Smartfi Home Loans

HECM Lending Guidelines

CONTENTS

INTRODUCTION

This lending guide is designed to assist the Smartfi team and our business partners with the origination, processing, and closing of reverse mortgage transactions. This manual is a live document and if printed may not reference the most up to date information, additions, and/or corrections. Smartfi reserves the right to interpret guidelines and to make any exceptions to the outlined policies and procedures as deemed necessary. While the highest precautions have been taken in order to assure the accuracy of this manual, Smartfi assumes no responsibility for errors and omissions.

HECM PRODUCT

Home Equity Conversion Mortgage (HECM)

Smartfi adheres to the federal guidelines as set out in the HUD handbook and all the mortgagee letters as they update or revise the HECM program. Smartfi operations processes both HECM refinance transactions and HECM for Purchase loans.

There are three (3) transaction types available under the HECM program.

They are as follows:

- **HECM Traditional**: A refinance in which the equity in the borrower's current property secures the mortgage.
- **HECM Refinance**: Also known as a HECM-to-HECM Refinance is a refinance of an existing HECM with a new HECM for the same borrower and property.
- **HECM Purchase**: A borrower purchases a new primary residence.

KEY COMPONENTS OF THE HECM STRUCTURE:

The following are key components that apply to all HECM transactions:

MAXIMUM CLAIM AMOUNT (MCA)

The MCA determines the principal limit, which represents the maximum amount that FHA will pay on a Claim for HECM insurance benefits.

- For refinance transaction, the MCA amount is equal to the lesser of the appraised value of the home or the applicable FHA lending limit for a given location at the time of loan originated.
    - For Purchase transactions, MCA amount is equal to the lesser of the appraised value, applicable FHA lending limit or contract sales prices.

FHA publishes updated limits effective for each calendar year. For the period January 1, 2025, through December 31, 2025 the maximum claim amount for FHA-insured HECMs will be $1,209,750.00.

PRINCIPAL LIMIT

The Principal limit is set at origination and is determined by multiplying the maximum claim amount by a factor defined by HUD. The factor is based upon the expected average mortgage interest rate and the age of the borrowers and/or Eligible Non-Borrowing Spouse (NBS), whichever is youngest.

The Principal Limit is calculated at closing and increases each month by 1/12th of the sum of the note rate and the annual mortgage insurance premium rate defined by HUD.

Note: Loan amount for HECMs is the Principal Limit amount.

MORTGAGE INSURANCE PREMIUM

The borrower is charged a MIP to offset the risk that the outstanding loan balance may exceed the subject property value when the loan becomes due and payable.

The borrower is charged an upfront initial MIP as defined by HUD, which is a percentage of the MCA, and an annual MIP as defined by HUD, which is a percentage of the outstanding mortgage balance.

- Initial MIP- Two (2) % of the MCA
- Annual MIP- For all HECM transactions is .50% of the outstanding principal balance.

EXPECTED AVERAGE MORTGAGE INTEREST RATE

The expected average mortgage interest rate is the rate used in the calculation of the principal limit and is based on either a fixed or an adjustable rate, as follows:

- Fixed rate loan: The expected rate is the fixed rate interest rate.
- Adjustable-rate loan: Expected rate is the sum of the margin and an index value. The expected rate and mortgage interest rate are set on the date of loan closing.

MANDATORY OBLIGATIONS

The Mandatory obligations (MO) are fees and charges incurred in connection with the origination of the HECM that are paid at loan closing. Mandatory obligations are defined as the following:

- Initial MIP
- Loan Origination Fee- The origination fee may be used to pay for services period by a sponsored third-party originator. The OF limit shall be the greater of $2,500 or two percent of the maximum claim amount of $200,000, plus one percent of any portion of the MCA that is greater than $200,000. The total amount of the OF may not exceed $6,000.
- HECM Counseling Fee
- Recording fees and recording taxes, or other charges incident to the recordation of the insured mortgage
- Credit report, credit report supplements
- Survey, if required by the lender or the borrower
- Title examination
- Tax Service Fee
- Lenders title insurance
- Fees paid to an Appraiser for the 1st and 2nd appraisals, as applicable,
- Flood Certification
- Repair Set-Asides
- Repair administration fee
- Delinquent Federal Debt
- Amounts required to discharge any existing liens on the property in accordance with the 12-month seasoning requirement,
- PACE/HERO liens,
- Judgment liens,
- Customary fees and charges for warranties, inspections, surveys, and engineer certification,
- Funds to pay contractors who performed repairs as a condition of closing, in accordance with standard FHA.
- Requirements for repairs required by the appraiser and/or underwriter.
- Property tax, flood, and hazard insurance payments scheduled for payment from the Property Charge Life Expectancy Set-Aside (LESA) or from HECM proceeds within the first 12 months disbursement period. Lenders must use the actual insurance premium and actual tax amount, if a new tax bill has not been issued, the lender must use the prior year's amount multiplied by 1.04, and
- Other charges as authorized by FHA.

For HECM Purchase transactions, MO also include the following:

- The amount of the principal that is advanced towards the purchase price of the subject property.
- Fees and charges for real estate purchase contracts

Note: Buy out of a spouse that also has a vested ownership interest in the subject property at the time of application as evidence by the title report will be permitted if there is a fully executed divorce decree, i.e., court order, that awards the property to our borrower and the buyout of the spouse. The buyout terms are required and if not included in the fully executed divorce decree, then a letter from the attorney representing the spouse stating the buyout terms is required. A property settlement agreement or separation agreement will not be considered a court order as it's an agreement between the parties only.

Note: Payoff of a Chapter 13 Bankruptcy is not included in the FHA's definition of MO therefore HECM proceeds may not be used to pay off any debts outside of delinquent federal debts or existing liens on the subject property. To satisfy an existing lien the seasoning requirements as defined in this guide must be met.

REFINANCE TRANSACTIONS

A refinance transaction is when a reverse mortgage is used to refinance a property when existing liens (if any) are paid off, typically using funds available at closing.

Below are the two (2) types of refinance transactions:

- HECM Traditional – is a HECM refinance used to pay off a non-HECM mortgage lien.
- HECM Refinance (HECM to HECM) is a HECM refinance used to pay off a HECM mortgage lien.

LIEN SEASONING

Smartfi will permit the payoff of existing non-HECM liens using HECM proceeds if the liens have been in place for longer than 12 months prior to the HECM closing, OR

If the lien resulted in cash to the borrower in an amount of $500 or less, whether at closing or through cumulative draws, prior to the date of the HECM closing.

In order to determine if the borrowers received $500 or less in cash Smartfi must review the HUD-1/Closing Disclosure from the transaction that resulted in a lien and the payoff statement. If the non-HECM lien is a HELOC Smartfi must review the HUD-1/Closing Disclosure and subsequent monthly mortgage statements in order to document that cumulative draws do not exceed the $500 or less limitation.

FHA's existing policy as indicated in the 2017 Final Rule does not consider funds paid to 3rd parties for construction and rehab to be "cash to borrower" as long as documentation is provided to show that loan proceeds in excess of $500 were paid to a Contractor, the seasoning requirements is considered satisfied.

UNSEASONED HOME EQUITY LINES OF CREDIT

The borrower may pay off, at closing, a Home Equity Line of Credit (HELOC) that **does not** meet seasoning requirements noted above from borrower funds, the HECM funds, or a combination of HECM and borrower funds as long as the HECM funds advanced at closing do not exceed 60 percent of the Principal Limit.

Seasoned HELOCs are included in and considered an MO.

BORROWER ELIGIBILITY

This section describes the following minimum eligibility requirements for the HECM loan:

- All borrowers must be 62 years of age or older on the day they sign the closing documents.
    - At the time of initial application, the youngest borrower must be within 60 days of his/her 62nd birthday.
- Borrower(s) must be residing in the subject property as their primary residence and must occupy the subject at both the time of application and closing.
    - A primary residence is defined as the dwelling where the borrower maintains their permanent residency a minimum of 183 days per calendar year.
    - The subject property is considered to be the primary residence of any borrower who is temporarily or permanently in a healthcare institution as long as the subject property is the primary residence of at least one (1) other borrower who is not in a healthcare institution.
- Borrower(s) must be a U.S. Citizen or a lawful resident alien.
    - Permanent Resident Alien
        - A copy of the front and back of an unexpired resident alien card is required, and
        - The application to indicate that the borrower is a lawful permanent resident alien.
        - Valid Social security number
    - Non-Permanent Resident Alien
        - The borrower has a valid social security number, and
        - The borrower is eligible to work in the U.S. and can provide an Employment Authorization Document (EAD) issued by the U.S. Citizenship and Immigration Services (USCIS).

OCCUPANCY

Occupancy must be documented in the loan file. At the discretion of Underwriting, additional documentation may be required to evidence primary residency of the subject property. This can include but is not limited to:

- Most recent bank statements reflecting the borrower's name, subject property address.
- Voter registration card
- Most recent credit card statement
- Most recent utility bills, including phone, cable.

MULTIPLE FHA INSURED LOANS

Both occupying and non-occupying borrowers and co-borrowers taking title to the property at settlement, are obligated on the mortgage note, and must sign all Security Instruments. FHA will generally not insure more than one (1) primary residence mortgage for any borrower.

When a borrower or co-borrower has cosigned for another FHA loan, **all** of the following documents on the existing FHA loan are required for eligibility:

- Note
- Copy of the executed deed
- Letter of explanation
- Proof that the other party has been making timely loan payments in full directly to the servicer for at least the most recent 12 months.
- A copy of the original 1003 from the closed FHA loan showing the borrower signed as a non-occupant co-signer.

The documentation will be reviewed to confirm if the borrower indicated they would be residing in the FHA-insured property. If the borrower indicated they intended to reside in the property, the borrower is ineligible for another FHA-insured loan until the following criteria is met:

- Paid off the FHA-insured mortgage on the previous residence with a re-conveyance, or
- Terminated ownership of that residence

FHA will generally not insure more than one (1) primary residence mortgage for any borrower. The following are exception situations in which the borrower may maintain multiple FHA-Insured mortgages:

- **Relocation**- If the borrower is relocating and re-establishing residency in another area within 100 miles from the current primary residence or is relocating for employment purposes, the borrower may obtain another mortgage using FHA-insured financing and is not required to sell the existing property covered by an FHA-Insured mortgage.

- **Increase in Family Size**-The borrower may be permitted to obtain another home with an FHA-insured mortgage if the number of legal dependents increases to the point that the present house no longer meets the family's needs.
    - The borrower must provide satisfactory evidence of the increase in dependents and property's failure to meet the family's needs.
    - The loan to value ratio must equal 75% or less or be paid down prior to closing. A current residential appraisal must be used to determine LTV compliance.
- **Vacating a Jointly Owned Property (Divorce)-** A borrower may be eligible for another FHA-insured mortgage if she/he is vacating a residence that will remain occupied by a co-borrower.
- **Non-Occupying Co-Borrower-** A non-occupying Co-Borrower on an existing FHA-insured mortgage may qualify for another FHA-insured mortgage on a new property to be their own principal residence. A borrower with an existing FHA-insured mortgage on their own principal residence may qualify as a non-occupying co-borrower on other FHA-insured mortgages.

Note: Reverse Mortgages- A legally married couple may not have more than one (1) primary residence at any given time and therefore may not qualify for more than one (1) HECM. There are no exceptions to this guideline.

FEDERAL EXCLUSION LISTS LIMITED DENIAL PARTICIPATION (LDP) AND SYSTEM FOR AWARD MANAGEMENT (SAM).

The System for Award Management (SAM) and Limited Denial of Participation (LDP) are web-based systems that identify parties excluded from receiving federal contracts and certain types of federal financial and non-financial assistance and benefits. These systems help to determine if a potential borrower is eligible for a reverse mortgage. An Applicant who is suspended, debarred, or otherwise excluded from participation in HUD's programs is not eligible for a HECM.

The LDP and SAM list is checked for the borrowers and any other party to the transaction, as follows:

- Borrowers
- Non-Borrowing Spouse
- Loan Officer
- Senior Processor
- Underwriter
- Appraiser

- Closing/Settlement Agent from escrow or title including, but not limited to the Closing/Settlement Agent identified in the Closing Protection Letter (CPL)
- Title Insurance Company
- Power of Attorney, Guardian, or Conservator
- Funder
- Wholesale Partner, if applicable
- Selling and Listing Real Estate Agents, if applicable
- Builder, if applicable
- Sellers

OFFICE OF FOREIGN ASSETS CONTROL (OFAC)

If a borrower or Non-Borrowing Spouse appears on the OFAC list, the file must contain documentation verifying it is not our borrower. If a clear OFAC printout is not documented in the file, the borrower is ineligible.

Note: OFAC is usually found on the credit report.

CAIVRS (CREDIT ALERT VERIFICATION REPORTING SYSTEM)

CAIVRS is a federal government database of delinquent federal debtors. The database also reports if the individual has had a claim paid by a reporting agency.

- A CAIVRS report must be pulled on every borrower, the CAIVRS report may not be older than 90 days at the time of underwriting and 120 days at closing.
- If CAIVRS screening indicates that the borrower is presently delinquent or has had a claim paid within the previous 3 years on a loan made or insured by FHA on his or her behalf, the borrower is not eligible unless FHA suspends the CAIVRS listing.

If a delinquent Federal Debt is reflected in CAIVRS, Smartfi must verify the validity and delinquency status of the debt by contacting the creditor agency using the contact phone number and debt reference number reflected in the Borrower’s CAIVRS report.

If the creditor agency confirms that the debt is valid and in delinquent status, then the Borrower is ineligible for an FHA-insured mortgage until the Borrower resolves the debt with the creditor agency in accordance with the Debt Collection Improvement Act.

The creditor agency that is owed the debt can verify that the debt has been resolved in accordance with the Debt Collection Improvement Act. The Mortgagee must include documentation from the creditor agency to support the verification and resolution of the debt. For debt reported through CAIVRS, the Mortgagee may obtain evidence of resolution by obtaining a clear CAIVRS report.

COUNSELING POLICY

HECM counseling is required for any borrower(s) who wants an FHA-insured HECM and it must occur before the borrower(s) incurs any costs for the loan. The counseling may be face to face or by telephone based on State specific requirements. FHA prefers face to face counseling, however they recognize many seniors prefer telephone counseling for a variety of reasons.

Parties Required to Attend HECM Counseling:

- Borrower(s): Individuals or current trust beneficiaries who are eligible and seeking a HECM for Purchase, Traditional Refinance or HECM Refinance loan must receive HECM counseling. If a borrower lacks competency, individuals with Durable Power of Attorney, or court appointed conservators or guardians receive the counseling, and then execute the counseling certificate on the borrower's behalf.
- Non-Borrowing Spouse (Eligible and Ineligible): Counseling is required to ensure that the borrower and Non-Borrowing Spouse both understand the implications of a HECM.
- Any Non-Borrowing Owner on title, even if they are deeding off.
- Life Estate: Person(s) holding a life estate interest must receive HECM counseling. Only a HECM borrower may hold a life estate interest in the subject property.
- Remainder man(s) must receive HECM Counseling even if they are deeding out of the life estate at closing.
- Trustee(s): It is strongly recommended, but not required for Trustee(s) to be counseled.

Note: If Non-Borrower Owners and or Remainer mans are found out during process, letter of explanation will be required stating why they did not receive counseling prior to application.

Note: For HECM to HECM (H2H) Counseling Waiver, see HECM to HECM section of this guide.

The Certificate must contain each of the following:

- All the names of the parties required to be counseled (borrower, co-borrower, NBS, AIF, etc.)
- Subject property address
- Name of the counselor
- Name of the counseling agency
- Employer Identification Number (EIN) of the agency

- Certificate number
- Date counseling completed.
- Certificate expiration date
- The certificate must be signed and dated by all required parties.

Expired Certificates- A counseling certificate is good for 180 days from the date HECM counseling was completed.

Note: See State Specific Requirements for additional requirements and limitations.

List of HUD Approved Counseling Agencies

The Loan Officer is required to provide the prospective borrower(s) with a list of HUD Approved Counseling Agencies. The list must include five (5) agencies in the local area or state, AND the National and Regional Intermediaries that receive supplemental HECM funding. At least one of the local agencies must be located within a reasonable driving distance with the intention of providing a face-to-face counseling option.

Ordering of Services

Services (appraisal and flood certificate) may not be ordered prior to a lender receiving the HECM Counseling Certificate evidencing all borrower(s), NBS or Non-Borrowing Property Owner(s) were counseled and have signed and dated the counseling certificate.

Note: If it is determined that services were ordered prior to the required criteria being met, the borrower(s) may not be charged for services.

LOAN APPLICATION

This section describes the loan application, borrower and lender requirements, and identification requirements.

An initial application may only be taken by a licensed Mortgage loan Originator (MLO) who holds an active license in NMLS for the state where the property is located or are sponsored by a federally chartered institution in the subject property state. The MLO consults with the borrower to explain program options, discuss eligibility, provide a Counseling Referral List, and collect the necessary information to produce the initial application package to submit to the borrower.

Note: A credit report can be ordered prior to application date.

DEFINITION OF APPLICATION

For purposes of initial disclosure requirements, the file is considered an application when the following data is obtained and an intent to proceed is given:

- Borrower and Co-Borrower's Name, as applicable
- Borrower's monthly income (all borrowers)
- Borrower's Social Security Number (all borrowers)
- Borrower's Date of Birth (all borrowers)
- Property address
- Estimate of the value of the property
- Interest Rate
- Product Type/Margin
- Principal Limit

The application may be in writing or electronically submitted, including a written record of an oral application (e.g., via telephone).

DEFINITION OF COMPLETED APPLICATION

For Reg B purposes, the application is considered a "completed application" upon receipt of all information needed to provide a decision on the loan. Smartfi defines this date when the following items have been received:

- Fully executed and completed written application package.
- Fully executed counseling certificate
- Identification documents including verification of DOB, SSN
- Credit Report
- Income/expense documentation
- Asset documentation
- Power of Attorney/Guardianship paperwork (if applicable)

RE-APPLICATION REQUIREMENTS

The following guidelines apply to situations when a new loan application is required, and when the original application can continue.

A new application (re-application) is required when:

- Borrower changes product:
    - When a borrower makes a decision to change programs, either from an FHA-insured HECM to the CHOICE program (or vice-versa), the existing loan must be adversed and a new application is required.
- Borrower removes him/herself from loan:

  - When a borrower chooses to remove him/herself from the loan after the initial application, a new application and loan number is required, and a new credit report must be obtained referencing only the remaining borrower.
  - Any existing services that have not expired may be used for the new loan including the appraisal and reverse mortgage counseling certificate.

The initial application can continue as follows:

- Death of a borrower: A borrower or co-borrower dies during the processing of the loan prior to closing.
- A death certificate must be provided and added to the file.
- Co-Borrower added after Initial Application: A co-borrower is being added to the loan after initial application.
  - The new co-borrower must sign all existing application documents and disclosures required for initial application. The application must be dated with the date that the co- borrower signs the application, not the date the original borrower executed their application.
- A letter of explanation (LOX) from the borrower must be added to the file explaining why there is an addition of the co-borrower.
- Co-borrower must receive counseling and provide a fully executed certificate.

GOOD FAITH ESTIMATE (GFE)

The timing of when a GFE can be generated is based upon how the application is taken. Applications may be taken telephone, face to face, mail, fax, e-mail, or Internet.

Application taken by Telephone, Face-to-Face, Mail, Fax, or E-mail

- When all data elements and the intent to proceed are received over the telephone or internet, the application date for initial disclosure timing is that day, application disclosures including a GFE can then be sent to the borrower(s).
- When an application is taken face-to-face (data elements and intent not received over the phone) then the GFE should not be included with the application docs. After the data is received, the GFE should then be printed and sent to the borrower(s). The application date for RESPA purposes is the date of the face-to-face interview. If the MLO has the ability to print documents during the face-to-face interview, then a GFE can be issued the same day.

If the MLO does not have the ability to print documents during the face-to-face interview, then the GFE must be printed and mailed within 3 business days.

- A GFE cannot be sent with a Mail, Fax, or E-mail application (sent blank), since data elements have not been obtained. Upon receiving a completed and signed application package, the GFE should then be printed and sent to the borrower(s). This must occur within 3 business days of receipt of the signed application package.
- Print dates will be verified to ensure compliance.
- For RESPA purposes GFE's printed prior to the initial application date (may be different than date on loan application) or outside of the three-day window are considered an incurable error and the file cannot proceed.

VALID CHANGE OF CIRCUMSTANCES (VCC)

When a Good Faith Estimate or other loan terms change then Smartfi will re-disclose the terms based on the valid change of circumstance fee sheet provided to us from the Partner.

The Broker partner must provide Smartfi with a complete VCC sheet within 3 days of being notified of the change. The form must be completed in its entirety. Any fees that need to be adjusted need to be included.

Smartfi will update the fee screen, generate the re-disclosure package, complete the Valid Change of Circumstance, and email the re-disclosure package to the partner for distribution to the borrowers.

ORIGINATION FEE

The loan origination fee limit shall be the greater of $2,500 or 2% of the maximum claim amount of $200,000, plus 1% of any portion of the maximum claim amount that is greater than $200,000. Fees for services performed by a sponsored third-party originator may be included as part of the loan origination fee. The total amount of the loan origination fee may not exceed $6,000.00.

IDENTIFICATION DOCUMENTATION REQUIREMENTS

In compliance with Section 326 of the USA PATRIOT Act which requires U.S. financial institutions to verify the identity of a customer when opening an account, lender/originator must obtain identifying documentation from each borrower/NBS/AIF/. Lender/originator must also verify the borrower(s) date of birth and Social Security Number.

Acceptable identification (ID), as follows:

- State issued driver's license (must not be expired)
- State issued ID card (must not be expired)
- Military ID card
- Passport (must not be expired)
- U.S. Alien Registration Card

- Birth Certificate (marriage license maybe required when linking names)
- Written verification from the Social Security Administration Evidence of Social Security Number
- Written verification from the Social Security Administration

Note: Personal Federal Tax Returns are not acceptable SS Verification.

SOCIAL SECURITY NUMBER (SSN) REQUIREMENTS

All HECM borrowers and any applicable Non-Borrowing Spouse must have a valid Social Security Number and provide evidence of his/her Social Security Number.

Evidence of Social Security Number includes:

- Social Security Card,
- Medicare Card – as of 2019 the SSN is no longer on Medicare cards. Cards issued prior to 2019 with the SSN are acceptable.,
- Social Security 1099 (SSA-1099),
- Non-SSA 1099,
- W2, or
- Successful processing of SSA-89 Authorization for the Social Security Administration (SSA) to release Social Security Number (SSN) Verification.

ALTERNATE CONTACT

Contact information for the borrower's alternate contact/nearest living relative must be obtained, as follows:

- First name and last name
- Address
- Phone number (cannot be the same as the borrower's phone number)
- Relationship to Borrower(s)

Note: The alternate contact may reside with the borrower at the subject property address; however, the alternate contact's phone number must be different than the borrower's phone number.

POWER OF ATTORNEY (POA)

If a borrower(s) is deemed incompetent a POA, Conservator or Guardian may be used. If using a POA it must clearly be established that the borrower was of sound mind at the time of executing the POA document(s) but is no longer of sound mind to handle his or her own financial affairs.

