



## **BROKER MEMO**

Date: September 8, 2009

Subject: Agencies clarify their Sound Mortgage Underwriting Practices

We have been advised that, although credit quality has dramatically improved over the last few months, Fannie Mae and Freddie Mac (The Agencies) are still seeing a number of deficiencies in the underwriting process. In order to improve underwriting quality and ultimately the performance of mortgages, the Agencies have announced revised underwriting requirements that will be effective as of 10/1/09. They also “strongly recommend” lenders implement them right away. You may find that some of the ‘revised guidelines’ seem redundant...as business has been done this way for some time, however there is enough new material for your review to be valuable.

You can expect the following guidelines to be effective going forward for ALL LOAN TYPES (Conventional, FHA, VA and USDA) as follows:

### **INCOME**

The Agencies require a two-year history of receipt of income used to qualify the borrower for most situations:

#### **W2 EMPLOYEES/NON SELF-EMPLOYED**

1. W-2's for the most recent two (2) years
2. Recent paycheck stubs verifying income for a minimum 30 day period
3. Telephone verification of employment not more than 10 calendar days prior to Note date.
4. For military income (in lieu of a telephone verification of employment) a Leave and Earnings Statement dated no more than 30 days prior to Note date.

#### **SELF EMPLOYED**

1. Complete signed individual federal tax returns for the most recent 2 year period - validated thru the IRS via form 4506 prior to final approval.
2. Complete business tax returns for the most recent 2 year period - validated thru the IRS via form 4506 prior to final approval.
3. Verification of existence of business through a third party source not more than 30 calendar days prior to the closing of the loan.

## **TAX EXEMPT INCOME**

Require the borrowers provide copies of tax returns to prove that income sources are in fact tax exempt.

## **INCOME FROM ALIMONY, CHILD SUPPORT OR SPOUSAL MAINTENANCE** (Conventional only)

1. Borrowers will be required to have a history of being entitled to receive alimony, child support, or spousal maintenance in addition to verifying it has actually been received.
2. The amount of this income source that can be used to qualify will depend upon how long the borrower has been entitled to receive the income. In all cases, the income source will need to be documented that it will continue for at least three (3) years after closing.
3. If the borrower has been entitled to receive the income for the most recent 12 months, the full amount of the income can be used for qualifying.
4. If the borrower has been entitled to receive the income for less than the most recent 12 months but for at least the most recent 6 months, then the income can be considered as long as it does not exceed 30% of the borrower's total qualifying monthly income
5. If the borrower has been entitled to receive the income for less than the most recent 6 months, the income cannot be considered for qualifying purposes.

## **TRAILING SPOUSE INCOME**

Trailing spouse income is no longer allowed for qualifying purposes.

## **RENTAL INCOME**

If an investment property is currently owned by the borrower for the most recent IRS tax year, the positive or negative cash flow for the property will be calculated based on the tax returns. If investment properties have been acquired subsequent to the most recent tax year, rental agreements may be provided to demonstrate income.

## **ASSETS**

In general, assets must be seasoned for a minimum of two months, so two months worth of bank statements (all pages of each statement, including blank pages) must be provided.

## **RETIREMENT ACCOUNTS**

The value of all retirement accounts, for qualifying purposes, has been re-defined to be the vested account balance less any outstanding loans secured by the retirement account. 70% of the "net" vested amount may be used.

## **DEPOSITORY, STOCK AND BONDS**

1. Proof of Liquidation is required when assets are needed for funds to close.  
Cash assets sufficient to close the loan must be verified.
2. Require evidence of the source of funds for any cash deposit (earnest money, lender deposit, etc) made by the borrower.

## **RESERVES**

The following outlines guidelines for using assets other than cash for cash reserves:

### **Stocks, Bonds, Mutual Funds, and other Securities**

Conventional: 70% of the account value may be used as cash reserves  
FHA: 100% of the account value may be used as cash reserves  
VA: 100% of the account value may be used as cash reserves

### **Retirement Accounts**

Conventional: 60% of the vested account value (after subtracting any loans)  
FHA: 60% of the vested account value (after subtracting any loans)  
VA: 70% of the vested account value (after subtracting any loans)

The stated goal of the Agencies is to improve the quality of loan originations by allowing lenders to review a more complete picture of the borrower's financial position. The net result will also include increased difficulty in approving some loan applications. As always, I will communicate the guidelines as clearly as possible to you and your buyers.

For questions, please contact your Account Executive. Thank you for your business.

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