Contents:

Fannie Mae Underwriting Guidelines Matrix

Although conventional loans meet the requirements of Fannie Mae and Freddie Mac, a greater emphasis here will be on Fannie Mae, the larger of the two GSEs.

Standard Fannie Mae Conforming Guidelines

A mortgage loan originator originating loan files must meet pre-determined underwriting guidelines to ensure a borrower's mortgage is saleable to Fannie Mae. Although many mortgage standards are universal, every originator should become familiar with significant underwriting criteria. Originators can obtain a more extensive review of these guidelines directly from Fannie Mae's servicing guide at http://www.fanniemae.com. Below is an overview of important underwriting guidelines.

Standard Underwriting Guidelines Matrix
Properties: single-family residence, 2-4 units, co-ops, leasehold estates, manufactured homes
Occupancy Type: principal residence, second homes and investment properties
Age of credit documents: Maximum age of credit documents is 120 days
Transaction Types: purchase money, refinance transactions, co-op share loans, mortgages with financed mortgage insurance
Second Liens: Closed-end seconds, HELOCs
Loan Purpose: Purchase, limited cash-out, cash-out
Amortization Type: fully amortized fixed rate, adjustable rate mortgages, convertible ARMs, balloon mortgages, biweekly payment schedule, temporary interest rate buy down
Borrower Eligibility: Persons who are legally able to obtain financing depending on state law. "There is no maximum age limit." **Non-US Citizens: "**Lawful permanent and non-permanent residents of the U.S." Each lender is responsible for determining eligibility status.
Credit Score: minimum 620 credit score; credit score requirements vary by transaction type, number of units and the following: Loan-to-Value (LTV), Combined Loan-to-Value, (CLTV), High Combined Loan to Value (HCLTV). Freddie Mac term for HCLTV is Total Loan-to-Value (TLTV)
LTV: • Purchase – The loan amount as a percentage of the purchase price or appraised value, whichever is less • Refinance – The loan amount as a percentage of the appraised value **CLTV:** Combines more than one loan **TLTV:** All outstanding loans, plus any available line of credit (HELOC), also referred to as HCLTV under Fannie Mae
Pre-purchase Education and Counseling: "HomeReady" borrowers will be required to take a high-quality online homeownership education course offered by Framework® Reference: Selling Guide Announcement SEL-2015-10 (September 29, 2015).

Fannie Mae Underwriting Guidelines Matrix

<table>
<tr><th colspan="3">Income</th></tr>
<tr><td>General</td><td>Salary</td><td>Self-employment</td></tr>
<tr><td>Mortgage loan originator to request permission to obtain tax return (IRS Form4506-T)
Non-taxable income can be used to qualify a borrower if the income is likely to continue for three years (Social Security, disability retirement, child support payment, workman's compensation, certain types of public assistance)
Borrower's non-taxable income may be grossed up by 25%</td><td>Evidence of receipt of stable income for two years
Likelihood of continuance of income for three years
Verify the source of income
Provide evidence of most recent 30 days' earnings
W2s covering the most recent two years
Verification of employment from borrower's employer (verbal or written)
Third-party verification source acceptable (payroll vendor)</td><td>Tax return for borrower earning 25% of their income from commissions
Individual with 25% or more ownership in a business
Borrowers employed by family member, receiving rental income, claiming business unreimbursed expenses; periodic employment</td></tr>
<tr><td colspan="3"><u>Under what conditions are tax returns required:</u>
Borrowers earning 25% of their income from commissions
Individuals with 25% or more ownership in a business
Borrowers employed by family members, receiving rental income, claiming business unreimbursed expenses
Periodic employment</td></tr>
<tr><td><u>Commission</u>:
Average of most recent two years' income</td><td><u>Bonus and/or Overtime</u>
Average income for the last two years</td><td><u>Student and Installment Loans</u>
Qualifying borrowers when no monthly payment is reflected:
1% - Student Loan Balances
5% - Installment Debt amount</td></tr>
<tr><th colspan="3">Assets</th></tr>
<tr><td><u>Earnest Money</u>
Must be borrower's own funds.
Considered a good faith deposit in a real estate purchase transaction.
Funds will be credited at closing.</td><td><u>Reserve</u>
Funds which can be easily converted to cash</td><td><u>Verification</u>
Verification of Deposit (VOD), bank and/ or portfolio statements for the most recent two months</td></tr>
<tr><td colspan="3">Acceptable Sources of Reserves – Generally funds that are easily convertible to cash</td></tr>
<tr><td colspan="3">Unacceptable Sources of Reserves – Funds that have not been vested and cannot easily be converted</td></tr>
</table>

into cash

Stocks, bonds, mutual funds: Maximum 100% of vested balance can be used to establish reserves