Power of Attorney Requirements

General Power of Attorney (POA) guidelines:

- The POA must be Durable (continues to be in effect if the borrower becomes incompetent after execution of the POA),
- The POA grants the power to execute a mortgage real estate transaction, complies with state law, and allows for the Note to be enforced in the jurisdiction. Preferably, the POA should specifically give the POA the right to mortgage, sell, or transfer property rights in the subject property,
- The POA must be acknowledged by a notary public authorized under applicable law,
- The POA must be reviewed and approved by the DE Underwriter,
- A written acknowledgment from the title company indicating the POA is acceptable to insure,
- The Attorney-In-Fact must be directed to sign the loan documents as indicated in the following example: "John Doe by Jane Doe as attorney-in-fact/AIF", and
- The POA must provide a valid (not expired) photo identification.
- Original POA (not a copy) must be provided for recording unless already recorded.
- When a POA is being used and the property is vested in a Trust, both the trust and the POA must be reviewed at the same time by an Attorney for Compliance with HECM/HUD guidelines.

POA for Legally competent Borrowers

A legally competent borrower must:

- Receive HECM counseling and fully execute the HECM counseling certificate.
- Execute the initial 1009.
- Execute the initial 92900A.
- Once completed, the AIF may execute the remainder of the initial application disclosures and/or closing documents.

For all legally competent applicants, the POA must not execute the HECM counseling certificate, initial 1009 and initial 92900A on behalf of the borrower.

A handwritten letter from the borrower indicating the reason why a POA is being used must be completed and provided prior to closing.

When POA is used to sign **only closing documents** then POA HECM counseling **is not** required. When a POA must receive HECM counseling he/she must execute the Counseling Certificate.

POA for Legally Incompetent Borrowers

A legally incompetent borrower may not sign the loan application or closing documents. Documents must be signed by the POA or a court-appointed conservator or guardian.

A legally incompetent borrower does not:

- Receive HECM counseling and fully execute the HECM counseling certificate.
- Execute any loan documents.

For all legally incompetent applicants, the POA must receive and execute the HECM counseling certificate and all other documents for the borrower.

The POA must receive HECM counseling.

For a POA to be valid, the individual must have been mentally competent at the time the POA document was signed. When the borrower is currently incompetent, a physician's letter is required.

Smartfi must be able to clearly determine all of the following:

- The POA was executed when the borrower was competent.
- Date the capacity issues was diagnosed.
- The borrower is no longer competent and able to manage their personal affairs.

Note: When the POA document requires two (2) physician's letters to establish mental competency then Smartfi must be provided with both physician's letters.

SIGNING WITH A MARK

If the borrower is mentally competent, but can only make a mark, we will accept the mark on the 1009, HUD-92900A, and counseling certificate and all other application and closing documents if the Signing with a Mark Affidavit is executed which indicates two (2) disinterested parties, one of which may be the Notary, witnessed the mark and attest this is the mark of the borrower.

For execution with a mark on the first Note, second Note, first Mortgage and second Mortgage, as applicable, a Signing with a Mark Affidavit is required for each document.

BLIND BORROWER SIGNING

Follow these requirements only for fully competent borrowers who are physically capable of signing documents and wish to sign themselves, but who cannot read the documents due to sight impairment.

Blind borrowers must:

Sign and date the application in the presence of two disinterested witnesses. The witnesses can be neighbors, or friends of the borrower. The witnesses should sign an acknowledgement letter confirming they witnessed the signing of the application package.

Sign and date an affidavit, with the witnesses in the presence of the notary, acknowledging that he or she understands the terms of the loan.

Approval of the title company verifying acceptable for closing.

Both borrower and disinterested witness will be required at closing.

CONSERVATORSHIP/GUARDIANSHIP

In the case of an incompetent borrower where a POA is insufficient or was never executed, a court appointed Conservator or Guardian can act on behalf of the incompetent borrower(s) to obtain a reverse mortgage.

A Conservatorship or Guardianship must be valid, and in force with no expiration date so the borrower has legal representation for the life of the loan. Temporary conservatorships or guardianships are not permitted since the borrower must have representation for the life of the loan.

Required Documentation

When a borrower has a Conservator or Guardian the file must contain the following documents:

- A copy of the executed court order/approval of the conservator/guardian to encumber the borrower with a reverse mortgage. If the executed court order identifies specific HECM Loan terms, i.e., interest rate, loan amount, etc. those terms MUST be met, or an updated executed court order is required.,
- A copy of the letter of Conservatorship or Guardianship,
- Title insurer must review and provide written approval for the use of the Conservator or Guardian,
- Conservator/Guardian must attend counseling to be counseled on the borrower’s behalf, the borrower and Conservator/Guardian must be identified at the top of the counseling certificate, and the Conservator/Guardian must sign and date the counseling certificate on the borrower’s behalf, and as the Conservator/Guardian, and
- Provide a copy of his/her valid (unexpired) photo identification.

ACCEPTABLE ACTIVITIES PRIOR TO RECEIVING COUNSELING:

Loan Officers may undertake only the following permissible activities prior to the applicant receiving counseling:

- Explain the program to the applicant.
- Discuss eligibility requirements.
- Provide information regarding the fees and charges associated with the product.
- Describe the potential financial implication of the program and product for the applicant.
- Provide the applicant with copies of the Security Instrument, mortgage Note and loan agreement.
- Complete the initial loan application package.
- Order the credit report.

FHA CASE NUMBER

An FHA Case Number is required for all HECM loans. The Case number may not be ordered until we have a fully executed application for borrower and property and a fully executed HECM Counseling Certification.

Ordering Services

The borrower must be counseled and sign and date the certification prior to ordering any services and incurring any fees. This includes but is not limited to the following:

- Appraisal (After FHA Case number has been assigned)
- Title
- Flood Certification
- FHA Case Number
- Inspections required to process the HECM loan.

CREDIT REPORTS

A three (3) repository merged credit report, a.k.a. a tri-merge credit report, is required for all HECM borrower(s). When income from an Eligible Non-Borrowing Spouse (ENBS) or Other Household Member (OHM) is being used to qualify then a tri-merge credit report is required for the ENBS or OHM.

Credit Reports Requirements

- The name of the lender ordering the report
- Cannot be older than 120 days at the time of loan funding.
- Contain all information from at least two credit repositories pertaining to credit, residence history, and public records information, be in an easy to read and understandable format, and not require code translations. The credit report may not contain whiteouts, erasures, or alterations.
- Correct borrower name, current street address, date of birth and social security number

    - A new credit report is required to be repulled when the borrower’s last name and or social security number is incorrect.
    - A new credit report does NOT need to be repulled for minor variations such as street and or directional; address variation is acceptable as long as there are no credit alerts; date of birth as long as documentation validating accurate date of birth is in the file.
- Any additional social Security Numbers linked to our borrowers must be researched and cleared.
- Any HAWK alerts must be researched and cleared.
- Any OFAC hits must be researched and cleared.
- All inquiries made within the last 90 days.
- Obtain a joint report for individuals with joint accounts; non-married multiple borrowers without joint accounts will require a separate credit report for each.
- Address discrepancies on the credit report must be researched and cleared. The borrowers may be required to provide a detailed letter of explanation for any additional address that have been reported in the prior 12 months.
- All credit and legal information not considered obsolete under the Fair Credit Report Act (FCRA), including information for the last seven years regarding:
    - Bankruptcies
    - Judgments
    - Lawsuits
    - Foreclosures
    - Tax liens; and
- For each borrower debt listed, the:
    - Date the account was opened.
    - High credit amount
    - Required monthly payment amount.
    - Unpaid balance and
    - Payment history

Note: FHA will permit lenders to order a credit report prior to completion of HECM counseling if the borrower wishes to perform a preliminary credit review of the borrowers’ financial obligations. Lenders may only collect the cost of the credit report at loan closing. If the HECM does not close, the borrower may not be charged.

TYPES OF CREDIT HISTORY / NON-TRADITIONAL CREDIT (HECM PURCHASE ONLY)

If a traditional credit report is available, Smartfi must use a traditional credit report. However, if a traditional credit report is not available, and the borrower is applying for a HECM for purchase, Smartfi must develop the borrower’s credit history using the requirements for nontraditional credit.

Smartfi is not required to develop non-traditional credit for borrowers seeking a traditional or refinance HECM. The borrower may be deemed to have an acceptable credit history.

Borrowers with no Credit History

For borrowers without a credit score, Smartfi must either obtain a Non-Traditional Mortgage Credit Report (NTMCR) from a credit reporting company or independently develop the borrower's credit history. Smartfi may independently verify the borrower's credit references by documenting the existence of the credit provider and that the provider extended credit to the borrower.

NTMCR completed by a credit agency; must verify:

- The existence of the credit providers
- The credit was extended to the borrower
- The creditor has published address or telephone number

Non-traditional credit verified by Smartfi, lender must:

- Use a published address or telephone number for the credit provider, and not rely solely on information provided by the borrower, and
- Obtain the most recent 12 months of cancelled checks, or equivalent proof of payment, demonstrating the timing of payment to the credit provider.

To verify the borrower's rental payment history, the lender must obtain a rental reference from the appropriate rental management company, provided the borrower is not renting from a family member, demonstrating the timing of payment of the most recent 12 months in lieu of 12 months of cancelled checks or equivalent proof of payment.

To be sufficient to establish the borrower's credit, the credit history must include three credit references, including at least one of the following:

- Rental housing payments (subject to independent verification if the borrower is a renter
- Telephone service
- Utility company payment history (if not included in the rental housing payment) including:
    - Gas;
    - Electricity;
    - Water;
    - Television service;
    - Internet service.

If Smartfi cannot obtain all three credit references from the list above, the lender may use the following sources of unreported recurring debt:

- Insurance premiums not payroll deducted (for example, medical, auto, life, renter's insurance)

- Payment to childcare providers is made to businesses that provide such services.
- School tuition
- Retail store credit cards (for example, from department, furniture, appliance stores, or specialty stores)
- Rent-to-own (for example, furniture, appliances).
- Payment of that part of medical bills not covered by insurance.
- A documented 12-month history of savings, evidenced by regular deposits, resulting in an increased balance to the account that:
- Were made at least quarterly, were not payroll deducted, and caused no insufficient funds (NSF) checks,
- Automobile lease, or
- A personal loan from an individual with repayment terms in writing and supported by cancelled checks to document the payments.

A minimum of 3 sources are required and each must have a 12-month history with no history of delinquent housing payments.

Borrowers who do not have traditional credit and cannot meet the above requirements for non-traditional credit are <u>ineligible</u> for a HECM purchase transaction.

NON-BORROWING SPOUSE (ELIGIBLE AND INELIGIBLE)

This section describes the eligibility and Ineligibility of Non-Borrowing Spouse (NBS).

An NBS is defined as the spouse of the HECM borrower determined by the law of the state in which the spouse and borrower reside or the state of which they were married. A NBS includes common law spouses.

The NBS will be classified as either an Eligible NBS or an Ineligible NBS which determines whether the borrower qualifies for the Deferral Period once the HECM loan has met a maturity event. The following applies to all NBS:

- All NBS must be named as a NBS in the HECM documents.
- All NBS must attend HECM counseling.
- All NBS must comply with FHA's requirements for disclosure and verification of SSN.
- The name and age must be verified.
- All NBS must have a Social Security Number

Eligible NBS

An Eligible NBS is defined as a NBS who meets the Deferral Period Requirements. The eligible NBS's credit report must be ran only if the income will be used as a compensating factor or to reduce family size when calculating residual income. A Non-Borrowing Spouse that meets the Qualifying Attributes requirements at application for a Deferral Period is an Eligible Non-Borrowing Spouse and may not elect to be ineligible.

Similarly, a Non-Borrowing Spouse that is ineligible at application because he/she does not satisfy the Qualifying Attributes requirements for a Deferral Period may not elect to be eligible. An Eligible Non-Borrowing Spouse may become an Ineligible Non-Borrowing Spouse should any of the Qualifying Attributes cease to be met during the loan term.

Smartfi must show documentation that borrowers are married. A marriage license, previous recorded deeds showing husband and wife, joint filed tax returns, etc., may be used to document the validity of the marriage.

Note: An Eligible NBS is not permitted in the state of Texas.

Ineligible NBS

An Ineligible NBS is defined as a NBS who does not meet the Deferral Period Requirements. Ineligible NBS is:

- Not protected by the deferral period.
- SSN must be entered into FHAC in order to obtain a case number.
- Must be named in the HECM documents.
- The lender must disclose the amount of mortgage proceeds that would have been available under the HECM if he/she were an Eligible NBS.
- Ineligible NBS Compensating Factors may NOT be used to qualify the HECM borrower.

Deferral Period

The deferral period was implemented as a safeguard to prevent the need for the NBS to refinance the HECM in order to stay in the home upon the death of the borrower.

The deferral period is defined as the period of time following the death of the last surviving borrower during which the due and payable status of a HECM is deferred.

Note: Only an Eligible NBS qualifies for a deferral period.

Deferral Period Requirements

The following requirements apply for the NBS to qualify for the Deferral Period.

- Eligible NBS must have been the spouse of the borrower at the time of loan closing and have remained the spouse of such borrower for the duration of the borrower's lifetime.
- Eligible NBS must be properly disclosed to the lender at origination.
- Eligible NBS must be named as a NBS in the HECM documents.

- Eligible NBS must have occupied and continue to occupy the property.

If the Eligible NBS fails to meet any of the above requirements, the Deferral Period of the due and payable status shall cease and the HECM will become immediately due and payable as a result of the death of the last borrower.

Death of Borrower

In the event the last surviving borrower predeceases the Eligible NBS, the due and payable status will be deferred for as long as the Eligible NBS continues to meet the following qualifying requirements:

- Within 30 days from the death of the last surviving borrower, the Eligible NBS must provide the Eligible NBS Certification. This must be submitted annually thereafter for the duration of the Deferral Period.
- Within 90 days from the death of the last surviving borrower, the Eligible NBS must establish legal ownership or other ongoing legal rights such as probate to remain in the property.
- Eligible NBS must ensure all other obligations of the borrower contained in the loan documents continue to be satisfied (i.e. property taxes, hazard insurance, required repairs).
- Eligible NBS must ensure the loan does not become due and payable due to other maturity events.

NBS Signature Requirements

Initial Application:

- Non-Borrowing Spouse consent for Social Security Administration to Verify Social Security Number.
- Non-Borrowing Spouse General Authorization
- Authorization for the Social Security Administration to Release Social Security Number Verification
- Application Truth in Lending Disclosure Important Terms (ARM Loans only)
- Truth in Lending Disclosure (Fixed Loans only)
- Eligible NBS Disclosure and Certification (Eligible NBS only)
- Ineligible NBS Disclosure and Certification (Ineligible NBS only)

Closing Documents:

- Non-Borrowing Spouse consent for Social Security Administration to Verify Social Security Number
- First and Second Security Instruments and Riders
- Notice of Right to Cancel
- Application Truth in Lending Disclosure Important Terms (ARM Loans only)
- Truth in Lending Disclosure (Fixed Loans only)
- Eligible NBS Disclosure and Certification (Eligible NBS only)
- Ineligible NBS Disclosure and Certification (Ineligible NBS only)

HECM REFINANCE

A HECM refinance, also known as a HECM-to-HECM transaction, exists when an existing HECM loan is refinanced into a new HECM loan.

- The refinance should result in at least a 5 to 1 cost to benefit ratio, with the cost to benefit analysis defined as follows:
  - Cost-Sum of the loan origination fee, initial MIP, and all third-party fees
  - Benefit=Additional cash or in term/tenure payments.

The following requirements must be met or provided in a HECM refinance Transaction:

- HECM Refinance Worksheet- The most recent Refinance Worksheet is provided by the current servicer.
  - If the HECM Refinance Worksheet reflects any default a letter of explanation must be provided identifying the cause of default. Smartfi must review to determine if default is likely to reoccur.
  - If the existing servicer has repairs set aside not yet completed, this amount cannot be financed in the new loan. The repairs must be completed prior to closing and new worksheet received.

SEASONING REQUIREMENT

- The FHA case number for the HECM refinance may not be requested until 12 months after the date of the prior HECM closing.

BENEFITS TESTS

All HECM refinances must provide a bona fide benefit to the borrower meeting one of the three options below:

- Written letter adding a borrower to the loan, OR
- Pass the closing cost and loan proceeds test, OR
- Pass the rate reduction and recapture tests.

Additional information on each of the above Benefit to the borrower:

- **Adding a Borrower**: The HECM refinance must be originated at the written request of the current HECM loan borrower to add as a borrower an eligible NBS or other eligible family member who is currently residing in the subject property as their primary residence and is otherwise qualified to be a borrower.
- **Closing Cost Test**: The increase in the new principal limit must be equal to or exceed five (5) times the total closing cost amount.

    - The increase in the principal limit is determined by subtracting the new principal limit of the HECM refinance from the borrower's current principal limit.
    - The total closing cost amount is defined as the total amount of closing costs being charged to the borrower in connection with the HECM refinance. This includes all charges paid outside of closing as well as financed through the HECM loan.
- **Loan Proceeds Test:** The available benefit amount must be equal to or exceed five percent (5%) of the HECM refinance principal limit.
    - The available benefit amount is determined by subtracting the sum of the HECM payoff and total closing cost amount by the current principal limit amount.
    - The HECM refinance principal limit is the principal limit that will be available by the HECM refinance.
- **Rate Reduction Test:** The initial combined interest rate of the new HECM Refinance must be at least 1% lower than the current combined interest rate of the existing HECM.
    - The initial combined interest rate is determined by adding the initial interest rate plus annual MIP.
    - The current combined interest rate is determined by the current interest rate plus annual MIP.

Note: Where the above requirements are not satisfied, it appears that the HECM to HECM is nevertheless to the borrower a "bona fide advantage," exception requests may be Capital Markets.

HECM REFINANCE MIP

The cost of the initial mortgage insurance premium (MIP) for the existing loan is credited to the MIP for the new loan. If the result is positive, the amount must be remitted to HUD as the initial MIP on the Refinance.

Note: If the MIP is negative, this will result in zero MIP being collected. No portion of the initial MIP may be refunded.

Formula:

1. New MCA multiplied by new initial MIP (%) =Value 1
2. New MCA minus old MCA, multiplied by 3% minus previously paid MIP = Value 2

Results- The IMIP is the lesser of Value 1 and Value 2.

COUNSELING

HECM Counseling is required unless FHA's HECM to HECM counseling waiver requirements are met. In some states the borrower and any applicable Non-Borrower Spouse cannot Opt-Out of HECM counseling even if all FHA requirements to do so are met. All competent borrowers must be counseled even if using a Power of Attorney.

COUNSELING WAIVER

FHA will allow borrowers and any non-Borrowing souse to Opt-out of HECM Counseling requirements only when all the below requires are met.

- The time between the date of closing on the original HECM and the date of the application for refinancing does not exceed 5 years.
- The borrower received the Anti-Churning disclosure in conjunction with the Good Faith Estimate,
- The increase in the borrowers' principal limit (as provided in the anti-churning disclosure at application) exceeds the total cost of the refinancing by 5 times.

Counseling **cannot** be waived in the states of California, Connecticut, Delaware, Indiana, Massachusetts, Minnesota, New York, North Carolina, Pennsylvania, Rhode Island, Tennessee, Texas & Vermont. These states require the borrower(s) and Non-Borrowing Spouse to attend HECM counseling regardless of FHA requirements being met to Opt-out of counseling. FHA requires that we abide by all State requirements as well, so in all cases the borrower(s) or Non-Borrowing Spouse CANNOT waive/opt out of counseling on a HECM-to-HECM refinance.

CASH FLOW/RESIDUAL INCOME ANALYSIS

The purpose of the cash flow/residual income analysis is to determine the capacity of the borrower to meet his or her documented financial obligations with his or her documented income.

Borrower's Income from any, or all, of the sources identified within this guide must be calculated and documented for all borrowers to the extent necessary to determine that the borrower has residual income equal to, or exceeding, the required amount based on geographic region and family size.

If Smartfi can determine the borrower's residual income is sufficient based on documentation for one (1) **or** more specific sources, it need not pursue additional documentation for additional sources of income.

GENERAL INCOME REQUIREMENTS

Effective income refers to income that may be used in the calculation of residual income. Effective income must be reasonably likely to continue through at least the first three (3) years of the mortgage.

Smartfi must document the borrower's income and employment history, verify the accuracy of amounts of income being reported and determine if the income can be considered as effective income in accordance with the requirements listed below.

- Smartfi may only consider income if it is legally derived and, when required, properly reported as income on the borrower's tax returns.
- Negative income must be subtracted from the borrower's gross monthly income and not treated as a recurring monthly liability unless otherwise noted.

RESIDUAL INCOME TABLE

The borrower's residual income is calculated by adding the total monthly income from all sources and subtracting the total monthly expenses.

To determine if the borrower's monthly residual income is sufficient to meet his/her financial obligations, compare the borrower's monthly residual income with the applicable family size, and region table below.

Table of Residual Incomes by Region				
Family Size	**Northeast**	**Midwest**	**South**	**West**
1	$ 540	$ 529	$ 529	$ 589
2	$ 906	$ 886	$ 886	$ 998
3	$ 946	$ 927	$ 927	$1,031
4 or more	$1,066	$1,041	$1,041	$1,160

States included on the Table of Residual Income:

Region	States
Northeast	CT, MA, ME, NH, NJ, NY, PA, RI, VT
Midwest	IA, IL, IN, KS, MI, MN, MO, ND, NE, OH, SD, WI
South	AL, AR, DC, DE, FL, GA, KY, LA, MD, MS, NC, OK, PR, SC,TN, TX, VA, VI, WV
West	AK, AZ, CA, CO, HI, ID, MT, NM, NV, OR, UT, WA, WY

When determining "family size" count all members of the household (without regard to the nature of the relationship) including the Non- Borrowing Spouse and Other Non-Borrowing Household Members as application.

Smartfi may omit a Non-Borrowing Spouse and Other Non-Borrowing Household member from the family size provided that their residual income is equal to or exceeds the income required for a one-person family size for the geographic area in which the property is located.

GROSSING UP NON-TAXABLE INCOME

The cash flow/residual income analysis will consider Federal Taxes. If no federal taxes are paid on some or all of a borrower's income, it will be reflected in the expenses analysis for residual income. Non-taxable income, therefore, **MAY NOT** be "grossed up."

EMPLOYMENT RELATED INCOME – GENERAL

Employment income refers to income received as an employee of a business that is reported on IRS Form W-2. Smartfi may use employment related income as effective income in accordance with the standards provided for each type of employment related income.

In assessing employment income Smartfi must recognize that many borrowers may have primary employment of less than 40 hours per week or may have recently returned to the workforce following retirement.

For all employment related income, Smartfi must verify the borrower's most recent two (2) years of employment and income, and document using one (1) of the methods below.

TRADITIONAL CURRENT EMPLOYMENT DOCUMENTATION

Smartfi must obtain the most recent pay stubs covering a minimum of 30 consecutive days period (if paid weekly or bi-weekly, pay stubs must cover a minimum of 28 consecutive days) that show the borrower's year-to-date earnings, Employer's name, and address, pay period, borrower's name and one (1) of the following:

- A written Verification of Employment (VOE) covering two (2) years; **OR**
- An electronic verification acceptable to FHA (Work Number, etc.)

Re-verification of employment must be completed within **10 days PRIOR TO DISBURSEMENT**. Verbal reverification of employment is acceptable.

