A spouse who acquired the property through a divorce settlement
- An employer that acquired the property through its relocation program
- An administrator, executor, or personal representative selling property of an estate

The underwriter must analyze the appraisal to determine:

- What has been improved, and if the improvements have been completed in a professional and workmanlike level
- If the appraiser indicates the improvements meet local codes
- If the neighborhood supports the improvements (could be over-improved)
- That the appraiser did not give dollar-for-dollar value increases in the value for the improvements, but justified any adjustments with comparables

### 4.7.2 INTER VIVOS REVOCABLE (“LIVING”) TRUST AND LAND TRUSTS (12/06)

Inter Vivos and Land Trusts are eligible provided that all of the following conditions are met:

- They are customary for the area
- The borrower (beneficiary of the trust) is a natural person
- Income and assets of the borrower (beneficiary) are used to qualify for the loan
- Both the borrower (beneficiary) and trustee, on behalf of the trust, execute the Note, and the borrower (beneficiary) is personally liable for the obligation
  - The trustee has legal right to grant a mortgage on the subject property
  - The lender will be conveyed clear title in the event of default by the borrower (beneficiary)

### 4.7.3 NON ARM’S LENGTH TRANSACTIONS (12/06)

A non arm’s length transaction is one in which the parties involved are not entirely independent of each other (i.e., family sales between parent and child, property in an estate, employee and employer, direct sale without a third party, renter and landlord, or flip transactions).

These loans require close examination to ensure that the equity position is not compromised. 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.

The appraiser must be informed of the non arm’s length transactions and discuss whether or not the market value has been affected by the relationship of the parties.

### 4.7.4 MAXIMUM LOAN TERM (12/06)

The term of the insured loan cannot exceed 40 years. There is no minimum loan term.

### 4.7.5 MINIMUM LOAN AMOUNT (12/06)

There is no minimum loan amount.

### 4.7.6 INTERESTED PARTY/SELLER CONTRIBUTIONS/THIRD-PARTY CONTRIBUTIONS (IPCs) (4/15/11)

Third-party contributions/IPCs are either a financing concession or a sales concession. IPCs are limited to interest rate buydowns, reasonable and customary closing costs that are normally paid by the borrower but which, in the subject transaction, are paid by the seller or other interested party such as the builder, developer, or real estate agent and any other payments or credits related to acquiring the property.

A lender or employer is not considered an interested party to a sales transaction unless it is the property seller or is affiliated with the property seller or another interested party to the transaction.

**Financing Concessions** include, but are not limited to, the following:

- Any third-party funds that are contributed to an interest rate buydown plan for the purpose of temporarily or permanently lowering the borrower’s payment and/or interest rate on the mortgage

- Contributions and payments in any form, such as:
  - Discount points
  - Commitment fees
  - Origination fees
  - Appraisal costs
  - Transfer taxes, stamps or attorneys fees
  - Interest rate shortfalls
  - Title insurance
  - Survey charges
  - Prepaid items such as hazard insurance premiums, interest charges, real estate taxes
- Donations by interested parties to a non-profit organization when the recipient of the funds entitles the borrower to a grant or down payment assistance will be considered a third-party contribution.

**NOTE:** Cash deposited by the borrower at closing to fund future payment of taxes, insurance, or other recurring expenses (generally referred to as impounds or escrow funds) must be paid from the borrower's own funds. If these items are paid by the seller or other third-party related to the transaction, they should be considered a sales concession.

#### 4.7.7 MAXIMUM ALLOWABLE CONTRIBUTIONS (3/1/11)

A maximum 3% of the property's sales price or appraised value, whichever is less, is allowed for:

- Loans with LTVs greater than 90%
- Properties in distressed markets

A maximum 6% of the property's sales price or appraised value, whichever is less, is allowed for:

- Loans with LTVs of 90% or less
- Jumbo loans (except in distressed markets)

#### 4.7.8 OTHER THIRD-PARTY CONTRIBUTIONS (4/15/11)

Contributions made by the borrower's employer or a family member are not included in the Maximum Allowable Contributions limitation. A family member's contribution is considered a gift and must comply with requirements for gift funds. Employer contributions are permissible if verified under the terms and conditions of an employee relocation agreement.

#### 4.7.9 SALES CONCESSIONS (1/08)

Sales concessions are interested party contributions (IPCs) that take the form of non-realty items, such as furniture, decorator allowance, giveaways (vacations, cars) and excess financing concessions. The terms of the sale as detailed in the purchase contract must be closely evaluated to determine the effect of any sales concessions. Sales concessions must be deducted from the lower of the purchase price or appraised value. For example:

\$ 101,000	Sales Price
100,000	Appraised Value
\$ 2,000	Concession Amount
Calculation:	
\$ 100,000	Appraised Value (lower of Sales Price/Appraised Value)
<u>- 2,000</u>	Concession Amount
<u>\$ 98,000</u>	Adjusted Value

The Loan amount would be calculated using the adjusted value and the maximum LTV for the product or program.

## Decorator Allowances

A decorator allowance may be included in seller-paid closing costs rather than considered a sales concession if there is an offsetting upgrade to the improvements (i.e., ceramic tile instead of linoleum, thermal pane windows, upgraded insulation, etc.). The sales contract must describe the upgrades. The Maximum Allowable Contributions limitations for third-party contributions, including these decorator allowances, will apply.

If the amount is a direct cash credit to the borrower on the HUD-1, it must always be treated as a sales concession and deducted from value.

## Excess Contributions

Financing contributions in excess of the limits should be considered sales concessions. In these instances, the amount of the concession must be subtracted from the lesser of the sales price or appraised value in order to determine LTV. For example:

\$ 7,840	Actual seller contributions
\$ 88,200	Loan amount
\$ 98,000	Sales price
\$ 100,000	Appraised value

On a 90% LTV fixed-rate mortgage, the maximum allowable contribution is 6% or \$5,880. The LTV ratio should be calculated on the reduced sales price (Adjusted Value) as follows:

\$ 98,000	Sales price (lesser of the sales price or appraised value)
\$ - 1,960	Excess contribution which is considered a sales concession (\$7,840 - \$5,880)
<u>\$ 96,040</u>	Adjusted Value

As a result, the adjusted LTV becomes:

\$ 88,200	Original Loan Amount
÷ 96,040	Adjusted Value
=	91.8% LTV

This example illustrates the effect of excess seller contributions. In order for this loan to be considered a true 90% LTV, the loan amount must be reduced to \$86,400:

\$ 86,400	Adjusted Loan Amount
÷ 96,040	Adjusted Value
=	90.0% LTV

If the loan amount is reduced to an adjusted LTV of 90%, the lender must verify sufficient funds to close. Otherwise, the loan should be underwritten and insured as a 91.8% LTV using 95% LTV loan eligibility criteria and premium rates.

## SECTION 5 – UNDERWRITING AND CREDIT

### 5.1 Underwriting Overview (11/09)

PMI assesses the characteristics indicative of the borrower's willingness and ability to repay the debt in a timely manner and ensures that the property securing the loan provides sufficient value for recovery if a mortgage default should occur.

These guidelines should not restrict underwriters from making good common-sense decisions. The underwriting process must continue to support viable business opportunities while also maintaining a quality book of business.

When PMI's underwriting manual is "silent" and does not address a guideline, the lender must follow Agency standard guidelines. If the lender typically uses Fannie Mae or Freddie Mac guidelines for underwriting, then those guidelines would apply when PMI is silent.

See pmiAFFORDABLE in **Section 3.4.6** guidelines for low- and moderate-income borrowers.

#### 5.1.1 LOAN APPLICATION ANALYSIS (12/06)

The mortgage application is the primary document that is used to establish the initial profile of the borrower. The borrower's application for a mortgage loan must be documented on the most current version of the FNMA/FHLMC Uniform Residential Loan Application. The loan application must contain sufficient information for the underwriter to reach an informed decision about whether to approve the loan for mortgage insurance. Additionally, a FNMA/FHLMC Uniform Underwriting and Transmittal Summary should be provided to summarize the key data from the loan application.

The initial loan application should be signed and dated by the borrower. A copy of the Agreement of Sale/ Sales Contract/Purchase and Sales Agreement, and/or Escrow Instructions should be provided to verify, clarify, and substantiate the loan application. Information given by the borrowers on the original application, whether handwritten or typed, must be consistent with both the identifying information in the credit report, as well as, the other verifications provided. All the subsequent documentation provided should support the information contained in the application.

Many lenders use loan origination software to prepare the final 1003; certain fields default to the most common response. To be sure that the "no" answers in the declarations is not just a typographical error, it is recommended that the underwriter review the borrower's handwritten loan application to verify consistency.

#### 5.1.2 COMPENSATING FACTORS (2/10)

Compensating factors are positive loan characteristics that add strength to a loan profile. They can be utilized when there are weaknesses in the file that need to be offset. Compensating factors are:

- The borrower demonstrates the ability to maintain a good credit history, accumulate savings, and maintain a debt-free position
- There is less than a ten point spread between the new housing debt ratio and the total debt ratio
- The borrower has significant equity in other real estate owned, generally 30% or higher
- The mortgage payment is being reduced and the borrower has had no late mortgage payments in the past 24 months
- The borrower has demonstrated the ability to devote a greater portion of income to housing expense as evidenced by the borrower's current housing and total debt ratios
- The current debt ratio will be reduced with new mortgage
- The borrower's current rent/housing payment is greater than, or equal to, the new housing (PITI) payment
- The new mortgage payment does not exceed 110% of the prior/existing mortgage or rental payment

- The new mortgage payment is less than the current housing (PITI) payment, or the new mortgage payment is equal to the existing payment, but the loan instrument has been improved
- The borrower has excellent liquid assets, represented by verified CDs, savings accounts, checking accounts, stocks and bonds (not retirement accounts) that are equal to at least 12 months PITI
- The borrower has additional short-term income (such as Social Security income, alimony, child support, note receivables, mortgage differential payments, trust income, VA benefits) that could not be counted as “stable” income because the income stream will not continue for at least three years beyond the date of the loan application

If these or any other conditions are considered, adequate documentation to support the compensating factors should be included in the loan file and de/tailed on the 1008.

### 5.1.3 AUTOMATED UNDERWRITING SYSTEM (3/28/11)

Loans submitted and approved by Desktop Underwriter® (DU®) and Loan Prospector® (LP®) see Section 3, Programs for PMI's DU/LP program.

All other automated underwriting system decisions (proprietary or custom) must meet PMI's eligibility and guidelines.

**Ineligible:**

- DU Refer, Refer with Caution IV, out of Score, and EA I, II, and III- Version 5.7 or earlier
- LP Caution or Caution A-Minus

## 5.2 CREDIT DOCUMENTATION AND EVALUATION

### 5.2.1 CREDIT REPORT (12/06)

A Residential Mortgage Credit Report, or tri-merged credit report (additional credit requirements may be applicable based on DU®/LP findings) from an independent credit reporting agency, is required.

Individual credit reports for all borrowers are required. Joint credit reports on married couples will be acceptable if the report clearly indicates a search of individual credit. The credit report should reflect the borrower's overall debt payment history and a public record search for each locality in which the borrower has lived during the past two years. The legal search must disclose whether any judgments, foreclosures, litigation, collections, garnishments, bankruptcies, or divorce actions were filed.

The credit report should provide the terms, balances, and ratings for all debts listed on the loan application. If the credit report does not contain a reference for each significant open debt on the loan application, including an outstanding mortgage loan, the lender should provide separate, direct credit verification.

A business credit report to supplement the individual credit report for a self-employed borrower may be requested at the underwriter's discretion.

### 5.2.2 CREDIT BUREAU ALERTS (12/06)

All three credit reporting bureaus now offer fraud detection, which alerts creditors to possible discrepancies. Called Hawk Alert, Safescan, and FACS, they identify possible inconsistencies between the loan application and the credit report. These inconsistencies can identify issues with the borrowers surname, current residence, invalid addresses or telephone numbers, employment, and Social Security Number. It is important that the underwriter review these notifications/alerts, confirming all information matches the information provided on the loan application, resolving any discrepancies. Below are some examples of actions that should be taken for the various alert messages:

- “...high probability Social Security number belongs to another.” If this statement appears, it may not be a misrepresentation. For instance, if a middle name or middle initial is not disclosed on the application, this may generate an alert. However, another name associated with the borrowers'

name, address, or social security number would warrant further investigation.

- "...SS reported deceased" or "SS # not issued by the Social Security Administration." There is a high probability of misrepresentation with these alerts. The underwriter must determine if there was an error in reporting.
- "ID Mismatch Alert" – Previous input address does not match file address. This could be an input error, or may indicate the borrower's primary address was misrepresented.
- "Telephone number inconsistent with address." This alert would require further investigation of the borrower's current address versus the correct phone number.
- "Employer is shown as self-employed." This alert would require further investigation to determine if the borrower's stated employer is actually a self-employed business.
- "OFAC Name Screen." Designed to screen an applicant's name against an enhanced U.S. Treasury Department's Office of Foreign Assets Control (OFAC) database of specially designated nationals, drug traffickers, and money launderers. Borrowers who are confirmed on this list are not eligible for mortgage insurance.
- "Borrower is a victim of fraud – contact Borrower prior to issuing new credit." This alert would require the borrowers be contacted to confirm they are pursuing new credit.

### 5.2.3 MULTIPLE SOCIAL SECURITY NUMBERS (12/06)

Under **extremely** rare circumstances, borrowers will have two social security numbers, generally due to a Social Security Administration error or if they are part of an INS amnesty program. Such situations are acceptable if the borrower provides an acceptable letter of explanation and the credit history has been checked and no derogatory credit is reported under both numbers.

### 5.2.4 CREDIT EVALUATION (4/15/11)

The borrower's credit history must be carefully evaluated to determine the borrower's credit reputation (i.e., his or her willingness to meet financial obligations under the agreed-upon terms). While credit reputation is a significant factor of risk, it is weighed against the borrower's capacity (financial ability) to meet the mortgage obligation, and compensating factors, such as the loan terms and down payment, when rendering an underwriting decision. Generally, a loan will not be declined for mortgage insurance based on only one component of risk.

