



**Guide to Underwriting
with DU[®]**

July 2005



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Foreword

Foreword

Introduction

The *Guide to Underwriting with DU*[®] (Guide) is a reference manual for underwriting Fannie Mae's conventional conforming loans with Desktop Underwriter[®] (DU). In addition to identifying the specific characteristics in the loan application and credit report that DU uses to evaluate risk and provide underwriting recommendations, the Guide also contains detailed information for complete and accurate submission to DU.

All data entry instructions in this Guide are provided specifically for Fannie Mae's online loan application (Form 1003) in the DO[®]/DU user interface for submission to DU. There are other methods you can use to enter loan data; for example, you can download the data into the DO/DU user interface through a loan origination system, or you can submit the loan data directly to DU from a loan origination system. However, regardless of the submission method, lenders are responsible for determining that all appropriate data are properly transmitted to DU.

Throughout the Guide, *data entry tips* are provided for a quick reference on entering information into specific data fields in the DO/DU user interface.

Definitions

DU

DU is an automated underwriting system developed by Fannie Mae to help mortgage lenders make informed credit decisions on conventional conforming and government loans. DU features fast and objective risk assessments, reduced data entry requirements, reduced documentation, and comprehensive underwriting reports.

Desktop Originator

Desktop Originator[®] (DO) is a technology tool developed by Fannie Mae that allows mortgage brokers to electronically enter a minimal amount of data in the loan application, order a credit report, submit the loan to DU via a sponsoring lender, and receive an underwriting recommendation and underwriting reports – all in a matter of minutes. Because DU is the industry leader in providing users with specific messages tailored for each individual loan, mortgage brokers may find DO particularly advantageous at the point of sale.

Custom DU

Custom DU is a comprehensive origination and underwriting tool seamlessly integrated with DU. This tool enables lenders to develop their own

automated underwriting guidelines for conforming and nonconforming loans, format their underwriting findings reports, and create specific loan-level messages.

DO/DU user interface

The DO/DU user interface is Fannie Mae's online tool for entering data, ordering credit reports, submitting loan applications to DU, and managing the automated underwriting process.

DU-only transaction

A DU-only transaction is a loan transaction that requires DU processing in order to deliver the loan to Fannie Mae.

DU for Government Loans

DU for Government Loans, previously the Government Underwriting Service (GUST[™]), is the component of DU that underwrites FHA and VA mortgage applications.

FICO[®] credit score

FICO credit scores, which are created by Fair Isaac Corporation and developed using statistical methods to evaluate information that has proven to be predictive of loan performance, are numerical values that rank individuals according to their credit risk at a given point in time. A FICO credit score "rank-orders" applicants according to the likelihood that they will default in the future, with higher scores being indicative of a lower default risk and lower scores being indicative of a greater default risk.

Loan application

The term "loan application," when used in this Guide, refers to Fannie Mae's online version of the Uniform Residential Loan Application (Form 1003), dated 01/04, in the DO/DU user interface. The online loan application is available in two formats: Quick 1003 and Full 1003. The Quick 1003 allows you to submit a loan to DU with a minimal set of loan data, primarily for a quick underwriting recommendation. The Full 1003 allows you to complete all data fields. However, regardless of whether you use the reduced set of data fields in the Quick 1003 or the complete set of data fields in the Full 1003, DU analyzes only the required (minimal) data elements to provide an underwriting recommendation and determine loan eligibility.

All data entry instructions in this Guide refer specifically to Fannie Mae's online loan application in the DO/DU user interface for submission to DU. Lenders must ensure that all appropriate data is properly transmitted to DU regardless of the submission method.

Sections in the loan application

The Guide uses the abbreviations in the following table when referring to the corresponding sections of the loan application in the DO/DU user interface:

Abbreviation	Corresponding Name in the DO/DU user interface
Section I	Type of Mortgage and Terms of Loan
Section II	Subject Property Address, and Purpose of Loan
Section III	Borrower Information
Section IV	Employment Information
Section V	Monthly Income and Combined Housing Expense
Section VI A	Assets
Section VI R	Real Estate Owned
Section VI L	Liabilities
Section VII	Details of Transaction
Section VIII	Declarations

Loan List screen

The Loan List screen in DO/DU displays available services, including Create Loan, Import Loan, Refresh Data, and Loan Search.

How this Guide is organized

[Chapter 1, Desktop Underwriter Product Eligibility](#), beginning on page 17, provides specific information about the Fannie Mae loan products and mortgage terms that are available through DU, including the eligibility criteria for mortgages secured by manufactured homes.

[Chapter 2, Underwriting Loans with Desktop Underwriter](#), beginning on page 89, defines the underwriting recommendations offered by DU, and provides information regarding the limited waiver of underwriting representations and warranties available for eligible loans that are recommended for approval through DU. Chapter 2 also provides information on how DU analyzes income, assets, and credit.

[Chapter 3, Streamlined Property Valuation and Inspection Requirements](#), beginning on page 145, explains the appraisal and inspection fieldwork requirements.

[Chapter 4, Underwriting Reports](#), beginning on page 167, describes the reports that are available through DU.

[Chapter 5, Underwriting Recommendations](#), beginning on page 179, focuses on the underwriting recommendations available through DU and the required lender follow-up.

[Chapter 6, Quality Assurance System for Desktop Underwriter](#), beginning on page 197, details the components of Fannie Mae's post-purchase review procedures and the lender's quality control requirements that are applicable to loans processed using DU.

[Appendix A: Required Data Elements – Loan Application \(Form 1003\)](#) on page 205.

[Appendix B: DU Required Data Elements Additional Data Screen](#) on page 211.

[Appendix C: Guidelines for Entering the Subject Property Address in DU](#) on page 212.

What's new in the July 2005 edition

The July 2005 edition of the Guide incorporates all applicable data from the *DO/DU Version 5.5 Release Notes*. These updates, which are described in greater detail in the Release Notes, include:

- Adding standard 40-year term mortgages to the product line.
- Updating the MyCommunityMortgage™ product to allow
 - cash-on-hand as a source of funds;
 - less mortgage insurance coverage;
 - subordinate financing other than Community Seconds®; and
 - 5/1 ARMs.
- Implementing a new collection payoff policy for principal residence transactions requiring only collections and chargeoffs totaling more than \$5,000 (instead of \$1,000) be paid at or prior to closing.
- Applying new condominium and PUD project limited review guidelines.
- Updating property appraisal and inspection information to include the forms dated March 2005.

Other updates to the Guide include:

- New information on Energy Efficient Mortgages and the Smart Commute® feature; and
- Clarification that premium pricing on Flexible mortgages is not subject to the contribution limits.

Additional resources

In addition to the Guide, there are a number of resources available on eFannieMae.com that are designed to increase your knowledge and to enhance your experience with DU. For more information, visit our Web site at:

www.efanniemae.com

Customer support

The Customer Contact Center is available to assist you with general questions about DU and the DO/DU user interface. You can reach the Customer Contact Center at 1-877-722-6757. For specific underwriting, servicing, and delivery information, contact your Fannie Mae account team.

Desktop Originator/Desktop Underwriter Release Notes

The following Release Notes and their accompanying charts and tables are available:

Global system

These Release Notes describe the global system enhancements that improve the overall experience with DO/DU, regardless of whether you use the DO/DU user interface, a loan origination system with an interface to DO/DU, or direct integration.

DU for Government Loans (previously the Government Underwriting Service)

These Release Notes describe enhancements regarding FHA and VA loans underwritten with DU.

Underwriting system

These Release Notes describe enhancements to the DU underwriting system and are associated with this Guide.

User interface

These Release Notes describe enhancements to the DO/DU User interface, which include visual design and functionality.

DU Connections™

DU Connections gives lenders access to a suite of services to order, fulfill, and manage origination and settlement services such as appraisal, flood, title, and closing/escrow.

E-mail Subscription Service

Sign up for our E-mail Subscription Service to get the latest DU news and resources delivered to your electronic inbox.

Expanded Approval™ with Timely Payment Rewards® *Lender Guide*

The Expanded Approval with Timely Payment Rewards (EA/TPR™) *Lender Guide* is provided for participating lenders. For additional information on the EA/TPR initiative, contact your Fannie Mae account team.

Fannie Mae Announcements

Fannie Mae Announcements (Announcements) provide updates and clarification on Fannie Mae policy (per the *Selling* and *Servicing Guides*). References to the Announcements are made throughout the Guide.

Fannie Mae's *Selling Guide*

Fannie Mae's *Selling Guide (Selling Guide)* provides information regarding loan eligibility and additional information about income, asset, and credit documentation and underwriting analysis. An electronic version of the *Selling Guide* is available through subscription to AllRegs[®], which provides a comprehensive and up-to-date library of Fannie Mae's Guides and Forms.

Fannie Mae Property GeoCoder™

The Fannie Mae Property GeoCoder is a free, Web-based application that can be used to determine whether a property is located in an area that qualifies for the FannieNeighbors[®] mortgage option.

Help Center

The Help Center is an online tool that Fannie Mae created to provide quick and easy access to a database of helpful information about using DO/DU. This tool is available from every screen in DO/DU 24 hours a day, 7 days a week. In addition to easy access to frequently asked questions, the Help Center has a "Chat with an Expert" feature that allows you to submit questions online to a representative from the Customer Contact Center. These questions will be answered during the hours of operation for the Chat with an Expert feature.

Loan origination systems

You may have access to an informational Web site that is provided by your loan origination system (LOS) vendor. Contact your LOS vendor for more information.

Taking the Mystery Out of Your Mortgage Loan

This consumer booklet, written in everyday language, describes the risk factors DU considers when evaluating a mortgage application and the various credit characteristics that it examines to assess a borrower's credit record.

Test credit reports and test borrowers

A number of test borrowers are available for DO/DU training and testing purposes. The test credit reports associated with the test borrowers, as well as the DU submissions, are free of charge.

Training resources

On efanniema.com, you can access DO/DU training tools, such as Quick Steps, Test Borrower Procedures and Characteristics Matrix, Practice Cases, and online training presentations for current DU releases. In addition, a number of free training sessions are available.

Chapter 1:
DU[®] Product Eligibility

Chapter 1: DU[®] Product Eligibility

Introduction

DU offers an empirically designed statistical assessment of mortgage default risk, enabling the tailoring of specific loan terms based on an individual borrower's risk profile. The benefits of using DU include streamlined credit documentation, streamlined property valuation process and report forms, various mortgage insurance options, expanded loan-to-value ratios (LTV), expanded combined loan-to-value ratios (CLTV), and exclusive product offerings. This chapter describes the loan terms that are available for conventional loans underwritten through DU that are eligible for sale to Fannie Mae.

Current product scope in DU

Conventional mortgages with the following characteristics can be underwritten with the current version of DU:

- first liens
- fixed-rate mortgages
- adjustable-rate mortgages (ARMs)
- mortgages with terms up to 40 years
- interest-only mortgages
- biweekly mortgages
- 7-year balloon mortgages
- mortgages with temporary interest-rate buydowns
- up to four borrowers
- non-occupant co-borrowers
- occupancy types
 - principal residences
 - second homes
 - investment properties
- property types
 - one- to four-unit properties
 - detached and attached homes
 - units in condominium, cooperative, and planned unit development (PUD) projects
 - manufactured homes
- loan purpose
 - purchase
 - refinance (limited cash-out and cash-out)
 - construction (purchase)
 - construction-permanent (refinance)

- special mortgage products
 - Community Lending products, including Fannie Mae’s Community Home Buyer’s Program™, Fannie 97® , Fannie 3/2® , MyCommunityMortgage, and FannieNeighbors®
 - Flexible mortgages, including Flexible 97™, Flexible 100™ , and Flexible mortgages with subordinate financing
 - HomeStyle® Renovation mortgages
 - InterestFirst™ mortgages
 - Negatively amortizing adjustable-rate mortgages

Note: Fannie Mae’s Streamlined Purchase Money Mortgages and Streamlined Refinance Mortgages, as defined in the *Selling Guide*, should be underwritten outside of DU.

FHA and VA loans can be underwritten using DU. Non-conforming conventional loans can be underwritten using other automated underwriting systems, such as GMAC/RFC’s AssetWiseSM, which may be accessible to lenders through DU. For details, contact your Fannie Mae account team.

Information concerning specific underwriting guidelines

40-year term mortgages

Standard 40-year mortgage products can be underwritten with DU. For complete details on 40-year mortgages that can be delivered to Fannie Mae, see *Selling Guide* Announcement 05-04.

Eligible transactions

The following transactions are eligible with 40-year terms:

- Fully amortizing;
- Fixed-rate mortgages or ARM Plans 2236, 3130, 2238, 3557, 2699, 3128, 2704, 3558, 2703, and 3559;
- One- to four-unit properties;
- Principal residence, second home, or investment property;
- Purchase, limited cash-out refinance, cash-out refinance, construction, or construction-permanent transactions.

Ineligible transactions

The following loan characteristics are not eligible with standard 40-year term mortgages:

- Manufactured homes
- Community Lending products
- Flexible mortgages
- HomeStyle™ Renovation mortgages
- InterestFirst™ mortgages
- Bi-weekly mortgages

Mortgage insurance

Standard mortgage insurance applies to mortgages with 40-year terms. The “Reduced MI” and “Lower-Cost MI” options are not available.

Loan-level price adjustment

A price adjustment equal to 0.125% of the loan amount will apply to mortgage-backed security (MBS) loans with 40-year terms. Pricing will be adjusted for whole loan delivery. DU will return a message reminding lenders that a loan-level price adjustment applies.

Maximum allowable loan-to-value (LTV) ratios

The LTV ratios, including the combined LTV (CLTV) and the home equity line of credit (HELOC) CLTV (HCLTV), for 40-year mortgages are the same as those for standard 30-year mortgages.

DU recommendations

Loans with 40-year terms that receive a Refer with Caution recommendation; an EA-I, -II, -III recommendation; or a Refer W Caution/IV recommendation are generally not eligible for delivery to Fannie Mae.

Cooperative share loans

Lenders must have approval in their Master Agreements to deliver cooperative share loans to Fannie Mae. The cooperative project must be reviewed in accordance with the *Selling Guide*, Part XII, Chapter 1, Section 101 to determine if the project meets Fannie Mae’s eligibility requirements. The loan amount, sales price, and appraised value must be submitted to DU *net* of the pro rata share of the project debt that is associated with the individual cooperative share unit.

Manufactured homes

Fannie Mae defines a manufactured home as any dwelling unit built on a permanent chassis and attached to a permanent foundation system. Other factory-built housing (not built on a permanent chassis), such as modular, prefabricated, panelized or sectional housing, is not considered manufactured housing and continues to be eligible for delivery under the guidelines stated in the *Selling Guide*.

Entering property type

The user should determine whether the property is a manufactured home before submitting the loan to DU. If the property is a manufactured home, the user should identify the property type as a manufactured home prior to the initial submission to DU. Any change to the property type will require that the loan be resubmitted to DU, which could result in changes to the underwriting recommendation and the property fieldwork recommendation.

Data entry tip: The manufactured home indicator is in the Subject Property Type field in the Additional Data screen.

Appraisal and property requirements for manufactured homes

Fannie Mae Announcement 03-06 described the guidelines for the selection of appraisers, required appraisal forms [Uniform Residential Appraisal Report \(Form 1004\)](#) and [Manufactured Home Appraisal Addendum \(Form 1004C\)](#), and identification of acceptable sources of manufactured housing data. In addition, the Announcement describes the property eligibility criteria for manufactured homes. Refer to Announcement 03-06 for complete details.

Property fieldwork recommendation

DU requires an appraisal on Form 1004 and the addendum Form 1004C for manufactured homes. In addition, if the manufactured home is located in a PUD, condominium or cooperative project, the lender should select Manufactured Home: Condo/PUD/Co-op as the property type. In those cases, DU will return a message instructing lenders to verify that the loan complies with Fannie Mae's project review requirements.

DU messaging related to property type

When the property type is entered as a manufactured home, DU will return a message acknowledging that the subject property was submitted as a manufactured home. The lender must verify that the property is legally classified as real property and that it meets the manufactured home property guidelines established in Fannie Mae Announcement 03-06.

Furthermore, when a property is not submitted as a manufactured home, DU will check the subject property address against manufactured home property addresses in our database. If our database indicates that the property may be a manufactured home, DU will return a message alerting the user. DU's issuance of this message does not necessarily mean that the property is a manufactured home, nor does the absence of this message indicate that Fannie Mae accepts the accuracy of the property type as it was submitted. The lender must research the subject property type and, if it is determined that the property is a manufactured home, the lender must correct the property type and resubmit the loan to DU.

If the lender determines that the property type is not a manufactured home, the loan may be delivered with the appraisal recommendation provided by DU.

Note: The lender may be required to repurchase a loan that was delivered to Fannie Mae if the property type was not correctly identified as a manufactured home when the loan was underwritten with DU or if the loan was not properly identified with Special Feature Code 235 at the time of delivery.

Eligible loan transactions

Manufactured homes may be financed with fully amortizing fixed-rate mortgages, or 7/1 or 10/1 ARMs, up to a maximum term of 30 years subject to certain limitations. Purchase and limited cash-out refinance transactions up to 95% LTV are permitted on principal residences and up to 90% LTV on second homes. Cash-out refinance transactions up to 65% LTV are permitted only on principal residences where the borrower has owned both the home and the land for at least one year and the loan term does not exceed

20 years. Refer to the [Maximum LTV for Mortgages Secured by Manufactured Homes Chart](#) on page 78.

DU processing

DU applies the manufactured home underwriting, eligibility, and appraisal guidelines when manufactured home is selected as the property type in the loan application. DU assigns a different level of risk to mortgages secured by manufactured homes than it does to mortgages secured by site-built homes.

As outlined in Announcement 03-06, mortgages secured by manufactured homes represent a unique credit risk; therefore, DU assigns a higher level of risk to mortgages secured by manufactured homes than it does to mortgages secured by other types of properties.

Mortgage insurance coverage and loan-level price adjustments

Borrower-paid mortgage insurance premiums can be financed in the principal balance as provided for in Part V, Section 101.03 of the *Selling Guide*.

Financing of any other forms of insurance or other costs is not permitted for purchase money mortgages, but is permitted for limited cash-out refinance transactions, as provided for in Part VII, Chapter 1, Section 103.02 of the *Selling Guide* and Fannie Mae Announcement 03-06.

We require a loan-level price adjustment of .50% for mortgages secured by manufactured homes that are delivered to us for whole loan delivery or MBS issuance.

Refer to the [Mortgage Insurance Coverage Excluding Flexible Mortgages](#) charts beginning on page 84.

Purchase transactions

Purchase money transactions are those in which the proceeds are used to finance the purchase of the manufactured home. Proceeds may also be used to purchase the land, or the land may be previously owned by the borrower, either free of any mortgage or subject to a mortgage that will be paid off with the proceeds of the new purchase money mortgage. The borrower does not receive any money back with a purchase money mortgage. The sales price of the manufactured home may also include bona fide and documented transportation, site preparation, and dwelling installation at the site. The purchase price of any personal property items (non-realty items) in conjunction with the purchase of the manufactured home must be deducted from the sales price and cannot be financed as part of the mortgage.

The lender must calculate and enter the sales price, land value, and appraised value according to the guidelines stated in Announcement 03-06. These guidelines are unique to manufactured home transactions. As such, it is incumbent upon the lender to establish the correct values for the purchase price of the home, the land value, and the appraised value, and to enter the data correctly in the loan application.

For a purchase transaction involving a **newly built** manufactured home that is being attached to a permanent foundation system, the following values must be calculated by the lender and entered in DU:

- In Line a of Section VII, enter the sales price of the manufactured home, and
- In Line c of Section VII, enter the value of the land based on the following:
 - If the borrower purchased the land more than 12 months preceding the loan application date or if the borrower acquired the land at any time as a gift, inheritance, or other non-purchase transaction, the value of the land will be its current appraised value.
 - If the borrower purchased the land 12 or fewer months preceding the loan application, the market value of the land will be the lesser of the lowest sales price at which the land was sold during that 12 months or its current appraised value.

Enter the appraised value based on the “as completed” appraised value of the manufactured home and land.

Data entry tip: For the purchase of a newly built manufactured home, enter the sales price of the home in Line a of Section VII and enter the value of the land (as defined herein) in Line c of Section VII. Enter the “as completed” appraised value in the Additional Data screen.

For a purchase transaction involving a manufactured home that **already exists** on its permanent foundation, the following values must be calculated by the lender and entered in DU:

- In Line a of Section VII, enter the sales price of the manufactured home and land, and
- Enter the appraised value based on the lesser of the following:
 - If the manufactured home was built in the 12 months preceding the loan application date, the lowest price at which the home was previously sold during that 12 month period plus the lower of the current appraised value of the land or the lowest price at which the land was sold during that 12 month period (if there was such a sale), or
 - The current appraised value of the manufactured home and land.

Data entry tip: For the purchase of an existing permanently affixed manufactured home, enter the sales price of the home and the land in Line a in Section VII. Enter the appraised value (as defined herein) in the Additional Data screen.

Limited cash-out refinance transactions

Refinance transactions for manufactured homes may involve the payoff of liens (if the home and land were encumbered by separate liens) or the payoff of a single lien (if the home and land were encumbered by one lien).

The appraised value is used by DU to determine the maximum LTV/CLTV ratios. The lender must calculate the appraised value according to the

guidelines stated in Announcement 03-06. The appraised value is based on when the borrower acquired the home and whether the home and land are secured by separate liens or a single lien. The appraised value may also be based on the lowest sales price of the home in the 12-month period preceding the loan application. The land value is based on when, and under what circumstances, the borrower acquired the land. It is incumbent upon the lender to establish the correct appraised value and to enter the data correctly in the loan application.

Enter the appraised value in DU based on the lower of the following:

- The current appraised value of the manufactured home and land, or
- If the manufactured home was owned by the borrower for less than 12 months on the loan application date and
 - If the home and land are secured by *separate liens*, enter the lowest price at which the home was previously sold during that 12 month period plus the lower of the current appraised value of the land or the lowest sales price at which the land was sold during that 12 month period, or
 - If the home and land are secured by *a single lien*, enter the lowest price at which the home and land were previously sold during that 12-month period.

Data entry tip: For limited cash-out refinances secured by manufactured homes, enter the appraised value (as defined herein) in the Additional Data screen.

Cash-out refinance transactions

The borrower must have owned both the manufactured home and land on which it is permanently affixed for at least 12 months preceding the date of the loan application. The loan term must be less than or equal to 20 years with a maximum LTV/CLTV/HCLTV of 65%.

Enter the current appraised value of the manufactured home and land.

Data entry tip: For cash-out refinances secured by manufactured homes, enter the appraised value in the Additional Data screen.

Ineligible loans

Mortgages secured by manufactured homes that have any of the following characteristics are not eligible for delivery to Fannie Mae and will receive an “Ineligible” recommendation from DU:

- Investment property
- Leasehold estate
- Rent credit (lease-purchase funds)
- Temporary interest-rate buydown
- Flexible mortgage
- HomeStyle Renovation mortgage
- InterstFirst mortgage

- Construction transaction
- Construction-to-permanent transaction
- Refer with Caution recommendation
- EA-III recommendation
- MyCommunityMortgage loan

Note: As noted above, the selection of Construction or Construction-to-permanent will result in an Ineligible recommendation from DU. However, certain types of construction-permanent transactions secured by manufactured homes are acceptable for delivery to Fannie Mae based on the characteristics of the transaction as described below.

A transaction that involves the conversion of interim construction financing to permanent financing is eligible for delivery to Fannie Mae provided the manufactured home (including installation) is 100% complete as evidenced by the appraiser's certificate of completion and provided the LTV is calculated in accordance with the guidelines in Fannie Mae Announcement 03-06.

These transactions should be submitted to DU as either a purchase or a refinance. If the home and land are both encumbered by a lien, or separate liens, that were obtained by the borrower for the purchase and permanent installation of the manufactured home, and the borrower holds title to the lot and wishes to refinance the existing lien(s) into permanent financing, then the loan purpose should be entered as a refinance. On the other hand, if the home is not already "owned" by the borrower (although the land may be), and the subject transaction is for the purpose of obtaining interim financing that will be modified to permanent financing, the loan should be entered as a purchase.

Borrower contributions

The borrower must make a 5% minimum down payment from his or her own funds on a purchase transaction. Additional required down payment funds may come from gifts in accordance with Part X, Chapter 6, Sections 603.06 and 603.07 of the *Selling Guide*. A borrower may also use funds provided by his or her employer as part of an established employer assistance program in accordance with Part X, Chapter 6, Section 603.09 of the *Selling Guide*.

DU does not consider the borrower's liquid funds in determining the borrower's minimum contribution to the transaction. Instead, DU will determine if the borrower is making the required down payment from his or her own funds based on the cash from borrower, cash deposit on sales contract, and borrower paid fees entered in Section VII.

The following data fields are used by DU to calculate the borrower's contribution:

- Cash from the borrower (in Section VII, Line p)
- + Cash deposit on sales contract (in Section VII, "Other Credits")
- + Borrower paid fees (in Section VII, "Other Credits")
- Gift funds (in Section VI A, "Cash-gift")
- = DU's estimate of borrower contributions

If DU determines that the borrower is not contributing 5% from the data fields described above, the loan will receive an "Ineligible" recommendation. DU will return a message stating that, based on the data entered, it appears that the borrower is not contributing the minimum required 5% down payment for this manufactured home transaction.

In addition to the two types of credits identified above (cash deposit on sales contract and borrower paid fees), there are a number of other types of credits that can be entered as "Other Credits" in Section VII. Furthermore, some loan origination systems do not map certain types of credits to DU. For example, a lender may enter "borrower paid fees" in its loan origination system, and that data may transfer to DU as a nonspecific credit type, such as "Other". Because there are a number of nonspecific other types of credits that could be entered, DU does not consider a credit that is entered, or mapped, as nonspecific credit (such as "Other" credit) toward borrower contribution.

If DU is unable to determine that the borrower is contributing the required 5% down payment due to data entry in the nonspecific credit field, the system will return a message stating that DU is not able to determine if the borrower is contributing the minimum required 5% down payment from his or her own funds for this manufactured home transaction. The lender must verify that the borrower is making the required minimum contribution; otherwise the case is not eligible for sale to Fannie Mae.

Trade equity from the borrower's existing manufactured home may be used as part of the borrower's minimum down payment requirement as stated in Announcement 03-06. Information on the existing manufactured home can be entered in the loan application as Pending Sale in Section VI R. DU will apply the standard formula (present market value X 90% less mortgages/liens) to calculate the net equity. To override DU's automatic calculation, enter the amount of net equity in Section VI A. When calculating the market value of the existing manufactured home that is being traded, the lender should do so in accordance with the guidelines stated in Announcement 03-06.

Land equity may be credited toward the borrower's minimum down payment requirement when the borrower holds title to the land on which the manufactured home will be permanently attached as stated in the Announcement. The lender must calculate the land equity according to the instructions in the Announcement and enter the amount of land equity as "Other" in Section VII, under "Other Credits". As stated above, DU does not

consider the nonspecific other credits in determining the borrower's contribution; therefore, if DU is unable to determine that the borrower is contributing the required 5%, DU will return a message advising the lender to verify the 5% borrower contribution.

Manufactured homes and Community Lending products

With the exception of MyCommunityMortgage loans, Community Lending products secured by manufactured homes are eligible subject to the maximum LTV/CLTV/HCLTV ratios, loan terms, and other criteria for mortgages secured by manufactured homes. For example, a 95% Community Home Buyers Program™ mortgage with a loan term of 20 years will be eligible. On the other hand, a Fannie 3/2™ mortgage where the borrower is not contributing 5% from his or her own funds will not be eligible.

DU recommendations

Mortgages secured by manufactured homes are eligible for delivery to Fannie Mae based on the recommendations they receive from DU.

- Loans that receive an “Approve/Eligible” or “Refer/Eligible” recommendation, or for lenders participating in our EA/TPR™ initiative, an “EA-I/Eligible” or “EA-II/Eligible” recommendation, are eligible. The TPR option is available for manufactured home transactions.
- Loans that receive a “Refer with Caution” recommendation, or for lenders participating in our EA/TPR initiative, an “EA-III” or “RWC-IV” recommendation, are not eligible for delivery to Fannie Mae.

Special feature code for a manufactured home

Lenders must use Special Feature Code 235, in addition to all other applicable special feature codes, when delivering mortgages secured by manufactured homes to Fannie Mae. DU returns a message in the Fannie Mae Underwriting Findings (Underwriting Findings) report to remind lenders of the special feature code that is required for mortgages secured by manufactured homes.

Delivery requirements

Refer to Announcement 03-06 for information on the delivery requirements for mortgages secured by manufactured homes.

Investment properties

Reserves

The borrower must have a minimum level of cash reserves for investment properties that will be delivered to Fannie Mae. For one-unit properties, the borrower must have at least two payments (of principal, interest, and escrows) available in reserves. For two- to four-unit properties, the borrower must have at least six payments (of principal, interest, and escrows) available in reserves.

When multiple mortgages made to the same borrower are delivered to us, the borrower's total liquid assets must be sufficient to satisfy the reserve requirement for all of the mortgages. For details, see [Multiple mortgages to the same borrower](#) section, below.

DU will calculate the reserve requirement when the investment property is the subject property.

Data entry tip: When the investment property is the subject property, DU will calculate required reserves. Do not subtract required reserves from liquid assets.

Total expense ratio

For investment property transactions, DU captures data from Section VI L to calculate the total expense ratio. You must ensure that the borrowers' total monthly primary residence housing expense – which includes principal, interest, hazard insurance, real estate taxes, mortgage insurance, and homeowner's association dues – is accounted for in the Liabilities screen.

Management experience and rent loss insurance

Typically, DU will require rental property management experience and rent loss insurance for purchase, construction, and limited cash-out refinance transactions with LTVs greater than 75%, and for cash-out refinances with LTVs greater than 70%. However, DU will waive these requirements, (i.e., DU will not issue the standard rent loss and property management messages) as long as the borrower is qualified with the full principal, interest, taxes, and insurance (PITI) payment on the subject property.

Data entry tip: To receive the management experience and rent loss waiver, the amount entered in the data field for subject net cash flow must be the negative value of the proposed PITI for the subject property. This will ensure that the PITI is included in the total expense ratio calculation. For example, if the total proposed PITI for the subject property is \$975, the subject net cash field must reflect at least -\$975 (negative \$975).

Form 1007, the Single-Family Comparable Rent Schedule, is required only when rental income is used to qualify the borrower.

Multiple mortgages to the same borrower

Second homes and investment properties

If the subject mortgage is secured by a second home or investment property – unless the subject mortgage is a HomeStyle[®] Renovation mortgage – the borrower may not own more than ten properties (including his or her principal residence) that are currently being financed. If the subject mortgage is a HomeStyle Renovation mortgage, the borrower may not own more than four properties (including his or her principal residence) that are currently being financed.

As stated in the *Selling Guide*, our limitation on the number of mortgages being financed applies to the total number of properties financed, not just the

number of mortgages sold to us. Joint ownership in residential real estate is considered the same as total ownership of an individual property. However, ownership in commercial or multifamily (more than four dwelling units) real estate is not included in the limitation. Refer to the *Selling Guide*, Part VII, Chapter 1, Section 101.05 for additional information.

DU will attempt to determine the number of outstanding mortgages (instead of the number of financed properties) for second homes. Real estate owned information can be submitted to DU in a variety of ways (including through various loan origination systems, complete REO data in the Full 1003, and through liability indicators); however, DU determines the number of mortgages and home equity lines of credit (HELOCs) on the credit report or in the liabilities section in the loan application. If DU detects ten or more mortgages, DU will return a specific message to advise you to confirm that the borrower does not own more than ten financed properties.

For all investment properties, regardless of the number of mortgages or HELOCs detected, DU will issue a message reminding you that the loan must comply with our limitation of the number of financed properties. Although DU will attempt to assist you in this calculation, it is the lender's responsibility to ensure that the loan is in compliance with the maximum property limitation.

Regardless of whether DU returns the specific message concerning the ten-property limit, it is the lender's responsibility to ensure that the loan complies with the guidelines. The lender should use special care in calculating the number of financed properties when it submits a number of investment properties (simultaneous loan applications) for the same borrower. For example, if the borrower is purchasing ten investment properties at the same time, DU will only know about the new subject property mortgage and any other mortgages that appear on the borrower's credit report. DU will not be aware that the borrower is purchasing and financing nine additional investment properties.

Number of months reserves

Borrowers who have multiple mortgages secured by investment properties must meet minimum reserve requirements for each investment property that will be delivered to Fannie Mae. This requirement pertains to all purchase and refinance transactions. For each two- to four-unit investment property, the minimum reserve requirement is six months of PITI. For each one-unit investment property underwritten with DU, the minimum reserve requirement is two months PITI payment.

DU will calculate the reserve requirement when the investment property is the subject property. However, for all other investment properties that will be delivered to Fannie Mae, the lender must calculate the reserves required for all investment properties, and subtract the amount of required reserves from the borrower's liquid assets prior to submitting the loan to DU.

Examples of how to calculate the required reserves and how to adjust the borrower's liquid assets are provided below:

Example: The borrowers own four properties: their principal residence, a one-unit investment property, a two-unit investment property, and a second

home. The borrowers are simultaneously refinancing their principal residence and both investment properties.

Before submitting each loan application to DU, the lender must calculate the amount of required reserves and subtract the amount from the borrowers' liquid assets:

- For the transaction involving the principal residence:
 - Calculate two months of the proposed PITI for the one-unit investment property. Subtract this amount from liquid assets;
 - Calculate six months of the proposed PITI for the two-unit investment property. Subtract this amount from liquid assets.
 - Do not calculate reserves for the principal residence.
 - Do not calculate reserves for the second home.
- For the transaction involving the one-unit investment property:
 - Calculate six months of the proposed PITI on the two-unit investment property. Subtract this amount from liquid assets.
 - Do not calculate reserves for the one-unit investment property.
 - Do not calculate reserves for the principal residence.
 - Do not calculate reserves for the second home.
- For the transaction involving the two-unit investment property:
 - Calculate two months of the proposed PITI on the one-unit investment property. Subtract this amount from liquid assets.
 - Do not calculate reserves for the two-unit investment property.
 - Do not calculate reserves for the principal residence.
 - Do not calculate reserves for the second home.

For additional information, see [Investment properties](#) on page 26.

Principal residence properties

Reserves

There are no minimum reserve requirements for principal residences, including owner-occupied multiple unit properties. Lenders are reminded that although we removed the minimum reserve requirements, reserves may be considered a compensating factor in the risk analysis, and may serve to improve the underwriting recommendation.

Non-occupant co-borrowers

A non-occupant transaction is one in which at least one borrower will occupy the property as his or her principal residence and one or more co-borrowers will not occupy the property.

With the exception of Flexible mortgages and Community Lending products, non-occupant co-borrowers are permitted with the same loan terms as those available for owner occupant borrowers. Although the non-occupant co-borrowers' liquid assets are included in the calculation of funds available for closing and reserves, if the LTV (or, if there is subordinate financing, the CLTV) exceeds 80%, the occupant borrowers must have 5% of their own

funds to contribute to the down payment and closing costs (except for mortgages secured by manufactured homes where the borrowers must contribute a minimum 5% from their own funds to the transaction regardless of the LTV/CLTV.) Assets that are jointly owned by the occupant borrowers and non-occupant co-borrowers are included in this 5% calculation provided the funds are entered on the occupying borrowers' loan application. DU will analyze the risk factors in the loan without the benefit of the non-occupant co-borrowers' income or liabilities. DU does not require verification of employment or income for non-occupant co-borrowers.

Note: To ensure that an accurate underwriting recommendation is obtained, non-occupant co-borrowers should be entered on a **separate** loan application instead of entering non-occupant co-borrowers as “co-borrowers” on the same loan application as the occupant borrowers.

Data entry tip: Enter non-occupant co-borrowers on a separate loan application within the same casefile.

Second home properties

Reserves

There are no minimum reserve requirements for second home properties. Lenders are reminded that reserves may be considered a compensating factor in the risk analysis performed by DU, and may serve to improve the underwriting recommendation.

Total expense ratio

For second home transactions, DU captures data from Section VI L to calculate the total expense ratio. You must ensure that the borrowers' total monthly primary residence housing expense – which includes principal, interest, hazard insurance, real estate taxes, mortgage insurance, and homeowner's association dues – is accounted for in the Liabilities screen.

Nonpermanent resident aliens

Nonpermanent resident aliens that are legal residents of the United States are eligible for financing under the same terms – products, transaction type, occupancy status, and LTV – offered to U.S. citizens and permanent resident aliens. Refer to Fannie Mae's *Selling Guide*, Part VII, Chapter 1, Section 101 for additional information.

Mortgage insurance coverage

Many loans that are processed and underwritten through DU have an added benefit of mortgage insurance options. For certain eligible loans, a number of mortgage insurance options are available, including “Reduced MI”, “Lower-Cost MI”, and standard conventional mortgage insurance. To assist lenders in determining the minimum required coverage and the mortgage insurance coverage options that are available for a particular loan, DU will issue a message identifying the mortgage insurance coverage options that are

available. For additional information, refer to the [Mortgage Insurance Coverage and Loan-Level Price Adjustment Requirements](#) charts beginning on page 84.

Note: For loans that receive an Ineligible recommendation, DU will not issue a specific mortgage insurance coverage message. Lenders must refer to the mortgage insurance coverage and loan-level price adjustments chart, or refer to their Master Agreements, to determine the appropriate insurance coverage.

Financed borrower-purchased mortgage insurance

Financed mortgage insurance is permitted for mortgages secured by a one-unit principal residence or second home, for a purchase (including construction if applicable) or a limited cash-out refinance (including construction-permanent if applicable) transaction as provided for in Part V, Chapter 1, Section 101.03 of the *Selling Guide*. Lenders must obtain a Financed Mortgage Insurance Premium Endorsement to the mortgage insurance policy.

The required mortgage insurance coverage, including “Reduced MI” and “Lower-Cost MI” with the associated loan-level price adjustment, is based on the LTV without the financed premium. For example, for an Approve/Eligible 30-year fixed-rate mortgage that has a 90% base LTV, and a total LTV with financed mortgage insurance of 93%, the “Reduced MI” coverage will be 17%, and the “Lower-Cost MI” coverage will be 12% with a loan-level price adjustment of .375%.

All other eligibility and pricing criteria are based on the total LTV with financed mortgage insurance. For example, the maximum eligible LTV for a limited cash-out refinance transaction will be 95%, regardless of whether the loan amount includes financed mortgage insurance. A pricing example is an ARM that has a 90% base LTV and a total LTV with financed mortgage insurance of 93%. The standard price adjustment of .25% for ARMs with LTVs greater than 90% would apply.

Lenders should enter the following data in Section VII: the total mortgage insurance premium in Line g, and the amount of the financed mortgage insurance premium in Line n. The loan amount without the financed mortgage insurance premium should be entered in the total loan amount field in Section I, which in turn will automatically populate Line m in Section VII.

Fannie 97 and all Flexible mortgages are not eligible for financed mortgage insurance.

Special feature code 281 is required for all mortgages with financed mortgage insurance. DU will identify the special feature code in the Underwriting Findings report.

Data entry tip: Enter the total mortgage insurance premium in Line g of Section VII, and enter the amount of premium financed by the borrower in Line n.

Note: If a lender’s Master Agreement has a negotiated variance that allows certain exceptions when underwriting loans with financed single mortgage

insurance premiums, the lender may be able to deliver these “Ineligible” loans if the loans meet the terms of the variance.

Lender-purchased mortgage insurance

Lenders should enter the total mortgage insurance premium in Section VII, Line g, and enter the amount of the lender-purchased mortgage insurance premium in as lender credit. DU will return a message regarding lender credit.

Data entry tip: Enter the total mortgage insurance premium in Line g of Section VII, and enter the amount the lender is purchasing as lender credit.

Special mortgage products

Community Lending products

Prior to submitting a Community Lending loan to DU, the Community Lending data must be entered in the loan application. In the DO/DU user interface, Additional Data screen, select “Yes” in the Community Lending indicator. Next, the Community Lending screen will prompt additional selections, including the metropolitan statistical area or county; product name (Community HomeBuyer’s Program™; Fannie 3/2™; Fannie 97®; MyCommunityMortgage; FannieNeighbors® eligible; Community Seconds); and income limit information.

Data entry tip: The Community Lending loan data must be entered prior to loan submission. On the Additional Data screen, enter “Yes” for Community Lending and follow the prompts.

Borrowers processed under a Community Lending product may be offered the same streamlined documentation requirements as non-Community Lending product borrowers. Furthermore, all of the DU appraisal and inspection forms – Form 2055, Form 2065, Form 2075, and Form 2095 – are available for Community Lending products. Lenders do not need a separate commitment in their Master Agreements to deliver standard Community Lending products underwritten with DU.

With the exception of mortgages secured by manufactured homes, Community Lending loans that receive a Refer with Caution recommendation from DU may be eligible for delivery to Fannie Mae if the lender has a separate commitment in its Master Agreement and the loan meets the Community Lending underwriting terms and conditions established by the lender’s Master Agreement. See Fannie Mae’s *Selling Guide*, Part VIII, Chapters 1 and 5, for additional information about Community Lending products.

Community Lending mortgages secured by manufactured homes

Community Lending loans – except MyCommunityMortgage loans – can be secured by manufactured homes. These loans are subject to the policies described in Announcement 03-06 concerning manufactured homes, notwithstanding any provisions in any Master Agreement, contract, or other

agreement to the contrary. See [Manufactured homes and Community Lending products](#) on page 26 in the Manufactured homes section for more information.

Community Lending income limits and the income limit adjustment factor

Based on the selection of the state, applicable metropolitan statistical area (MSA), or county where the subject property is located, the Department of Housing and Urban Development (HUD) area median income limit will display in the Community Lending screen in the DO/DU user interface.

The income limit adjustment factor is dependent upon the location of the subject property. Typically, the median income field defaults to 100%; however, for certain identified high-cost areas, the income limit adjustment factor will be higher than 100%. Except for FannieNeighbors, DU will compare the borrowers' income to the Community Lending Income Limit data field on the Community Lending screen. If the borrowers' qualifying income exceeds the Community Lending income limit that is in DU, then the loan will be ineligible. Lenders can modify the income limit adjustment factor in the Community Lending screen, but should do so only if the loan is subject to other specified limits pursuant to participation in a mortgage revenue bond program or a federal or state program. Income limits may also be adjusted for certain MyCommunityMortgage loans as described in [Borrower Income Limits](#) in the [MyCommunityMortgage](#) section.

Following is a list of the high-cost areas:

Bergen-Passaic, NJ (MSA)	120%	Nassau-Suffolk, NY (MSA)	165%
Portland, OR (MSA)	120%	Newburgh MSA (Orange County), NY	165%
Seattle, WA (MSA)	120%	New York, NY (MSA)	165%
Newark, NJ (MSA)	125%	Rockland County, NY	165%
Boston, MA (MSA)	135%	Ulster County, NY	165%
California (State)	140%	Westchester County, NY	165%
Dutchess County, NY	165%	Hawaii (State)	170%

Note: The HUD Area Median Incomes can also be found on Fannie Mae's Web site at eFannieMae.com. The income limits used for Community Lending loans are specific to Fannie Mae, and may differ from the median incomes posted on HUD's Web site.

Community Seconds[®] mortgages

When a loan that is subject to a Community Seconds mortgage is underwritten with DU, the lender is not required to obtain approval to originate Community Seconds loans in its Master Agreement. The loan must be a Fannie Mae-approved Community Seconds transaction, or warrantable as such by the lender. The terms of the loan must be documented, and the lender must verify that the loan and borrower meet all of the product requirements, including those pertaining to maximum income limits, loan repayment terms, and homebuyer education. Further, the Community

Seconds mortgage must provide for guidelines that describe how the second mortgage lien is to be handled if the borrower experiences a catastrophic event that results in the borrower's having to sell the property.

If a monthly payment is associated with the Community Seconds mortgage, it should be included in the Section V data field for the proposed other financing (P&I) for inclusion in the total debt-to-income ratio calculation. The balance of the Community Seconds mortgage must be entered for inclusion in the CLTV.

The Community Seconds indicator is in the Community Lending screen and should be selected only when the subject transaction is a Community Lending product. When the loan is identified as having a Community Seconds mortgage, DU will issue verification messages for the lender to confirm the eligibility of the loan according to Community Seconds guidelines.

The lender must identify the mortgage (including Flexible mortgages and HomeStyle Renovation mortgages) as having a Community Seconds mortgage by using Special Feature Code 118 when delivering any mortgage that has a Community Seconds loan.

Data entry tip: Community Seconds indicator should only be used when the subject first mortgage is a Community Lending product.

FannieNeighbors[®]

A loan is eligible as a FannieNeighbors loan if the subject property is located in an eligible low- or moderate-income area or qualified census tract. Lenders must confirm outside of DU that the property is located in a FannieNeighbors-eligible area; they can do so by contacting their lead Fannie Mae regional office or by visiting our Web site.

Lenders may also use the Fannie Mae Property GeoCoder[™], a free, online application, to determine whether a property qualifies for the FannieNeighbors option. The Fannie Mae Property GeoCoder is accessible on our Web site.

The Community Lending income limits do not apply to FannieNeighbors.