Retirement: Maximum 60% of non-vested balance (100% of vested balance) can be used to establish reserves

Stock options and non-restricted stock are no longer eligible for use as reserves

Gift Funds: Acceptable from an eligible source, such as relative, domestic partner, fiancée, fiancé, church, municipality, or non-profit organization. "Must not be an interested third-party." (**The seller or lender cannot provide gift funds, unless they are an acceptable donor**).

If LTV ≤ 80% - 1-4 unit principal residence or second home – no min. contribution required from borrower

If LTV > 80% - 1 unit principal residence - no min. contribution required from borrower
2-4 unit properties – 5% contribution (3% special programs)required from borrower.

Credit

Credit Score	*Traditional Credit Reports*	*Non-traditional Credit Reports*
• Required for most Fannie Mae products which can be obtained from the three FICO system credit bureaus: Equifax, Experian and Trans Union. • Each borrower should have a minimum of two scores. *Representative Score* • Two credit scores~~;~~ use the lower of the two • Use the middle score if three scores • If multiple borrowers, use the lower of the representative score	• Require four tradelines with a mix of revolving and installment for 24 months • No history of delinquency for 30, 60, 90+ days • No public record which would jeopardize lien (judgments, foreclosures, collections, charged-off accounts) • No history of delinquent mortgage or rental payments • Revolving Accounts: No late reporting in the most recent 12 months; one 30-day late in 24 months • Installments: No late reporting in the most recent 24 months • DTI limit: 50%	• Four sources of active non-traditional credit with a 12-month history • No delinquent rental payment history • Only one 30-day delinquency from one of the sources

Liabilities

Types of Liabilities: owner-occupied mortgage payment, revolving/open-end and charge accounts, lease payments, real estate loans, HELOCs, non-reimbursed employee expenses, alimony, child support, all other reoccurring monthly debts. For installment debts with a balance of less than 10 payments, an underwriter may choose not to include them in the qualifying debt ratios.

Total Monthly Debts or Debt to income ratio (DTI) or Debt Service: 36% for manually underwritten files including the housing payment.

Housing Expense: 28% for manually underwritten files which includes principal, interest, escrowed taxes and hazard insurance; mortgage insurance, homeowner's association dues; monthly condo or co-op fees and any subordinate financing, if applicable.

Fannie Mae Underwriting Guidelines Matrix

Hazard (property) Insurance Coverage: **"**For a first mortgage, Fannie Mae requires coverage equal to the lesser of the following: ➢100% of the insurable value of the improvements, as established by the property insurer; or ➢the unpaid principal balance of the mortgage, as long as it equals the minimum amount—80% of the insurable value of the improvements—required to compensate for damage or loss on a replacement cost basis. If it does not, then coverage that does provide the minimum required amount must be obtained." **Deductible Amount: "**The maximum allowable deductible for insurance covering a property (including common elements in a PUD, condo, or co-op project) securing a first mortgage loan is **5% of the face amount of the policy**. When a policy provides for a separate wind-loss deductible (either in the policy itself or in a separate endorsement), that deductible must be no greater than 5% of the face amount of the policy." **Flood Insurance: "**The lender must ensure that any flood insurance required for the security property is in place."
Mortgage Insurance: When the lender's loan-to-value of the property exceeds 80%, or the lender is financing more than 80% of the value of the property securing the loan, the borrower will be required to carry mortgage insurance to protect the lender in the event of the borrower's default. This mortgage insurance is referred to as **Private Mortgage Insurance (PMI)**. The Homeowners Protection Act (HPA) sets the requirements for cancelation of mortgage insurance. 1. **Borrower requested termination**: Loan-to-Value reaches 80% based on the value of the home at the time of the loan origination and the borrower requests termination 2. **Automatic termination**: Loan-to-Value reaches 78%, of the original value and cancellation is automatic. 3. **Good payment history**: ***Requested*** termination requires a good payment history: (a) No **60 day** late payments in 24 months preceding termination (b) No **30 day** late payments in the 12 months preceding termination (c) Must be **current** at the time of termination**.** The PMI premium is determined by the PMI company and is based on the LTV and other factors, such as a borrower's credit and other risk factors. PMI is based on the loan amount, calculated on an annual basis and paid monthly with each mortgage payment.
Net Rental Income Formula: (gross rental income* × 75%) − mortgage payment − insurance/maintenance/taxes/misc. = net rental income **Used only if tax returns are not available.*
Tax Forms: Schedule C – Sole Proprietor Schedule E – Rental Schedules Form 2106 – Unreimbursed Employee Expenses Form 4506-T or Form 8821–To obtain tax transcripts