ALTERNATIVE CURRENT EMPLOYMENT DOCUMENTATION

If using alternative documentation, Smartfi must obtain copies of the pay stubs covering the most recent 30 consecutive day period (if paid weekly or bi-weekly, pay stubs must cover a minimum of 28 consecutive days) that show the borrower's year-to-date earnings, Employer's name, and address, pay period, borrower's name, and the following:

- Obtain copies of the original IRS W-2 forms from the previous two (2) years; AND
- Document current employment by telephone. Sign, and date the verification documentation, and note the name, title, and telephone number of the person with whom employment was verified.

Re-Verification of employment must be completed within **10 days PRIOR TO DISBURSEMENT**. Verbal re-verification of employment is acceptable.

PAST EMPLOYMENT DOCUMENTATION

Direct verification of the borrower's employment history for the previous two years is not required if all of the following conditions are met:

- The current employer confirms a two (2) year employment history, or a paystub reflects a hiring date;
- Only base pay is used in calculating effective income (no overtime or bonuses); AND
- The borrower executes IRS Form 4506, Request for Copy of Tax Returns, or IRS Form 8821 Tax Information Authorization, for the previous two (2) tax years.

If the borrower has not been employed with the same employer for the previous two (2) years and/or not all conditions immediately above can be met, then Smartfi must obtain one (1) or a combination of the following for the most recent two (2) years to verify the borrower's employment history:

- W-2(s);
- VOE(s);
- Electronic verification acceptable to FHA; OR
- Evidence supporting enrollment in school or the military during the most recent two (2) full years.

CALCULATION OF EFFECTIVE INCOME – SALARY

For employees who are salaried and whose income has been and will likely be consistently earned, Smartfi must use the current salary to calculate effective income.

CALCULATION OF EFFECTIVE INCOME – HOURLY

For employees who are paid hourly, and whose hours do not vary, Smartfi must consider the borrower's current hourly rate to calculate effective income.

For employees who are paid hourly, and whose hours vary, Smartfi must average the income over the previous two (2) years. If Smartfi can document an increase in pay rate the underwriter may use the most recent 12-month average of hours at the current pay rate.

PART-TIME INCOME

Part-Time employment refers to employment that is not the borrower's primary employment and is generally performed for less than 40 hours per week. Smartfi may use part-time income as effective income if the borrower has worked a part-time job uninterrupted for the past two (2) years, and the current position is reasonably likely to continue.

Smartfi must average the income over the previous two (2) years. If the underwriter can document an increase in pay rate the underwriter may use a 12-month average of hours at the current pay rate.

OVERTIME AND BONUS INCOME

Overtime and Bonus income refers to income that the borrower receives in addition to the borrower's normal salary. Smartfi may use overtime and bonus income as effective income if the borrower has received this income for the past two (2) years and it is reasonably likely to continue.

Periods of overtime and bonus income less than two (2) years may be considered effective income if Smartfi documents that the overtime and bonus income has been consistently earned over a period of not less than one (1) year and is reasonably likely to continue.

Calculating Overtime and Bonus Income

For borrowers with bonus or overtime income, Smartfi must average the income earned over the previous two (2) years to calculate effective income. However, if the overtime or bonus income from the current year decreases by 20% or more from the previous year, Smartfi **MUST** use the current year's income.

TIP/GRATUITY INCOME

Tip income averaged over a 2-year period, may be included for qualification purposes provided it meets the following requirements:

- Borrower must have a 2-year history evidencing receipt of tip income
- Tip income must be stable or increasing, and likely to continue
- Provide a verification of employment letter or 2 years of personal income tax returns (including W-2s).
- Current paystub with year-to-date earnings for the most recent 30 days

Note: If the tip income is not reported on the paystub for income tax returns, it may not be used for qualifying or as a compensating factor.

COMMISSION INCOME

Commission income refers to income that is paid contingent upon the conducting of a business transaction or the performance of a service.

Smartfi may use commission income as effective income if the borrower earned the income for at least one (1) year in the same or similar line of work and it is reasonably likely to continue.

For commission income less than or equal to 25% of the borrower's total earnings, Smartfi must use traditional or alternative employment documentation.

For commission income greater than 25% of the borrower's total earnings, Smartfi must obtain signed tax returns including all applicable schedules, for the last two (2) years. In lieu of signed tax returns from the borrower, the underwriter may obtain a signed IRS Form 4506-C, and tax transcripts directly from the IRS.

Calculating Commission Income

Smartfi must calculate effective income from commission by using the LESSER of:

- The average net commission income earned over the previous two (2) years.
- The length of time commission income has been earned is less than 2 years.
- The average net commission income earned over the previous one year.

Smartfi must calculate net commission income by subtracting the unreimbursed business expenses from the gross commission income. Smartfi must reduce the effective income by the amount of any unreimbursed employee business expenses, as shown on the borrower's Tax Return 1040s Schedule A.

AUTOMOBILE ALLOWANCES

Automobile Allowance refers to funds provided by the borrower's employer for automobile related expenses.

Smartfi must verify and document the automobile allowance received from the employer for the previous 2 years. Smartfi must also obtain federal tax returns with Schedule A, IRS Form 2106 Employee Business Expenses, for the previous 2 years.

Calculating Automobile Allowance Income

Smartfi must determine the portion of the allowance that can be considered effective income. Smartfi must subtract automobile expenses as shown IRS Form 2106 from the automobile allowance before calculating effective income based on the current amount of the allowance received.

If the borrower uses the standard per-mile rate in calculating automobile expenses, as opposed to the actual cost method, the portion that the IRS considers depreciation may be added back to the income. Expenses that must be treated as recurring debt include:

- The borrower's monthly car payment
- Any loss resulting from the calculation of the difference between the actual expenditures and the expense account allowance.

Automobile allowance refers to the amount of automobile allowance that exceeds the mortgagor's actual automobile expenditures.

SEASONAL INCOME

Seasonal income refers to employment that is not year-round, regardless of the number of hours per week the borrower works on the job. Smartfi may consider seasonal employment as effective income if the borrower has worked the same line of work for the past two (2) years and is reasonably likely to be rehired for the next season. Smartfi may consider unemployment income an effective income for those with effective seasonal employment income.

For seasonal employees with unemployment income, Smartfi must document the unemployment income for two (2) full years and there must be reasonable assurance that this income will continue.

Calculating Seasonal Income

For employees with seasonal income, Smartfi must average the income earned over the previous two (2) full years to calculate effective income.

EMPLOYER HOUSING SUBSIDY

Employer Housing Subsidy refers to employer provided housing assistance. Smartfi may utilize employer housing subsidy as effective income. Smartfi must verify and document the existence and the amount of the housing subsidy.

Calculating Employer Housing Subsidy Income

For borrowers receiving an employer housing subsidy, Smartfi may add the employer housing subsidy to the total effective income.

INCOME FROM EMPLOYMENT WITH FAMILY-OWNED BUSINESS

Family-Owned Business Income refers to income earned from a business owned by the borrower's family, but in which the borrower is **NOT** an owner.

Smartfi may consider family-owned business income as effective income if the borrower is not an owner in the family-owned business.

Smartfi must verify and document that the borrower is not an owner in the family-owned business by using official business documents showing the ownership percentage.

Official business documents include corporate resolutions or other business organizational documents, business tax returns or Schedule K-1 (IRS Form 1065), or an official letter from a certified public accountant on their business letterhead.

In addition to traditional or alternative documentation requirements, Smartfi must obtain copies of signed personal tax returns or tax transcripts.

Calculating Income from Employment with Family-Owned Business

Salary

For borrowers who are salaried and whose income has been and will likely continue to be consistently earned, Smartfi must use the current salary to calculate effective income.

Hourly

For borrowers who are paid hourly, and whose hours do not vary, Smartfi must consider the borrower's current hourly rate to calculate effective income.

For borrowers who are paid hourly, and whose hours vary, Smartfi must average the income over the previous two (2) years. If Smartfi can document an increase in pay rate Smartfi may use the most recent 12-month average of hours at the current pay rate.

FREQUENT CHANGES IN EMPLOYMENT

If the borrower has changed jobs more than three (3) times in the previous 12-month period, or has changed lines of work, Smartfi must take additional steps to verify and document the stability of the borrower's employment income.

Smartfi must obtain:

- Transcripts of training and education demonstrating qualification for a new position; OR
- Employment documentation evidencing continual increase income and/or benefits.

GAPS IN EMPLOYMENT

For borrowers with gaps in employment of six (6) months or more (an extended absence), Smartfi may consider the borrower's current income as effective income if it can be verified and documented that:

- The borrower has been employed in the current job for at least six (6) months at the time of case number assignment; AND
- A two (2) year work history prior to the absence from employment using standard or alternative employment verification.

TEMPORARY REDUCTIONS IN INCOME

For borrowers with a temporary reduction in income due to a short-term disability or similar circumstance, Smartfi may consider the borrower's current income as effective income, if it can be verified and documented that:

- The borrower intends to return to work;
- The borrower has the right to return to work; AND
- The borrower can meet their financial obligations taking into account any reduction of income due to the circumstance.

Smartfi must provide the following documentation for borrowers on temporary leave:

- A written statement from the mortgagor confirming the mortgagor's intent to return to work, and the intended date of return; and
- Documentation generated by current employer confirming the mortgagor's eligibility to return to current employer after temporary leave; and
- Documentation of sufficient liquid assets used to supplement the borrower's income through intended date of work with current employer.

RETURNING TO WORK AFTER RETIREMENT

Smartfi may consider the income of borrowers who have returned to work after retirement of more than two years if it can verify and document:

The borrower has been employed in the current job for at least six months at the time of case assignment,

Written VOE will be required to validate start dated and employment continuance.

SELF-EMPLOYMENT INCOME

Self-Employment income refers to income generated by a business in which the borrower has a 25% or greater ownership interest.

There are four (4) basic types of business structures. They include:

- Sole proprietorships,
- Corporations,
- Limited liability of "S" corporations, AND
- Partnerships

Smartfi may consider self-employment income if the borrower has been self-employed for at least two (2) years. If the borrower has been self-employed between one (1) and two (2) years, Smartfi may only consider the income as effective income if the borrower was previously employed in the same line of work in which the borrower is self-employed or in a related occupation for at least two (2) years.

Income obtained from businesses with annual earnings that are stable or increasing is acceptable. If the income from the businesses shows a greater than 20% decline in effective income over the analysis period, Smartfi must document that the business income is now stable.

Smartfi may consider income as stable after a 20% reduction if Smartfi can document the reduction in income was the result of an extenuating circumstance, and the borrower can demonstrate the income has been stable or increasing for a minimum of 12 months.

Required Documentation for Self-Employed Income

Smartfi must obtain complete federal income tax returns, including all schedules.

In lieu of signed individual or business tax returns from the borrower, Smartfi may obtain a signed IRS Form 4506-C, and tax transcripts directly from the IRS.

Smartfi must obtain a year-to-date profit and loss (P&L) statement and balance sheet **if** more than a calendar quarter has elapsed since date of the most recent calendar or fiscal year-end tax return was filed by the borrower.

A balance sheet **is not** required for self-employed borrowers filing Schedule C income.

If the income used to calculate residual income exceeds the two (2) year average of tax returns, an audited P&L or signed quarterly tax return obtained from IRS is required.

Note: We must obtain a business credit report for all corporations and "S" corporations.

Calculating Self-Employed Income

Smartfi must analyze the borrower's tax returns to determine the gross self-employment income. The borrower must provide personal and business, as applicable, federal income tax returns with all schedules for the most recent 2 years and a YTD P & L with balance sheet for the current year. (A balance sheet is not required for self-employment filed using Schedule C).

IRS approved extensions for filing of returns may be considered on a case-by-case basis.

Smartfi must calculate the gross self-employment income by using the **LESSER** of:

- The average gross self-employment income earned over the previous two (2) years; OR
- The average gross self-employment income earned over the previous one (1)year.

Note: If the borrower pays themselves W-2 income, the most recent 2 years of W-2s as well as the most recent 30 days of paystubs will be required.

MILITARY INCOME

Military income refers to income received by military personnel during their period of active, Reserve, or National Guard service, including:

- Base pay;
- Basic allowance for housing;
- Clothing allowances;
- Flight or hazard pay;
- Basic allowance for Subsistence, and
- Proficiency pay.

Smartfi may not use education benefits as effective income.

- Smartfi must obtain a copy of the borrower's military Leave and Earnings Statement (LES).
- Smartfi must verify the Expiration Term of the Service date of the LES. If the Expiration Term of Service date is within the first 12 months of the mortgage, military income may only be considered effective income if the borrower presents their intent to continue military service at time of receipt.

Calculating Military Income

Smartfi must use the current amount of military income received to calculate effective income.

FOREIGN INCOME

Foreign income is income received outside of the United States. Foreign income may be acceptable, only if all the following requirements are met:

- The income must be reported on the borrowers' US tax returns.
- The income must meet standard income documentation requirement for the income type and be converted to US dollars.
- Income received in a foreign bank account must be converted to US dollars.

Note: To convert foreign funds to US dollars, the exchange rate of the foreign currency to US currency must be documented with a currency conversion. Refer to the following site for exchange-rate information: http://online.wsj.com/mdc.public/page2_3021-forex.html.

Calculating Foreign Income

The greater of the following calculations may be used:

- A 12-month average of the exchange rate, OR
- 75% of the current exchange rate

Note: The DE Underwriter must be diligent in satisfactorily documenting and validating occupancy of the subject property.

EXPECTED INCOME

Expected Income refers to income from cost-of-living adjustments, performance raises, a new job, or retirement that has not been, but will be received within 60 Days of mortgage closing.

Smartfi may consider Expected Income as effective income except when expected income is to be derived from a family-owned business.

Smartfi must verify and document the existence and amount of expected income with the employer in writing and that it is guaranteed to begin within 60 Days of mortgage closing. For expected retirement income, the lender must verify the amount and that it is guaranteed to begin within 60 Days of the mortgage closing.

Calculating Expected Income

Income is calculated in accordance with the standards for the type of income being received. Smartfi must also verify that the borrower will have sufficient income or liquid assets to meet his or her financial obligations between mortgage closing and the beginning of the receipt of the income.

NON-TAXABLE INCOME

Refers to types of income not subject to federal taxes, which includes, but is not limited to:

- Some portion of Social Security Income;
- Some federal government employee retirement income;
- Railroad Retirement benefits;
- Some state government retirement income;
- Certain types of disability and public assistance payments;
- Child support;
- Military allowance; and
- Other income that is documented as being exempt from federal income taxes.

NON-EMPLOYMENT SOURCES OF INCOME

Smartfi must verify and document any income used in the cash flow/residual income from the following below sources:

SOCIAL SECURITY RETIREMENT INCOME

Social Security Retirement Income or Supplemental Security Income (SSI) refers to income received from the SSA other than disability income.

Smartfi must verify and document the borrower's receipt of retirement income from the SSA. For Social Security Retirement income, Smartfi must obtain the Awards letter or equivalent **and** one (1) of the following documents:

- Recent bank statement evidencing direct deposit of SS income, or
- Federal tax returns, or
- Social Security Benefit Statement, SSA Form 1099/1042S.

If the Notice of Award or equivalent document does not have a defined expiration date, the underwriter must consider the income effective and reasonably likely to continue. The underwriter should not request additional documentation from the borrower to demonstrate continuance of Social Security Income.

Note: When ONLY Social Security Retirement Income is used as effective income and the below thresholds are met, we will NOT include a Federal and/or State income tax liability in the monthly expenses.

Borrower files his/her federal tax return as an Individual and Social Security Income is $25,000 or less; **or** Joint federal tax return and combined Social Security Income is $32,000 or less.

Calculating Social Security Retirement Income

Smartfi must use the current amount of SS Income received to calculate effective income.

PENSION INCOME

Pension refers to income received from the borrower's former employer(s).

Smartfi must verify and document the borrower's receipt of periodic payment from the borrower's pension and that the payments are likely to continue for at least three (3) years.

Smartfi must obtain any one of the following documents:

- A copy of the borrower's pension/retirement letter from the former employer
- The most recent bank statement evidencing receipt of income from the former employer; OR
- Federal tax returns

Note: If documentation does not clearly identify the recipient, additional documentation will be required.

We do **not** need to document continuance for **FEDERAL pensions**. If the source of the pension income is the federal government, including VA (Veterans Affairs), we must consider the income effective and reasonably likely to continue. Evidence income is likely to continue for at least 3 years is required for any state, municipal, or private pension income.

Calculating Pension Income

Smartfi must use the current amount of pension income received to calculate effective income.

VETERANS AFFAIRS BENEFITS

For VA benefits, Smartfi must obtain a copy of the VA award letter/verification of benefits, showing the amount of the assistance and the expiration date of benefits, if any. For VA Pensions, continuance will be assumed unless termination date is shown.

Smartfi must obtain from the borrower a copy of the veteran's last Benefits Letter showing the amount of the assistance, and one of the following documents:

- federal tax returns; or
- The most recent bank statement evidencing receipt of income from the VA.

DISABILITY BENEFITS

Disability benefits refer to benefits received from the SSA, Department of Veterans Affairs (VA), or a private disability insurance provider. Smartfi must verify and document receipt of the above benefit by obtaining documentation that establishes the award of benefit to the borrower. This documentation must clearly show that the income is stable and expected to continue.

The following are requirements for each type of disability benefit:

SOCIAL SECURITY DISABILITY BENEFITS

This category includes Supplement Security Income (SSI). Smartfi will require the most recent Notice of Award letter from the SSA and borrower's most recent bank statement evidencing receipt of the income from SSA.

VETERANS AFFAIRS DISABILITY BENEFITS

Smartfi must obtain a copy of the Veteran's most recent benefits letter showing the amount of assistance granted and the borrower's most recent bank statement evidencing receipt of income from the VA.

PRIVATE DISABILITY BENEFITS

Smartfi will require documentation from the private disability insurance provider showing the amount of assistance and expiration date of the benefits, if any, and the borrowers most recent bank statement evidencing receipt of income from insurance provider.

If any disability income is due to expire within three years from the date of the mortgage application, that income cannot be used as effective income.

If the Notice of Award or equivalent document does not have a defined expiration date, the underwriter may consider the income effective and reasonably likely to continue.

Smartfi may not rely upon a pending or current reevaluation of medical eligibility for benefit payments as evidence that the benefit payment is not reasonably likely to continue.

Under no circumstances may we inquire into or request documentation concerning the nature of the disability or the medical condition of the borrower.

Calculating Disability Benefits

The lender must use the most recent amount of benefits received to calculate effective income.

INDIVIDUAL RETIREMENT ACCOUNT (IRA) AND 401(K) INCOME

An Individual Retirement Account (IRA/401(k)) Income refers to income received from these types of accounts.

Smartfi must verify and document the borrower's receipt of recurring IRA/401(k) distribution income and that it is reasonably likely to continue for three (3) years.

Smartfi must obtain the most recent IRA/401(k) statement AND one (1) of the following:

- Federal tax returns; OR
- The most recent bank statement evidence receipt of income.

Calculating Individual Retirement Account (IRA) and 401(k) Income

For borrowers with IRA/401(k) income that has been and will be consistently received, Smartfi must use the current amount of IRA/401(k) income received to calculate effective income.

For borrowers with fluctuating IRA/401(k) income, Smartfi must use the average of IRA/401(k) income received over the previous two (2) years to calculate effective income. If IRA/401(k) income has been received for less than two (2) years, Smartfi must use the average over the time of receipt.

RENTAL INCOME FROM THE SUBJECT PROPERTY

Rental income from the Subject Property refers to income received when the subject property has 2-4 units. Smartfi may consider rental income from existing and prospective tenants if documented in accordance with the following requirements.

Limited or No History of Rental Income

Where the borrower does not have a history of rental income from the subject property since the previous tax filing: Smartfi must verify and document the proposed rental income by obtaining an appraisal showing fair market rent (use FNMA 1025 Small Residential Income Property Appraisal Report) and the prospective leases, if available.

History of Rental Income

Where the borrower has a history of rental income from the subject property since the previous tax filing, Smartfi must verify and document the existing rental income by obtaining:

- the current lease
- rental history over the previous 24 months that is free of unexplained gaps greater than three (3) months (such gaps could be explained by student, seasonal, or military renters or property rehabilitation)

- and the borrower's most recent tax returns, including Schedule E, from the previous two (2) years.

For properties with less than two (2) years of rental income history, Smartfi must document the date of acquisition by providing the Deed, Settlement Statement, or other legal document.

Calculating Rental Income from the Subject Property

Smartfi **MUST** add the net subject property rental income to the borrower's gross income.

Limited or No History of Rental Income Calculation

To calculate the effective income from the subject property where the borrower does not have a history of rental income from the subject property since the previous tax filing, Smartfi must use the **LESSER** of:

- The monthly operating income reported on FNMA Form 216; OR
- 75% of the LESSER of:
- Fair market rent reported by the appraiser; OR
- The rent reflected in the lease or other rental agreement.

History of Rental Income Calculation

Smartfi must calculate the rental income by averaging the amount shown on Schedule E.

Depreciation, mortgage interest, taxes, insurance, and any HOA dues shown on Schedule E may be added back to the net income or loss.

If the property has been owned for less than two (2) years, Smartfi must annualize the rental income from the length of time the property has been owned.

Note: When reviewing Schedule E, be sure to review property type and fair days rented.

Note: Smartfi will require Tax transcripts for each tax year used for qualifying income.

RENTAL INCOME – OTHER REAL ESTATE HOLDINGS

Rental income from other real estate holdings may be considered as effective income if the documentation requirements listed below are met. If rental income is derived from the property being vacated by the borrower, the borrower must:

- be relocating to an area more than 100 miles from the borrower's current principal residence.
- Smartfi **MUST** obtain a lease agreement of at least one (1) year's duration after the mortgage has closed, and
- evidence of payment of the security deposit or first month's rent.

Smartfi may consider rental income from other properties if documented in accordance with the following requirements.

Limited or No History of Rental Income

Where the borrower does not have a history of rental income since the previous tax filing, **including** property being vacated by the borrower Smartfi **MUST** obtain an appraisal evidencing market rent **AND** that the borrower has at least 25% equity in the property. The appraisal is not required to be completed by an FHA Roster appraiser.

Two to Four Units

Smartfi **MUST** verify and document the proposed rental income by obtaining an appraisal showing fair market rent (use FNMA Form 1025, Small Residential Income Property

Appraisal Report) and the prospective leases if available.

One Unit

Smartfi **MUST** verify and document the proposed rental income by obtaining a FNMA Form 1004, Uniform Residential Appraisal Report, FNMA Form 1007, Single Family Comparable Rent Schedule, and FNMA Form 216, Operating Income Statement, showing fair market rent and, if available, the prospective lease.

History of Rental Income

Smartfi must obtain the borrower's last two (2) years tax returns with Schedule E.

Calculating Rental Income from Other Real Estate Holdings Limited or No History of Rental Income

To calculate the effective net rental income from other real estate holdings where the borrower does not have a history of rental income since the previous tax filing, Smartfi **MUST** deduct the principal, interest, taxes, and insurance payment (PITI) from the **LESSER** of:

- The monthly operating income reported on FNMA Form 216; OR
- 75% of the LESSER of:
- Fair market rent reported by the appraiser; OR
- The rent reflected in the lease or other rental agreement.

History of Rental Income Calculation

Smartfi must calculate the net rental income by averaging the amount shown on Schedule E provided the borrower continues to own all properties included on Schedule E. Depreciation shown on Schedule E may be added back to the net income or loss. If the property has been owned less than two (2) years, the underwriter must annualize the rental income for the length of time the property has been owned.

For properties with less than two (2) years of rental income history, the underwriter must document the date of acquisition by providing the Deed, Settlement Statement, or other legal document.