Data entry tip: Because some third-party loan origination systems do not capture Community Lending information, (e.g., FannieNeighbors), you may need to access the Community Lending screen directly from the Additional Data screen in the DO/DU user interface.

MyCommunityMortgage

MyCommunityMortgage is a suite of Community Lending product options offered by Fannie Mae that can increase the likelihood of homeownership for low- and moderate-income borrowers. In DU, several MyCommunityMortgage products (including Community 97[™], Community 100[™], Community 100 Plus[™], Community Solutions[™], Enhanced Community[™] 2-4 Family, and Community Renovation[™] 1- to 4-Family) are compiled into a single product selection, MyCommunityMortgage, in the online loan application. When MyCommunityMortgage is selected, DU will automatically apply appropriate product guidelines based on the loan characteristics.

All lenders must complete the required approval process, which includes obtaining the MyCommunityMortgage Terms and Conditions in their Master Agreements (Terms and Conditions), and registration process. Lenders must be “activated” in DU before they can successfully submit MyCommunityMortgage loans. Lenders must also obtain separate approval to deliver certain MyCommunityMortgage products, such as Community Renovation loans. For details, please contact your Fannie Mae Contact Team.

Borrower income limits for MyCommunityMortgage: The borrower’s income may not exceed 100% of the median income that the Department of Housing and Urban Development (HUD) publishes for the property’s location, except for (i) higher income limits allowed for certain high-cost areas as specified in the Fannie Mae *Selling Guide* (Selling Guide), (ii) an income limit of 115% of the HUD-published median in nonmetropolitan counties, (iii) an income limit of 115% of the HUD-published median for loans under Community HomeChoice™, and (iv) borrower incomes imposed by other organizations (such as when a housing finance agency or an employer provides down payment or closing costs assistance) as specified in the *Selling Guide*.

DU automatically applies the 100% income limit for Community Lending products, except when the property is located in certain identified high-cost areas, in which case DU automatically applies the higher income limit factor. However, the lender should enter the appropriate limit (115% for those properties located in nonmetropolitan areas and for Community HomeChoice loans, and the appropriate limit imposed by other organizations) in the Community Lending Income Limit data field in the Community Lending screen.

As a reminder, there are no income limits when the subject property is located in a designated FannieNeighbors™ area.

The following underwriting guidelines apply to MyCommunityMortgage loans underwritten in DU. For manually underwritten loans, refer to the lender’s Terms and Conditions.

- **Eligible transactions**
MyCommunityMortgage is available for a purchase or limited cash-out refinance transaction.
- **Eligible mortgages**
The mortgage must be a conventional fixed-rate, fully amortizing loan with a term of 30 years or less, or – *for one- to two-unit properties* – a 5/1, 7/1, or 10/1 ARM (Fannie Mae Plan 659, 660, 661, 2724, 2725, 750, 751, 1423, 1437, 2726, 2727, 2728, or 2729). Three- to four unit properties are ineligible for ARMs.
Note: For ARM plans that are not listed on the user interface, the lender must select the appropriate generic ARM plan to submit the loan to DU; however, the lender must use the Fannie Mae ARM plan number when delivering the loan.
- **Eligible property types:** One-unit properties, including single units located in condominium or planned unit development (PUD) projects,

and two- to four-unit properties are eligible. Cooperative share units are eligible only with manual underwriting. Manufactured homes are not eligible with MyCommunityMortgage loans.

- **Contributions – minimum required from borrower:** The minimum contribution is based on the number of units and must come from the borrowers’ own funds:
 - One-unit properties require a minimum contribution of \$500.
 - Two-unit properties require a minimum contribution of 3% of the property’s sales price.
 - Three- to four-unit properties require a minimum contribution of 3% of the property’s sales price. Exception: Three- to four-unit properties that secure Community Renovation loans require a minimum contribution of 5% of the property’s sales price.

For limited cash-out refinance transactions, the borrower is not required to make a minimum contribution.

- **Minimum reserves:** There is no minimum reserve requirement for MyCommunityMortgage loans; however, as with all loans, DU will consider the amount of reserves, if any, in the overall risk of the loan. If reserves are entered in the DU loan application, DU may return a message to verify the reserves, in which case lenders must comply with the DU verification message.
- **MyCommunityMortgage LTV and CLTV limits:** There are maximum LTV and CLTV ratios, as well as minimum CLTV ratios, for MyCommunityMortgage loans. See the [Minimum and Maximum LTV/CLTV Chart for MyCommunityMortgage Loans](#) on page 80.
- **Subordinate financing:** Community Seconds mortgages, which are described above, and certain non-Community Seconds are permitted in conjunction with one- to four-unit properties secured by MyCommunityMortgage loans with the exception of Community Renovation loans. Home equity lines of credit and seller-carried seconds are not permitted.

For details on MyCommunityMortgage loans with subordinate financing, refer to the lender’s Terms and Conditions.

- **Mortgage insurance coverage:** Fannie Mae requires significantly less mortgage insurance coverage for MyCommunityMortgage loans than what is required for other mortgage products. The minimum required mortgage insurance coverage for MyCommunityMortgage loans is listed below:

LTV Ratios	MI Coverage
> 80% <=85%	6%
> 85% <= 90%	12%
> 90% <= 95%	16%

LTV Ratios	MI Coverage
> 95% <= 97%	18%
> 97% <= 100%	20%

MyCommunityMortgage loans are not eligible for the “Reduced MI” and “Lower-Cost MI” coverage options.

Borrower-paid mortgage insurance premiums can be financed in the principal balance with a maximum LTV of 100% *including the financed mortgage insurance* for certain MyCommunityMortgage loans.

When the principal balance includes financed mortgage insurance and the maximum LTV (including financed mortgage insurance) is greater than 95% and less than or equal to 100%, the following guidelines apply:

- The property must be one-unit.
- Loans that receive an EA recommendation are not eligible for financed mortgage insurance.
- Community Renovation mortgages are limited to 95% LTV.
- Lenders must use Special Feature Code 574 at delivery.

Note: In financing mortgage insurance, the maximum LTV including any financed mortgage insurance premium is 100%. Within this LTV limit, borrowers may finance the mortgage insurance premium in whole or in part up to 100% LTV. These financing options may not be available through all mortgage insurance companies. Check with your mortgage insurance provider for details.

For additional information on financed mortgage insurance, see the *Selling Guide*, Part V, Chapter 1, Section 101.

- **Loan-level price adjustment:** Typically, Community Lending loans are not subject to loan-level price adjustments. However, the following loan characteristics are subject to loan-level price adjustments over the base MyCommunityMortgage pricing:
 - 5/1 ARMs with an LTV greater than 90% are subject to a loan-level price adjustment of 0.25%; and
 - Loans with a non-Community Seconds subordinate lien are subject to a loan-level price adjustment of 0.50%.
- **DU recommendations:** MyCommunityMortgage loans are eligible for delivery to Fannie Mae based on the DU recommendations.
 - Loans that receive an Approve/Eligible recommendation are eligible for delivery to Fannie Mae provided the lender has the requisite approval to deliver MyCommunityMortgage loans as stated earlier. Loans receiving Approve/Eligible recommendation are eligible for the limited waiver of representations and warranties.
 - Loans that receive a Refer/Eligible recommendation may be eligible for delivery. The lender must comply with our existing policies when underwriting loans with Refer/Eligible recommendations.

- Loans that receive a Refer with Caution recommendation are generally not eligible for delivery. Lenders may manually underwrite these loans according to their Terms and Conditions.
- Loans that receive an EA-I/ or -II/Eligible recommendation are eligible for delivery except when the loan is subject to borrower-financed mortgage insurance.
- Loans that receive an EA-III or Refer W Caution/IV are generally not eligible for delivery. (However, lenders may manually underwrite these loans according to their Terms and Conditions.)

As a reminder, the guidelines for TPR (including the TPR feature), the EA/TPR special feature codes and loan-level price adjustments do not apply to loans delivered as MyCommunityMortgage loans.

Note: If a loan is not eligible as a MyCommunityMortgage loan in DU, and the loan does not comply with the lender’s Terms and Conditions for MyCommunityMortgage, the lender has the option of removing the MyCommunityMortgage selection and resubmitting the loan to DU.

- **Special feature codes:** When delivering loans to Fannie Mae, lenders must use the applicable special feature codes for MyCommunityMortgage loans in addition to all other applicable special feature codes, such as the codes used for DU-underwritten loans. DU will return a message in the Underwriting Findings report to remind lenders of the required special feature codes. As noted above, Special Feature Code 574 applies to certain mortgages with financed mortgage insurance. Additional special feature codes for MyCommunityMortgage loans underwritten with DU are listed below:

LTV Special Feature Codes	
1-unit property	2- to 4-unit property
LTV ≤ 97% = SFC 460 LTV > 97 and ≤ 100 = SFC 480	LTV ≤ 97% = SFC 519

Community Renovation Special Feature Codes		
1-unit property	2-unit property	3- to 4-unit property
215 and 519	215 and 519	215 and 519

- **Ineligible loans:** Loans with the following characteristics are not eligible for MyCommunityMortgage in DU and must be manually underwritten based on the lender’s Terms and Conditions.
 - CLTV below 95% (90% for 3- to 4-unit Community Renovation loans)
 - Temporary interest-rate buydowns
 - Non-occupant co-borrowers
 - Cooperative share units
 - Borrowers with exclusively nontraditional credit histories

The following transactions are not eligible in conjunction with any MyCommunityMortgage loans:

- Second home transactions
 - Investor transactions
 - Manufactured homes
 - Cash-out refinance transactions
- **Specific MyCommunityMortgage product features:** Below is a list of various MyCommunityMortgage products and how their manual underwriting guidelines apply to loans underwritten with DU. You will find that many of the manual underwriting flexibilities are already offered for all DU-processed loans.
 - **Community Solutions™:** Many of the underwriting flexibilities that are currently offered under the Community Solutions product for borrowers in certain professions (e.g., teachers, firefighters) are already available to all borrowers in DU. On the other hand, temporary buydowns and gifted reserves are not eligible for loans underwritten with DU because the benefits of these features, namely the higher maximum expense ratio and no reserve requirement, are already considered by DU.
 - **Community HomeChoice™:** Community HomeChoice offers expanded underwriting flexibilities to persons defined as handicapped under the federal Fair Housing Amendments Act. Lenders must refer to their Terms and Conditions for detailed information. Many of the underwriting flexibilities that are currently offered under the Community HomeChoice product are available to all borrowers in DU. As a result, lenders may not need to apply the Community HomeChoice flexibilities to loans underwritten with DU. If the loan received an Approve/, EA-I/, EA-II/, or Refer/ Eligible recommendation from DU, the mortgage is eligible for delivery as a non-HomeChoice product.

One of the flexibilities of the Community HomeChoice product is that it allows non-occupant co-borrowers. Because loans with non-occupant co-borrowers are not eligible for delivery as Community Lending loans except under the Community HomeChoice option, DU returns an Ineligible recommendation for these loans. To remind lenders that these loans may be eligible under the Community HomeChoice product guidelines, DU will also return a message that the loan may be delivered according to the lender's Terms and Conditions. If a loan with an Approve, EA-I, or EA-II recommendation is ineligible, and non-occupancy is the only reason given for ineligibility, the loan will be eligible for the limited waiver of representations and warranties provided that the loan complies with all applicable Community HomeChoice requirements.

Note: For HomeChoice loans, the borrower income limit is 115% of the HUD area median income. As stated above, lenders may adjust the income factor in the Community Lending screen when applicable.

- **Energy Efficient Mortgage (EEM):** The EEM option for MyCommunityMortgage loans allows the amount of energy savings to be applied toward qualifying income based on the guidelines in the lender’s Terms and Conditions. The monthly energy savings should be entered as “Other Income” in Section V, Other Income. The energy savings value must be added to the appraised value. Refer to the Terms and Conditions for more specific guidelines, data entry instructions, and documentation requirements.

Note: EEM may also be available on a negotiated basis for loans other than MyCommunityMortgage. In such cases, the lender must determine outside of DU whether the loan complies with the requirements according to the lender’s contract.

- **Boarder income:** Part X, Section 402.22 (“Boarder Income Guidelines”) of the *Selling Guide* describes Fannie Mae’s guidelines for consideration of rental income from a live-in aid or a relative living with the borrower. For MyCommunityMortgage loans, the renter is not required to be a live-in aid or a relative. Enter this income as “Boarder Income” (if the Boarder Income selection is not available in your loan origination system, use “Other Income”) in Section V, Other Income.
- **Section 8 for Homeownership:** Monthly Section 8 vouchers for housing assistance can be used as income to qualify the borrower. See the Terms and Conditions for details. Enter Section 8 income as “Other Income” in Section V.
- **Community Renovation™:** Community Renovation is eligible in conjunction with 1- to 4-unit properties. Lenders must obtain special approval in their Terms and Conditions to deliver these loans to Fannie Mae. The total cost of the home improvements must be entered in Section VII, Line b. The maximum allowable cost of improvements is 50% of the “as-completed” value of the subject property.

For purchase transactions, the Appraised Value amount entered in DU should be the “as-completed” value. For refinance transactions, the Appraised Value entered in DU should be the lesser of the “as-completed” appraised value of the property or the sum of the unpaid principal balances of all outstanding liens and the total renovation costs. Refer to the Terms and Condition for details.

Borrower-paid mortgage insurance premiums can be financed in the principal balance with a maximum LTV of 95%. With the exception of the maximum LTV, all other MyCommunityMortgage guidelines for financed mortgage insurance apply.

- **Smart Commute®:** The Smart Commute feature is available for MyCommunityMortgage loans; however, lenders must apply the Smart Commute guidelines outside of DU to ensure that the loan complies with all applicable guidelines.
- **Homebuyer education, landlord counseling, and quality control/delinquency counseling:** Lenders must follow the provisions detailed

in the Fannie Mae *Servicing Guide* and *Selling Guide*, and their Terms and Conditions, as applicable.

- **Cash-on-Hand:** Borrowers who meet the underwriting criteria listed below may be able to use cash-on-hand for the down payment and closing costs on MyCommunityMortgage loans when purchasing their one-unit, principal residence.

The cash-on-hand policy does not apply to Community Renovation loans.

The lender must verify and document that the following underwriting requirements are met:

- The borrower customarily uses cash for expenses and that usage and reasonableness of using cash, as well as the amount of funds saved, are consistent with the borrower's previous payment practices. An example for determining the reasonableness of the amount of funds saved would be through the use of an income and expense budget.
- The borrower's credit report and other verifications indicate limited use of credit, and no depository relationship exists between the borrower and a financial institution.
- The borrower must provide a written and signed statement that discloses the source of funds and states that the funds have not been borrowed.
- The borrower must deposit with a financial institution funds sufficient for the down payment and closing costs at the time of loan application or no less than 30 days prior to closing.
- Data must be entered correctly prior to submitting the loan to DU.

The lender must ensure that the amount of cash-on-hand is entered as "Cash on Hand" in the Assets section (Section VI) of the online loan application.

If a third party loan origination system is used where "Cash on Hand" is not an available asset type, or where the asset type does not correctly transmit to DU, the user must access the DO/DU online loan application and enter the amount in the Assets section as "Cash on Hand".

When "Cash on Hand" is selected, DU will return a message specific to the cash-on-hand guidelines.

DU will use the "Cash on Hand" amount to calculate the available funds to close. However, cash-on-hand funds will not be used to calculate reserves. For example, if a borrower needs \$2,000 to close and the amount of cash-on-hand is \$3,000, DU would count the cash-on-hand as sufficient funds to close; however, DU would not apply the remaining \$1,000 toward reserves.

Energy Efficient Mortgages

Lenders that are approved to deliver Energy Efficient Mortgages (EEM) to Fannie Mae may underwrite these loans with DU; however, lenders must refer to their EEM Terms and Conditions for specific loan submission instructions and delivery guidelines.

Flexible mortgages

The Flexible mortgage products (Flexible 97[®] and Flexible 100[™]) and Flexible mortgages with subordinate financing, are designed for borrowers who have, or choose to use, minimal funds for the down payment or closing costs for the purchase or limited cash-out refinance of their principal residences.

Flexible mortgages must be underwritten through DU, and are available nationwide to all lenders that use DU through both their retail and wholesale channels of business, if applicable. Lenders are not required to obtain approval in their Master Agreement to originate and sell Flexible mortgages underwritten through DU.

Flexible mortgages are available with terms from 15 to 30 years; however, all Flexible mortgages with terms less than 30 years will be underwritten the same as 30-year loans. DU will not consider the shorter amortization term as a compensating factor in the risk analysis. Additionally, the mortgage insurance and loan-level price adjustment options will be the same without regard to the amortization term.

ARM plans available with Flexible mortgages

Flexible mortgages are available with certain 5/1, 7/1, and 10/1 ARM plans. The following ARM plans may be delivered as Flexible mortgages:

- 5/1 ARM plans 659, 660, 661, 2724, 2725, and 3252. Lenders should use the “FM GENERIC, 5 YR” plan to underwrite Plans 659, 2724, and 2725.
- 7/1 ARM plans 750, 751, 2726, and 2727. Lenders should use the “FM GENERIC, 7 YR” plan to underwrite Plans 2726 and 2727.
- 10/1 ARM plans 1423, 1437, 2728, and 2729. Lenders should use the “FM GENERIC, 10 YR” plan to underwrite Plans 2728 and 2729.

Flexible mortgage products and features

The Flexible mortgage product line and features are defined below:

- **Flexible 97 mortgages:** Flexible mortgages with an LTV > 95% and ≤ 97% – regardless of whether the loan has subordinate financing.

This category also includes the expanded down payment flexibility for purchase transactions with LTVs of 90 – 95% where the borrower does not have 5% of his or her own funds. Additionally, if subordinate financing exists, the CLTV must be ≤ 97% for the transaction to be considered a Flexible 97 loan.

- **Flexible 100 mortgages:** Flexible mortgages with an LTV > 97% and ≤ 100% – regardless of whether the loan has subordinate financing.
- **Flexible mortgages with subordinate financing:** Flexible mortgages where the LTV is ≤ 95% **and** the CLTV is > 95%.

DU will automatically apply the underwriting guidelines for Flexible mortgages to loans with certain LTVs and CLTVs that have the following characteristics:

- LTV greater than 95 up to 100%;
LTV between 90 and 95% where the borrowers lack 5% of their own funds (purchase transaction only);
- CLTV greater than 95 up to 105%;
- principal residence of all borrowers;
- loan purpose is purchase or limited cash-out refinance;
- fully amortizing fixed-rate mortgage, 5/1, 7/1, or 10/1 ARM;
- one-unit property (excluding units in cooperative projects);
- the loan is not a Community Lending product, HomeStyle Renovation mortgage, construction, or construction-permanent transaction; and
- the property type is not a manufactured home

Flexible mortgages with subordinate financing

As stated above, subordinate financing (excluding home equity lines of credit and seller-carried second mortgages) is permitted with Flexible mortgages. If the CLTV exceeds 100%, the subordinate financing must be a Community Seconds loan and the lender must identify the loan as having a Community Seconds subordinate lien by using Special Feature Code 118 upon delivery to Fannie Mae. See [Community Seconds mortgages](#) above for more information.

All subordinate liens, including Community Seconds loans, must be entered in the loan application.

Note: When the CLTV exceeds 100%, DU will look for the existence of a new subordinate lien or an existing subordinate lien that will be resubordinated and will issue verification messages for the lender to confirm the eligibility of the loan according to Community Seconds guidelines.

Data entry tip: Do not use the Community Seconds indicator in the Community Lending screen when the Community Seconds is subject to a Flexible mortgage.

All subordinate liens must be closed-end mortgages. Fannie Mae does not currently purchase the subordinate lien associated with a Flexible mortgage.

Flexible mortgage LTV and CLTV limits

The maximum LTV for a Flexible mortgage is 100%. The maximum CLTV is 105%. (If the CLTV exceeds 100% on a Flexible mortgage, the

subordinate financing must be a Community Seconds loan.) See the [Maximum LTV Chart for Flexible Mortgages](#) on page 81.

Expanded down payment flexibility for loans with lower LTVs

Flexible mortgage guidelines are also applied to purchase transactions with LTVs of 90 – 95% if the borrower does not have 5% of his or her own funds to contribute to the transaction (as required under our standard mortgage guidelines) and the 5 – 10% down payment comes from acceptable Flexible sources of funds, such as a gift. With the exception of temporary buydowns, this Flexible transaction is treated the same as a Flexible 97% mortgage. For example, mortgage insurance coverage, price adjustment options, and special feature codes are the same for this transaction as they are for a Flexible 97 mortgage. For these transactions with a temporary buydown, the loan is qualified at the bought-down rate plus 1%, whereas a 97% Flexible mortgage with a temporary buydown is qualified at the note rate.

DU will also apply the Flexible mortgage guidelines to loans submitted when the field for unsecured borrowed funds is selected as a source of down payment in Section II, regardless of whether the borrower has 5% of his or her own funds.

Data entry tip: When unsecured borrowed funds is selected as a source of down payment, DU will apply Flexible mortgage underwriting guidelines regardless of whether the borrower has 5% of his or her own funds.

The typical transaction that is eligible for the expanded Flexible 97 mortgage guidelines is one in which the borrower receives a 10% gift and obtains a 90% loan. For this loan to be considered a Flexible mortgage the borrowers cannot have 5% of their own funds in liquid assets. If the borrower *does* have 5% in liquid assets, the loan could meet Fannie Mae's standard eligibility requirements and, as such, is not eligible for delivery as a Flexible mortgage.

If the borrower is receiving a gift under these expanded guidelines, the actual dollar amount of the gift must be reflected in DU. Without entry of the gift amount, DU is unable to determine if the borrower has 5% to contribute to the transaction; thus the Flexible mortgage underwriting guidelines will not be applied.

Data entry tip: When entering gift funds for a Flexible mortgage with an expanded down payment, enter the actual dollar amount of the gift as an asset.

The following charts provide examples of LTV and CLTV ratios where DU will apply the Flexible mortgage guidelines, the applicable Flexible mortgage product feature, and examples of loans where DU will not apply Flexible mortgage guidelines.

Examples of Flexible mortgages without subordinate financing

LTV	Flexible Mortgage?
> 97 – ≤ 100%	Yes, Flexible 100
> 95 – ≤ 97%	Yes, Flexible 97
≥ 90 – ≤ 95% (and borrower lacks 5% own funds)	Yes, Flexible 97
< 90% (and borrower lacks 5% own funds)	No

Examples of Flexible mortgages with subordinate financing

LTV	CLTV	Is this a Flexible mortgage?
> 97 – ≤ 100%	> 97 – ≤ 105%	Yes, Flexible 100
> 95 – ≤ 97%	> 95 – ≤ 105%	Yes, Flexible 97
≤ 95%	> 95 – ≤ 105% (such as 80/20; 80/20/5)	Yes, Flexible mortgage w/Subordinate Financing
97%	100	Yes, Flexible 97
≥ 90 – ≤ 95% and borrower lacks 5% own funds	≤ 95% (such as 90/5)	Yes, Flexible 97
< 90% and borrower lacks 5% own funds	≤ 95% (such as 80/10)	No

Contributions – minimum required from borrower

For purchase transactions, the borrower must make a minimum contribution to the transaction. A borrower who obtains a Flexible 97 mortgage must make a minimum 3% down payment, all of which can come from approved Flexible sources. A borrower who obtains a Flexible 100 mortgage or a Flexible mortgage (other than a Flexible 97) with a CLTV ≥ 100% does not have to make a down payment; however, he or she must make a minimum contribution toward the payment of closing costs and prepaid fees.

Borrowers have the option of either making a minimum contribution of 3% of the sales price from approved Flexible sources or making a minimum contribution of \$500 from their own funds.

Note: Flexible 97 mortgages are not eligible for the \$500 contribution feature.

If the minimum \$500 contribution feature is used, interested-party contributions, subject to standard contribution limits, and premium pricing can be applied to any amount above the borrower’s initial \$500 contribution. Flexible mortgage underwriting and eligibility guidelines, including LTV/CLTV ratios (such as 80/20), mortgage insurance coverage, loan-level price adjustments, and loan delivery, apply equally without regard to the minimum contribution.

For limited cash-out refinance transactions, the borrower does not need to make a minimum contribution; however, the borrower must use approved

Flexible sources of funds to cover all or a portion of the closing costs and prepaid fees.

Identifying Flexible mortgages with the \$500 contribution feature

It is important to properly identify Flexible 100 mortgages and Flexible mortgages with subordinate financing where the borrower has used the \$500 contribution feature. Lenders must use Special Feature Code 564, together with any other applicable Flexible mortgage special feature codes, when delivering these loans to Fannie Mae. This applies to all Flexible 100 mortgages and Flexible mortgages with subordinate financing where the borrower contribution is at least \$500 from their own funds but less than 3% (of the sales price) total contribution including approved Flexible sources. Special Feature Code 564 is required for all recommendations, including EA recommendations. Special Feature Code 564 must be reported in addition to the applicable Flexible and EA special feature codes. Special Feature Code 564 must not be used for Flexible mortgages with the 3% borrower contribution. As a reminder, all appropriate special feature codes must be reported at delivery in order for the loan to be eligible for the limited waiver of representations and warranties.

DU will monitor the performance of mortgages with the \$500 contribution feature based primarily on information entered in Section VII, specifically in Line L, Other Credits. DU relies on the data provided in this section to calculate the amount of borrower and seller contributions, and to evaluate the types of credits the borrower will receive at closing. It is extremely important to submit accurate data on other credits to DU. If you use a loan origination system, make sure all data in Section VII, Other Credits, is mapped correctly to DU.

Sources of funds for the down payment, closing costs, and prepaids

With the Flexible mortgage product, borrowers are not required to have a minimum investment from their own funds in the transaction, as is required for all other Fannie Mae transactions. The borrower is permitted to obtain funds for the down payment, closing costs, and prepaids from sources that are allowed only with a Flexible mortgage. While the down payment may not come from an interested party to the transaction (nor can a donor obtain the funds from an interested party to the transaction to give to the borrower), it is permissible for an interested party to fund all or part of the borrower's closing costs – subject to the applicable interested party contribution limits – after the borrower's minimum contribution has been met. In addition to the borrower's own funds, the following sources of funds are permitted:

- **Gifts or grants:** Borrowers can obtain a gift from a relative, domestic partner, fiancée, or fiancé, or can receive a grant from an employer, public agency, or nonprofit organization to assist them with any or all of the down payment and closing costs (including prepaid fees). To be considered in the borrower's liquid assets, the gift or grant must be recognized in DU as a gift in Section VI A. Gifts and grants must be

provided with no repayment required or expected. Gifts of equity are not permitted.

Note: The Underwriting Findings report will include gift messages that are unique to Flexible mortgages when a gift is entered as either a source of down payment (in Full 1003, Section II) or entered as an asset. For Flexible mortgages, the standard gift documentation is required, including a signed gift letter, as described in Fannie Mae's *Selling Guide*, Part X, Chapter 6, Section 603.

Data entry tip: Enter gifts and grants as a gift in Section VI A.

- **Unsecured loan from relative, domestic partner, fiancée, or fiancé:** Borrowers can obtain an unsecured loan from a relative, domestic partner, fiancée, or fiancé to assist them with any or all of the down payment, closing costs, and prepaids. The unsecured loan must be a fixed-rate loan, generally at an interest rate that does not exceed the note rate of the mortgage. (Up to 2 percentage points above the note rate is permitted.) The unsecured loan can provide for a balloon payment, however not within the first five years of the loan. The borrower must provide a document that is signed by the donor that identifies the donor's name, address, relationship to the borrower, and the terms of the loan. Evidence of the transfer of funds to the borrower is also required. The donor cannot be an interested party to the transaction, nor can the donor obtain the funds to lend to the borrower from an interested party to the transaction. The unsecured loan must be entered in DU as a gift either in Section II or as a gift in Section VI A. It must also be entered in Section VI L, and the payment must be included in the total expense ratio calculation. The borrower must disclose the unsecured loan by answering "yes" to question h in Section VIII.

Note: The Underwriting Findings report will include gift messages that are unique to Flexible mortgages when a gift is entered as either a source of down payment or as an asset.

Data entry tip: Unsecured loans from a relative, domestic partner, fiancée, or fiancé should be entered in Section VI A as a gift. Also enter the loan, including the monthly payment, in Section VI L as an installment debt.

- **Unsecured loans from employers or nonprofit organizations:** Borrowers can obtain an unsecured loan from an employer, public agency, or nonprofit organization (not including credit unions) to assist with the down payment, closing costs, and prepaids. The terms and conditions of the loan must be documented with a copy of an award letter or legal agreement from the provider. Evidence of the transfer of the funds must also be provided – such as a copy of the donor's check and evidence of deposit or a HUD-1 Settlement Statement. The unsecured loan must be a fixed-rate loan, generally at an interest rate that does not exceed the note rate of the mortgage. (Up to 2 percentage points above the note rate is permitted.) The unsecured loan can provide for a balloon payment, however, not within the first five years of the loan. The amount of the unsecured loan should be entered in Section VII, under

other credits as follows: for loans from employers, enter as employer assisted housing; for loans from nonprofit organizations, select other. A corresponding liability should be entered in Section VI L, and the payment should be included in the total expense ratio calculation. The borrower should also disclose the loan by answering “yes” to question h in Section VIII.

Data entry tips:

- Unsecured loans from employers should be entered as employee assisted housing under other credits in Section VII. (The DO/DU user interface will automatically populate Line l from other credits.) Enter the loan and the monthly payment in Section VI L. Select “yes” to question h in Section VIII.
- Unsecured loans from non-profit organizations should be entered as other under other credits in Section VII. (The DO/DU user interface will automatically populate Line l from other credits.) Enter the loan and the monthly payment in Section VI L. Select “yes” to question h in Section VIII.
- **Secured borrowed funds:** Borrowers can borrow against an asset, such as a life insurance policy or 401(k) account, and the secured loan does not have to be entered in Section VI L as a liability, provided the appropriate documentation is obtained. Refer to the *Selling Guide*, Part X, Chapter 6, Section 603. The amount of the secured loan should be entered as secured borrowed funds in Section VI A. The loan amount should be subtracted from the value of the asset, and the net asset value should be entered in Section VI A in the appropriate field. For example, if the borrower has a vested value of \$30,000 in his or her 401(k) account (less any taxes or penalties) and borrows \$10,000 against the 401(k), the amount entered as secured borrowed funds would be \$10,000. The amount entered as retirement funds would be \$20,000. The borrower should also disclose the loan by answering “yes” to question h in Section VIII.
- **Community Seconds:** Community Seconds can be subordinated to Flexible mortgages. If the CLTV exceeds 100%, the subordinate financing must be a Community Seconds loan and the lender must identify the loan as having a Community Seconds subordinate lien by using Special Feature Code 118 upon delivery to Fannie Mae. See [Community Seconds mortgages](#) above for more information.

Sources of funds for the closing costs and prepaids

Interested-party contributions up to 3% of the property’s sales price and premium pricing are permitted to be used to cover closing costs above the borrower’s minimum contribution. Loans with interested-party contributions and premium pricing must comply with Fannie Mae guidelines described in the *Selling Guide*, Part VII, Chapter 1, Section 113 and Part X, Chapter 6, Section 602.

- **Interested-party contributions:** Any closing costs that are normally paid by the property purchaser are considered contributions if they are

paid by an interested party to the transaction, such as the property seller, builder, developer, real estate agent, real estate broker, or any of the interested party's affiliates. The standard interested-party contribution limits – 9%, 6%, or 3% – are based on the CLTV. Interested parties may contribute up to the maximum allowable limit to fund the closing costs and prepaids.

- **Premium pricing:** The borrower can fund the closing costs and prepaids through the lender by paying a higher interest rate on the loan as long as the increase in the mortgage interest rate does not equate to more than 3% of the property's sale price.

Note: Generally, the total amount of funds the borrower receives from outside sources is limited to the amount of the down payment, closing costs, and prepaid fees. For example, if the down payment, closing costs, and prepaid fees equal \$5,000, and the borrower is obtaining a \$3,000 gift, the maximum amount of contributions is \$2,000.

Delivery requirements for loans with interested-party contributions

Flexible mortgages, including loans with LTVs up to 100% that have interested party contributions up to 3% of the sales price, are eligible for whole loan delivery or MBS delivery.

Example: The borrower applies for a 100% LTV first mortgage. Closing costs and prepaid fees total 4% of the sales price. The borrower obtains a gift for 3%, and the seller contributes 1% toward closing costs. This loan is eligible for whole loan delivery or MBS delivery.

Mortgage insurance and loan-level price adjustments

Various mortgage insurance coverage options are available for certain Flexible mortgages. Financed mortgage insurance, however, is not permitted on Flexible mortgages. The lender may select from different levels of mortgage insurance when applicable. Each level of coverage has an associated loan-level price adjustment that may vary depending on the LTV and recommendation

Refer to the [Mortgage Insurance Coverage and Loan-Level Price Adjustment Requirement chart for Flexible mortgages](#) on page 85.

Special feature codes for Flexible mortgages will be listed in the Underwriting Findings report.

Temporary buydowns

Temporary buydowns are permitted on all Flexible mortgages; however, the applicable qualifying rate varies depending on the LTV of the first mortgage. For Flexible mortgages with LTVs greater than 95% (for example, Flexible 97), the borrower will be qualified at the note rate. For Flexible mortgages with LTVs of 95% or less (for example, 80/20), the borrower will be qualified at 1 percentage point above the bought-down rate. With the exception of the qualifying rate, all temporary buydown guidelines outlined in the Selling Guide, Part VII, Chapter 1, Section 104, apply to Flexible

mortgages. As a reminder, buydown funds paid by interested parties are subject to the applicable interested-party contribution limits based on the CLTV.

Data entry tip: For mortgages with temporary buydowns, enter the first year bought-down rate in the Additional Data screen. DU will determine the applicable qualifying rate and calculate the qualifying ratios accordingly.

Nonpermanent resident aliens

The Flexible mortgage products are available to nonpermanent resident aliens at the same terms available to permanent residents and U.S. citizens.

Flexible mortgages that receive a Refer with Caution recommendation

Flexible mortgages that receive a Refer with Caution recommendation will be identified by DU as either eligible or ineligible for delivery to Fannie Mae.

- **Refer with Caution recommendations that are eligible for delivery:** DU will identify certain Flexible mortgages that receive a Refer with Caution recommendation as eligible for delivery to Fannie Mae subject to a *higher* loan-level price adjustment than what is required for loans that receive an Approve or Refer recommendation. For 5/1 ARMs that receive an “eligible” Refer with Caution recommendation, an additional .25% loan-level price adjustment applies. If the lender delivers the loan to Fannie Mae, pays the applicable price adjustment, and complies with all the requirements in the Underwriting Findings report, then the loan will be eligible for the limited waiver of underwriting representations and warranties.
- **Refer with Caution recommendations that are not eligible for delivery:** DU will also return an Underwriting Findings message that identifies Refer with Caution loans that are not eligible for delivery due to excessive layering of risk. Exceptions to the Refer with Caution policy are described in Chapter 5.

Flexible mortgages that receive Expanded Approval with Timely Payment Rewards® (EA/TPR™) recommendations

For lenders participating in our EA/TPR initiative, Flexible mortgage loans are eligible to receive EA-I, -II, or -III/Eligible recommendations. Lenders must deliver these loans with the applicable special feature code for EA mortgages, and not with special feature codes for Flexible mortgages. The loan-level price adjustments for loans that receive EA recommendations apply.

- Loans without subordinate financing that have LTVs greater than 95% that receive EA-I, -II, or -III/Eligible recommendations are eligible for delivery. (The TPR feature is available for EA-II and -III/Eligible recommendations, subject to EA guidelines.)
- Loans with subordinate financing that have CLTVs greater than 95% (such as 80/20) that receive EA-I/Eligible recommendations are eligible

for delivery. (Subordinate financing is not allowed on EA-II and -III recommendations.)

- Loans that receive Refer W Caution/IV recommendations are not eligible for delivery to Fannie Mae.

Ineligible loans

Generally, Flexible mortgages that are ineligible (Approve, Refer, or Refer with Caution) should not be delivered to Fannie Mae. Lenders are not permitted to combine other variances they have negotiated outside of DU with Flexible mortgages.

Generic adjustable-rate mortgage plans

A number of generic adjustable-rate mortgage (ARM) plans are available for underwriting with DU. These generic ARM plans are provided to assist lenders in underwriting their negotiated ARMs and standard ARM plans (such as certain LIBOR ARMs) that are not specifically identified in the ARM Plan field in the DO/DU user interface. Although lenders must continue to obtain approval in their Master Agreements to deliver negotiated products, lenders will not need approval in their Master Agreements to deliver standard Fannie Mae ARM plans that are underwritten with DU using generic ARM plans.

Loans underwritten through DU as generic ARMs will be eligible to receive the same benefits inherent with all loans underwritten with DU, including reduced income and asset documentation, reduced property fieldwork documentation, and the limited waiver of underwriting representations and warranties for loans that receive an Approve/Eligible recommendation.

Generic ARMs are available in the ARM Plan list in the Additional Data screen in the DO/DU user interface. Lenders have the option of selecting a specific Fannie Mae ARM plan, the Lender ARM plan, or a generic ARM plan. The lender should select the appropriate generic ARM plan when the specific Fannie Mae ARM plan is not listed.

The following generic ARM plans are available in the DO/DU user interface:

- FM GENERIC, 6 MONTH
- FM GENERIC, 1 YR., 1% ANNUAL Cap
- FM GENERIC, 1 YR, 2% ANNUAL Cap
- FM GENERIC, 3 YR
- FM GENERIC, 5 YR
- FM GENERIC, 7 YR
- FM GENERIC, 10 YR
- FM GENERIC, NEGATIVE AMORTIZATION

Note: The generic ARM plans are provided as tools for underwriting with DU. While the generic plan names, such as FM GENERIC, 6 MONTH, should be used to submit the loans to DU, the generic plan names *must not* be used in closing documents or for delivery purposes. The lender *must* identify the applicable Fannie Mae ARM Plan Number when delivering the loan to Fannie Mae.

Eligible transactions, eligible property types, maximum LTVs

Eligible loan transactions, eligible property types, and maximum LTVs, CLTVs, and home equity combined loan-to-value ratios (HCLTV) for generic ARMs will be based on the equivalent standard Fannie Mae ARM plans (equivalent with respect to the initial interest rate adjustment period).

Ineligible loans

Generic ARMs will be ineligible based on the equivalent standard Fannie Mae ARM guidelines. For example, ARMs are not permitted on most Community Lending products; therefore, if Generic ARM is selected on a Community Lending product that does not allow ARMs, DU will return an Ineligible recommendation.

DU processing

DU applies standard Fannie Mae ARM underwriting and eligibility guidelines to the generic ARM plan equivalent based on the initial interest rate adjustment period. For example, if the lender selects FM GENERIC, 1 YR, 2% ANNUAL Cap, DU will apply the same qualifying rules, eligibility rules, and risk assessment as it does for a standard Fannie Mae 1-year ARM with a 2% annual cap, such as Fannie Mae ARM plan 720. In this example, DU will calculate the qualifying rate (as it does for all 1-year ARMs with 2% annual cap) at 2 percentage points above the note rate.

In processing generic ARM plans, DU will:

- Apply standard ARM eligibility guidelines;
- Qualify borrowers based on standard ARM qualifying guidelines;
- Allow temporary buydowns based on standard ARM guidelines;
- Allow generic ARM plans equivalent to standard ARM plans on special mortgage products (for example, generic 5-, 7-, and 10-year ARMs would be treated as “eligible” in conjunction with Flexible mortgages);

- Evaluate the risk assessment based on the initial interest rate adjustment period for the ARM; and
- Return a specific message stating that the loan was underwritten as a generic ARM.

The ARM Qualifying Rate field is not required for submission. If the qualifying rate is entered for a Fannie Mae ARM plan or generic ARM plan (other than the generic negative amortization ARM plan), DU will ignore the qualifying rate when calculating the expense ratio and will instead apply our standard ARM qualifying rate policies based on the initial interest rate adjustment period of the ARM. For the Lender ARM Plan selection in the Product Plan Number field, DU will use the qualifying rate entered by the user, if provided. If a qualifying rate is not entered for the Lender ARM Plan, DU will calculate the qualifying rate at 2 percentage points above the note rate.

The ARM Index Value and ARM Index Margin fields are not required for submission. If entered, DU will calculate the fully indexed rate and determine if the note rate (start rate) is within our limits for all 6-month, 1- and 3-year ARMs, including the equivalent generic ARM plans. If the margin and index are not provided, DU will issue a message requiring that the lender confirm that the start rate is within our limits.

Data entry tips:

- For Fannie Mae standard and generic ARM plans, do not enter a qualifying rate. DU will determine the qualifying rate. (If a rate is entered, DU will ignore it.)
- For the Lender ARM plan, enter the qualifying rate. DU will use the rate entered. (If a rate is not entered, DU will apply a qualifying rate equal to 2 percentage points above the note rate.)

Mortgage insurance coverage

Standard adjustable-rate mortgage insurance coverage is required. The “Reduced MI” and “Lower-Cost MI” options are not available with generic ARM plans.

Property fieldwork recommendations

The DU appraisal and inspection forms 2055, 2065, 2075, and 2095 are available.

DU recommendations

Loans submitted with generic ARM plans that receive Approve/Eligible recommendations are eligible for the limited waiver of underwriting representations and warranties provided that the actual ARM plan meets Fannie Mae’s guidelines or the terms of the lender’s negotiated commitment.

Loans with Approve/Ineligible or Refer/Ineligible recommendations may be delivered only if the lender has a variance that allows delivery of such ARMs with the specific Ineligible characteristics. (The lender must also comply

with our existing policies with respect to underwriting Refer/Ineligible loans.)

Generic 5-, 7-, and 10-year ARM plans are eligible to receive an EA recommendation.

HomeStyle® Renovation mortgages

The HomeStyle Renovation mortgage is a Fannie Mae product that allows the purchase or limited cash-out refinance of an existing home for the purpose of including the cost of home improvements in the subject mortgage. Financing is based on the “as-completed” value of the property – borrowers can use up to 50 % of the “as-completed” value for improvements or repairs. Fannie Mae does not specify which improvements a borrower may or may not finance. The Renovation work should be performed by contractors who are licensed, registered, or certified, or who have the highest level of certification required. Lenders must be approved in their Master Agreement to originate and deliver HomeStyle Renovation mortgages. With the exception of the expanded loan terms available in DU, all other HomeStyle Renovation mortgage requirements in the Master Agreement are applicable.

Eligible property types

One- to four-unit properties and single units in a condominium or cooperative project are eligible. Manufactured homes are not permitted; however, modular homes that are pre-assembled and transported to the site (follow-up site construction is necessary) are permitted and should be reflected in DU as a detached home.

Data entry for HomeStyle Renovation mortgages

DU identifies HomeStyle Renovation mortgages based on the entry of a dollar amount in Line b of Section VII when lenders select either purchase or refinance as the loan purpose in Section II and the loan is not submitted as Community Lending. If a dollar value is entered in Line b of Section VII, DU will automatically underwrite the loan according to the HomeStyle Renovation mortgage guidelines. Verification messages will also identify the loan as having been underwritten as a HomeStyle Renovation mortgage.

Data entry tip: Data entered in Section VII, Line b, identifies the loan as a HomeStyle Renovation mortgage when Purchase or Refinance is selected in Section II and Community Lending is not selected.

Note: The HomeStyle Construction to Permanent mortgage is a single closing construction transaction. Although specific HomeStyle Renovation mortgage messages will not be provided in the Underwriting Findings report for HomeStyle Construction to Permanent loans, the loan may be processed using DU. For the loan purpose in Section II, select construction. Do not enter any data on Line b of Section VII. The lender must determine outside of DU that the HomeStyle Construction to Permanent guidelines are met.

Data entry tip: HomeStyle Construction to Permanent mortgages must be entered as construction in Section II. Do not enter any data in Section VII, Line b.

Section VII. Details of Transaction

It is essential to enter correct data in Section VII to obtain an accurate underwriting recommendation. The following information is provided to assist users in entering data for HomeStyle Renovation mortgages.

Line a. Purchase price: For purchase transactions, the “as-is” purchase price of the property (not including any costs or value of improvements) is entered in Line a.

Line b. Alterations, improvements, repairs: Lenders calculate the cost of the home improvements based on a pre-established formula that includes the cost of the materials and labor (provided by the contractor), contingency reserves, costs of inspections, fees, and permits, etc. The total cost of the home improvements must be entered in Line b. The maximum allowable cost of improvements is 50% of the “as-completed” value.

Note: Fannie Mae Form 1035, *HomeStyle Maximum Mortgage Worksheet*, was designed to assist lenders in the calculation of rehabilitation costs, the maximum home improvement amount, and the maximum LTV ratio.

Line c. Land: Not applicable to HomeStyle Renovation mortgages.

Line d. Refinance amount: Enter the outstanding principal balance of the existing first mortgage, the payoff of the outstanding principal balance of any existing subordinate mortgage that was used to acquire the subject property and that will be paid off with the proceeds of the new loan.

Appraised Value

The appraiser establishes the value of the home based on the review of plans and specifications prepared by the contractor, and provides an “as-completed” appraised value of the property.