Fannie Mae Underwriting Guidelines Matrix

Occupancy:

Timeframe to occupy a property after settlement is 60 days.

Seller Concessions: Fannie Mae will allow the seller or an interested party to contribute to the borrower's closing costs and/or prepaid charges under the following conditions based on the l**ower** of the sales price or the appraised value.

Occupancy Type	LTV/CLTV Ratio	**Maximum Contribution** *(Based on the Sales Price)*
Principal residence or second home	Greater than 90%	3%
	75.01% – 90%	6%
	75% or less	9%
Investment property	All CLTV ratios	2%

Automated Underwriting: Fannie Mae and Freddie Mac uses a computer-based **automated underwriting system (AUS)** to evaluate an applicant's information to provide automated findings. Based on the applicant's information entered, the electronic system will either provide recommendations to accept a loan or refer the loan to an underwriter for a manual review of the file.

Both Fannie Mae and Freddie Mac have their own proprietary automated underwriting system.

- The Fannie Mae system is **Desktop Underwriter (DU)**
- The Freddie Mac system is **Loan Prospector (LP)**

A borrower must provide documentation to support any information submitted to the AUS systems:

- The findings from the AUS systems outline the required documentation that needs to be submitted with the loan file.
- Each file, whether it receives an approval or referral from the automated system, must be a **fully documented loan** (most recent record of the past 30-days of paystubs, the most recent 60-days of bank statements and the most recent two years of W2 tax forms).

Source: Fannie Mae

Fannie Mae Underwriting Guidelines Matrix

Definitions and Terms

Word/Term	Fannie Underwriting and Definitions Guide
Properties	▪ **Single family** – A single unit ▪ **Multi-family** – considered 2-4 units ▪ **Co-ops** – ownership rights to a unit where the owns share in common services and expenses ▪ **Leasehold estates** – properties where the land has a long-term lease which will extend 5 years beyond the loan term ▪ **Manufactured homes** – Manufactured homes attached to land and considered real property (excludes rental units)
Occupancy Type	▪ **Principle residence** – occupied by owner as primary residence ▪ **Second home** – typically a vacation home in a resort area must be at least 50 miles from primary residence ▪ **Investment properties** – purchased as non-owner-occupied properties
Age of credit documentation	Credit documents such as credit reports, income and asset documents like bank statements must not be more than 4 months old when the borrower signs the promissory note at closing.
Transaction Types	▪ **Purchase money mortgage** – where proceeds are used to finance the purchase of a home. Non- Fannie Mae seller financing may also be defined as a purchase money mortgage. ▪ **Refinance** – replacing an existing loan with another loan ▪ **CO-OP share loans** – financing a property in a co-op where owners share in common services ▪ **Mortgages with financed mortgage insurance** – mortgages where the upfront mortgage insurance premium is financed into the loan
Second Liens	Loans that are not primary and are in a junior position. These loans can: ▪ Be closed-end with a defined ending date with no reuse of the loan funds ▪ Open end secured by the equity in the home called a Home Equity Line of Credit (HELOC)
Loan purpose	▪ **Purchase** – loan to finance a real estate purchase ▪ **Limited cash out** – a refinance transaction where the lender will allow the borrower some cash back typically limited to 2% of the loan amount or $2,000 whichever is less ▪ **Cash out** – a refinance transaction where the borrower is removing cash from the equity in the property to be used for expenditures that are not associated with the property (ex. debt consolidation)
Amortization Type/Loan Products	Amortization – loan term and payment period ▪ **Fully amortized fixed rate** – loan principal and interest payments remain the same for the life of the loan and will pay off the loans by the due date ▪ **Adjustable rate loans** – loans where the rate can adjust over the life of the loan