When evaluating the credit report, the underwriter should always consider the borrower's entire credit history. However, more weight should be given to the borrower's paying habits within the most recent two years. The following factors should be considered:

- The type and amount of outstanding credit
- How long the borrower has had credit
- How the borrower uses available credit
- Recent changes in the number of open accounts or overall amount of credit outstanding
- The payment history and status of all open accounts
- Any recent inquiries shown on the credit report
- All public record or collection items

The borrower's credit history should reflect the following:

- 0x30 mortgage late payments in the last 12 months (non DU/LP loans)
- 0x60 mortgage late payments in the last 12 months (DU/LP loans)
- 0x60 installment or revolving account late payments in the last twelve months

When analyzing the credit report, close attention should be given to the following:

#### **Balance-to-Credit Limit**

The underwriter should evaluate the borrower's ability to manage credit. A pattern of revolving accounts at or near their limits, especially when combined with newly opened accounts, may indicate that the borrower is at risk of becoming overextended. A pattern of high balance-to-limits may also indicate the

following risk characteristics:

- The borrower is making minimum payments on revolving accounts rather than reducing the debt and, therefore, may be near his or her credit capacity.
- The borrower relies on credit to meet day-to-day living expenses.
- The borrower will have no "cushion" for short term interruptions of income or emergencies such as a costly auto repair or replacing a hot water heater. Any such event could trigger a financial set-back and, possibly, mortgage delinquency.
- The borrower lacks the financial experience to manage credit.

### **Excessive Use of Credit**

Caution must be exercised if the borrower is carrying a significant amount of consumer debt. Numerous revolving accounts which are at or near their limit may indicate that the borrower is living beyond his/her income level.

The underwriter should review the spread between the mortgage- and total debt-to-income ratios. An excessive spread is generally considered to be an amount greater than 10 points. Particular attention should be given to the borrower's credit pattern when underwriting refinance transactions to ascertain that the borrower does not have a history of debt consolidation through refinancing.

### **Recent Inquiries**

If the credit report shows recent inquiries, the underwriter must determine if credit has been granted as a result of the borrower's request. A letter from the credit provider, or an update to the credit report, may be accepted as verification of the disposition of the credit requests.

Recent inquiries may simply mean that the borrower is searching for the most favorable mortgage terms. It may, however, indicate increased credit risk, such as the following:

- The borrower intends to borrow funds for the earnest money deposit, down payment, or closing costs
- The borrower is marginally qualified and has been rejected by other mortgage lenders; the loan is being "shopped"
- The borrower is attempting to "leverage" his or her financial position
- The borrower is in danger of over-extending their credit

### **Age of Accounts**

Recently opened accounts, or recent, significant increases in account balances, may indicate that the borrower is using credit for the earnest money deposit, down payment, or closing costs for the mortgage, is in danger of over-extension of credit, or lacks sufficient financial experience to manage credit.

### **Authorized Users of Credit**

An authorized user tradeline may be considered when analyzing the borrower's credit history/payment if it meets Agency guidelines; however, cannot be used to validate the credit score.

### **Credit Counseling (Effective 1/1/10)**

If the borrower has accounts listed on the credit report as credit counseling, the borrower must have completed their credit counseling to be eligible for mortgage insurance. After completion the borrower must have established a minimum of three current, active, and open accounts with a minimum of twelve months history and no late payments.

## **5.2.5 DEROGATORY CREDIT ISSUES (4/15/11)**

### **Derogatory Credit / Slow Payment Patterns**

When derogatory credit appears on the credit report, or through direct verification of credit, the underwriter must determine if late payments were related to an isolated event, which is not likely to reoccur, or represent a pattern of disregard for obligations.

Delinquent mortgage credit must be closely analyzed. A pattern of 15-day lates on a mortgage may indicate that the borrower has difficulty making payments. Delinquencies over 30 days reflect the borrower's inability to pay or disregard for credit obligations.

### **Collections, Judgments, Charge-offs, Litigation, Garnishments, and Repossessions**

These items should generally be paid in full, or satisfied at, or prior to closing and are required to be paid in full if they will affect the mortgage loans first lien title position.

### **Tax Liens**

State and federal tax liens must be paid in full at or prior to closing, as they will affect the mortgage's first lien position.

### **5.2.5.1 LETTER OF EXPLANATION FOR ABOVE DEROGATORY ITEMS (4/15/11)**

When the underwriter determines that the derogatory credit is deemed relevant to the underwriting decision, a written letter regarding the recent slow payments, excessive number of slow payments, late payments on mortgages, or other derogatory credit should be provided by the borrower to fully explain the circumstances for the delinquencies. However, this is not a required document.

The borrower must have established other good credit. Favorable consideration may be given, based on "reasonableness" of the explanation and if all other credit is paid "as agreed."

### **5.2.5.2 BANKRUPTCY (4/15/11)**

#### **Bankruptcy**

To be considered for mortgage insurance approval, a bankruptcy must be fully discharged for at least four years (with documented extenuating circumstances a bankruptcy discharged for two years will be considered). The borrower must have subsequently re-established credit.

A loan to a borrower, whose bankruptcy was discharged within the past two years, is not considered eligible for insurance.

**Multiple Filings:** Borrowers who have multiple bankruptcy filings within the last seven years may be eligible for insurance; however, a five year waiting period is required, and careful review of the circumstances that cause multiple filings must be conducted to ensure the borrower has over come the difficulties that caused the filings.

#### **Re-Established Credit:**

The borrower must re-establish good credit, demonstrating the ability to manage financial affairs. The credit report should not reflect any serious derogatory credit since the date of discharge (i.e., no mortgage or housing-related late payments, no collections, judgments, liens, or garnishments, no revolving or installment accounts 60 or more days late and only isolated incidents of 30-day late payments on revolving accounts).

**Extenuating Circumstances:** A bankruptcy beyond the borrower's control, such as one resulting from extended family illness, should receive more favorable consideration than one that has occurred because of poor financial management. In all cases, the borrower should furnish satisfactory written explanation, copies of documentation supporting the event and illustrating factors that contributed to the inability to resolve the problems that occurred from the event have been resolved, copies of the bankruptcy petition, schedule of debts, and evidence of discharge.

<b>Summary of Bankruptcy Waiting Periods</b>		
<b>Derogatory Event</b>	<b>Waiting Period Requirements</b>	<b>Waiting Period with Documented Extenuating Circumstances</b>
Chapter 7 or 11	4 years	2 years
Chapter 13	Discharged – 2 years Dismissed – 4 years	Discharged – NA Dismissed – 2 years
Multiple Filings	5 years	3 years

### **5.2.5.4 FORECLOSURE (4/15/11)**

#### **Foreclosure**

A borrower who has been foreclosed upon should be considered as high risk, and the circumstances for the event considered carefully.

The loan to a borrower, who was foreclosed up to seven years prior to the new loan application date, should be evaluated on a case-by-case basis only. With acceptable documented extenuating circumstances, the new loan can be considered after 3 years, provided the LTV does not exceed 90%. The circumstances surrounding the foreclosure and the borrower's written explanation must be carefully evaluated. Documentation must be provided to support the borrower's statements regarding the extenuating circumstances surrounding the foreclosure, and should validate the timelines and events that caused the foreclosure.

Extenuating circumstances should be granted only if the foreclosure sale resulted from a regional catastrophe beyond the control of the borrower. For example:

There was an economic downturn that caused wide-spread unemployment and resulted in the loss of property value. The borrower (1) lost his/her job; (2) he/she accepting a lower paying job and depleted all savings while attempting to maintain timely debt repayment; (3) due to the out-migration of population, there was no market for the property (hence, values declined); and (4) the borrower had to relocate to find employment in his/her field.

If the borrower has successfully regained financial strength and demonstrates favorable regard for obligations, positive consideration may be given.

Conversely, if the borrower has derogatory credit since the foreclosure (even though it might be considered minor), has incurred excessive obligations, or has not demonstrated an ability to save, he/she has not proven to be a favorable risk and should not be considered eligible for coverage.

### **5.2.5.5 DEED-IN-LIEU, SHORT SALE (4/15/11)**

#### **Deed-in-Lieu / Short Sale**

A borrower who has given a deed-in-lieu of foreclosure or short sale should be considered as high risk, and the circumstances for the event considered carefully.

The loan to a borrower, who gave a deed-in-lieu/short sale up to seven years prior to the new loan application date, should be evaluated on a case-by-case basis only. With acceptable documented extenuating circumstances, the new loan can be considered after 2 years, provided the LTV does not exceed 90%. The circumstances surrounding the deed-in-lieu/short sale and the borrower's written explanation must be carefully evaluated. Documentation must be provided to support the borrower's statements regarding the extenuating circumstances surrounding the deed-in-lieu/short sale, and should validate the timelines and events that caused the deed-in-lieu/short sale.

Extenuating circumstances should be granted only if the deed-in-lieu/short sale resulted from a regional catastrophe beyond the control of the borrower. For example:

There was an economic downturn that caused wide-spread unemployment and resulted in the loss of property value. The borrower (1) lost his/her job; (2) he/she accepting a lower paying job and depleted all savings while attempting to maintain timely debt repayment; (3) due to the out-migration of population, there was no market for the property (hence, values declined); and (4) the borrower had to relocate to find employment in his/her field.

If the borrower has successfully regained financial strength and demonstrates favorable regard for obligations, positive consideration may be given.

Conversely, if the borrower has derogatory credit since the foreclosure (even though it might be considered minor), has incurred excessive obligations, or has not demonstrated an ability to save, he/she has not proven to be a favorable risk and should not be considered eligible for coverage.

### Summary of Foreclosure / Deed-in-Lieu / Short Sale Waiting Periods

Derogatory Event	Waiting Period Requirements	Waiting Period with Documented Extenuating Circumstances
Foreclosure	7 years	3 years, maximum 90% LTV
Deed-in-Lieu / Short sale	Up to 90% LTV – 4 years 90% and above – 7 years	2 years, maximum 90% LTV

#### 5.2.5.6 LETTER OF EXPLANATION FOR ABOVE SIGNIFICANT DEROGATORY CREDIT EVENTS (4/15/11)

When the borrower has a bankruptcy, foreclosure, deed-in-lieu, or short sale a written letter of explanation and supporting documents must be provided. The documentation and letter of explanation must detail and support the timelines and circumstances for the event. The underwriter will use the letter to determine whether extenuating circumstances existed, which will determine the required waiting time for a new loan with mortgage insurance.

To exercise the reduced waiting periods the letter of explanation and supporting documents are required.

#### 5.2.5.7 PREVIOUSLY PAID CLAIM (4/15/11)

PMI will generally not insure a loan to a borrower on whom we have previously paid a claim.

#### 5.2.6 NONTRADITIONAL CREDIT AND “NO CREDIT” GUIDELINES (7/11/11)

##### Eligibility Criteria

- All loans must be underwritten by PMI; PDQ delegated submission not eligible
- Purchase or Rate/Term Refinance
- Primary Residences
- Maximum 95% LTV/CLTV
- Maximum loan amount of \$417,000 (\$625,500 Alaska/Hawaii)
- Minimum 3% borrower contribution from own funds
- Minimum 2 months reserves

##### Credit References

- A minimum of 4 sources of non-traditional credit with at least 12 months history required:
  - one housing-related;
  - one a utility company; and
  - two from other sources.

- Credit references must have at least a quarterly repayment requirement. Creditors that require payment at time of services rendered would not be considered a credit reference. Credit references that do not comply with these guidelines would not be considered a valid credit reference.
- 0x30 housing lates in the past 12 months; 0x60 late payments in past 12 months for all other credit references
- Borrowers with a Bankruptcy/Foreclosure/Deed-in-Lieu/Short sale are not eligible
- No collections or judgments (except medical) in past 24 months; judgments must be satisfied

### Documentation Requirements

- Acceptable documentation for all credit references can be one of following:
  - Twelve (12) months of consecutive account statements; or
  - A current account statement with 12 months of cancelled checks or paid receipts; or
  - Lender direct-written verification which must include all of the information required on a non-traditional credit report and a current statement provided by the creditor; or
  - A non-traditional credit report.

### Acceptable Sources of Non-traditional Credit

- Housing-Related Source

Lenders must obtain at least one housing related source for a non-traditional credit history, either through a credit reporting agency or with a VOR. The credit agency must specify in the report whether verification was obtained from a professional management company or from an individual landlord.

If the VOR is completed by an individual landlord, 12 months canceled checks are required.

Borrowers who do not have a rental reference because they are living at home to save for a down payment can utilize a savings history reference.

A savings history can be used as one of the credit references even when a housing reference is provided. The loan must contain documentation, preferably bank statements, showing at least a 12-month history of periodic deposits (at least quarterly) that are comparable to a rental payment and show a growing account balance.

- Utilities (Not included in Housing Payment)

Electricity, gas, water, and payments for telephone and cable television service.

- Other Payment Sources

- For medical insurance coverage, automobile insurance, life insurance policies and rental insurance payments (excluding any payroll deductions).
- Payments to local, department, furniture, appliance, specialty stores; rental payments related to durable goods (including automobiles); medical; school tuition;
- Payments for child care; loans obtained by an individual (if there is a written agreement and the borrower can provide copies of cancelled checks to indicate payments are consistent with terms of the agreement); and authorized user accounts (if there is written documentation to support the borrower has been solely responsible for payments during the most recent 12 months).

The consumer reporting agency should provide the lender all documentation received for each credit reference listed on the credit report.

### Borrower has a Valid Credit Score and the Co-borrower has NO Credit

- The borrower's income must represent more than 50% of the totally qualifying income. In addition, the DTI based on that borrower's income cannot exceed 45%.
- It is not necessary to develop a nontraditional credit report for the Co-borrower.
- Loan will be priced using non-traditional credit rates.

**Borrower has a valid credit score and the Co-borrower has Non-traditional Credit**

- Develop a minimum of 4 sources of non-traditional credit for the Co-borrower.
- Loan will be priced using non-traditional credit rates.

**All borrowers have Non-traditional Credit**

- Develop a minimum of 4 sources of nontraditional credit for each borrower

**Mortgage Insurance**

- Loans with a non-traditional credit receive rates that are comparable to a 620 credit score.
- Monthly, NuMonthly, and Annual premium plans only. Super Single premium plan is not eligible.