For purchase transactions, the Appraised Value amount entered in DU should be the “as-completed” value. For refinance transactions, the Appraised Value entered in DU should be the *lesser of* the “as-completed” appraised value of the property or the sum of the unpaid principal balances of all outstanding liens and the total renovation costs. See the *Selling Guide*, Part VII, Chapter 1, Section 116 for more information.

Subordinate financing with HomeStyle Renovation mortgages

Community Seconds loans are permitted in conjunction with HomeStyle Renovation mortgages. Furthermore, when subordinate financing exists and the CLTV exceeds 95%, the subordinate lien must be a Community Seconds loan. The lender must use Special Feature Code 118 upon delivery to Fannie Mae. Refer to [Community Seconds mortgages](#) on page 33 for additional information.

Note: When the CLTV exceeds 95%, DU looks for the existence of a subordinate lien in Section VII, Line j, and issues verification messages for the lender to confirm the eligibility of the loan according to the Community Seconds guidelines. On HomeStyle Renovation mortgages, do not use the Community Seconds indicator in the Community Lending screen.

Data entry tip: Do not use the Community Seconds indicator in the Community Lending screen when the Community Seconds is subject to a HomeStyle Renovation mortgage.

LTV calculations

DU calculates the LTVs for HomeStyle Renovation mortgage purchase and refinance transactions as follows:

HomeStyle Renovation Mortgage LTV Calculations	
Purchase	$\frac{\text{Loan amount}}{\text{Lesser of: purchase price and improvements (Line a plus Line b) or the Appraised value*}}$
Refinance	$\frac{\text{Loan amount}}{\text{Appraised value*}}$

***Note:** As stated above in the Appraised Value section, for purchase transactions, the Appraised Value amount entered in DU should be the “as-completed” value. For refinance transactions, the Appraised Value entered in DU should be the *lesser* of the “as-completed” appraised value of the property or the sum of the unpaid principal balances of all outstanding liens and the total renovation costs.

Limited cash-out refinance guidelines

The maximum LTV for HomeStyle Renovation mortgage limited cash-out refinance transactions is 95%. In accordance with the requirements of Fannie Mae *Selling Guide* (Part VII, Chapter 1, Section 116), cash back to the borrower on any limited cash-out refinance transaction on any HomeStyle Renovation mortgage is prohibited without regard to the LTV.

The new loan amount for limited cash-out refinances under the HomeStyle Renovation mortgage product may include:

- the payoff of the outstanding principal balance of an existing first mortgage,
- the payoff of the outstanding principal balance of any existing subordinate mortgage that was used to acquire the subject property,
- the financing of closing costs (including prepaid expenses), and
- the cost of improvements that will be made to the property in conjunction with the transaction.

Note: Cash-out refinance transactions are not permitted under the HomeStyle Renovation mortgage product.

Multiple mortgages to the same borrower (HomeStyle Renovation mortgages)

In accordance with Fannie Mae’s *Selling Guide* (Part VII, Chapter 1, Section 116), we limit the financed-property limitation for HomeStyle Renovation mortgages to four properties for investment property and second home transactions.

InterestFirst™ mortgages

Fannie Mae's InterestFirst mortgage offers borrowers lower initial monthly payments than those available with traditional loan products by offering an interest-only period followed by a fully amortizing period. It allows interest-only payments based on the note rate for an initial period, then converts to a fully amortizing loan for the remainder of the loan term. During the interest-only period, borrowers may make principal curtailments of any amount. After a curtailment, the new principal balance will be adjusted, and the next scheduled monthly payment will be reduced accordingly.

Lenders must obtain approval in their Master Agreements to deliver InterestFirst mortgages to Fannie Mae. Additionally, there are unique servicing requirements for these types of mortgages. Lenders should refer to Fannie Mae's *Selling* and *Servicing Guides*.

Eligible transactions

InterestFirst is available with 30-year fixed-rate mortgages and certain fixed-period ARMs for the purchase or refinance of one-unit principal residences and second homes.

Fixed-rate 30-year mortgages: The interest-only payment period is 10 or 15 years; thereafter, the monthly payment adjusts to fully amortize the loan over the remaining term of 20 or 15 years. The note rate remains constant throughout the term of the loan.

Fixed-period 3/1, 5/1, 7/1, and 10/1 ARM plans: The interest-only payment period is 3, 5, 7, or 10 years depending on the ARM plan; thereafter, the monthly payment adjusts to fully amortize the loan over the remaining term (27, 25, 23, or 20 years, as applicable).

ARM indices: InterestFirst ARMs must be tied to either the US Treasury securities with a constant maturity of one-year (CMT-indexed) or the one-year London Interbank Offered Rate (LIBOR-indexed). InterestFirst ARMs cannot contain a fixed-rate conversion option.

Eligible InterestFirst ARM Plans

Below are the Fannie Mae ARM plans that are eligible in conjunction with InterestFirst mortgages.

InterestFirst ARM Plans			
ARM Plans	Index	Initial fixed period – Interest rate caps	Interest-only period
3513	CMT	3/1 ARM – 2/2/6	10 years
3514	LIBOR	3/1 ARM – 2/2/6	10 years
3270	LIBOR	3/1 ARM – 2/2/6	3 years
3271	CMT	3/1 ARM – 2/2/6	3 years
3515	CMT	5/1 ARM – 2/2/5	10 years
3516	LIBOR	5/1 ARM – 2/2/5	10 years

InterestFirst ARM Plans			
ARM Plans	Index	Initial fixed period – Interest rate caps	Interest-only period
3502	LIBOR	5/1 ARM – 5/2/5	5 years
3503	CMT	5/1 ARM – 5/2/5	5 years
3504	CMT	5/1 ARM – 5/2/5	10 years
3505	LIBOR	5/1 ARM – 5/2/5	10 years
3223	LIBOR	5/1 ARM – 2/2/5	5 years
3226	CMT	5/1/ ARM – 2/2/5	5 years
3517	CMT	7/1 ARM – 5/2/5	10 years
3518	LIBOR	7/1 ARM – 5/2/5	10 years
3224	LIBOR	7/1 ARM – 5/2/5	7 years
3227	CMT	7/1 ARM – 5/2/5	7 years
3225	LIBOR	10/1 ARM – 5/2/5	10 years
3228	CMT	10/1 ARM – 5/2/5	10 years

Note: Fannie Mae ARM plans that are not listed in this table are not eligible for delivery as InterestFirst mortgages. Plans 660, 750, 1423, 2725, 2727, and 2729, while not eligible as InterestFirst, are eligible as standard ARMs.

We strongly recommend that users select the actual Fannie Mae ARM plan (instead of a Generic ARM plan) to submit loans to DU whenever possible. This will enable DU to return messages specific to the Fannie ARM plan, including eligible loan transactions and property types, loan-level price adjustments, mortgage insurance coverage, and special feature codes; this will facilitate accurate underwriting, processing, and delivery of these loans.

While the generic plan names (such as FM GENERIC, 5 YR) can be used to submit loans to DU, the generic plan names **must not** be used in the closing documents or for delivery purposes. The lender **must** identify the applicable Fannie Mae ARM Plan Number (such as 3515) when delivering the loan to Fannie Mae. For details on delivering loans to Fannie Mae, refer to the *Mae Selling Guide*, Part VI.

Eligible property types for InterestFirst mortgages

One-unit properties, including units located in condominium or PUD projects are eligible. Manufactured homes and units in cooperative projects are not eligible.

DU processing

DU will apply the InterestFirst underwriting guidelines when the lender selects the Interest Only option in the Repayment Type field in the Additional Data screen. The Interest Only selection is used for both the fixed-rate and fixed-period ARM InterestFirst mortgages.

In processing the InterestFirst mortgage, DU will:

- Assign a slightly higher level of risk than that of a fully amortizing fixed-rate mortgage;
- Use the interest-only payment, including taxes and insurance (ITI), to calculate reserves;
- For fixed-rate mortgages, DU will use the ITI payment when considering the maximum allowed total expense ratio. For ARMS, DU considers the ARM plan, interest-rate caps, and interest-only period when evaluating the maximum total expense ratio. As a benefit to borrowers who apply for the 10-year interest-only payment period, and in recognition of the reduction to payment shock on these plans, DU will allow a slightly more liberal total expense ratio than that allowed on shorter interest-only periods;
- Display the interest portion of the principal and interest payment (P&I) in the proposed housing payment on the Underwriting Analysis report and in Section V of the loan application; and
- Return a message stating that the loan was underwritten as an InterestFirst mortgage and the lender must have approval in its Master Agreement to deliver the loan to Fannie Mae.

Mortgage insurance coverage

Standard mortgage insurance coverage for 30-year fixed-rate mortgages or fixed-period ARMs is required. The “Reduced MI” and “Lower-Cost MI” options are not available for InterestFirst mortgages.

Loan-level price adjustments

In addition to other standard loan-level price adjustments, a price adjustment of .25% is required for fixed-rate InterestFirst mortgages with LTVs greater than 90%. If subordinate financing exists and the LTV exceeds 75%, a .25% loan-level price adjustment applies (without regard to the CLTV). The standard subordinate financing loan-level price adjustments that apply to mortgages with LTVs greater than 65% and CLTVs greater than 90% do not apply to InterestFirst mortgages. There are no special feature codes required for InterestFirst mortgages with subordinate financing, and lenders should not use Special Feature Codes 338 or 339 upon delivery. DU will return the standard loan-level price adjustment message when applicable.

Property fieldwork recommendations

The DU appraisal and inspection forms 2055, 2065, and 2075 are available.

DU recommendations for InterestFirst mortgages

- Loans with Approve/Eligible or Refer/Eligible recommendations are eligible for delivery to Fannie Mae provided the lender has InterestFirst approval in its Master Agreement, as stated earlier. Loans receiving Approve/Eligible recommendations will be eligible for the limited waiver of underwriting representations and warranties.

- Loans with Approve/Ineligible or Refer/Ineligible recommendations, generally, are not eligible for delivery.
- Loans with Refer with Caution recommendations are not eligible for delivery.
- Loans with Expanded Approval recommendations are not eligible for delivery.

Negatively amortizing ARMs

Negative amortization is the gradual increase in the mortgage debt that occurs when the monthly installment is not sufficient to fully repay both principal and interest. The shortage, which is the result of insufficient interest repayment, is added to the unpaid principal balance creating “negative” amortization. ARMs with negative amortization represent a higher risk than fully amortizing ARMs, and will continue to require approval in the Master Agreement to be delivered to Fannie Mae.

To assist lenders that originate negatively amortizing ARMs, we are adding a new generic ARM plan – FM Generic, Negative Amortization – to the list of ARM plans that may be submitted to DU. In addition, loans that receive Approve/Eligible recommendations from DU are eligible for the limited waiver of underwriting representations and warranties for lenders that have approval in their Master Agreements to deliver negatively amortizing ARMs.

Eligible transactions

Negatively amortizing ARMs are available with loan terms to a maximum of 30 years for the purchase and refinance of one-unit, principal residence and second home properties.

Eligible property types

One-unit properties, including single units located in condominium, cooperative, or PUD projects, are eligible.

DU processing for negatively-amortizing ARMs

DU applies underwriting guidelines that are appropriate for the higher risk of negatively amortizing ARMs when the generic negative amortization ARM plan is selected in the ARM Plan field in the Additional Data screen.

Note: The generic negative amortization ARM plan is provided as a tool for underwriting with DU. While the generic plan name, FM GENERIC NEGATIVE AMORTIZATION, should be used to submit the loan to DU, the generic plan name ***must not*** be used in the closing documents or for delivery purposes. The lender ***must*** identify the correct Fannie Mae ARM plan number when delivering these loans to Fannie Mae.

In processing a negatively amortizing ARM, DU will:

- Use the interest rate entered by the lender in the ARM Qualifying Rate field to qualify the borrower and calculate reserves. If an interest rate is not entered, DU automatically uses 7.5%;

- Assign a level of risk that is somewhat higher than that of standard short-term ARM plans (6-month and 1-year ARMs); and
- Return a message stating that the loan was underwritten as a negatively amortizing ARM and that the lender must have approval to deliver negatively amortizing ARMs.

Mortgage insurance coverage

Standard mortgage insurance coverage for ARM plans is required. The “Reduced MI” and “Lower-Cost MI” options are not available for negatively amortizing ARMs.

Property fieldwork recommendations

DU Form 2055 (or Form 2095 for cooperative units) with an interior and exterior inspection is required.

DU recommendations

- Approve/Eligible or Refer/Eligible recommendations are eligible for delivery to Fannie Mae. Approve/Eligible recommendations are eligible for the limited waiver of underwriting representations and warranties.
- Approve/Ineligible or Refer/Ineligible recommendations may be delivered only if the lender has a variance that allows delivery of negative amortization ARMs with the specific Ineligible characteristics. (The lender must also comply with our existing policies with respect to underwriting Refer/Ineligible loans.)
- Refer with Caution recommendations are not eligible for delivery.
- Expanded Approval recommendations are not eligible for delivery.

Smart Commute[®]

The Smart Commute feature may be available for certain standard mortgage products according to a lender’s negotiated contract. DU does not contain the rules to determine if the loan complies with the Smart Commute guidelines; therefore, lenders that are approved to deliver loans with this feature to Fannie Mae must apply the appropriate guidelines outside of DU.

Information concerning specific transaction types

Biweekly mortgages

Biweekly payment plans are eligible with fully amortizing fixed-rate loans that have loan terms less than or equal to 30 years. Lenders must indicate that the loan has a biweekly payment in DU. The proposed monthly payment in Section V, as calculated by the system, will reflect the full monthly payment and not the biweekly payment. Furthermore, the full monthly payment is used in the calculation of the qualifying ratios. Lenders will be required to confirm that biweekly mortgages comply with the requirements in the *Selling Guide*, Part VII, Chapter 1, Section 110.

Conversions of construction-to-permanent financing

The conversion of construction-to-permanent financing involves the granting of a long-term mortgage to a borrower for the purpose of replacing interim construction financing that the borrower has obtained to fund the construction of a new residence.

The borrower must hold title to the lot, which can have been previously acquired or can be purchased as part of the transaction. The borrower must be the primary obligor on the mortgage or deed of trust note for the permanent financing.

A construction-to-permanent financing mortgage can be closed as a single transaction or as two separate transactions, and may be closed as a purchase money transaction, a limited cash-out refinance transaction, or a cash-out refinance transaction. When the loan is closed as a refinance transaction, the borrower must have held legal title to the lot before he or she applied for the construction financing and must be named as the borrower for the construction loan.

Generally, Fannie Mae's policies and guidelines stated in the *Selling Guide*, Part VII, Chapter 1, Section 103, for conversions of construction-to-permanent financing are applicable to loans underwritten with DU. However, DU requires construction-to-permanent transactions to be submitted based on the following criteria:

- *A single closing transaction* is used to describe one closing for both the interim construction loan and the permanent financing, and must be entered as construction in Section II. In this Guide and the messages provided by DU, this is referred to as a one-time close construction transaction. DU will process a construction transaction as a purchase money transaction.
- *Two separate closing transactions* is used to describe two separate closings – one for the interim construction phase and another for the permanent financing – and must be entered as construction-permanent in Section II. In this Guide and the messages provided by DU, this type of transaction is referred to as construction-permanent. DU will process a Construction-permanent transaction as a refinance transaction.

Construction

Eligible property types

One- to-two unit site-built homes are eligible. Manufactured homes and units in a condominium or cooperative project are not eligible. Modular homes that are pre-assembled and transported to the site (follow-up site construction is necessary) are permitted and should be reflected in DU as a detached home.

Data entry for construction transactions

There are unique data entry requirements for construction transactions, which are described below.

Section II

Purpose of loan: Lenders must select construction as the loan purpose in Section II. DU processes construction transactions as purchase money mortgages, and issues specific one-time close construction transaction messages.

Data entry tip: Enter single closing (one-time close) construction transactions as Construction in Section II.

Loan terms: The loan should be underwritten through DU based on the terms of the permanent loan at modification. Because the interest rate is unknown and is subject to change over the course of the construction period, the lender may want to submit the loan at a higher interest rate to ensure that the borrower will still qualify if there is an increase in rates. If there are changes to the terms of the loan during the process, the loan must be resubmitted if the change in data falls outside the tolerances permitted as detailed in [Resubmission policy](#) on page 93.

Section VI A

Lot acquired by inheritance: If the borrower received the lot through an inheritance, the current appraised value of the lot should be entered in Section VI A as an other liquid asset.

Lot acquired as gift: If the borrower received the lot as a gift, the current appraised value of the lot should be entered in Section VI A as a gift. Our standard gift requirements are applicable. DU will issue a verification message requiring documentation of the gift, and verification that the gift is from an eligible donor. In addition, the borrower must provide a copy of the deed that verifies the donor and the transfer of ownership of the lot.

Section VI L

Loan on the lot: Because the cost or value of the lot and lot equity are entered in Section VII, care must be taken when reflecting the loan on the lot in Section VI L so that the borrower's assets and expense ratio are computed accurately. One of the following two options may be considered when entering the loan on the lot:

- Enter the loan in Section VI L as an installment liability without a monthly payment. The payment on the lot should not be included in the qualifying ratio. Do not mark the loan as paid by closing, because doing so will overstate the amount of funds required to close, or
- Omit the loan from Section VI L.

Section VII

Line a. Purchase price: Enter the purchase price or cost of construction. If the borrower acquires the lot from the builder as part of the transaction, include the cost of the lot in Line a.

Data entry tip: DU requires the purchase price in Line a, Section VII, in order to underwrite a construction transaction. Loans submitted without a purchase price receive an error message.

Line b. Alterations, improvements, repairs: Not applicable to construction transactions.

Line c. Land: If the borrower acquires the lot separately, the cost or value of the lot must be entered in Line c according to these guidelines:

- *Purchased within the past 12 months:* Enter the sales price of the lot. The lender must document the cost of the land by providing a copy of the purchase agreement/contract or settlement statement. (Closing costs associated with the purchase of the land should not be included in Line c.)
- *Purchased more than 12 months ago:* Enter the current appraised value of the lot. The appraiser will have to document the value of the lot separately.
- *Gifted or inherited lot:* If the borrower received the land as a gift or inheritance, enter the current appraised value of the land. The appraiser will have to document the value of the lot separately. The value of the lot that was gifted or inherited must be entered in Section VI A as described above.

Line d. Refinance: Not applicable to construction transactions.

Line l. Other credits: If the borrower purchased the lot in a separate transaction, the equity in the lot must be entered as other credit. If the borrower has an outstanding loan on the property, the credit amount is calculated as the amount in Line c less the balance of any liens on the lot. If the borrower owns the lot free and clear, the other credits amount should match the amount in Line c.

Following are examples of how credits should be entered under description of other credits, which will in turn automatically populate Line l in Section VII:

Example 1: Borrower purchased the lot eight months ago at a cost of \$20,000 and paid cash.

Line c: \$20,000 (sales price of lot)

Line l: \$20,000 ($\$20,000 - 0 = \text{equity}$)

Example 2: Borrower purchased the lot eighteen months ago at a cost of \$20,000 and paid cash. The appraiser valued the lot at \$30,000.

Line c: \$30,000 (current appraised value)

Line l: \$30,000 ($\$30,000 - 0 = \text{equity}$)

Example 3: Borrower purchased the lot eight months ago at a cost of \$20,000 – \$5,000 paid in cash and \$15,000 from a loan on the property. The current balance on the loan is \$14,000.

Line c: \$20,000 (sales price of lot)

Line l: \$6,000 ($\$20,000 - \$14,000 = \text{equity}$)

Example 4: Borrower purchased the lot eighteen months ago for \$20,000 – \$5,000 paid in cash and \$15,000 from a loan on the property. The current balance on the loan is \$14,000. The appraiser valued the lot at \$30,000.

Line c: \$30,000 (current value)

Line l: \$16,000 ($\$30,000 - 14,000 = \text{equity}$)

Data entry tips:

- For construction transactions, enter the lot equity amount in Section VII, as an other credit. Exception: if the LTV exceeds 80% and the borrowers' required 5% contribution is comprised of lot equity, enter the lot equity amount in borrowers' liquid asset.
- For construction transactions where the lot was received as a gift, enter the current appraised value of the lot in Section VI A as a gift.
- For construction transactions where lot was received through an inheritance, enter the current appraised value of the lot in Section VI A as an other liquid asset.

Appraised value

The appraiser establishes the value of the home based on the review of plans and specifications prepared by the contractor/builder and provides an "as-completed" appraised value of the property including the lot value. As noted above, the appraiser may be required to provide a separate value for the lot in addition to the "as-completed" value. Enter the "as-completed" value as the appraised value.

If the appraisal was completed based on plans and specifications, a final interior inspection of the property is required. A certificate of completion form is required in addition to photographs of the completed property.

LTV calculations

The LTV is calculated based on the lesser of the acquisition cost or the appraised value. The acquisition cost is based on the purchase price/cost of construction plus the value of the lot entered in the Section VII, if acquired separately. DU calculates the LTV for Construction transactions as follows:

$\frac{\text{Loan amount}}{\text{Lesser of: acquisition cost (Line a plus Line c) or appraised Value}}$

Age of documents for construction transactions

All verification documents (paystubs, bank statements, Verification of Employment, Verification of Deposits, credit reports) must be dated within 180 days of the closing date. Our requirements with regard to the age of the verification documents (180 days) for construction transactions are based on the original (interim) note date. The verification documents do not have to be updated when the loan is modified to the permanent long-term mortgage.

Construction transaction examples

Building on the examples above for data entry of other credit, we have provided additional information to create examples to show how all data should be reflected in Lines a, c, l, m, and p in Section VII. The table also reflects the resulting LTV calculation.

Section VII. Details of Transaction		Example 1	Example 2	Example 3	Example 4	Example 5
a	Purchase price	\$80,000	\$80,000	\$80,000	\$80,000	\$100,000
c	Land	\$20,000	\$30,000	\$20,000	\$30,000	0
l	Other credits	\$20,000	\$30,000	\$6,000	\$16,000	0
m	Loan amount	\$75,000	\$75,000	\$90,000	\$90,000	\$95,000
p	Cash from borrower	\$5,000	\$5,000	\$4,000	\$4,000	\$5,000
Acquisition cost		\$100,000	\$110,000	\$100,000	\$110,000	\$100,000
Appraised value		\$100,000	\$105,000	\$105,000	\$110,000	\$105,000
LTV		75%	72%	90%	82%	95%

Following are examples used in the table above for single closing transactions construction transactions:

1. Borrower purchased the lot eight months ago at a cost of \$20,000 for cash and contracts with the builder to build the home for \$80,000.
2. Borrower purchased the lot eighteen months ago at a cost of \$20,000 and paid cash. The appraiser valued the land at \$30,000. The borrower contracts with the builder to build the home for \$80,000.
3. Borrower purchased the lot eight months ago at a cost of \$20,000: \$5,000 paid in cash and \$15,000 from a loan on the property. The current balance on the loan is \$14,000. The borrower contracts with the builder to build the home for \$80,000.
4. Borrower purchased the lot eighteen months ago for \$20,000: \$5,000 paid in cash and \$15,000 from a loan on the property. The current balance on the loan is \$14,000. The appraiser valued the lot at \$30,000. The borrower contracts with the builder to build the home for \$80,000.
5. Borrower contracts with the builder to buy the lot and build the home for \$100,000.

Construction-permanent

The maximum LTV/CLTV will be based on the occupancy of the property and the respective LTV/CLTV requirements for limited cash-out and cash-out refinances. DU will determine if the loan is eligible as a limited cash-out refinance or as a cash-out refinance. If the case is not eligible as either type of refinance, it will be ineligible, and the Underwriting Findings report will issue the failed refinance eligibility messages as applicable.

Example: If the property will be the principal residence of the borrower, the LTV is greater than 90%, and the borrower is receiving more than 2% of the loan amount in cash back, then the loan will be ineligible.

When the loan is closed as a refinance transaction, the borrower must have held legal title to the lot before he or she applied for the construction financing and must be named as the borrower for the construction loan. The lender must provide documentation to support this.

Eligible property types

One- to four-unit properties, including units in a condominium or cooperative project, are eligible. Manufactured homes are not eligible.

Data entry for construction-permanent transactions

There are unique data entry requirements for construction-permanent transactions, which are described below.

Section II

Loan purpose: Users must select construction-permanent as the loan purpose in Section II. DU processes construction-permanent transactions as refinance mortgages.

Data entry tip: Enter transactions that have two separate closings as Construction-Permanent in Section II.

Section VI A

Lot acquired by gift or inheritance: If the borrower received the lot through a gift or an inheritance, the current appraised value of the lot should be entered in Section VI A as an other liquid asset.

Section VI L

The interim construction loan should be entered as a mortgage and marked Paid By Close. If entering REO data in the Schedule of Real Estate Owned in the Full 1003, you should match the interim construction mortgage to the subject property. If using indicators and data fields in lieu of entering complete REO data, use the Subject Property indicator in Section VI L. The outstanding loan balance must reflect the total amount of the interim construction loan upon completion – the fully drawn amount. Include any separate unpaid liens against the lot if applicable. The total unpaid balance should be entered in Section VII, Line d.

REO screen

If entering REO data in the Schedule of Real Estate Owned in the Full 1003, the subject property must be identified in the Property Indicator field. The property should be entered as Subject of the Loan, or as Refi of Current Residence if the borrowers are already residing in the property. If using indicators and data fields in lieu of entering complete REO, use the Subject Property indicator in Section VI L.

Section VII

Line d: Refinance: Enter the total amount of the interim construction loan upon completion – the fully drawn amount. Include any separate unpaid liens against the lot if applicable. This amount should match the amount of the mortgage entered in Section VI L, as described above.

Appraised value

The appraised value is determined, in part, based on when and how the lot was acquired as stated in the *Selling Guide*, Part VII, Chapter 1, Section 103.

- *If purchased within the 12 months* prior to the application date for the construction financing, the lender should enter into the Appraised Value field the lesser of (1) the current appraised value for the property (both the lot and the improvements) or (2) the total acquisition costs (which are

the sum of the costs of the improvements and the sales price of the lot). The appraiser will have to document the value of the lot separately.

- *If purchased 12 or more months* prior to the application date for the construction financing, the lender should enter into the Appraised Value field the current appraised value for the property (both the lot and the improvements). The appraiser will have to document the value of the lot separately.
- *If received as a gift or through an inheritance*, regardless of the date of acquisition, the lender should use the current value of the lot **and the costs of improvements** in determining the appraised value for the property. The appraiser will have to document the value of the lot separately.

DU returns a message alerting the lender of the correct way to enter the appraised value if the lot was acquired less than 12 months from the date of application.

If the appraisal was completed based on plans and specifications, a final interior inspection of the property is required. A certificate of completion form is required in addition to photographs of the completed property.

Age of documents for construction-permanent transactions

All verification documents (paystubs, bank statements, Verifications of Employment, Verifications of Deposit, credit reports) must be dated within 180 days of the closing date of the subject loan.

New construction purchase transactions

If the borrower is purchasing a home under construction and never held title to the lot, this type of transaction should be treated as a purchase. The lender must select Purchase as the loan purpose in Section II. The lender will be required to satisfy the following additional requirement, even though DU will not issue a verification message for it:

A final *interior* inspection of the property is required prior to closing. A certificate of completion form is required in addition to photographs of the completed property.

Age of documents for new construction purchase transactions

Although the document expiration rules (and messages) will only permit documents to be 120 days old at the time the loan is closed, the lender does not have to obtain updated verification documents unless they will be more than 180 days old when the loan is closed.

Refinances

A refinance transaction involves the repayment of an existing debt from the proceeds of a new mortgage that has the same borrower and the same security property. We also consider as a refinance transaction one in which the present property owner obtains a mortgage on a property that does not already have a mortgage lien against it.

Data entry for refinances

For all refinances, the CLTV is calculated based on the loan amount of the new loan plus the unpaid balance of any subordinate liens listed in Section VI L or on Line j in Section VII.

Cash-out refinance

For cash-out refinance transactions, include the balance of all mortgage and non-mortgage debts that will be paid off with the proceeds of the subject transaction on Line d in Section VII. A loan-level price adjustment is associated with cash-out refinances that have LTVs in excess of 70%. See the [Loan-Level Price Adjustment Requirements chart](#) on page 86.

Limited cash-out refinance

For limited cash-out refinance transactions, enter in Section VII, Line d, the total payoff of the outstanding principal balance of the existing first mortgage and the payoff of the outstanding principal balance of any existing subordinate mortgage that was used to acquire the subject property. Prepayment penalties, if applicable, should be included in the payoff amount. Do not include the payoff of any other liabilities in Line d.

The definition for limited cash-out refinances that was provided in Fannie Mae Announcement 02-11 will apply to DU-processed loans. The loan amount for limited cash-out refinances may include:

- the payoff of the outstanding principal balance of an existing first mortgage,
- the payoff of the outstanding principal balance of any existing subordinate mortgage that was used to acquire the subject property,
- the financing of closing costs (including prepaid expenses), and
- cash back to the borrower in an amount no more than the lesser of 2% of the new mortgage or \$2,000.

DU cannot determine whether subordinate liens that are being paid off were used to acquire the property. As a result, DU will issue a message for every limited cash-out refinance transaction with more than one mortgage on the subject property (including home equity lines of credit) that are marked Paid By Close. The message, which will appear prominently at the top of the Underwriting Findings report, will require the lender to verify that the subordinate lien meets our guidelines for limited cash-out refinances.

Data entry tips:

- Non-mortgage debts that will be paid from proceeds of cash-out refinances should be included in Line d of Section VII.
- Non-mortgage debts that will be paid at closing on limited cash-out refinances should not be included in Line d of Section VII. They should be marked Paid By Close in Section VI L.

No cash-out refinance

The no cash-out refinance option is no longer a valid loan purpose. If a loan is submitted as a no cash-out refinance, DU will issue a message instructing the lender to change the refinance purpose to limited cash-out.

Refinance transactions for properties located in Texas

- A verification message will be issued for all owner-occupied refinance transactions, including construction-permanent transaction, on properties located in the state of Texas. The verification message will require that the lender delivering the loan to Fannie Mae have a Master Agreement authorizing delivery of loans that are originated in accordance with Article XVI, Section 50(a)(6) of the Texas Constitution. This applies to all cash-out refinances and may apply to some limited refinances.
- The lender will be required to confirm that the loan meets the terms of its Master Agreement outside of DU.

Note: DU *does not* contain the specific eligibility rules needed to determine eligibility in accordance with Article XVI, Section 50(a)(6) of the Texas Constitution or the requirements of the lender’s Master Agreement. Lenders must determine outside of DU that cash-out refinance mortgages securing properties in Texas are eligible for sale to Fannie Mae, and should be aware that even though a loan may receive an Approve/Eligible recommendation, the loan may not be eligible for delivery according to Section 50(a)(6) of the Texas Constitution or the lender’s Master Agreement. Refer to your Master Agreement and Fannie Mae’s *Selling Guide*, Part VII, Chapter 1, Section 112, and Fannie Mae Announcement 03-10 for additional information about originating and delivering this type of loan.

- Texas cash-out refinance transactions that receive an EA recommendation are not eligible for delivery to Fannie Mae with the TPR feature.

Subordinate liens: Home equity lines of credit and closed-end liens

If there is a home equity line of credit subordinated to the subject loan, the CLTV is based on the “drawn” or outstanding balance of the home equity line of credit at the time the subject loan is closed. The home equity line of credit CLTV ratio (HCLTV) is based on the maximum credit limit of the equity line.

You can enter the undrawn HELOC amount in Section VII, in which case DU will calculate the HCLTV ratio and advise you if the HCLTV exceeds the maximum allowed. If the undrawn amount is not entered, DU will return a message identifying the maximum HCLTV ratio. The lender must independently verify that the HCLTV meets Fannie Mae’s guidelines. The maximum HCLTV limits are identified in the [Maximum LTV charts](#), beginning on page 77.

The following examples show various LTV, CLTV, and HCLTV calculations for one-unit, principal residence, purchase transactions:

	Example 1	Example 2	Example 3	Example 4
Sales price/appraised value	\$100,000	\$100,000	\$100,000	\$100,000
First mortgage/loan amount	\$80,000	\$80,000	\$80,000	\$87,000
HELOC outstanding balance	\$10,000	\$10,000	0	\$8,000
HELOC credit limit	\$20,000	\$25,000	\$20,000	\$10,000

	Example 1	Example 2	Example 3	Example 4
LTV	80%	80%	80%	87%
CLTV (outstanding balance)	90%	90%	80%	95%
HCLTV	100%	105%	100%	97%

Examples 1, 3, and 4 represent eligible transactions per our HCLTV and CLTV guidelines.

Example 2 is not eligible for delivery to Fannie Mae because the HCLTV exceeds 100%.

Entering loan data for HELOCs and closed-end subordinate liens

The outstanding balances of subordinate liens (including drawn HELOC amounts and closed-end second mortgages) that are secured by the subject property should be entered in the loan application based on whether the subordinate lien is a new lien or an existing lien.

Note: For refinance transactions with an existing subordinate lien, it is important to either select the Subject Property Lien mortgage liability indicator in Section VI L or to complete the REO data fields in Section VI R (the Schedule of Real Estate Owned) in the Full 1003.

- **New subordinate liens: Section VII**

For both purchase and refinance transactions, the outstanding balances of new subordinate liens closed simultaneously with the first mortgage should be entered in Section VII, Line j. For HELOCs, enter the amount that will be drawn at closing. If the borrower will not draw down any portion of the HELOC at closing (i.e., if the outstanding balance at closing will be \$0.00), no data is entered for the HELOC in Line j.

The monthly payment associated with the outstanding balance of new subordinate liens must be entered in Section V in the proposed monthly housing expense field as Other Financing P&I. For HELOCs, enter the monthly payment associated with the amount drawn at the time of closing.

Data entry tip: For both purchase and refinance transactions, enter the outstanding balance of a new subordinate lien in Section VII, Line j. Enter the monthly payment for the new subordinate lien in Section V, Proposed Monthly Housing, Other Financing P&I.

- **Existing subordinate liens: Section VI L**

The outstanding balances of existing subordinate liens on refinance transactions secured against the subject property should be entered in Section VI L and either identified as a Subject Property Lien with the mortgage indicator or matched to the subject property in the in the Full 1003. If the subordinate lien will be paid off at closing, select Paid By Close. For HELOCs, enter the amount of outstanding funds that have been drawn prior to closing or that will be drawn at closing.

The monthly payments associated with the outstanding balance of existing subordinate liens that will be resubordinated must be reflected in Section VI L as well as entered in Section V in the proposed monthly housing expense field as Other Financing P&I. For HELOCs, enter the monthly payment associated with the drawn amount that will be resubordinated at the time of closing.

Data entry tip: The amount of the outstanding balance of an existing subordinate lien should be entered in Section VI L and either identified as a Subject Property Lien with the mortgage indicator or matched to the subject property in the in the Full 1003. Include the monthly payment for an existing lien in Section V, Proposed Monthly Housing, Other Financing P&I.

- **Undrawn HELOC amount: Section VII**
You can enter an amount in the Undrawn HELOC Amount field in Section VII of the loan application in the DO/DU user interface. This data is not required for loan submission; however, if information is provided, DU will calculate the HCLTV and advise the lender if the HCLTV ratio exceeds the maximum allowed. On the other hand, if the undrawn HELOC amount is not provided, DU will issue a message identifying the maximum allowable HCLTV limit for the subject transaction. The lender must independently verify that the HCLTV meets Fannie Mae guidelines.

Note: For information on Community Seconds, refer to [Community Seconds mortgages](#) on page 33.

Special feature codes

Fannie Mae requires lenders to specifically identify certain mortgages at delivery by using a special feature code to describe the unique characteristics of the individual mortgage, the mortgage product, the terms of a specific negotiated transaction, and to identify DU-processed mortgages. Special feature codes are part of the loan delivery data included on the *Loan Schedule* (Form 1068 and 1069) and the *Schedule of Mortgages* (Form 2005).

The proper reporting of special feature codes is an important factor in the lender receiving the limited waiver of representations and warranties for DU-processed loans as described in [Chapter 2](#) of this Guide. As a reminder, loans that were processed in DU must be identified by using either Special Feature Code 127 – if the lender delivering the loan to Fannie Mae is the lender that underwrote the loan through DU – or Special Feature Code 214 – if the lender delivering the loan to Fannie Mae is not the lender that underwrote the loan through DU.

The following list of special feature codes is provided to assist you in determining which codes may be associated with DU-processed loans. Other special feature codes may also be required at loan delivery. Refer to Part VI, Chapter 2, Section 203 of the *Selling Guide* for more information and a comprehensive list of special feature codes.

Although DU will identify the following special feature codes in the Underwriting Findings report, there are other special feature codes, which DU may not be able to identify, that could be required for loan delivery.

SFC	Description
003	Cash-out Refinance
007	Limited Cash-out / No Cash-out Refinance
009	Moderate Interest Rate Buydown
014	Significant Interest Rate Buydown
061	Community Home Buyer's Program
072	Employer Assisted Housing Mortgage
074	Fannie 3/2 Mortgage
118	Community Seconds (if applicable)
118	HomeStyle with Community Seconds
121	Fannie 97 Mortgage
127	DU-processed loan – lender delivering loan is the same lender that underwrote the loan in DU
214	DU-processed loan – lender delivering loan is not the lender that underwrote the loan in DU
187	80-10-10
206	Flexible Mortgage (90-97 LTV)
215	HomeStyle Renovation Mortgage; MyCommunityMortgage Community Renovation
235	Manufactured Home
281	Financed Single Premium MI
304	Texas Equity Take-Out Mortgage (if applicable)
338	80-15-5/90-5-5 Mortgage
339	75-20-5 Mortgage
340	Expanded Approval-I
341	EA-II / Non-TPR
342	EA-III / Non-TPR
357	Property Inspection Waiver
376	EA-III/TPR

SFC	Description
439	Non-permanent Resident Alien Borrower(s)
412	Flexible Mortgage (100 LTV)
446	Flexible Mortgage with Subordinate Financing
459	EA-II/TPR
460	MyCommunityMortgage 97
480	MyCommunityMortgage 100
519	MyCommunityMortgage 2-4; MyCommunityMortgage Community Renovation
564	Flexible Mortgage with Minimum Contribution Option
574	MyCommunityMortgage with Split Premium Financed Mortgage Insurance

Maximum allowable loan-to-value ratios

Generally, Fannie Mae determines the LTV for first mortgages by dividing the mortgage balance at the time the mortgage is delivered to Fannie Mae for purchase (or for securitization) by the property's value – normally defined as the lower of the sales price or appraised value. However, DU determines the LTV by dividing the submitted loan amount by the lesser of the sales price (Line a plus Line c in Section VII) or the appraised value (or the lender's estimated "value"). If the estimated value differs from the appraised value, you must correct the information in DU to reflect the appraised value and resubmit the loan application.

Data entry tip: You may enter the estimated value in the Property Appraised Value field in the Additional Data screen. If the appraised value is different than the estimated, correct the data and resubmit the loan application.

The maximum allowable LTV, CLTV, and HCLTV ratios are based on the type of mortgage, the method of amortization, the number of dwelling units, the occupancy status, and the property type.

Charts

The following charts apply to loans underwritten with DU:

- LTV Chart for Standard Fixed-Rate, ARM, and Balloon Mortgages
- LTV Chart for Mortgages Secured by Manufactured Homes
- LTV Chart for Community Lending Loans
- LTV Chart for MyCommunityMortgage Loans in DU
- LTV Chart for Flexible Mortgages
- LTV Chart for HomeStyle Renovation Mortgages
- LTV Chart for InterestFirst Mortgages
- LTV Chart for Negatively Amortizing ARMs
- Mortgage Insurance Coverage (Excluding Flexible Mortgages)
- Mortgage Insurance Coverage and Loan-Level Price Adjustment Requirements for Flexible mortgages
- Loan-Level Price Adjustment Requirements

LTV Chart for Standard Fixed-Rate, ARM, and Balloon Mortgages (1)

Excluding special mortgage products and mortgages secured by manufactured homes (2)

Purpose	Units	Product Type Fixed-rate, ARM, and Balloon (3)	LTV	CLTV	HCLTV
Principal Residence					
Purchase	1-2	All	95	95	100
	3-4	All	80	80	85
	Co-op	All	95	NA	NA
Construction (4)	1-2	All	95	95	100
Limited cash-out refinance	1-2	All	95	95	100
	3-4	All	80	80	85
	Co-op	All	90	NA	NA
Cash-out refinance	1-2	All	90	90	95
	3-4	All	75	75	80
	Co-op	All	85	NA	NA
Second Home					
Purchase	1	All	95	95	100
	Co-op	All	90	NA	NA
Construction (4)	1	All	95	95	100
Limited cash-out refinance	1	All	95	95	100
	Co-op	All	80	NA	NA
Cash-out refinance	1	All	90	90	95
Investment Property (5)					
Purchase	1-2	All	90	90	95
	3-4	All	75	75	80
Construction (4)	1-2	All	90	90	95
Limited cash-out refinance	1-2	All	90	90	95
	3-4	All	75	75	80
Cash-out refinance	1-2	All	85	85	90
	3-4	All	70	70	75

Footnotes:

- (1) Standard 40-year mortgages are available only on fixed-rate mortgages and certain ARMs.
- (2) For special mortgage products, including Community Lending loans, Flexible mortgages, HomeStyle Renovation mortgages, InterestFirst mortgages, negatively amortizing adjustable-rate mortgages, and for mortgages secured by manufactured homes, see the LTV charts on the following pages.
- (3) Balloon mortgages are not allowed in conjunction with ARM products or 40-year amortization terms.
- (4) Construction transactions are not permitted for units in a condominium project or for units in a cooperative project.
- (5) Investment properties may not secure cooperative share loans.

LTV Chart for Mortgages Secured by Manufactured Homes (1)

Purpose	Product Type Fixed-rate and 7/1 and 10/1 ARMs	Loan Term ≤ 20 Years	Loan Term > 20 and ≤ 30 Years
		LTV/CLTV/HCLTV	LTV/CLTV/HCLTV
Principal Residence			
Purchase	All	95	95
Limited cash-out refinance	All	95	95
Cash-out refinances	All	65	NA
Second Home			
Purchase	All	90	90
Limited cash-out refinance	All	90	90

Footnote:

- (1) The following are not permitted with manufactured homes: Flexible mortgages, HomeStyle Renovation mortgages, InterestFirst mortgages, construction, construction-to-permanent transactions, leasehold estates, investment properties, and 40-year terms.

**LTV Chart for Community Lending Products (1)
Excluding MyCommunityMortgage**

Products	Purpose	LTV	CLTV (2)	HCLTV
Community Home Buyer's Program and FannieNeighbors	Purchase and Limited cash-out refinance	95	105	100
Fannie 3/2	Purchase and Limited cash-out refinance	95	105	100
Fannie 97(3)	Purchase and Limited cash-out refinance	97(4)	105	NA

Footnotes:

- (1) All loans must be fully amortizing fixed-rate mortgages with a minimum term of 15 years and a maximum term of 30 years secured by one-unit principal residences. All borrowers must occupy the property and cannot own other residential property. The following are not permitted on Community Lending products: Flexible mortgages, HomeStyle Renovation mortgages, InterestFirst mortgages, temporary buydowns, and 40-year terms.
Note: When a Community Lending product is secured by a manufactured home, the loan must comply with all manufactured home policies including the LTV/CLTV/HCLTV ratios.
- (2) The CLTV may exceed 95% up to a maximum of 100% if the mortgage is part of a Community Seconds transaction (or up to 105% if the program description or guidelines of the second mortgage provider address how the second lien is to be handled on the occurrence of a catastrophic event that requires the property to be sold). Subordinate liens, including Community Seconds, are not permitted with cooperative share loans.
- (3) The LTV is limited to 95% for cooperative share loans.
- (4) The LTV can exceed 95% if the mortgage being refinanced was initially originated as a Fannie 97 loan.

LTV Chart for MyCommunityMortgage Loans in DU(1)

Product	Purpose	Units	LTV	CLTV	
			Maximum	Minimum	Maximum(2)
MyCommunityMortgage	Purchase and Limited cash-out refinance	1	100	95	105
	Purchase Limited cash-out refinance	2	97	95	105
	Purchase Limited cash-out refinance	3-4	95	95	105
Community Renovation	Purchase Limited cash-out refinance	1	97	95	105
	Purchase Limited cash-out refinance	2	97	95	105
	Purchase Limited cash-out refinance	3-4	90	90	105

Footnotes:

- (1) Loans must be fully amortizing with a maximum term of 30 years and secured by 1- to 4-unit principal residences. There is no minimum loan term. Loans secured by 1- to 2-unit properties must be fixed-rate mortgages or certain 5-, 7-, or 10-year ARM Plans; loans secured by 3- to 4-unit properties must be fixed-rate mortgages. HELOCs are not permitted on MyCommunityMortgage loans. Except for Community HomeChoice, all borrowers must occupy the property and cannot own other residential property. The following are not permitted on MyCommunityMortgage loans: Flexible mortgages, InterestFirst mortgages, manufactured homes, cooperative units, and 40-year terms. Two- to four-unit properties may not be located in condominium or PUD projects. Lenders must have approval in their Master Agreements to originate and deliver MyCommunityMortgage loans.
- (2) The CLTV may exceed 95% up to a maximum of 100% if the mortgage is part of a Community Seconds transaction (or up to 105% if the program description or guidelines of the second mortgage provider address how the second lien is to be handled on the occurrence of a catastrophic event that requires the property to be sold). Subordinate financing, including Community Seconds, are not permitted with cooperative share loans.