Positive net rental income **MUST** be added to the borrower's effective income. Negative net rental income **MUST** be included as a **debt/liability**.

INCOME FROM BOARDERS OF THE SUBJECT PROPERTY AND/OR ADU

Boarder refers to an individual renting space inside the borrower's dwelling unit.

Rental income from boarders is only acceptable if the borrower has a two-year history of receiving income from boarders that is shown on the tax return and the borrower is currently receiving boarder income.

Smartfi must obtain two (2) years of borrower's tax returns evidencing income from boarders and the current lease.

Calculating Rental Income from Boarders

Smartfi must calculate the effective income by using the **LESSER** of the two-year average or the current lease.

> **Note: For HECM for Purchase transaction, the lender must obtain a copy of the executed written agreement documenting their intent to continue boarding with the borrower.**

INVESTMENT INCOME

Investment income refers to interest and dividend income received from assets such as certificates of deposits, mutual funds, stocks, bonds, money markets, and savings and checking accounts.

Smartfi must verify and document the borrower's investment income by obtaining tax returns for the previous two (2) years **AND** the most recent asset statement.

Calculating Investment Income

Smartfi must calculate investment income by using the **LESSER** of:

- The average investment income earned over the previous two (2) years; OR
- The average investment income earned over the previous one (1) year.

Smartfi **MUST** subtract any of the assets used for the required cash investment for a HECM for Purchase from the borrower's liquid assets prior to calculating any interest or dividend income.

CAPITAL GAINS AND LOSSES

Capital gains refers to a profit that results from a disposition of a capital asset, such as stock, bond, or real estate, where the amount realized on the disposition exceeds the purchase price.

Capital gains or losses must be considered when determining effective income, when the individual has a constant turnover of assets resulting in gains or losses.

Three (3) years' tax returns are required to evaluate an earnings trend. If the trend:

- Results in a gain, it may be added as effective income, OR
- Consistently shows a loss, it **MUST** be deducted from the total income.

Note: Carryover loss does not need to be subtracted from income, this will show $3000 on the Tax Return.

ROYALTY INCOME

Royalty income is a payment received for the use and exploitation of artistic or literary works, patents, and mineral rights. Royalty income is generally of two types: royalties for the use of copyrights, trademarks, and patents, and royalties from the extraction of oil, gas, or minerals.

Smartfi must verify and document the following:

- Royalty contract agreement, or statement confirmation amount, frequency, and duration of the income, AND
- The borrowers previous 2 years signed federal income tax returns, including the related IRS Form 1040, Schedule E.

Confirm that the borrower has received royalty payments for at least 12 months, and that the payments will continue for a minimum of 3 years after closing.

Calculating Royalty Income

Smartfi must calculate the royalty income by using the lesser of:

- The average royalty income earned over the most recent two years; or

- The average royalty income earned over the previous 1 year if income is declining.

TRUST ACCOUNTS INCOME

Trust income refers to income that is regularly distributed to a borrower from a trust.

Smartfi must verify and document the following items:

- Existence of the Trust Agreement or other Trustee Statement
- The frequency, duration, and amount of the distribution
- Most recent bank statement or transaction history from the bank
- That regular payments will continue for at least the first 3 years of the mortgage term.

Calculating Trust Accounts Income

Smartfi **MUST** use the income based on the terms and conditions in the Trust Agreement or other trustee statement to calculate effective income.

ANNUITIES OR SIMILAR INCOME

Annuity income refers to a fixed sum of money periodically paid to the borrower from a source other than employment.

Smartfi will require ONE of the following:

- Copy of Annuity agreement establishing amount of annuity, frequency, and at least a 3-year continuance with most recent bank statement evidencing receipt of annuity income
- Signed letter from managing financial institution establishing amount of annuity, frequency, and at least a 3-year continuance with most recent bank statement evidencing receipt of annuity income.

Calculating Annuities and Similar Income

Smartfi must use the current rate of the annuity to calculate effective income.

Smartfi must subtract any of the assets used for the required cash investment for HECM for Purchase from the borrower’s liquid assets prior to calculating any annuity income.

NOTES RECEIVABLE INCOME

Notes receivable income refers to income received by the borrower as payee or holder in due course of a promissory note or similar credit instrument.

Smartfi must verify and document the existence of the note. The underwriter must also verify and document the payments have been consistently received for the previous 12 months by obtaining tax returns, deposit slips or cancelled checks, **AND** that such payments are guaranteed to continue for the first three (3) years of the mortgage.

Calculating Notes Receivable Income

For borrowers who have been and will be receiving a consistent amount of notes receivable income, Smartfi must use the current rate of income to calculate effective income.

For borrowers whose notes receivable income fluctuates, Smartfi must use the average of the income received over the previous year to calculate effective income.

ALIMONY, CHILD SUPPORT, MAINTENANCE INCOME

Alimony, Child Support, or Maintenance income refers to income received from a former spouse or partner or from a non-custodial parent of the borrower's minor dependent.

Smartfi must obtain a fully executed copy of the borrower's final divorce decree, legal separation agreement, court order, or voluntary payment agreement with documentation receipt.

When using a final divorce decree, legal separation agreement or court order, Smartfi must obtain evidence of receipt using deposits on bank statements, cancelled checks, or documentation from the child support agency for the most recent three (3) months that supports the amount used as effective income.

Smartfi must document the voluntary payment agreement with 12 months of cancelled checks, deposit slips, or tax returns.

Smartfi must provide evidence that the claimed income will continue for at least three (3) years. Smartfi may use the front and pertinent pages of the divorce decree/settlement agreement and/or court order showing the financial details.

Calculating Alimony, Child Support, Maintenance Income

When using a final divorce decree, legal separation agreement or court order, if the borrower has received consistent alimony, child support, or other maintenance payments for the most recent three (3) months, Smartfi may use the current payment to calculate effective income.

When using evidence of voluntary payments, if the borrower has received consistent alimony, child support, or other maintenance payments for the most recent six (6) months, Smartfi may use the current payment to calculate effective income.

If the alimony, child support, or other maintenance payments have not been consistently received for the most recent six (6) months, Smartfi must use the average of the income received over the previous two (2) years to calculate effective income. If alimony, child support, or other maintenance income has been received for less than two (2) years, Smartfi must use the average over the time of receipt.

FOSTER CARE INCOME

Foster care income is income received from a state or county-sponsored agency or organization for providing temporary care for one or more children.

Foster care income is paid to the caregiver for the benefit of the foster individual.

Smartfi must document the foster care income with the following:

- Letters of verification from the organization providing the income, and
- Copies of bank statements or checks for the most recent 30 days, showing the payments received for providing foster care, and
- Documentation showing the borrower has a two-year history of providing foster care services and that there is a likelihood of 3 years continuation.

Calculation of Foster Care Income

Effective income used should be the lesser of:

- The current amounts received, or
- A Two-year average of amounts received.

GOVERNMENT ASSISTANCE NON-CASH BENEFITS

Smartfi may count as income non-cash benefits being received by the borrower through Federal, state, or local government programs, e.g., Supplemental Nutritional Assistance Program (SNAP), energy assistance, etc. In determining whether such benefits may be counted as income Smartfi **MUST**:

- Verify that the benefits are being received at the time of loan application, or that an Award letter has been issued, and benefits will begin to be received within 60 days. Smartfi may not count benefits for which the borrower is potentially eligible and intends to apply;
- Verify that the benefits are not subject to any specific termination date other than one related to the death of the borrower or the sale of the property; AND
- Verify that approval of the HECM will not jeopardize continued eligibility for the benefits, e.g., HECM proceeds would trigger disqualification based on program income or asset requirements.

Some benefit programs may result in a reduction in the borrower's expenses rather than increasing their income (e.g., the borrower is charged a lower rate for insurance). In these cases, the reduced amount may be used in calculating expenses and must not be treated as income. See **Expense Analysis**.

OTHER PUBLIC ASSISTANCE

Public assistance refers to income received from government assistance programs.

Smartfi must verify and document the income received from the government agency. If any public assistance income is due to expire within three years from the date of mortgage application, that income cannot be used as effective income. If the documentation does not have an expiration date, the lender may consider the income effective and reasonably likely to continue.

Calculating Other Public Assistance Income

Smartfi must use the current rate of public assistance received to calculate effective income.

IMPUTED INCOME FROM ASSET DISSIPATION

Regular income from interest, dividends, or other returns from the borrower's investments may be included in the calculation of residual income provided that such income is properly documented.

Alternatively, Smartfi may estimate imputed income from dissipation of liquid assets, defined as assets that can be converted to cash within one-year without payment of an IRS penalty. The borrower does not have to liquidate assets in order to obtain HECM financing.

It is not permitted to count the same asset twice, i.e., as a source of interest income and as imputed income from the dissipation of the asset. This applies to income from interest, dividends, or other returns on the account.

If any funds to close will come from the account, Smartfi will first subtract the funds to close from the account balance before dissipating the funds.

If the account receives deposits from other sources of effective income, i.e., social security, pension, W-2 income etc., and those sources are income being included in the borrower's financial assessment, Smartfi will subtract any of those deposit from the ending balance of the most recent months statement before dissipating.

Liquid asset sources from which imputed income may be calculated include:

Asset Source	Amount To Be Counted
Savings and Checking Accounts, Certificates of Deposit, Roth IRAs and any other assets that are not subject to Federal taxes.	100%
Other assets that are subject to Federal taxes	85% *

*Smartfi may use the borrower's actual tax rate based on Federal tax returns from the prior year if tax rate is lower than 15% or no discount if borrower does not have a Federal tax obligation.

Smartfi **MUST** calculate the combined value of assets and calculate income from these sources.

Divide the total adjusted value by the remaining life expectancy.

If the asset is jointly held with a Non-Borrowing Spouse or other party not obligated on the mortgage, the asset may be counted provided that the borrower provides documentation that the borrower has unrestricted access to that asset.

> **Note: Assets may not be dissipated from an account where the borrower is not an owner of the account.**

ASSET DISSIPATION CALCULATION TABLE

Total discounted asset value-funds to close (if applicable) / Life expectancy in months = Total monthly income from assets.

ASSETS – CHECKING AND SAVINGS ACCOUNTS

Checking and savings accounts refer to funds from borrower-held accounts.

If to be considered as part of the financial assessment, Smartfi must verify and document the existence of and amounts in the borrower's checking and savings accounts.

If the borrower does not hold the deposit account solely, all non-borrower parties on the account must provide a written statement that the borrower has full access to and use of the funds.

Smartfi must obtain a written Verification of Deposit (VOD) and the borrower's most recent statement for each account.

If a VOD is not obtained, a statement showing the previous month's ending balance for the most recent month is required. If the previous month's balance is not shown, Smartfi must obtain statement(s) for the most recent two (2) months.

ASSETS – CASH ON HAND

Cash on hand refers to cash held by the borrower outside of a financial institution.

Smartfi must verify that the borrower's cash on hand is deposited in a financial institution or held by escrow/title company.

Smartfi must verify and document the borrower's cash on hand by obtaining an explanation from the borrower describing how the funds were accumulated **AND** the amount of time it took to accumulate the funds.

Smartfi must also determine the reasonableness of the accumulation based on the time period during which the funds were saved and the borrower's:

- Income stream;
- Spending habits.
- Documented expenses; AND
- History of using financial institutions

ASSETS – RETIREMENT ACCOUNTS

Retirement accounts refer to assets accumulated by the borrower for the purpose of retirement.

Smartfi must obtain the most recent monthly or quarterly statement to verify and document the existence and amounts in the borrower's retirement accounts, the borrower's eligibility for withdrawals, and the terms and conditions for withdrawal from any retirement account.

ASSETS- STOCKS AND BONDS

Stocks and bonds are investment assets accumulated by the borrower.

Smartfi must determine the value of stocks and bonds from the most recent monthly or quarterly statement.

If the stocks and bonds are not held in a brokerage account, Smartfi must determine the current value of the stocks and bonds through third party verification. Government-issued savings bonds are valued at the original purchase price, unless Smartfi verifies and documents that the bonds are eligible for redemption.

Smartfi must verify and document the existence of the borrower's stocks and bonds by

obtaining brokerage statement(s) for each account for the most recent two (2) months. Evidence of liquidation is **NOT** required.

For stocks and bonds not held in a brokerage account Smartfi must obtain a copy of each stock or bond certificate.

ASSETS- PRIVATE SAVINGS CLUBS

Private Savings Clubs refer to a non-traditional method of savings by making deposits into a member arranged resource pool. Smartfi may consider private savings club funds that are distributed to and received by the borrower as an acceptable source of funds.

Smartfi must verify and document the establishment and duration of the club, and the

borrower's receipt of funds from the club. Smartfi must also determine that the received funds were reasonably accumulated and not borrowed.

Smartfi must obtain the club's account ledgers and receipts, **AND** verification from the club treasurer that the club is still active.

INCOME FROM AN ELIGIBLE NON-BORROWING SPOUSE (ENBS)

An Eligible Non-Borrowing Spouse is defined as the spouse, as determined by the law of the state in which the spouse and borrower reside or the state of celebration, of the HECM borrower at the time of closing.

An Eligible Non-Borrowing Spouse may voluntarily provide information on his or her income and the lender may use the residual income of the Eligible Non-Borrowing Souse in one of 2 ways:

- As a compensating factor; or
- To reduce the family size by one

The income must be documented in accordance with Financial Assessment requirements based on the source of income. **Non-taxable income may not be grossed up, and imputed income from dissipated assets may not be included.**

Note: A credit report will be required for expense analysis only, willingness will not apply.

INCOME FROM OTHER NON-BORROWING HOUSEHOLD MEMBERS

"Other Non-Borrowing Household Members" is defined as a person who occupies the property to be secured with the HECM, who is not the spouse of the borrower and who also is not a borrower. An Other Non-Borrowing Household Member may voluntarily provide information on his or her income and Smartfi may use his or her residual income to reduce the family size. See **Table of Residual Income**.

To be used to reduce family size, the Other Non-Borrowing Household Member must disclose and have his or her SSN verified and must meet the same documentation and verification standards as required for the borrower's income. **Non-taxable income may not be grossed up, and imputed income from dissipated assets may not be included.**

> **Note: A credit report will be required for expense analysis only, willingness will not apply.**

CREDIT HISTORY AND PROPERTY CHARGE PAYMENTS HISTORY ANALYSIS

Smartfi must determine if the borrower(s) have demonstrated the willingness to timely meet his or her financial obligations by analyzing the credit history. The DE Underwriter is to analyze the borrower(s) credit history, liabilities, and debts to determine the willingness to meet his or her financial obligations.

Smartfi may take into consideration that some borrowers seek a HECM due to financial difficulties, which may be reflected in the borrower's credit report. Smartfi must also consider to what extent the proceeds of the HECM could provide a solution to any such financial difficulties.

When serious derogatory credit such as foreclosures, bankruptcies, defaults, and late mortgage payments are on the borrower(s) record documenting extenuating circumstances is required. Absent documented Extenuating Circumstances, serious derogatory credit under such circumstances must be viewed as especially significant events that call into question the ability of the borrower(s) to manage his or her financial obligations.

If a traditional credit report is not available, and the borrower is applying for a Traditional or Refinance HECM, Smartfi is not required to develop the borrower's credit history using the requirements for non-traditional and insufficient credit. The borrower may be deemed to have an acceptable credit history.

EVALUATING CREDIT HISTORY

Smartfi must examine the borrower's overall pattern of credit behavior, not just isolated unsatisfactory or slow payments, to determine the borrower's ability to manage their financial obligations.

Smartfi does not need to consider the credit history of an Eligible NBS or Other Non-borrowing house member.

Smartfi must evaluate the borrower's payment histories in the following order:

- Current or previous mortgage debt and housing expenses and related expenses, including utilities;
- Installment debts; and
- Revolving Charge Accounts
- Significant Derogatory accounts

PAYMENT HISTORY ON HOUSING OBLIGATIONS

Smartfi must determine the borrowers housing obligation payment history for the borrower's principal residence through:

- The credit report;
- Verification of rent received directly from the landlord (or landlords with no identity-of-interest with the borrower);
- Verification of mortgage received directly from the borrowers servicer; OR
- A review of canceled checks that cover the most recent 12-month period.

Smartfi must verify and document the previous 12 months' housing history for the mortgagor's principal residence. For borrowers who indicate they are living mortgage or rent-free, Smartfi must obtain verification through the title report or other information, or if they are not the owner, from the property owner where they are residing, the borrower has been living rent-free and the amount of time the borrower has been living rent free.

If there has been a change in the borrower's principal residence, we must verify the prior payment history to have a complete 12-month payment history.

A mortgage that has been modified must utilize the payment history in accordance with the modification agreement from the time period of modification in determining late housing payments.

OTHER REAL ESTATE OWNED MORTGAGE PAYMENT HISTORY-

If the borrower owns any other real estate with an outstanding mortgage, then a 24-month mortgage payment history is also required.

If a borrower sold their primary residence or any other property in the 24 months prior to the application date, the borrower will still be required to provide a payment history for any mortgage payments, property taxes, hazard insurance and HOA dues that were due during the period of ownership that coincides with the lookback period for each (12 months for mortgage and hazard insurance and 24 months for property taxes and HOA dues).

SATISFACTORY CREDIT HISTORY

Smartfi will consider the borrower(s) to have satisfactory credit if all the following items below are met:

- All housing and installment payments were made on time for the past 12 months.
- Has no more than 2 30-day late mortgage or installment payments in the past 24 months; AND
- Has no major derogatory credit on revolving accounts in the past 12 months
    - Revolving derogatory debt includes any payment made more than 1x90 or 3x60, from the date credit was pulled.

Credit Payment History requiring additional analysis

If a borrower’s credit history does not reflect satisfactory credit as stated above, the borrower’s payment history requires additional analysis.

Smartfi must analyze the delinquent accounts to determine whether late payments were based on a disregard for financial obligations, an inability to manage debt, or Extenuating Circumstances. Smartfi must document this analysis in the file. Any explanation or documentation of delinquent accounts must be consistent with other information in the file.

Where the borrower has not met the requirements for satisfactory credit above, and no Extenuating Circumstance can be documented, Smartfi must at a minimum require a Fully Funded Life Expectancy Set-Aside (LESA).

Where a Fully funded LESA is required, Smartfi must still determine if the borrower’s credit history provides reasonable assurance that the borrower can effectively manage financial obligations even when real estate taxes and insurance are paid directly by the Lender through the LESA.

SIGNIFICANT DEROGATORY CREDIT INCLUDE BUT ARE NOT LIMITED TO:

- Collections Accounts
- Charge-Off Accounts
- Bankruptcy (chap 7, 11 or 13)
- Foreclosure/NOD/Short Sale
- Mortgage Loan Modification
- Liens/Judgments
- Disputed derogatory credit
- Delinquent federal debt
- Delinquent FHA Insured Mortgages

Note: If the above items appear on the credit report or other documentation in the loan file, they are required to be addressed even if over 24 months old.

PAST DUE ACCOUNTS

If any accounts appearing on the credit report reflect a past due balance, we are not required to evidence the payments have been brought current, however we are required to review the payment history to determine if the credit history is satisfactory.

COLLECTION ACCOUNTS

A collection account is a borrower's loan or debt that has been submitted to a collection agency through a creditor.

Smartfi must determine if collection accounts were a result of:

- The borrowers disregard for financial obligations;
- The borrower's inability to manage debt; or
- Extenuating circumstances

Smartfi must document reasons for approving a borrower for a HECM when the borrower has any collections accounts.

The borrower must provide a letter of explanation, which is supported by documentation, for each outstanding collection account. The explanation and supporting documentation must be consistent with other credit information in the file.

Refer to Expense Analysis for additional requirements where the borrower has more than $2000 in collection accounts.

CHARGE OFF ACCOUNTS

A Charge off account refers to a borrower's loan or debt that has been written off by a creditor.

Smartfi must determine if charge off accounts were a result of:

- The borrowers disregard for financial obligations;
- The borrower's inability to manage debt; or
- Extenuating circumstances

Smartfi must document reasons for approving a borrower for a HECM when the borrower has any charge off accounts.

The borrower must provide a letter of explanation, which is supported by documentation, for each outstanding charge off account. The explanation and supporting documentation must be consistent with other credit information in the file.

Note: Charge off Accounts are not included in the Expense Analysis.

DISPUTED DEROGATORY CREDIT ACCOUNT

A Disputed Derogatory Credit Account refers to disputed charge off accounts, disputed collect accounts, and disputed accounts with late payments in the last 24 months.

Smartfi must analyze the documentation provided for consistency with other credit information to determine if the derogatory credit account should be considered in the financial assessment.

The following items need NOT be considered by Smartfi:

- Disputed medical accounts, and
- Disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use provided the mortgagee includes a copy of the police report or other documentation from the creditor to support the status of the account in the file.

If the credit report indicates that the borrower is disputing derogatory credit accounts, the borrower must provide a letter of explanation and documentation supporting the basis for the dispute.

If the dispute derogatory credit resulted from identity theft, credit card theft or unauthorized use balances, Smartfi must obtain a copy of the police report or other documentation from the creditor to support the status of the accounts.

Refer to the Expense Analysis for additional requirements where the borrower has more than $1,000 in disputed derogatory accounts.

JUDGEMENTS

Judgment refers to any debt or monetary liability of the borrower created by a court, or other adjudicating body. Smartfi must verify that court-ordered judgments are resolved or paid off prior to or at closing.

Regardless of the amount of outstanding judgments, Smartfi must determine if the judgment was a result of:

- The borrowers disregard for financial obligations;
- The borrower’s inability to manage debt; or
- Extenuating circumstances

A judgment is considered resolved if the borrower has entered into a valid agreement with the creditor to make regular payments on the debt, the borrower has made timely payments for at least three months of scheduled payments and the judgment will not supersede the FHA-insured mortgage lien.

The borrower cannot prepay scheduled payments in order to meet the required minimum of three months of payments.

Smartfi must include the agreed payment amount in the borrowers' expenses when calculating residual income.

Smartfi must obtain a copy of the agreement and evidence that payments were made on time in accordance with the agreement.

Smartfi must provide the following documentation:

- Evidence of payment in full, if paid prior to settlement; or
- Payoff statement, if paid at settlement; or
- Payment arrangement with creditor, if not paid prior to or at settlement, and subordination agreement for any liens existing on title.

Judgment may be considered a mandatory obligation and paid with HECM proceeds at closing if judgment is reflected on title. If it does not reflect on title but reflects on credit or judgment search, then the judgment must be satisfied with properly sourced and seasoned funds prior to the closing.

DELINQUENT FEDERAL NON-TAX DEBT

Smartfi is required to determine whether the borrowers have delinquent federal non-tax debt. We may obtain information on delinquent federal debts from public records, credit reports or equivalent, and must check all borrowers against the Credit Alert Verification Reporting System (CAIVR).

If a delinquent federal debt is reflected the Processor must verify the validity and delinquency status of the debt by contacting the creditor agency to whom the debt is owed. If the debt was identified through CAIVRs, we must contact the creditor agency using the contact phone number and debt reference number reflected in the borrower's CAIVRs report.

If the creditor agency confirms that the debt is valid and in delinquent status as defined by the Debt Collection Improvement act, then the borrower is ineligible for an FHA-insured mortgage until the borrower resolves the debt with the creditor agency.

Smartfi may not find a borrower ineligible solely based on CAIVRs information that we have not verified. If resolved either by determining that the information in CAIVRs is no longer valid or by resolving the delinquent status as stated above, we may continue to process the application.