**Ineligible:**

- DU/LP Program
- Distressed Markets
- Construction-Permanent Loans
- Jumbo loans
- Second Home
- Cash Out Refinance
- PDQ Delegated Submission

## 5.3 CREDIT SCORES

### 5.3.1 CREDIT SCORING (12/06)

Credit scores are available from each of the three major national credit providers:

- Equifax - Beacon<sup>SM</sup> score
- TransUnion – Empirica<sup>®</sup> score
- Experian - TRW/FICO score

The lender should use the most current classic FICO credit score for each borrower. Credit scores range from low to high with the lower scores representing poorer credit. When the borrower has too few trade lines or has been in the credit system for too little time, a credit score will not be provided. When no credit score is available the borrower is not eligible for insurance. In addition to the use of credit scores, the underwriter must evaluate the credit report and other sources of credit information to determine the borrower's credit history.

### 5.3.2 VALID CREDIT SCORE (4/27/11)

For a credit score to be accepted by PMI in the underwriting process, the borrower must have an established credit history verified through traditional credit repositories. The score must be based on sufficient, accurate information. Too little information or information that is significantly inaccurate makes the credit score unusable.

Although a credit score can be generated with one trade line, PMI does not consider the credit score valid unless at least three trade lines are evaluated for at least 12 months, regardless of AUS decision. (Trade lines may be open or closed) (Authorized user accounts cannot be used to validate the credit score).

**Note:** A trade line is defined as a revolving or installment payment account. The trade line must not be in dispute and must clearly belong to the borrower in order to be eligible for consideration.

Collections, judgments, charge-offs, repossessions, foreclosures, bankruptcy repayment plans, and credit counseling are not eligible trade lines.

### 5.3.3 QUALIFYING CREDIT SCORE (6/10)

PMI requires a minimum of two credit scores when credit scores are required. To determine the appropriate score to use, the following guidelines will apply:

- For a single borrower with two credit scores, use the lowest score
- For a single borrower with three credit scores, use the middle score, or if two are identical, use the identical score
- For more than one borrower, select the appropriate score for each borrower using the above criteria, and then the borrower with the lowest score should be used

For example:

Borrower #1 has credit scores of **680**, **695**, and **730**; Borrower #2 has scores of **750** and **765**. The middle score for Borrower #1 (**695**) and the lowest score for Borrower #2 (**750**) should be considered. The borrower with the lowest score will be used. In this case, the credit score of **695** will be used.

### 5.3.4 METHODS FOR DETERMINING CREDIT SCORE (2/07)

PMI's standard credit scoring methodology is the Lower/Middle Method. PMI may accept other methods for selecting the representative credit score provided the lender requests and receives approval from the National Accounts Operations Team.

In New York or when the credit report is invalid due to incorrect data, the credit score may not be used to determine eligibility/pricing, the comparable credit criteria document details the credit characteristics to determine correct pricing levels.

#### Lower/Middle Method

This is PMI's method for entering and scoring credit. Two or three scores are obtained for each borrower. If two are obtained, the lower score is the individual borrower's representative score; if three, the middle score is the borrower's representative score. The lowest individual borrower's representative score is considered the Indicator Score for the loan.

## 5.4 LIABILITIES AND OTHER DEBT (12/06)

The borrower's liabilities include all debts of a continuing nature, including:

- Housing expense on the borrower's primary residence (this includes a rental or mortgage payment)
- Installment loan debts with a remaining payment term greater than 10 months
- Revolving or open credit
- All lease payments
- Mortgage and other related expenses on any non-income producing real estate or net operating losses on investment properties
- Alimony, child support, and separate maintenance payments
- Taxes and insurance on any properties owned free and clear

### 5.4.1 LIABILITIES (12/06)

For each liability, the underwriter must determine the unpaid balance, repayment terms, and the borrower's payment history. The credit report should be used as a resource for obtaining this information. If the credit report does not contain a reference for each significant open debt shown on the Loan Application, including outstanding mortgage debt, bank, student, or credit union loans; the lender must provide separate credit verification.

If a current liability appears on the credit report that is not shown on the loan application, the borrower should provide a reasonable explanation for the undisclosed debt. Documentation may be required to

support the borrower's explanation. For example:

- The borrower explains that he/she forgot about the loan because he/she co-signed for a relative and the relative is making all of the payments. Copies of 12-months canceled checks from the relative may be required to support the explanation.

### 5.4.2 PAYOFF OR PAYDOWN OF DEBT FOR QUALIFICATION (4/15/11)

Payoff or paydown of debt solely to qualify must be carefully evaluated and considered in the overall loan analysis. The borrower's history of credit use should be a factor in determining whether the appropriate approach is to include or exclude debt for qualification. As a rule-of-thumb:

- **Installment Loans** -- that are being paid off or paid down to 10 or fewer remaining monthly payments, should generally not be included in the borrower's long-term debt.
- **Revolving Accounts** -- If a revolving account is to be paid off and closed, a monthly payment on the current outstanding balance does not need to be included in the borrower's long-term debt. If a revolving debt is to be paid off but not closed, a monthly payment on the current outstanding balance should generally be considered as long-term debt.

### 5.4.3 OTHER DEBT (3/1/11)

#### Housing Expense

The current mortgage payment or rental payment (housing expense), if not verified on the credit report, can be verified with a Verification of Rent or Verification of Mortgage form. (The VOR is not a required document; however, if provided and not completed by a Corporation, 12 months cancelled checks should be utilized.)

PMI prefers that each borrower have at least a 12-months rental or mortgage payment history; however, some borrowers starting out may not meet this requirement. It is up to the underwriter to establish a comfort level with the borrower's willingness to repay debt by reviewing all aspects of the borrower payment history.

For example, a new couple starting out may have lived with a relative rent free to save money for a down payment. In this situation the underwriter could review the savings history for the borrower and develop a payment history (payments to savings accounts) from the bank statements.

#### Installment Debt

Generally, all installment debt that is not secured by a financial asset – including student loans, automobile loans, and home equity loans – should be considered as part of the borrowers monthly debt obligations only if there are more than ten monthly payments remaining to be paid on the account.

An installment debt with fewer monthly payments remaining should also be considered as a recurring monthly debt obligation if it significantly affects the borrower's ability to meet his or her credit obligations.

Deferred installment debt – such as student loans and loans in forbearance – must also be included as part of the borrower's recurring monthly debt obligations. If the credit report does not indicate a payment amount a copy of the borrower's payment letter or forbearance agreement should be obtained so the payment amount can be determined.

#### Revolving Charge/Open Accounts/Lines of Credit

Revolving charge accounts, open accounts, and unsecured lines of credit are open-ended and should be treated as long-term debts. These trades include credit cards, department store charge cards, and personal lines of credit. (Equity Lines of Credit secured by real estate should be included in the housing expense.) The minimum payment should be calculated as 5% of the outstanding balance unless otherwise indicated on the credit report or alternate verification form.

Open 30-day charge accounts require the balance to be paid in full every month. PMI does not require open 30-day charge accounts to be included in the debt-to-income ratio. Open 30-day charge accounts must be paid off at or prior to closing if:

- the borrower is unable to document sufficient assets to cover the unpaid balance, or
- the borrower is unable to document that the charges will be reimbursed by his or her employer

Flexible Spending Cards, not to be confused with Flexible Benefits Credit Cards, is a type of revolving credit account. Also known as World Cards, Signature Cards, and/or No Preset Spending Limit Cards are a typical credit card with the exception that the card has both a revolving component and an open end component.

### **Auto Lease Payments**

Because the expiration of a lease agreement for an automobile typically leads to either a new lease agreement, the buyout of the existing lease, or the purchase of a new vehicle; auto lease payments should always be included in long-term debt regardless of the number of remaining months on the lease.

### **Loans Secured By Financial Assets**

Loans secured by the borrower's savings account, Certificate of Deposit, or other investment account (including a margin account against the borrower's stock portfolio) need not be considered long-term debt. The security instrument allows the lender the right to access the asset to fulfill the obligation; payment is generally not required.

Loans against tax-favored retirement accounts (i.e., IRAs, Keoghs, Elective Deferral - Section 401(K), and Tax-Sheltered Annuity - Section 403(B) plans) are generally considered to be a withdrawal from the plan. If funds are not repaid within a specified period of time, generally 60 days, the Internal Revenue Service is notified of the distribution and the borrower is subject to tax and penalty on the amount withdrawn. Loans against IRAs, Keoghs, 401(K)s and 403(B)s should not be considered long-term debt.

Depending upon the structure and terms of a Defined Benefit Pension Plan, a borrower may be entitled to a loan against his or her invested funds. Again, depending upon the structure and terms of the plan, repayment on a periodic basis may or may not be required. A copy of the pension plan agreement and statement from the plan administrator should be requested to verify the borrower's repayment obligation and treatment for long-term debt.

If there is a loan against any of the borrower's assets, only the amount net of the outstanding loan balance should be considered in determining the borrower's assets.

### **Alimony/Child Support/Separate Maintenance Payments**

Alimony, child support, and separate maintenance payments with duration greater than 10 months should be treated as long-term debt.

The debt should generally be documented with court records (i.e., the borrower's Divorce Decree or Legal Separation Agreement). Borrowers, in many cases, feel that it is an invasion of their privacy and prefer not to provide these documents. The lender is, none-the-less, expected to verify the borrower's long-term debt by whatever means possible. Copies of 12-months canceled checks or a statement from the court custodian verifying receipt of payments may be accepted as verification of the payment amount.

Despite a Petition for Divorce appearing on the credit report, if there is nothing in the file that would cause the underwriter to believe that there is an obligation, a copy of the legal document is not required if:

- The borrower answers "no" to question "g.", "Are you obligated to pay alimony, child support, or separate maintenance?" on the Uniform Residential Loan Application, Section VIII., Declarations;
- or**
- The borrower provides a letter stating that he/she has no obligation for alimony, child support, or separate maintenance payments.

Many lenders use loan origination software to prepare the final 1003; certain fields default to the most common response. To be sure that the "no" is not just a typographical error, it is recommended that the

underwriter review the borrower's handwritten loan application to verify consistency.

### **Payments on Other Real Estate Owned**

When the borrower owns mortgaged real estate (other than investment property), the monthly payments of principal, interest, taxes, insurance, and other associated costs for real estate owned (other than the subject property) should be included in long-term debt. This will include second homes, vacant land, properties owned free and clear, and other non-income producing property.

### **Home Equity Lines of Credit**

When the loan also has a home equity line of credit that provides for a monthly payment of principal and interest or interest only, the payment on the home equity line of credit must be considered as part of the borrowers recurring monthly debt. If the home equity line of credit does not require a payment due to no balance, there is no recurring monthly debt obligation so the lender does not need to develop an equivalent payment amount.

Calculating payments, when none is stated on the Credit Report or HELOC documents:

- The payment calculation should be an amount that will amortize the balance of the equity line of credit over the remaining term at the interest rate currently in effect for the equity line on the date of the new loan application. If the remaining term is not specified, a repayment term of five years should be used.

### **Non-reimbursed Employee Expenses**

When the borrower has non-reimbursed business expenses, such as classroom supplies, uniforms, meals, gasoline, automobile insurance and/or automobile taxes, the recurring monthly debt obligation for such expenses must be determined by developing a 24-month average using information from the IRS 1040, Schedule A and net out any automobile depreciation claimed on the Employee Business Expense Form 2106. If there is not a 24-month history of these expenses an annualized monthly average should be developed and added to the borrowers recurring monthly expenses.

Consequently, when calculating the total debt-to-income ratio, the 24-month average for non-reimbursed business expenses should be subtracted from the borrower's stable monthly income, unless such expenses are automobile lease payments or automobile loan payments, in which case they are to be considered part of the borrower's recurring monthly debt obligations. If there is not a 24-month history of such expenses, the lender should develop an annualized monthly average for the expenses and add this calculated amount to the borrower's monthly debt obligations.

### **Business Debt in Borrowers Name**

When a self-employed borrower claims an obligation on the personal credit report is being paid by the borrower's business the underwriter must confirm that the obligation is paid out of the company funds and was considered in the cash flow analysis of the business.

- When the account in question does not have a history of delinquency, the business provides acceptable documentation the business paid the debt (12 months' cancelled company checks) and the underwriter's cash flow analysis of the business took the payment into consideration, then the payment need not be counted as a monthly recurring debt.
  - If the business does not provide sufficient evidence that the obligation was paid out of company funds, the payment must be considered part of the borrower's individual monthly recurring debt.
  - If the business does provide acceptable evidence of payment of the debt, but the cash flow analysis does not reflect any business expenses that related to the obligation, it is reasonable to assume the obligation has not been considered in the cash flow of the business. When this is the case, the debt must be considered part of the borrower's individual monthly recurring debt.
- When the account in question does have delinquency, the full monthly obligation must be considered as part of the borrower's individual monthly recurring debt. (To ensure the debt is only counted once, the net income of the business may need to be adjusted for any expenses related, if any, to the

obligation.)

## Student Loans

Deferred installment debt – such as student loans – must be included as part of the borrower's recurring monthly debt obligations. If the borrower's credit report does not indicate the monthly payment that will be payable at the end of the deferment period, the lender should request a copy of the borrower's payment letter or forbearance agreement so that it can be determined what payment amount to use in calculating the borrower's total monthly obligations.

### 5.4.4 CONTINGENT LIABILITIES (12/06)

The borrower may have a contingent liability as the result of co-signing a loan to enable another party to obtain credit. Not all contingent liabilities will need to be counted as part of the borrower's recurring monthly debt obligation. The contingent liability will not be considered a debt of the borrower if all of the following criteria are met:

- The loan is at least 12 months' old and the primary obligor has made all payments on the loan
- The history of payments by the primary obligor is documented
- The loan is current and there have been no delinquent payments since origination of the loan

If payment by the primary obligor cannot be verified, or if a sufficient or acceptable payment history has not been established, the loan should be included in the borrower's monthly recurring debt.