Fannie Mae Underwriting Guidelines Matrix

	▪ **Convertible ARM** – an adjustable rate loan where a small fee is paid at closing giving the borrower the right to transfer to a fixed rate without refinancing the loan ▪ **Balloon mortgage** – a loan where the payments will not pay off the loan by the due date of the loan. Borrower's usually refinance to pay off a balloon mortgage ▪ **Biweekly payment schedule** – making payments every two weeks. Equates to one extra payment a year and reduces interest over the life of the loan ▪ **Temporary interest rate buy-down** – means that the borrower will have a lower interest during the first few years of the loan. Ex. 2/1 buy-down, the note rate on the loan is reduced by 2% in year one and 1% in year 2. The lender or seller generally pay for the cost of the buy-down.
Borrower eligibility	▪ State law determines when a borrower is old enough to enter into a contract ▪ The Equal Credit Opportunity Act (ECOA) does not allow discrimination based on age if the borrower is old enough to enter into a contract ▪ There is no maximum age limit
Non-US Citizens	Lawful permanent and non-permanent residents of the U.S. are eligible for financing. The lender determines eligibility.
Credit Score	Fannie Mae uses the representative score as part of the borrower's qualifying process: ▪ **Single score** – not eligible ▪ **Two scores** – use the lower of the two as the representative score ▪ **Three scores** – use the middle score as the representative score ▪ **Multiple borrowers** – use the lowest representative score Minimum credit score eligible for purchase by Fannie Mae ▪ Fixed rate – 640 ▪ ARM – 660
LTV/CLTV/TLTV	Lenders make loans based on the value of the property. ▪ **Loan to value** – the loan amount as a percentage of the purchase price or appraised value whichever is less ▪ **Combined loan to value** – combining more than one loan as a percentage of the value ▪ **Total Loan to Value** – is a Freddie Mac term that means the maximum debt potential. A combination of any outstanding debts against the property and the HELOC.
HomeReady Mortgage	Designed for credit worthy low to moderate income borrowers. Provides expanded financing in low income communities and requires borrowers to participate in pre-purchase education.
IRS Form 4506T	Borrower signs form allowing the lender to get a copy of the filed tax transcript as part of the income verification process

Fannie Mae Underwriting Guidelines Matrix

Non-taxable income	▪ Non-taxable income like social security, disability and child support can be used as qualifying income as long as it will continue for at least three years. ▪ ECOA does not allow discrimination based on income. Since gross income is used to qualify the borrower to make it fair for the non-taxable income we increase it by 25 percent to make it equivalent to taxable income. This is called grossing up income.
Salary	▪ Must show evidence of stable income over past two years ▪ Must show that non-employment income will likely continue for at least three more years (ex. Social Security, Child Support, Disability, Alimony) ▪ Must provide most recent 30 days of pay-stubs ▪ Provide W2s covering the most recent 2 years ▪ Verbal employer verification ▪ Third party verification accepted (ex. Payroll service)
Self - Employment	Employed individuals are considered self-employed under the following circumstances: ▪ Borrower earns 25% or more of income in commission or incentives ▪ Borrower owns 25% or more of a company ▪ Borrower is employed by family members
Tax Returns required	Fannie Mae requires two years of filed tax returns for the following: ▪ Borrower earns 25% or more of income in commission or incentives ▪ Borrower owns 25% or more of a company ▪ Borrower is employed by family members ▪ Borrower has periodic employment ▪ Borrower has rental property ▪ Borrower claiming unreimbursed business expenses
Commission, bonus, overtime, tips and self - employment income	These forms of income may be used if the income can be verified that it has been received for at least two years
Debt balance no monthly payment	▪ **General** – multiply the balance by 5% to use as a qualifying payment ▪ **Student loans** - multiply the balance by 1% to use as a qualifying payment
Earnest Money Deposit	▪ Good faith deposit held by a seller or real estate broker on a real estate purchase transaction ▪ Funds are credited to the borrower when the loan closes
Reserves	Assets that are easily converted to cash. May be required by the underwriter to provide more security that funds will be available to meet the monthly debt commitments.
Acceptable Reserves	▪ **Stock portfolio account** – allows 100% of account value for reserves ▪ **Retirement account** – allows 60% of non-vested interest in account to be used for reserves. IRS penalties assessed for early withdrawal
Gift Funds	Fannie Mae allows gift funds on primary and second home purchases, not