In order for a borrower with verified delinquent federal debt to become eligible, the borrower must resolve their federal non-tax debt in accordance with the Debt Collection Improvement Act.

The creditor agency that is owed the debt can verify that the debt has been resolved in accordance with the Debt Collection Improvement Act. Smartfi must include documentation from the creditor agency to support the verification and resolution of the debt. For debt reported through CAIVRs, when possible, we may obtain evidence of resolution by obtaining a clear CAIVRs report.

DELINQUENT FEDERAL TAX DEBT

Borrowers with delinquent federal tax debt are ineligible until the debt has been resolved with the creditor agency.

Tax liens may remain unpaid if:

- The borrower has entered into a valid repayment agreement with the lien holder to make regular payments on the debt; and
- The borrower has made timely payments for at least 3 months of scheduled payments. The borrower cannot prepay scheduled payments in order to meet the required minimum of 3 months of payments.

Smartfi is required to:

- Include the payment amount in the expenses when calculating residual income,
- Check public records and credit information to verify that the borrower(s) are not presently delinquent on any Federal Debt and does not have a tax lien placed against their property for a debt owed to the federal government.
- Include documentation from the Internal Revenue Service (IRS) evidencing the repayment agreement and verification of payments made, if applicable.

Note: Federal tax liens may be paid at closing as a mandatory obligation with valid payoff.

STATE TAX LIENS

Smartfi must check public records and credit information to verify that the borrower is not presently delinquent on any State Debt and does not have a tax lien placed against their property for a debt owed to the state government.

State tax liens assessed to the borrower that are not shown on the preliminary title report are not considered mandatory obligations and proof of satisfaction is not required. All state liens showing on the preliminary title report must be resolved in one of the following ways:

- Document the debt has been satisfied.
- Lien will be paid in full using HECM proceeds.

DELINQUENT MORTGAGE PAYMENTS

If the borrowers are currently delinquent on an FHA-insured mortgage on their principal residence, and the HECM will pay off the delinquent mortgage, the borrower may be eligible provided they meet all other HECM requirements.

However, in all cases where there is a delinquent mortgage on the principal residence, whether FHA-insured or not, Smartfi must evaluate the circumstances leading to the delinquency, and determine whether the HECM pay-off represents a sustainable solution to the issues that caused the delinquency.

If borrowers are currently delinquent on other FHA-insured mortgages associated with investment properties, they are ineligible for a new FHA-insured mortgage unless the delinquency is resolved.

DEED-IN-LIEU/FORECLOSURE / SHORT SALE ON GOVERNMENT-INSURED LOAN IN THE LAST 3 YEARS.

A borrower whose previous principal residence or other real property was foreclosed on, had a short sale completed or was given a deed-in-lieu of foreclosure **within the three years** prior to the closing date of the new loan is **not eligible** for a new FHA-insured mortgage **if the loan was government insured (FHA, VA, or USDA).**

> **Note: The minimum 3-year period for government loans starts on the date the claim was paid and ends on the closing date of the new loan.**

Foreclosure / Short Sale on a Conventional Loan in the last 3 years

If the foreclosure/deed-in-lieu/short sale was on a **conventional loan**, there is no waiting period before a new application can be taken. If the borrower wishes to proceed **without a LESA** and the date of the foreclosure/deed-in-lieu/short sale is within three years of the date of the credit report, the borrower will need to provide acceptable* extenuating circumstances as well as supporting documentation.

Acceptable extenuating circumstances must be one of the following:

- Death of a primary wage earner
- Serious long-term un-insured medical illness
- Divorce –*NOT* considered an extenuating circumstance. An exception may be granted where a borrower's loan was current at the time of his/her divorce, the ex-spouse received the property, and the loan was later foreclosed.

> **Note: The inability to sell a property due to a job transfer or relocation to another area does NOT qualify as an extenuating circumstance.**

Supporting documentation is required for the above extenuating circumstances and must show dates of occurrences coinciding with foreclosure dates. If the borrower will close with a LESA or the date of the delinquency is outside of three years from the date of the credit report, the borrower will only need to provide a detailed LOE regarding the extenuating circumstances that led to the delinquency. Approval is subject to underwriter discretion.

BANKRUPTCY CHAPTER 7, 11 AND 13

The following guidelines apply to HECM refinance ONLY. See HECM for Purchase section for more information regarding Bankruptcy.

Chapter 7 & 11

There are no mandatory waiting periods after a bankruptcy discharge nor are their specific repayment history eligibility requirements for borrowers applying for traditional or refinance HECMs. Inherently, bankruptcy does not demonstrate the willingness or capacity to manage debt. Smartfi must evaluate the following if bankruptcy has occurred within 2 years of the application date.

- The borrower’s credit history before and after the bankruptcy. There should be no late payments, collections or charge-offs after the bankruptcy discharge dated.
- The number of re-established tradelines after the bankruptcy and each account balance in proportion to the credit limit.
- Borrowers written letter of explanation as to what led up to the bankruptcy.
- Supporting documentation for any extenuating circumstances.

If the bankruptcy was discharged more than two (2) years from the application date the borrower must have exhibited a documented ability to manage their financial affairs in a responsible manner.

Chapter 13

If the Chapter 13 bankruptcy is going to remain open and under repayment at the close of the loan, the following must be met:

- Receive a complete copy of the bankruptcy documents.
- Smartfi must determine that the borrower’s payment performance in the Chapter 13 bankruptcy has been satisfactory, and all required payments have been made on time;
- The borrower has received written permission from the bankruptcy court to enter into the reverse mortgage transaction.
- Smartfi will need to thoroughly review the approval from the Courts to ensure that no verbiage has been included requiring the payoff of the Chapter 13. If the written approval reflects any specific reverse mortgage terms.
- The monthly payment must be included in the expenses for Residual income determination, and

Note: Chapter 13 may not be paid off using HECM proceeds, except delinquent federal debts or existing liens on the subject property.

Property Charge Payment History Analysis

Smartfi must determine if the borrower has demonstrated the willingness to timely meet his or her financial obligations by analyzing the borrower's property charge payment history.

Smartfi must pay particular attention to situations where late property charge payments are on the borrower's record. Absent documented Extenuation Circumstances, such circumstances must be viewed as especially significant events that call into question the ability of the borrower to manage his or her financial obligations.

Property charges include:

- All property taxes – school, city, county, state, etc.
- Where a taxing authority has permanently waived or otherwise permanently exempted the borrower from payment of property taxes, i.e., taxes are not due and payable and do not accrue or result in a lien against the property, such taxed may be excluded from the financial assessment. Documentation for the waiver or exemption must be placed in the case binder.
- Where a taxing authority has deferred the payment of property taxes, i.e., liability for taxes remains, but payment is deferred until a certain point in the future, such taxes may be excluded from the financial assessment provided:
  - That the deferral period will be in place until the death of the borrower or the sale of the property, whichever occurs first;
  - That a lien senior to the HECM first and second mortgages will not be created upon the termination of the deferral period; AND
  - Documentation on the deferral is placed in the case binder.

  Note: The borrower shall not participate in a real estate tax deferral program or permit any liens to be recorded against the property.

- Homeowners/hazard insurance and flood insurance;
- Homeowners' association (HOA), condominium or planned unit development (PUD) fees:
- Ground rents; and
- Other assessments levied by municipalities or under State law.

Smartfi may consider the borrower to have a satisfactory property charge payment history were, at the time of loan application:

- All property charges (for all retained properties) are current and there are no property tax arrearages in the prior 24 months.
- HOA, condominium, or PUD fees (for all properties owned) are current and there were no arrearages in the prior 24 months.

Note: Documentation will be required to determine the payment of property charges for all properties owned in accordance with the above.

If the taxes and insurance is/are/were escrowed by the current lender for minimum the last 24 months as evidenced by a recent mortgage statement or escrow account analysis, then further payment history documentation is not required.

If the subject property was owned for less than 24 months, the prior residence must also be verified to complete a 24-month history.

Smartfi must verify if hazard insurance has been in place for the past 12 months. No payment history on hazard insurance is required.

Note: If hazard insurance has not been in place for the past 12 months a full year premium must be paid at closing.

Note: When borrower has forced placed Homeowners insurance, a LESA will be applied.

Smartfi must determine and document the reason for any late payments, i.e., disregard for financial obligations, an inability to manage debt, or if there were extenuating circumstances.

Where the borrower has not demonstrated the willingness to meet his or her financial obligations as stated above and no Extenuating Circumstance can be documented, Smartfi must, at a minimum, require a Fully Funded LESA.

Property Charges as a Percentage of Gross Income

HUD has identified situations where property charges exceed 10% of the borrower's gross income as carrying greater levels of risk of default. This does not require an automatic LESA, something to be aware of when reviewing the overall risk of the file.

EXPENSES ANALYSIS

Monthly Expense Analysis refers to the analysis of the borrower's monthly expenses required to calculate Residual Income.

Using the credit report, 1009, Part VI of URLA or equivalent, most recent Federal and state income tax returns, and other documents that may be available to the underwriter (e.g., bank statements) Smartfi **MUST** identify all secured and unsecured debts. Smartfi **MUST** calculate:

- Federal and State Income Taxes;
- FICA;
- Property charges for the subject property;
- Estimated utility and maintenance expenses.
- Installment account payments;
- Any other owned property mortgage obligations (debt and property charges);
- Revolving credit account payments;
- Alimony and child support payments;
- Judgments under payment plans against the borrower;
- Payments required under any bankruptcy plans; AND
- Other obligations described in this guide.

Where the borrower benefits from Federal, state, or local benefit programs that reduce borrower expenses, the reduced amounts may be used to calculate expenses provided that Smartfi complies with the requirements of Government Assistance Non-Cash Benefits.

FICA TAX

The **Federal Insurance Contributions Act (FICA)** is the federal law that requires you to withhold two separate taxes from **the wages** you earn.

FICA tax is **NOT** paid on Social Security Retirement Income, Pension Income, Annuity Income, 401k, or IRA distribution income, etc.

LIENS PAID OFF USING HECM PROCEEDS

Where a lien against the property, such as a mortgage, is being paid off with HECM proceeds, the monthly payment associated with that lien is NOT included in the expense analysis.

GENERAL LIABILITIES AND DEBTS

Smartfi must determine the borrower's monthly liabilities by reviewing all debts listed on the credit report, Part VI or URLA or equivalent, tax returns, bank statements, and pay stubs. Smartfi must document the reasons for exclusion of any debt listed on these documents.

All applicable monthly liabilities must be included in the expense analysis. Closed-end debts do not have to be included if they will be paid off within 10 months and the cumulative payments of all such debts are less than or equal to 5% of the borrower's gross monthly income. The borrower **may not** pay down the balance in order to meet the 10-month requirement.

Accounts for which the borrower is an authorized user **MUST** be included in an expense analysis **UNLESS** Smartfi can document that the primary account holder has made all required payments for the previous 12 months. If less than three payments have been required on the account, the payment must be included in the expense analysis.

Negative income **MUST** be subtracted from the borrower's gross monthly income, and not treated as a recurring monthly liability unless otherwise noted.

Loans secured against deposited funds, where repayment may be obtained through extinguishing the asset and these funds are not including in calculating the borrower's assets, do not require consideration in the expense analysis.

UNDISCLOSED DEBTS AND INQUIRIES

When a debt or obligation is revealed during the application process that was not listed on the application and/or credit report, Smartfi must:

- Verify the actual monthly payment amount; AND
- Include the payment amount in the expense analysis.

Smartfi must obtain an explanation from the borrower for all inquiries shown on the credit report that were made in the last 90 days.

Smartfi must document all undisclosed debt and support its analysis of the borrower's debt.

FEDERAL DEBT

Federal debts refers to non-delinquent debt owed to the federal government for which regular payments are being made.

The amount of the required payment **MUST** be included in the expense analysis.

Smartfi must include documentation from the federal agency evidencing the repayment agreement and verification of payments made, if applicable.

ALIMONY, CHILD SUPPORT AND MAINTENANCE

Alimony, child support, and other maintenance are court-ordered or otherwise agreed upon payments.

For alimony, if the borrower's income was not reduced by the amount of the monthly alimony obligation in Smartfi calculation of the borrower's gross monthly income, Smartfi must verify and include the monthly obligation in its calculation of the borrower's debt.

Child support and other maintenance are to be treated as a recurring liability and Smartfi must include the monthly obligation in the expense analysis.

Smartfi must obtain the official signed divorce decree, separation agreement, maintenance agreement, or other legal order. Smartfi must also obtain the borrower's pay stubs covering no less than 28 consecutive days to verify whether the borrower is subject to any order of garnishment relating to alimony, child support, or other maintenance.

Smartfi must calculate the borrower's monthly obligation from the **GREATER** of:

- The amount shown on the most recent decree or agreement establishing the borrower's payment obligation; OR
- The monthly amount of the garnishment.

DEFERRED OBLIGATIONS (EXCLUDING STUDENT LOANS)

Refers to liabilities that have been incurred, but where payment is deferred or has not yet commenced, including accounts in forbearance. We must verify and include deferred obligations in the expense analysis. If the actual monthly payment is not available for installment debt, we must utilize the terms of the debt OR 5% of the outstanding balance to establish the monthly payment.

Smartfi must obtain written documentation of the deferral of the liability from the creditor **AND** evidence of the outstanding balance and terms of the deferred liability. Smartfi must obtain evidence of the anticipated monthly payment obligation, if available.

Note: If the credit report reflects the account to be deferred or forbearance status then obtaining documentation from the creditor for same is not required.

INSTALLMENT LOANS

Installment loans (excluding student loans) refer to loans, not secured by real estate, that require the periodic payment of principal and interest. A loan secured by an interest in a timeshare must be considered an installment loan.

Smartfi must include the monthly payment shown on the credit report, loan agreement, or payment statement in the expense analysis.

If the payment shown on the credit report is used to calculate the monthly debts, no further documentation is required.

If the credit report does not include a payment for the loan, or the payment reported on the credit report is greater than the payment on the loan agreement or statement, Smartfi must obtain a copy of the loan agreement or statement to document the amount of the payment.

STUDENT LOANS

Student loan refers to liabilities incurred for educational purposes. Smartfi must include all student loans in the expense analysis, regardless of the payment type or if payments are deferred or in forbearance.

If the payment used in the expense analysis is less than the payment reported on the borrower(s) credit report, then written documentation of the actual monthly payment, the payment status, and evidence of the outstanding balance and the terms from the creditor or student loan servicer are required.

For outstanding student loans, regardless of payment status Smartfi must use:

- The payment amount reported on the credit report or the actual documented payment, when the payment amount is above zero; OR
- 0.50% of the outstanding loan balance, when the payment reported on the borrower's credit report is zero.

Smartfi may exclude the payment amount from the monthly debt calculation where written documentation from the student loan program, creditor, or student loan servicer indicates that the loan balance has been forgiven, canceled, discharged, or otherwise paid in full.

Note: Where a student loan payment has been suspended in accordance with COVID-19 emergency relief, we may use the payment amount reported on the credit report or the actual documented payment prior to suspension, when that payment amount is above $0.

REVOLVING CHARGE ACCOUNTS

Revolving charge accounts refers to a credit arrangement that requires the borrower to make periodic payments but does not require the full repayment by a specified point of time.

Smartfi must include in the expense analysis the payment shown on the credit report for each revolving account with a balance. Where the credit report does not include a payment, Smartfi must use the payment shown on the current account statement or 5% of the outstanding balance.

Smartfi must use the credit report to document the terms, balance and payment amount on the account, if available.

30 DAY ACCOUNTS

30-day accounts refer to a credit arrangement that requires the borrower to pay the outstanding balance on the account every month.

Smartfi must verify the borrower pays the outstanding balance in full on every 30-day account each month for the past 12 months. 30-day accounts that are paid monthly **are not** included in the expense analysis. If the credit report reflects any late payments in the last 12 months, Smartfi must utilize 5% of the outstanding balance as the borrower's monthly debt to be included in the expense analysis.

Smartfi must use the credit report to document that the borrower has paid the balance on the account monthly for the previous 12 months. Smartfi must use the credit report to document the balance and must document sufficient funds are available to pay off the balance.

BUSINESS DEBT IN BORROWER'S NAME

Business debt in the borrower's name refers to liabilities reported on the borrower's personal credit report, but payment for the debt is attributed to the borrower's business.

When business debt is report on the borrower's personal credit report, the debt **MUST** be included in the expense analysis, **UNLESS** Smartfi can document that the debt is being paid by the borrower's business, **AND** the debt was considered in the cash-flow analysis of the borrower's business.

When a self-employed borrower states that debt appearing on their personal credit report is being paid by their business, Smartfi **MUST** obtain documentation that the debt is paid out of company funds **AND** that the debt was considered in the cash-flow analysis of the borrower's business. The debt is considered in the cash flow analysis where the borrower's business tax returns reflect a business expense related to the obligation, equal to or greater than the amount of payment documented as paid out of company funds. Where the borrower's business tax returns show an interest expense related to the obligation, only the interest portion of the debt is considered in the cash flow analysis.

DISPUTED DEROGATORY ACCOUNTS

Disputed derogatory credit accounts refer to disputed charge off accounts, disputed collection accounts, and disputed accounts with late payments in the last 24 months.

If the borrower has $1,000 or more collectively in disputed derogatory credit accounts, Smartfi **MUST** include a monthly payment in the expense analysis.

The following items are excluded from the expense analysis & will not be counted toward the $1,000 limit:

- Disputed medical accounts; AND
- Disputed derogatory credit resulting from identity theft, credit card theft or unauthorized use.

Non-derogatory disputed account and Disputed Accounts Not Indicated on the

Credit Report

Non-derogatory disputed accounts include the following types of accounts:

- Disputed accounts with zero balance,
- Disputed accounts with late payments aged 24 months or greater,
- Disputed accounts that are current and paid as agreed.

If a borrower is disputing non-derogatory accounts or is disputing accounts which are not indicated on the credit report as being disputed, Smartfi must analyze the effect of the disputed accounts in the expense analysis.

CONTINGENT LIABILITIES

Contingent liability is a liability that may result in the obligation to repay only where a specific event occurs. For example, contingent liability exists when an individual can be held responsible for the repayment of a debt if another party defaults on the payment. Contingent liabilities may include cosigner liabilities and liabilities resulting from a mortgage assumption without a release of liability.

Smartfi must include monthly payments on contingent liabilities in the expense analysis **UNLESS** Smartfi verifies that there is no possibility that the debt holder will pursue debt collection against the borrower should the other party default, **OR** the other party has made 12 months of timely payments.

MORTGAGE ASSUMPTIONS

Smartfi must obtain the agreement creating the contingent liability or assumption agreement **AND** deed showing transfer or title out of the borrower's name.

COSIGNED LIABILITIES

If the cosigned liability is not included in the monthly obligations, Smartfi must obtain documentation to evidence that the other party to the debt has been making regular on-time payments during the previous 12 months AND does not have a history of delinquent payments on the loan.

COURT ORDERED DIVORCE DECREE

Smartfi must obtain a copy of the divorce decree ordering the spouse to make payments.

COLLECTION ACCOUNTS

A collection account is a borrower's loan or debt that has been submitted to a collection agency by a creditor.

If the credit report used in the analysis show cumulative outstanding collection account balances of $2,000 or GREATER, Smartfi must:

- Verify that the debt is paid in full at time of or prior to settlement using an acceptable source of funds; OR
- Verify that the borrower has made payment arrangements with the creditor; OR
- If a payment arrangement is not available, calculate the monthly payment using 5% of the outstanding balance of each collection and include the payment in the expense analysis.

Smartfi **MUST** provide the following documentation:

- Evidence of payment in full, if paid prior to settlement;
- Payoff statement, if paid at settlement;
- Payment arrangement with creditor, if not paid prior to or at settlement

If Smartfi uses 5% of the outstanding balance as the monthly payment no documentation is required.

Medical Collections do NOT need to be included in the expense analysis.

CHARGE OFF ACCOUNTS

A charge off account refers to a borrower's loan or debt that has been written off by the creditor.

Charge off accounts **DO NOT** need to be included in the expense analysis.

PRIVATE SAVINGS CLUB

Private Savings Clubs refers to non-traditional methods of saving by making deposits into a member-managed resource pool.

IF the borrower is obligated to continue making ongoing contributions under the pooled savings agreement, this obligation **MUST** be included in the expenses analysis.

Smartfi **MUST** verify AND document the establishment and duration of the borrower's membership in the club **AND** the amount of the borrower's required contribution to the club.

Smartfi must also obtain the club's account ledgers and receipts, and verification from the club treasurer that the club is still active.

FEDERAL AND STATE INCOME TAXES

Smartfi must use current pay stubs, tax tables, or federal, state, and local tax returns from the most recent tax year, to document federal, state and local taxes.

MAINTENANCE AND UTILITY CHARGES

Smartfi will use the square footage from page 1 of the appraisal report under square feet of gross living area above grade to calculate the monthly charges to be included in the expenses. i.e., 1250 sq. feet x .14 =$175.00.

SELF-REPORTED UTILITIES

A borrower can elect to have utility payments (electric, telephone, cable/internet, etc.) reported on his/her credit report to increase his/her credit score based on timely payment of these expenses. The above maintenance and utility charges account for the utility payments due on the subject property therefore any self-reported utilities do not need to be included in the monthly expense analysis.

DOCUMENTATION STANDARDS FOR PROPERTY CHARGES

Smartfi must verify and document the amount of property charges in accordance with the following requirements:

- **Property taxes**: **MUST** document the amount of property taxes due from all taxing authorities through written statements or on-line printouts from the taxing authorities, or through copies of bills. If the current year's property taxes are not available, Smartfi shall calculate monthly expenses based on 1.04 percent of the prior year's tax bill.

> **Note: Where property taxes are deferred or waived, the amount of property taxes may be excluded from monthly expenses.**

- **Homeowners/hazard insurance**: **MUST** obtain the current year's declaration sheet for the policy that reflects the annual premium. Where the homeowners hazard policy was previously in place, Smartfi shall base the cost upon the quote provided to the borrower.

> **Note: If the current year's declaration sheet is not available, Smartfi shall calculate monthly expenses based on 1.04 percent of the prior year's premium.**

- **Flood Insurance**: **MUST** obtain the current year's declaration sheet for the policy that reflects the annual premium. Where no flood policy was previously in place Smartfi shall base the cost upon the quote provided to the borrower.
- **HOA, PUD, & Condo Fees**: **MUST** obtain from the appraisal or from a written statement from the association or its management agent, documentation on the amount of monthly fees.
- **Other Assessments**: **MUST** obtain from the party levying the assessment or its management agent a written statement documenting the amount of any other assessments.
- **Ground Rent**: **MUST** obtain from the deed, the lessor, or its management agent a written statement documenting the amount of the ground rent payment.

EXPENSE ANALYSIS FOR ELIGIBLE NON-BORROWING SPOUSES

Smartfi must analyze an Eligible NBS's obligations from the sources specified in **Expense Analysis IF** an Eligible NBS's income is used as a compensating factor **or** to reduce family size.

The Eligible NBS expenses **MUST** meet the same documentation and verification standards as required for the borrower's expenses.

EXPENSE ANALYSIS FOR OTHER NON-BORROWING HOUSEHOLD MEMBERS

Smartfi must analyze an Other Non-Borrowing Household Member's obligations from the sources specified in **Expense Analysis IF** an Other Non-Borrowing Household Member's income is to be used to reduce family size.

The Other Non-Borrowing Household Member's expenses **MUST** meet the same documentation and verification standards as required for the borrower's expenses.