LTV Chart for Flexible Mortgages (1)

LTV Range	Product Type Fixed-rate, 5/1, 7/1, and 10/1 ARM	Purpose	LTV	CLTV (2)	HCLTV (3)
LTV ≤ 95.00% with CLTV > 95.00% (e.g., 80/20, 95/5)	All	Purchase and Limited cash-out refinance	≤ 95	> 95 – 105	NA
LTV 90.00 – 95.00% (4)	All	Purchase	95	95	NA
LTV 95.01 to 97.00% (Flexible 97)	All	Purchase and Limited cash-out refinance	97	105	NA
LTV 97.01 to 100.00% (Flexible 100)	All	Purchase and Limited cash-out refinance	100	105	NA

Footnotes:

- (1) All loans must be fully amortizing, fixed-rate mortgages with terms not less than 15 years; 5/1, 7/1 or 10/1 ARMs, secured by one-unit, principal residences. All borrowers must occupy the property. The following are not permitted with a Flexible mortgage: financed mortgage insurance, Community Lending products, HomeStyle Renovation mortgages, InterestFirst mortgages, cooperative share loans, construction, construction-to-permanent transactions, manufactured homes, and 40-year terms.
- (2) If the CLTV is greater than 100%, the subordinate financing must be a Community Seconds loan. The program description or guidelines for the subsidized second mortgage must address how the second lien is to be handled on the occurrence of a catastrophic event that requires the property to be sold.
- (3) Home equity lines of credit are not permitted with Flexible mortgages.
- (4) Flexible mortgage guidelines are applied to purchase-money transaction with LTVs of 90 – 95% if the borrowers do not have 5% of their own funds to contribute to the transaction and the 5 – 10% down payment comes from acceptable Flexible sources. This Flexible mortgage transaction is treated the same as a Flexible 97 mortgage with regard to mortgage insurance coverage, loan-level price adjustments, and Special Feature Codes.

LTV Chart for HomeStyle® Renovation Mortgages (1)

Purpose	Units	Product Type Fixed-rate, ARM, and Balloon	LTV	CLTV	HCLTV
Principal Residence					
Purchase	1	Fixed-rate	95	105 (2)	100
	2	Fixed-rate	95	100 (2)	100
	1-2	ARM and Balloon	95	95	100
	3-4	All	80	80	85
	Co-op	All	95	NA	NA
Limited cash-out refinance	1-2	All	95 (3)	95 (3)	100
	3-4	All	80	80	85
	Co-op	All	90	NA	NA
Second Home					
Purchase	1	All	95	95	100
	Co-op	All	90	NA	NA
Limited cash-out refinance	1	All	95 (3)	95 (3)	100
	Co-op	All	80	NA	NA
Investment Property (4)					
Purchase	1	Fixed-rate 3/1 to 10/1 ARMs Balloon	80	80	95
Limited cash-out refinance	1	Fixed-rate 3/1 to 10/1 ARMs Balloon	80	80	95

Footnotes:

- (1) The following are not permitted with HomeStyle Renovation mortgages: Community Lending products, Flexible mortgages, InterestFirst mortgages, negatively amortizing adjustable-rate mortgages, manufactured homes, and 40-year terms. Lenders must have approval in their Master Agreement to deliver HomeStyle Renovation mortgages to Fannie Mae.
- (2) The CLTV may exceed 95% up to a maximum of 100% if the mortgage is part of a Community Seconds transaction (or up to 105% for one-unit properties, if the program description or guidelines of the second mortgage provider address how the second lien is to be handled on the occurrence of a catastrophic event that requires the property to be sold).
- (3) The borrower cannot receive any cash back at closing. If the borrower receives **any** cash proceeds from the closing, the loan is ineligible for delivery.
- (4) Investment properties may not secure cooperative share loans.

LTV Chart for InterestFirst™ Mortgages (1)

Purpose	Product Type Fixed-rate and ARM	LTV	CLTV	HCLTV
Purchase	Fixed-rate	95	95	100
	3/1 to 10/1 ARMs	90	90	95
Construction (2)	Fixed-rate	95	95	100
	3/1 to 10/1 ARMs	90	90	95
Limited cash-out refinance	Fixed-rate	95	95	100
	3/1 to 10/1 ARMs	90	90	95
Cash-out refinance	Fixed-rate	90	90	95
	3/1 to 10/1 ARMs	70	70	75

Footnotes:

- (1) All loans must be 30-year mortgages secured by one-unit, principal residences or second homes. The following are not permitted on InterestFirst mortgages: Community Lending products, Flexible mortgages, HomeStyle Renovation mortgages, temporary buydowns, manufactured homes, investment properties, balloon mortgages, units in a cooperative project, and 40-year terms. Lenders must have approval in their Master Agreements to deliver InterestFirst mortgages to Fannie Mae.
- (2) Construction transactions are not permitted for units in condominium projects.

LTV Chart for Negatively Amortizing ARMs (1)

Purpose	LTV	With subordinate financing		HCLTV
		LTV	CLTV	
Principal Residence				
Purchase	90	80	90	NA
Construction (2)	90	80	90	NA
Limited cash-out refinance	90	80	90	NA
Cash-out refinance	80	80	80	NA
Second Home				
Purchase	90	80	90	NA
Construction (2)	90	80	90	NA
Limited cash-out refinance	90	80	90	NA
Cash-out refinance	80	80	80	NA

Footnotes:

- (1) Manufactured homes and 40-year terms are not permitted with negatively amortizing adjustable-rate mortgages. Lenders must have approval in their Master Agreements to deliver negatively amortizing ARMs to Fannie Mae.
- (2) Construction transactions are not permitted for units in condominium projects.

Mortgage Insurance Coverage Excluding Flexible Mortgages (1)

Product Description	LTV							
	80.01 – 85.00%	85.01 – 90.00%		90.01 – 95.00%		95.01 – 97.00%(2)		97.01 – 100% (2)
Principal Residence		Apv/Elig*	Other*	Apv/Elig*	Other*	Apv/Elig*	Other*	
Fixed-rate Term > 20 ≤ 30 year w/out Community Seconds	12%	17% or 12% and .375	25%	25% or 18% and .75	30%	35% or 18% and 1.25	35%	NA
Fixed-rate Term > 20 ≤ 30 year with Community Seconds	12%	25%		30%		35% or 18% and 1.25	35%	
Fixed-rate term ≤ 20 year	6%	12%		25%		35% or 18% and 1.25	35%	
Cash-out refinances term > 20 ≤ 30 year	12%	25%		NA		NA		
Cash-out refinances Term ≤ 20 year	6%	12%		NA		NA		
Interest First mortgages	12%	25%		30%		NA		
ARMs Term ≤ 30 year	12%	25%		30%		NA		
7-year balloon mortgages	12%	25%		30%		NA		
MyCommunityMortgage	6%	12%		16%		18%		20%
Second Home and Investment Property								
Fixed-rate mortgages Term > 20 ≤ 30 year	12%	25%		30%		NA		NA
Fixed-rate mortgages Term ≤ 20 year	6%	12%		25%				
ARMs Term ≤ 30 year	12%	25%		30%				
7-year balloon mortgages	12%	25%		30%				
Manufactured Home – Principal Residence and Second Home								
Term > 20 ≤ 30 year	17%	30%		35%(3)		NA		NA
Term ≤ 20 year	12%	25%		30%				
Standard 40-Year Term – Principal Residence, Second Home, and Investment Property								
Fixed-rate and ARMs	12%	25%		30%		NA		NA

***Apv/Elig** refers to loans that receive an Approve/Eligible recommendation. The price adjustment that applies to the Lower-Cost MI option is noted in this column. **Other** refers to loans that receive any recommendation other than Approve/Eligible – including EA- -I, -II, and -III. For EA pricing, refer to your Expanded Approval contract.

Footnotes:

- (1) For mortgage insurance for Flexible mortgages, see [Mortgage Insurance Coverage and Loan-Level Price Adjustment Requirements for Flexible Mortgages](#).
- (2) If the LTV exceeds 95%, the loan must be originated according to Fannie 97 or MyCommunityMortgage guidelines.
- (3) Principal residence only.

Mortgage Insurance Coverage and Loan-Level Price Adjustment Requirements for Flexible Mortgages (1)

LTV	Approve/Refer			Refer with Caution (2)			
	MI Coverage	Price Adjustment	Special Feature Code (3)	MI Coverage	Price Adjustment	Special Feature Code (3)	
LTV to 80.00% and CLTV > 95.00% <i>With subordinate financing (e.g., 80/20, 70/30)</i>	NA	1.50%	446	NA	5/1 ARM	3.25%	446, 340
					Other	3.00%	
LTV 80.01 – 95.00% and CLTV > 95.00% <i>With subordinate financing (e.g., 90/10)</i>	18%	1.50%	446	18%	5/1 ARM	3.25%	446, 340
					Other	3.00%	
LTV 90.00 – 95.00% and CLTV ≤ 95% (4) <i>With or without sub financing</i>	18%	1.75%	206	35%	5/1 ARM	1.75%	340
	35%	.50%	206		Other	1.50%	
LTV 95.01 – 97.00% <i>With or without sub financing (Flexible 97)</i>	18%	1.75%	206	35%	5/1 ARM	1.75%	340
	35%	.50%	206		Other	1.50%	
LTV 97.01 – 100.00% <i>With or without sub financing (Flexible 100)</i>	25%	1.50%	412	35%	5/1 ARM	1.75%	340
	35%	1.00%	412		Other	1.50%	

Footnotes:

- (1) Mortgage insurance cannot be financed on Flexible mortgages. For ARMs, there may be an additional price adjustment. Refer to the [Loan-Level Price Adjustment Requirements](#) chart. For mortgage insurance coverage on other products, refer to the [Mortgage Insurance Coverage Excluding Flexible Mortgages](#) chart.
- (2) DU will identify certain loans with Refer with Caution recommendations as eligible for delivery with a loan-level price adjustment. The price adjustment for 5/1 ARMs is in addition to the standard ARM price adjustment that applies to ARMs with LTVs greater than 90%. The mortgage insurance coverage also applies to loans that receive EA-I, EA-II, and EA-III/Eligible recommendations. For the EA loan-level price adjustments and special feature codes, refer to the *Expanded Approval Eligibility Matrix* on eFannieMae.com and your Expanded Approval contract.
- (3) As with all loans, the lender must use the special feature code for loans underwritten with DU (127 or 214) upon delivery. In addition, if there is a Community Seconds subordinate lien, the lender must use Special Feature Code 118. For Flexible mortgages with the \$500 borrower contribution feature, lenders must use Special Feature Code 564.
- (4) The mortgage insurance coverage options and associated loan-level price adjustments also apply to Flexible mortgages with LTVs between 90 – 95% where the borrower lacks 5% of his or her own funds, and obtains the down payment from Flexible sources of funds.

Loan-Level Price Adjustment Requirements

Product Description	Special Feature Code	LTV Range					
		≤ 70.00%	70.01 – 75.00%	75.01 – 80.00%	80.01 – 85.00%	85.01 – 90.00%	90.01 – 100.00%
ARM	NA	NA	NA	NA	NA	NA	.25%(1)
7-year balloon mortgage	NA	NA	NA	NA	NA	NA	1.00%
2-unit property	NA	NA	NA	NA	NA	NA	.50%
Cash-out refinance	003	NA	.50%	.50%	.75%	.75%	NA
InterestFirst mortgage	NA	NA	NA	NA	NA	NA	.25%
Investment property	NA	1.50%	1.50%	2.00%	2.50%	2.50%	NA
Manufactured home	235	.50%	.50%	.50%	.50%	.50%	.50%
Standard 40-year term (MBS)	NA	.125%	.125%	.125%	.125%	.125%	.125%

Footnote:

(1) The .25% loan-level price adjustment also applies to MyCommunityMortgage 5/1 ARMs.

Mortgages with Subordinate Financing (excluding Flexible mortgages)

LTV Range	CLTV Range	Examples of Typical Financing Structures	Loan-Level Price Adjustment	Special Feature Code
65.01% – 75%	90.01% – 95%	75/20/5	.25%	339
75.01% – 95%	90.01% – 95%	80/15/5 and 90/5/5	.25%	338
75.01% – 90%	76.01% – 90%	80/10/10	NA	187
InterestFirst Mortgages 75.01% – 95%	75.01 – 95%	80/10/10	.25%	NA

Note: These price adjustments are not applicable for Community Lending mortgages with a Community Seconds loan; however, a loan-level price adjustment of .50% will apply to MyCommunityMortgage loans that have non-Community Seconds.

Loan-level price adjustments are cumulative. The price adjustments shown above are in addition to any applicable price adjustments related to mortgage insurance coverage. For example:

- 85% LTV cash-out refinance secured by an investment property: 3.25% total loan-level price adjustment (.75 + 2.50)
- 95% LTV adjustable-rate mortgage secured by a two-unit property: .75% total loan-level price adjustment (.25 + .50)
- 95% LTV fixed-rate mortgage secured by a two-unit property with 18% mortgage insurance: 1.25% total loan-level price adjustment (.50 + .75)
- 80% LTV, 90% CLTV InterestFirst mortgage: .25% total loan-level price adjustment

Chapter 2:
Underwriting Loans with
DU[®]

Chapter 2: Underwriting Loans with DU[®]

Introduction

DU analyzes borrower and property data from the loan application and credit report, and issues underwriting findings based on the data. This chapter describes the income, asset, and liability data that DU uses in performing its underwriting analysis and the follow-up processing steps that are required to satisfy DU's closing conditions.

Required data elements for loans submitted to DU

DU performs its underwriting analysis using either a complete loan application (Full 1003), or a reduced loan application (Quick 1003). The option to underwrite using a minimal amount of data in the loan application supports a point-of-sale environment, where quick (yet conditional) credit recommendations can be made using the information gathered during a borrower interview. When the loan application is submitted to DU with a limited data set, the lender and the borrower must complete a Form 1003 prior to closing, though Fannie Mae has fewer requirements for a complete loan application for loans underwritten by DU than for loans that are manually underwritten. The Form 1003 is not required at loan delivery; however, Fannie Mae requires that a complete loan application be maintained in the permanent loan file. See [Appendix A](#) on page 205 for a list of the data elements required for the Form 1003.

The lender may automatically copy liabilities to Section VI L from the credit report by selecting the auto-populate liabilities option at the time the credit report is ordered. When this option is selected, it is not necessary to obtain additional borrower disclosure for tradelines appearing on the credit report. However, any liabilities that do not appear on the credit report must be disclosed in Section VI L prior to the final submission to DU. Regardless of whether the lender uses the auto-populate liability option or enters liabilities in the loan application, the lender must obtain full disclosure from all borrowers of existing financial obligations, including total housing expenses.

The Additional Data screen has certain fields that must be accurately completed prior to submitting the loan to DU. Some of the data entry fields in this window include, but are not limited to, Community Lending data, appraised value, type of property, balloon indicator, and ARM data. For example, certain ARM information must be completed prior to submitting the loan for underwriting. See [Appendix B](#) on page 211 for a list of the data elements required for the Additional Data screen.

Lenders are not required to prepare a Form 1008 – Uniform Underwriting and Transmittal Summary – for loans underwritten with DU and subsequently delivered to Fannie Mae. However, the final Underwriting

Findings report and the Underwriting Analysis produced by DU must be maintained in the permanent loan file.

Using DU as a pre-qualification tool

Lenders may use DU as a pre-qualification tool as long as they have obtained written authorization from prospective loan applicants to request and receive a credit report. When using DU for loans where the address is unknown, or not yet determined, enter only the state information. Do not enter street address, city or ZIP Code information. If, however, a loan origination system (LOS) requires an entry for the street address, we request that you enter TBD in that field.

Data entry tip: For pre-qualifications, enter only the state in the address field in Section II.

DU will issue a message that the submitted address is not complete. This message should assist lenders in identifying their pre-qualification loans. Once it is finalized, the subject property address should be entered and the loan resubmitted to DU to determine the actual level of appraisal fieldwork required for delivery.

Note: Because many pre-qualifications are submitted before a property is selected by the borrower, there is a possibility that any modification to property type could result in changes to the underwriting recommendation and verification requirements. For example, if a property type is initially submitted as detached, and is subsequently changed to a different property type, the recommendation and verification documentation could change.

Data entry tip: A change in the property type field in the Additional Data screen may result in a change in the underwriting recommendation.

The underwriting recommendation

After each loan is submitted for underwriting analysis, DU displays the underwriting recommendation on the Loan List screen and on the Underwriting Findings report. Generally, the recommendation is defined in terms of DU's risk assessment of the loan and in terms of meeting the requirements of Fannie Mae eligibility. The recommendation will be one of the following: Approve/Eligible, Approve/Ineligible, Refer/Eligible, Refer/Ineligible, Refer with Caution, or Out of Scope.

In addition, for lenders participating in our EA/TPR™ initiative, the recommendation may be EA-I, -II, or -III/Eligible; EA-I, EA-II, or EA-III/Ineligible, or RWC-IV/Ineligible. Refer to the *Expanded Approval™ with Timely Payment Rewards® Lender Guide* for complete information.

A brief explanation of each recommendation is provided below. For more details about the recommendations and the required follow-up procedures, see [Chapter 5, Underwriting Recommendations](#), beginning on page 179.

- **Approve/Eligible** – Based on the data submitted to DU, the loan appears to meet both Fannie Mae’s credit risk and eligibility requirements.
- **Approve/Ineligible** – Based on the data submitted to DU, the loan appears to meet Fannie Mae’s credit risk requirements; however, the loan does not appear to meet Fannie Mae’s eligibility requirements.
- **Refer/Eligible** – Based on the data submitted to DU, the loan does not appear to meet Fannie Mae’s credit risk requirements. The loan appears to meet Fannie Mae’s eligibility requirements.
- **Refer/Ineligible** – Based on the data submitted to DU, the loan does not appear to meet Fannie Mae’s credit risk and eligibility requirements.
- **Refer with Caution** – DU has evaluated a combination of risk factors, including the LTV, housing and expense ratios, available assets, each borrower’s credit history, employment status, product type, property type, and purpose of the loan. Based on the data submitted, the loan does not appear to meet the credit risk requirements in DU. The credit risk represented by a Refer with Caution loan is statistically greater than the credit risk of loans that receive an Approve or Refer recommendation.

Loans that receive a Refer with Caution recommendation may or may not meet Fannie Mae’s eligibility requirements. The Underwriting Findings report will identify when the loan is ineligible and the reasons for the ineligibility.

- **EA-I, -II, -III/Eligible** – Based on the data submitted to DU, the loan appears to meet Fannie Mae’s expanded range of credit risk subject to appropriate EA price adjustments; the loan appears to meet Fannie Mae’s eligibility requirements.
- **EA-I, -II, -III/Ineligible** – Based on the data submitted to DU, the loan appears to meet Fannie Mae’s expanded range of credit risk subject to appropriate EA price adjustments; however, the loan does not appear to meet Fannie Mae’s eligibility requirements and, generally, is not eligible for delivery to Fannie Mae.
- **Refer W Caution/IV/ Ineligible** – Based on the data submitted to DU, the loan does not appear to meet the expanded credit risk requirements in DU and, generally, is not eligible for delivery to Fannie Mae.
- **Out of Scope** – DU does not contain the rules or models that are necessary in order to underwrite the product, borrower, or type of loan submitted. Therefore, DU will not produce messages (Findings, Verification, Observation, or Lender Guidance) or the Underwriting Analysis report for Out of Scope loans. DU will identify in a message the reason that a loan is Out of Scope.

Documentation requirements

For each loan, DU indicates the *minimum* income and asset verification requirements, credit-related documentation requirements, and the required level of property fieldwork necessary to complete processing of the loan file. These requirements are based on the specific risk factors present in each loan file and appear in the Underwriting Findings report in the section titled Verification Messages/Approval Conditions. See [Chapter 4, Underwriting Reports](#), beginning on page 167 for information on the reports provided by DU.

DU produces verification and appraisal requirements for referred loans as well as for loans recommended for approval. While loans receiving an Approve recommendation through DU will have the most streamlined processing requirements, referred loans will also benefit from processing requirements that are more streamlined than the documentation requirements described in Fannie Mae's *Selling Guide*, Part X, Chapter 1.

Note: For loans that receive a Refer or Refer with Caution recommendation, the lender must document the compensating factors as well as the rationale that was applied in the course of making the final decision to approve the loan outside of DU. If the factors supporting a lender's decision to approve the loan cannot be derived from the verifications listed in the Fannie Mae Underwriting Findings report provided by DU, the lender must request additional verifications or documentation as appropriate and include this information in the permanent loan file.

Reviewing the documentation

For all DU underwriting recommendations, including Approve/Eligible, lenders must apply due diligence when reviewing the documentation in the loan file to determine if there is any potentially derogatory or contradictory information *that is not part of the data submitted to DU* or if there is any erroneous information in the data submitted to DU (such as errors in the credit report data). Lenders are obligated to take action when contradictory, derogatory, or erroneous information would justify additional investigation or would provide grounds for a decision that is different from the recommendation that DU delivers. For example, if the credit report reflects a previous foreclosure but the information was not accurately mapped to DU, then the lender must consider this event when making its final underwriting decision. Furthermore, while DU offers a streamlined level of documentation, a more comprehensive level of documentation is always acceptable and in some instances should be required by the lender when circumstances in the loan file warrant it.

Age of documents

The age of documents for loans processed through DU is the same as for loans that are manually underwritten and described in Fannie Mae's *Selling Guide*, Part X, Chapter 1. Credit documents must be no more than 120 days old on the date the note is signed. However, if the property is new

construction, the documents may be up to 180 days old. When the age of the documents is greater than we allow, the lender must obtain updated written verifications.

Resubmission policy

Generally, the terms of the closed loan must match the terms of the final submission in DU. For example, occupancy type, product type, amortization, loan term, property type, loan purpose, sales price, and appraised value should reflect the loan as it was closed.

In addition, the verification documents should be reviewed and the verified values compared to the data used to underwrite the loan. It is possible that some loans will not require additional underwriting submissions as long as the requested documentation supports the information submitted to DU within the allowable tolerances listed below:

Interest rate: For approved fixed-rate loans (not subject to a temporary buydown) secured by principal residences or second homes, DU issues a message identifying the maximum interest rate (up to one percentage point above the submitted note rate) at which the loan can close without being resubmitted.

For ARM products, if an interest rate increase results in the total expense ratio increasing by more than two percentage points, the loan must be resubmitted to DU. The lender is responsible for determining that the start rate and all other ARM parameters are in compliance with Fannie Mae guidelines.

For fixed-rate and ARMs, if the interest rate decreases from that submitted to DU, the loan does not have to be resubmitted solely for the interest rate decrease. However, if the lower interest rate was the result of a permanent interest rate buydown, the loan application must be updated to reflect any change in discount points and closing costs.

Income: If verified income is less than the income on the loan application submitted to DU by more than 5% of the borrower's total income, the lender must update the income on the loan application and resubmit the loan to DU. For example, if the total monthly income on the loan application is \$5,000 and verified income (from paystubs or tax returns) is \$4,800, the loan does not have to be resubmitted. If verified income is greater than the loan application indicates, the data must be updated, and the loan must be resubmitted if the loan is subject to HUD median income limits (for example, as with Community Lending products). In all cases, including principal or secondary employment, the loan application must accurately indicate whether the borrower is self-employed.

Debts: If DU detects undisclosed debts (debts on the credit report that are not on the loan application) or if it detects discrepancies between the credit report payments and balances and those on the loan application, a verification message may require the lender to reconcile the data. If, upon reconciliation, the lender determines that the debts on the loan application are

inaccurate, the lender must resubmit the loan if the difference affects the total expense ratio by more than 2 percentage points.

If the lender discovers that the borrower has a debt that was not disclosed on the loan application, the lender must update the loan application and resubmit the loan to DU if the monthly payment will increase the total expense ratio by more than 2 percentage points. For example, upon review of the borrower's paystub, the lender discovers a payroll deduction for a loan the borrower did not disclose on the initial application. If this payroll deduction results in an increase to the total expense ratio that is greater than 2 percentage points, then the debt must be added to the loan application, and the loan must be resubmitted to DU.

Assets: If the Underwriting Findings report returns a message that a specific amount of assets must be verified, at a minimum, the lender must verify the specified amount.

Loan amount: For refinance transactions, we will allow the following tolerances to the loan amount.

- Increase: The loan amount may increase \$500 or up to 1% of the loan amount, whichever is less.
- Decrease: The loan amount may decrease 5% of the loan amount.

The loan amount tolerances are permitted provided the new LTV/CLTV does not result in a change to the amount of required mortgage insurance coverage, a different loan-level price adjustment, or a change to loan eligibility. For example, if a loan is underwritten at \$100,000 and the appraised value is \$120,000 (which equals 83.3% LTV), the actual loan amount can go up to \$100,500 (which equals 83.75% LTV) without requiring resubmission. On the other hand, if the original loan amount was \$108,000 (90% LTV), an increase without resubmission is not permitted because it would result in an LTV of 91%. The higher LTV requires different mortgage insurance coverage, and may result in the loan not being eligible for delivery.

Furthermore, the loan amount tolerance does not apply to Fannie Mae's requirements regarding the amount of cash back to the borrower on a limited cash-out refinance transaction. The lender must ensure that cash back to the borrower not exceed the lesser of 2% of the loan amount or \$2,000, with the exception of HomeStyle Renovation mortgages. On HomeStyle Renovation mortgages, the borrower may not receive any cash back on a limited cash out refinance transaction.

Note: The actual loan amount must be reported to Fannie Mae at loan delivery.

Limited waiver of representations and warranties

For certain loans submitted to DU, Fannie Mae will waive some underwriting representations and warranties that are typically required of the lender when it delivers loans to Fannie Mae. The terms of those limited waivers are outlined below.

If (i) DU recommends to approve a borrower's application for mortgage financing, and (ii) DU indicates that the related mortgage loan is eligible for sale to Fannie Mae, and (iii) an authorized DU licensee (the "Licensee") or another Approved Lender (as defined below) elects to sell that mortgage loan to Fannie Mae, Fannie Mae will not require such lender to warrant that the mortgage loan complies with the Fannie Mae *Selling Guide* requirements contained in DU (as reflected in the data fields included in DU and the reports generated by DU), with regard to the mortgage loan's eligibility for delivery to Fannie Mae and the application of the approval underwriting recommendation provided by DU as it pertains to the borrower's creditworthiness; provided, however, that:

- (a) all data pertaining to the applicable mortgage loan are complete and accurate, and all data on which the underwriting recommendation by DU was based remain unchanged as of the closing date for such mortgage loan or comply with the requirements set forth above relating to [resubmissions](#);
- (b) verification of all such data is provided with the loan file and such verification complies with Fannie Mae's requirements as set forth in Fannie Mae's *Selling Guide* and this Guide;
- (c) Licensee or such Approved Lender, as the case may be, uses the appropriate special feature codes, as specified in the delivery reporting requirements of Fannie Mae's *Selling Guide* (relating to the use of special feature codes) or as otherwise specified by Fannie Mae in this Guide. Special feature codes are required for all loans that receive an Expanded Approval Level I, II, or III recommendation, including those loans with Timely Payment Rewards feature. Without limiting the generality of the foregoing, Special Feature Code 127 must be used if the lender delivering the loan to Fannie Mae is the lender that underwrote the loan through DU. However, if the lender delivering the loan to Fannie Mae is not the lender that underwrote the loan through DU, then Special Feature Code 214 must be used;
- (d) Licensee or Approved Lender takes all appropriate action in response to the Verification Messages/Approval Conditions that appear in the Underwriting Findings report that DU produces with respect to the related mortgage loan application prior to the closing of the loan, with proper documentation in the loan file;
- (e) Licensee and any such Approved Lender comply with all other instructions and restrictions set forth in the most recent version of this Guide, as it may be supplemented or amended from time to time by Release Notes or otherwise; and
- (f) Licensee and Approved Lender comply with the requirements set forth in the *Selling Guide*, Part I, Chapter 2, Section 202.2 and Fannie Mae announcements that amend the *Selling Guide*.
- (g) Approved Lender reports the proper DU-assigned casefile ID on *Loan Schedule* (Form 1068 or 1069) or *Schedule of Mortgages* (Form 2005) at the time of delivery.

The foregoing waiver of underwriting representations and warranties *does not apply to*: (i) loans that receive a Refer/Eligible, Refer/Ineligible, or Out

of Scope recommendation; loans that receive a Refer with Caution recommendation (except certain eligible Flexible mortgages as described in [Flexible mortgages that receive a Refer with Caution recommendation](#) on page 50); and loans that receive an Approve/Ineligible recommendation, even if the reason for the ineligibility is covered by the lender's Master Agreement, unless the limited waiver is specifically granted in the Terms and Conditions for a particular variance; (ii) the eligibility and underwriting representations and warranties that apply to the property, appraisal or alternative property inspection as set forth in the *Selling Guide* and this Guide; (iii) government loans that are underwritten with DU and subsequently sold to Fannie Mae; and (iv) seasoned loans, as defined in Fannie Mae's *Selling Guide*, that are delivered to Fannie Mae. All seasoned loans that are delivered to Fannie Mae, including those that received an Approve/Eligible recommendation from DU, are required to meet our seasoned mortgage requirements as set forth in Fannie Mae's *Selling Guide*, Part III, Chapter 4, Section 403.

Notwithstanding the foregoing, all other representations and warranties that are set forth in the Mortgage Selling and Servicing Contract between Fannie Mae and Licensee (or between Fannie Mae and such Approved Lender) and in Fannie Mae's *Selling Guide* shall apply. Licensee's use of DU does not relieve Licensee (or any other Approved Lender) of any obligation set forth in such Mortgage Selling and Servicing Contract, in Fannie Mae's *Selling Guide* or in any other agreement between Fannie Mae and Licensee (or between Fannie Mae and any other Approved Lender), except (i) as expressly set forth in this section of this Guide with respect to Fannie Mae's limited waiver of representations and warranties, and (ii) as expressly set forth in the streamlined documentation, streamlined appraisal and alternative property inspection, and any DU recommendation or findings relating to streamlined documentation requirements, streamlined appraisal requirements, alternative property inspection requirements, and any similar requirements provided by DU. The grant of any such relief shall be subject to Licensee's satisfaction of the requirements set forth in paragraphs (a) through (f) of this section.

For purposes of this section, "Approved Lender" shall mean any mortgage lender that is a party to a Fannie Mae Mortgage Selling and Servicing Contract at the time the mortgage loan in question is sold to Fannie Mae.

Note: DU assigns a unique casefile ID for each casefile created in DO or DU. The casefile ID is specifically assigned to one casefile and should not be used for any other loan. The DU casefile ID, which is located on both the Underwriting Findings report and the Underwriting Analysis report, must be reported at the time of delivery regardless of the DU recommendation.

Income and employment processing

DU will base its income analysis on the income that is entered on the loan application. In some cases the lender may choose to exclude some of the income from the loan application if borrowers are able to qualify without it, such as bonus and commission income. However, for transactions that are

subject to income limitations, such as Community Lending loans, all income must be entered and documented.

Income from the requested documentation must support the amounts disclosed on the loan application within the allowable tolerances as described in the Guide. See [Resubmission policy](#) on page 93. Lenders must review the documentation for any unusual increases or decreases in income, and must determine that income used for qualifying is reasonably stable and is likely to continue at current levels.

Note: The level of income documentation offered by DU may not be adequate for every borrower and every situation. For example, it may be difficult for a lender to develop an accurate average monthly income from a current paystub for borrowers who work seasonal jobs, or for borrowers who work on a contract basis with several short-term jobs over the course of a year. In unique situations such as these, the lenders may have to obtain additional documentation, such as additional paystubs, W-2s, 1099s, or federal tax returns to support their calculation of income.

Furthermore, lenders may need to evaluate certain income and employment situations on a case-by-case basis. For example, lenders should use underwriting judgment to determine when future income can be included for borrowers – such as teachers and recent graduates – who have bona fide employment contracts for future employment. Another example is a case where a lender determines whether it would be appropriate to enter an independent contractor as a salaried borrower instead of self-employed. Lenders should carefully evaluate these types of situations and maintain all supporting documentation in the permanent loan file.

Income and employment verification

The following table explains the types of income and the verification options offered by DU. The amount and type of documentation required depend on DU's analysis of risk and the type of income the borrower earns, such as wage earnings, commission income, or self-employment. Verification messages will be provided on the Underwriting Findings report.

Income Type	Verification Requirements and Income Calculations
<p>Salary or Hourly Wage Earnings (Base Income)</p>	<p>A message will be issued for each current job requiring income and employment to be documented according to one of the following:</p> <ul style="list-style-type: none"> • verbal verification of employment (verbal VOE); • one paystub and telephone confirmation (or in lieu of telephone confirmation, an additional paystub dated within 30 days of closing); or • one paystub, telephone confirmation, and the previous year's W-2. <p>History of salary or hourly wage earnings: Borrowers must have been employed a minimum of 30 days in</p>

Income Type	Verification Requirements and Income Calculations
	<p>their current positions in order to use the income for qualifying purposes. Generally, lenders do not have to verify prior employment history unless the level of documentation specified in the Underwriting Findings report requires the previous year's W-2.</p> <p>Employment gaps: Explanations of employment gaps are not required for loans that receive Approve or Expanded Approval™ recommendations. For all other loans, the lender should assess the stability of the income. If there are previous employment gaps that are likely to recur and are likely to affect the stability of the income, the lender should factor these into the underwriting decision before approving the loan outside of DU.</p> <p>Income calculation: When using a verbal VOE to document income, the stated net income used for qualifying purposes must be reasonable based on the borrower's occupation, tenure, and title.</p> <p>When using a paystub to document income, the lender should calculate the borrower's base monthly income.</p> <p>Documentation requirements: For information on the documentation requirements for a verbal VOE, paystub, federal income tax return, W-2, etc., see Documentation and follow-up processing requirements on page 109.</p>
Bonus and Overtime	<p>DU will require bonus and overtime income to be documented according to one of the following options:</p> <ul style="list-style-type: none"> • verbal verification of employment (verbal VOE); • one paystub and telephone confirmation (or in lieu of telephone confirmation, an additional paystub dated within 30 days of closing); or • one paystub, telephone confirmation, and the previous year's W-2. <p>Income calculation: When using a verbal VOE, the stated bonus and overtime income used for qualifying purposes must be reasonable based on the borrower's occupation, tenure, and title.</p> <p>When using a paystub that reflects year-to-date bonus and overtime income, the bonus and overtime income must be annualized (divided by 12). If the lender chooses to average the bonus and overtime over a longer period of time, additional documentation must be provided. It may also be necessary to obtain additional information or documentation from the borrower to establish the stability of the bonus and overtime income.</p>

Income Type	Verification Requirements and Income Calculations
	<p data-bbox="641 258 1372 426">Data entry tip: Bonus and overtime income must be annualized (divided by 12) when the documentation only covers year-to-date earnings (YTD). For example, if the paystub is dated June 30 and the bonus and/or overtime income YTD is \$6,000, enter \$500 on the loan application.</p> <p data-bbox="620 457 1372 619">Documentation requirements: For information on the documentation requirements for a verbal VOE, paystub, federal income tax return, W-2, etc., see Documentation and follow-up processing requirements on page 109.</p>
Commission	<p data-bbox="620 640 1339 703">The level of documentation required for commission income will vary based on its percentage of employment income:</p> <p data-bbox="620 724 1063 751">Commission income less than 25%:</p> <p data-bbox="620 756 1372 892">If a borrower's commission income is less than 25% of his or her employment income (including base, commission, overtime, and bonus income), DU will require the income to be documented according to one of the following options:</p> <ul data-bbox="620 903 1372 1123" style="list-style-type: none"> • verbal VOE; • one paystub and telephone confirmation (in lieu of telephone confirmation, an additional paystub dated within 30 days of closing); or • one paystub, telephone confirmation, and previous year's W-2. <p data-bbox="620 1144 1096 1171">History of commission less than 25%:</p> <p data-bbox="620 1176 1323 1270">We do not have a stated minimum history requirement for commission income that is less than 25% of the borrower's employment income.</p> <p data-bbox="620 1291 1258 1318">Commission income equal to or greater than 25%:</p> <p data-bbox="620 1323 1372 1480">If a borrower's commission earning is equal to or greater than 25% of his or her employment income (including base, commission, overtime, and bonus income), DU will require the income to be documented according to one of the following options:</p> <ul data-bbox="620 1501 1242 1606" style="list-style-type: none"> • verbal VOE; • one year's personal federal income tax return; or • two years' personal federal income tax returns. <p data-bbox="620 1627 1388 1816">When the documentation level requires one or two years' personal federal income tax returns, the lender must obtain written permission from the borrower on IRS Form 4506 (Request for Copy of Tax Form) or IRS Form 4506-T (Request for Transcript of Tax Return) to request copies of federal income tax returns.</p> <p data-bbox="620 1837 1323 1869">Note: At least six months of commission income must be</p>

Income Type	Verification Requirements and Income Calculations
	<p>documented on the previous year's filed tax return for the income to be used for qualifying purposes.</p> <p>History of commission income equal to or greater than 25%: Generally, we do not have a stated minimum history requirement for commission income that equals or exceeds 25% of the borrower's employment income. However, if the documentation level provided by DU requires one or two years' personal federal tax returns, at least six months of commission income must be documented on the filed tax return(s) for it to be used for qualifying purposes.</p> <p>Income calculation: When using a verbal VOE to document income, the stated net commission income used for qualifying purposes must be reasonable based on the borrower's occupation, tenure, and title. When using a paystub, calculate an average monthly income based on the year-to-date commission.</p> <p>When using tax returns, the lender should calculate an average monthly income based on the documentation requested by DU. For example, if one year's tax return is requested, and the income reported on the filed tax return reflects only six months of commission income, divide the reported commission income by 12.</p> <p>Documentation requirements: For information on the documentation requirements for a verbal VOE, paystub, federal income tax return, W-2, etc., see Documentation and follow-up processing requirements on page 109.</p>
Employment by relative	<p>If the borrower is employed by a relative, the lender should carefully evaluate the borrower's earnings and determine whether the borrower owns any part of the business. Borrowers having a 25% or greater ownership interest in the business should be identified as being self-employed in Section IV, and may be required to provide federal income tax returns.</p>
Second job income	<p>A message will be issued for each borrower's second job and DU will require income to be documented according to one of the following options:</p> <ul style="list-style-type: none"> • one paystub and the previous year's W-2; or • two years' personal federal income tax returns. <p>History of second job employment: The borrower must have a 12-month history on all second jobs in order to include the income in DU for qualifying purposes. DU will check in Section IV for the 12-month history and, if it is less than 12 months, the system will issue a message that the income must be removed from DU. Income should be calculated based on an average of the paystub and W-2 earnings</p>

Income Type	Verification Requirements and Income Calculations
	<p>or the tax returns, as applicable.</p> <p>The income from second jobs must be included in the Base Income field in Section V for the income to be included in the qualifying ratios.</p> <div data-bbox="630 390 1377 499" style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: The second job income amount must be included in the Base Income field in Section V to be considered by DU.</p> </div> <p>Documentation requirements: For details on the documentation requirements for a paystub, federal income tax return, W-2, etc., see Documentation and follow-up processing requirements on page 109.</p>
<p>Self-employment income</p>	<p>We consider any individual self-employed who has a 25% or greater ownership interest in a business. As described in the <i>Selling Guide</i>, Part X, Chapter 5, the lender should analyze each of the following factors before approving a mortgage for a self-employed borrower:</p> <ul style="list-style-type: none"> • the stability of the borrower’s income; • the location and nature of the borrower’s business, the demand for the product or service offered by the business, the financial strength of the business, and the ability of the business to continue generating sufficient income to enable the borrower to make the payments on the requested mortgage; and • the marketability of the property that is secured for the mortgage as a private residence (rather than as the location of a business), since the property could be the source of repayment for the mortgage should the borrower’s business fail. <p>DU will require self-employment income to be documented according to one of the following options:</p> <ul style="list-style-type: none"> • verbal VOE; • one year’s personal federal income tax return; • two years’ personal federal income tax returns; or • two years’ personal and two years’ business federal income tax returns. Business tax returns do not have to be provided unless the business is a corporation, an “S” corporation, or a partnership. <p>In addition, the lender must obtain written permission from the borrower on IRS Form 4506 (Request for Copy of Tax Form) or IRS Form 4506-T (Request for Transcript of Tax Return) to request copies of federal income tax returns.</p> <p>Note: At least six months of self-employment income must be documented on the previous year’s filed tax return for the income to be used for qualifying purposes.</p>

Income Type	Verification Requirements and Income Calculations
	<p>History of self-employment: Generally, borrowers must have been self-employed for at least one year. If tax returns are required by DU, at least six months of self-employment income must be reported on the previous year's filed tax return to use the income for qualifying purposes.</p> <p>If the borrower has not been self-employed for at least one year, and the lender elects to underwrite the loan, the lender must confirm that the borrower is in the same line of work, and the borrower must be able to document a reasonable probability of success based on market feasibility studies and pro forma financial statements for the business. The lender must carefully analyze the following factors: the borrower's training and experience, the location and nature of the business, and the demand for that type of business in the area. If the self-employment does not meet the above guidelines, the lender must remove the income from the application and resubmit the case for underwriting.</p> <p>Income calculation: When using a verbal VOE, the lender must determine that the amount of stated net income is reasonable based on the type of business and the borrower's tenure.</p> <p>When using tax returns, the lender should calculate an average monthly net income based on the documentation requested by DU. For example, if one year's tax return is requested, and the income reported on the filed tax return reflects only six months of self-employment income, divide the reported net self-employment income by 12.</p> <p>The lender may use Fannie Mae Form 1084 to compute an average monthly income, or the lender may use any other type of cash flow analysis that applies the same principles as our form. The lender must include a copy of its written analysis in the permanent loan file.</p> <p>Note: If DU requires two years of tax returns but the borrower has only been self-employed for one year, the lender must verify that the borrower has been self-employed for at least one year, and that at least six months of self-employment income was reported on the previous year's filed tax return, and there was one year of employment prior to the self-employment. In other words, at least two years of employment must be verified. Furthermore, the lender should carefully analyze the documentation and consider the borrower's previous experience and training to evaluate whether the income is stable and likely to continue. A requirement for more than one year of tax returns indicates that the loan represents a higher level of risk than that of a loan where less documentation is required. The lender should calculate the qualifying income on a 12-month average based on the self-employment income reported on the previous</p>

Income Type	Verification Requirements and Income Calculations
	<p>year's filed tax return.</p> <p>Documentation requirements: For information on the documentation requirements for a verbal VOE, paystub, federal income tax return, W-2, etc., see Documentation and follow-up processing requirements on page 109.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p>Data entry tip: Enter the "net income" from self-employment in the Base Income field in Section V.</p> </div>
<p>Other/non-employment income</p>	<p>Generally, income from sources other than employment must be verified according to the procedures in Fannie Mae's <i>Selling Guide</i>, Part X, Chapter 4, Section 402, and Fannie Mae announcements when the income is to be used for qualifying purposes. Non-employment income can be used for qualifying as long as it is verified and calculated by the lender. Other income should be entered in Section V as Other Income.</p> <p>Other Income DU offers a number of Other Income options listed below that may be selected in the loan application. Income sources that are not listed, such as tips, should be entered as Other Types of Income. Unless stated otherwise, qualifying income from the following sources should be verified according to Fannie Mae's <i>Selling Guide</i>, Part X, Chapter 4, Section 402.</p> <p>Note: Section 8 for Homeownership income can be used to qualify borrowers in conjunction with MyCommunityMortgage loans according to the lender's Terms and Conditions. Enter Section 8 as "Other Income". Lenders must use Special Feature Code 445 when delivering these loans.</p> <ul style="list-style-type: none"> • Alimony and/or child support income The required documentation for alimony, child support, and separate maintenance income for loans submitted to DU varies from Fannie Mae's standard requirements. For these types of income, a three-month history of receipt is required and must be documented. In addition, documentation that the income will continue for at least three years should be obtained. • Automobile/Expense Account Income • Boarder Income • Foster Care • Military Base Pay • Military Clothes Allowance • Military Combat Pay • Military Flight Pay • Military Hazard Pay • Military Overseas Pay • Military Prop Pay • Military Quarters Allowance