Payments assigned to another party through a Court Order can, in some cases, become the responsibility of the original obligor in the event of default. If the obligation is not to be considered a long-term debt of the borrower, both evidence of the Court Order and timely repayment by another party should be provided. For example:

The borrower's credit report shows a delinquent obligation. They have provided a divorce decree and settlement statement showing that the debt was assigned to the ex-spouse. Despite the agreement between the parties, if the ex-spouse defaults on this debt, the borrower may still be held liable. Unless a written release of liability from the lender is provided, this obligation would be included in the borrower's long-term debt. If, however, the obligation is current, does not have a history of delinquencies, and is assigned to the ex-spouse through the court-ordered property settlement, it is not necessary to consider this debt when qualifying our borrower.

Because a mortgage loan assumption may or may not include release of liability of the original obligor, the decision to include the debt as the borrower's liability should be determined using the above criteria unless satisfactory evidence of release of liability of the borrower is provided.

### 5.5 DEBT-TO-INCOME RATIOS (4/15/11)

Debt-to-income (DTI) ratios are used to compare the borrower's anticipated monthly housing expense and total monthly obligations to his or her stable monthly gross income. Historically, lenders have used two different qualifying ratios – a monthly housing expense-to-income ratio and a total monthly obligations-to-income ratio – to assess whether a borrower is able to meet the expenses involved in home ownership. However, since research has not demonstrated that there is a significant relationship between the incidence of mortgage default and the borrowers' monthly housing expense to income ratios, our emphasis is on the total debt to income ratio (which consists of two components – monthly housing expense and the total of other monthly obligations).

#### Housing Payment

The Monthly Housing Payment includes the following:

- Principal and interest for the mortgage that is secured by the borrower's principal residence;
- Monthly cost for:

- Hazard insurance
- Real estate taxes
- Mortgage insurance premium; and when applicable
  - Home owner association dues
  - Leasehold payments
  - Ground Rent
  - Special assessments
- Payments for subordinate financing

### **Total Debt Ratio**

#### **Maximum DTI: 45%**

Total monthly obligations are the sum of the following:

- Monthly Housing Payment - as described above
- Installment debts extending beyond ten months
- Monthly PITI for second homes and other non-investment property that are non-income producing
- Lease payments - regardless of remaining lease term
- Revolving charge, open accounts, and lines of credit - calculated at 5% of the outstanding balance unless otherwise documented
- Alimony, child support, or separate maintenance payments - with more than 10 remaining payments
- Negative net rental income - from investment properties owned by the borrower
- Current real estate taxes and hazard insurance premiums for real estate owned free and clear

For loans that are manually underwritten, submitted and approved by Desktop Underwriter® or Loan Prospector® or loans using a custom or proprietary AUS system, the proposed total monthly debt should be no greater than 45% of the borrower's stable monthly income.

In addition, when the income from more than one borrower is used and not all the borrowers will occupy the property, the owner occupant borrower should have a debt to income ratio of 45% or less, excluding the income and debt from the non-occupant co-borrower.

## **5.6 QUALIFYING RATE/PAYMENT (4/15/11)**

Fixed-rate, fixed payment mortgages will be qualified at the contract Note Rate.

Fixed-rate mortgages with temporary buydowns will be underwritten at the initial, bought-down rate.

Adjustable Rate Mortgages (ARMs) should be underwritten at a rate which anticipates "payment shock" to the borrower, based on the discount (or "spread") between the initial payment rate and the fully indexed accrual rate (FIAR), borrower occupancy, and the possibility for negative amortization.

- Short term ARMs (3 years or less fixed rate period) qualify using the greater of the note rate plus 2% or the Fully Indexed Accrual Rate (FIAR)
- 5/1 ARMS - qualify using the greater of the note rate plus 2% or the Fully Indexed Accrual Rate (FIAR)
- Hybrid ARMs (fixed rate periods of 7 years or greater) qualify the note rate

## SECTION 6 – INCOME

### 6.1 Stability and Continuance of Income (2/11)

A qualified borrower should have long-term, stable income from employment or other acceptable sources. Borrowers who are in a line of work in which advancement is possible because of a continuing demand, who have demonstrated the ability to maintain full employment, and have advanced in standing should receive favorable consideration despite occasional job changes.

Employment should be verified for two full consecutive years. A borrower who has changed jobs to advance within the same line of work, which maintains income continuity, and is successful in that work, will also receive favorable consideration. The borrower should explain any employment gaps that extend beyond one month.

The borrower's probability for continued employment should be evidenced in the file. In the case of negative comments received from the employer, the lender must perform a detailed investigation. A summary of their findings should be provided in the insurance application package and the underwriting decision should be supported by system comments to the file.

#### 6.1.1 INCOME ANALYSIS (12/06)

Stable monthly income considered for qualification is the borrower's verified gross monthly earnings from primary employment plus stable acceptable secondary income such as bonuses, part-time employment, commissions, or overtime. Income should be verified in writing by a reliable source.

Verified secondary income may be considered for qualification if it has been received by the borrower for at least the past two consecutive years and continuation is probable based on foreseeable circumstances.

#### 6.1.2 INCOME CALCULATION (12/06)

Individuals generally receive income in fixed regular increments, usually paid monthly, semi-monthly, bi-weekly, or weekly. Some individuals are paid hourly based on a fixed or fluctuating set of hours per week. Each income is calculated differently as follows:

- Hourly: Hourly rate x number of hours x 52 weeks divided by 12 = Monthly Base Income
- Weekly: Weekly base salary x 52 weeks divided by 12 = Monthly Base Income
- Biweekly: Biweekly base salary x 26 weeks divided by 12 = Monthly Base Income
- Semi-Monthly: Semi-monthly base salary x 24 weeks divided by 12 = Monthly Base Income
- Monthly: Monthly base pay as shown. (For some professions, i.e., teachers, monthly pay may not be based on a 12-month basis. The term for monthly pay increments should be confirmed as annualized over 12 months)
- Annually: Annual Base Rate of Pay (without overtime, bonus, or commissions) divided by 12 = Monthly Base Income

The Year-to-Date earnings for each payment type should be reviewed to ensure its consistency with the calculated monthly base income.

In order to use other income to qualify (overtime, bonus, commissions, etc) there must be a minimum 2-year history of receipt and it must be expected to continue. This type of income should be calculated as follows:

YTD	Earnings from the paycheck stub or VOE
Plus	Wages earned from the W-2 for the previous year
Divided	<u>Number of months</u>
Equals	Average Monthly Income

Minus Monthly Based Income  
 Equals Average Other Earnings per Month

It is important to see an earnings trend that is level or increasing from year to year. When earnings show a decline, there must be strong compensating factors to support using the income.

## 6.2 VERIFICATION AND DOCUMENTATION

In general, a two year history of income from any source is required to consider the income stable. To demonstrate the likelihood that a consistent level of income will be received for borrowers with less predictable sources of income, robust information about prior earnings must be verified. Examples of less predictable income sources include commissions, bonuses, substantial amounts of overtime pay, or employment that is subject to time limits, such as contract employees or tradespersons.

Income should be determined to have a likelihood of continuance for three years. When the income falls in a category that does not have a defined expiration date, such as Social Security Disability or VA Disability, the income may be considered stable, predictable, and likely to continue and additional documentation is not required.

All base income from employment is considered for qualification provided proper verification is received and the income can be deemed likely to continue.

PMI accepts verification from specialized agencies, such as The Work Number, as long as the income and employment are verified.

### 6.2.1 DOCUMENTATION (3/1/11)

Documents should be no more than 120 days old on the date that PMI approves the loan. Underwriter discretion will be exercised for determining whether re-certification of any document is necessary.

The requirements for full documentation and documentation efficiencies that are permitted are detailed below.

#### Full/Substitute Income Documentation

This consists of verification of the borrower's employment and income for at least two full years. Any gaps in employment greater than one month must be explained. The following documents are required:

- A verbal Verification of Employment (completed prior to closing); and
- Verification of Employment, or
- One paystub, which contains at least 30 days of year-to-date earnings and two years' W-2s, or
- Two years' personal or business tax returns (if self-employed) and a year-to-date P&L for the business

#### Income Document Efficiencies (DU/LP loans)

This consists of verification of the borrower's employment and income for various timeframes determined by the multiple risk factors in the loan. Gaps in employment need to be verified when required by the findings. One of the following documentation sets will be required:

- A verbal Verification of Employment (completed prior to closing); and
- Verification of Employment
- One paystub, which contains at least 30 days of year-to-date earnings, and a verbal verification of employment
- One paystub and the most recent year's W-2s and a verbal verification of employment
- One year's personal federal tax returns
- Two years' personal federal tax returns
- Two years' personal and two years' business federal tax returns (if self-employed).

A document efficiency of only a verbal Verification of Employment is not acceptable; at a minimum a paystub with 30 days' earnings must be provided.

## 6.3 SOURCES OF INCOME (4/15/11)

### Salaried and Other Income (4/15/11)

For borrowers that receive income from salaried or the following sources, use Agency standard underwriting guidelines. There must be a documented history of receipt and the income should be likely to continue for three years.

- |   |   |
|---|---|
| <ul style="list-style-type: none"> <li>▪ Automobile Allowance</li> <li>▪ Alimony and Child Support</li> <li>▪ Boarder Income</li> <li>▪ Bonus Income</li> <li>▪ Commission Income</li> <li>▪ Foster Care Income</li> <li>▪ Interest and Dividend</li> <li>▪ Military Income</li> <li>▪ Mortgage Interest Differential</li> <li>▪ Non Taxable Income</li> <li>▪ Note Receivable</li> </ul> | <ul style="list-style-type: none"> <li>▪ Overtime</li> <li>▪ Part-time, seasonal or second Job Income</li> <li>▪ Rental income from Investment Property</li> <li>▪ Retirement Income</li> <li>▪ Social security Income</li> <li>▪ Tip Income</li> <li>▪ Trust Income</li> <li>▪ Unemployment Benefits</li> <li>▪ VA Benefits</li> <li>▪ Welfare Benefits</li> </ul> |
|---|---|

### 6.3.1 NEW EMPLOYMENT, EMPLOYMENT GAPS AND RE-ENTERING THE WORKFORCE (4/15/11)

#### New Employment Income (12/06)

If the borrower has an employment history of less than two years and was previously in school, the lender should provide a copy of the diploma. Employment should be sufficiently documented (e.g., employment contract). Special consideration should be given to the upward mobility of a new college or trade school graduate. These borrowers will be considered favorably if they have secured gainful employment and adequate future income and job opportunities can be anticipated because of their education and training.

Follow Agency standard guidelines when the borrower has been employed for less than two years and was previously attending school or a training program. The underwriter should relate the borrower's education/training to future income potential, employment opportunities, and employment stability.

#### Employment Gaps (4/15/11)

Generally, the borrower should provide an explanation for any gap in employment for six months. This can be detailed on the employment section of the loan application.

#### Re-entering the Workforce

A borrower who is re-entering the workforce and has less than a two-year employment history is acceptable if there is evidence of a previous employment history and the current employment is verified.

## 6.4 OTHER INCOME SOURCES (4/15/11)

### 6.4.1 ANNUITY (12/06)

Annuity income is similar to pension and social security income except that it may not be payable for life. A copy of the most recent updated annuity renewal statement showing the effective date, amount, frequency, and duration of the benefit payments showing the income will continue for at least 3 years must be obtained.

### **6.4.2 CAPITAL GAINS (12/06)**

Income received from a capital gain is generally a one-time transaction; therefore, it should not be considered as stable monthly income. However, if the borrower needs to rely on the income from capital gains to qualify, copies of two years of the borrower's tax returns which include the Schedule D must be provided. When the tax returns show that he or she has realized capital gains for the last two years, the lender may develop an average income from the capital gains and use that amount as part of the income -- as long as the borrower provides evidence that there is additional property or assets that can be sold to generate additional capital gains.

### **6.4.3 DISABILITY (12/06)**

Disability benefit payments should be treated as stable income – unless the terms of the disability policy specifically limit the stability or continuity of the benefit payments. Benefits that have a defined expiration date must have a remaining term of at least three years to be used for qualifying the borrower. When a borrower is currently receiving short-term disability payments that will decrease to a lesser amount within the next three years because they are being converted to long-term benefits, you must use the amount of the long-term payments in determining the borrower's stable income.

The lender should obtain a copy of the borrower's disability policy or benefits statement to verify the amount of disability payments and to determine whether there is a contractually established termination or modification date. In addition, the lender should obtain a statement from the benefits' payer (insurance company, employer, or other qualified disinterested party) to confirm the borrower's current eligibility for the disability benefits.

### **6.4.4 FAMILY BUSINESS/INTERESTED PARTY (12/06)**

When a borrower is employed by a relative, closely-held family business, the seller, real estate agent, Title Company, mortgage broker, or any other interested third-party, the VOE cannot be the sole source of income verification. Signed federal income tax returns for two years or W2's and pay stubs are required.

### **6.4.5 FAMILY MEDICAL LEAVE-OF-ABSENCE (FMLA) (11/09)**

FMLA is considered unpaid leave or short-term disability. If the borrower is on FMLA and is not expected to return to work before the loan closes, only the income from employment that the borrower is currently receiving may be used to qualify, and must be expected to continue.

Regular/full-time pay may only be considered if the borrower has actually returned to work by the time the loan closes. Employment status and income must be verified prior to the loan closing. If the borrower is not currently receiving income, their regular full-time pay may not be used to qualify – even if they plan on returning to work at some future specified time. Income from accumulated vacation and sick time may not be used to qualify because its continuance cannot be verified.

### **6.4.6 GIFT INCOME (12/06)**

Gift income can only be considered if the borrower has a 2-year history of receiving it and the donor will verify the likelihood of its continuance. Tax-free gift income is not permitted. Tax returns are required to verify that the borrower pays tax on any gift income used to qualify.

### **6.4.7 INHERITANCE AND OTHER GUARANTEED INCOME (12/06)**

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 this income and verify

that it will continue.

A copy of the inheritance or 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 pay-out. For example, the income is guaranteed to continue for the next 20 years but the borrower has only received one payment/installment.

### **6.4.8 GAMBLING WINNINGS (12/06)**

These funds are usually considered as a lump sum distribution and therefore not considered income unless the borrower is a professional gambler and there is evidence via their tax returns that the income has been received consistently for at least 2 years. (Expenses listed on Schedule A must be deducted from the qualifying income.)