OTHER OBLIGATIONS NOT CONSIDERED DEBT:

- Medical collections;
- Automatic deductions from savings, when not associated with another type of obligation;
- Retirement contributions, such as 401K accounts or 401K loans;
- Collateralized loans secured by depository accounts;
- Child care;
- Commuting costs;
- Union dues;
- Insurance, other than property insurance;
- Open accounts with zero balance; and
- Voluntary deductions, when not associated with another type of obligation.

Property Taxes as a Percentage of Gross Income: FHA has identified situations where property taxes exceed 10% of the borrower's gross income as carrying a greater level of risk of default. Smartfi must calculate property taxes as a percentage of gross income and enter this figure on the FA Worksheet.

PROPERTY CHARGE FUNDING REQUIREMENTS

LIFE EXPECTANCY SET-ASIDE (LESA)

A LESA is an amount withheld from the borrower's proceeds for the payment of property charges during the file of the borrower. The need for a LESA, the funding amount of the LESA, and the structure of the LESA, are based on the results of the Financial Assessment of the borrower.

Where Smartfi determines that the borrower has demonstrated the willingness and the capacity to meet his or her property charge obligations, a Life Expectancy Set-Aside is NOT required.

When the borrower has not demonstrated the willingness and/or capacity to meet his or her property charge obligations, a Life Expectancy Set-Aside is required.

Note: If Smartfi does not require a LESA, a borrower may elect to have a fully-funded LESA.

PROJECTED LIFE EXPECTANCY PROPERTY CHARGES

To determine the funding amount of a Life Expectancy Set-Aside, Smartfi must first calculate the Projected Life Expectancy Property Charge Cost. The formula for calculating the Projected Life Expectancy Property Charge Cost includes:

- the projected sum of:
- Current property taxes;
- Homeowners insurance premiums; and
- Flood insurance premiums.
- A factor to reflect increases in tax and insurance rates;
- The HECM expected average mortgage interest rate; AND
- The life expectancy of the youngest borrower.

LIFE EXPECTANCY PROPERTY CHARGE COST FORMULA

Projected Life Expectancy Property Charge Cost =

$$(1.2 \times PC / 12) \times \{(1 + c)\ m+1 - (1+c)\} / \{c \times (1+c)m\}$$

PC (property charges) / 12 is the current total monthly property charge for property taxes, homeowners' insurance and flood insurance.

m is the TALC life expectancy in years of the youngest borrower x 12 (e.g., for a 75-year-old borrower, TALC life expectancy is 12 years x 12 months = 144).

c is the monthly compounding rate which is defined as the expected rate plus the annual MIP rate / 12.

The **PC / 12** is multiplied by 1.2 to take into account expected increases in property taxes and hazard and flood insurance over the life expectancy of the youngest borrower.

Note: The Fully Funded LESA will use HECM proceeds to pay property taxes and insurance premiums on behalf of the borrower. The borrower remains responsible for all other property charges (e.g., HOA, PUD, or Condo Fee, Other Assessments, Ground Rent, etc.).

LIFE EXPECTANCY SET-ASIDE- PARTIALLY FUNDED

Where Smartfi determines, based on the results of the FA that the borrower has demonstrated the willingness to meet his or her financial obligations, but has not demonstrated the capacity to do so, the Life Expectancy Set-Aside **MUST** be partially funded.

Through the Partially Funded Life Expectancy Set-Aside the borrower will receive semi-annual payments from HECM proceeds to be used to pay property taxes and insurance premiums. The borrower remains responsible for timely payment of all property charges.

FORMULA FOR CALCULATING PARTIALLY FUNDED LIFE EXPECTANCY SET-ASIDE

(1.2 x MRIS) x {(1+c)m+1 – (1+c)} / {cx (1+c)m}

MRIS (**M**onthly **R**esidual **I**ncome **S**hortfall) is the residual income gap – the difference between the borrower's monthly residual income, and the applicable amount of residual income for the borrower's geographic region and family size, based on the Table of Residual Income.

m is the TALC life expectancy in years of the youngest borrower x 12 (e.g., for a 75-year-old borrower, TALC life expectancy is 12 years x 12 months = 144)

c is the monthly compounding rate which is defined as the expected rate plus the annual MIP rate / 12

The **MRIS** is multiplied by 1.2 to take into account expected increases in property taxes and hazard and flood insurance over the life expectancy of the youngest borrower.

Additional Requirement for Use of Partially Funded Life Expectancy Set-Aside

Where the projected Partially Funded Life Expectancy Set-Aside is greater than 75% of the Projected Life Expectancy Property Charge Cost, the borrower is NOT eligible for a Partially Funded Life Expectancy Set-Aside. Smartfi must require as a condition of mortgage approval a Fully Funded Life Expectancy Set-Aside.

Life Expectancy Table

The figure used for life expectancy is taken from the U.S. Decennial Life Tables for 1979-1981 Females found at Title 12, Appendix L. The life expectancy figures to be used are provided in Appendix 2 in the fourth column title Loan Period 2 (life expectancy) (in years). Smartfi must select the age of the youngest borrower (rounded to nearest whole year) **AND** use the corresponding life expectancy figure found in the fourth column of the table for the borrower's life expectancy.

Note: A partial LESA is only permitted on ARM products.

When a LESA is required on a HECM Purchase Smartfi must use 1.25% of the purchase price for the property taxes unless title is able to confirm the first year of property taxes.

EXTENUATING CIRCUMSTANCES AND COMPENSATING FACTORS

Where the borrower's credit and/or property charge payment history does not meet the criteria described in these sections, Smartfi must consider any Extenuating Circumstances that led to the credit or property charge issues.

Extenuating Circumstances beyond the borrower's control may include, but are not limited to:

- Loss of income due to death or divorce of a spouse that directly resulted in late payment of obligations;
- Loss of income due to the borrowers or spouse unemployment, reduced work hours or furloughs, or emergency medical treatment or hospitalizations that directly resulted in late payments of obligations; or
- Increase in financial obligations due to emergency medical treatment or hospitalization for the borrower or spouse, emergency property repairs not covered by homeowners or flood insurance, divorce, or other causes that directly resulted in late payments of obligations.

Smartfi must document the presence of any Extenuating Circumstances as part of the financial assessment. Documentation of Extenuating Circumstances must demonstrate:

- The connection between the specific occurrences and the measurable impact of the occurrences on the borrowers finances;
- That no other actions, not directly or indirectly related to the financial problem, were taken the borrower that contributed to the derogatory incident (e.g., assuming new financial obligations, voluntarily terminating employment or reducing hours, etc.);
- The likelihood that these circumstances will not recur. In assessing the likelihood that the circumstances will not recur, Smartfi may consider the impact of the HECM on the borrowers' circumstances, through the elimination of financial obligations and/or through an increase in borrowers' income; and
- That the borrower demonstrated financial liquidity through non-HECM assets, additional sources of income, access to revolving credit or other factors that enhance his or her ability to endure financial challenges.

For example, if a borrower cited loss of income due to unemployment as the cause of late payments, the documentation should show include the following:

- The credit report indicates that the borrower had satisfactory credit prior to being unemployed;
- The borrower's documented income, including any unemployment compensation received, was insufficient to make timely payments on all outstanding accounts;
- The credit report indicates that the borrower did not incur new debt that contributed to the borrower's inability to meet all obligations in a timely manner; **AND**

- The borrower is employed again and/or has alternate sources of income.

Note: Possible documentation required may include, but is not limited to: Letter of Explanations, paid invoices, credit report, Doctors letters, death certificates, employment related items/documents, corresponding tax return, attorney, or CPA letters. Bankruptcy and/or debt consolidation is not considered a valid extenuating circumstances to avoid a LESA.

When evaluating an extenuating circumstance exists, underwriting ask:

- Is the derogatory event an isolated incident?
- Was the derogatory event caused by something outside the borrower's control.

Compensating Factors-Residual Income Shortfall

Where the borrower's residual income does not meet the applicable standard in the Cashflow Analysis section, Smartfi may consider Compensating Factors.

Compensating Factors-Other sources of income

Income from the sources described below may be cited as a CF where the borrower's residual income, combined with documented income from 1 or more of these sources, **equals or exceeds** the residual income required for the borrower(s) family size & geographic region, **and** we can document that the specific criteria for the individual CF has been met.

- Eligible Non-Borrower Spouse Income- Documented residual income from an Eligible NBS;
- Overtime, Seasonal, part-time or Bonus income- Borrowers have documented overtime bonus, part-time or season income that the borrower has received for at least 6 months, and it will likely continue; (normal income documentation required including VOE)
- Expected Social Security or Pension Income-Borrower has received an Award letter stating that the borrower will begin receiving Pension or Social Security income within the next 12 months from loan closing. The award letter must confirm the exact monthly income and start date; or
- Imputed Income from HECM- An increase in monthly income would result from dissipating available HECM proceeds remaining AFTER Closing (based on original principal limit less required Repair, Life Expectancy & Servicing Set-Asides & disbursements for mandatory obligations).

Note: Smartfi will allow imputed income from dissipation of HECM proceeds as a sole source of income to meet residual income requirements when:

No other compensating factors are being used, when borrower has zero income; and,

Borrower(s) pass the Financial Assessment for credit and property chargers without using Extenuation circumstances.

Compensating Factors- Other Resources

The following CF may be cited where a borrower's **baseline residual income is 80-99%** of the applicable amount for his or her family size and geographic region on the Table of Residual Income in Section…. And Smartfi can document that the specific criteria described for the individual CF has been met.

- **Property Charge Payment History -**borrowers meet all the following:
    - Borrower have paid their own property charges directly for at least the last 24 months (i.e., they were NOT paid by a lender from an escrow account or by another party)
    - Borrower have made all property charge payments without incurring penalties during the last 24 months; AND
    - Borrower current income is not less than income during the previous 24 months.
- **Assets equal to life expectancy property charges** – Borrower(s) have assets (excluding HECM Proceeds) equivalent to the anticipated property charge payments for the life expectancy of the borrower(s) that were not dissipated or considered in the residual income calculation;
- **HECM sufficient to pay off debts** – HECM proceeds remaining after closing that were not dissipated and counted as income, are sufficient to pay off revolving & installment debt, including revolving and installment accounts in collection status, that would reduce monthly payments to the extent that the residual income would meet or exceed the applicable standard for the borrower(s) family size & geographic region.
- **Access to other credit** – Borrower(s) have access to revolving credit that provides the borrower(s) with financial liquidity that would enhance his/her ability to endure a financial hardship. The credit report shows established credit lines, other than his or her housing payment, in the borrower(s) name, open for at least 6 months; and we can document that these accounts have been paid off in full monthly for at least the past 6 months.

Note: Borrowers who do not have any established credit other than their housing payment, not other credit lines in their own name open for at least 6 months, or who cannot document that all other accounts are paid off in full monthly for at least 6 months, do not qualify under this criterion. Borrowers with credit lines in which they are authorized users do not qualify under this criterion.

If after applying the above CF, the borrower does not meet or exceed 100% of the required residual income, a LESA must be applied.

When a Fully Funded LESA is required Smartfi may consider what the borrowers monthly residual income is after monthly taxes, homeowners & flood insurance, as applicable, are hypothetically removed from the monthly expenses.

Smartfi must document any Extenuating Circumstances to address derogatory credit and/or property charge payment history, and/or Compensating Factors to support residual income shortfalls.

Smartfi must identify in writing on the Financial Assessment Worksheet all specific circumstances and factors it relied upon to make its favorable determination. Supporting documentation must be included in the origination case binder.

PRELIMINARY TITLE COMMITMENT

A title commitment (preliminary title report) and 24-month chain of title/deed history is required for every loan. The title policy must be written on the 2006 ALTA Standard form or the ALTA Short form.

The title policy must be written on the 2006 ALTA Standard form or the ALTA Short form. All title commitments must include:

- All liens of record
- Full legal description
- Property address
- The proposed coverage amount (must be the maximum claim amount)
- A 24-month chain of title

Date of Commitment

The commitment/effective date must not be older than 120 days at the time of closing.

Note: State of Texas the commitment/effective date cannot be more than 90 days old at time of closing.

PROPOSED INSURED

Smartfi Home Loans, LLC, ISAOA

In the state of **Texas**, the title company may not include ISAOA, they must include the Texas verbiage.

TITLE COVERAGE AMOUNT

Minimum amount of Title coverage required is the Maximum Claim Amount. The Maximum Claim Amount is the LESSER of appraised value, purchase price, or HECM lending limit.

VESTING

A mortgagor is not required to be a borrower; however, any borrower is required to be on title.

Mortgagor shall hold title to the entire property which is the security for the mortgage. If there are multiple mortgagors, all the mortgagors must collectively hold title.

If one or more mortgagors hold a life estate in the property, for purposes of this section only, the term "mortgagor" shall include each holder of a future interest in the property (remainder or reversion) who has executed the mortgage.

If Non-Borrowing Spouses and Non-Borrowing owners of the property will continue to hold title to the property which serves as collateral for the HECM, such Non-Borrowing Spouses and Non-Borrowing Owners must sign the mortgage as mortgagors, evidencing their commitment of the property as security for the mortgage.

Minnesota

Only the HECM borrower(s) may have a vested ownership interest in the subject property after loan closing.

DEATH CERTIFICATE

A death certificate is required when a deceased person is being removed from title. This includes any person named in a Trust.

An Affidavit of Death may also be required based on state requirements as determined by the Title company. The title company or settlement agent must state in writing that the deceased party can be removed from title at closing without Probate being completed.

LEGAL DESCRIPTION

The legal description must match the most recent recorded Deed and the appraisal report.

OUTSTANDING MORTGAGES, LIENS & JUDGMENTS:

- All liens on title must be paid off.
- All taxes coming due within 60 days of closing must be paid in full.
- Any delinquent taxes must be brought current at closing.
- Deferral programs are not allowed, and borrowers must terminate any such program.

SUBORDINATE LIENS

There shall be no outstanding or unpaid obligations, either unsecured or secured, arising from, or incurred in connection with the HECM transaction. This includes any outstanding or unpaid obligations on the subject property. In all cases the borrower may not borrow funds from any source in order to close on a HECM.

All first mortgage liens, secured or unsecured, must be satisfied prior to or at the time of closing. All existing second liens as evidence by title and credit may be re-subordinated to third lien position behind the first and second HECM liens.

A satisfactory subordination agreement from the existing second lender/lien holder is required. The subordination agreement must reflect the full amount of the existing second lien, account for the maximum mortgage amount of 150% of the Max Claim Amount, must not place any restrictions on the reverse mortgage lender, HUD or terms of the HECM, must reflect the lien will be in third lien position for HECM adjustable Rate and second lien position for HECM Fixed Rate.

24 MONTH CHAIN OF TITLE

Recent vesting and/or ownership changes may require explanation and occupancy documentation. HECM for purchase loans do not allow transfers of the subject property in the 90 days prior to the date of the purchase contract.

Oklahoma Title

Oklahoma is an abstract state where title companies require the borrowers to obtain their title abstract and arrange for an attorney to review it before the title company provides a Title Commitment. Some title companies may provide a "Title Report" in lieu of the Title Commitment. However, this **does not** provide the same lender coverage as a title insurance policy. Smartfi requires a Title Commitment in each Oklahoma loan file prior to closing.

OIL AND MINERAL RIGHTS

Smartfi may allow outstanding oil, water or mineral rights, or damage caused by the exercise of such rights. Damage is typically covered under the actual recorded oil or mineral lease, or else the title company insures against it. (Any noticeable damage will be required to be repaired) (No visible drilling may be apparent).

Smartfi may allow oil and mineral leases if they are common for the area and are customarily waived by prudent leading institutions and leading attorneys within the community without causing the property to be uninsurable by FHA.

UNDIVIDED INTEREST

Shared lots with undivided interest, i.e., properties with legal descriptions that read "an undivided 1/2 (or 1/3,) interest in and to lot..........." are NOT eligible for mortgage insurance. If requested to complete an appraisal on a property with this kind of legal description, the appraiser should REJECT the property as the lot is not considered a Fee Simple entity. The lender should be notified of this rejection as soon as it is determined by the appraiser. Condos are exempt from this rule, and they will typically show an undivided interest in their legal description. PUDs may show an undivided interest, but this is only acceptable if it applies to the common area, not the lot on which the property sits. If clarification of the legal description is needed to determine this, please reach out to the title company.

VESTED IN A BUSINESS/CORPORATION AT APPLICATION

For this type of vesting to be acceptable, the borrower must provide documented proof that they are 100% owner of the company. If acceptable, Smartfi will require the borrower to deed the property out of the business and transfer it to themselves as individuals at close. If borrower(s) are not 100% owner, the loan is not acceptable and will be denied.

TITLE SEASONING

There is no seasoning requirement other than at least one borrower must be on title at the time of application. For recent transfers into borrower’s name prior to application, occupancy documentation will be required.

HERO/PACE PROGRAM

- Properties that have participated in the PACE/HERO Program will have a tax assessment on title
- The assessment will be in the first lien position

- The assessment/lien must be paid at closing and CANNOT be subordinated
- Underwriter is required to verify any notice of assessment and/or notices on title to ensure they are not part of a PACE/HERO assessment

PACE/HERO assessments on title are required to be paid off at time of closing.

UCC REQUIREMENTS AND EXCEPTIONS

Any UCC filing or exception in title must be terminated. Final title policy may not have exceptions for leased equipment or power purchase agreements. Title must provide the termination.

SURVEYS

Smartfi requires survey coverage on all loans. In most states, the title company will automatically provide survey coverage without a survey. Typically, borrowers in Texas, Florida, and New Mexico will need additional documentation to ensure that the survey coverage is extended and acceptable.

TEXAS:

Title will be required to confirm on a supplement or directly on the title commitment that they have reviewed the survey and that they will issue the T-19 endorsement without any survey related exceptions. The only exception that is acceptable is if the prelim shows an exception due to "shortages in area."

FL, NM, AND OH:

Fully Executed Survey affidavit will be required at closing.

LIFE ESTATES

Property held in a life estate is eligible for an FHA reverse mortgage.

A life estate is an interest in real property allowing the owner of the life estate to use the property during his or her lifetime.

On the death of the owner of the life estate, his or her rights in the property cease, leaving a fee simple title to the property in the holders of the future interest in the property (Remaindermen).

The borrower and all holders of any future interest in the property must execute the deeds at closing.

Holders of future interest will need to execute the following at closing: Deed of Trust & any riders, Rescission & Truth in Lending.

Holders of future interest do not execute the note or loan agreement.

Remaindermen must attend counseling.

Smartfi must obtain a copy of the document granting the borrower a life estate.

Note: The party or parties holding the remainder or reversionary interest must be an individual and may not be a trust or LLC.

SOLAR LEASES/ SOLAR SYSTEMS

A solar lease is an energy system the borrower does not fully own. It is part of the subject property but is not included in the subject property value.

Property requirements

A conventional heating system must be in place, the heating system cannot rely entirely on solar.

If leased, the solar electric system must not be given any value in the appraisal.

When a solar system enhances a conventional heating system, or is used for energy efficiency, we require one of the following:

- The borrower may own the solar electric system,
- If the borrower leases the system, he or she may buy the system at closing,
- If the borrower wants to continue the lease, the underwriter will review the file to ensure that it meets U.S. Department of Housing and Urban Development (HUD) Compliance guidelines.

Solar Notice of Contracts are acceptable to remain on title.

Solar Lease Requirements

In order to be eligible for a HECM, a home that operates with a leased energy system or PPA (power purchase agreement) must not have any restrictions that prevent the borrower from freely transferring the property. Solar leases are acceptable provided the conveyance (ownership transfer) of the insured property does not cause any of the following:

- The conveyance is voided, or voidable by a third party.
- The lease agreement is the basis of contractual liability of the borrower, including rights of first refusal, pre-emptive rights or options related to a borrowers' efforts to convey.

- For example, a right of first refusal requires the borrower to give the leasing agent the first right to purchase or refuse the property, which makes the property ineligible.
- The conveyance could result in termination of all or part of the borrower's interest in the property.
- The conveyance is subject to the consent of a third party.
- The conveyance is subject to limits on the number of sales proceeds a borrower can retain because of a lien or sales clause, and so forth.
- The lease agreement cannot be considered grounds for accelerating the insured mortgage.
- The lease agreement cannot be considered grounds for increasing the interest rate of the insured mortgage.

LEASEHOLD ESTATES

Leasehold interest refers to real estate where the residential improvements are located on land that is subject to a long-term lease agreement from the underlying fee simple owner, creating a divided estate in the property. Smartfi will accept leasehold interest properties so long as the leasehold agreement is reviewed and approved by our legal counsel. A copy of the leasehold agreement must be provided, and the requirements are as follows.

SFR or PUD properties only

- Lease must be renewable for not less than 99 years, or a lease with the actuarial life expectancy of the borrower.
- The value or replacement of the property shall be the value or replacement cost of the leasehold estate, which shall in all cases be less than the value of replacement cost of the property in fee simple.

Note: Sub-leasehold Estates are not eligible for FHA mortgage insurance.

TRUSTS

General Trust Guidelines

HUD will insure HECMs on properties held in the name of an inter vivo or "living" trust.

A living trust is created while grantors are alive rather than one created at/after death.

A trust agreement outlines the responsibilities of the trustee, who has a fiduciary responsibility to hold and manage the trust assets for the "beneficiary."

The trust holds legal title, while the beneficiary holds equitable title, which means he or she has the right to use the property or purchase it if the trust fails in some way to manage it properly.

Under the HECM program, all borrowers must be primary beneficiaries of the trust but not all primary beneficiaries must be borrowers if the non-borrowing primary beneficiaries could qualify for the HECM (be of age 62 or older and reside in the subject property).

The borrower(s) may or may not be Trustee(s) of the trust; however, if they are, they must sign the required documents as both Borrower and Trustee.

Note: We can close Texas properties in Revocable Trusts.

REVOCABLE TRUSTS

A revocable trust is one that:

- An individual created during his or her lifetime
- Becomes effective during its creator's lifetime
- Can be changed or cancelled by its creator at any time, for any reason, during that individual's lifetime.

Please see below for Trust Approval requirements.

Note: The revocability of some trusts may change on the death of one borrower.

IRREVOCABLE TRUSTS

An irrevocable trust cannot be changed or cancelled once it is set up without the consent of the beneficiary. An irrevocable trust is an arrangement in which the grantor permanently departs with the ownership and control of the property.

When the borrower is mentally incompetent, and property is vested in a trust:

- If the property is vested in a trust, the trust must also be carefully examined for any requirements in the determination of the borrower's mental incapacity. For example, the trust may require two doctors' letters where the power of attorney document does not, or the trust may require specific verbiage to be included in the letters. All requirements outlined in both the trust and the power of attorney must be met.
- If the borrower is the trustee and has been determined incapable of handing his/her financial affairs and all required documentation has been provided to prove this per the trust directive, the successor trustee will take on the role of trustee. This information must be provided to the title company so that an

affidavit of change of trustee can be completed and final vesting will reflect the successor trustee.
- The attorney in fact will sign all documents on behalf of the borrower as an individual and the successor trustee will sign on behalf of the trust.

LAND TRUSTS (ILLINOIS LAND TRUST)

A land trust provides a unique form of ownership of real property. In an Illinois land trust, the legal and equitable title lies with the trustee and the beneficiary retains what is referred to as a personal property interest.

The beneficiary has the exclusive power to direct or control the trustee in dealing with the title and the exclusive control of the management, operation, renting and selling of the trust property together with the exclusive rights to the proceeds from the property.