	investment properties. They must come from an acceptable donor: ▪ Relative ▪ Domestic partner ▪ Fiancée ▪ Non-profit The donor may not be, or affiliated with, the: ▪ Builder ▪ Developer ▪ Real estate agent ▪ Seller ▪ Or other interested party to the transaction
Credit Score	Fannie Mae uses the FICO credit reporting system, developed by the Fair Isaac and Company. The system uses three national credit bureaus: ▪ Equifax ▪ Experian ▪ Transunion
Representative credit score	Each bureau provides a score that is derived from an algorithm that lenders use as part of the determination that a borrower is likely to meet the loan payment requirements. Fannie Mae uses the representative score that will generally impact the interest rate and terms of the loan. Representative Score (requires a minimum of two scores) ▪ Two bureaus reporting (two scores) – use the lower of the two scores ▪ Three bureaus reporting (three scores) – use the middle numerical score ▪ More than one borrower – use the lowest representative score
Traditional Credit	▪ Required credit and public record information for each locality where the borrower has lived within the past 2 years All credit must be reported that is not considered obsolete: ▪ General credit information is not considered obsolete up to 7 years (legal statute) ▪ Bankruptcy is not considered obsolete up to 10 years (legal requirement)
Non-Traditional Credit	▪ Borrower does not have a credit score ▪ Use rental, utilities and other credit records not reported in traditional credit reports ▪ Generally, 12-month history required
Liabilities	There are levels of liabilities highest to lowest: ▪ Mortgage payment ▪ Installment ▪ Revolving The underwriter may choose to not include installment debt with 10 payments or less to pay. This will provide the borrower with greater qualifying loan amount.
Debt to income	▪ Monthly debts as a percentage of monthly gross income, income before

(DTI) **(Back end ratio)** **Housing payment to income** **(Front end ratio)**	taxes ▪ For manually underwritten conventional loans the maximum DTI is 36% ▪ Included in the DTI is the amount of debt allowed for the housing payment. For conventional loans the maximum housing payment ratio is 28%
Automated underwriting (AUS)	Purchasers, insurers and guarantors of mortgage loans make decisions based on the borrower's ability to meet delivery requirements. These entities have significant historical data on loan performance based on borrower profiles. This data is incorporated in computer based models that allow any borrower's credit profile to be compared to borrowers in the database. This allows for a system decision, not a human underwriter determination. Either the system will recommend that the loan be approved, denied or submitted for further review (refer) by an underwriter and also establish the required supporting documents. This process is automated underwriting (AUS). It often allows DTI ratios that exceed the maximum allowed by a manual underwritten loan. ex. greater than 36% for conventional. ▪ Fannie Mae AUS system – Desktop underwriter (DU) ▪ Freddie Mac AUS system – Loan prospector (LP) Lenders that meet the terms of an AUS decision are protected from liability in cases where the DTI exceeded 36% because the decision was not determined by the lender but by the AUS.
Hazard insurance	Insurance coverage is determined by the insurance company and is only for the improvements (dwelling) not the land: Requires the lower of: ▪ 100% of the insurable value of the improvements ▪ The unpaid balance, but not less than 80% of the value of the improvements It a violation of the law to require a borrower to carry insurance coverage that exceeds the replacement value of the improvements. The borrower can have a deductible that is up to 5 percent of the face amount of the policy.
Flood insurance	The lender is responsible for determining if the structure is located in a flood zone which would require the borrower to carry flood insurance.
Mortgage Insurance for conventional, Private mortgage insurance (PMI)	Mortgage insurance is required when the lender originating a conventional loan is loaning the borrower more than 80% of the value. Here are the facts about Private Mortgage Insurance required on conventional conforming loans: ▪ Required if the lender is loaning more than 80% of the value

	▪ Mortgage insurance premiums are primarily based on LTV, credit score, and loan product. The higher the risk the higher the mortgage insurance premium. ▪ Coverage limitations are limited to a maximum of 35% ○ Ex. A borrower defaults and the outstanding balance is $100,000 with 35% coverage the lender will receive $35,000 and will need to receive $65,000 in the foreclosure sale to break even.