### **6.4.9 MORTGAGE CREDIT CERTIFICATES (2/09)**

Mortgage Credit Certificates (MCCs) were authorized by Congress under the 1984 Tax Reform Act to reduce the amount of federal income tax paid by qualified homebuyers. The homebuyer can claim a federal tax credit for a specified percentage (usually 20 or 25%) of the mortgage interest payments. The MCC credit is effective as long as the property remains the borrower's principal residence.

- A copy of the MCC should be included in the mortgage insurance application package
- The maximum possible mortgage credit certificate income should be added to the borrower's income rather than used to reduce the mortgage payment

### **6.4.10 ROYALTY PAYMENTS (12/06)**

There must be documented evidence that the borrower has received the royalty payments for at least 12 months and will continue to receive them for at least three years after the date of the loan application. Copies of two years tax returns including the supplemental Schedule E will be required to verify the income.

### **6.4.11 SELF-EMPLOYED INCOME (4/15/11)**

A borrower with a 25% or more ownership interest in a business or who receives 25% or more of their income from sources other than salary is considered self-employed. If a borrower is self-employed, the stability of the business concern and the borrower's income pattern must be established. Consideration must be given to the following:

- The borrower should have been self-employed for at least two years prior to the loan application. Personal and business tax returns should reflect increases in income and assets with likelihood for continued growth.
- A borrower who has been self-employed between one and two years must have at least two years of previous successful employment in the same occupation in order to be considered favorably. In addition, the Lender must consider the borrower experience, and the acceptance of the company service or products in the marketplace, before considering the income as qualifying income. It should be documented how it was determined that the borrower's income was deemed acceptable.
- A borrower who has been self-employed for less than one year has not established a history of stable self-employment earnings and is generally not eligible for coverage.

#### **Documentation**

The following documentation should be provided for all self-employed borrowers:

- Signed individual federal income tax returns (1040's) including all schedules for the previous two years.
- If the PMI approval date is more than 120 days after the business year-end, a current financial statement including a balance sheet and year-to-date profit/loss statement should be provided.

Audited statements are preferred, but if not audited, must be signed by the preparer and borrower.

- If the business is a Corporation, S-Corporation, or a Partnership, copies of signed federal business tax returns for the last two years, complete with all schedules and current financial statements, should be provided.
- A business credit report may be required at the underwriter's discretion.

The income of self-employed borrowers must be analyzed differently due to the nature of self-employment.

- The growth of the business is crucial
- The viability, and therefore stability, of the business field is critical to the ability of the borrower to meet ongoing obligations
- The length of time self-employed and overall experience in the field must be considered
- Comparison of financial documents and tax returns must be completed

PMI's Income Analysis - Cash Flow Method uses a "top down" method to determine average income for self-employed borrowers based upon recent past performance. The form lists sources of allowable income and encourages a close examination and evaluation of the tax returns and financial statements.

For more information on analyzing tax returns, contact your PMI representative for our training publication – 2008 Underwriting the Self-Employed Borrower.

### **6.4.12 UNACCEPTABLE INCOME (11/09)**

The following types of income or compensation are generally considered unacceptable for the purpose of qualifying borrowers. (Exceptions, at underwriter discretion in the application of good, common-sense underwriting, will be considered.)

- Expense account reimbursements
- VA education benefits
- Retained earnings from business
- Any source of income that cannot be verified by the lender
- Income that is not likely to continue more than three years
- Trailing Co-Borrower Income

## SECTION 7 - ASSETS

### 7.1 BORROWER'S ASSETS

Assets are an important factor when determining a borrower's creditworthiness and financial strength. The borrower must have sufficient liquid assets for the down payment, closing costs, prepaid expenses, and reserves. Assets should be reviewed in conjunction with income and credit to determine the reasonableness of the transaction. A pattern of savings and an ability to manage assets should be demonstrated, as well as, confirmation that the funds are from an acceptable legal source.

The underwriter must verify that the borrower has sufficient assets to complete the mortgage transaction (down payment, closing costs and prepaids) and provide reserves, if required.

Generally, we require the borrower to use his or her savings, or other liquid assets, to make a minimum cash down payment. Once the minimum down payment for the program has been met, the remainder of the funds can come from other acceptable sources, such as gift funds, grants, etc.

#### 7.1.1 ASSETS NEEDED TO CLOSE THE LOAN (4/15/11)

Funds required to close the loan consist of the down payment, which generally includes a deposit on the sales contract and/or an earnest money deposit, closings costs, prepaids and reserves.

##### **Deposit on Sales Contract/Earnest Money Deposit (12/06)**

The source of funds from the deposit on the sales contract must be verified if the funds are needed to qualify. The assets should reflect that the earnest money deposited with the purchase contract is from the borrower's own funds. If it cannot be determined that these funds were withdrawn from the borrower's account, additional verification of the source, and evidence that funds have actually changed hands from the borrower to the seller, REALTOR®, escrow agent, or settlement attorney, should be provided. Large earnest money deposits and deposits that exceed the amount customary for the area should be closely evaluated.

##### **Closing Costs (Effective 1/10)**

Closing costs are expenses that are incidental to the sale of real estate, such as loan fees, title fees, appraisal fee, etc., and may be paid outside of escrow. It is acceptable for these fees to be paid outside of escrow by using the borrower's credit card. The underwriter must confirm that the debts are calculated correctly to include any increase in credit card balances that may occur from paying these expenses via credit card.

For refinance transactions, the closing costs may be included in the loan amount.

##### **Prepaid Items (11/09)**

Prepaid items such as taxes, hazard insurance, ground rent, etc. are expenses that are paid in advance and usually prorated upon the sale.

Typically, the following prepaid settlement costs are paid by the borrower, but can be paid by other parties (if paid by other parties the Interested Party/Seller Contributions maximums apply) or be financed:

- Interest charges covering any period after the settlement date
- Real estate taxes covering any period after the settlement date
- Hazard insurance premiums; and
- Escrow accruals required for renewal of the mortgage insurance premium (unless the premium is being financed as part of the mortgage amount)

## Reserves (11/09)

The borrower should generally have 2 or 3 months mortgage payments in the form of liquid assets remaining as reserve funds after closing. Cash reserves are of particular importance for loans with high LTVs, jumbo loans, or properties that may be in need of repair. The underwriter should not deny an application solely because the borrower's remaining liquid assets are less than 2 to 3 months mortgage payments. Assets are only one of the underwriting factors considered in the overall evaluation of the loan.

When a borrower is purchasing a new home that requires insurance and has an existing primary residence that will be converted to a second home or investment property instead of being sold, the borrower is required to have six months' PITI for both properties. This applies to manually underwritten and DU®/LP loans.

## 7.2 MINIMUM BORROWERS CONTRIBUTION (4/15/11)

**Down Payment** – the borrower must have a minimum contribution to the down payment from their own funds as follow:

- Owner Occupied with LTVs up to 97% - minimum 3%
- Jumbo and Second Homes with LTVs up to and including 90% - minimum 5%

**Reserves** – the borrower must have verified reserves for all loans

- Minimum 2 months PITI
- Cannot be proceeds from the subject mortgage
- For conversion of primary residences, generally 6 months reserves are required per property unless there is 30% documented equity, then the reserve requirement can be reduced to 2 months.

Gift funds can be used to pay the remainder of the down payment, closing costs, prepaid items and reserves once the minimum borrower contribution has been met.

### 7.2.1 Source of Borrower's Own Funds

- Checking and Savings Accounts which have been seasoned or sourced and are under the ownership and control of the borrower.
- Stocks, Bonds, Mutual Funds, Certificates of Deposit, Money Market funds and Retirement Accounts which are owned by the borrower and liquidated.
- Proceeds from the sale of real estate owned.
- Sale of personal assets meeting the following requirements:
  - Borrower's seasoned ownership of the asset is evidenced.
  - Current value is determined by an independent and reputable source.
  - Bill of sale is provided along with evidence of borrower's receipt of the funds.
  - The party purchasing the asset may not be related to the borrower or a party to the transaction.
- Funds held by or for the benefit of the seller including:
  - Deposit on Sales Contract/Earnest money deposit which is seasoned or sourced.
- Rent paid on an Option to Purchase which exceeds fair market rent and is defined in the contract as down payment.
- Borrowed funds secured by an asset owned by the borrower, as long as the party providing the secured loan is not a party to the transaction.
- Credit for value of subject property lot owned by the borrower (for construction-permanent loans)

### 7.2.2 Other Sources of Funds

After meeting the minimum contribution required the following can be used to provide additional down payment, closing costs and reserves.

- Gift Funds - Gift funds from an eligible donor are permitted when the funds are owned by the donor and transferred to the borrower, prior to or at the time of closing
  - Eligible gift donor(s)
    - Individuals who are related to the borrower by blood, marriage, adoption or legal guardianship
    - Individuals who demonstrate a long standing established relationship with the borrower specifically fiancé, fiancée or domestic partners
  - Ineligible gift donor(s)
    - Individuals who benefit financially from the closing of the transaction
    - Individuals who are, or have an affiliation with, the builder, developer, real estate agent, or any other interested party to the transaction
- Gifts of Equity
  - Gifts of equity provided by the seller of the property who is related to the borrower by blood, marriage, adoption or legal guardianship
- Grant funds
  - Repayment of the grant, in whole or in part, is not expected or required except upon resale or refinance of the property
  - Grant is part of a formal gift program
  - In the event the grant funds result in a recorded lien on the subject property, the CLTV may not exceed the maximum published eligible LTV for the transaction type
- Cash value of Life Insurance (rather than face value) that is verified. The borrower must be the owner of the policy and not the beneficiary

## 7.3 ASSET GUIDELINES (4/15/11)

For the following asset types follow the GSE standard underwriting guidelines.

- |   |   |
|---|---|
| <ul style="list-style-type: none"> <li>▪ Borrowed Funds</li> <li>▪ Cash on Hand</li> <li>▪ Deposits on Sales contracts</li> <li>▪ Gifts of Equity</li> <li>▪ Retirement Accounts</li> <li>▪ Sales Proceeds from Current Home</li> </ul> | <ul style="list-style-type: none"> <li>▪ Bridge Loans</li> <li>▪ Checking and Savings Accounts</li> <li>▪ Gifts/Grants</li> <li>▪ Rent with Option to Buy</li> <li>▪ Sale of Personal Assets</li> <li>▪ Stocks and Bonds</li> </ul> |
|---|---|

Other types of assets and the appropriate treatment for loan qualification are detailed below. If the loan is not being originated for sale to the GSEs, PMI will use Fannie Mae® guidelines.

### Business Accounts (Effective 1/1/10)

To utilize funds from the borrower's business funds for the down payment, a letter must be obtained from the CPA stating the borrower has access to the funds, and that there will be no detrimental impact to the business so that it may continue to operate profitably if the funds are withdrawn.

### Collateral Pledge Account

Several Combined Asset Mortgage (CAM) programs include a pledged collateral account as additional security for the mortgage loan.

The type of pledged asset (Certificate of Deposit, Life Insurance, Annuity, etc.) and minimum cash equity will vary by CAM program. Prior program approval by PMI is required. The borrower's ability to fund the collateral account should be verified in the same manner as funds for down payment and closing costs. Collateral pledge funds cannot be used to make the monthly payments nor can they be released without PMI's prior approval.

### Land Equity

For a construction-permanent end loan, the borrower's equity in the land may be recognized as down payment. If the land was purchased within the last 12 months, the purchase price less any existing liens will establish the borrower's equity. If the land was purchased over 12 months ago, the equity may be based on the current appraised value of the land less any liens.

### Property Listed for Sale

When the property is listed for sale, but has not sold, the borrower can be qualified on the basis of the anticipated equity. If the sales price has not been established, calculate the anticipated equity as follows:

$$\text{Listing Price} - (10\% \text{ of listing price} + \text{All liens}) = \text{Equity}$$

When the sales price has been established, calculate the anticipated equity as follows:

$$\text{Sales Price} - (\text{Sales Cost} + \text{All Liens}) = \text{Equity}$$

Sales costs are typically 8 to 10%, which includes sales commission and closing costs paid by seller.

If the underwriter relies upon the lender's closing condition requiring sale and evidence of minimum net proceeds, the approval should represent this reliance.

### 1031 Property Exchange

A 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 qualified property with another, rather than selling it.

A 1031 Exchange is an exchange of qualified property. A 1031 Tax Deferred Exchange can be used as the down payment for the purchase of an investment property with the following requirements:

- 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.

### Trust Accounts

Trust account funds may be used for the down payment and closing costs if the borrower is a beneficiary of the trust and has access to the assets. A statement from the trustee should be provided to verify the liquidity and availability of funds to the borrower.

### Unsecured Loans

Unsecured loans are generally considered an unacceptable source of funds for down payment and closing. Examples of unacceptable borrowed funds include signature loans, lines of credit, cash advances on credit cards, and overdraft protection on checking accounts.

### Unverified Funds

Unverified funds are not acceptable for down payment or closing costs unless they meet requirements for borrowed funds, or reflect monies to be saved from the borrower's monthly income prior to loan closing.

If the down payment and/or closing costs are to be saved prior to closing, the required amount should be realistic in relationship to the borrower's current income, outstanding obligations, and the loan closing date. A statement from the borrower, together with a proposed budget, is recommended. Prior to loan closing, the lender should verify that sufficient funds are available and obtain an updated credit report to ensure that funds were not borrowed.

### 7.4 VERIFYING ASSETS (11/09)

Assets must be verified to ensure the borrower has sufficient funds to complete the mortgage transaction, and if required, adequate reserves after closing. Assets may be verified with 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.

**Internet Downloads:** For documents that are downloaded from the Internet, existence of the website from which the documents were derived should be verified. Documents that are downloaded from the Internet by the borrower must clearly identify the institution and the source of the information must be included in the Internet or "fax" banner that is at the top of the document. Printed web pages must show the Uniform Resource Locator (URL) address, and the date and time printed. They must be identifiable as the borrower's accounts.

### 7.5 INELIGIBLE SOURCE OF FUNDS (12/06)

The following sources of funds may not be used in the calculation of assets:

- Proceeds from unsecured loans or person loans
- Gifts which must be repaid in full or partially
- Sweat Equity (except as permitted with community lending programs)
- Cash on Hand (except as permitted with community lending programs)
- Cash advances from a credit card or other revolving account
- Salary/bonus advances received against future earnings

## SECTION 8 – PROPERTY AND APPRAISAL

### 8.1 PROPERTY DEFINITIONS (5/16/11)

#### Single-Family Detached, Attached, Townhouse, Row House

In detached properties, the homeowner is deeded the land on which the improvements lie, which includes landscaping.