The only power the trustee has in relation to the land is the power to convey title. The trustee can only use this power when properly authorized by the beneficiary.

Land trusts require Smartfi attorney approval, written approval from title & the trustee is required to complete the trust acknowledgement.

If the trustee is listed as a company, the representative of that company who will be acting as trustee will be required to provide evidence that s/he is authorized to sign on behalf of the company.

TRUST APPROVAL REQUIREMENTS

Beneficiaries

The Borrowers must be the primary beneficiaries of the trust. They cannot be the residual, contingent, or alternate beneficiaries. For more information, consult your legal counsel.

Special legal opinions may be required for Illinois Land Trusts.

Trust Documents

The trustee is under fiduciary responsibility to hold and manage the trust assets for the beneficiary. The trustee’s responsibilities are set out in a trust agreement.

A complete copy of the “Declaration of Trust” or “Trust Agreement” must be submitted to the underwriter and the title company with all amendments and schedules.

Trust Approval

For all reverse mortgage products, the eligibility of a property held by trust is subject to review and approval of the trust by a qualified attorney (at Underwriters discretion) AND the title company.

New Deed Requirements

When the Trust has been Amended and Restated a new deed is required to add the Restated Date

If the borrower is a trustee and is not competent, they must be removed as Trustee. UW to ensure all Trust requirements for competency have been met per the trust. A new deed to remove trustee or to add a successor trustee is required.

Deceased trustees must be removed from vesting. This may require a deed to add a successor trustee if trust requires a successor for the deceased trustee.

EASEMENTS, RESTRICTIONS, AND ENCROACHMENTS

Smartfi considers all easements, restrictions, or encroachments and their impact on the market value of the subject property.

- An easement grants rights to access or use the real property of another person without owning it. Typical easements in general will not cause the property to be ineligible for FHA financing.
- Smartfi may allow the following easements under HUD's General Waiver guidelines. These will not cause the property to be uninsurable by FHA:
  - Typical easements for public utilities, party walls, driveways, and other purposes.
  - Easements for public utilities along one or more of the property lines and extending not more than 10 feet from and for drainage or irrigation ditches along the rear 10 feet of the property – provided the exercise of the rights there does not interfere with any of the buildings or improvements located on the subject property.
  - Easements for underground conduits which are in place and do not extend under any buildings on the subject property.
  - Mutual easements for joint driveways constructed partly on the subject property and partly on adjoining property – provided the agreements creating such easements are of record.

Restrictions are general limitations as to the use or placement of real estate. Smartfi may allow the following restrictions under the General Waiver guidelines without causing the property to be uninsurable by FHA:

- Typical building and use restrictions which:
  - Are coupled with a reversionary clause – provided there has been no violation prior to the date of the deed to the Commissioner.
  - Are not coupled with a reversionary clause and have not been violated to a material extent.
- If the restriction set forth is being violated, Smartfi will review for one of the following allowable exceptions:

- Violations of cost or set back restrictions which do not provide a penalty of reversion or forfeiture of title, or a lien for liquidated damages which may be superior to the lien of the insured mortgage.
- Violations of such restrictions which do provide for such penalties – provided such penalty rights have been duly released or subordinated to the lien of the insured mortgage or provided a policy of title insurance is furnished expressly insuring the Commissioner against loss by reason of such penalties.
- Violations of a restrictions based on race, color, or creed: even where such restrictions provide for a penalty of reversion or forfeiture of title or a lien for liquidated damages.

An **encroachment** exists when a structure from one property extends over the property line of another property.

For example, a garage roof overhangs a neighbor's property line, a retaining wall crosses the neighbor's property line, or a driveway/pool is paved a few inches past the boundary line.

The existence of an encroachment is usually confirmed with a boundary line survey or an appraiser.

Results of such a survey are usually recorded as a matter of public record and become attached to the title of the offending property.

Appraiser is required to identify all encroachments on appraisal report.

An encroachment may be acceptable if the adjoining landowner, or the local governing authority, provides a perpetual encroachment easement filed in the County Clerk and Recorder's office.

PROPERTY & APPRAISAL

Smartfi must determine if the property provides sufficient collateral for the HECM. The property must comply with the requirements for Title II Forward and Reverse Mortgage.

Smartfi must evaluate and determine if the property complies with HUD's Property Acceptability Criteria. Existing and New Construction Properties must comply with minimum property requirements and minimum property standards by constructions status.

Note: The effective date of the appraisal cannot be before the FHA case assignment date. Exception can be made to allow the appraisal date to be after the case assignment when Smartfi can certify in the appraisal login screen appraisal was ordered for a conventional financing, or other government-guaranteed loan purposes and was performed by an FHA Roster Appraiser, or the previous FHA case number was cancelled.

APPRAISAL REQUIREMENTS

- All FHA, FIREAA, USPAP, Appraiser Independence, and State requirements must be followed, UAD format is required for Single Family Residence (FNMA 1004) and Individual Condominium Unit (FNMA 1073) which includes Site Condo, and the case number must be reflected on top righthand corner of the first page of the report. The address must be in a United States Postal Service (USPS) format,
- The Appraiser must confirm/state that the subject property meets HUD Minimum Property Requirements as per Handbook 4000.1,
- If the report is completed subject to repairs, then the appraiser must state that the subject property will meet HUD Minimum Property Requirements upon completion of the repairs, and must provide itemized cost to cure estimate,
- Smartfi will review all comparable sales on every report and compare to other comparable sales that were available at the time of the appraisal as may be shown in an AVM or CDA. Any discrepancies must be addressed by the appraiser. Smartfi may request that the appraiser explain in detail why certain other like comparable sales were omitted from value consideration.

APPRAISER RESPONSIBILITY TO REPORT PROPERTY COMPLIANCE

The Appraiser must observe, analyze, and report that the Property meets HUD's MPR and MPS.

Minimum Property Requirements (MPR) refer to general requirements that all homes insured by FHA be safe, sound, and secure.

Minimum Property Standards (MPS) refer to regulatory requirements relating to the safety, soundness, and security of New Construction.

Every Property must be safe, sound, and secure so that the lender can determine eligibility. The Appraiser must note every instance where the Property is not safe, sound, and secure and does not comply with FHA's MPR and MPS.

All appraisals of properties that are to be secured by FHA-insured mortgages must be reported on one of the following forms based on property type:

- Uniform Resident Appraisal Report - for all 1-unit single family dwellings, including a PUD (Fannie Mae Form 1004)
- Manufactured Home Appraisal Report - for all manufactured homes (Fannie Mae Form 1004C)
- Individual Condominium Unit Appraisal Report - for all individual condominium units and site condos (Fannie Mae Form 1073)
- Small Residential Income Property Appraisal Report - for all 2-4-unit dwellings (Fannie Mae Form 1025)

- Market Conditions Addendum to the Appraisal report (Fannie Mae Form 1004MC) is required for all one-to-four unit properties.

ELIGIBLE PROPERTIES

- 1–4-unit dwelling, including modular homes,
- Attached or detached PUD's
- Townhouses (detached or semi-detached)
- Row houses
- Site condominiums that meet FHA's definition
- Manufactured housing that meets HUD and Lender requirements
- Condominium units in HUD-approved condominium projects
- Log homes with log home comparable sales,
- New Construction with Certificate of Occupancy (CO) issued prior to closing. Property must be 100% complete prior to closing.
- Legal non-conforming that can be re-built AS IS if destroyed.

INELIGIBLE PROPERTIES

- Unimproved land
- Homes located on Indian Tribal Land,
- Manufactured home built prior to June 15, 1976 (mobile home)
- Single wide manufactured homes
- Manufactured homes on land (not on a permanent foundation)
- Manufactured homes located on a land lease/leasehold
- Commercial properties
- Units in co-operative or condo-hotel projects
- Properties that cultivate or harvest Marijuana plants on premises
- Working farms and properties used for agricultural purposes or commercial enterprise.
- Property contaminated by the presence of methamphetamine (meth), either by its
- Timeshares or segmented ownership properties
- Properties used as short-term rentals (under 30 days) or any property that provides hotel-type services.
- Properties situated in any area defined by the U.S. Geological Survey Observation as Lava Flow Zones 1 or 2 (for example, summit areas, active parts of the rift zone, areas adjacent to any downslope from Kilauea or Mauna Loa)
- Properties located within the Coastal Barrier Resources System (CBRS) or within an Otherwise Protected Area (OPA)

UNIQUE PROPERTIES-NON-STANDARD HOUSE STYLES

Eligibility of any unique property/non-standard house style is determined by whether or not the property is structurally sound, built to conform to Minimum Property Standards, and readily marketable. Other eligibility factors may apply depending on what makes the home unique.

A unique property includes any of the following:

- Log home
- Exceptionally small home
- Mixed use, live/work
- Lower than normal ceiling height
- Dome home
- Earth berm home (sheltered housing)
- Other houses that in the appraiser's professional option are unique.

PROPERTY DEFINITIONS

ONE UNIT

A one-unit Property is a residential Property with a single Dwelling Unit, **or** with a single Dwelling Unit and a single ADU.

TWO UNIT

A two-unit Property is a residential Property with two individual Dwelling Units.

For any 2–4-unit property a completed, signed, and dated form HUD-92561, *Borrower's Contract with Respect to Hotel and Transient Use of Property* is required.

THREE TO FOUR UNIT

A three- to four-unit Property is either:

- a residential Property with three or four individual Dwelling Units; **or**
- a residential Property with 2 individual Dwelling Units and one ADU or 3 individual Dwelling Units and one ADU.

For any 2–4-unit property a completed, signed, and dated form HUD-92561, *Borrower's Contract with Respect to Hotel and Transient Use of Property* is required.

ACCESSORY DWELLING UNIT

Homes with an ADU are permitted if the following conditions are met:

- Must be common and customary to the area as evidence by comparable sales,
- If the ADU is rented and we are using that rental income to qualify then we **must** obtain evidence from the local municipality having jurisdiction that local code allows for the ADU to be rented.,
- Borrower(s) do not reside in the ADU,
- Existence of the accessory unit must not jeopardize any future hazard insurance claims,
- There can only be one (1) ADU contained within, attached, or detached to the subject property.

CONDOMINIUM UNIT

A condominium development is created by state or local law and is characterized by fee-simple ownership of a unit, which is defined in the condominium documents, together with common areas. The property interest in these areas is both common and undivided on the part of all unit owners, each of whom belongs to the HOA that typically maintains the Property and collects assessments or dues from each unit owner.

A Condominium Project must be FHA approved.

CONDOMINIUM PROJECTS

Condominium Project refers to a project in which one-family Dwelling Units are attached, semidetached, or detached, or Manufactured Home units, and in which owners hold an undivided interest in Common Elements.

Common Elements refer to the Condominium Project's common areas and facilities including underlying land and buildings, driveways, parking areas, elevators, outside hallways, recreation and landscaped areas, and other elements described in the condominium declaration.

For approved projects, Smartfi reviews the HUD 9991 to verify Individual Owner concentration, leasehold, gut rehabilitation, new construction, or manufactured home project, as applicable, requirements, units in arrears for condominium association fees, insurance requirements, and owner occupancy percentage to ensure continued compliance with FHA requirements.

The following documents will be required:

- FHA Connection condominium print out showing as an HRAP or DELRAP approved project as of the date the FHA case # was assigned,

- Form HUD 9991 FHA Condominium Loan Level/Single-Unit approval – Sections 1 – 3 completed within 45 days of Underwriting,
- Master Insurance Policy Declaration page – Hazard, Liability, Fidelity (aka crime/employee dishonesty)
- HO-6 coverage: the unit owner is required to obtain a "walls-in" coverage policy **if** the master or blanket policy does not include interior unit coverage, including replacement of interior improvements and betterment coverage to ensure improvements that the borrower(s) may have made to the unit. **Coverage must be at least 20% of the appraised value.**
- Flood Insurance Policy, if applicable.
- The HOA is required to obtain & maintain flood insurance coverage under the NFIP on buildings located in a SFHA. Flood insurance required for a condominium unit must be at minimum, the ***lowest*** of:
- The maximum claim amount on the loan **OR**
- The replacement cost of the building **OR**
- The maximum amount of insurance available under the National Flood Insurance program ($250,000).

The maximum limit of building insurance coverage of a residential condominium building in a regular program community is $250,000 times (x) the number of units in the building (not to exceed the building's replacement cost).

Note: Smartfi does not offer financing for Single Unit Approval Condos.

SITE CONDOMINIUMS

A Site Condominium refers to:

- a Condominium Project that consists entirely of single-family detached dwellings that have no shared garages, or any other attached buildings; **or**
- a Condominium Project that:
    - consists of single family detached or horizontally attached (townhouse) dwellings where the unit consists of the dwelling **and** land;
    - does not contain any Manufactured Housing units; and
    - is encumbered by a declaration of condominium covenants or a condominium form of ownership.

The Unit owner must be responsible for all insurance and maintenance costs, excluding landscaping, of the Site Condominium. A master insurance policy that provides unit dwelling coverage is not acceptable.

Site Condominiums do not require Condominium Project Approval or Single-Unit Approval.

Manufactured Housing condominium units **may not** be processed as Site Condominiums and **are not** eligible for Single-Unit Approval.

HOMEOWNERS' AND CONDOMINIUM ASSOCIATIONS

For properties that are located within a Homeowners' Association (HOA) or Condominium Association, Smartfi must conduct a review of the recorded Declaration and/or recorded Covenants, Conditions, and Restrictions 9&R) which are in place for the association. When conducting the review, Smartfi must determine whether the recorded Declaration and/or CC&Rs require prior approval by the association of any non-purchase money mortgage what will encumber the property.

In those situations where such a requirement exists, Smartfi must obtain the approval of the association in writing.

MANUFACTURED HOUSING CONDOMINIUM PROJECTS

A Manufactured Home Condominium Project (MHCP) refers to a Condominium Project that consists of two or more Manufactured Homes. A Manufactured Housing Condo project must be FHA approved as evidenced by FHA Connection. The project must be approved at the time of FHA Case # assignment date.

The Appraiser must report the appraisal on Fannie Mae Form 1004C/Freddie Mac Form 70-B, *Manufactured Home Appraisal Report*.

In addition to the requirements for analysis and reporting of the Manufactured Home, the Appraiser must inspect the Condominium Project and provide the project information data as an addendum to the appraisal report. Required data includes all data elements as found in the Project Information Section of Fannie Mae Form 1073/Freddie Mac Form 465.

MANUFACTURED HOUSING

Manufactured Housing is a Structure that is transportable in one or more sections.

To be eligible Manufactured Housing must:

- be designed as a one-family dwelling;
- have a floor area of not less than 400 square feet;
- have the HUD Certification Label affixed or have obtained a letter of label verification issued on behalf of HUD, evidencing the house was constructed on or after June 15, 1976, in compliance with the Federal Manufactured Home Construction and Safety Standards;
- be classified as real estate (but need not be treated as real estate for purposes of state taxation);
- be built and remain on a permanent foundation.
- be designed to be used as a dwelling with a permanent foundation built in accordance with the Permanent Foundations Guide for Manufactured Housing (PFGMH); and
- have been directly transported from the manufacturer or the dealership to the site.

MANUFACTURED HOME ADDITIONAL REQUIREMENTS

If the appraisal indicates the HUD Certification Label is missing from the Manufactured Housing unit, we must obtain a label verification from the institute for Building Technology and Safety (IBTS).

We must obtain a certification by an engineer or architect, who is licensed/registered in the state where the Manufactured Home is located, attesting to compliance with the PFGMH.

We may obtain a copy of the foundation certification from a previous FHA-insured Mortgage, showing that the foundation met the guidelines published in the PFGMH that were in effect at the time of certification, provided there are no alterations and/or observable damage to the foundation since the original certification.

If the Appraiser notes additions or alterations to the Manufactured Housing unit, we must ensure the addition was addressed in the foundation certification.

If the additions or alterations were not addressed in the foundation certification, we must obtain:

- an inspection by the state administrative agency that inspects Manufactured Housing for compliance; or
- certification of the structural integrity from a licensed structural engineer if the state does not employ inspectors.

Running Gear

Running Gear refers to a mechanical system designed to allow the Manufactured Housing unit to be towed over public roads. The towing hitch and Running Gear must be removed.

The Appraiser must notify Smartfi and report deficiency of MPR or MPS if the Running Gear or towing hitch are still attached to the Manufactured Housing unit.

MODULAR HOUSING

Modular Housing refers to Structures constructed according to state and local codes off-site in a factory, transported to a building lot, and assembled by a contractor into a finished house. Although quality can vary, all of the materials –from framing, roofing, and plumbing to cabinetry, interior finish and electrical– are identical to what is found in comparable quality conventional “stick-built” housing.

The Appraiser must treat Modular Housing the same as stick-built housing, including reporting the appraisal on the same form. The Appraiser must select and analyze appropriate comparable sales, which may include conventionally built housing, Modular Housing or Manufactured Housing.

MINIMUM PROPERTY REQUIREMENTS (MPR) AND MINIMUM PROPERTY STANDARDS (MPS) BY CONSTRUCTION STATUS

EXISTING CONSTRUCTION DEFINITION

Existing Construction refers to a Property that has been 100 percent complete for over one (1) year **or** has been completed for less than one (1) year and was previously occupied.

For the HECM program, FHA defines “existing properties” as those where construction has been completed and the property is habitable.

NEW CONSTRUCTION DEFINITION

Existing Less than One Year refers to a Property that is 100 percent complete and has been completed less than one year from the date of the issuance of the CO or equivalent. The property MUST have never been occupied.

For New Construction, the Appraiser must notify the Mortgagee of the deficiencies when the Property does not comply with FHA’s MPR and MPS, including 24 CFR §§200.926a-200.926e.

New Construction Proposed Construction, or Under Construction but not yet complete, less than 90%, then the appraisal is to be completed “Subject to completion per plans & specifications on the basis of a hypothetical condition that the improvements have been completed”. The HUD 92051 Compliance Inspection Report completed by the appraiser is required to document completion per the Plans & Specifications. The CIR Section IV. Must be completed and signed by the DE underwriter.

Property in new subdivision or project, the selected comparable sales must include at least one sale from outside of the subject property subdivision or project, and at least one comparable sale from within the subject property subdivision or project.

New Construction Additional Requirements

Smartfi must obtain the following:

Smartfi must provide the appraiser with a fully executed form HUD-92541 signed and dated no more than 30 days prior to the date the appraisal was ordered.

For Properties 90 percent completed or less, Smartfi must provide a copy of the floor plan, plot plan, and any other exhibits necessary to allow the appraiser to determine the size and level of finish of the house they are appraising.

Form HUD-92544, Warranty of Completion of Construction

Copy of the CO (or equivalent), if available from local authority with jurisdiction;

Required inspections, as applicable;

Provide Form HUD-NPMA-99-A, Subterranean Termite Protection Builder’s Guarantee or Form HUD-NPMA-99-B, New Construction Subterranean Termite Service Record. Unless the

Property is in a county listed as not required on HUD's "Termite Treatment Exception Areas" list. https://www.hud.gov/sites/dfiles/SFH/documents/SFH_POLI_TERMITE.pdf

A well water test is required for all newly constructed properties serviced by a private well.

New construction located in a flood zone if it was completed less than one year from the date of Certification of Occupancy, refence HUD Handbook 4000.1.

Note: Existing Properties are those where construction has been completed and the property is habitable. A Certificate of Occupancy (CO) does not have to be issued for the appraisal report to be completed, however Smartfi requires a CO, or its equivalent, issued by the local jurisdiction prior to loan closing.

ADDITIONAL MANUFACTURED HOME ON PROPERTY

If the additional manufactured home is occupied, it must be handled in ONE of the following ways:

- The MFH must meet ALL requirements for manufactured housing AND the subject property must be treated as either an ADU or a two-unit property with similar comparable. Appraiser must also confirm that local zoning allows for ADU's or 2 units as applicable.
- It must be removed from the subject property before closing. Confirmation of this must be provided via a 1004D / reinspection.
- The land must be surveyed and the portion of land on which the MFH is located must be legally split from the land containing the primary residence. This must be completed prior to closing and the appraisal must not include the portion of land containing the MFH.

If the manufactured home is being used for storage, all the following is required:

- The kitchen must be rendered inoperable and kitchen elements removed.
- The appraiser must provide interior photos of the home showing storage use only, with kitchen removal.
- Utilities must be disconnected.
- The appraiser must certify that there are no health and safety issues.

APPRAISAL VALUATION AND REPORTING PROTOCOLS

PHOTOGRAPH, EXHIBITS AND MAP REQUIREMENTS

The Appraiser must include a legible street map showing the location of the subject and each of the comparable properties, including sales, rentals, listings, and other data points utilized. If substantial distance exists between the subject and comparable properties, additional legible maps must be included.

The Appraiser must include:

- a building sketch showing the GLA, all exterior dimensions of the house, patios, porches, decks, garages, breezeways, and any other attachments or outbuildings contributing value. The sketch must show "covered" or "uncovered" to indicate a roof or no roof (such as over a patio).
- must show the calculations used to arrive at the estimated GLA.
- provide an interior sketch or floor plan for Properties exhibiting functional obsolescence attributable to the floor plan design.

Appraisal Photo Requirements

The Appraiser must provide photographs of the subject property and comparable sales.

Photo requirements of the subject property include:

- Kitchen(s),
- Main living area,
- All bathrooms,
- All bedrooms,
- Basement, attic and crawl space (if applicable),
- Any recent updates, such as restoration, remodeling, or renovation,
- Front and rear photos of the subject exterior at opposite angles to show all sides of the dwelling improvements,
- Street scene photographs to include a portion of the subject site,
- Deficiencies requiring repair the appraiser must provide photographs of the deficiency or condition requiring inspection or repair,
- Any other rooms representing overall condition.

Note: For Comparable Sales, Listings, Pending Sales, Rentals, etc. the appraiser must provide front photo views of each comparable utilized. Photographs should be taken at an angle to depict both the front and the side when possible. Multiple Listing Service (MLS) photographs are acceptable to exhibit comparable condition at the time of sale. However, Appraisers must include their own photographs as well, to document compliance of a curb side inspection of the comp.

APPRAISAL REQUIREMENTS

The following are key requirements of the appraisal:

- The effective date of the appraisal must be on or after the case number assignment date.

- The property owner must reflect the borrower's names on a refinance transaction.
- If the property is non-owner occupied, the loan will be rejected unless the transaction is a purchase.
- Present Land Use should not reflect a current change underway to non-residential use.

QUALITY OF APPRAISAL

The DE Underwriter must evaluate the appraisal to ensure it complies with the requirements in Valuation and Reporting Protocols and any additional appraisal requirements that are specific to the subject property.

VALUATION DEVELOPMENT

There are three valuation approaches as applied to one-to four-residential unit Properties:

- Sales comparison approach;
- Cost approach; and
- Income approach to value.

The Appraiser must obtain credible and verifiable data to support the application of the three approaches to value.

The Appraiser must perform a thorough analysis of the characteristics of the market, including the supply of properties that would compete with the subject and the corresponding demand.

EFFECTIVE AGE AND REMAINING ECONOMIC LIFE

The effective age reflects the condition of a property relative to similar competitive properties. The effective age may be greater than, less than, or equal to the actual age. Any significant difference between the actual and effective ages requires an explanation.

The Appraiser must state the remaining economic life as a single number or as a range for all property types, including condominiums. The Appraiser must provide an explanation if the remaining economic life is less than 30 years. FHA will not insure a property if the remaining economic life is less than 30 years. The Appraiser must provide a list of repairs/updates and an estimated cost to cure for the property to have at least 30 years of REL at the time of loan closing.