Homeowners Protection Act (HPA)	Prior to the late 90s if a borrower was required to carry mortgage insurance there was no required or automatic mechanism to cancel the insurance. Uninformed consumers often carried mortgage insurance way beyond the time the loan was a risk to the lender. To address this issue Congress passed the Homeowners Protection Act which became effective in 1999.
	
	HPA has two methods to terminate private mortgage insurance on conventional loans:
	▪ **Automatic termination**
	    ○ Automatically terminates when the borrower's loan balance reaches 78% of the original value
	    ○ No required action by the borrower for the termination to occur other than the borrower is current on the loan at the time of termination
	▪ **Requested termination**
	    ○ Available to borrowers that have paid down their mortgage loan balance to 80% of the original value.
	    ○ Borrower must initiate the request
	    ○ Borrower must meet the "good payment history requirement.
	        ➢ No 60-day late payments within the past 24 months
	        ➢ No 30-day late payments within the past 12 months
	        ➢ Must be current at the time of termination.

Rental Income	Rental income, less rental and property related expenses, are defined as "net rental income" calculated based on two scenarios: ▪ Borrower has included the rental income and associated expenses on the tax return (actual net rental income on the return is used) ▪ Borrower is allowed to use a verified and documented lease agreement to verify rental income. The borrower will be allowed to use 75% of the rental revenue. There is a 25% deduction for customary vacancy and maintenance factors. ▪ Positive net rental income adds to the borrower's income and negative net rental income reduces the borrower's income for mortgage loan qualifying purposes.
Popular tax forms used in mortgage financing	▪ **Form 1040** – individual tax return form ▪ **Schedule C** – sole proprietor (single owner business) ▪ **Schedule E** – rent revenues and expenses ▪ **Form 2106** – unreimbursed employee expenses ▪ **Form 4506T** – allows access to filed taxes transcript

	▪ **W2** – Shows borrower's annual gross income
Occupancy	Property must be occupied by the borrower within 60 days of loan closing
Seller Concessions	A seller is an "interested party contributor" (IPC) and is not allowed to provide gifts toward the borrower's down payment or participate in any (IPCs) not disclosed during the settlement process. However, the seller is allowed to contribute to the borrower's closing costs and any pre-paid items associated with the loan transaction. Any IPCs are deducted from the sales price when determining LTV and CLTV ratios. The following are the guidelines for conventional mortgages: ▪ Seller and or IPCs are based on the LTV which is the lower of the sales price or the appraised value. Ex. Appraised value $220,000 Sales Price $200,000 the value to be used is the sales price because it is lower. ▪ Less than 10% down or LTV greater than 90% (100-10), maximum seller contribution 3% ▪ Less than 25% down and up to 10% or LTV 75.01%-90%, maximum seller contribution 6% ▪ More than 25% down or LTV less than 75%, maximum seller contribution 9% ▪ Investment/non-owner occupied, the maximum seller contributions of all LTVs is 2% Seller contributions may never exceed the actual closing costs and prepaid items associated with the loan.
Non-conforming loans	▪ Loans that exceed the conventional conforming guidelines for maximum loan amount over $510,400 for a single unit property in standard areas are non-conforming loans and are not deliverable to Fannie Mae and Freddie Mac. They are purchased by other investors on the secondary market. ▪ Exception – high cost areas are allowed to have loan limits that exceed the conforming loan limits by up to 50 percent of the conforming limit of $510,400 which is $765,600 and in some areas like Alaska and Hawaii the limit can exceed $765,600. Under this scenario these loans would still be considered conforming loans.
Borrower categories	▪ **Prime** – borrowers or "A" borrowers with the lowest risk generally have high credit scores, good assets and income and employment history. These borrowers get the best loan terms. ▪ **Alt/A** – borrowers that have credit attributes that are slightly more risky than prime but more sound than subprime. ▪ **Subprime** – borrowers that are substantially more risky than prime and are often referred to as B/C borrowers. Because these borrowers have limited loan options they are often victims of predatory lending practices.