In attached, semi-detached, and townhouse properties, the homeowner is deeded a specific portion of land on which the improvements lie. Minimal common elements may include landscaping, sidewalks, and common walls. Any Homeowners' Association dues or monthly maintenance fees (or the monthly equivalent of quarterly or annual fees), or special assessments, should be included in the monthly housing expense when calculating the debt-to-income ratios.

#### 2-unit Property

In a two-unit attached dwelling or two single-family homes on one lot, the homeowner is deeded the land on which the improvements lie, which includes landscaping. Both units must be titled together as one property on the legal description and should be grouped together on the county tax rolls.

#### Planned Unit Developments

A Planned Unit Development (PUD) is a comprehensive development plan for a large land area. It usually includes residences, roads, schools, recreational facilities, and service areas in addition to commercial, office, and industrial areas. A subdivision having lots or areas owned in common and reserved for the use of some or all of the owners of the separately-owned lots may also be considered a PUD.

To be considered a PUD, membership in a Homeowners' Association is required, and there must be mandatory assessments for the use and enjoyment of the common areas. Zoning is not the basis for classifying a project as a PUD. Any Homeowners' Association dues or monthly maintenance fees (or the monthly equivalent of quarterly or annual fees) should be included in the monthly housing expense when calculating debt-to-income ratios.

#### Condominium Properties

Condominium projects may be designed and built for use as condominiums, or converted to condominiums, through filing of a legal Declaration of Condominium or Master Deed from properties designed and built as apartments or other improvements. Condominium conversion projects generally represent a higher risk; therefore, unique property standards are outlined for properties built as condominium projects and for those converted to condominiums.

#### Site Condominium

Detached Site condominiums that meet the detached definition below can follow standard single family detached property guidelines.

- Detached – A single-family totally detached dwelling (surrounded by free-standing walls), with no shared garages or other attached buildings that is sited on a separate lot may follow single-family guidelines. Detached single-family residences utilize a single family appraisal form:
  - The subject unit is a single-family detached unit
  - The appraiser must comment on any effect that buyer resistance to the condominium form of ownership has on the market value of the individual unit
  - For new projects, the appraisal must include at least one comparable sale that is a detached condominium (which may be located either in a competing project or in the subject project, if is offered by a builder other than the one that built the subject unit)

Attached Site Condominiums must comply with PMI Condo Project Criteria:

- Attached – A single-family condo dwelling that is attached (including zero-lot lines, party walls or shared airspace), has shared garages or other attached buildings must meet PMI Condominium

Project Criteria and utilize a condominium appraisal form.

### **Modular, Panel and Pre-Fab Homes**

These are factory modules/panels that are assembled in factories and then trucked to the site and built as a home. These properties qualify using the same criteria as a single family detached home.

## **8.2 APPRAISAL REQUIREMENTS (5/16/11)**

All appraisals must be in writing. Electronic appraisals are acceptable but must be in a standard format as detailed below.

- Single-family and Detached PUDs - Uniform Residential Appraisal Form (Fannie Mae Form 1004/Freddie Mac Form 70, dated 2005)
- Condominiums - Individual Condominium or PUD Unit Form (Fannie Mae Form 1073/Freddie Mac Form 465 dated March 2005)
- Cooperative Housing Units -- Individual Cooperative Interest Appraisal Report - Fannie Mae Form 2090
- 2-Unit Properties — The Small Residential Income Property appraisal Report (Fannie Mae Form 1025/ Freddie Mac Form 1072 dated March 2005) and The Operating Income Statement (Fannie Mae Form 216)

The appraisal report should be prepared by a state-certified or state-licensed appraiser in accordance with Uniform Standards of Professional Appraisal Practices (USPAP).

### **Ineligible:**

- 2055 Exterior only
- Drive-by Inspections
- Property Inspection Waivers (PIW) and Property Inspection Alternatives (PIA)

## **8.3 DISTRESSED MARKETS POLICY ( 3/1/11 AND 4/25/11 )**

It is critical to review and analyze the appraisal to ensure that the property value is supported before implementing the Distressed Markets Policy. A poor, inaccurate, or incorrect appraisal is not corrected by a reduction in the loan-to value (LTV).

PMI's Distressed Markets are defined when one of the following indicators is present:

1. The subject property is located in a state, MSA/MSAD, or non-MSA area on the PMI Distressed Markets List
  - If the lender can provide documentation that the property is not in a declining market, it can be considered for insurance by submitting the loan to the National Underwriting Center
2. The declining property value box is checked on the appraisal report
  - A property can be considered for insurance using PMI's standard guidelines when the declining property value box is checked on the appraisal by submitting the loan to the National Underwriting Center

The value of the subject property must be well supported; therefore, we recommend obtaining the following with the origination appraisal report.

- Two comparables sales that have closed within the last 90 days prior to the effective date of the appraisal; **and**
- A current listing of a comparable property to demonstrate the subject property's neighborhood is not continuing to decline; **and**
- A detailed explanation from the appraiser as to why property values are declining in the area and what effect falling home prices have had on the value and marketability of the subject property.

Once the above criteria have been considered and a valid and accurate appraised value is established, identify the property's location (state, MSA/MSAD, or non-MSA area) from the PMI Distressed Markets List and apply the following LTV maximums.



# 2011 Underwriting Guidelines Manual

			Full Doc					
			Standard			Jumbo Loans*		
			Loan Amount	Min Credit Score	Max DTI	Loan Amount	Min Credit Score	Max DTI
<b>Owner-Occupied</b> Purchase or Rate/ Term Refinance	1 & 2 Units (attached <sup>1</sup> , detached, condos <sup>1</sup> & PUD's)	95/95	\$417,000	720	45%	Not Eligible		
		90/90	\$417,000	680	45%	\$417,001 - \$625,500	740	45%
		85/85	\$417,000	680	45%	\$417,001 - \$625,500	740	45%
	Co-ops	85/85	\$417,000	700	45%	\$417,001 - \$625,500	740	45%
Cash-Out Refinance			Not Eligible			Not Eligible		

NOTE: \* Approved FHFA high cost areas only – certain high-cost areas - maximum \$729,750

1. Attached housing is not eligible in Florida

Additionally, the following are not eligible for mortgage insurance:

- Florida Attached housing (condominiums, attached PUDs, 3-4 units, co-ops, townhomes and row houses)
- Third Party Originations
- ARMs with an initial fixed period of less than 5 years
- Interested Party Contributions greater than 3%
- Reduced Appraisal Forms – 2055 Exterior only, drive-by inspections, Property Inspection Waivers (PIW) and Property Inspection Alternatives (PIA)
- Loans with an EA III/Eligible recommendation from Desktop Underwriter®
- Cash-out refinances
- Rehabilitation Loans
- Interest-only loans
- Limited Documentation
- Investment Property
- Second home
- Borrowers with nontraditional credit
- Construction-Permanent loans
- Rehabilitation loans
- Potential and Scheduled negative amortization mortgages
- Option Payment mortgages
- New Condominium projects

See the [Distressed Markets List](#)

## 8.4 Property Evaluation (12/06)

Adequacy of the collateral is a critical element of risk in the mortgage loan. PMI maintains standards for residential properties that are considered sound, reasonable, and necessary to ensure quality. These standards are consistent with Fannie Mae and Freddie Mac property eligibility criteria, support PMI's corporate objectives, and provide for compliance with state insurance laws, Fair Lending and Equal Credit Opportunities laws.

The value of the property represents the ultimate security for the mortgage loan. Value may be described as the present worth of future benefits arising from the ownership of real property. The market value of real estate is the most probable selling price in terms of money, which a property should bring in a competitive and open market under all conditions requisite to a fair sale, i.e. the buyer and seller, each

acting prudently, knowledgeably, and assuming the price is not affected by undue stimulus. Each appraisal must be reviewed in detail to evaluate the following:

- Adequate support for the value of the property by the appraiser
- Present and future marketability of the property
- Completeness and correctness of the appraisal forms and exhibits
- Applicability and timeliness of the data used to determine marketability
- Consistency, logic and accuracy of the appraisal

All property evaluations must be made in relation to the marketing conditions of each respective property territory. Real estate factors which affect property valuation include:

- Inventory/Housing supply levels
- Demand
- Appreciation/depreciation rates
- Type and availability of financing

All appraisal reports must be carefully analyzed to ensure that they do not contain comments which can make loans uninsurable by PMI. PMI's claim settlement position could be seriously affected in the case of foreclosure if comments in the appraisal report are inconsistent with underwriting policy and are overlooked when the certificate is issued. For example:

If comments regarding the improvements or comparative market data indicate that the property is in poor condition, the extent of repairs to be made should be documented in order to preserve the ability to enforce "restoration of damages."

### 8.5 PROPERTY STANDARDS (5/16/11)

PMI's property standards vary by market acceptance for each property type. Following are the general parameters under which property is considered acceptable collateral for loans insured by PMI. Minor deviations to these property standards may be considered in relation to the overall evaluation of the property, and should not be used as the only reason for rejection of a loan.

#### General Property Conditions

- The appraisal should contain sufficient information so that the reader is able to understand the report and will not be misled or confused
- The neighborhood is one of the most important considerations in evaluating the property as security for the loan because it outlines the general marketability of the property. If the appraiser has noted any of the following items in the Neighborhood section of the appraisal report, careful consideration should be given to insuring loans in the neighborhood:
  - Growth Rate – Slow
  - Property Values – Declining
  - Demand/Supply – Oversupply
  - Marketing Time - Over 6 months
  - Change in Present Land Use - Likely or In Process from single-family use
  - Any comment that indicates adverse influences affecting marketability or market conditions in the neighborhood. For example:
    - Factors that may influence marketability include proximity to employment and support services (i.e., grocery stores, dry cleaners), adequacy of transportation, ingress and egress to/from the neighborhood, presence of environmental hazards, airport or traffic noise, or buffers protecting properties from adverse influences
    - Factors that may affect market conditions include the inventory of competing properties, overbuilding, sales and financing concessions (i.e., marketing programs offering loan discounts, interest rate buydowns, and other give-a ways) and availability of financing
- Vacancy rate of neighborhood is low and stable
- Neighborhood is "built-up" over 25% and is showing steady growth

- Marketing time is less than 6 months
- Design and material usage should be typical of the neighborhood. Pioneering designs such as underground improvements, irregular floor plans, log cabins, and geodesic domes, which lack a ready resale market, are generally not acceptable.
- The site of the subject property should be typical of the neighborhood and sufficient in size to adequately support all improvements

The following conditions should be evident in the Site section of the appraisal report and any deviations should be adequately explained in the Comments section:

- Size and shape of the lot adequately support all improvements
- Site characteristics are typical of the area
- Maximum lot size is 10 acres provided the property is residential in nature. Agricultural-type properties are not eligible
- The Highest and Best Use as improved should be the present use and expected to be a residential use
- There should be no easements or encroachments which could adversely affect the market value
- Any adverse site conditions (i.e., special assessments, slide areas, illegal or legal non-conforming zoning use) or superior site conditions (i.e., view) that would affect value or marketability, should be discussed in the appraiser's comments, and have corresponding and appropriate adjustments made to Land Value in the Cost Approach and Site/View in the Sales Comparison Analysis, if applicable.
- Site does not have soil conditions designated as "dangerous to health" or "unsupportive of improvements."

Note: If the appraisal report notes that the subject property is negatively affected by environmental hazards the loan should not be insured by PMI.

- The Improvements section of the appraisal report should be fully developed so that the underwriter is able to determine that the improvements are typical for the neighborhood. Any items not typical of the area, which could cause loss of marketability, must be explained in the Comments section. The following conditions should be present:
  - The improvements should be in a livable state and not in need of any major repairs or remodeling in order to be marketable
  - Livable square footage for detached properties should generally not be less than 650 square feet and should be typical for the area
  - Additional features (such as energy efficient items), condition of the improvements (i.e., physical or functional depreciation, repairs needed, and quality of construction), and adverse environmental conditions (such as toxic substances), must be addressed by the appraiser's comments and have appropriate, corresponding adjustments made to the Cost Approach or Sales Comparison Analysis, if applicable
- In the Sales Comparison Analysis (also known as the Market Data Approach), an estimate of value is determined by comparing the subject property with recently-sold properties similar to the subject. Since no two properties are exactly alike, each comparable is compared to the subject property, and the sales price of the comparable property is adjusted for any dissimilar feature. The following considerations should be given to review of the Sales Comparison Analysis:
  - Market appeal should be demonstrated by comparable sales having similar size, layout, and characteristics to the subject
  - Three comparable sales from the subject's marketing area should be used. In new subdivisions, the appraisal should have at least one sale within the general market area and one sale within the subject subdivision or project. Preferably, the third sale should also be from within the same subdivision or project as the subject, as long as it is an arms length sale, and the builder/developer is not involved with the sale.
  - Comparable sales should be no more than six months old unless the reason is satisfactorily addressed by the appraiser. Shorter marketing times are necessary for property in either declining or increasing value markets.
  - Sales concessions and financing concessions must be consistent with information provided in the Neighborhood analysis section. The appraiser should make appropriate adjustments to

the comparable sales to reflect the value of these concessions. Additional explanation may be required to support the adjustments.

- Builder/seller contributions are limited to interest rate buydowns and reasonable and customary closing costs, which would normally be paid by the borrower and are subject to program limitations.
- Total net adjustment of each comparable sale should generally be within  $\pm 15\%$  of its sales price; line item adjustments should not exceed  $\pm 10\%$ ; gross adjustments should be within  $\pm 25\%$ .
- The Income Approach is only required when the subject property is located in a neighborhood where rental properties are prevalent, and economic market rents and gross rent multipliers can be substantiated for development of an indication of value. If this situation does not exist, the appraiser should indicate that the Income Approach is “not applicable.”
- Condition comments should not reflect any items that may detrimentally affect the market value or marketability of the property. All new construction or major remodeling should be completed prior to the insuring the loan.

The final estimate of value should fall within the range of indicated values shown by the final adjusted sales prices of the comparable sales.