Income Type	Verification Requirements and Income Calculations
	<ul style="list-style-type: none"> • Military Rations Allowance • Military Variable Housing Allowance • Mortgage Credit Certificate (MCC) MCC will be allowed according to the requirements in the <i>Selling Guide</i>, Part X, Chapter 4, Section 402.25 and will be treated as income by DU. • Notes Receivable/Installment • Other Types of Income • Pension/Retirement Income • Real Estate, Mortgage Differential Income • Social Security/Disability Income • Trailing Co-Borrower Income Anticipated trailing co-borrower income is allowed subject to the guidelines and documentation requirements of the Fannie Mae <i>Selling Guide</i>, Part X, Section 402.26, except as otherwise indicated below: <ul style="list-style-type: none"> – Loans must receive an Approve/Eligible recommendation. Loans that receive an EA recommendation are not eligible. If a loan receives a recommendation other than Approve/Eligible, the lender must remove the trailing co-borrower’s anticipated income and resubmit the loan. – DU will not impose the total debt-to-income ratio, minimum reserves, and representative credit score required by the <i>Selling Guide</i>. <p>Note: For both DU-processed and manually-processed loans, the co-borrower’s anticipated income cannot exceed 33% of the total qualifying income.</p> • Trust Income • Unemployment/Welfare Income • VA Benefits (Non-education) <p>Level of verification: Income from the requested documentation must support the amounts disclosed on the loan application within the allowable tolerances as described on the Guide. See Resubmission policy on page 93. Lenders must review the documentation to determine if there are unusual increases or decreases in income and must ascertain that income used for qualifying is reasonably stable and likely to continue at current levels.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p>Data entry tips:</p> <ul style="list-style-type: none"> • Only actual employer information should be entered in Section IV. For example, do not enter “retired” or “homemaker” as the borrower’s current employer. • Any income from sources other than active employment should be entered as other income in Section V. </div>

Income Type	Verification Requirements and Income Calculations
	<ul style="list-style-type: none"> All military income (for example, base pay, military ration) can be combined and entered as base income in Section V. This does not apply to FHA or VA loans.
Nontaxable income	<p>The <i>Selling Guide</i> provides special consideration for regular sources of income that are nontaxable – such as child support payments, social security benefits, disability retirement payments, workers' compensation benefits, certain types of public assistance payments, food stamps, etc. The lender must verify that the particular source of income is nontaxable and that both the income and its tax-exempt status are likely to continue. The lender may develop an "adjusted gross income" for the borrower by adding an amount equal to 25% of the nontaxable income to the borrower's income (or more if the actual amount of federal and state taxes is greater than 25%). The adjusted gross income should be entered for the specific nontaxable income type for use in qualifying the borrower. Refer to Part X, Chapter 4, Section 402 for additional information about documenting and calculating the income.</p> <p>Note: Certain loan origination systems offer an automatic calculation of “adjusted gross income” when nontaxable income types are entered in the loan application. In order to use the adjusted gross income for qualifying purposes in DU, the lender must determine that the nontaxable income meets all of the requirements of the <i>Selling Guide</i> as noted above. If the lender determines that all requirements are not met, the income should be adjusted downward. Furthermore, DU does not provide any unique messaging identifying the use of adjusted gross income.</p>
Net rental income (other than the subject property)	<p>There are two methods you can use to submit net rental income to DU: You can either (1) manually enter the net rental income in Section V or (2) complete the REO data in the Full 1003 (or your LOS). If both methods are used, DU will use the net rental income from Section V and provide a message if there is a conflict of data.</p> <p>(1) Because DU does not require complete REO data, you can calculate the net rental income outside of DU for all rental properties (other than the subject property) and then enter the total amount (either positive or negative) in the Net Rental field in Section V for the appropriate borrower.</p> <p>(2) If you complete the full REO data on each rental property (other than the subject property), DU will preliminarily calculate the net rental income. DU uses the following formula:</p> <p>(gross rental income × 75%) – mortgage payment – insurance/maintenance/taxes/misc. = net rental income</p>

Income Type	Verification Requirements and Income Calculations
	<ul style="list-style-type: none"> • The lender should override DU’s preliminarily calculated net rental income if the lender’s calculation (based on the documentation above) is different from DU’s calculation. <p>The net rental income applies only to rental properties already owned by the borrower. For rental income on the subject property, see the Subject net cash flow section below.</p> <p>If the combined total net rental income for all rental properties is positive, DU adds the net rental income to the qualifying income. If the total is negative, DU treats the loss as a liability and includes it in the total expense ratio.</p> <p>Calculation and documentation of net rental income</p> <p>The calculation and documentation for net rental income as described in the <i>Selling Guide</i>, Part X, Chapter 4, Section 402, are the same for DU-processed loans as they are for manually underwritten loans except that DU requires only one year’s tax return (instead of two).</p> <ul style="list-style-type: none"> • Proposed rent – such as when borrowers will rent their current principal residence – must be supported by an appraiser’s opinion of market rent for that particular property. • Verify the net rental income or loss with the borrower’s most recent signed federal income tax return (Pages 1 & 2 and Schedule E of IRS Form 1040 (Schedule E). In addition, the lender must obtain written permission from the borrower on IRS Form 4506 (Request for Copy of Tax Form) or IRS Form 4506-T (Request for Transcript of Tax Return). The lender should analyze the borrower’s rental cash flow and calculate the net rental income (or loss), making sure that depreciation or any interest, taxes, or insurance expenses were added back to the borrower’s cash flow analysis. • A copy of the lease agreement(s) may be used as evidence of rental income only if the property is not listed on Schedule E because it was acquired subsequent to filing the tax return. • If the borrower has no history of receiving rental income and there is no current lease, the lender may rely on an appraiser’s opinion of market rent (<i>Single Family Comparable Rent Schedule</i> – Form 1007) or a <i>Small Residential Income Property Appraisal Report</i> – Form 1025. Net rental income will equal 75% of the gross rental income less the proposed principal, interest, taxes, and insurance payment (PITI). • If the borrower’s principal residence is a two- to four-unit property, you can use rental income from the principal residence to qualify the borrower. With the exception of subtracting the borrower’s principal mortgage payment from

Income Type	Verification Requirements and Income Calculations
	<p>the gross rental income, all other calculations and documentation requirements stated above apply.</p> <p>Note: If the total expense ratio submitted to DU includes the entire rental property payment (income from the rental property is not considered), documentation of net rental income is not required.</p> <div style="border: 1px solid black; padding: 5px; margin: 10px 0;"> <p>Data entry tips:</p> <p>When manually entering net rental income in Section V:</p> <ul style="list-style-type: none"> • Calculate the total net rental income from all rental properties (except the subject property) and enter the total positive or negative amount in the Net Rental field in Section V. • To use net rental income from a borrower's owner-occupied two- to four-unit property when the borrower is purchasing or refinancing a second home or investment property, enter the net rental income from the borrower's principal residence as Net Rental in Section V. <p>When complete REO data is entered:</p> <ul style="list-style-type: none"> • To override DU's calculation from complete REO data, enter the net rental income amount directly in the Net Rental field in the Full 1003, Section VI R. • If the borrower is purchasing a principal residence <i>and</i> is retaining his or her current residence as a rental property, show the current principal residence as Rental in the Property Disposition field and complete the Net Rental field in the Full 1003, Section VI R. </div> <p>To use net rental income from a borrower's owner-occupied two- to four-unit property when the subject loan transaction is to purchase or refinance a second home or investment property, enter the net rental income from the borrower's principal residence as Net Rental in Section V.</p>

Income Type	Verification Requirements and Income Calculations
<p>Subject net cash flow</p>	<p>The lender should calculate subject property net cash flow for two- to four-unit principal residences and all investment properties (those that are security properties for the subject mortgage). DU will not calculate the subject property net cash flow.</p> <p>Note: Although negative subject net cash flow values appear to reduce the gross monthly income in Section V, DU actually treats the negative value as a liability and includes it in the total expense ratio.</p> <div data-bbox="630 621 1377 726" style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: DU will not calculate the subject net cash flow. This must be calculated outside of DU and entered in Section V in the Subject Net h field.</p> </div> <p>Calculation and documentation for subject net cash flow The calculation and documentation of subject net cash flow is the same for DU-processed loans as it is for manually underwritten loans with the following exceptions: DU requires only one year’s tax return (instead of two) and DU does not require the Operating Income Statement (Form 216).</p> <ul style="list-style-type: none"> • If the borrower has a history of receiving rental income for the subject property, verify the net cash flow with the borrower’s most recent year’s signed federal income tax return – pages 1 and 2 and Schedule E. In addition, the lender must obtain written permission from the borrower on IRS Form 4506 (Request for Copy of Tax Form) or IRS Form 4506-T (Request for Transcript of Tax Return). The lender should analyze the borrower’s rental cash flow and calculate the subject net rental income (or loss), making sure that depreciation or any interest, taxes, or insurance expenses were added back to the borrower’s cash flow analysis. • If the borrower has no history of receiving rental income on the subject property, the gross rental income will be based on the lesser of an appraiser’s opinion of market rent documented with a <i>Single Family Comparable Rent Schedule</i> – Form 1007 or a <i>Small Residential Income Property Appraisal Report</i> – Form 1025, or on actual rent from a current lease agreement, if applicable. A copy of a current lease agreement may be used only if the property is not listed on Schedule E because the property was acquired subsequent to filing the tax return. <p>Calculating net cash flow: The subject net cash flow calculation will depend on whether the subject property is a two- to four-unit principal residence or an investment property. See below.</p>

Income Type	Verification Requirements and Income Calculations
	<ul style="list-style-type: none"> <li data-bbox="623 254 1377 558"> <p><i>Two- to four-unit principal residences:</i> The subject net cash flow is equal to 75% of the gross rental income. Enter this amount in Section V. It will be included in the total qualifying income. Do not subtract the PITI from the rental income, because the PITI is included in the total proposed mortgage payment and is considered in the qualifying ratio.</p> <p>Note: On MyCommunityMortgage three- to four-unit properties the subject net cash flow is equal to 65% of the gross rental income.</p> <div data-bbox="651 579 1377 722" style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: Do not enter a negative subject net cash flow value for two- to four-unit principal residences, because the entire PITI is already included in the qualifying ratio.</p> </div> <li data-bbox="623 751 1377 919"> <p><i>Investment properties:</i> If the subject net cash flow is positive, enter the amount in Section V. It will be included in the total qualifying income. If the cash flow is negative, enter the amount in Section V as a negative value. DU will include it in the total expense ratio calculation as a liability.</p> <div data-bbox="651 940 1377 1117" style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: If you choose not to include income from the subject property in the qualifying ratios for investment properties, enter the entire proposed PITI should be entered as a negative amount in the Subject Net Cash field in Section V.</p> </div> <p data-bbox="623 1146 1377 1276">Note: If the total expense ratio submitted to DU includes the entire subject property payment and income from the property is not considered, documentation of subject net cash flow is not required.</p>

Documentation and follow-up processing requirements

The following table shows the documentation and follow-up processing requirements that are required for each income type. While DU requests the minimum level of documentation required, the lender may elect to obtain a deeper level of documentation. For example, if DU requests a telephone confirmation, the lender may choose instead to obtain a current paystub.

Income Documentation	Follow-up Processing Requirements
<p>Verbal Verification of Employment (Verbal VOE) or telephone confirmation</p>	<p>Based on the characteristics of the loan and the risk profile of the borrower, DU may offer a verbal VOE or a telephone confirmation.</p> <p>Because the requirement for a verbal VOE is based on the terms of the loan, changes to certain loan characteristics may result in DU requiring a deeper level of documentation upon resubmission. For example, a verbal VOE may be acceptable</p>

Income Documentation	Follow-up Processing Requirements
	<p>for a loan with an LTV of 80%; however, a paystub may be required if the LTV increases.</p> <p>The lender should continue to provide the borrower's monthly income, as stated on the Form 1003, on the Loan Schedule (Form 1068 or 1069) or Schedule of Mortgages (Form 2005) submitted in connection with loan delivery or MBS pool deliveries.</p> <p>VOE requirements for hourly, salary, and commission income:</p> <ul style="list-style-type: none"> • To comply with the verbal VOE requirement, the lender must independently obtain a phone number and, if possible, an address for the borrower's employer. This can be accomplished by using a telephone book or directory assistance, or by contacting the applicable licensing bureau. The lender must contact the employer and confirm the borrower's current employment status within 30 days of the closing date. The conversation must be documented. It should include the name and title of the person who confirmed the employment, the date of the call, and the source of the phone number. The written documentation should also include the name and title of the person who performed the verification for the lender. • When DU requires a verbal VOE, the stated income of the borrower that is used to qualify for the loan must be reasonable based on the borrower's occupation, tenure, and title. If the lender is unable to determine the reasonableness of the income, the lender is encouraged to obtain at least one year of personal federal income tax returns. <p>VOE requirements for self-employment income:</p> <ul style="list-style-type: none"> • To comply with the verbal VOE requirement, the lender must independently obtain a phone number and address for the borrower's business and must document the source of the information and the name and title of the lender's employee who obtained the information. This can be accomplished by using a telephone book or directory assistance, or by contacting the applicable licensing bureau. • When DU offers a verbal VOE, the stated income of the borrower that is used to qualify for the loan must be reasonable based on the type of business and the borrower's tenure in this line of work. The stated income should be representative of the borrower's monthly "net income." If the lender is unable to determine the reasonableness of the income, the lender is encouraged to obtain at least one year of personal federal income tax returns.

Income Documentation	Follow-up Processing Requirements
	for Transcript of Tax Return).
Paystub	The paystub should be dated no earlier than 30 days prior to the initial loan application date and must include year-to-date (YTD) income covering a period of at least 30 days.
W-2	The lender must obtain a paystub for the current job and W-2s for all jobs held in the prior year.
Verification of Employment Form 1005 (VOE)	<p>A VOE with YTD income may be substituted for the verbal VOE, or paystub, or for the paystub and W-2. The VOE must include a minimum of 30 days YTD income. The VOE must contain prior year earnings if it is a substitute for the W-2.</p> <p>Lenders can calculate a monthly average income based on the current YTD earnings of base income; however, as noted above, bonus and overtime income should be annualized.</p> <p>Note: Any income marked “not likely to continue” on the VOE should not be entered into DU for qualifying purposes.</p>
Personal federal income tax returns	<p>Copies of tax returns that were filed with the IRS must be signed by the borrowers who filed the returns. All supporting schedules must be included. In addition, the lender must obtain written permission from the borrower on IRS Form 4506 (Request for Copy of Tax Form) or IRS Form 4506-T (Request for Transcript of Tax Return) to request copies of federal income tax returns as specified in the Underwriting Findings report.</p> <p>Commission income: The filed tax returns must include a minimum of six months of commission earnings for the income to be used for qualifying purposes. In addition, if commission income represents 25% or more of the commissioned borrower’s income, and it is more than 60 days from the date of the last filed tax return, obtain a current paystub or IRS Form(s) 1099 and confirm that current earnings support the income on the tax returns.</p> <p>For loans originated between January 1 and April 15, and the borrower has not yet filed his or her prior year’s tax return, the lender must determine if alternative documentation, including IRS Forms 1099 or W-2 from the previous year, is sufficient to document the self-employment income. Taking into consideration business expenses that are deducted from earnings, the lender should develop an average monthly net income for qualifying purposes based on the documentation requested in the Underwriting Findings report. Additionally, the lender must obtain a current paystub. If the commission income on the paystub does not support the commission income reported on the 1099 or W-2 from the prior year, the qualifying income should be adjusted accordingly.</p> <p>Self-employed income: The filed tax returns must include a minimum of six months of</p>

Income Documentation	Follow-up Processing Requirements
	<p>self-employment income for the income to be included.</p> <p>For loans originated between January 1 and April 15, and the borrower has not yet filed his or her prior year's tax return, the lender must determine if alternative documentation, including IRS Forms 1099 or W-2 from the previous year, is sufficient to document the self-employment income. Taking into consideration business expenses that are deducted from earnings, the lender should develop an average monthly net income for qualifying purposes based on the documentation requested in the Underwriting Findings report.</p> <p>In addition to obtaining IRS Forms 1099 or W-2, the lender must obtain copies of the filed income tax returns for the number of years indicated in the Underwriting Findings report (i.e., one or two years' returns).</p>
<p>Two years' business federal income tax returns</p>	<p>For certain higher risk transactions, DU may return a message requiring two years' business federal income tax returns, along with an additional message allowing the waiver of the business tax returns according to the policy in Fannie Mae's <i>Selling Guide</i>. However, business tax returns do not have to be provided unless the business is a corporation, an "S" corporation, or a partnership.</p>

Asset processing

DU will base its analysis on the market value of the assets entered on the loan application that it considers liquid. If DU requires assets to be verified, a verification message will identify the documentation requirements for each liquid asset listed on the application. In addition, a verification message will indicate the amount of assets that the lender is required to verify. In some cases, this message will include only the amount of funds needed for closing (and the amount of debts to be paid by closing). In other cases, it will include some level of reserves (or all reserves) in addition to funds needed for closing.

Lenders must document at a minimum the value of assets sufficient to cover the dollar amount specified in the message "*Assets totaling \$xxxx.xx must be verified.*" This may result in asset Verification Messages/Approval Conditions in the Underwriting Findings report for which the lender does not provide any documentation.

For example, assume the closing costs and down payment for a loan total \$8,000, and the following assets are entered on the loan application:

Checking Account	\$5,000
Retirement Funds	\$7,000
Stocks	\$10,000

In this example, DU issues a verification message for each asset (checking, retirement, and stocks), in addition to a message stating that “*Assets totaling \$12,000 must be verified.*” Based on its risk analysis, DU is requiring \$4,000 in reserves to be verified in addition to funds needed for closing. To comply with this requirement, the lender can verify any two of the three assets listed on the application. If the lender documents the checking account and the stocks (totaling \$15,000), the retirement account does not have to be verified to be in compliance with the verification messages.

Note: DU may recommend loans for approval that are marginally short of funds needed for closing; however, this does not relieve the lender of the requirement to verify all funds needed for closing (as indicated in a verification message). It is preferable to obtain full borrower disclosure of all available assets before the case is initially underwritten.

If the lender is unable to verify the amount of assets required in the verification message, the asset values must be updated and the loan must be resubmitted for underwriting.

Asset categories

DU recognizes two categories of assets: *liquid assets* and *non-liquid assets*. In its risk analysis, DU considers the amount of liquid assets, but does not consider the amount of non-liquid assets. Non-liquid assets do not have to be verified, and will not be identified in a verification message.

Asset Category	Asset Types
Liquid assets	DU considers the following assets liquid, and includes the value in the amount of funds available for closing and reserves: <ul style="list-style-type: none"> • Bond • Bridge Loan • Cash on Hand • Certificate of Deposit • Checking Account • Gift • Gift of Equity • Money Market Fund • Mutual Fund • Net Equity • Other Liquid Asset • Retirement Fund (<i>See next page</i>) • Savings Account • Secured Borrowed Funds • Stock • Trust Funds
Non-liquid assets	DU considers the following assets listed in Section VI A as non-liquid, and does not include the value in the amount of funds available for closing and reserves: <ul style="list-style-type: none"> • Cash Deposit on Sales

Asset Category	Asset Types
	<ul style="list-style-type: none"> • Net Worth of Business • Other Non-Liquid Asset

Asset types and verification

The following tables identify asset types that can be entered, along with documentation requirements for verifying each asset type. The amount and type of documentation required depend on the system's analysis of risk and the type of assets.

Depository assets

Depository Asset Types	Verification Requirements
<ul style="list-style-type: none"> • Certificate of deposit • Checking account • Money market fund • Savings account 	<p>A verification message will be issued for all depository assets requiring documentation per one of the following options:</p> <ul style="list-style-type: none"> • one monthly bank statement, or • two consecutive monthly bank statements. <p>Follow-up processing requirements:</p> <ul style="list-style-type: none"> • Monthly bank statements must be dated within 45 days of the initial loan application date. • Quarterly bank statements must be dated within 90 days of the initial loan application date, and the lender must confirm that the funds in the account have not been transferred to another asset account that is verified with more current documentation. • A Verification of Deposit Form 1006 (VOD) can be obtained in place of bank statements. <p>Satisfactory explanation and documentation should be provided for large deposits.</p>

Non-depository assets

Generally, non-depository assets must be verified according to the procedures in the *Selling Guide*. DU will specify the verification requirements for each non-depository asset in the Underwriting Findings report.

The required documentation will be based on the type of non-depository account and is described below:

Note: Satisfactory explanation and documentation should be provided for large deposits or increases, as applicable (i.e., bonds, stocks or trust fund accounts). If a borrower provides a quarterly statement, the lender must confirm that the funds in the account have not been transferred to another asset account that is verified with more current documentation.

Non-Depository Asset Types	Verification Requirements
Bond	Document the value of the bond with a current brokerage account statement or other acceptable documentation. Proof of liquidation is not required.
Bridge loan (liquid asset)	<p>Bridge loans are considered liquid assets. Enter the amount under Bridge Loan in Section VI A. Do not include the amount of the bridge loan in any other liquid asset. (For example, do not enter the amount of the loan both as a bridge loan and in a checking account, even if the loan funds have been deposited.)</p> <p>Follow-up processing requirements: Obtain copies of the bridge loan documents.</p> <p>Note: It may also be necessary to enter the bridge loan as a recurring liability in Section VI L with a corresponding monthly payment. See Bridge loan liability.</p>
Cash deposit on sales contract (earnest money)	<p>When cash deposit on sales contract (earnest money) is entered in Section VI A, DU does not consider it liquid. Therefore, in order to give the borrower credit for earnest money that is not already reflected in a liquid account, the lender must enter the earnest money amount as follows:</p> <ul style="list-style-type: none"> • If the earnest money check has not cleared the borrower's bank account, the amount can be included in a depository account such as a checking or savings account; or • If the earnest money check has cleared the borrower's bank account, the amount can be entered as an Other Credit in Section VII, where it is assumed to be verified. <p>Do not enter earnest money in a depository account and in Other Credit.</p> <p>Follow-up processing requirements: When cash deposit on sales contract is entered in Line I, Other Credits, in Section VII, DU will issue a message stating that if the deposit is used to make any part of the down payment that must come from the borrower's own funds, the source of funds for the deposit must be verified. Refer to the <i>Selling Guide</i>, Part X, Chapter 6, Section 603, for additional guidance.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p>Data entry tip: If the earnest money check has not cleared the borrower's account, the amount should be included in a checking or savings account. If the check has cleared and the amount of the earnest money is not already included in a liquid asset, enter the amount in Other Credits in Section VII. Do not enter the amount in both places.</p> </div>
Cash-on-hand	Except for MyCommunityMortgage loans, cash-on-hand is not an acceptable source of funds for conventional loans.

Non-Depository Asset Types	Verification Requirements
	<p>Note: See the MyCommunityMortgage section for details and requirements regarding cash-on-hand.</p>
<p>Gift</p>	<p>Gifts (or grants) are permitted for owner-occupied and second home purchase and refinance transactions. All gift funds, including grants, must be from eligible sources – a relative, domestic partner, fiancée, fiancé, church, municipality, or nonprofit organization – as outlined in Fannie Mae’s <i>Selling Guide</i>, Part X, Chapter 6, Section 603. In addition, for Flexible mortgages, a gift or grant may also come from the borrower’s employer or from a public agency.</p> <p>All gifts must be entered in the loan application – either in the Full 1003, Section II, as a source of down payment or in Section VI A as a gift. DU will issue a gift message indicating how the gift must be verified.</p> <ul style="list-style-type: none"> • When a gift is entered in Section VI A as a gift, the funds are included in available funds. It is important that the gift amount is identified separately as a gift even if the funds have already been deposited in a liquid asset account owned by the borrower (such as checking or savings account). The balance of the liquid asset account entered in the loan application must be adjusted accordingly to prevent duplicate entry of funds. For example, if the borrowers’ verified checking account reflects a balance of \$15,000, and \$5,000 of that amount was from a gift, the checking account balance should be adjusted to reflect \$10,000, and the \$5,000 should be entered separately as a gift. • When a gift is entered in Section II as a source of down payment, the funds are not included in the available funds. <p>Note: Gift funds are considered liquid only when the funds are entered as a gift in Section VI A.</p> <p>Some loan origination systems (LOS) may not provide a “gift” data entry option, or the gift entry may not map correctly to DU. (For example, the LOS may identify the gift as a checking account when the data is transmitted to DU.) The lender must ensure that gift information has been properly identified in DU.</p> <div style="border: 1px solid black; padding: 5px; margin: 10px 0;"> <p>Data entry tip: Enter the amount of gift funds in Section VI A as a gift. Do not include the amount in another liquid asset account.</p> </div> <p>Follow-up processing requirements: Gift verification requirements may vary depending upon the risk of the transaction, the loan terms, and whether the loan is a Flexible mortgage.</p>

Non-Depository Asset Types	Verification Requirements
	<p>Approve recommendations: DU offers streamlined gift documentation requirements for all loans that receive an Approve recommendation, with the exception of Flexible mortgages as noted below. A verification message will require documentation of the name, address, and phone number of the donor; the amount of the gift; the relationship of the donor to the borrower; and verification that the borrower received the gift funds prior to or at closing. The receipt of funds can be verified by providing a copy of the gift check, a copy of the HUD-1 Settlement Statement showing the credit for the funds received at closing, or evidence that the borrower deposited the funds. The lender does not have to obtain a signed gift letter.</p> <p>Referred loans and all Flexible mortgages: Fannie Mae’s standard gift requirements are applicable for loans that do not receive an Approve recommendation, and for all Flexible mortgages. For information about the gift requirements for Flexible mortgages, see Flexible mortgages on page 34.</p>
Gift of equity	<p>A gift of equity is permitted for most principal residence and second home purchase money transactions. The gift of equity should be entered in Section VI A, as Gift of Equity.</p> <p>The lender must confirm outside of DU that the borrowers have contributed at least 5% of their own funds to the transaction if the gift of equity is less than 20%.</p> <p>The maximum gift of equity is calculated as follows: $(\text{Down payment} + \text{closing costs} + \text{prepaids}) - \text{borrowers' 5\% contribution} = \text{maximum gift of equity}$</p> <div style="border: 1px solid black; padding: 2px; margin: 5px 0;"> <p>Data entry tip: Enter gift of equity in Section VI A.</p> </div> <p>Follow-up processing requirements:</p> <ul style="list-style-type: none"> • All recommendations: A gift of equity must always be documented with a <i>signed</i> gift letter. In addition, the gift of equity should appear on the HUD-1 Settlement Statement, a copy of which should be retained in the loan file. • Flexible mortgages: A gift of equity is not permitted on Flexible mortgages
Mutual fund	Document the value with a current brokerage account statement. Proof of liquidation is not required.
Net equity (from properties pending sale)	<p>When full REO data is entered, DU automatically calculates the estimated net equity from properties marked pending sale in Section VI R using the following formula:</p> $(\text{Present Market Value} \times 90\%) - \text{Amount of Mtgs. \& Liens}$ <p>However, because full REO data is not required, you can</p>

Non-Depository Asset Types	Verification Requirements
	<p>calculate the net equity outside of DU and enter the amount (positive or negative) as Net Equity in Section VI A.</p> <p>If net equity is calculated from data in Section VI R and is also entered in Section VI A, DU will use the amount from Section VI A.</p> <p>When the net equity is positive, DU will add the amount to the funds available for closing. When the net equity is negative, DU will subtract the amount from the funds available for closing.</p> <p>Follow-up processing requirements: A photocopy of the fully executed settlement statement is required.</p>
Net worth of business	<p>When net worth of business is entered in Section VI A, DU does not consider it liquid. If the borrower is using proceeds from the sale of his or her business, the net proceeds should be entered in a depository account, such as a checking or savings account.</p>
Other non-liquid asset	<p>Non-liquid assets such as automobiles and net worth of business owned do not have to be entered or verified, and as such will not be identified in a verification message.</p>
Other liquid asset	<p>Enter the value of personal assets that will be converted to a liquid asset (or sold) prior to closing. For example, enter as an other liquid asset the net cash value of life insurance, automobiles, or other personal assets that will be sold, or the amount of pending tax refunds that will be received prior to closing. A verification message will require evidence of the value of the asset and confirmation that the asset was converted to cash.</p> <p>Note: Some loan origination systems may not provide an asset type for other liquid assets, or the entry may not map correctly to DU. In such cases, assets that would otherwise have been entered as an other liquid asset should be included in a depository account, such as a checking or savings account, if the assets will be converted to cash prior to closing. Appropriate documentation should be included in the loan file.</p>
Proceeds from sold properties	<p>Proceeds from properties that have already been sold should be included in a depository account, such as a checking or savings account.</p> <div data-bbox="638 1635 1386 1709" style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: The proceeds from sold properties should be included in the borrower's liquid assets.</p> </div>
Retirement fund	<p>To account for withdrawal penalties and taxes, enter 70% of the vested amount of the account as the value of this asset. Refer to the <i>Selling Guide</i>, Part X, Chapter 6, Section 603. for complete information.</p>

Non-Depository Asset Types	Verification Requirements
	<p>Follow-up processing requirements: If these assets are needed to support the amount of funds required for closing and reserves, document with a recent depository or brokerage account statement. If used for closing, document the conditions under which the funds may be withdrawn.</p> <p>Note: If the retirement account allows for withdrawals only in connection with the borrower's employment termination, retirement, or death, the retirement account should not be entered.</p>
Secured borrowed funds	<p>Borrowers can borrow against an asset they own, such as a 401(k) account or real estate, according to the requirements of the <i>Selling Guide</i>, Part X, Chapter 6, Section 603. The amount of the secured loan should be entered as secured borrowed funds in Section VI A. The secured loan amount should be subtracted from the market value of the actual asset, and the net asset value should be entered in the appropriate field in Section VI A. For example, if the borrower has a vested value, less taxes and penalties, of \$30,000 in a 401(k) account and borrows \$10,000 against the 401(k), you should enter \$10,000 as secured borrowed funds and enter \$20,000 as retirement funds.</p> <p>Loans that are secured against a liquid asset owned by the borrower (such as a 401(k) or mutual fund) do not have to be entered as liabilities in Section VI L if the appropriate documentation is provided.</p> <p>Loans that are secured against real estate, or any other non-liquid asset, must be entered as liabilities in Section VI L.</p> <p>Note: When a retirement fund is used as security for the borrowed funds, 70% of the vested amount of the retirement fund less the amount of the secured loan should be entered in Section VI A as a retirement fund.</p>
Stock	Document the value of the stock with a current brokerage account statement or a photocopy of the stock certificate accompanied by a current dated newspaper list. Proof of liquidation is not required.
Trust fund	Trust funds should be documented in accordance with the instructions provided in the <i>Selling Guide</i> , Part X, Chapter 6, Section 603.

Credit processing

Before a loan is submitted to DU, a three-in-file merged credit report must be requested for all borrowers on the loan application. Beginning with Version

5.4, DU will process conventional loan applications that include borrowers who do not have traditional credit histories *as long as at least one borrower* on the application has traditional credit (including FICO scores) disclosed on the three-in-file merged credit report.

Special guidelines for loan applications that include borrowers without traditional credit

The credit reports for borrowers who lack traditional credit histories must state clearly that no credit history for that borrower has been found. For example, the credit report should contain a statement such as “Score not available due to lack of credit history,” “Subject does not have sufficient credit,” or “Score not available; no qualifying accounts present.” As in all cases, lenders must ensure that the credit report accurately reflects the borrower’s information. DU will return a message stating that the lender must verify the accuracy of the name, Social Security number, and current address of a borrower who lacks traditional credit to ensure that the credit report was correctly ordered and that the borrower truly lacks traditional credit. In other words, lenders must ensure that the credit agency did not erroneously report the lack of traditional credit because incorrect information was used when ordering the credit report.

To ensure that the overall risk assessment is appropriate for loans involving borrowers without traditional credit, DU will apply the following additional underwriting guidelines:

- The loan must be secured by a one-unit, principal residence.
- Purchase money and limited cash-out refinance transactions are eligible.
- Cash-out refinance transactions are not eligible.
- Income used to qualify may not come from self-employment.
- All borrowers must occupy the property.
- The borrowers with traditional credit histories must contribute more than 50% of the combined income used to qualify.

If the loan does not meet these guidelines, DU will return an Out of Scope recommendation.

Note: If the borrower who does not have traditional credit is obligated to meet any financial obligation, such as child support and alimony, the lender must independently verify that the borrower has an acceptable payment history.

Credit liabilities

Lenders can automatically copy the liabilities from the credit report directly to the loan application by using the auto-populate liabilities option in the DO/DU user interface. Lenders should determine whether their loan origination systems offer this option for use with DU. If the lender’s loan origination system does not provide this option, or if the lender elects not to

use the auto-populate liabilities option, the lender must manually enter all liabilities in Section VI L of the loan application.

Note: While lenders have the option of copying liabilities directly from the credit report to the loan application, this does not relieve the lender of the obligation to obtain full disclosure from all borrowers – including borrowers who do not have traditional credit – of all existing credit obligations. Any liabilities that do not appear on the credit report, such as monthly housing expenses for taxes, insurance, etc., should be disclosed in Section VI L prior to final submission for underwriting.

DU uses the liabilities from the loan application – not the debts from the credit report – to calculate the total expense ratio. To help ensure that all appropriate liabilities are included in the total expense ratio, DU performs a series of reasonableness tests comparing loan application balances and payments with the credit report balances and payments. If the values on the loan application are less than the values on the credit report by more than selected tolerances, the lender will be required to justify discrepancies between the two.

Using the auto-populate liabilities option

If the lender uses the auto-populate liabilities option **before** liabilities have been manually entered on the loan application:

- Open accounts with balances equal to or greater than \$100 with a monthly payment on the credit report will be automatically copied to Section VI L of the loan application.
- Closed accounts on the credit report are not automatically copied to the loan application. If the account has an outstanding balance, the lender must manually enter the liability in Section VI L for inclusion in the total expense ratio.

Data entry tip: Select the auto-populate liabilities option to automatically copy liabilities from the credit report to the loan application.

If the lender selects the auto-populate liabilities option **after** liabilities have been manually entered on the loan application:

- DU attempts to match any existing liability accounts listed on Section VI L of the loan application to the credit report liabilities by using a combination of account name and account number. Open accounts from the credit report that were not manually entered on the loan application will be automatically copied to the loan application.
- DU uses the information on the loan application to calculate the total expense ratio. If there is a discrepancy between the debts on the loan application and the debts on the credit report, lenders should update the loan application values with verified values (from either the credit report or other outside verification) if these values are needed to calculate accurate ratios.

Note: Regardless of when (or if) the auto-populate liabilities option is used, lenders should reconcile the debts on the loan application to the credit report.

If duplicate accounts or accounts that do not belong to the borrowers were copied to the loan application and included in the total expense ratio, lenders may omit these debts from Section VI L. Debts that are omitted will not be counted in the total expense ratio.

Credit report requirements

Lenders are required to request a three-in-file merged credit report from one of the credit information providers listed on our Web site, and must maintain a printed copy of the credit report used by DU in the permanent loan file. A DU observation message will identify all of the credit reports evaluated by DU during the loan submission.

A list of the credit information providers available for use with DU may be found at:

<http://www.efanniemae.com/sf/refmaterials/creditproviders/>

Lenders must also request credit scores for each borrower when they order the credit report. The credit scores we require in DU are produced from software developed by Fair Isaac Corporation (FICO[®]). The standard FICO credit scoring model, known as classic FICO, is available from the three major credit repositories: Equifax Inc., TransUnion, LLC, and Experian Information Solutions. Even though the FICO score is not an integral part of DU's risk assessment (DU performs its own credit analysis), we recommend that lenders and brokers use the most recent versions of the classic FICO scores in all of their mortgage transactions, including manually underwritten loans. As of the date of this writing, the most recent versions are:

- Equifax Beacon[®] 5.0,
- TransUnion FICO[®] Risk Score, Classic 04, and
- Experian/Fair Isaac Risk Model V2SM.

If you are uncertain as to whether you are receiving the most current classic FICO scores in your credit reports, you are encouraged to contact your credit agencies to request the most current versions.

DU evaluates characteristics within the credit report that research has proven to be predictive of mortgage default instead of relying solely on the credit scores as a measure of the borrower's creditworthiness. However, lenders are required to request the three credit scores in their three-in-file merged credit reports received through DU.

As stated above, at least one borrower must have traditional credit reported on the credit report. If one or two of the credit repositories do not contain any credit information for the borrowers who have traditional credit, the credit report is still acceptable as long as credit data is available from one repository, a FICO credit score is obtained from that repository, and the lender requested a three-in-file merged report.

If every borrower on the loan application lacks at least one credit score, the loan will receive an Out of Scope recommendation. With the exception of DU-only transactions, the loan must be manually underwritten outside of DU. An alternative credit history (nontraditional credit report) may need to

be provided for those borrowers who do not have sufficient credit files or credit scores.

Note: For all loans, including those that receive Approve recommendations, the lender is responsible for reviewing the credit report, as well as all credit information, to determine that the credit report meets Fannie Mae’s requirements, and that the data evaluated by DU was accurate. Furthermore, the lender must take all appropriate action in accordance with applicable State and Federal laws to confirm the legitimacy of each borrower’s identification when the credit report contains security or identification alerts, or when there are any other indications present that should be investigated by the lender to ensure the accuracy of the borrower’s identity. The lender is obligated to take appropriate action when information that was not considered by DU would result in a recommendation other than that returned by DU. For guidelines about errors in the credit report data, see [Chapter 5, Underwriting Recommendations](#), beginning on page 179.

Credit documentation

The following table lists documentation requirements for verifying credit-related items in the loan. (Generally, loans that receive Expanded Approval Levels I, II, or III will receive the same verification requirements as loans that receive an Approve recommendation.)

Credit-related Condition	Verification Requirements
Alimony, child support, and maintenance payments	<p>The total expense ratio calculation must include alimony, child support, and separate maintenance obligations only if the borrower is required to continue making the payments for more than ten months. If a monthly payment is entered in Section VI L, but the number of months left to pay is not entered, DU will automatically include the payment in the total expense ratio calculation.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p>Data entry tip: Enter alimony, child support, and maintenance payments in Section VI L under Additional Expenses.</p> </div>
Closed accounts	<p>Accounts that are reported as closed on the credit report will not be automatically copied to the loan application. DU may issue a message alerting the lender that there are closed accounts with material balances. When applicable, these accounts should be added to the loan application for inclusion in the total expense ratio calculation.</p>
Consumer credit counseling services	<p>DU does not identify when a borrower is participating in a consumer credit counseling service. The presence of consumer credit counseling service does not alter the underwriting recommendation. Whether the borrower has or has not completed his or her participation in the sessions before closing on the mortgage transaction is not relevant since it is the borrower’s credit history that is of primary importance. For additional information, refer to the <i>Selling Guide</i>, Part X, Chapter 8, Section 801.</p>

Credit-related Condition	Verification Requirements
<p>Contingent liabilities</p>	<p>Generally, lenders should comply with the documentation requirements outlined in Fannie Mae’s <i>Selling Guide</i>, Part X, Chapter 7, Section 702, for contingent liabilities that are not included in Section VI L or in the total expense ratio calculation.</p> <p>Co-signed loan, property settlement “buy-out,” mortgage assumption, court-ordered assignment of debt:</p> <p>Lenders should follow the requirements outlined in the <i>Selling Guide</i>, Part X, Chapter 7, Section 702.02 for contingent liabilities by documenting timely payment of the most recent 12-month period. Otherwise, the debt obligation should be included in the borrower’s total expense ratio. (DU cannot identify contingent liabilities; however, if the contingent liability is omitted from underwriting, it will be included in the message that identifies omitted accounts.)</p> <p>Lenders are responsible for the appropriate documentation even though DU may not specifically message.)</p> <p>Bridge (or swing) loan liability:</p> <p>Fannie Mae provides for exclusion of the monthly bridge loan payment and the associated mortgage payment (for the property on which the bridge loan is secured) from the total expense ratio calculation if certain criteria are met. The following data entry guidance is provided to ensure correct calculation of the borrower’s assets and ratios when the borrower has a bridge loan and meets the criteria in Fannie Mae’s <i>Selling Guide</i>, Part X, Chapter 7, Section 702:</p> <ul style="list-style-type: none"> • Do not enter the bridge loan as a liability. • If there is an existing mortgage (other than the bridge loan) on the associated property, enter that mortgage in Section VI L and mark it “Omit”. (The mortgage payment will not be included in the expense ratio.) • Enter the property associated with the bridge loan in Section VI R. Mark the property “Sold” in the Full 1003, or “Omit” in the Quick 1003, Section VI L. <p>When Bridge Loan is selected, DU will issue a specific message.</p> <p>Note: For instructions on entering a bridge loan as a liquid asset, see Bridge loan liquid asset.</p> <p>Loans secured by the borrower’s financial assets:</p> <p>Loans that are secured against a liquid asset owned by the borrower (such as a 401(k) or mutual fund) do not have to be entered as liabilities in Section VI L if the appropriate documentation described in the <i>Selling Guide</i> is provided.</p> <p>Loans that are secured against real estate, or any other non-liquid asset, must be entered as liabilities in Section VI L.</p>

Credit-related Condition	Verification Requirements
<p>Current primary housing expense</p>	<p>The borrower’s current primary housing expense must be included in the total expense ratio when the subject transaction involves a second home or investment property. (The current housing expense is not included for principal residence transactions because DU uses the proposed housing expenses to calculate the ratio.)</p> <p><u>For second home or investment property transactions:</u></p> <p>Enter the total current primary housing expenses in Section VII. Exception: in those cases where the borrower rents (vs. owns) his or her primary residence, enter the amount of rent the borrower pays in Section V.</p> <p>Note: The total current monthly housing expense consists of principal, interest, hazard insurance, real estate taxes, mortgage insurance, and homeowner’s association (HOA) dues, as applicable. If the mortgage payment amount does not include all monthly expenses, such as taxes, insurance, or HOA dues, you can either update the payment to reflect all expenses or you must enter these expenses as “Taxes” or “Other” in the “Other Liabilities” of Section VII, in which case you would annualize the monthly payment and enter the annualized amount as the balance.</p> <p>For information on entering data on mortgage liabilities, including those that will be paid off at or prior to closing, see Mortgages and HELOCs below.</p> <div style="border: 1px solid black; padding: 5px; margin-top: 10px;"> <p>Data entry tip: For second home and investment property transactions, you must ensure that the borrower’s total current housing expenses on his or her primary residence are reflected in Section VI L.</p> </div>
<p>Inquiries</p>	<p>Lenders should examine the inquiries to determine whether they represent potential sources of undisclosed credit. Keep in mind that the loan application must accurately reflect the borrower’s financial obligations. If new debt was obtained, the lender may need to correct the loan application and resubmit the case.</p>

Credit-related Condition	Verification Requirements
Installment debt	<p>When the auto-populate liabilities option is selected, installment loans that do not have a payment on the credit report will be copied to the loan application if the account has a balance. Lenders will need to enter a payment on the loan application, even if the account has a deferred payment option, such as those available with student loans or retail purchase accounts. The monthly payments of deferred accounts should be included in the total expense ratio calculation. Installment debts with ten or fewer payments remaining will not be included in the qualifying ratio.</p>
Job-related expense (Nonreimbursed employee expenses)	<p>Nonreimbursed employee expenses should be subtracted from total income, unless such expenses are automobile lease or loan payment, in which case they should be considered part of the borrower's recurrent monthly debt obligations. Lenders must develop a 24-month average of these expenses as instructed in Fannie Mae Announcement 03-13.</p> <div data-bbox="639 789 1411 963" style="border: 1px solid black; padding: 5px;"> <p><i>Data entry tip:</i> Nonreimbursed employee expenses, except automobile lease or loan payments, must be subtracted from the borrower's base income, and should not be entered as a recurring liability. Auto lease or loan payments must be entered as recurring monthly debt obligations.</p> </div>
Lease payments	<p>Automobile lease payments should always be included in the total expense ratio calculation, without regard to the number of months remaining on the lease. Because loan origination systems and credit agencies may not properly convey lease accounts to DU, lenders should exercise care when reconciling liabilities to determine that lease accounts have been properly identified in DU.</p>
Mortgage liabilities, including home equity line of credit (HELOC)	<p>Information on existing mortgages should be reflected in Section VI L, and either identified with the property lien indicator or matched to the property in the Schedule of Real Estate Owned (REO). For information on using the property lien indicators and completing the Schedule of REO, see REO processing on page 133.</p> <p>Mortgages that will be – or have been – paid off, should reflect the mortgage balance and should be marked Paid by Close or Omit, as applicable.</p> <p>For second home and investment transactions, the borrower's current primary housing expenses must be reflected in Section VI L and must include all applicable housing expenses, such as hazard insurance, real estate taxes, mortgage insurance, and homeowner's association dues. See Current primary housing expense section on page 125.</p> <p>The monthly payment on a subordinate lien secured by the subject property must also be entered in Section V, Proposed Combined Housing Expenses, as Other Financing (P&I).</p> <p>For details on entering new and existing subordinate liens,</p>

Credit-related Condition	Verification Requirements
	<p>including drawn and undrawn HELOCs, see Subordinate liens on page 70.</p> <div style="border: 1px solid black; padding: 5px;"> <p>Data entry tips: Mortgages secured by properties that are Pending Sale should be marked Paid By Close. If you are not entering complete REO data, calculate the net equity outside of DU and enter it as a Net Equity asset in Section VI A. Mortgages secured by properties that are Sold should be marked Omit.</p> <p>If mortgages are entered in the Quick 1003, use appropriate indicators. If entered in the Full 1003, match liabilities to properties from Schedule of REO. Account owner and property owner must be the same.</p> <p>For second home and investment transactions, make sure the borrower's total current primary housing expenses is reflected in Section VI L.</p> </div>
Omitted accounts	<p>Supporting documentation is required when a credit report liability with a balance greater than zero is omitted from the loan application.</p> <div style="border: 1px solid black; padding: 5px;"> <p>Data entry tip: Omit mortgages that are matched to Sold properties.</p> </div>
Out-of-date tradelines	<p>For loans that do not receive Approve recommendations, DU will list open accounts on the credit report with balances that have not been reported by the creditor within the last 90 days of the credit report date. A message will be issued recommending that lenders obtain updated balance and account history information for these accounts and factor this into their final underwriting decision.</p>
Possible non-applicant debts	<p>The Underwriting Findings report will list any debts that are identified as “possible non-applicant debts” on the credit report. If the debts are on the loan application, DU includes them in the back ratio but does not include them in the credit profile analysis. If these debts do not belong to the borrower, the lender may provide supporting documentation, remove them from the loan application, and resubmit the loan.</p>
Revolving accounts	<p>When the auto-populate liabilities option is selected, if there is an open revolving account on the credit report that does not have a monthly payment but has a balance greater than \$100, DU will calculate a minimum payment. The calculated monthly payment will be the greater of \$10 or 5% of the outstanding balance. Revolving debts with ten or less payments remaining will not be included in the qualifying ratio.</p>
30-day accounts	<p>30-day accounts are not included in the total expense ratio and, generally, should be marked Paid By Close in Section VI L. DU will add this to the amount of funds the borrower needs to close.</p>

Credit-related Condition	Verification Requirements
Unrated tradelines	For loans that do not receive Approve recommendations, DU may request verification of the payment history of unrated tradelines that appear on a credit report. Lenders may decide to obtain updated balance and account history information for these accounts and factor this into their final underwriting decision.
Unverified liabilities	<p>An unverified liability is defined as an account that was manually entered in Section VI L that is either not on the credit report or is not “matched” to an account on the credit report.</p> <p>For loans that do not receive Approve recommendations, independent verification of creditor balance, payment amount, and credit history of liability must be obtained if needed to substantially support the lender’s decision to approve the loan.</p>
Verification of mortgage payment or rental payment history	When a verification of mortgage or verification of rental payment history is required, DU will include the requirement in the Underwriting Findings report. This requirement is waived for some loans.
Undisclosed debts	<p>An undisclosed debt is defined as one that is on the credit report but not on the loan application. DU compares the balances and payments of the debts on the credit report with the debts on the loan application. If DU finds material differences, lenders are required to confirm that all debts from the credit report are included on the loan application. In addition, lenders must provide documentation to support the use of payments and balances lower than those on the credit report.</p> <p>Undisclosed debts may be identified in the Underwriting Findings report if they have a material impact on the case. Lenders are required to either add the debt to the loan application and to resubmit the loan if the debt affects the total expense ratio by more than the allowable tolerances or to provide documentation that supports the omission from the loan application. See Resubmission policy on page 93.</p>

Derogatory credit

The following table lists documentation requirements for derogatory accounts.