### **Two-to-Four Units Appraisal Review (5/16/11)**

Small residential income properties (2-units) should be considered favorably as security. The following are additional considerations in review of the 2-4 units property appraisal:

- There is less than a one year supply of 2-4 units in the subject's immediate area.
- Maximum marketing time is less than nine months.
- The vacancy rate of the neighborhood is low and stable.
- The apartment occupancy rate in the area is at least 90%.
- The neighborhood is at least 50% built-up or is showing steady growth.
- No sales or rental concessions (i.e., give-aways, free trips, decorator allowances, rebates, etc.) are being offered.
- Land is owned in fee-simple estate.
- Floor plan and unit sizes are functional.
- Size and shape of the lot adequately support all improvements.
- Site is typical of competing 2-4 units and the market area.
- Design and material usage are typical of the neighborhood. No pioneering designs should be accepted.
- Generally, the livable square footage is not less than 550 square feet per unit.
- The improvements section should indicate that features of the property, including modernization, on-site parking facilities, appliances, and insulation are typical for the market area.
- The Small Residential Income Property Analysis Report must provide comparable rental data from which the potential economic rents of the subject property can be accurately projected. The comparable rental data should include the following:
  - Three comparable rental properties within subjects marketing area whose characteristics are similar to the subject
  - Adequate information on the comparable rental properties should be provided to enable an informed evaluation of actual and forecasted rents
  - Analysis of monthly rent per square foot of living area and monthly rent by room count comparing the subject to the comparable rental properties
- The major difference between the Sales Comparison Analysis of a single-family property and that of a 2-4 unit property is the consideration of units of value. The appraiser calculates units of value to determine the most common price 2-4 unit buyers and sellers of residential income properties will use to make their purchase decision.
- Units of value in the Sales Comparison Analysis of 2-4 unit properties include:
  - Sales Price per square foot of Gross Building Area
  - Gross Monthly Rent Multiplier

- Sales Price per Unit
- Sales Price per Room

When reviewing the Sales Comparison Analysis of a 2-4 unit property, additional consideration should be given to the following:

- Financing or other sales concessions must be considered in relation to typical market acceptance and appropriate adjustments should be made to the comparable sales to reflect the value of these concessions.
- The final reconciliation of value should consider any unadjusted units of value reported in the Sales Comparison Analysis.
- Total expenses and replacement reserves should be typical to those of competing properties.
- The appraiser's comments should indicate that there are no conditions which could detrimentally affect the market value or marketability of the property.
- All new construction or major remodeling should be completed prior to insuring the loan.

### **8.6 DISTRESSED AND DECLINING MARKETS APPRAISAL REVIEW (3/08)**

It is critical to review and analyze the appraisal for every loan to ensure that the property value is supported. This review should be completed regardless of any AUS, collateral assessment model, or other messaging received. A poor, inaccurate, or incorrect appraisal report is not corrected by a reduction in the LTV.

This information is provided to give guidance on how to identify distressed/declining markets in the event such information may not be indicated on the appraisal report, or when the AUS messaging indicates a distressed/declining market. It is important to recognize that the AUS messaging and the information provided in the appraisal can be helpful in determining when a more careful review of the appraised value is required.

Although, there is no standard industry definition of what constitutes a distressed/declining market, generally this is a specific geographic area with property values that have been influenced by foreclosure, unemployment, and other factors affecting the property values in those areas, or specific geographic areas, with property values that have been declining, or are likely to decline.

From a lending perspective, the greatest credit risk occurs when a property is overvalued. The overvaluing of a property results in the understatement of the (LTV) ratio and/or insufficient collateral. The possibility of overvaluation increases in a distressed/declining market. With recent trends indicating that home prices are falling in many areas across the country, it is important to thoroughly review the appraisal report to ensure that it accurately reflects the current market value of the subject property.

There are a number of factors found on the appraisal report that can be used to determine if a property is located in an area where prices are falling. These factors include the property's location, comparable sales, neighborhood characteristics, and current market trends. The degree to which these factors influence the subject property's value should be fully disclosed and supported by the appraiser on the appraisal report.

#### **Appraiser's Responsibilities**

It is the responsibility of the appraiser to use industry data and market trend information to determine if property values are declining in a particular area. The appraiser's analysis should demonstrate an understanding of the subject property's location, neighborhood characteristics, and current market conditions in order to accurately assess the value of the subject property in a specific geographic area. In short, the appraisal needs to support the value given by the appraiser.

### Underwriter's Responsibilities

It is the underwriter's responsibility to complete a thorough evaluation of the appraisal to ensure that the report is complete, accurate, and consistent with appraisal and investor standards, and that it provides a reasonable determination of the property value. The underwriter should be able to determine from the information provided on the appraisal report whether or not the property value constitutes sufficient security for the mortgage. Identifying inconsistencies within the appraisal report as they relate to the property value is a critical part of the appraisal review.

Underwriters are required to review the appraisal in its entirety for completeness, accuracy, and consistency to ensure that it provides an adequate determination of property value, regardless of what message is received from any Automated Underwriting Systems (AUS), or other collateral assessment models.

### AUS Messages

When loans are reviewed by an AUS, the underwriter is expected to:

- Review the appraisal to ensure consistency with appraisal standards and evaluate the properties acceptability as security for the loan as it relates to its value and marketability
- Ensure that the appraiser analyzes current listings and contract sales along with the most recent closed sales. If the appraisal report does not accurately reflect the current market conditions, additional clarification, justification, and comparables should be requested from the appraiser.

There are several key phrases or messages that may be received regarding the appraisal, which can be used as indicators of property value:

- ...returned the following standardized address and census tract for... This is the address that will be used in its property valuation and fieldwork...
- ...collateral assessment model indicates that the submitted value estimate for this ....transaction may be excessive.
- ...collateral assessment model indicates that the ....appears to have an excessive rate of appreciation....
- The subject property has been identified as being located in either an area of declining home prices or in an area where it may be difficult to assess home values...
- Review for accuracy: The estimated value of property or net purchase price submitted for this transaction may have a higher rate of appreciation than the local market...
- Form (2055, 2065, 2075) is the minimum assessment required ...

A message that simply indicates the form number required for the appraisal and is *not* an assurance that the value of the property is accurate. The absence of any of the above messages does not indicate that the submitted value is appropriate as the appraised value for the property. The appraisal would still require a thorough review for completeness and accuracy.

### Appraisal Review Process

**Property Location** – A good starting point is to determine where the subject property is located by referring to the location map.

- Determine if the location map has been reduced in size or “zoomed-out” in order to fit all of the comparables and the subject property on the same map; check to see if the street names are visible. The location map should clearly identify the location of the subject property. Cross-check the property location through mapping websites. Compare streets on the location map to the neighborhood boundaries provided on page one of the appraisals.
- The neighborhood description should be compared to the location map to determine if there are any barriers, such as a freeway, major thoroughfare, creek/river, hills/mountains, park/golf course or large designated open space that determines the subject property's neighborhood boundaries.

- Refer to the location map to determine if the same types of barriers separate the subject property from the comparable sales. This could indicate that the comparable sales are in a different neighborhood from the subject property. In such instances, additional comparables should be requested.

**Comparable Sales** - The comparable sales should be as similar as possible to the subject property. Inconsistencies among the comparables decrease the accuracy of the appraised value. In using the sales comparison approach, the following guidelines will help ensure that the comparables support the value of the subject property:

- *Number of comparables* – A minimum of three closed comparables should be provided that are similar to the subject property in location, age, condition, room count, lot size, and square footage, etc.
- *Proximity to subject* - As a general rule, the comparables should be within one mile of the subject property. The appraiser should provide an explanation for any sale that is considered to be outside the neighborhood boundaries (i.e., separated from the subject property by a barrier or boundary referenced by the appraiser on page one.)
- *Date of Sale/Time* – The marketing time of the subject property and the comparables do not have to be the same, but there should be a correlation between the two. Although the comparables' date of sale is required to have closed within the last 12 months of the effective appraisal date, using the most recent comparables available helps ensure that current market conditions are reflected.
  - Comparable sales over 6 months old should be explained by the appraiser. For example, if the comparables are not recent (i.e., 6-12 months old) they may not reflect the most current price trends in the area. The comparables' sales prices may in fact be inflated, if prices have declined in the area.
  - If the appraisal indicates that the subject property has a marketing time of less than 3 months in the *Neighborhood* section, but the comparables are 12 months old, the appraiser should provide a detailed explanation as to why there is such a large difference in the marketing times of "similar" properties.
    - For example, the appraiser's explanation might be "the neighborhood is very stable, limited sales have occurred, and they sell quickly when they come on the market." An unacceptable response would be "comparables less than 12 months old are not available." While this may be a true statement, it does not explain why the appraiser indicates the marketing time as less than 3 months.
- *Similar Unit Structures* - Compare the photographs of the comparable sales to determine if the subject property is the same type of unit structure. For example, if the subject property is a ranch-style home, but the comparables are two-story homes, then the comparables and subject property are not similar properties. Additional comparables should be requested to reflect the same type of unit structure.
- *Functionality* – The comparable sales should have the same functionality as the subject property. For example, if the subject property has a 4 bedroom/2 bathroom count, then a similar property should generally have an equal room count, not a smaller one of 3 bedroom/2 baths. A value adjustment may not adequately address the differences in functionality between 3/2 and 4/2 room counts; even if they have the same or similar square footage, because room count is driven by a different market influence. The appraiser must address significant differences between the subject property and the comparable sales if they raise doubts about the validity of the comparable sales as good indicators of value.
- In established subdivisions, Planned Unit Developments (PUD), or condominiums (condos), the comparables should be from the same subdivision or PUD. An explanation is required from the appraiser as to why comparables are located outside the boundaries of the subdivision/PUD.
- In new subdivisions and condo projects, the appraisal should have at least one sale within the general market area, and one sale with the subject subdivision or project. The third comparable sale should also be from within the same subdivision or project, as long as it is an arm's length sale, and the builder/developer is not involved with the sale.

- In rural areas, the value of the property should be fully supported by the appraisal. The appraisal report should provide a thorough analysis of the subject's property value, if it is located in a rural area, as the comparable sales may well be located a considerable distance from the subject property. When assessing the value of a rural property, it is crucial that the appraiser is familiar with rural lending practices, as they differ greatly from suburban or urban markets.

### Neighborhood Section

The *Neighborhood* section of the appraisal report identifies several factors, which may provide insight as to whether a property is located in a distressed/declining market. These factors include the property's general location, the built-up and growth rates in the area, the trend in property values, the demand for housing versus supply, and marketing time. The neighborhood boundaries, as well as, a description of the neighborhood itself should be described in this section.

Generally, a detailed explanation from the appraiser is required when the following Neighborhood and/or Unit Housing Trends characteristics are indicated on the appraisal report.

- Location - *Rural*
- Built-Up - *Under 25%*
- Growth Rate - *Slow*
- Property Values - *Declining*
- Demand/Supply - *Oversupply*
- Marketing Time - *Over 6 months*

If the appraisal reflects an over supply of properties, the marketing time exceeds six months, or the other comments within the appraisal report indicate that the values are declining, the appraiser must supply comments supporting the increasing or stable selection.

It would be highly unlikely that all of the above mentioned "red flags" would be marked on the same appraisal. However, the following combination of *Neighborhood Characteristics* and *Housing Unit Trends*, although not comprehensive, may point to a distressed/declining market which should prompt further investigation:

- Built-Up Under 25% / Market Time Under 3 months
- Growth Slow / Marketing Time Under 3 months
- Growth Slow / Demand/Supply Shortage
- Property Values Stable / Marketing Time Over 6 months

### Neighborhood Characteristics

*Location* – In general, rural properties are more difficult to value than Urban or Suburban areas due to their mixed characteristics, such as; large lots, varying house designs and styles, and the agricultural influence of the surrounding area. Rural areas are typically less than 25% developed and exhibit slower growth and longer marketing times than urban or suburban neighborhoods.

*Built-Up* – This rate (expressed as a percentage) indicates the extent to which the neighborhood has been developed. If the neighborhood is under 25% developed, the development progress and its impact on property values should be addressed in detail by the appraiser, as this may indicate weak price appreciation. Rural areas zoned residential or with a Built-Up rate of over 75% indicates an inconsistency that warrants further investigation to ensure that the comparables and the subject property are located in the same market area. Confirmation that the property is actually located in a rural area, as opposed to a suburban or urban area where the Built-Up rates are typically higher, should be obtained from the appraiser.

*Growth* - This helps determine the current stage in the life cycle of the subject property, as well as, the neighborhood. Growth in new and developing areas is generally "Rapid." Once all of the land is developed, growth becomes more balanced and is considered "Stable." Growth continues in older and established neighborhoods due to changes in land use or redevelopment. If growth is indicated as

“Slow”, a detailed explanation should be provided as to why, since this may indicate that prices are weakening and that the subject property is located in a distressed/declining market.

### Unit Housing Trends

*Property Values* - The appraiser must identify whether the property values in the neighborhood are “Increasing,” “Stable,” or “Declining.” Maximum financing is only appropriate when property values are stable or increasing.

*Demand/Supply* – If an “Oversupply” of housing inventory is indicated, then an adequate explanation of its impact on the value, as well as, the marketability of the subject property should be addressed. An oversupply of housing may result in a softening of house prices. In general, when there is more than a six-month supply of housing inventory, the market is considered to be a “buyer’s market.” Typically, in a buyer’s market, the supply of houses exceeds the demand, which tends to drive prices down and can lead to increased sales incentives.

*Marketing Time* – If a marketing time of “over 6 months” is indicated, then the appraiser should provide an adequate description of the property’s marketability. Longer marketing times are often an indication of declining home prices.

*Price Range* – The sales price of the comparable sales and the price of the appraised value of the subject property should be close to the predominate value in the neighborhood. Otherwise, the appraiser may have used overpriced comparables to determine the value of the subject property.

*Neighborhood Boundaries* - The comments made in the *Neighborhood Boundaries* section should clearly outline the neighborhood in which the subject property is located. Generally, neighborhoods do not encompass an entire city, town, township, borough, etc. Specific boundaries, natural or otherwise, such as a freeway, a major thoroughfare, creek/river, large open space, railroad tracks, hill/mountain range, park/golf course, etc., typically mark the borders of a neighborhood. The identification of boundaries ensures that the comparables are located in the same neighborhood as the subject property. Comparable sales located outside the neighborhood boundaries are not acceptable.