Derogatory Credit Condition	Verification Requirements
Duplicate public records	<p>Items that typically appear in the Public Records section of the credit report (judgments, bankruptcies, foreclosures, and tax liens) are often duplicated because the credit agencies may not attempt to merge items of this severe nature. As a result, these items may also appear in more than one verification message in the Underwriting Findings report.</p> <p>If it is clear from the credit report data that the items are duplicates (identical account numbers, date filed, and dollar amounts), the lender can disregard the duplicates and document the item once. However, if it is unclear from the credit report whether any of the items are duplicated, the lender should treat each item individually and obtain the required documentation for each item, as indicated in the verification messages.</p>
Judgments, garnishments, and liens	<p>Open judgments, garnishments, and all outstanding liens that are in the Public Records section of the credit report will be identified in the Underwriting Findings report, and must be paid off at or prior to closing. Documentation of the satisfaction of these liabilities, along with verification of funds sufficient to satisfy these obligations, must also be maintained in the permanent loan file.</p>
Late payments	<p>For loans that do not receive Approve recommendations, lenders should confirm the accuracy of the information with the borrower. Additional documentation should be collected if the lender determines it is necessary to justify an approval.</p>
Mortgage delinquencies	<p>DU applies the following guidelines to the processing of loans with mortgage delinquencies:</p> <ul style="list-style-type: none"> • If any borrower's credit report contains a mortgage tradeline that is 60 or more days past-due when the account was last reported by the creditor and the account was reported within the 12 months prior to the credit report date, the loan will receive a Refer with Caution recommendation (or RWC/IV for Expanded Approval loans) and will be ineligible for delivery. <p>This policy applies to all mortgage tradelines, including first liens, second liens, home improvement loans, HELOCs, and mobile home loans.</p> <ul style="list-style-type: none"> • If an account is reported on the credit report as a non-mortgage tradeline, and yet the account is listed on the loan application as a mortgage, DU will analyze the credit history of the tradeline as a mortgage. For example, if the credit report identifies an account as a revolving account, and the account is listed as a HELOC on the loan application, DU will evaluate the credit history of the account as a mortgage. Any late payments in the

Derogatory Credit Condition	Verification Requirements
	<p>credit report will be treated by DU as delinquent mortgage payments.</p> <ul style="list-style-type: none"> • With the exception of loans that receive an Approve recommendation, if there is a mortgage that (i) is not rated on the credit report, (i.e., if the current account status or manner of payment/MOP code is “U”); (ii) was not reported within 90 days of the credit report date; or (iii) is disclosed on the loan application but not reported on the credit report, DU will issue a message requiring the lender to confirm that the account is not two or more payments past-due as of the date of the application. If the lender determines that the borrower does have a mortgage that is past due by two or more payments, then the loan is not eligible for delivery to Fannie Mae. • Borrowers may not bring past-due mortgage accounts current prior to closing in order to circumvent our policy regarding past-due mortgages. However, the lender may apply some discretion with regard to the application of this policy if it determines <i>and documents</i> that the past-due account status was not the fault of the borrower (for example, if the mortgage servicer misapplied or lost the borrower’s payment). • Loans may receive a Refer recommendation due to excessive prior mortgage delinquency if the borrower has a mortgage tradeline on his or her credit report that has one or more 60-, 90-, 120-, or 150-day delinquency reported within the 12 months prior to the credit report date. Such loans that would otherwise receive an Approve recommendation will receive a Refer recommendation. The lender will be required to document the circumstances of the excessive late payment(s) and determine that the borrower is not likely to have a similar recurrence on a mortgage in the future. <p>The above policies will apply to all mortgage tradelines, including first liens, second liens, home improvement loans, HELOCs, and mobile home loans.</p>
Past-due, collections, and charge-off accounts	<p>For principal residence and second home transactions underwritten with DU, collections and chargeoffs totaling more than \$5,000 must be paid at or prior to closing.</p> <p>Note: For investment properties, individual accounts equal to or greater than \$250 and accounts that total more than \$1,000 must be paid at or prior to closing.</p>
Prior bankruptcy or foreclosure (including deed-in-lieu of foreclosure)	<p>Identification of bankruptcies in the credit report: DU applies the following guidelines to the processing of bankruptcies:</p> <ul style="list-style-type: none"> • If a bankruptcy was filed within the 24-month period prior to the credit report date, the loan will receive a Refer with Caution

Derogatory Credit Condition	Verification Requirements
	<p>recommendation (or RWC/IV for Expanded Approval loans) and will be ineligible for delivery to Fannie Mae.</p> <ul style="list-style-type: none"> • If the date filed is unknown but it appears that the bankruptcy was discharged within 24 months, then DU will return a Refer recommendation if the loan would have otherwise received an Approve recommendation. The lender must confirm that the bankruptcy was not filed within the most recent 24-month period. • If a bankruptcy was filed more than 24 months before the credit report date, the lender must confirm that the bankruptcy was discharged at the time of the loan application. (This applies to all recommendations.) • For loans that receive a Refer with Caution recommendation that are not ineligible for delivery, the lender should consider the prior bankruptcy when evaluating the loan. Lenders must determine that the borrower has sufficiently reestablished an acceptable credit history and consider the prior bankruptcy in light of all other risk factors and the layering of risk. • DU will ignore tradeline accounts that are reported with a bankruptcy status code or manner of payment/MOP code of “7” if there is at least one bankruptcy reported in a public record. In this scenario, we are assuming that the date filed and the date discharged in the public record are more accurate than the dates in the tradeline, i.e., specific filed and discharged dates do not exist in the tradeline. • If the bankruptcy is not reported in a public record, but a tradeline is reported with a bankruptcy status code, then the lender will need to verify the actual filed and discharged dates to determine that the bankruptcy meets the DU 24-month policy. <p>Identification of foreclosures (including deeds-in-lieu of foreclosure) in the credit report: DU applies the following guidelines to the processing of foreclosures:</p> <ul style="list-style-type: none"> • Mortgage accounts, including first liens, second liens, home improvement loans, HELOCs, and mobile home loans, will be identified as a foreclosure if there is a current status or manner of payment/MOP code of “8” – foreclosure, or “9” – collection or chargeoff. • If a foreclosure was reported within the 24-month period prior to the credit report date, the loan will receive a Refer with Caution recommendation (or RWC/IV for Expanded Approval loans) and will be ineligible for delivery to Fannie Mae.

Derogatory Credit Condition	Verification Requirements
	<ul style="list-style-type: none"> • If a foreclosure was reported more than 24 months before the credit report date, the existence of the foreclosure is acceptable provided there are no additional eligibility criteria applied to the loan. • Foreclosure laws vary by state and the time it takes to complete the process may vary by state. DU assumes that the date the foreclosure was reported in the tradeline is the date of the foreclosure sale or liquidation. The lender must confirm that all foreclosures are satisfied. • For all loans that receive a Refer with Caution recommendation that are not ineligible for delivery, the lender should consider the foreclosure when evaluating the loan. Lenders must determine that the borrower has sufficiently reestablished an acceptable credit history and consider the foreclosure in light of all other risk factors and layering of risk.
Repossessions	For loans that do not receive Approve recommendations, DU will advise the lender to obtain an explanation of the repossessions.

Other processing requirements

Real estate owned (REO)

Proper entry of real estate owned (REO) data is essential to the risk analysis and affects the validity of the underwriting recommendation. Traditionally, REO data was entered in the Schedule of Real Estate Owned in the loan application, and all mortgages and HELOC liabilities were matched to their corresponding properties. However, in lieu of entering complete REO data and performing the matching function, you may use certain indicators and other data fields as described below to provide DU with the appropriate information.

The Schedule of Real Estate Owned is available in the Full 1003 for customers that choose to enter complete data. The REO screen is not available in the Quick 1003.

Data entry in Full 1003 and Quick 1003

If you choose to match mortgage liabilities and properties in the Full 1003, or if your LOS sends REO data to DO/DU, you will not need to use the Subject Property Lien or Rental Property Lien indicators in Section VII. However, if you use the indicators and enter full REO data, DU will use the data from the indicators and return a message when the data is inconsistent. If you do not use the mortgage indicators, and you do not enter REO data, DU will count the mortgage payments in the borrower's total expense ratio.

Using Indicators and data fields

Using Mortgage/HELOC liability indicators

As stated earlier, in lieu of entering detailed REO data and matching mortgage and HELOC liabilities with their corresponding properties, lenders can use the Subject Property Lien and Rental Property Lien indicators to identify mortgage/HELOC liabilities. Using these indicators will instruct DU whether or not to consider the mortgage and HELOC liabilities in the borrower's total expense ratio.

- Click **Rental Property Lien** to identify mortgages and HELOCs that are secured by a rental property.
- Click **Subject Property Lien** to identify mortgages and HELOCs that are secured by the subject property. Use this indicator for refinance transactions, including construction-permanent loans.

You can click both indicators if they both apply to a particular mortgage or HELOC.

The following indicators in Section VI L are also very important and should be used with mortgages and HELOCs whenever applicable:

- Use **Paid By Close** to identify mortgages and HELOCs secured by properties that are pending sale, including mortgages that will be paid off

with proceeds from the refinance of the subject property. DU will continue to exclude these liabilities from the total expense ratio and from the LTV, CLTV, and HCLTV ratios.

- Use **Omit** to identify mortgages and HELOCs that were secured by properties that have since been sold. DU will continue to exclude these liabilities from the total expense ratio and from the LTV, CLTV, and HCLTV ratios, and will not consider the balances of these mortgages in the funds needed to close.

With the traditional entry of complete REO data, DU automatically calculates the net equity of properties pending sale and net rental income. When you use the indicators and data fields described above in lieu of complete REO data, you should calculate these amounts and enter them in the loan application.

- Use the **Net Rental** field in Section V in Monthly Income to manually enter net rental income (positive or negative).

The net rental income amount should reflect the total income or loss from all rental properties owned by the borrower, excluding the subject property. For example, if the borrower owns two rental properties and has a positive net rental income of \$500 on one property and a net rental loss of \$100 on the other, you would enter **400** in the Net Rental field. If the total calculation results in a negative amount (a loss), you should enter a negative amount in the Net Rental field. For example, if the calculation results in a net loss of \$100, you would enter **-100** in the Net Rental field. DU will consider negative net rental income as a liability.

Note: The Net Rental field should not include any rental income the borrower receives from the subject property or from a second home or vacation home. As a reminder, subject net cash flow must be calculated outside of DU and entered in the Subject Net Cash field in Section V.

- Use the **Net Equity** field in Section VI Assets to manually enter the net equity from properties that are pending sale.

You must calculate the net equity outside of DU and enter the amount (positive or negative) in Section VI A. When net equity is positive, DU adds it to the funds available for closing; when net equity is negative, DU subtracts it from the funds available for closing.

Data entry examples using indicators and data fields

The following five examples illustrate how to use the mortgage and HELOC liability indicators and other data fields, as applicable, in lieu of entering complete REO data in the Schedule of Real Estate Owned in the Full 1003.

Example 1:

Subject transaction: Borrower is purchasing a principal residence. She is selling her current principal residence, which has one mortgage and one HELOC. The estimated net equity from the pending sale of her current residence is \$25,000. Borrower also owns a rental property, which will be retained as a rental. The rental property has one mortgage and calculated net rental income of \$800.

Real Estate Owned by Borrower	Liabilities Screen				Income Screen	Assets Screen
	Rental Lien	Subject Lien	Paid By Close	Omit	Net Rental	Net Equity
Current principal residence to be sold has: <ul style="list-style-type: none"> • One mortgage and • One HELOC 			X			\$25,000
Rental property has: <ul style="list-style-type: none"> • One mortgage 	X				\$800	

Example 2:

Subject transaction: Borrowers are purchasing a principal residence. Their current principal residence, which has one mortgage and one HELOC, will be retained as a rental property, and has calculated net rental income of \$500.

Real Estate Owned by Borrower	Liabilities Screen				Income Screen	Assets Screen
	Rental Lien	Subject Lien	Paid By Close	Omit	Net Rental	Net Equity
Current principal residence to be retained as rental property has: <ul style="list-style-type: none"> • One mortgage and • One HELOC 	X				\$500	

Example 3:

Subject transaction: Borrower is refinancing his 4-unit principal residence, which has one mortgage and one HELOC. He is paying off his first mortgage and maintaining his current HELOC. Calculated net cash flow income is \$1,000.

Real Estate Owned by Borrower	Liabilities Screen				Income Screen	Assets Screen
	Rental Lien	Subject Lien	Paid By Close	Omit	Net Rental	Net Equity
Current principal residence to be refinanced has:					Do not enter an amount in Net Rental. Enter the \$1,000 in Subject Net Cash.	
<ul style="list-style-type: none"> • One mortgage and 	X	X	X			
<ul style="list-style-type: none"> • One HELOC 	X	X				

Example 4:

Subject transaction: Borrower is purchasing a second home. Borrower owns current principal residence, which has one mortgage. Borrower also owns two rental properties with one mortgage each. The combined net rental income for both rental properties results in a loss of \$300 per month.

Real Estate Owned by Borrower	Liabilities Screen				Income Screen	Assets Screen
	Rental Lien	Subject Lien	Paid By Close	Omit	Net Rental	Net Equity
Current principal residence has:						
<ul style="list-style-type: none"> • One mortgage 						
Rental property #1 has:					-\$300 (combined total)	
<ul style="list-style-type: none"> • One mortgage 	X					
Rental property #2 has:					(included in total)	
<ul style="list-style-type: none"> • One mortgage 	X					

Example 5:

Subject transaction: Borrower is purchasing a rental property. Borrower owns current residence, which has one mortgage and one HELOC. Calculated subject net cash flow is \$500.

Real Estate Owned by Borrower	Liabilities Screen				Income Screen	Assets Screen
	Rental Lien	Subject Lien	Paid By Close	Omit	Net Rental	Net Equity
Current principal residence has: <ul style="list-style-type: none"> • One mortgage and • One HELOC 						
Purchasing rental property					Do not enter an amount in Net Rental. Enter the \$500 in Subject Net Cash.	

Entering detailed REO data

If you choose to enter complete REO data in the online loan application, you must do so in Section VI R (the REO screen) in the Full 1003.

All mortgages and HELOCs that are auto-populated from the credit report are automatically identified in Section VI L in both the Full 1003 and the Quick 1003. In the Quick 1003, mortgages are placed in a section titled “Mortgage Liabilities (HELOC, Mortgage)” in Section VI L.

To match a mortgage or HELOC liability with its respective property, select the property from the data field provided in Section VI L. The data field in the Full 1003 is titled “If mortgage or HELOC, select property”. If the property does not appear in the list, enter the property address in the REO screen in the Full 1003.

Note: The Subject Property Lien and Rental Property Lien indicators are available in the Full 1003 as well as in the Quick 1003.

To enter data for additional mortgage liabilities in the Full 1003, click Insert More Liabilities. DU automatically refreshes the screen, and the selected liabilities move to the Mortgage Liabilities section. Conversely, if a non-mortgage liability incorrectly appears in the Mortgage Liabilities section, you can move it to the top of the screen by correcting the liability type.

Property Indicator field

The Property Indicator is required only when complete REO data is entered in Section VI L, REO screen, in the Full 1003. The following table illustrates the proper selections for each property:

Selection name	When to use the selection
Current Residence	Use this selection to identify the borrower's current principal residence except when the subject loan transaction is to refinance the borrower's current principal residence. (In which case, select Refi of Current Residence.)
Subject of the Loan	Use this selection to identify the subject property for a refinance or construction-permanent transaction of a second home, vacation home, or an investment property.
Refi of Current Residence	Use this selection to identify the subject property for a refinance or construction-permanent transaction of the borrower's current principal residence.
Not Applicable (or <blank>)	For properties that do not meet any of the conditions listed above, select Not Applicable or simply leave the Property Indicator field blank. For example, you would select Not Applicable for rental properties that are not the subject property.

Note: DU provides guidance on the correct selections for various REO properties while in the Full 1003 in the DU user interface.

Property Disposition

The Property Disposition field selections identified below are required if you complete the REO in the Full 1003. Use one of the following selections:

- **Sold:** At the time of the application the property has already been sold. Any sale proceeds should be included in a liquid asset. DU will not calculate net equity for Sold properties and will ignore any values in the risk analysis.

Note: Omit mortgages on properties entered as Sold; otherwise, DU will include the monthly payments in the total expense ratio.

Data entry tip: Omit mortgages on properties that are entered as Sold.

- **Pending Sale:** This applies to properties that are under contract at the time of the loan application that will close at or before the closing of the subject property. For properties that are pending sale, you can enter the Net Equity asset in Section VI A (the Assets screen). On the other hand, if you enter complete REO information in the REO screen in the Full 1003 and Net Equity is not entered as an asset, DU will calculate the net equity from the REO screen and include it in the borrower's available funds.

DU calculates the net equity based on the following formula, and considers the net equity in the borrowers' available funds:

$(\text{Present Market Value} \times 90\%) - \text{Amt. of Mtgs./Liens}$

The lender can override DU's calculation of net proceeds by entering the value in net equity in Section VI A.

Note: Select Paid By Close for mortgages secured by properties that are Pending Sale; otherwise, DU will include the mortgage payment in the total expense ratio.

Data entry tips: To override the automatic calculation of net equity for properties entered as Pending Sale, enter the amount of net equity in Section VI A. Mark mortgages as Paid By Close on properties that are entered as Pending Sale.

Rental: This applies only to rental properties and should not be used for the subject property. It should also be used when borrowers are purchasing a principal residence and will maintain their current residence as a rental property. DU calculates net rental income or loss based on the following formula:

$(\text{Gross Rental Income} \times 75\%) - (\text{Mtg. payments} + \text{Insur., Maint. /Tax/Misc.}) = \text{net rental income or loss}$

To override DU's calculation, use the Net Rental Income field in the complete REO screen or the Net Rental field in Section V. Enter the net rental income (either positive or negative) as calculated based on Schedule E of the borrower's federal income tax returns or the current lease agreement (use 75% of the gross rent and subtract PITI).

Note: If you entered complete rental information in the Schedule of Real Estate Owned in the Full 1003, DU will auto-populate both the Net Rental Income field in the REO screen and the Net Rental field in Section V calculated by DU.

If the net rental income is positive, it will be added to the borrower's qualifying income. If negative, the loss will be treated as a liability and included in the total expense ratio calculation.

If multiple rental properties are entered in Section VI R, DU will combine the rental income or loss on all properties for all borrowers and derive a "net" value for use in the ratio calculations. For example, if Borrower A owns a rental property that has net rental income of \$200 per month, and Borrower B owns a rental property that has a net rental loss of \$50 per month, the net rental income will be calculated as \$150. This is the value that will be used in the ratio calculation. If the loan's total net rental income is positive, it will be included in the income message on the Underwriting Findings report as belonging to the primary borrower.

Note: Values entered in the Gross Rental Income field in Section VI R will only be considered for rental properties and will be ignored if entered on the borrower's current residence or on a second home.

Data entry tips: In the Full 1003, to override the automatic calculation of net rental income for a rental property, enter an amount in the Net Rental Income field in Section VI R. If the borrowers' current residence is a two- to four-unit property, and the subject property is an investment property or second home, the net rental income from the borrowers' current two- to four-unit principal residence should be entered as Net Rental income in Section V.

When complete REO data is entered in the Full 1003, net rental income is considered only for rental properties and is ignored in the ratio calculation if it is entered for the borrower's current residence or for a second home.

- **Retained:** The borrower will retain ownership of the property after the closing of the loan. For example, "retained" applies to the borrower's current residence if the purpose of the loan is to refinance that residence. A retained property would also apply to a second home already owned by the borrowers. This field may also be used for rental property where rental income is not used to qualify the borrowers.

Data entry tip: It is acceptable to enter rental properties as Retained if no rental income is used in qualifying.

Note: Any amount in the Insurance, Maintenance, Taxes field will be included in the total expense ratio calculation if the Property Indicator field is blank. Do not enter tax and insurance values separately if these amounts are already included in the mortgage payment in Section VI R or in Section VI L.

Entering data for properties owned without mortgage liabilities

For properties that are owned free and clear (no mortgage liabilities), the lender can choose to enter the property information in Schedule of Real Estate Owned in the Full 1003 or enter the housing expenses in Section VI L. If the borrower owns a second home for which there are no mortgages, you must do one of the following:

- In the Schedule of Real Estate Owned in the Full 1003, complete all of the REO information for the second home, including the monthly insurance, maintenance, and tax information. This information will be included in the expense ratio calculation; or
- In Section VI L, Additional Expenses section, enter the monthly expenses for the second home and select Other Expense in the Expense Type field.

Details of transaction – data entry instructions

Interested-party contributions

Some closing costs and prepaid settlement costs are generally paid by the property purchaser, while other costs are the responsibility of the property seller. Other costs may be paid by either the property purchaser or the property seller. When any costs that are normally paid by the property purchaser are paid (indirectly or directly) by someone else, they are considered to be interested-party contributions. All contributions may be paid by any interested party to the property sales transaction, although Fannie Mae may impose limitations on the amount of the contributions.

All interested-party contributions should be entered in the online loan application – *including payments for items excluded from our contribution limits that are traditionally paid by the property seller on behalf of the borrower in a particular market.*

DU considers all interested-party contributions (including those entered in Line k, Borrower's closing costs paid by Seller, and those entered as Seller Credit under Other Credits) in its maximum contribution calculation. DU will return a message alerting the user when it appears the contributions exceed the maximum allowed based on the CLTV and occupancy. If the amount of contributions is in excess of the maximum allowed, for underwriting purposes, you must make a downward adjustment to the sales price of the property to reflect the excess contribution amount. Lenders must determine that all closing costs and contributions paid by interested parties meet Fannie Mae guidelines.

All closing costs (including prepaids) paid by – or on behalf of – the borrower should be entered in Line f.

Other credits

There are a number of credits that may be entered in Section VII as “Other” credits. DU will automatically total the amount of the credits and enter the total in Line l:

- Cash deposit on sales contract,
- Seller Credit (if preferred, seller credit may be entered in Line k, Closing Costs Paid by Seller, instead of under Other Credits),
- Lender Credit,
- Relocation Funds,
- Employer Assisted Housing,
- Lease Purchase Funds,
- Other, and
- Borrower Paid Fees.

DU performs many calculations and issues several specific verification messages based on the Other Credits selections. For example, DU considers the cash deposit on sales contract (when entered as an other credit) when calculating the borrower's minimum required contribution.

Note: Many loan origination systems do not offer the list of other credit types, and some lenders that use these systems manually enter the other credits as a text entry. DU is not able to distinguish the text that is entered as other credits through other loan origination systems; therefore, specific verification messages will not be issued, and the associated calculations will not be performed. Lenders are responsible for the accuracy of the information entered in Section VII and must confirm outside of DU that the credits do not exceed allowable limits and are in accordance with all Fannie Mae guidelines. Appropriate documentation must be provided.



Chapter 3:
**Streamlined Property Valuation and
Inspection Requirements**

Chapter 3: Streamlined Property Valuation and Inspection Requirements

Introduction

This chapter describes the streamlined property valuation and inspection requirements for loans processed through DU[®] as well as DU's required minimum property documentation and lender review requirements. Our complete property and appraisal requirements are contained in the *Selling Guide*. The property appraisal and inspection forms are available on eFannieMae.com.

Overview

The property component of DU provides lenders with streamlined property appraisal and inspection processes using alternative property valuation and report form options for most loans. DU is designed to reduce the time and expense of documenting property appraisals and performing the property review, while enabling lenders to manage the overall process in a more efficient manner.

The collateral assessment component of DU relies on the use of proprietary risk assessment techniques and automated property valuation models within the system to determine the necessary level of property fieldwork as well as streamlined report forms for use with loans processed through the system.

DU provides lenders with the tools to better manage the appraisal process. However, we hold lenders responsible for the selection of the appraiser; the ordering and review of the appraisal, property-related documentation and inspection; as well the quality of the appraisal and the inspection documentation.

Note: The section in Announcement 04-07 entitled “*Lender’s Analysis of the Contract For Sale and Sale History of the Subject Property*” clarifies Fannie Mae’s expectation of lenders in their review of appraisal reports and defines revisions to the underwriting policy to more specifically address the issue of property flipping. This information applies to DU-processed loans as well as manually underwritten loans.

Roles of the underwriter and appraiser

We consider an accurate property valuation and review to be one of the key elements that helps to ensure the prudent underwriting of mortgage loans. Fannie Mae holds the lender responsible for the accuracy of the appraisal or inspection and its assessment of the marketability of the property. Therefore, it is important for lenders and appraisers to understand their roles in the process.

The appraiser's role is to provide the lender with

- An accurate, adequately supported opinion of value; and/or
- A complete, accurate description of the property.

The underwriter's role is to

- Review the appraisal or the property inspection report to ensure that it is of professional quality and is prepared in a way that is consistent with our requirements;
- Analyze the property based on the appraisal or property inspection report; and
- Judge the property's acceptability as security for the mortgage requested in view of its value and marketability.

Traditional warranties

Lenders are responsible for the traditional warranties to Fannie Mae regarding the selection of the appraiser and the quality of the appraisal and property documentation for loans processed through DU. Because lenders are solely accountable for the performance of the appraisers they select, they should use well-qualified appraisers who have appropriate knowledge and experience for the types of assignments that lenders intend to refer to them. Fannie Mae requires lenders to use appraisers that are state-licensed or -certified (in accordance with the provisions of Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989).

We expect a lender to use an appraiser that not only has the knowledge and experience that is required to perform a professional quality appraisal for the specific geographic location and the particular property type for which the lender needs an appraisal, but also has the knowledge about, and access to, the necessary and appropriate data sources for the area in which the appraisal assignment is located.

The lender's management of the appraisal process is especially important for the streamlined property appraisal and inspection documentation offered for loans underwritten through DU. For example, an appraisal based on an exterior-only property inspection requires an appraiser to obtain data about the physical characteristics of the subject property. The appraiser must then exercise his or her professional judgment regarding the adequacy of that data to perform a reliable appraisal, instead of developing the information based on an interior property inspection. In such cases, it is critical for lenders to use well-qualified appraisers that have access to the appropriate data sources.

There are specific requirements for appraisals of manufactured homes. Refer to Fannie Mae Announcement 03-06 for complete details.

Entering the subject property data

The accuracy of the property address and the property type are vital to DU's collateral assessment. Following are guidelines for entering this data into DU. Users must ensure that their loan origination system transfers these data fields correctly to DU.

Standardized address

A "standardized" property address is a valid property address within our database. One of the key steps in DU's collateral assessment process is the ability to match a submitted property address to a "standardized" address. When a loan is submitted for underwriting, the collateral assessment component within DU evaluates the subject property address on the loan application and attempts to match that address to a list of standardized property addresses in our database. In the comparison process, the system will either locate the exact address, or a similar address, or will determine that there is no match within our database.

Guidelines for entering the subject property address

DU may be able to confirm that the submitted purchase price for a purchase money transaction or the lender's estimated value for a refinance transaction is acceptable for that loan transaction, and recommend either a property inspection or a streamlined appraisal. The proper entry of address data into DU is extremely important because inaccurate or missing address entries will result in the system determining that the loan transaction is ineligible for streamlined fieldwork and reporting.

In addition to the guidelines provided below, refer to [Appendix C, Guidelines for Entering the Subject Property Address in DU](#) on page 213, which includes pre- and post-directional abbreviations and street suffix abbreviations to help ensure that the subject property address is entered correctly.

Entering address data

- Place the house number at the beginning of the street address (if there is not a separate field for the house number).
- Enter either complete names (e.g., Avenue or Street) or the appropriate abbreviations provided in the following tables.
- Enter a valid street suffix in uppercase (e.g., AVE, PKWY, or TER). See [Standard address-related abbreviation tables](#) on page 214.
- Include apartment, suite, unit number, or letters after the street name if there is not a separate unit number field.
- Include the city, state, and ZIP Code of the subject property. For the state, enter the abbreviation recommended by the U.S. Postal Service.

- Do not use punctuation in addresses (e.g., periods, commas, colons, semicolons, slashes, and asterisks). Dashes are permitted if they apply to the street number or ZIP+4.
- Do not include the pound sign (“#”) for the unit number if the unit number is entered in the unit number field. (DU will automatically insert a # symbol in the address in the Findings and printed loan application.) *Do* enter a pound sign before the unit number if you are entering the unit number, together with the street number and name, all in one field.
- Do not include identifiers such as APT, BLDG, UNIT, or STE in the address or unit number fields.
- Include pre-directional abbreviations (e.g., 123 N Main St) and post-directional (e.g., 123 Broad Street NW) in the Street Name field. See the list below.
- Ensure accurate spelling and typing.

Property address matched to a standardized address

When DU locates an exact match, or what it considers to be a probable match, it will return a message identifying the standardized address, along with the census tract, that was used in the analysis to determine the fieldwork recommendation. (This message is in addition to the property fieldwork message that DU currently provides; however, this message will not appear for cooperative or two- to four-unit properties.)

Note: Because DU is using the standardized address to determine the property value and the fieldwork recommendation, the lender must ensure that the standardized address is, in fact, the correct address for the subject property.

The standardized address message that will appear in the Underwriting Findings report is:

DU returned the following standardized address and census tract for the subject property: _____.

This is the address that DU used in its property valuation and fieldwork recommendation. Regardless of the property fieldwork required by Desktop Underwriter, if this address is not valid for the subject property, the lender must obtain an appraisal reported on Form 2055 with an interior and exterior property inspection.

Property address not matched to a standardized address

If DU is unable to match the subject property to a standardized property address in our database, the system returns the following message:

Desktop Underwriter could not verify the submitted subject property address for this transaction. Fannie Mae will accept delivery of this case with an appraisal based on an interior and exterior property inspection reported on Form 2055 for single-family properties, or Form 2095 for cooperative properties. Alternatively, you can modify the subject address and resubmit to verify if the system can offer a more streamlined property fieldwork recommendation.

Incomplete property address

When a property address is incomplete, DU will return the following message:

The system could not determine a property fieldwork recommendation for this case because the submitted property address is incomplete. You can resubmit the case with a complete property address to receive a property fieldwork recommendation.

Entering address for a pre-qualification loan

When using DU for loans where the address is unknown, or not yet determined, enter the state information only. Do not enter any data in the following fields: street address, city, or ZIP Code. However, if your loan origination system requires an entry for street address, we request that you enter TBD in that field.

The system will then issue the following message acknowledging that the submitted address is not complete:

The system could not determine a property fieldwork recommendation for this case because the submitted property address is incomplete. You can resubmit the case with a complete property address to receive a property fieldwork recommendation.

We believe that this message will assist our customers in keeping track of their pre-qualification loans and help to eliminate any confusion as to what appraisal fieldwork and documentation are required until an actual address is entered. Always re-enter the subject address once it is finalized to determine the actual level of appraisal fieldwork required for delivery.

Entering property type

The property type is an important component for DU to analyze the overall level of risk, and to determine the level of property fieldwork. The property types in the loan application are listed in the DO/DU user interface under Subject Property Type:

- Attached
- Condominium
- Co-operative
- Detached Condo
- Detached
- High Rise Condo
- Manufactured Home
- Manufactured Home: Condo/PUD/Co-Op
- Planned Unit Development (PUD)

Note: If you use a loan origination system that does not support each of the property types listed in the DO/DU online loan application, you may not receive all of the benefits of DU's functionality that are specific to each property type.

DU will allow only one property type selection. While there may be various possible property combinations, for example, a detached cooperative unit, the following guidelines should be followed:

- Condominium must be selected when the condominium is an attached unit.
- Co-Operative must be selected regardless of whether the unit is attached or detached.
- Detached Condo should be selected to identify a site built, single-family home (not a manufactured home) that is in a condominium project. If Detached Condo is not available in your loan origination system, you must select Condominium.
- Manufactured Home must be selected when the property is a manufactured home, except when a manufactured home is in a condominium, PUD, or cooperative project. (In those cases, Manufactured Home: Condo/PUD/Co-Op must be selected). A manufactured home must be built (and installed) under the Federal Manufactured Home Construction and Safety Standards that HUD established in 1976, as they were in force at the time the home was manufactured. Fannie Mae does not consider other types of factory-built housing, such as modular homes, or other types of prefabricated housing as manufactured housing. (For additional requirement, see the *Selling Guide* and Fannie Mae Announcement 03-06.)
- Manufactured Home: Condo/PUD/Co-Op should be selected to identify manufactured homes that are located in a condominium, PUD, or cooperative project. If Manufactured Home: Condo/PUD/Co-Op is not available in your loan origination system, you must select Manufactured Housing.
- Planned Unit Development (PUD) must be selected regardless of whether the unit is attached or detached.

Appraisal and inspection recommendations and documentation requirements

The streamlined property valuation process and the streamlined report forms are among the benefits available for DU-processed loans. As part of its overall risk analysis, DU will recommend the appropriate level of property fieldwork documentation based on a number of factors which are described below.

Property fieldwork recommendations

DU returns the property fieldwork recommendation based on the data submitted. The recommendations may change when certain data is changed and the loan is resubmitted to DU. While we minimize the chances of the fieldwork recommendation changing, there are factors that could influence the property fieldwork recommendation.

Factors that may contribute to the fieldwork recommendation include, but are not limited to:

- Eligibility
- Standardized property address
- Purchase price
- Loan purpose
- Loan amount
- Appraised value (or lender's estimated value)*
- Occupancy
- Number of units
- Property type
- Refinance purpose
- Combined loan-to-value ratio

*The lender's estimated value is entered in the Appraised Value field.

A change to any of the above factors may result in a different property fieldwork recommendation.

Appraisal and inspection fieldwork recommendations

The system will recommend one of the following documentation levels for each eligible one-unit property (excluding manufactured homes and units in a cooperative project) processed through the system with a valid property address:

- Appraisal with interior and exterior property inspection reported on the Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055).
- Appraisal with exterior-only property inspection reported on either Desktop Underwriter Qualitative Analysis Appraisal Report (Form 2065*) or Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055), or
- Exterior-only property inspection reported on the Desktop Underwriter Property Inspection Report (Form 2075).

*Effective November 1, 2005, Form 2065 will be retired. For loans where DU recommended Form 2065, the lender must obtain, at a minimum, the March 2005 version of Form 2055 if the appraisal is performed on or after November 1, 2005.

When DU recommends Form 2075, Fannie Mae will rely on the property valuation performed by the system. In such cases, the message generated by DU will acknowledge that the system accepts the submitted purchase price for a purchase money transaction or the lender's estimated value for a refinance transaction as the value of the property for the specific transaction. An appraisal is not required for these transactions as long as the property does not have any apparent adverse physical deficiencies or conditions, or apparent adverse environmental condition, and the subject property conforms to the neighborhood. Therefore, the lender is not responsible for the

traditional warranties regarding the valuation of the property that is performed by DU.

One-unit investment properties are eligible for streamlined appraisals with exterior-only or interior and exterior inspections reported on Forms 2055 and 2065. Additionally, the Single Family Comparable Rent Schedule (Form 1007) is required. Fannie Mae's standard property documentation – the Small Residential Income Property Appraisal Report (Form 1025) – is required for two- to four-unit properties processed through the system.

Cooperative share loans are eligible for streamlined appraisals with exterior-only or interior and exterior inspections reported on the Desktop Underwriter Individual Cooperative Interest Appraisal Report (Form 2095).

Manufactured homes are not eligible for streamlined appraisals. The [Uniform Residential Appraisal Report \(Form 1004\)](#) and [Manufactured Home Appraisal Addendum \(Form 1004C\)](#) will be required. Fannie Mae Announcement 03-06 describes the guidelines for the selection of appraisers, identifies acceptable sources of manufactured housing data, and describes the property eligibility criteria for manufactured homes. Refer to the Announcement for complete details.

Note: With *Selling Guide Announcement 05-02*, Fannie Mae released eleven final appraisal report forms, which are dated March 2005. These final forms must be used for appraisals performed on or after November 1, 2005. DU messages will remind lenders that the March 2005 appraisal forms must be used beginning November 1, 2005.

DU messages related to excessive property valuation

DU will return messages related to excessive property valuation risk to assist lenders in managing property-related risk when certain loan characteristics exist with refinance transactions secured by one-unit properties (except cooperative units). One message alerts the user when the lender's estimated value appears to be excessive for the local market based on our proprietary collateral assessment models. Another message will alert the user when the risk characteristics of the loan correlate historically with excessive property valuations. Furthermore, two additional messages help identify transactions submitted to DU with subject property values that, according to a recent prior sale, appear to exceed the level of appreciation for the local market.

Excessive value message

This message helps identify refinance transactions submitted to the system where the lender's initial value estimate appears to be excessive for the local market. The intent of this message is to help our customers identify those refinance transactions that were submitted to DU with estimated values that appear to be excessively high based on market data and our predicted value. This message is provided to help our customers better understand and manage refinance transactions that have value estimates that may be excessively high; the presence of the message does **not** indicate that the loan is ineligible for delivery to Fannie Mae.

The Desktop Underwriter collateral assessment model indicates that the submitted value estimate for this (insert refinance or cash-out refinance) transaction may be excessive for the local market. The lender should carefully review the appraisal for this transaction.

DU will generate this message only when an estimated or appraised value appears to be excessive based on available market data. When the system generates this message, an appraisal with an interior and exterior inspection reported on Form 2055 is required. It is recommended that the lender take special care when reviewing the appraisal and underwriting the property for these transactions. The lender may also wish to implement additional quality control procedures.

Combination message for quality assurance and excessive value

DU will return the following quality assurance message as another tool to assist lenders in managing property-related risk when there is a combination of both inflated value risk and excessive value risk. For those loans, DU will generate the following new single combined message:

The Desktop Underwriter collateral assessment model indicates that the submitted property value estimate for this (insert refinance or cash-out refinance) transaction may be excessive for the local market. In addition, the risk characteristics for this transaction are consistent with loans Fannie Mae has historically found to contribute to inflated property valuations. The lender should carefully review the appraisal for this transaction.

Rapid appreciation message:

The Desktop Underwriter collateral assessment model indicates that the submitted property value estimate for this refinance transaction (or sales price for a purchase money transaction) appears to have a higher rate of appreciation as compared to the local market based on an analysis of a recent prior sale of the subject property. The lender should carefully review the appraisal for this transaction.

Combined rapid appreciation and quality assurance message:

The Desktop Underwriter collateral assessment model indicates that the submitted property value estimate for this refinance transaction appears to have a higher rate of appreciation as compared to the local market based on an analysis of a recent prior sale of the subject property. In addition, the risk characteristics for this transaction are consistent with those Fannie Mae has historically found to contribute to inflated property valuations. The lender should carefully review the appraisal for this transaction.

Note: The absence of any of the above messages does not indicate Fannie Mae's acceptance of the appraised value (either the estimated or actual value) entered for the property. Lenders continue to be responsible for the data entered and, when DU requires an appraisal, for the property appraisal representations and warranties

Overview of streamlined property report forms

We designed the DU property report forms to provide a concise format for presenting the appraiser's description of the property and, in the case of Forms 2055, 2065, and 2095, to provide a concise valuation analysis that leads to the opinion of market value. The DU report forms are also compatible for electronic transmission and computer-based analysis and review. For example, the forms feature a series of key questions for the appraiser to address in a convenient "yes/no" format versus the traditional open space for comments. An overview of each form follows. For viewing or reproducing these forms, go to eFannieMae.com at:

<http://www.efanniemae.com/sf/guides/ssg/>

Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055)

The Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055) is designed to streamline the property valuation process by offering an exterior-only inspection option, and a reduced level of appraisal report documentation for one-unit properties (including individual units in condominium and PUD projects). Form 2055 allows the appraiser to use the traditional quantitative sales comparison analysis with precise dollar adjustments in estimating a subject property value.

Desktop Underwriter Qualitative Analysis Appraisal Report (Form 2065)

The Desktop Underwriter Qualitative Analysis Appraisal Report (Form 2065) offers an exterior-only property inspection option and the use of a relative or qualitative sales comparison analysis (instead of the traditional dollar-adjustment quantitative sales comparison analysis that is required by our standard report forms and Form 2055). The qualitative sales comparison analysis enables the appraiser to analyze market data and report the results of his or her analysis in terms of value relationships between the comparable properties and the subject property without assigning an estimated dollar value to those relationships.

Note: Form 2065 will be retired effective November 1, 2005. For loans where DU recommended Form 2065, the lender must obtain, at a minimum, the March 2005 version of Form 2055 if the appraisal is performed on or after November 1, 2005.

Desktop Underwriter Property Inspection Report (Form 2075)

The Desktop Underwriter Property Inspection Report (Form 2075) is a property inspection report. It requires an exterior-only inspection of the subject property from the street by a state-licensed or -certified appraiser. Form 2075 is not an appraisal report.

When DU recommends Form 2075, we will rely on the property valuation performed by the proprietary automated property valuation model within the system. Lenders are not required to obtain an appraisal of the property for

the specific transaction processed through the system, unless the property inspection reveals apparent adverse physical deficiencies or conditions, apparent adverse environmental conditions, or that the subject property does not conform to the neighborhood.

Loan transactions and property types that are eligible to receive a recommendation for Form 2075 are:

- CLTV \leq 90%,
- One unit property,
- Purchase, no cash-out, limited-cash-out refinance transactions (including Community Lending, Flexible, Generic ARM, and InterestFirst mortgage products).

The following transactions and property types are not eligible to receive a recommendation for Form 2075:

- Two- to four-unit property,
- Investment property,
- Co-Operative unit,
- Manufactured Home,
- Manufactured Home: Condo/PUD/Co-Op
- Construction-permanent,
- Construction,
- HomeStyle[®] Renovation Mortgage, and
- Negatively amortizing ARMs.

Desktop Underwriter Individual Cooperative Interest Appraisal Report (Form 2095)

The Desktop Underwriter Individual Cooperative Interest Appraisal Report (Form 2095) enables approved cooperative share loan lenders to take advantage of DU's streamlined appraisal process and reduced documentation for one-unit cooperative interest properties. Form 2095 streamlines the traditional valuation approach and level of property fieldwork for cooperative properties, and provides the flexibility to report an appraisal based on either an exterior-only inspection of the property or an inspection of both the interior and exterior of the property.

Requirements for property documentation

Our alternative property valuation and reporting processes represent the minimum documentation requirements for loans processed through DU. A lender may elect to obtain only the minimum documentation we require, or it may require the appraiser to provide additional documentation for any reason. However, we require lenders to upgrade the property documentation to the next higher level under certain circumstances. For example,

- When DU recommends an exterior-only property inspection reported on Form 2075, the appraiser is required to comment on the conformity of

the subject property to zoning regulations and other properties in the neighborhood, the highest and best use of the property as improved, as well as on any apparent adverse physical deficiencies or environmental conditions. Lenders are required to obtain an appraisal with an interior and exterior inspection if the property does not conform to the neighborhood or if adverse physical deficiencies or environmental conditions were observed. Examples of this include a subject property that is significantly larger or smaller than the properties in the neighborhood, significantly older or newer than the properties in the neighborhood, or has apparent physical deficiencies requiring significant repairs.

- When DU recommends an appraisal with an exterior-only inspection reported on either Form 2055 or 2065, we require the appraiser to obtain sufficient information about the physical characteristics of the subject property from reliable sources. The appraiser's description of the physical characteristics of the property should be based on what he or she considers to be reliable data sources for the property and location. The appraiser is expected to use the same type of data sources that he or she uses for comparable sales. If the appraiser's exterior-only inspection of the property and available data sources do not provide sufficient information about the property to perform the appraisal, we require the exterior-only inspection appraisal to be upgraded to an appraisal with an interior and exterior inspection reported on Form 2055. For example, if the appraiser cannot adequately view the property from the street, or apparent adverse physical deficiencies or environmental conditions were observed, or the appraiser needs additional information about the physical conditions of the property, the lender must upgrade the exterior-only inspection appraisal to an appraisal with an interior and exterior inspection.

Lenders may require a higher level of property documentation for loans processed through DU. For example, supplemental documentation from the appraiser might be necessary to address specific underwriting concerns. As another example, to address its concerns, the lender might ask the appraiser to provide a replacement cost estimate, data about additional comparable sales, and listings, etc. (The DU appraisal report form does not require this level of detail.) In addition, lenders may always upgrade our documentation recommendation to a higher level.

The use of Fannie Mae's streamlined documentation is available not only to the lender that submitted the mortgage to DU for evaluation, but also to any lender that subsequently delivers the mortgage to, or services it for, Fannie Mae, provided that the loan terms of the closed mortgage (including but not limited to loan-to-value ratios (LTV, CLTV, and HCLTV), amortization type, and property type) match the data entered in DU.

Age of appraisal and property inspection

The property must have been appraised (or inspected, if that is the level of property fieldwork recommended for a DU-processed mortgage) within the 12 months that precede the date of the note and mortgage.

When an appraisal report will be more than four months old on the date of the note and mortgage – regardless of whether the property was appraised as proposed or existing construction – the appraiser must inspect the exterior of the property and review current market data to determine whether the property has declined in value since the date of the original appraisal.

When a property inspection report (Form 2075) will be more than four months old on the date of the note and mortgage, the appraiser must re-inspect the property and prepare a new Desktop Underwriter Property Inspection Report (Form 2075).

Refer to the *Selling Guide*, Part XI, Chapter 2, Section 201 for additional information.

Appraisals with exterior-only property inspections (Forms 2055, 2065, and 2095)

The option for providing a streamlined appraisal that is based only on an exterior inspection of the property is based on DU's risk assessment of the mortgage and the appraiser's ability to obtain sufficient information about the physical characteristics of the subject property from reliable sources. When DU recommends an exterior-only property inspection, the appraiser's description of the physical characteristics of the property should be based on what he or she considers to be reliable data sources for the property and location. The appraiser should use the same type of data sources that he or she uses for comparable sales. Acceptable data sources include the following:

- Multiple listing service (MLS) information,
- Tax and assessment records,
- Information from prior inspections or previous appraisal files, and
- Information provided by the property owner.

If the appraiser's exterior inspection of the property does not provide sufficient information about the subject property to perform the appraisal, he or she must also inspect the interior of the property. Some of the reasons why an appraiser might choose to inspect both the exterior and interior of a property include the following:

- The appraiser cannot adequately view the property improvements from the street;
- The appraiser is unable to reconcile significant discrepancies among the available data sources with respect to the size, condition, or other factors about the property;
- The appraiser observed apparent physical deficiencies or adverse property conditions during the exterior property inspection; or
- The appraiser needs additional information for a property that is undergoing Renovation.

Although DU identifies which transactions are eligible for the exterior-only inspection option, appraisers are responsible for determining if adequate information is available about the property to develop a reliable appraisal without

inspecting the interior of the property. Appraisers cannot rationally develop an appraisal if adequate information on the subject property is not available.

Required exhibits to appraisal and inspection forms

The exhibits required to support the Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055), the Desktop Underwriter Qualitative Analysis Appraisal Report (Form 2065), the Desktop Underwriter Individual Cooperative Interest Appraisal Report (Form 2095), and the Desktop Underwriter Property Inspection Report (Form 2075) are based on the type of property inspection recommended by DU.

Appraisal with an interior and exterior inspection using Form 2055 or 2095

The following exhibits are required:

- A street map that shows the location of the subject property and the location of the comparable sales.
- An exterior building sketch of the improvements that indicates the dimensions.
- A photograph that shows the front, the rear, and a street scene of the subject property.
- Photographs that show the front of each comparable sale.

Appraisal with an exterior-only inspection using Form 2055, 2065, or 2095

The following exhibits are required:

- A street map that shows the location of the subject property and the location of the comparable sales.
- A photograph that shows the front scene of the subject property. (Photographs of the rear of the subject property, the street scene, and the comparable sales are not required, nor is a building sketch of the improvements.)

Exterior-only inspection using Form 2075

The following exhibits are required:

- A street map that shows the location of the subject property.
- A photograph that shows the front scene of the subject property.

Qualitative vs. quantitative sales comparison analysis

The sales comparison approach to value is an analysis of comparable sales, contract offerings, and listings of the properties that are most comparable to the subject property. In the sales comparison approach, appraisers analyze significant differences between properties to identify those that affect value. These significant differences are generally referred to as elements of comparison and include such items as sales or financing concessions, date of sale, location, age, condition, size, and amenities. The appraiser's analysis of transactions in a particular market area theoretically results in the appraiser's identifying how much each different element of comparison affects the value of properties in that particular location. After analyzing the differences, the appraiser then makes adjustments to the comparable sales – expressed as either qualitative or quantitative adjustments – in terms of the overall comparability of the comparable sales to the subject property in order to estimate the market value of the subject property.

The Desktop Underwriter Quantitative Analysis Appraisal Report (Form 2055), the Desktop Underwriter Individual Cooperative Interest Appraisal Report (Form 2095), and our standard appraisal report forms for one-unit properties require a quantitative sales comparison analysis in which the appraiser assigns a dollar value to reflect the market's reaction to any features of the comparable sale that differ from those of the subject property.

The Desktop Underwriter Qualitative Analysis Appraisal Report (Form 2065) requires a qualitative sales comparison analysis. The appraiser must analyze market data (both comparable sales and listings) and report the results of his or her analysis in terms of value relationships between the comparable properties and the subject property, without assigning an estimated dollar value to each of those relationships. This approach is consistent with the way that buyers and sellers typically evaluate the differences between properties.

- If a feature of a comparable sale is superior to, or more favorable than, the same feature of the subject property, the appraiser should report a negative (–) relationship.
- If a feature of a comparable sale is inferior to, or less favorable than, the same feature of the subject property, the appraiser should report a positive (+) relationship.
- If a feature of a comparable sale is equal to the same feature of the subject property, the appraiser should report an equal (=) relationship.

For example, if a feature of a comparable sale is superior to, or more favorable than, the same feature for the subject property, an appraiser using the traditional process reduces the price of the comparable sale by a precise dollar amount in order to compare the property to the subject property. When using the Form 2065 process, the appraiser will simply report a negative (–) relationship between the comparable sale and the subject property without estimating a precise dollar amount.

This “paired” data analysis comparison logic is similar to that required by our other appraisal report forms. However, in this case, the appraiser is not required to quantify the market’s reaction to the variations by assigning a dollar value to each variation.

Although the appraiser does not have to quantify the dollar amount of a sales or financing concession on Form 2065, he or she will have to consider whether the sales price of a comparable sale was affected by the concessions. If so, he or she will have to reflect the results of this qualitative analysis by reporting a negative relationship (–) if the sales price of the comparable sale was affected by the concessions.

The appraiser’s overall comparison of the subject property and the comparable sales that are shown on Form 2065 must take into consideration the value relationships for each of the features of the properties. The appraiser must report at the bottom of the sales comparison analysis grid the overall comparison of each comparable sale to the subject property – indicating whether the sale is superior, equal, or inferior to the subject property. The appraiser does not apply and report dollar adjustments to describe specific relationships between a comparable sale and the subject property in a qualitative sales comparison analysis; therefore, he or she must analyze and reconcile the market data in order to estimate the market value of the subject property. In doing this, the appraiser should give the most weight to the sales that are the most similar to the subject property based on the relative comparison analysis.

Uniform Standards of Professional Appraisal Practice

All of the DU appraisal report forms recognize the Uniform Standards of Professional Appraisal Practice (USPAP) as the minimum appraisal standards for the appraisal industry. In fact, the Desktop Underwriter Report Forms 2055 and 2065 and the underlying appraisal development processes were reviewed by the Appraisal Standards Board of The Appraisal Foundation. The board concluded that, if the appraisal is properly developed and reported, these report forms and the underlying appraisal development processes will result in a summary appraisal report that complies with the applicable sections of the USPAP.

The valuation analysis performed in connection with both of the DU appraisal reports is based solely on the sales comparison approach to values since that generally is the most reliable indicator of value for one-unit properties. To reduce the time and costs associated with performing the appraisal, we do not require the appraiser to develop the cost and income approaches to value.

Appraisals that are documented on Forms 2055, 2065, and 2095 are considered limited appraisals that are subject to the Departure Provision of the USPAP if the cost and income approaches to value would otherwise be applicable under those standards. A limited appraisal is not determined by the extent of the inspection of the subject property. Therefore, the DU

appraisal reports should not be considered limited solely because of the exterior-only property inspection options. It should be noted that some appraisals documented on these forms will be considered as complete appraisals when the cost and income approaches to value are not applicable, because the omission of these approaches for the particular type of appraisal assignment is not a departure from the USPAP. For example, a complete appraisal of a residential property assumes that the appraiser used, if appropriate, all of the approaches to value – cost approach, income approach, and sales comparison approach. On the other hand, a limited appraisal of a residential property occurs if the appraiser does not use one of the approaches to value and that approach is appropriate or necessary for the particular appraisal assignment. Appraisers are allowed to omit an approach to value as long as that omission does not result in an appraisal that is misleading or meaningless. For example, it is generally not appropriate for an appraiser to omit the sales comparison approach for the appraisal of a single-family property, because that approach is generally the best indicator of market value for that property type. The Appraiser's Certification that appears on the forms assumes that the appraisal is a limited appraisal unless the appraiser specifically identifies it as a complete appraisal in the report.

Fannie Mae will continue to have its own separate appraisal requirements to supplement the minimum requirements of the USPAP to ensure that all our specific concerns are addressed for any given appraisal. For instance, Forms 2055, 2065, and 2095 reflect our supplemental analysis and reporting requirements that exceed the minimum requirements of the USPAP. The DU appraisal reports are designed in a way that results in an appraiser being able to be in full compliance with our requirements if he or she addresses all the specific information on the forms and presents the data accurately and completely.

Although the extent of the appraisal process an appraiser is required to complete is reflected in our report forms, the forms are not designed nor intended to control the appraisal process. As with all appraisal report forms, state-licensed and -certified appraisers should go beyond any limitations of a particular report form, with additional analysis, comments, and exhibits being used when they are necessary (based on the appraiser's professional judgment) to adequately document the valuation process or to support the appraiser's conclusions. The extent of the appraiser's data collection, analysis, and reporting is determined by the complexity of the appraisal assignment, not the form or format of the report. Therefore, if the appraiser believes the cost or income approaches to value or additional market data are necessary for a particular appraisal, he or she should document the supplemental analysis or market data in the report or as an exhibit to the report.

Project review requirements

Based on the risk analysis, DU will determine the appropriate level of project review for properties located in a condominium or planned-unit development (PUD) project. The lender will be required to perform either a limited or full review of the project, as defined by the *Selling Guide*, except as described below.

Limited project reviews for loans underwritten with DU

Certain guidelines regarding limited project reviews are more liberal for loans underwritten with DU than for loans that are manually underwritten. Mortgages secured by condominiums and attached PUD units that meet the following criteria are eligible for a limited project review when underwritten with DU:

- The subject legal phase is complete; and
- The subject property is not a **manufactured home**; and the transaction is either a
- Principal residence with a CLTV of 80% or less (regardless of the DU recommendation); or
- Principal residence that receive an Approve* recommendation from DU (regardless of the CLTV); or
- Second home with a CLTV of 75% or less (regardless of the DU recommendation); or
- Investment property with a CLTV of 75% or less that receive an Approve* recommendation from DU.

Except as stated above, all other limited review requirements in the *Selling Guide* apply to DU loans

The following charts outline the project review requirements for condominiums and PUDs submitted to DU.

Condo and PUD Project Minimum Review Requirements			
Occupancy and CLTV	DU Recommendation	Attached Condo and PUD	Detached(1) Condo
Principal Residence CLTV ≤ 80	All	Limited review if subject legal phase is complete.	Limited review
Principal Residence all CLTVs	Approve	Limited review if subject legal phase is complete.	Limited review
Principal Residence CLTV > 80	Refer, Refer with Caution, Expanded Approval	Full review	Limited review

Condo and PUD Project Minimum Review Requirements			
Occupancy and CLTV	DU Recommendation	Attached Condo and PUD	Detached(1) Condo
Second Home CLTV ≤ 75	All	Limited review if subject legal phase is complete.	Limited review
Second Home CLTV > 75	All	Full review	Limited review
Investment Property CLTV ≤ 75	Approve	Limited review if subject legal phase is complete.	Limited review
Investment Property CLTV ≤ 75	Refer, Refer with Caution, Expanded Approval	Full review	Limited review
Investment Property CLTV > 75	All	Full review	Limited review

Footnote:

(1) Detached PUDs do not require a project review.

Chapter 4:
Underwriting Reports

Chapter 4: Underwriting Reports

Introduction

DU creates standard underwriting reports for each loan that is submitted for analysis. This chapter describes the reports provided by DU and the information DU uses to create these reports. These reports are summarized below:

- **Fannie Mae Underwriting Findings** (Underwriting Findings) report—summarizes the overall underwriting recommendation and then lists the steps necessary to complete the processing of the loan file. The Underwriting Findings report is typically the first report viewed by an underwriter or a loan officer after the underwriting analysis has been performed by DU.
- **Underwriting Analysis** report – contains much of the same information requested on the Transmittal Summary (Form 1008), as well as key values used in the underwriting analysis.

Each time a loan is submitted to DU, the information in these reports is updated with information from the most recent submission. The date and time of each submission are recorded on each report. The reports can be viewed online or printed. A copy of each report representing the final loan submission should be maintained in the loan file.

The names of the primary borrower and the co-borrower are displayed in the top section of both the Underwriting Findings report and the Underwriting Analysis report. The names of additional co-borrowers, if any, are not displayed.

DU assigns a unique casefile ID for each casefile. The DU casefile ID is located at the top of both the Underwriting Findings report and the Underwriting Analysis report.

Underwriting Findings report

DU provides users with specific messages tailored for each individual loan. These detailed messages are designed to facilitate the ease with which users may process and close loans, in many cases alleviating the need to refer to supplemental guides. In addition, DU provides a number of “potential red flag” messages that are designed to help our customers detect inconsistencies and potentially fraudulent transactions.

The Underwriting Findings report is divided into sections, and each section contains a different type of message. The table below explains the types of messages appearing in each section of this report. Certain specific messages will be provided based on DU's risk analysis. For example, some messages will be returned only on Approve recommendations (including Expanded Approval recommendations), while other messages will be returned only on Refer or Refer with Caution recommendations.

Fannie Mae Underwriting Findings	
SUMMARY	
Recommendation	
Primary Borrower	Co-Borrower
Lender Loan Number	Casefile ID
Underwriting Run Date	Submitted By
Mortgage Information	
LTV/CLTV	Note Rate
Housing Expense Ratio	Loan Type
Total Expense Ratio	Loan Term
Total Loan Amount	Amortization Type
Sales Price	Loan Purpose
Appraised Value	Refi Purpose
Property Information	
Address	Property Type
RISK/ELIGIBILITY	
Messages pertaining to the risk assessment and the underwriting recommendation of the loan are located in this section. If the loan receives a Refer, Ineligible, or Out of Scope recommendation, DU will identify the reasons for the recommendation.	
POTENTIAL RED FLAGS	
Messages pertaining to potential red flags in the loan application will appear in this section. The appearance of these messages does not affect the underwriting recommendation from DU – they are designed to help lenders detect inconsistencies and potentially fraudulent transactions. Neither the presence nor absence of these messages alters the lender's responsibility to ensure accurate information in all areas of the loan process.	
Possible inconsistencies in the occupancy type: A message alerts users when the subject transaction is a refinance of the borrower's primary residence and the subject property address appears to be inconsistent with the occupying borrower's current address. Another message alerts users of potential misrepresentation of owner occupancy on certain purchase and refinance loan transactions where the borrower(s) may own other property.	
Excessive resubmissions: A message alerts users when an unusually high number of loan resubmissions may be the result of data manipulation.	
Rapid appreciation: Messages help identify purchase and refinance transactions with subject property values that, according to a recent prior sale, appear to exceed the level of appreciation for the local market.	
Excessive value: A message helps identify refinance transactions submitted to the system where the lender's initial value estimate appears to be excessive for the local market.	

Quality assurance: Messages identify transactions that have risk characteristics that historically have been found to contribute to inflated property valuation.

Manufactured home caution: A message alerts users when a property type was not submitted as a manufactured home, but our property database indicates that it may be a manufactured home.

Social Security number alerts: Various messages identify potential issues with the borrower's Social Security number, e.g., invalid format; numbers not issued; age/number discrepancies; and Social Security numbers associated with deceased individuals.

Inconsistency liabilities: A message advises users when the liabilities on the credit report do not match the liabilities on the loan application.

FINDINGS

DU provides lenders with loan-level messages that will identify the risk factors that contributed to the recommendation. These messages serve as a valuable tool in helping loan officers, mortgage brokers, loan processors, and underwriters understand the important components of the risk evaluation and are a valuable resource when discussing the loan application with the borrower.

Risk assessment (strength) messages for loans with Approve recommendations: For loans that receive an Approve recommendation, DU may identify certain strengths in the loan application that contributed to the recommendation. The absence of a "strength" message indicates that no single factor strongly influenced the recommendation. Instead, the combined positive effect of several factors resulted in the loan receiving an Approve recommendation. In addition, for certain loans with higher LTVs, the presence of mortgage insurance can have a positive impact on the risk assessment. When this occurs, DU will issue a message in the Findings section.

Significant risk factor message: For loans that do not receive an Approve recommendation, DU may identify one or more risk factors that had a significant impact on the recommendation.

Layering of risk message: In addition to the significant risk factors, DU may also identify (for loans that do not receive an Approve recommendation) one or more secondary risk factors that contributed to additional layering of risk. Although the secondary risk factors do not carry as much weight in the mortgage scoring model as the significant risk factors, they do contribute to the overall recommendation, and for a borderline case, could make the difference between a loan receiving an Approve or a Refer with Caution recommendation.

Credit profile message: When the "credit profile" – a combination of the credit characteristics – is listed as a significant risk factor in the significant risk factor message, DU will issue another message in the Findings section that will identify the adverse credit characteristics that contributed to the high-risk assessment of the credit profile.

VERIFICATION MESSAGES/APPROVAL CONDITIONS

The Verification Messages/Approval Conditions section identifies the follow-up processing steps the lender must complete to comply with DU's requirements. Income and asset verification requirements and any required credit verifications appear here, as well as the type of property fieldwork that must be completed. For loans with LTVs greater than 80%, a message regarding mortgage insurance will be provided. For cases receiving a Refer or Refer with Caution recommendation, this section lists the **minimum** documentation requirements for the loan; however, additional documentation can and should be requested when it supports the lender's decision to approve a referred loan. DU may provide messages requesting additional explanations related to specific weaknesses in the loan.

(For additional guidance, see [Chapter 5, Underwriting Recommendations](#), beginning on page 179.)

Credit and Liabilities
If the loan application contains certain credit-related issues, such as unverified mortgages and collection accounts, messages regarding these liabilities will be provided here.
Employment and Income
The documentation requirements for the borrower's income is shown here.
Assets
The amount of funds that need to be verified, as well as the documentation requirements, are shown here.
Property and Appraisal Information
All fieldwork recommendations and project information messages are shown here.
Ratio Information
If the loan application does not contain certain monthly housing obligations, such as taxes, insurance, and homeowner's association dues on the subject property, messages will be provided here advising the user that these items were not included in the total expense ratio.
OBSERVATIONS
The Observations section identifies the version of DU that was used to analyze the loan, the institution that submitted the loan, the Casefile ID number, the name of the credit agency, the credit report ID number, and the number of times the loan has been submitted to DU.
This section also lists additional information, such as:
<ul style="list-style-type: none"> • certain special feature codes, • credit scores that were obtained by the credit agency selected by the user, • sources and amount of income that were used in the analysis, • type and amount of assets that were counted toward available funds, and • unverified and undisclosed debt.
LENDER GUIDANCE FOR USE WITH APPLICANTS
The messages in this section are designed to assist the lender in discussions with the borrower about the aspects of the borrower's mortgage application that were the most significant to the recommendation process. This section of messages appears for loans that do not receive an Approve recommendation, and the messages provide detail about each significant risk factor and each credit characteristic identified in the Findings messages. In addition, there may be one or more "suggestion" messages that identify areas of the borrower's application that upon modification may improve the recommendation.
Suggestion messages: For certain loans that do not receive an Approve recommendation, DU issues one or more messages that will identify possible modifications to the loan terms that may result in a more favorable recommendation. For example, if the loan is a one-year ARM and there is a high likelihood that the loan will be approved as a longer-term ARM or as a fixed-rate loan, DU will issue a message to that effect. The presence of the message does not guarantee an Approve recommendation – the lender will need to modify the loan data and resubmit the loan to obtain an actual Approve recommendation (and the limited waiver of underwriting representations and warranties).

The Underwriting Analysis report

The Underwriting Analysis report is divided into sections. The table below describes the types of information appearing in each section of this report. This report is designed to resemble Form 1008 (Transmittal Summary) and contains information that summarizes the underwriting analysis. While information from this report can be used to manually complete Form 1008, Form 1008 is not required to be completed on loans underwritten with DU provided the lender maintains a copy of the Underwriting Analysis report in the loan file.

Underwriting Analysis Report	
Recommendation	Co-Borrower
Primary Borrower	Casefile ID
Lender Loan Number	Submitted By
Underwriting Run Date	
PROPERTY INFORMATION	
Property Address	Number of Units
Property Type	Occupancy Status
MORTGAGE INFORMATION	
Loan Type	LTV/CLTV
Amortization Type	Loan Amount
Balloon	Financed MI Amount
Community Lending	Total Loan Amount
Payment Frequency	Sales Price
Lien Type	Appraised Value
Amt. Subordinate Fin.	P&I
Loan Purpose	Note Rate
Refi. Purpose	Qualifying Rate
Owner Existing Mtg.	Bought Down Rate
Buydown	Term (Months)
INCOME (1)	QUALIFYING RATIOS
Base	Housing Expense
Commission	Total Expense
Bonus	EXPENSE RATIOS
Overtime	Including ≤ 10 Mos.
Other	With Undisclosed Debt
Positive Net Rental	
Subj. Pos. Cash Flow	
Total	

PROPOSED MONTHLY PAYMENT (2)	
First P&I (Qualifying)	Negative Net Rental
Second P&I	Subj. Neg. Cash Flow
Hazard Insurance	All Other Payments
Taxes	Total Expense Payment
Mortgage Insurance	
HOA Fees	Present Housing Payment
Other	
Total Housing Payment	
Funds(3)	
Required	Net Cash Back
Available	Reserves
Cash Back	Months Reserves
The recommendation for this case is:	

(1) These calculations do not include the income or liabilities of non-occupant co-borrowers on principal residences. See [Total expense qualifying ratio calculations](#) on page 173 for additional information.

(2) This calculation reflects the proposed monthly housing payment of the subject loan regardless of the occupancy; for example, if the loan is for a second home or investment property, the proposed monthly payment of the subject property will be displayed. The principal and interest of the subject property (First P&I) is calculated by DU. The housing payment detail is displayed from Section V.

(3) The calculations for funds are described below:

- **Required** – This is calculated from Section VII, Line p, plus any debt marked Paid By Close that is not attributed to a property being sold. However, debts marked Paid By Close on cash-out refinance transactions are not included in the calculation, as these debts are generally included in Section VII, Line d.
- **Available** – This is the sum of the liquid assets listed on the loan application for all borrowers, including the liquid assets of non-occupant co-borrowers on principal residences.
- **Cash Back** – This is cash to the borrower and is shown in Section VII, Line p.
- **Shortage** – This is shown when the amount of required funds is greater than the amount of available funds.
- **Net Cash Back** – This is shown when there is a shortage. It is calculated by subtracting the amount of shortage from the cash back. If the amount of required funds is less than or equal to the amount of available funds, the net cash back will be the same as cash back.
- **Reserves** – This amount includes excess available funds after subtracting required funds; excludes reserves attributed to cash back from a cash-out refinance transaction.
- **Months Reserves** – This amount is calculated by dividing the amount of reserves by the total proposed monthly housing payment.

Total expense qualifying ratio calculations

DU considers the total expense ratio, which includes the proposed monthly housing expense for the subject property, in the risk assessment. The proposed monthly housing payment consists of principal, interest, taxes, and insurance (PITI). DU automatically calculates the P&I on the subject property; you must calculate and enter the monthly escrow amounts for hazard insurance, real estate taxes, and, if applicable, mortgage insurance and homeowner association dues in the Proposed column under Combined Housing Expense in Section V.

Note: Principal payments are not considered in the proposed housing payment for InterestFirst mortgages.

The Current housing expense fields in Section V should always be completed with the borrower's current principal housing expenses – including when the subject transaction is for a second home or investment property. The following chart summarizes the components of the total expense ratio based on the number of units and occupancy of the subject property.

Occupancy	Units	Income for ratio calculation (1)	Total expenses included in ratio (2)
Principal	1	Income of all occupant borrowers	Proposed housing expense and Liabilities of all occupant borrowers
Principal	2-4	Income of all occupant borrowers and Positive subject net cash flow (3)	Proposed housing expense (4) and Liabilities of all occupant borrowers
Second	1	Income of all borrowers	All borrowers' current monthly housing expenses on their primary residences from Section VI L (and, if applicable, rent amount from current housing expense field in Section V) and Proposed housing expense and Liabilities of all borrowers
Investment	1-4	Income of all borrowers and Positive subject net cash flow (5)	All borrowers' current monthly housing expenses on their primary residences from Section VI L (and, if applicable, rent amount from current housing expense field in Section V) and Negative subject net cash flow (5) and Liabilities of all borrowers

Footnotes:

- (1) The total income of all borrowers including net rental income on investment properties.
- (2) Liabilities of all borrowers, including debts with more than 10 months remaining, lease payments, negative net rental obligations, and second home obligations including taxes, maintenance, and insurance payments on properties that are owned free and clear and listed in Section VI R.

- (3) Subject net cash flow for two- to four-unit principal residences, when used to qualify the borrower, must be manually calculated. Only positive net cash flow should be entered – do not enter a negative amount for subject net cash flow on a principal residence because the entire proposed housing payment is already factored in the ratio. (If there is a non-occupant co-borrower, the total positive net cash flow income from the two- to four-unit property should be credited to the occupant borrower.)
- (4) The proposed monthly housing payment is not adjusted for any rental income of the other units.
- (5) Subject net cash flow for investment properties, when used to qualify the borrower, must be manually calculated. Both positive and negative net cash flow should be entered in Section V. If the value is positive, it will be added to qualifying income. If the value is negative, it will be treated as a liability and included in the total expense ratio calculation. If the lender chooses not to include income from the property in the qualifying ratios, the entire proposed monthly payment should be entered as negative net cash flow in Section V.

Qualifying interest rate for proposed monthly housing expense

The proposed monthly housing expense is included in the total expense ratio analysis performed by DU. The following table identifies the formulas DU uses to determine qualifying rates for the proposed monthly housing payment.

Product	Occupancy	Qualifying Rate
Fixed-rate mortgages without temporary buydowns		
Fixed-rate Balloon	All	Initial note rate
Fixed-rate mortgages with temporary buydowns		
Fixed-rate Balloon	Principal	1 percentage point above the bought-down rate
	Second home	Initial note rate
	Investment property	NA
Flexible mortgages with temporary buydowns		
Fixed-rate 3- to 10-Year ARMs	Principal	LTV > 95% Initial note rate
		LTV ≤ 95% 1 percentage point above the bought-down rate
ARMs without temporary buydowns		
6-Month ARM 1-Year ARM with 2% annual cap	All	2 percentage points above initial note rate
1-Year ARM with 1% annual cap 3- to 10-Year ARMs	All	Initial note rate
ARMs with temporary buydowns		
6-Month ARM 1-Year ARM	NA	NA
3- to 10-Year ARMs	Principal	1 percentage point above the bought-down rate
	Second home	Initial note rate

Product	Occupancy	Qualifying Rate
ARMs with temporary buydowns - Continued		
	Investment property	NA
InterestFirst Mortgages		
Fixed-rate	All	Initial note rate Interest-only payment (ITI)
3- to 10-Year ARMs	All	Varies based on the ARM plan, interest-rate caps, and interest-only period (1)
Negatively amortizing ARMs		
All	Principal Second home	Interest rate entered in the ARM Qualifying Rate field (If an interest rate is not entered, DU uses 7.5%)
	Investment property	NA

Footnote:

- (1) For InterestFirst ARMs, the qualifying rate shown on the Underwriting Analysis report will reflect the ITI payment at the initial note rate. However, when determining the maximum allowable total expense ratio, DU may apply a different rate based on the information above.

Chapter 5:
Underwriting
Recommendations

Chapter 5: Underwriting Recommendations

Introduction

This chapter describes the underwriting recommendations that DU produces after each loan is analyzed, and the minimum follow-up processing steps that are required as a result of the recommendation. The recommendation identifies both the credit risk assessment of the loan and the eligibility of the loan according to Fannie Mae's guidelines that are in place in DU. The underwriting recommendation is displayed on the Loan List screen, the Fannie Mae Underwriting Findings (Underwriting Findings) report, and the Underwriting Analysis report.

Risk factors evaluated by DU

Fannie Mae is committed to working with lenders to achieve our shared goals of increasing homeownership, especially for low-and moderate-income borrowers, while at the same time preventing unlawful housing discrimination. DU helps lenders thoroughly evaluate the credit risk of home mortgage loans. It complements – not replaces – the considered judgment of experienced underwriters. DU provides an objective assessment of the risk of each mortgage application based on the past performance of more than two million mortgage loans. With DU, lenders have access to fast, objective underwriting recommendations that are specific to each mortgage application. The system conducts this analysis uniformly, and without regard to race, gender or other prohibited factors. DU uses validated, statistically significant variables that have been shown to be predictive of default across all groups. We have engineered, tested, and refined DU in full compliance with fair lending laws.

As part of the overall risk analysis of mortgage applications, DU evaluates characteristics within the credit report that research has proven to be predictive of mortgage default and loan performance. Accordingly, we regularly review and fine-tune the risk assessment capabilities in DU based on new data and loan performance to further enhance the risk assessment performed by DU.

Credit characteristics evaluated by DU

DU considers the following characteristics in the credit report to assess the creditworthiness of borrowers who have traditional credit histories. A more comprehensive definition follows:

- Credit history – The age, number, and type of accounts.

- Delinquent accounts – The occurrence and severity of late payments, the length of time since delinquency occurred, and the number and type of accounts that were not paid as agreed.
- Mortgage accounts – A history of mortgage accounts, the length of time since delinquency has occurred, the severity of delinquency, the reduction in the balance of existing mortgages, and age of the accounts.
- Revolving credit utilization – The amount of revolving credit a borrower has available, for both existing and recently opened credit cards.
- Public records, foreclosures, and collection accounts. The existence of significant derogatory credit and the recency of the delinquency.
- Inquiries – A pattern of borrowers seeking and/or obtaining new or additional credit.

DU looks at all types of accounts in the evaluation, including revolving, installment, mortgage, 30-day accounts, lines of credit, and open and closed accounts. It weighs each of the credit characteristics based on the amount of risk and its significance to the underwriting recommendation. Using the information in the borrower's credit report, DU assesses a borrower's credit behavior over a period of time.

Credit history

A borrower's credit history is an account of how well the borrower has handled credit, both now and in the past. Generally, the longer a borrower has had an established credit history, the less risk. An older, established history – even though the accounts may have zero balances – will have a more positive impact on the borrower's credit profile than newly established accounts.

A borrower who has a relatively new credit history (a few recently opened accounts) is not automatically considered a high credit risk. Making payments as agreed on newly established accounts signifies lower risk than not making payments as agreed.

Delinquent accounts

Payment history is a significant factor in the evaluation of the borrower's credit. DU considers the severity of the delinquencies (30, 60, 90, or more days late), the length of time since the delinquencies, the number of accounts that were not paid as agreed, and the type of accounts with delinquencies.

A payment history that includes bills that are 30 days or more past-due, or a history of paying bills late as evidenced by a number of accounts with late payments, will have a negative impact on the borrower's credit profile. A history of paying a mortgage loan late will have an even more negative impact on the credit profile. The amount of time that has elapsed since an account was delinquent is an important factor included in the evaluation of the payment history. The more recent a delinquency, the higher the risk. For example, a 30-day late payment that is less than three months old indicates a higher risk than a 30-day late payment that occurred several years ago.

Mortgage accounts

Research has shown that borrowers who have no history of mortgage obligations represent a higher risk than borrowers who have had mortgage obligations. In addition, the relationship between the original mortgage balance and the current unpaid balance has proven to be an indicator of risk. The lower the percentage of principal that has been paid down on the mortgage, the higher the risk. The length of time since delinquency (if any) has occurred, the severity of delinquency, and the age of the mortgage accounts are also factored into the credit analysis.

Revolving credit utilization

The establishment, use, and amount of revolving credit a borrower has available are important. Generally, the lower the balances are on revolving credit as a percentage of the credit limit, the lower the risk. A borrower whose revolving credit utilization is high is considered a greater risk than someone who has a history of managing his or her credit card accounts more conservatively.

Public records, foreclosures, and collection accounts

A credit history that includes any significant derogatory credit event that was reported as a public record, such as bankruptcy filings, foreclosures, deeds-in-lieu of foreclosure, judgments, tax liens, or accounts that have been turned over to a collection agency, is considered higher risk than one that does not.

The more recently such events occurred, the more adverse the impact is on the credit profile. Although most public record information is retained in the credit history for seven years (ten years for bankruptcies), as time passes, it does become less significant to DU's credit evaluation.

Inquiries

DU evaluates inquiries made within the most recent six months of the credit report date. Historically, a high number of inquiries can indicate a higher degree of risk. However, multiple inquiries made by several creditors within a short time frame because a borrower was attempting to obtain the most favorable loan rate or terms generally do not indicate higher risk and are not considered as such in the credit evaluation. Borrowers who have frequently applied for, or obtained, new or additional credit represent a higher risk.

Note: We require the credit agencies to report all inquiries in the most recent twelve-month period, even though DU only evaluates inquiries in the most recent six months. The reason for this difference is that we are continuing to research the impact of inquiries to determine if it is preferable to evaluate a longer inquiry history. If our research validates that a longer inquiry history is more advantageous in measuring default risk, we may adjust our credit analysis in the future.

Non-credit risk factors evaluated by DU

The non-credit risk factors evaluated by DU include the borrower's equity and LTV; liquid reserves; loan purpose, term, and type; occupancy status; total expense ratio; property type; number of borrowers; and self-

employment status. DU performs a comprehensive evaluation of these factors, weighing each factor based on the amount of risk it represents and its importance to the recommendation. DU analyzes the results of this comprehensive evaluation along with the evaluation of the credit profile to arrive at its recommendation about the loan application.

Borrower's equity and LTV

The amount of equity in the property is a very important component of the risk analysis. A borrower who makes a large down payment or who has considerable equity in his or her property is less likely to default on a mortgage loan than a borrower who makes a small down payment or has a small amount of equity in a property. In other words, the more equity a borrower has in the property, the lower the risk associated with the borrower's mortgage loan.

DU may use a low LTV ratio to offset other risks that it may identify in the loan application.

Furthermore, DU considers the existence of mortgage insurance as a mitigating risk factor when evaluating higher LTV loans (greater than 85%), most notably for the purchase of a one-unit property that will be the borrower's principal residence.

Liquid reserves

Liquid reserves are those financial assets that are available to a borrower after a loan closes. Reserves are calculated as the total amount of liquid assets remaining after the loan transaction closes divided by the proposed monthly housing expense. Some examples of liquid reserves include funds in a checking or savings accounts; the net value of stocks, bonds, and mutual funds; the vested portion of 401(k) accounts; and funds in an IRA or a Keogh retirement account.

DU considers higher amounts of liquid reserves as more favorable than lower amounts or no reserves. Research has shown that mortgages to borrowers with higher amounts of liquid reserves tend to have lower default rates. As with a low LTV ratio, DU may consider high amounts of reserves as an offset for other risks that it may identify in the loan application.

Loan purpose

There is a certain level of risk associated with every transaction, whether it is a purchase or a refinance. In general, a purchase transaction represents less risk than a refinance transaction. In its evaluation of refinances, DU analyzes the increase in the new loan amount from the unpaid principal balance (UPB) of the first mortgage that is being refinanced. The increase in the new loan amount may be the result of equity taken out of the property (cash to the borrower), the financing of closing costs and prepaid fees, or the payoff of subordinate liens. As the loan amount increases as a percentage of the existing UPB, the level of risk increases. Moreover, our historical default experience indicates that the level of default risk is even greater for higher LTV refinance mortgages relative to higher LTV purchase transactions when all other risk factors are held constant. There is more uncertainty about the value of the property for a refinance transaction. Purchase transactions have

the benefit of a sales price that was mutually agreed upon by a willing buyer and seller in an arm's-length sales transaction. The lack of a market transaction with a refinance can create uncertainty as to the value of the loan security.

Loan term

Research has shown that mortgages to borrowers who *choose* to finance their mortgages over shorter terms and build up equity in their properties faster generally tend to perform better than mortgages with longer amortization periods. This is true particularly at lower LTVs. As a result, DU considers the loan term in combination with the LTV in its evaluation. Shorter-term mortgages at low LTVs represent lower default risk than short-term mortgages at high LTVs. In addition, shorter-term mortgages at low LTVs represent lower default risk than long-term mortgages at any LTV.

Loan/amortization type

Research has shown that there is a difference in loan performance based on the manner in which the mortgage amortizes. Fully amortizing fixed-rate mortgages and fixed-period adjustable-rate mortgages (3-, 5-, 7-, and 10-year ARMs) represent the least amount of risk. Balloon mortgages and interest-only mortgages (e.g., Fannie Mae's InterestFirst Mortgage) represent additional risk. Of moderate risk are six-month and one-year ARMs. Finally, negatively amortizing ARMs (or those that contain the potential for negative amortization) represent the greatest risk of all amortization types.

Occupancy type

Performance statistics on investor loans are notably worse than those of owner-occupied or second home loans, especially at higher LTVs. Therefore, DU will assign a higher level of risk to all investment property transactions.

Total expense ratio

In DU's evaluation, generally, the lower the borrower's total expense ratio, the lower the associated risk. As the ratio increases, the level of risk also tends to increase; and an excessively high ratio will have the greatest adverse impact on the recommendation when there are other high-risk factors present.

Property type

Another important factor that DU considers in the risk analysis is the collateral or property type. DU currently differentiates the risk based on the number of units, and in some cases the property type (e.g., manufactured home, condominium, and cooperative properties). One-unit properties that are not in a condominium or cooperative project represent the least risk; two-unit properties, and units in condominium or cooperative projects represent increased risk; and manufactured homes and three- and four-unit properties have significantly increased risk.

Co-borrowers

DU considers the number of borrowers (who have traditional credit) on a mortgage application in its evaluation because, generally, the presence of more than one borrower with traditional credit helps to reduce risk. Research has shown that mortgages that have more than one borrower tend to have a lower default rate than mortgages with one borrower. However, additional borrowers tend to reduce risk only when they have good credit histories.

Self-employment

Self-employment introduces an additional layer of risk to a mortgage loan application that is not present with salaried borrowers. Research has shown that self-employed borrowers tend to default on their mortgages more often than salaried borrowers, when all other risk factors are held constant.

DU takes this additional risk into consideration in its overall evaluation. However, this additional risk is generally considered adverse only when a self-employed borrower has other risk factors associated with his or her loan that are also higher risk, such as a history of delinquent accounts or a low level of savings.

Summary

None of these factors alone determines a borrower's ability or willingness to make his or her mortgage payments. DU evaluates all of the risk factors together and identifies low-risk factors that can offset high-risk factors. When several high-risk factors are present in a loan application without sufficient offsets, the likelihood of default increases. DU helps to identify and manage this risk.

The DU recommendations

DU analyzes information in the loan application and credit report for credit risk and eligibility requirements (whether the mortgage is eligible to be sold to Fannie Mae). DU issues a recommendation based on the assessment of the overall risk profile of the loan. The Fannie Mae Underwriting Findings (Underwriting Findings) report displays the recommendation and the required follow-up procedures. Refer to [Chapter 4, Underwriting Reports](#), beginning on page 167, for information on the reports provided by DU.

Approve/Eligible

Based on the data submitted to DU, the loan appears to meet both Fannie Mae's credit risk and eligibility requirements.

Lenders must comply with all of the Verification Messages/Approval Conditions listed in the Underwriting Findings report and document the loan file accordingly. Lenders must apply due diligence when reviewing the documentation in the loan file to determine if there is any potentially derogatory or contradictory information *that is not part of the data analyzed*

by Desktop Underwriter. Furthermore, lenders should review the credit report to confirm that the data that DU evaluated with respect to the borrower's credit history was accurate and complete. Lenders are obligated to take action when erroneous data in the credit report or contradictory or derogatory information in the loan file would justify additional investigation or would provide grounds for a decision that is different from the recommendation that DU delivered. For example, if a foreclosure was reported in the credit report but was not detected by DU (i.e., was not referenced in any verification messages) the lender must determine if the loan complies with the guidelines. See [Chapter 2, Underwriting Loans with Desktop Underwriter](#), beginning on page 89.

If all of the necessary conditions are met, the limited waiver of underwriting representations and warranties applies to loans that receive an Approve/Eligible recommendation.

Approve/Ineligible

Based on the data submitted to DU, the loan appears to meet Fannie Mae's credit risk requirements; however, the loan does not appear to meet Fannie Mae's eligibility requirements.

The loan appears to meet Fannie Mae's credit risk requirements based on eligibility parameters (such as product and maximum LTV) implemented in DU. However, the Approve recommendation does not take into consideration any additional credit risk that might be associated with the ineligibility condition. The lender must determine if the condition that caused the ineligibility creates an additional layering of credit risk that should be considered.

A lender can deliver loans that receive an Approve/Ineligible recommendation to Fannie Mae if the lender has a negotiated variance in its Master Agreement that covers the ineligible condition specific to the loan transaction.

The limited waiver of underwriting representations and warranties does not apply to loans that receive an Approve/Ineligible recommendation.

Refer/Eligible

Based on the data submitted to DU, the loan does not appear to meet Fannie Mae's credit risk requirements; however, the loan appears to meet Fannie Mae's eligibility requirements.

DU evaluated a combination of risk factors, including the LTV, total expense ratio, available assets, each borrower's credit history, employment status, property type, product type, and the purpose of the loan. Based on the data submitted, DU is not able to recommend approval of the loan. The Underwriting Findings report will identify the overriding factor(s) that resulted in the loan being referred. The lender must review the conditions that resulted in the referral and determine if the loan meets Fannie Mae's credit risk requirements as described in the *Selling Guide*, Part X, Chapter 3.

The lender should evaluate the accuracy of the data submitted, all relevant risk factors, and any factors outside of the data considered by DU when determining whether to approve the loan. We expect the lender to employ prudent underwriting judgment in assessing whether a loan that received a Refer recommendation should be approved by the lender and delivered to Fannie Mae.

The Underwriting Findings report will identify the reason(s) for referral. The reason will be specific to a particular risk factor: funds to close, total expense ratio, previous bankruptcy or foreclosure, or mortgage delinquency. When a loan is referred, the lender should follow these procedures in determining whether the loan represents an acceptable credit risk:

1. Review the Underwriting Findings report to determine why the loan was referred. In some cases, the referral may have been caused by a problem with the data submitted to DU. Refer to the following chart for guidance on specific referral reasons and possible data entry problems the lender may be able to correct.
2. Review the loan data in DU for accuracy. Verify that all income, assets, and liabilities have been accurately submitted to DU and fully disclosed by the borrower. If meaningful information was not included in the data submitted to DU, it should be entered into the loan and the loan resubmitted.
3. Review the reason(s) for the referral and all relevant information considered by DU to gain a full understanding of the risk factors in the loan. For example, consider factors such as the LTV, total expense ratio, product type, loan purpose, income stability, employment status, available assets, and credit history. In addition to the individual reason(s) the loan was referred, determine if the layering of risk factors is acceptable.