*Neighborhood Description* - Comments in this section provide information regarding neighborhood characteristics, identification, and marketability. This may include comments on the proximity to employment centers, amenities, and adverse environmental influences.

*Market Conditions* – This section is where the appraiser provides adequate support for the neighborhood characteristics. Comments regarding the trend in property values, demand and supply, marketing times, and data on comparable properties in the neighborhood should be supported in detail. Any indication of weak or falling home prices warrant further investigation, as this may indicate the subject property is located in a distressed/declining market.

### Inconsistent/Questionable Information

If inconsistent or questionable data appears on the appraisal report, or if such information points toward distressed/declining home prices, the underwriter should:

- Request written explanations from the appraiser regarding inconsistencies and/or questionable data
- Require detailed explanations to support the use of questionable data/information, such as, large price adjustments, marketing times over 6 months, and comparable sales older than 6 months, etc.
- Request additional comparables or listings to confirm the value of the subject property, if those provided appear to be located outside the subject property’s neighborhood, far exceed the predominate price in the area, or are a different unit structure, etc.

## 8.7 CONDOMINIUM PROJECT ELIGIBILITY (3/1/11 AND 3/28/11)

PMI does not approve condominium projects. The review of the appraisal and compliance with PMI guidelines does not constitute a project approval. We insure condominiums that meet the following criteria:

All Condominium projects must meet the following guidelines:

- Must meet Fannie Mae or Freddie Mac Guidelines
- No single entity (the same individual, investor group, partnership, or corporation) may own more than 10% of the units within the project
- No more than 15% of the total units in the project can be 30 or more days past due on the payment of condo/association fee payments
- No more than 33% of the project can be insured by PMI

When determining condo project acceptability, PMI expects the lender will:

- Determine that the project meets standard Agency guidelines and the criteria detailed below
- Provide supporting documentation for the determination

Supporting Documentation can be, but is not limited to the following:

- HOA Questionnaire - can be used to determine investor concentration, commercial usage, single entity ownership and project delinquency levels
- Budget/Balance Sheet - utilized when a budget analysis is required (all projects except those that receive a Limited or Streamlined Review option from DU or LP)
- Appraisal - used to determine project characteristics, ownership, pre-sale levels, marketability, and completion levels
- Other documents deemed necessary by the lender

Site Condominiums:

- Attached must follow PMI Condominium Eligibility Criteria
- Detached follow single family guidelines

### **DU LIMITED OR LP STREAMLINED REVIEW RECOMMENDATION**

- Maximum 90% LTV
- Established projects only

Review the appraisal to determine the following guidelines are met, no further documentation on the project is necessary:

- Must be 100% complete including all common areas and the HOA has been turned over to unit owners
- Maximum 30% investor (non-owner occupied) concentration
- No more than 20% commercial usage

Ineligible for Limited/Streamlined review:

- Projects up to ten units
- Additional ineligible projects detailed below

### **ALL OTHER ESTABLISHED PROJECTS**

- Maximum 97% LTV
- Must be 100% complete including all common areas and the HOA has been turned over to unit owners
- Maximum 30% investor (non-owner occupied) concentration
- No more than 20% commercial usage
- Complete Budget Review
  - Must be adequate; and
  - Must provide for funding for replacement reserves and deferred maintenance of at least 10%; and
  - Must provide adequate funding for insurance deductible amounts

Ineligible:

- Detailed below

### **PROJECTS UP TO 10 UNITS**

- Maximum 97% LTV
- Must be 100% complete with all common areas complete and HOA turned over to unit owners

- HOA must have a binding arbitration agreement
- No commercial usage
- Maximum Investor Concentration, as follows:
  - 9-10 Unit Property - Three units
  - 6-8 Unit Property - Two units
  - 4-5 Unit Property - One units
  - 2-3 Unit Property - None
- Complete Budget Review
  - Must be adequate; and
  - Must provide for funding for replacement reserves and deferred maintenance of at least 10%; and
  - Must provide adequate funding for insurance deductible amounts

Ineligible for up to 10 units:

- Limited or Streamlined Review
- Additional ineligible projects detailed below

### NEW PROJECTS

- Maximum 97% LTV
- Must be 90% complete including all common areas and the HOA has been turned over to unit owners
- Pre-sale requirement: at least 70% of the total units in the project or subject legal phase must have been conveyed or be under a bona fide contract for purchase to owner-occupant primary residence or second home purchasers
- No more than 20% commercial usage
- Individual units must be available for immediate occupancy at the time of the loan closing
- Complete Budget Review
  - Must be adequate; and
  - Must provide for funding for replacement reserves and deferred maintenance of at least 10%; and
  - Must provide adequate funding for insurance deductible amounts

Ineligible new projects:

- Projects in Distressed Markets
- Additional ineligible projects detailed below

### Ineligible projects:

- Projects that are ineligible to Fannie Mae or Freddie Mac
- Attached properties located in Florida
- Projects with pending lawsuits that impact the safety, structural soundness, habitability or functional use of the project
- Projects with outstanding environmental issues
- Any project or building that is owned by several owners as tenants-in-common
- Condotels
- Kiddy condos (condominiums purchased for student occupancy)
- Timeshare, fractional or incremental ownership
- Manufactured housing site condominiums
- Multi-dwelling unit condominiums

## 8.8 CONDOMINIUM CONVERSIONS (2/09)

Condominium conversions include apartments or improvements built for other uses and converted to condominium projects through legal filing of a Declaration of Condominium or Master Deed. Rehabilitation of the property may or may not have taken place at the time of conversion. It should be

noted that condominium conversion projects are higher-risk properties.

Resale of converted condominium units are eligible for insurance if all units have been previously sold to individuals other than the developer, the project has been turned over to the HOA, and all other condominium project eligibility requirements have been met.

### 8.9 COOPERATIVE HOUSING UNITS (6/10)

Cooperative housing (co-ops) is a form of multiple ownership of real estate in which a corporation, trust, or business entity holds title to a property and grants occupancy rights through purchase of stock representing the value of a particular apartment or unit. Title to the apartment or unit is evidenced through issuance of a Proprietary Lease.

Co-ops **cannot** be insured under PMI's First Lien Master Policy. Before a co-op loan can be considered, PMI must file a Co-op master policy with each the state's insurance department. PMI is currently approved by California, Connecticut, District of Columbia, Florida, Illinois, Maryland, Massachusetts, Minnesota, New Jersey, New York, Vermont, and Virginia to insure Co-ops. To be eligible for LPMI, both the property and the lender must be domiciled in one of the approved states.

Lenders must be prior approved and issued a Co-op master policy UW 2180.00, to submit co-op loans to PMI. The lender is responsible for determining that the Co-op meets project requirements and is warrantable prior to submission to PMI.

The following is provided for **informational purposes only**. Co-op lenders must obtain relevant documentation to ascertain that the cooperative corporation is a validly-formed entity authorized to carry out its independent purposes in compliance with all applicable state and local laws. The cooperative documents must provide:

- Terms that sufficiently explain the manner in which the corporation is managed and controlled
- A legally permissible procedure for handling any losses or proceeds from condemnation, destruction, or liquidation of all or part of the project, or from termination of the project
- Coverage requirements for hazard, flood, liability, and fidelity insurance
- Cooperative Loan Agreement
- Recognition Agreement
- Proprietary Lease and Security Agreement
- Assignment of the Proprietary Lease
- Membership certificate, stock, or shares
  - UCC Financing Statement
  - Evidence of Stock Power

#### Cooperative General Characteristics

- Living Space – Owned by Cooperative Corporation and leased to the member/tenant/stockholder
- Financing – Blanket mortgage and unit share loan
- Collateral – Blanket mortgage on real estate; unit share loan o pledge of stock/proprietary lease
- Mortgagor – Cooperative Corporation on blanket mortgage; Cooperative member pledging shares on unit mortgage (junior to blanket mortgage)
- Common Areas and Facilities – Owned by Cooperative Corporation
- Real Estates Taxes – Paid by Cooperative corporation
- Homeowners' Association Dues – Monthly Maintenance Fee
- Basic Project Documents – Articles of Incorporation, By-Laws, Proprietary Lease, Stock/Membership Certificates, Share Loan Agreement, Recognition Agreement, Security Agreement, and UCC Financial Statement
- Income Tax Deductions – Proportionate pass-through of blanket mortgage interest and RE taxes to members under Section 216; direct deduction of unit share loan interest

For a co-op to be considered for approval the following underwriting guidelines must apply and consideration will be given to the following co-op project characteristics:

- Owner-occupied and second home properties only
- Fixed-rate/positively amortizing, positively amortizing ARM loans, Balloon Mortgages (minimum term of 5 years) are eligible
- Subordinate financing is not eligible
- Projects should have a minimum of five units
- Projects situated on leased land are not eligible
- Projects with over 20% investor ownership are not eligible
- Commercial space should not exceed 20% of the total building space
- Buildings that were originally built for purposes other than residential use are generally not eligible

### Cooperative Housing Unit Appraisal Review

Additional appraisal considerations are as follows:

- The unit should be appraised using the Fannie Mae/Freddie Mac Individual Cooperative Interest Appraisal Report or the Individual Condominium Unit Appraisal Report with addendums to address the market value of the cooperative shares over and above the pro rata share of the blanket mortgage(s). Alternative appraisal forms must be prior-approved by PMI's National Real Estate Analyst/Appraiser.
- The appraiser must utilize only cooperative units as comparable sales. PMI will **not** insure cooperative housing in pioneering areas. If cooperative comparable sales are not available, the cooperative loan is **not eligible** for mortgage insurance.
- The appraiser should compare the subject unit to the general marketing area as well as to other units in the subject co-op.
- Design of competing co-ops used as comparables should be the same as the subject (i.e., townhouses, mid-rise, high-rise, etc.) and should have similar common amenities and recreational facilities.
- Estimated market values for in-house purchased units must be appraised as if purchased by outside purchasers. The appraisal should also state "inside purchase".
- The expiration of the shareholder's Proprietary Lease must occur after the expiration of the blanket mortgage term.
- Blanket Mortgage
  - The terms of the blanket mortgage must be disclosed at the time of application.
  - If the project's blanket mortgage involves a balloon payment, the loan must have a minimum term of three years remaining after the PMI Commitment and Certificate of Insurance effective date.
  - The blanket mortgage must be current at the time of commitment.
- If Fannie Mae owns the blanket mortgage, the value of the Proprietary Lease should be calculated by subtracting the borrower's portion of the blanket mortgage from the purchase price. The blanket mortgage is **not** to be included in the insured loan amount.

For example:	Purchase Price	\$100,000
	Borrower's Portion of the	- 10,000
	Adjusted Price	90,000
	10% Down	- 9,000
	Insured Loan Amount	<u>\$ 81,000</u>

- The appraiser must provide the pro rata share of the blanket mortgage payments that are attributable to the unit, as determined by dividing the number of shares attributable to the unit by the total number of project shares. The appraiser certifies in the appraisal report that the pro rata share of the blanket mortgage on the real estate has not been included in the opinion of market value. The pro rata share should generally not exceed 30%.
- The appraiser should complete the section regarding the unit being subject to a stock transfer fee (flip tax). When there is a fee the value of the unit must be reduced by the amount of this fee.

### 8.10 LEASEHOLD PROPERTIES (12/06)

A leasehold estate grants the lessee (borrower) the right to use and occupy real estate for a stated term and under certain conditions. This right is granted through execution of a Lease or subsequent Assignment of Lease.

Due to the lease term and restrictions and additional expense of leasehold payments, leasehold estates have generally not been as widely accepted or marketable as fee simple estates. To consider properties on leased land, the following conditions must apply:

- Comparable sales of leasehold estates must be readily available as an indication of marketability.
- Term of the land lease must exceed the term of the insured loan.
- Land lease payments must not increase the total monthly housing payment by more than 1%.
- If the insured loan has provisions for term extensions, the land lease must also have the same provisions.
- Monthly lease payments (or the monthly equivalent of quarterly or annual lease payments) must be added to the borrower's monthly housing expense when calculating debt-to-income ratios.

### 8.11 RURAL PROPERTIES (12/06)

Rural neighborhoods are typically less than 25% developed and exhibit slow growth. When evaluating rural property, just as with urban or suburban properties, the underwriter must ascertain that the property is readily marketable and constitutes sufficient security for the mortgage loan in the event of default.

#### General Property Conditions

Rural properties should be considered favorably as collateral if the following general property conditions exist:

- The nature of the property is primarily residential and the borrower does not intend to use the property for operation of a non-residential purpose such as a farm, orchard, or ranch. Agricultural-type properties are not eligible.
- PMI generally insures properties up to 10 acres provided the property is residential in nature.

#### Rural Property Appraisal Review

The following are major considerations to be reviewed in the rural property appraisal report:

- The neighborhood growth rate should be rapid or stable
- Property values should be stable or increasing
- Demand/supply should be in shortage or balanced
- Marketing time for rural properties should be less than twelve months
- In general, the land should not exceed ten acres or land value exceeds 50% of total estimated value. It is not an acceptable practice for the appraiser to provide a value based on a portion of the land, i.e., instead of the entire parcel to meet the maximum site requirements. Agricultural-type properties are not eligible.
- Location adjustments exceeding 15% should be satisfactorily explained by the appraiser
- The property should be connected to at least one public utility. Utilities to the site should be standard for the community, accepted by the residents of the property, and support year-round use.
- On-site and off-site improvements should include all-weather public roads, paved or graveled driveways, and paved parking
- Estimated value of all building structures (excluding house and garage) such as barns, sheds, corrals, tack rooms, etc., should not exceed 20% of the total estimated value
- The appraiser should provide a satisfactory explanation if all comparable sales are located more than five miles from the subject property
- The site size should be typical for the area
- The site should be marketable for residential use

- The size of the comparable sales' sites should be similar to the subject. If the size of all comparables differs from the subject by more than +/-50%, the appraiser must provide a satisfactory explanation
- Any adjustments to value for mineral rights must be fully explained by the appraiser