The lender should evaluate the risk factors in a comprehensive manner and apply judgment in deciding which loans warrant approval. The rationale that was applied in the course of making the final decision should be clearly documented in the loan file. If the factors supporting the final decision cannot be derived from the verifications listed in the Underwriting Findings report, request additional verifications or documentation as appropriate, and include this information in the loan file.

The limited waiver of underwriting representations and warranties does not apply to loans that receive a Refer/Eligible recommendation.

Underwriting Guidelines for Loans with Refer Recommendations	
Referral reason	Data issues/Required follow-up
Insufficient funds to close	All borrowers, regardless of their specific risk characteristics, must demonstrate that they have sufficient funds to close. If the case refers for insufficient funds to close, the lender should first verify that there are no problems with the data submitted to DU. For example, determine if any liabilities were improperly

Underwriting Guidelines for Loans with Refer Recommendations	
Referral reason	Data issues/Required follow-up
	<p>marked to be paid by closing. (These are automatically added to funds required for closing for purchase and limited cash-out refinance transactions.)</p> <p>In the case of a refinance, ensure that mortgages and home equity lines of credit marked to be paid by closing are matched to the correct property and that the property is marked as the subject property, current residence, or both in Section VI R.</p> <p>The lender must verify that the borrower has sufficient liquid assets to cover the down payment and all closing costs and that all funds are from eligible sources.</p>
Total expense ratio	<p>If the total expense ratio for a loan exceeds the maximum ratio permitted in DU, the loan will be referred. The lender must determine if there are problems with the data analyzed by the system; if so, those problems should be corrected, and the loan should be resubmitted or the file must be documented accordingly. Data problems the lender should look for:</p> <p>Ensure that all debts in Section VI L represent the borrower's debts. Duplicate debts that were copied from the credit report and tradelines that do not belong to the borrower should be omitted from the loan application. Appropriate documentation should be provided confirming the status and ownership of those debts.</p> <p>Verify that debts to be paid by closing are marked as such in Section VI L. This includes any mortgages that are to be paid off with the proceeds of the loan, as in the case of a refinance.</p> <p>Review the proposed housing expenses to ensure that all proposed housing expenses are accurately recorded in Section V.</p> <p>Verify that the taxes and insurance payments for retained properties were not entered in both Section VI R and in the monthly mortgage payment field in Section VI L. Otherwise, this will cause double counting in the total expense ratio.</p>

Underwriting Guidelines for Loans with Refer Recommendations	
Referral reason	Data issues/Required follow-up
	<p>If all of the data submitted to DU are accurate and the loan still refers for ratios, the lender should carefully review the borrower's income, assets, and liabilities, in addition to other relevant risk factors (such as LTV, loan product, income stability, and employment status) when deciding if the loan meets our credit risk requirements. If there are circumstances that sufficiently mitigate the high ratio risk, such as considerable verified assets that can be drawn upon as needed to pay monthly obligations, or debts that will be paid off shortly after closing (e.g., a bridge loan), the loan may represent an acceptable overall risk even though the total expense ratio is high.</p>
Bankruptcy or foreclosure	<p>The lender must determine that the loan meets Fannie Mae's requirements as described in Chapter 2, Underwriting Loans with DU, beginning on page 89. Documentation of the discharge of the bankruptcy or completion of the foreclosure is required.</p>
Mortgage delinquency	<p>If the borrower has a mortgage tradeline on his or her credit report that has one or more 60-, 90-, 120-, or 150-day delinquency reported within the twelve months prior to the credit report date, then loans that would otherwise receive an Approve recommendation will receive a Refer recommendation. The lender must document the circumstances of the excessive late payment(s) and determine that the borrower is not likely to have a similar recurrence of mortgage delinquency in the future.</p> <p>This policy applies to all mortgage tradelines, including first liens, second liens, home improvement loans, home equity lines of credit, and mobile home loans.</p>

Refer/Ineligible

Based on the data submitted to DU, the loan does not appear to meet Fannie Mae's credit risk and eligibility requirements.

DU evaluated a combination of risk factors, including the LTV, total expense ratio, available assets, each borrower's credit history, employment status, property type, product type, and the purpose of the loan. Based on the data submitted, DU is not able to recommend approval of the loan. The

Underwriting Findings report will identify the overriding factor or factors that resulted in the loan being referred. In addition, the Refer recommendation did not take into consideration any additional credit risk that might be associated with the ineligibility condition. The lender must review the conditions that resulted in the referral and consider any additional risk associated with the ineligibility condition and determine if the loan meets Fannie Mae's credit risk requirements as described in the *Selling Guide*, Part X, Chapter 3.

The lender should apply the guidelines for Refer/Eligible loans as explained above. In addition, the lender should consider if the ineligibility condition creates an additional layering of credit risk. If the lender determines that the loan meets Fannie Mae's credit risk requirements, the loan can be delivered to Fannie Mae if the lender has a negotiated variance in its Master Agreement that covers the ineligible condition specific to the loan transaction.

The limited waiver of underwriting representations and warranties does not apply to loans that receive a Refer/Ineligible recommendation.

Refer with Caution

DU has evaluated a combination of risk factors, including the LTV, total expense ratio, available assets, each borrower's credit history, employment status, occupancy status, property type, product type, and purpose of the loan. Based on the data submitted, the loan does not appear to meet Fannie Mae's credit risk requirements. The layering and degree of risk factors that result in a Refer with Caution recommendation represent a greater risk of default than for those loans that receive an Approve or Refer recommendation.

DU also assesses the eligibility of the loan. Generally, ineligibility is related to the loan parameters (such as maximum LTV, number of units, and loan purpose); however, loans receiving a Refer with Caution recommendation may also be ineligible due to the excessive credit risk of the transaction. The lender must review the Underwriting Findings report to determine if the case meets Fannie Mae's eligibility requirements; ineligibility conditions will appear in the top section of the report. If the loan is Eligible, there will not be any eligibility messages.

Generally, any loan that receives a Refer with Caution recommendation does not represent a level of risk that is acceptable to Fannie Mae; however, there are some circumstances that do warrant the lender's consideration. If the loan is not ineligible for delivery due to the transaction type (listed above) or excessive risk, as indicated in the Underwriting Findings report, the loan file should be reviewed carefully to determine if the following conditions exist:

1. Review the loan data in DU for accuracy. Verify that all income, assets, and liabilities have been accurately recorded and fully disclosed by the borrower. If meaningful information was not included in the data submitted to DU, it should be entered into the loan and the loan resubmitted.

2. Review the data in the credit report to determine if the information accurately represents the applicant's credit history. Accounts that do not belong to the borrower or derogatory information that is reported in error could have had an impact on the outcome of the loan. Refer to the following section regarding errors in the credit report for additional guidance.
3. Determine if there is any information outside of the data submitted to DU that could have an impact on the underwriting decision. For example, investigate whether there were any extenuating circumstances that contributed to serious instances of derogatory credit. The lender may not consider the factors that DU has already evaluated as compensation for the risk in the loan.

If the data DU considered was an accurate representation of the borrower's income, assets, liabilities, and credit profile, and there were no extenuating circumstances that were significant enough to compensate for the multiple layers of risk in the file, the lender should exercise caution in delivering the loan to Fannie Mae. If the loan is ineligible for reasons other than the transaction type or excessive risk, the lender must also have a negotiated variance in its Master Agreement that covers the ineligible condition specific to the loan transaction.

Community Lending loans

Community Lending loans that receive a Refer with Caution recommendation from DU may be eligible for delivery to Fannie Mae if the loan meets the Community Lending underwriting terms and conditions established by the lender's Master Agreement or variance. DU issues a message for all Community Lending products that receive a Refer with Caution recommendation advising the lender to refer to its Community Lending Master Agreement to determine if the loan is eligible for delivery. See [Community Lending products](#) on page 32.

Additional requirements for high-risk loans

The following transactions represent a high degree of credit risk and are ineligible for delivery to Fannie Mae if the loan receives a Refer with Caution recommendation for any reason other than inaccurate data on the borrower's credit report:

- Flexible mortgages, unless identified by DU as eligible for delivery subject to the appropriate loan-level price adjustment. (Refer to [Flexible mortgages](#) on page 34);
- InterestFirst mortgages;
- Mortgages secured by manufactured homes; and
- Negatively amortizing ARMs

If there are **significant** material credit errors in the credit report, and those errors have had a negative impact on the underwriting recommendation from DU resulting in a Refer with Caution (or EA-I, -II, or-III) recommendation, lenders may disregard the DU risk recommendation if the following criteria are met:

- All decisions to override DU’s risk recommendation must be based solely on documented evidence of the presence of erroneous credit data.
- The Underwriting Findings report must list “Credit Profile” as the significant risk factor. In addition, the credit data error must directly relate to one or more of the credit characteristics identified in the credit profile message from DU.
- Errors in the credit data must be *derogatory* in nature and *significant*.

Lenders should make every effort to correct the borrower’s credit information through the credit repository and resubmit the loan to DU before electing to manually underwrite the loan. If it is not possible to correct the error in the borrower’s credit record before loan closing, the loan may be manually underwritten according to Fannie Mae guidelines. However, when manually underwriting these loans, the lender must consider all of the risk factors inherent in these loan products. As an example, Flexible sources of funds and high CLTVs impose unique risks that should be taken into consideration when the lender makes the final loan decision.

We expect the lender to override a Refer with Caution recommendation on these high-risk loan products based solely on inaccurate credit data as described above and not because the lender disagrees with the recommendation.

If the lender determines that the mortgage complies with the required guidelines, the loan may be delivered to Fannie Mae subject to the loan-level price adjustment and mortgage insurance options that apply for the loan products that receive an Approve or Refer recommendation with DU. Lenders should use **all applicable Special Feature Codes** when delivering the loan.

Note: These loans are not eligible for the limited waiver of the underwriting representations and warranties.

Expanded Approval™ recommendations: EA-I, -II, -III, and Refer W Caution/IV

Lenders that participate in the Expanded Approval with Timely Payment Rewards® (EA/TPR™) initiative are eligible to receive Expanded Approval (EA) recommendations with DU. Refer to the *Expanded Approval with Timely Payments Rewards Lender Guide* for complete details. If all of the necessary conditions are met (according to requirements in Chapter 2 of this Guide and the Expanded Approval with Timely Payments Rewards *Lender Guide*), the limited waiver of underwriting representations and warranties applies to loans that receive an EA/Eligible recommendation.

Refer W Caution/IV is the EA recommendation that represents the highest level of risk and, generally, loans that receive this recommendation are not eligible for delivery to Fannie Mae.

Out of Scope

DU does not contain the rules or models that are necessary to help lenders make informed credit decisions on the loan product, borrower, or type of loan submitted. DU does not produce messages in the Underwriting Findings report or the Underwriting Analysis report for Out of Scope loans. DU does identify the reason the loan was Out of Scope.

One example of a loan that would receive an Out of Scope recommendation is a loan that has a borrower who lacks a traditional credit history, but that does not comply with the additional underwriting guidelines for loans to such borrowers. Another example is second lien mortgages. The current version of DU does not assess the acceptable level of risk for these loan types.

With the exception of DU-only transactions, loans that are Out of Scope must be manually underwritten according to the requirements of the *Selling Guide*.

Errors in the credit report

For all loans and for all underwriting recommendations – including Approve – the lender must review the credit reports to determine if all the data that DU evaluated was accurate. Significant errors in the borrower's credit file could have an effect on the risk analysis of the loan.

Errors of derogatory credit

If there are significant errors (such as accounts that do not belong to the borrower) in the credit report, the lender must determine whether the errors had a significant impact on the underwriting recommendation. Errors that are the result of the merge do not typically affect the credit or risk analysis of the loan. For example, public record information is typically duplicated on the credit report because the credit agencies do not attempt to merge or match items of this severe nature. A public record item may appear in the credit report three times – once from each repository – but the duplication will not affect the risk analysis of the case. Furthermore, DU attempts to identify duplicate tradelines that are the result of the merge, and ignores duplicate accounts in the credit analysis.

If it is determined that significant derogatory credit has been reported in error, the lender must obtain written documentation that supports the error. This may be in the form of a supplement to the credit report, a new mortgage credit report, or documentation from the credit provider that reported the error. If it appears that the errors are both *significant* and *derogatory* in nature and they have affected the risk analysis performed by DU (as indicated in the credit-related risk factor messages in the Findings section of the Underwriting Findings report), the lender should evaluate the borrower's credit outside of DU in conjunction with all other risk factors in the case.

Other errors in the credit data

In some cases, the printed credit report may contain derogatory information that is not identified by DU in the Underwriting Findings report. Certain

errors are the result of reporting errors by the credit agency or individual creditors. For example, the credit report may indicate that the borrower had a previous foreclosure; however, if the Underwriting Findings report does not reference a foreclosure, this is an indication of a reporting error. DU did not consider the foreclosure in its analysis of the loan. In situations such as these, the lender is obligated to take action when information not considered by DU would result in a recommendation other than that returned by the system.

Non-applicant debts

In a small number of cases, credit reports may include accounts identified as “possible non-applicant” accounts (or with another similar notation). Non-applicant accounts may belong to the borrower, or they may truly belong to another individual. Typical causes of non-applicant accounts are Junior/Senior situations, individuals who frequently move, and non-related individuals who have identical names. Non-applicant accounts may also be debts the borrower applied for under a different Social Security number or address (indicating potential fraud).

If possible non-applicant accounts appear on the credit report, the lender should investigate whether they belong to the borrower. DU ignores non-applicant accounts in the risk analysis and issues a message in the Underwriting Findings report alerting the lender of the existence of the accounts. If it is determined that the accounts belong to the borrower, the lender must determine if the recommendation is accurate based on the severity of the information, especially if the non-applicant accounts were significant and derogatory in nature. If so, the lender should evaluate the borrower’s credit outside of DU in conjunction with all other risk factors in the case.

Extenuating circumstances

An extenuating circumstance is an event over which the borrower had no control (such as an extended illness, extended unemployment as a result of company layoffs, death of a spouse or co-borrower, etc.) that has been resolved, and that is not likely to recur. The extenuating circumstance results in a sudden, significant, and prolonged reduction in income or a catastrophic increase in financial obligations. However, extenuating circumstances cannot be solely defined by the event; they must take into consideration the interrelationship between the event, the severity of the resulting hardship, and the extent of the applicant’s efforts to resolve the situation. For example, a job layoff in itself should not automatically be considered an extenuating circumstance (even if it supported by documentation from a third party). If, however, the unemployment that results from a job layoff was prolonged and the loss of income was significant in relation to the applicant’s obligations and available assets at the time of the layoff, then the layoff can be considered an extenuating circumstance.

If the lender determines that the credit analysis was heavily influenced by credit deficiencies that were the result of an extenuating circumstance, with

the exception of DU-only transactions, the lender should disregard the credit analysis performed by DU and fully evaluate all relevant risk factors in the loan. The lender must obtain written documentation to fully support the causes relating to the extenuating circumstances. The documentation should confirm the nature of the event that led to the bankruptcy or foreclosure and illustrate that the borrower had no reasonable options other than to default on his or her financial obligations.

The lender should review the documentation and fully evaluate the circumstances surrounding the event. The lender must determine that the borrower has an acceptable payment record under the re-established credit history. The borrower's re-established credit history must reveal a payment record that illustrates that the borrower now has the willingness and ability to manage his or her finances. For additional information about extenuating circumstances, refer to the *Selling Guide*, Part X, Chapter 8, Section 803.

Chapter 6:
Quality Assurance for DU[®] Loans

Chapter 6: Quality Assurance for DU[®] Loans

Introduction

The quality control measures that relate to a lender's mortgage-selling activities are defined in the *Selling Guide*, Part I, Chapter 3, Section 301. Generally, the lender's quality assurance process is simplified for mortgages underwritten through DU. The quality assurance process requirements will vary depending on DU's underwriting recommendation.

Note: The Expanded Approval[™] with Timely Payment Rewards[®] *Lender Guide* provides information specific to the quality assurance requirements for loans that received an Expanded Approval (EA) recommendation.

The following table lists the components of the requirements specific to loans underwritten with DU for the lender's quality assurance system, including a data integrity review to determine that the data submitted to DU is complete and accurate, and that the data matches information found on the documents in the loan file. (This data integrity review requirement means that a lender's quality assurance staff will need to have access to DU and be proficient in its use.)

Quality assurance requirements

Quality Assurance Component	DU Quality Assurance Requirements
Loan Selection	
Selection criteria	<p>The lender must comply with the mortgage review process described in the <i>Selling Guide</i>, Part I, Chapter 3.</p> <p>The lender should include in the selection a representative sample of loans underwritten by DU, and delivered to Fannie Mae, that receive any of the following recommendations:</p> <ul style="list-style-type: none"> • Approve/Eligible, • Approve/Ineligible, • Refer/Eligible, • Refer/Ineligible, • Refer with Caution, • EA-I, -II, -III/Eligible, and • EA-I, -II, -III/Ineligible

Quality Assurance Component	DU Quality Assurance Requirements
	<p>Note: Loans that receive an Ineligible recommendation may be delivered only if the lender has a variance in its Master Agreement that permits the ineligible loan characteristic.</p> <p>Loans that receive a Refer W Caution/IV recommendation represent a high degree of risk and are, generally, not eligible for delivery to Fannie Mae.</p>

Quality Assurance Component	DU Quality Assurance Requirements
Data Integrity Review and Re-Verification	
<p>Loan application</p>	<p>The lender must verify data integrity by checking the information provided on the loan application, the closing documents, and all data analyzed by DU. This data includes, but is not limited to, the borrower's name, Social Security number, property address, property type, mortgage term, mortgage type, loan purpose, loan amount, LTV, CLTV, employment, income, assets, liabilities, Section VII, and Section VIII.</p> <p>If any of these fields were entered incorrectly, the data must be corrected and the loan must be resubmitted to DU(except as stated earlier in the section, Resubmission policy on page 93 of this Guide).</p> <p>If the loan received one of the Social Security messages from DU described in Social Security number messages, the lender must perform due diligence to determine the accuracy of the borrower's Social Security number. The lender should review the other documents in the loan file, such as paystubs, W-2 Forms, tax returns, and the credit report. The lender must determine the appropriate steps to take to ensure the accuracy of the Social Security number.</p> <p>Note: If a loan initially received an Approve/Eligible recommendation based on incorrect data, and the loan is resubmitted with the correct data, the loan could receive a different underwriting recommendation from DU. The lender must follow the underwriting review based on the corrected DU recommendation.</p>

Quality Assurance Component	DU Quality Assurance Requirements
Data Integrity Review and Re-Verification	
	When a DU recommendation indicates that the loan was not eligible for delivery to Fannie Mae, the lender should advise its lead Fannie Mae account team of these findings.
Employment, income, and asset information	The lender must re-verify the borrower’s income, employment, and asset information directly with the source of the original documentation in accordance with the requirements of Fannie Mae’s <i>Selling Guide</i> , Part I, Chapter 3, Section 301.
Credit report	<p>The lender must verify that the credit report meets the requirements specified in this Guide, and that data in the credit report was accurately evaluated by DU. See Chapter 2, Underwriting Loans with DU, beginning on page 89.</p> <p>It is not necessary for the lender to obtain a new credit report for a DU-processed mortgage unless data in the credit report evaluated by DU included significant errors or data from the credit agency was not accurately evaluated by DU. (For example, if the credit report indicated that the borrower had a recent, previous bankruptcy and that information was not evaluated by DU, the underwriting recommendation may not be valid, and a new credit report should be obtained.)</p> <p>When a new credit report is obtained, the lender must re-verify the borrower’s credit history by obtaining a new three-in-file merged credit report from a source other than the original credit reporting agency.</p>
Property fieldwork documentation	<p>For 10% of the mortgages it selects for a quality assurance review, the lender must re-verify the appraisal (or property inspection) by ordering a review appraisal (or property inspection) to check the work of the original appraiser in accordance with the requirements of the <i>Selling Guide</i>, Part XI, Fannie Mae Announcements, and the Guide to Underwriting with Desktop Underwriter, Chapter 3.</p> <p>The review appraisal – or property inspection</p>

Quality Assurance Component	DU Quality Assurance Requirements
Data Integrity Review and Re-Verification	
	<p>report – must be consistent with the level of review that was conducted after DU’s recommendation was received. (For example, if the minimal appraisal documentation required by DU was a Form 2055 exterior-only appraisal, the quality assurance system should request the same.)</p> <p>If the loan received an excessive property valuation message from DU, the lender should take special care when reviewing the appraisal and underwriting the property.</p>
Material discrepancies	<p>If there are material discrepancies between the data that DU used and the data from the source documents that are not within the tolerances stated in this Guide, the loan application must be resubmitted to DU using correct data. See Resubmission policy on page 93.</p> <p>When material differences indicate that the loan was not eligible for delivery to Fannie Mae, the lender must contact its Fannie Mae Account team.</p>

Quality Assurance Component	DU Quality Assurance Requirements
Underwriting review based on DU’s recommendation	
Approve/Eligible EA-I, -II, -III/Eligible	<p>The quality assurance review focuses on validating the data integrity of the loan file. The lender is not required to underwrite the loan outside of DU. The review should confirm that all Verification Messages/Approval Conditions listed on the Underwriting Findings report have been satisfied and adequately documented.</p>
Refer/Eligible	<p>The quality assurance review should validate the data integrity of the loan file and address the reasons for referral to the lender’s underwriter and the steps that were taken to resolve or compensate for the conditions resulting in the referral.</p> <p>While it may not be necessary to completely re-underwrite the mortgage, the review must address whether the file includes sufficient written documentation to support the lender’s</p>

Quality Assurance Component	DU Quality Assurance Requirements
Underwriting review based on DU's recommendation	
	decision to approve the referred mortgage, and to ensure that the loan meets Fannie Mae's guidelines. The review should confirm that, at a minimum, all Verification Messages/Approval Conditions listed on the Underwriting Findings report have been satisfied and adequately documented.
Refer with Caution	The quality assurance review should validate the data integrity of the loan file and address the reasons for the referral to the lender and the steps that were taken to resolve or compensate for the conditions that resulted in the referral.
Out of Scope	The quality assurance review should be consistent with the review performed for a manually underwritten mortgage.
Ineligible (Approve, EA-I, -II, -III, Refer, or Refer with Caution)	<p>The review must confirm whether the lender has a negotiated contract that provides for the delivery of a mortgage with the characteristics in question and whether the file includes sufficient written documentation to support the lender's decision to approve the ineligible mortgage.</p> <p>In addition, the review must confirm whether the lender considered any additional layering of risk resulting from the ineligibility criteria in the lender's final decision to approve the loan.</p>

Post-closing vs. pre-funding reviews

Most quality assurance systems apply to post-closing mortgage reviews. However, since pre-funding reviews provide more timely feedback to the origination staff and can prevent the consideration of misrepresented information in the mortgage origination process, we strongly encourage a lender to include them as part of its quality assurance system.

Appendices

Appendix A: Required Data Elements – Loan Application (Form 1003)

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Section I. Type of Mortgage and Terms of Loan			
Pre-approval indicator			
Mortgage type applied for	X	X	
Other type text			X
Agency case number			X
Lender case number		X	
Original loan amount	X	X	
Interest rate	X	X	
Number of months	X	X	
Amortization type	X	X	
Other type explanation text			X
Product/ARM type text			
Section II. Property Information and Purpose of Loan			
Subject property street address(3)		X	
Property city(3)		X	
Property state(3)	X	X	
Property zip(3)		X	
Property ZIP + 4			X
Number of units	X	X	
Legal description type			X
Metes/bounds/other description			X
Year built			X
Purpose of loan	X	X	
Other purpose explanation text			X
Occupancy type	X	X	
Manner in which title held			X
Estate held	X	X	X
Title names text			X
<i>Construction:</i>			
Year lot acquired			X
Original cost			X
Amount existing liens			X
Present value of lot			X
Cost of improvements			X
<i>Refinance:</i>			
Year acquired			X
Original cost			X
Amount existing liens			X

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Purpose of refinance	if refinance	if refinance	
Describe improvements			X
Improvements made/to be made			X
Cost of improvements			X
<i>Sources of funds:</i>			
Source of funds type			X
Source of funds amount			X
Source of funds explanation			X
Section III. Borrower Information			
Social Security numbers	X	X	
Borrower first name	X	X	
Borrower middle name	if applicable	X	
Borrower last name	X	X	
Borrower generation	if applicable	X	
Home phone number			X
Age			
Date of Birth		X	
Years of school			X
Marital status		X	
Number of dependents			X
Ages of dependents			X
Borrower current street	X	X	
Borrower current city	X	X	
Borrower current state	X	X	
Borrower current zip	X	X	
Borrower ZIP + 4			X
Own/rent			X
Number of years at current residence			X
Months at residence			X
Borrower previous street			X
Borrower previous city			X
Borrower previous state			X
Borrower previous zip			X
Borrower previous ZIP + 4			X
Borrower previous own/rent			X
Borrower previous number of years			X
Borrower previous number of months			X
Section IV. Employment Information			
Current employer name		X	
Self-employed indicator	X	X	
Employer street			X
Employer city			X
Employer state			X
Employer zip			X
Employer ZIP + 4			X
Years on job	X	X	
Months on job	X	X	
Years in this line of work			X

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Position/title			X
Business phone			X
Former employer name			X
Former self-employed indicator			X
Former employer city			X
Former employer street			X
Former employer state			X
Former employer zip			X
Former employer ZIP + 4			X
Former employment from date			X
Former employment to date			X
Former monthly income amount			X
Former position/title			X
Former business phone			X
Current employment indicator	if applicable		
Section V. Monthly Income and Combined Housing Expense Information			
Base employment income	if applicable	if applicable	
Overtime income	if applicable	if applicable	
Bonus income	if applicable	if applicable	
Commission income	if applicable	if applicable	
Dividend/interest income	if applicable	if applicable	
Net rental income	(calculated)	(calculated)	
Subj Net cash flow	if applicable	if applicable	
Other income type	if applicable	if applicable	
Monthly income amount	if applicable	if applicable	
Present rent	if applicable	if applicable	
Present first P&I	if applicable	if applicable	
Present second P&I	if applicable	if applicable	
Present hazard insurance	if applicable	if applicable	
Present real estate taxes	if applicable	if applicable	
Present mortgage insurance	if applicable	if applicable	
Present HOA dues	if applicable	if applicable	
Other expense	if applicable	if applicable	
Total present housing payment(4)	(calculated)	(calculated)	
Proposed first P&I	(calculated)	(calculated)	
Proposed second P&I	if applicable	if applicable	
Proposed hazard insurance	X	X	
Proposed real estate taxes	X	X	
Proposed mortgage insurance	if applicable	if applicable	
Proposed HOA dues	if applicable	if applicable	
Proposed other expense	if applicable	if applicable	
Total proposed housing payment(5)	(calculated)	(calculated)	

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Section VI. Assets			
Jointly/not jointly		X	
Cash deposit held by			X
Institution name			X
Institution street			X
Institution city			X
Institution state			X
Institution zip			X
Institution ZIP + 4			X
Asset type	X	X	
Account number			X
Market value	X	X	
Number of shares indicator			X
Stock/bond description			X
<i>If type is automobile:</i>			
Auto description			X
<i>If type is life insurance:</i>			
Life insurance face value			X
Description if type is other		X	
Section VI. Liabilities			
Name of creditor		X	
Creditor street address			X
Creditor city			X
Creditor state			X
Creditor zip			X
Creditor ZIP + 4			X
Type of liability	X	X	
Account number		X	
Payment	X	X	
Balance	X	X	
Number of months	(calculated)	(calculated)	
Satisfied by sale/refinance indicator	if applicable	if applicable	
Recipient of alimony/child support (receiver name and \$ amount)		if applicable	
Job related expense information	if applicable	if applicable	
Section VI. Real Estate Owned			
Property street address		X	
Property city		X	
Property state		X	
Property zip		X	
Property ZIP + 4		X	
Plans for REO		X	
Property type		if not subject	
Market value		X	
Amount of mortgages/liens		if applicable	
Gross rental income		if applicable	
Mortgage payment		if applicable	
Insurance, maintenance, taxes, misc.		if applicable	
Net rental income		(calculated)	
Subject property indicator		if applicable	

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Current residence indicator		if applicable	
Section VII. Details of Transaction			
a. Purchase price	if applicable	if applicable	
b. Alterations, improvements, repairs	if applicable	if applicable	
c. Land	if applicable	if applicable	
d. Refinance	if applicable	if applicable	
e. Estimated prepaid items	if applicable	if applicable	
f. Estimated closing costs	if applicable	if applicable	
g. PMI, MIP, funding fee	if applicable	if applicable	
h. Discount (borrower paid)	if applicable	if applicable	
i. <i>Total costs</i>	<i>(calculated)</i>	<i>(calculated)</i>	
j. Subordinate financing	if applicable	if applicable	
k. Closing costs paid by seller	if applicable	if applicable	
l. <i>Other Credits</i> <i>(Total of Other Credit section)</i>	<i>(calculated)</i>	<i>(calculated)</i>	
m. <i>Loan amount</i>	<i>(calculated)</i>	<i>(calculated)</i>	
n. PMI, MIP, funding fee financed	if applicable	if applicable	
o. <i>Total loan amount (m+n)</i>	<i>(calculated)</i>	<i>(calculated)</i>	
p. <i>Cash from (-)/To borrower</i>	<i>(calculated)</i>	<i>(calculated)</i>	
HELOC Information			
Undrawn HELOC amount			
Other Credits			
Description of Other Credits	if applicable	if applicable	
Other credit Amount	if applicable	if applicable	
Section VIII. Declarations			
Declaration type	all required	all required	
Yes/No	all required	all required	
Explanation		if applicable	
Type of property owned		if applicable	
How title held code		if applicable	
Section IX. Acknowledgment and Agreement			
Borrower signature		X	
Borrower signature date		X	
Section X. Information for Government Monitoring Purposes			
Do not wish to furnish		X	
Ethnicity		X	
Race		X	
Other text			X
Sex		X	
How application taken code		X	
Interviewer name		X	
Interviewer date		X	
Interviewer phone number			X
Interviewer employer name		X	
Interviewer employer street address		X	
Street address 2		X	
Interviewer employer city		X	
Interviewer employer state		X	

Form 1003 field	Quick 1003 This information is required for DU submission(1).	Complete 1003 This information must be maintained in the permanent file.	Optional for Fannie Mae Form 1003
Interviewer employer zip		X	
Interviewer employer ZIP + 4		X	

Footnotes:

- (1) This column reflects the data entry requirements for the loan application in the DO/DU user interface. It does not represent data entry or integration requirements for other loan origination systems.
- (2) The information required for a “Fannie Mae complete Form 1003” is required on the “final” Form 1003 that is part of the permanent loan file of every loan. These elements do not have to be submitted to DU; however, they do need to be entered on the final Form 1003.
- (3) The entire subject property address must be completed in order for the property fieldwork analysis to be completed. Loans can be underwritten without this information; however, DU will not specify the required level of property fieldwork.
- (4) The present housing payment should always be the current housing payment for the borrower’s principal residence.
- (5) The proposed housing payment will always be the proposed payment for the subject property (principal residence, second home, or investment property as applicable).

Appendix B: DU Required Data Elements Additional Data Screen ⁽¹⁾

Data fields in the DO/DU loan application	Required for DU submission (2)
Appraisal Information	
Property Appraised Value: (Actual) (Estimated)	X (3)
Fieldwork Obtained	
Appraiser information (in Full 1003)	
Loan Information	
Community Lending*	X
Seller Provided Below Market Financing	
First Year Buydown Rate	if applicable
Lien Type	X
Payment Frequency	X
Repayment Type	X
Subject Property Type	X
Balloon indicator	if "Yes"
Balloon Mortgage Term (months)	if "Yes"
Will Escrow be Waived?	
Product Code (in Full 1003)	
Loan Documentation Code (in Full 1003)	
PUD/Condo Classification Code (in Full 1003)	
If ARM:	
ARM Plan	X
ARM Index Value	
ARM Index Margin	
ARM Qualifying Rate	
APR Spread %	
HOEPA indicator	if "Yes"
*If Community Lending:	
Metropolitan Statistical Area or County	X
Community Lending Product	X
FannieNeighbors Eligible	X
Community Seconds	X
Income Limit	
HUD Area Median Income	
Income Limit Adjustment Factor	
Community Lending Income Limit	

Footnotes:

- (1) The Additional Case Date screen contains additional data fields, some of which must be completed before a loan can be submitted to DU. Lenders are not required to prepare a Form 1008 for loans underwritten by DU. A copy of the Fannie Mae Underwriting Findings report must be maintained in the permanent loan file.
- (2) This column indicates which fields must be completed prior to submitting the loan to DU.
- (3) When an appraisal is obtained, this field must reflect the actual appraised value.

Appendix C:

Guidelines for Entering the Subject Property Address

One of the key steps in DU's collateral assessment process is the ability to match a submitted property address to an address in our database. Once matched, DU may be able to confirm that the submitted sales price or estimated value is adequate for the loan transaction, and recommend either a property inspection or a streamlined appraisal. The proper entry of address data into DU is extremely important. Inaccurate or missing address entries can cause the system to determine that a submitted address is ineligible for streamlined fieldwork and reporting.

Entering address data

- Place the house number at the beginning of the street address (if there is not a separate field for the house number).
- Enter either complete names (e.g., Avenue or Street) or the appropriate abbreviations provided in the following tables.
- Enter a valid street suffix in uppercase (e.g., AVE, PKWY, or TER). See [Standard address-related abbreviation tables](#) on page 214.
- Include apartment, suite, unit number, or letters after the street name if there is not a separate unit number field.
- Include the city, state, and ZIP Code of the subject property. For the state, enter the abbreviation recommended by the U.S. Postal Service.
- Do not use punctuation in addresses (e.g., periods, commas, colons, semicolons, slashes, and asterisks). Dashes are permitted if they apply to the street number or ZIP+4.
- Do not include the pound sign (“#”) for the unit number if the unit number is entered in the unit number field. (DU will automatically insert a # symbol in the address in the Findings and printed loan application.) *Do* enter a pound sign before the unit number if you are entering the unit number, together with the street number and name, all in one field.
- Do not include identifiers such as APT, BLDG, UNIT, or STE in the address or unit number fields.
- Include pre-directional abbreviations (e.g., 123 N Main St) and post-directional (e.g., 123 Broad Street NW) in the Street Name field. See the list below.
- Ensure accurate spelling and typing.
- Re-enter the property address if it changes and resubmit the loan to DU.

Entering address data for pre-qualification loans

When using DU for loans where the address is unknown, or not yet determined, enter the state information only. Do not enter any data in the following fields: street address, city, or ZIP Code. However, if your loan origination system requires an entry for the street address, we request that you enter TBD in that field.

The system will then issue a message acknowledging that the submitted address is not complete, and, therefore, that DU cannot recommend any type of appraisal fieldwork. You will receive no appraisal recommendation until a complete address is entered. We believe that this message will assist our customers in keeping track of their pre-qualification loans and help to eliminate any confusion as to what appraisal fieldwork and documentation are required until an actual address is entered. Always re-enter the subject address once it is finalized to determine the actual level of appraisal fieldwork required for delivery.

Standard address-related abbreviation tables¹

To ensure that the data you enter is interpreted correctly, check the following tables for the standard address-related information:

[Table 1: Pre- and post-directional abbreviations](#)

[Table 2: Street suffix abbreviations](#)

[Table 3: Routes](#)

[Table 4: Special characters](#)

Table 1: Pre- and post-directional abbreviations

Direction	Abbreviation	Examples
North	N	123 N Broad Street
South	S	123 S Broad Street
East	E	123 E Broad Street
West	W	123 W Broad Street
Northeast	NE	123 Broad Street NE
Northwest	NW	123 Broad Street NW
Southeast	SE	123 Broad Street SE
Southwest	SW	123 Broad Street SW

¹ Excerpted from U.S. Postal Addressing Standards, Publication 28, November 1997.

Note: There is one exception to this rule. If the street name is a directional word – North, East, South, or West – enter the full word for the street name (e.g., 123 North ST SW).

Table 2: Street suffix abbreviations

The following table lists examples of primary street suffix names and common street types and their suffix abbreviations. These street suffix abbreviations are the recommended official Standard Suffix Abbreviations of the U.S. Postal Service.

Street Type	Abbreviation	Example
Alley	ALY	123 Main ALY
Annex	ANX	123 Main ANX
Arcade	ARC	123 Main ARC
Avenue	AVE	123 Main AVE
Bayou	BYU	123 Main BYU
Beach	BCH	123 Main BCH
Bend	BND	123 Main BND
Bluff	BLF	123 Main BLF
Bluffs	BLFS	123 Main BLFS
Bottom	BTM	123 Main BTM
Boulevard	BLVD	123 Main BLVD
Branch	BR	123 Main BR
Bridge	BRG	123 Main BRG
Brook	BRK	123 Main BRK
Brooks	BRKS	123 Main BRKS
Burg	BG	123 Main BG
Burgs	BGS	123 Main BGS
Bypass	BYP	123 Main BYP
Camp	CP	123 Main CP
Canyon	CYN	123 Main CYN
Cape	CPE	123 Main CPE
Causeway	CSWY	123 Main CSWY
Center	CTR	123 Main CTR
Centers	CTRS	123 Main CTRS
Circle	CIR	123 Main CIR
Circles	CIRS	123 Main CIRS

Street Type	Abbreviation	Example
Cliff	CLF	123 Main CLF
Cliffs	CLFS	123 Main CLFS
Club	CLB	123 Main CLB
Common	CMN	123 Main CMN
Commons	CMNS	123 Main CMNS
Corner	COR	123 Main COR
Corners	CORS	123 Main CORS
Course	CRSE	123 Main CRSE
Court	CT	123 Main CT
Courts	CTS	123 Main CTS
Cove	CV	123 Main CV
Coves	CVS	123 Main CVS
Creek	CRK	123 Main CRK
Crescent	CRES	123 Main CRES
Crest	CRST	123 Main CRST
Crossing	XING	123 Main XING
Crossroad	XRD	123 Main XRD
Crossroads	XRDS	123 Main XRDS
Curve	CURV	123 Main CURV
Dale	DL	123 Main DL
Dam	DM	123 Main DM
Divide	DV	123 Main DV
Drive	DR	123 Main DR
Drives	DRS	123 Main DRS
Estate	EST	123 Main EST
Estates	ESTS	123 Main ESTS
Expressway	EXPY	123 Main EXPY
Extension	EXT	123 Main EXT
Extensions	EXTS	123 Main EXTS
Fall	FALL	123 Main FALL
Falls	FLS	123 Main FLS
Ferry	FRY	123 Main FRY

Street Type	Abbreviation	Example
Field	FLD	123 Main FLD
Fields	FLDS	123 Main FLDS
Flat	FLT	123 Main FLT
Flats	FLTS	123 Main FLTS
Ford	FRD	123 Main FRD
Fords	FRDS	123 Main FRDS
Forest	FRST	123 Main FRST
Forge	FRG	123 Main FRG
Forges	FRGS	123 Main FRGS
Fork	FRK	123 Main FRK
Forks	FRKS	123 Main FRKS
Fort	FT	123 Main FT
Freeway	FWY	123 Main FWY
Garden	GDN	123 Main GDN
Gardens	GDNS	123 Main GDNS
Gateway	GTWY	123 Main GTWY
Glen	GLN	123 Main GLN
Glens	GLNS	123 Main GLNS
Green	GRN	123 Main GRN
Greens	GRNS	123 Main GRNS
Grove	GRV	123 Main GRV
Groves	GRVS	123 Main GRVS
Harbor	HBR	123 Main HBR
Harbors	HBRS	123 Main HBRS
Haven	HVN	123 Main HVN
Heights	HTS	123 Main HTS
Highway	HWY	123 Main HWY
Hill	HL	123 Main HL
Hills	HLS	123 Main HLS
Hollow	HOLW	123 Main HOLW
Inlet	INLT	123 Main INLT
Island	IS	123 Main IS

Street Type	Abbreviation	Example
Islands	ISS	123 Main ISS
Isle	ISLE	123 Main ISLE
Junction	JCT	123 Main JCT
Junctions	JCTS	123 Main JCTS
Key	KY	123 Main KY
Keys	KYS	123 Main KYS
Knoll	KNL	123 Main KNL
Knolls	KNLS	123 Main KNLS
Lake	LK	123 Main LK
Lakes	LKS	123 Main LKS
Land	LAND	123 Main LAND
Landing	LNDG	123 Main LNDG
Lane	LN	123 Main LN
Light	LGT	123 Main LGT
Lights	LGTS	123 Main LGTS
Loaf	LF	123 Main LF
Lock	LCK	123 Main LCK
Locks	LCKS	123 Main LCKS
Lodge	LDG	123 Main LDG
Loop	LOOP	123 Main LOOP
Mall	MALL	123 Main MALL
Manor	MNR	123 Main MNR
Manors	MNRS	123 Main MNRS
Meadow	MDW	123 Main MDW
Meadows	MDWS	123 Main MDWS
Mews	MEWS	123 Main MEWS
Mill	ML	123 Main ML
Mills	MLS	123 Main MLS
Mission	MSN	123 Main MSN
Motorway	MTWY	123 Main MTWY
Mount	MT	123 Main MT
Mountain	MTN	123 Main MTN

Street Type	Abbreviation	Example
Mountains	MTNS	123 Main MTNS
Neck	NCK	123 Main NCK
Orchard	ORCH	123 Main ORCH
Oval	OVAL	123 Main OVAL
Overpass	OPAS	123 Main OPAS
Park	PARK	123 Main PARK
Parks	PARKS	123 Main PARK
Parkway	PKWY	123 Main PKWY
Pass	PASS	123 Main PASS
Passage	PSGE	123 Main PSGE
Path	PATH	123 Main PATH
Pike	PIKE	123 Main PIKE
Pine	PNE	123 Main PNE
Pines	PNES	123 Main PNES
Place	PL	123 Main PL
Plain	PLN	123 Main PLN
Plains	PLNS	123 Main PLNS
Plaza	PLZ	123 Main PLZ
Point	PT	123 Main PT
Points	PTS	123 Main PTS
Port	PRT	123 Main PRT
Ports	PRTS	123 Main PRTS
Prairie	PR	123 Main PR
Radial	RADL	123 Main RADL
Ramp	RAMP	123 Main RAMP
Ranch	RNCH	123 Main RNCH
Rapid	RPD	123 Main RPD
Rapids	RPDS	123 Main RPDS
Rest	RST	123 Main RST
Ridge	RDG	123 Main RDG
Ridges	RDGS	123 Main RDGS
River	RIV	123 Main RIV

Street Type	Abbreviation	Example
Road	RD	123 Main RD
Roads	RDS	123 Main RDS
Route	RTE	123 Main RTE
Row	ROW	123 Main ROW
Rue	RUE	123 Main RUE
Run	RUN	123 Main RUN
Shoal	SHL	123 Main SHL
Shoals	SHLS	123 Main SHLS
Shore	SHR	123 Main SHR
Shores	SHRS	123 Main SHRS
Skyway	SKWY	123 Main SKWY
Spring	SPG	123 Main SPG
Springs	SPGS	123 Main SPGS
Spur	SPUR	123 Main SPUR
Spurs	SPURS	123 Main SPUR
Square	SQ	123 Main SQ
Squares	SQS	123 Main and East SQS
Station	STA	123 Main STA
Stravenue	STRA	123 Main STRA
Stream	STRM	123 Main STRM
Street	ST	123 Main ST
Streets	STS	123 Main and East STS
Summit	SMT	123 Main SMT
Terrace	TER	123 Main TER
Throughway	TRWY	123 Main TRWY
Trace	TRCE	123 Main TRCE
Track	TRAK	123 Main TRAK
Trafficway	TRFY	123 Main TRFY
Trail	TRL	123 Main TRL
Trailer	TRLR	123 Main TRLR
Tunnel	TUNL	123 Main TUNL
Turnpike	TPKE	123 Main TPKE

Street Type	Abbreviation	Example
Underpass	UPAS	123 Main UPAS
Union	UN	123 Main UN
Unions	UNS	123 Main UNS
Valley	VLY	123 Main VLY
Viaduct	VIA	123 Main VIA
View	VW	123 Main VW
Views	VWS	123 Main VWS
Village	VLG	123 Main VLG
Villages	VLGS	123 Main VLGS
Ville	VL	123 Main VL
Vista	VIS	123 Main VIS
Walk	WALK	123 Main WALK
Walks	WALK	123 Main WALK
Wall	WALL	123 Main WALL
Way	WAY	123 Main WAY
Ways	WAYS	123 Main and East WAYS
Well	WL	123 Main WL
Wells	WLS	123 Main WLS

Table 3: Routes

Address Type	Abbreviation	Example
Route	RT	RT 30 Main ST
Rural Free Delivery	RFD	RFD 5
Rural Route	RR	RR 2

Table 4: Special characters

Remove all special characters, multiple blanks, and punctuation as listed below.

Spaces	Double spaces/blanks change to single-space or blank, except between state abbreviations and ZIP Codes or ZIP+4 Codes. Example: 123<space> Main ST Anytown,<space>GA<space><space>12345
*	Asterisks
,	Commas
.	Periods
()	Parentheses
" "	Quotations
:	Colons
;	Semi-colons
'	Apostrophes
-	Hyphens should only be used in the ZIP+4 Code and in the street number. Spaces before and after the hyphen or slashes (/) should removed from the address line. Example: GA 12345-6789
@	At symbol
&	Ampersand

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