LAND VALUATION

If the cost approach is applicable, the Appraiser must estimate the site value. Acceptable methodology used to estimate land value include sales comparison, allocation, and extraction.

The Appraiser must include a summary of the supporting documentation and analysis in the appraisal. The Appraiser must maintain comparable land sales data and analysis or other supporting information in the Appraiser's file and include it by reference in the appraisal. For Properties with Excess Land, the Appraiser must include all comparable land sale data and analysis in the report.

ESTIMATE OF COST NEW FOR HOUSING

The Appraiser may use either the replacement cost or the reproduction cost. The Appraiser must state the method used and the source of the data.

The Appraiser must use the current version of a published cost data source recognized by the industry. The Appraiser must report the quality rating selected and utilized, as well as identify the source of the data, and its publication and/or effective date. The Appraiser is expected to be aware of local cost data from builders, contractors, building supply firms, and other building industry participants as a check against the published cost data.

INCOME APPROACH TO VALUE FOR RESIDENTIAL PROPERTIES

The Appraiser should apply the income approach to a Single-Family residential Property when there is evidence of recently rented and then sold data pairs.

The Appraiser must verify if the subject or the comparable rentals and sales are subject to rent control restrictions. If comparable sales do not have rent control restrictions similar to those of the subject, an appropriate adjustment should be applied.

The Appraiser must analyze rental data and provide support for the estimated market rents and adjustments applied to the comparable rentals in the reconciliation of this approach.

The Appraiser must derive the Gross Rent Multiplier (GRM) factor from market data and support it prior to applying it to the market rent for the subject.

SALES COMPARISON APPROACH

The Appraiser must present the data, points of comparison, and analysis; provide support for the Appraiser's choice of comparable properties, and the adjustments for dissimilarities to the subject; and include sufficient description and explanation to support the facts, analyses, and the Appraiser's conclusion.

If the data from the market area is insufficient to support some of these requirements, the Appraiser must provide the best information available and include an explanation of the issue, the data available, the conclusions reached, and the steps taken by the Appraiser to attempt to meet the guidelines.

The Appraiser must include as many comparable properties as are necessary to support the Appraiser's analysis and conclusion. At a minimum, the Appraiser must include the most recent and relevant sales, preferably within the last six months. The Appraiser must include at least three sales that settled no longer than 12 months prior to the effective date of the appraisal. The Appraiser must provide additional support by including more sales, offerings, offerings now under contract, or relevant sales that settled more than 12 months prior to the effective date of the appraisal.

For manufactured homes, the Appraiser must include a sufficient number of sales to produce a credible value. The Appraiser must include at least two Manufactured Homes in the comparable sales grid. When considering sales to be utilized as comparable properties, the Appraiser must note the conditions of the sale and the motivation of the sellers and purchasers.

In some markets, identity of interest (non-arm's length) sales constitute the majority of recent transactions of similar properties and thus are significant in the analysis of the subject. This assignment is to estimate Market Value, so REO sales, short sales and other non-arm's length transactions must not automatically be chosen as comparable properties. If there is compelling evidence in the market to warrant their use, the Appraiser must provide additional explanation and support in the "Analysis" section of the sales comparison approach.

RE-USE OF APPRAISALS

Appraisals that were used to close a previous FHA loan cannot be re-used, even if less than four (4) months old. Each new FHA loan requires a new appraisal.

SECOND APPRAISALS

Second appraisals are ONLY permitted under the following circumstances:

- FHA completes a Collateral Risk Assessment and requires a 2nd appraisal,
- The DE Underwriter determines that the initial appraisal contains material deficiencies,
- The appraiser who performed the first appraisal is on our Exclusionary List, or
- The first appraisal expires.

The following requirements apply to second appraisals and FHA case numbers:

- An appraisal update must be performed before the initial appraisal, (with no extension), has expired. Where the initial appraisal is subsequently updated, the updated appraisal is valid for a period of 360 Days after the effective date of the initial appraisal report that is being updated.
- When the case number and/or counseling certificate have expired along with the appraisal, a new case number is required. A second appraisal does not extend the case assignment validity period.

APPRAISAL EXPIRATION-EXTENSION

The appraisal must not expire prior to the funding date.

An appraisal of existing properties is valid for 180 days from the effective date on the appraisal. The validity period may be extended per the discretion of Underwriting, as follows, if the subject property is not in a declining market.

The 1004D must be effective prior to the expiration date of the original appraisal. When the 1004D is completed, the appraisal update extends the validity period of the original appraisal by 180 days making it valid for a cumulative total of one year.

Note: ML 2022-11 has removed the option for 30-day extension.

A 1004D may never be ordered when the property is in a declining market.

The following provisions apply to the updated report:

- The report may not be used when the subject property has declined in value or when improvements have been made to the subject property that cannot be viewed from the street. Additionally, the updated report may not be used when the exterior inspection of the house shows significant changes that were not in existence at the time of the original appraisal report.
- If a substitute Appraiser is used due to the lack of the original Appraiser availability, the substitute Appraiser must state they concur with the analysis and conclusions in the original appraisal report, and the Mortgagee must document in the case binder why the original Appraiser was not used.
- The Appraiser must incorporate the original report being updated by attachment rather than by reference.
- In the event the appraisal and counseling certificate have expired, a new application and FHA case number are required. If the counseling certificate is still valid, the borrower does not need to re-apply because of an expired appraisal.
- If the appraisal has expired, the existing case number must be cancelled and a new case number obtained prior to ordering a new appraisal report. The effective date of the new appraisal must be after the new case number assignment.

INCREASING MARKETS

In an increasing market, positive Market Condition Adjustments should be applied if there is sufficient proof of the trend from a credible source based on a thorough analysis of specific market trends and as evidenced by a sale and resale comparison.

DECLINING MARKETS

Although there is no standard industry definition, for purposes of performing appraisals of Properties that are to be collateral for FHA-insured Mortgages, a Declining Market refers to any neighborhood, market area or region that demonstrates a decline in prices or deterioration in other market conditions as evidenced by an oversupply of existing inventory and extended marketing times. Generally, a trend in the housing market is identifiable when it extends for a period of at least six months or two quarters prior to the effective date of the appraisal.

In a Declining Market, negative Market Condition Adjustments should be applied if there is sufficient proof of the trend from a credible source based on a thorough analysis of specific market trends and as evidenced by a sale and resale comparison.

The Appraiser must accurately report market conditions and determine when housing trends are increasing, stable or declining. The Appraiser must provide a summary comment as to the continuance of the current trend or if the trend appears to be changing and provide support for all conclusions. If the Appraiser bases the adjustment on a published source, the Appraiser must include a copy of which must be included in the addendum.

The Appraiser must include an absorption rate analysis, and at least two comparable sales that closed within 90 Days prior to the effective date of the appraisal. If the Appraiser cannot comply with this requirement due to the lack of market data, a detailed explanation is required.

The Appraiser must include a minimum of two active listings or pending sales on the appraisal grid (in addition to at least three recently settled sales).

For active listings or pending sales, the Appraiser must:

- ensure they are market tested and have reasonable market exposure to avoid the use of overpriced properties as comparable properties;
- use the actual contract purchase price, or, when not available, adjust comparable properties to reflect listing to sale price ratios; include the original list price, any revised list prices, and calculate the total Days on Market (DOM). The Appraiser must provide an explanation for the
- DOM that does not approximate periods reported in the "Neighborhood" section of the appraisal reporting form;
- reconcile the Adjusted Values of active listings or pending sales with the Adjusted Values of the settled sales provided; and
- If the Adjusted Values of the settled comparable properties are higher than the Adjusted Values of the active listings or pending sales, determine if a Market Condition Adjustment is appropriate.

APPRAISERS SIGNATURE

The FHA Roster Appraiser must sign the certification of the appraisal and perform all parts of the analysis and reconciliation. Appraiser trainees or licensees may not sign the appraisal report. A trainee or licensee may assist in any part of the appraisal, but the opinions and analysis must be performed by the FHA Roster Appraiser. A trainee or licensee may accompany the FHA Roster Appraiser on the observations but may not perform the observations in place of the FHA Roster Appraiser. The FHA Roster Appraiser must select the comparable properties and perform all critical analyses contained in the appraisal report as well as the Market Conditions Addendum to the appraisal form. The FHA Roster Appraiser must also inspect the subject Property and at least the exterior of the comparable properties.

If another appraiser or trainee appraiser provided assistance or participated in the preparation of the appraisal, the FHA Roster Appraiser must disclose the name of the appraiser or trainee appraiser in the report and their role in developing the appraisal.

APPRAISAL DELIVERY

As mandated by the Consumer Financial Protection Bureau (CFPB's) Equal Credit Opportunity Act (ECOA) Valuation's Rule, Smartfi complies with the following provisions:

- Notify applicants of their right to receive copies of all valuations and appraisals developed, along with other information required in the notice.
- Applicants must be notified in writing within three (3) days of application of the right to receive a copy of any appraisal developed in connection with the application.
- The Right to Receive a Copy of an Appraisal and Other Written Valuations is included in the application package.
- Provide applicants with a copy of each appraisal and other written valuations promptly upon completion or three (3) business days prior to consummation (for closed-end credit) or account opening (for open-end credit), whichever is earlier.
- There must be a three (3)-day wait from delivery/email transmittal of the final appraisal to the closing of the loan unless a signed waiver as described below is obtained.
- The applicant may waive the timing requirement for the ECOA Valuations Rule and agree to receive appraisal copies at consummation or account opening.
- If a second appraisal is ordered, for any reason, a copy of each appraisal must be delivered to the borrower.
- Updated versions of an appraisal must be provided to the applicant following the timing requirement (the earlier of promptly upon completion or three (3) business days prior to closing) unless the timing requirement has been waived by the applicant.

Note: For Wholesale Smartfi sends a copy of the appraisal at the time the appraisal is received and sent to the Partner.

CRAWL SPACE & ATTIC REQUIREMENTS

Crawl Space

There must be adequate access to the crawl space, and the appraiser must be able to access the crawl space for inspection. In cases where access is limited, a head and shoulders inspection will suffice. If there is no access but there is evidence of a deficient condition (such as a water-stained subfloor or the smell of mold) the appraiser must report this condition and a 3rd. party inspection by a licensed plumber or contractor will be required. If there is no access and no evidence of any deficient conditions, the appraiser must report the lack of accessibility to the area in the appraisal and confirm that there is no evidence of any deficient conditions.

In addition:

- The floor joists must be sufficiently above ground level to provide access for maintenance repair of ductwork and plumbing.
- If the crawl space contains any system components, the minimum required vertical clearance is 18 inches between grade and the bottom of the floor joists
- The crawl space must be properly vented unless the area is mechanically conditioned.
- The crawl space must be clear of trash, debris, and vermin.
- The crawl space must not be excessively damp and must not have any water ponding. If moisture problems are evident, a vapor barrier and/or prevention of water infiltration is required.
- Any earth to wood contact must be repaired.

The appraiser must report any evidence that may indicate issues with structural support, dampness, damage, or vermin that may affect the safety, soundness, and security of the property.

Attic

Appraiser must inspect the attic and comment that it meets FHA/HUD's minimum requirements. If the appraiser is unable to view the area safely, a 1004D / reinspection will be required, and the borrower will need to decide for the appraiser's safe access to the attic.

If there is no access or scuttle, the Appraiser must report the lack of accessibility to the area in the appraisal report and comment that the attic appears to be adequately ventilated from the exterior. There is no requirement to cut open walls, ceilings, or floors.

An observation performed in accordance with these guidelines is visual and is not technically exhaustive.

BASEMENT

The Appraiser must comment if the basement is not free of dampness, wetness, or obvious structural problems that might affect the health and safety of occupants or the soundness of the structure.

CHARACTERISTICS OF PROPERTY IMPROVEMENTS

Requirements for Living Unit

The Appraiser must comment if each living unit does not contain any one of the following:

- A continuing and sufficient supply of safe and potable water under adequate pressure and of appropriate quality for all household uses;
- Sanitary facilities and a safe method of sewage disposal. Every living unit must have at least one bathroom, which must include, at a minimum, a water closet, lavatory, and a bathtub or shower;
- Adequate space for healthful and comfortable living conditions;
- Heating adequate for healthful and comfortable living conditions;
- Domestic hot water; and
- Electricity adequate for lighting, cooking and for mechanical equipment used in the living unit.

FHA does not have a minimum size requirement for one- to four-family dwellings and condominium units. For Manufactured Housing requirements, see the Manufactured Housing section.

We must ensure that cabinets and built-in appliances that are considered real property are present & operational.

NON-STANDARD HOUSE STYLES

Non-Standard House Style refers to unique Properties in the market area, including log houses, earth sheltered housing, dome houses, houses with lower-than-normal ceiling heights, and other houses that in the Appraiser's professional opinion, are unique.

The Appraiser must provide a comment that the non-standard house style appears structurally sound and readily marketable and must apply appropriate techniques for analysis and evaluation. In order for such a property to be fully marketable, the Appraiser must demonstrate that it is located in an area of other similar types of construction and blend in with the landscape.

The Appraiser may require additional education, experience, or assistance for these types of Properties.

GROSS LIVING AREA

Gross Living Area (GLA) refers to the total area of finished, above-grade residential space calculated by measuring the outside perimeter of the Structure. It includes only finished, habitable, above-grade living space.

The Appraiser must: Identify non-contiguous living area and analyze its effect on functional utility;

- Ensure that finished basements and unfinished attic areas are not included in the total GLA; and
- Use the same measurement techniques for the subject and comparable sales, and
- Report the building dimensions in a consistent manner.

When any part of a finished level is below grade, the Appraiser must report all of that level as below grade finished area, and report that space on a different line in the appraisal report, **UNLESS** the market considers it to be Partially Below-Grade Habitable Space.

ADDITIONS AND CONVERTED SPACE

The Appraiser must treat room additions and garage conversions as part of the GLA of the dwelling, provided that the addition or conversion space:

- Is accessible from the interior of the main dwelling in a functional manner;
- Has a permanent and sufficient heat source; and
- Was built in keeping with the design, appeal, and quality of construction of the main dwelling.

Room additions and garage conversions that do not meet the criteria listed above are to be addressed as a separate line item in the sales grid, not in the GLA. The Appraiser must address the impact of inferior quality garage conversions and room additions on marketability as well as Contributory Value, if any.

The Appraiser must analyze and report differences in functional utility when selecting comparable properties of similar total GLA that do not include converted living space. If the Appraiser chooses to include converted living spaces as GLA, the Appraiser must include an explanation detailing the composition of the GLA reported for the comparable sales, functional utility of the subject and comparable properties, and market reaction.

Alternatively, the Appraiser may consider and analyze converted living spaces on a separate line within the sales comparison grid including the functional utility line in order to demonstrate market reaction.

The Appraiser must not add an ADU or secondary living area to the GLA.

UNPERMITTED ADDITIONS

When a property has an unpermitted addition, the appraiser needs to comment on the space, whether or not the addition was completed in a workmanlike manner, if the space is legal based upon current zoning, and if the collateral in its entirety can be rebuilt in case of complete destruction. If the additional square footage is not legal and cannot be rebuilt, we may not lend on this property regardless of the quality of construction.

An example of this would be a detached enclosed room (recreation, extra living space, etc.) that is not part of the main house, and the current zoning does not allow for any type of accessory unit not attached to the main dwelling.

ADDITIONAL OR SECOND KITCHEN

When a single-family residence has more than one full kitchen, the appraisal should discuss the legality of multiple kitchens based upon zoning and city/county ordinances. If multiple kitchens are legal and comparable sales can be found with the same amenity, it is acceptable.

If the appraisal omits discussion on multiple kitchens, a condition should be made for the appraiser to comment on the legality and marketability of the additional kitchens.

If the appraisal reflects that the additional kitchen(s) are not legal, the property is ineligible. In the event the borrower seeks a remedy, the borrower should be counseled that the property is ineligible and at such time that the property complies with applicable building codes, the property may become eligible. At no time should Smartfi advise the borrower to make any changes to their property.

In the event the borrower chooses to take remedial action, ascertain whether the actions can be completed within a reasonable period of time such that expiration of material items such as case number, appraisal, or credit report does not occur. If remedial action as discussed below cannot be accomplished within this period, the loan must be denied for ineligible property and the borrower invited to submit a new application when the property conforms with applicable building codes.

Remedial action acceptable:

1. For properties without a tenant occupying the space or unit with the additional kitchen, the property is eligible at such time an appraiser confirms the removal of the kitchen which removal returns the property to compliance with existing building codes which must be confirmed by an appraiser.
2. For properties with a tenant occupying the unit or space with the additional kitchen, the property will be eligible at such time that the unit or space including the additional kitchen is properly permitted, evidencing compliance with applicable building codes which must be confirmed by an appraiser.

DETERMINATION OF DEFECTIVE CONDITIONS

Defective Conditions refer to defective construction, evidence of continuing settlement, excessive dampness, leakage, decay, termites, environmental hazards, or other conditions affecting the health and safety of occupants, collateral security, or structural soundness of the dwelling.

The Appraiser must identify defective conditions that are curable and will make the Property comply with HUD's MPR or MPS when cured and provide an estimated cost to cure.

If the Appraiser cannot determine that a property meets FHA's MPR or MPS, an inspection by a qualified individual or Entity may be required.

Conditions that require an inspection by qualified individuals or Entities include:

- Standing water against the foundation and/or excessively damp basements;
- Hazardous materials on the site or within the improvements;
- Faulty or defective mechanical systems (electrical, plumbing or heating/cooling);
- Evidence of possible structural failure (e.g., settlement or bulging foundation wall, unsupported floor joists, cracked masonry walls or foundation);
- Evidence of possible pest infestation;
- Leaking or worn-out roofs; or
- Any other condition that is in the professional judgment of the Appraiser warrants inspection.

Appraisers may not recommend inspections only as a means of limiting liability. The reason for or indication of a particular problem must be given when requiring an inspection.

The Appraiser must observe, analyze, and report defective conditions and must also provide photographic documentation of those conditions in the appraisal report.

MINIMUM PROPERTY REQUIREMENTS AND MINIMUM PROPERTY STANDARDS

MPR and MPS form the basis for identifying the deficiencies of the Property that the Appraiser must note within the appraisal report.

CONDITION OF THE PROPERTY

If the appraiser notes that the property is in fair condition, repairs must be completed prior to closing to bring the property up to at least average condition. For any property where the cost of repairs to meet FHA minimum property standards exceed 15% of the maximum claim amount the repairs must be completed prior to closing or the property is ineligible.

EASEMENTS AND DEED RESTRICTIONS

An Easement refers to an interest in land owned by another person, consisting of the right to use or control the land, or an area above or below it, for a specific limited purpose.

A Deed Restriction refers to a private agreement that restricts the use of real estate in some way and is listed in the deed.

The Appraiser must note the presence of any Easements and Deed Restrictions to assist the Lender in determining eligibility.

The Appraiser must analyze and report the effect that Easements and other legal restrictions, such as Deed Restrictions, may have on the use, value, and marketability of the Property. The Appraiser must review recorded subdivision plats when available through the normal course of business.

ENCROACHMENTS

An Encroachment refers to an interference with or intrusion onto another's property.

The Appraiser must report the presence of any Encroachments so that the Lender can determine eligibility.

The Appraiser must identify any Encroachments of the subject's dwelling, garage, or other improvement onto an adjacent property, Right-of-Way, Utility Easement, or building restriction line.

The Appraiser must also identify any Encroachments of a neighboring dwelling, garage, other physical Structure, or improvements onto the subject Property.

Encroachment by the subject or adjacent property fences is acceptable provided such encroachment does not affect the marketability of the subject property.

ENVIRONMENTAL AND SAFETY HAZARDS

The Appraiser must report known environmental and safety hazards and adverse conditions that may affect the health and safety of the occupants, the Property's ability to serve as collateral, and the structural soundness of the improvements.

Environmental and safety hazards may include defective lead-based paint, mold, toxic chemicals, radioactive materials, other pollution, hazardous activities, and potential damage to the Structure from soil or other differential ground movements, subsidence, flood, and other hazards.

The property must be free from all environmental and safety hazards and adverse conditions that may affect the health and safety of the occupants, the property's ability to serve as collateral, and the structural soundness of the improvements.

Lead-Based Paint

Improvements Built on or Before 1978

The Appraiser must note the condition and location of all defective paint and require repair in compliance with 24 CFR § 200.810(c) and any applicable EPA requirements. The Appraiser must observe all interior and exterior surfaces, including common areas, stairs, deck, porch, railings, windows and doors, for defective paint (cracking, scaling, chipping, peeling, or loose). Exterior surfaces include those surfaces on fences, detached garages, storage sheds, and other outbuildings and appurtenant Structures.

Exterior paint

- Raw, exposed wood located on the exterior of the home must be protected from the weather. i.e., staining/sealing, paint, etc.

Interior paint

- For defective paint surface(s) in homes the scraping and painting can be waived if the borrower(s) execute a Lead Base Paint Certification that evidences no children under the age of six (6) will be **or** are residing in the home.
- The appraiser must indicate if the noted condition of the home (e.g. C3, C4) will remain as is if he/she completed the report subject to correction of interior paint surfaces when the DE Underwriter is going to permit waiving interior painting.

A Property's ability to serve as collateral for the HECM program may qualify for an exception from the remediation of defective lead-based paint surfaces. To qualify for the exception under the Lead-Based Paint Poisoning Act, as amended by the Residential Lead-Base Paint Hazard Reduction Act of 1992, Smartfi must obtain the borrower(s) certification that the property qualifies as a housing for the elderly and that no child under six years of age resides or is expected to reside in the home.

When performing an appraisal for the Property that meets the LPPA exception requirements:

the appraiser must receive from Smartfi a copy of the borrower certification that the property qualifies for the exception;

the repair of defective interior and exterior lead-based paint surfaces is not required to meet MPR and the appraisal report must reflect the impact of the property's defective lead-based paint; and

the appraisal report must prominently include the statement: "The mortgagee has identified that they have obtained borrower certification that this property qualifies for the exception from mitigating lead-based paint hazards under the Lead-Based Paint Poisoning Prevention Act".

METHAMPHETAMINE CONTAMINATED PROPERTY

If the Lender notifies the Appraiser or the Appraiser has evidence that a property is contaminated by the presence of methamphetamine (meth), either by its manufacture or by consumption, the Appraiser must render the appraisal subject to the Property being certified safe for habitation.

If the effective date of the appraisal is prior to certification that the Property (site and dwelling) is safe for habitation, the Appraiser will complete the appraisal subject to certification that the Property is safe for habitation.

If the effective date of the appraisal is after certification that the Property (site and dwelling) is safe for habitation, and the Lender has provided a copy of the certification by the certified hygienist, the Appraiser must include a copy of the certification in the appraisal report.

The Appraiser must analyze and report any long-term stigma caused by the Property's contamination by meth and the impact on value or marketability.

MARIJUANA PRODUCTION

Any property where marijuana is grown or processed, regardless of quantity or state law will need to be reviewed with management.

WOOD DESTROYING INSECTS/ORGANISMS/TERMITES

The Appraiser must observe the foundation and perimeter of the buildings for evidence of wood destroying pests. The Appraiser's observation is not required to be at the same level as a qualified pest control specialist.

If there is evidence or notification of infestation, including a prior treatment, the Appraiser must mark the evidence of infestation box in the "Improvements" section of the appraisal and make the appraisal subject to inspection by a qualified pest control specialist.

When a termite inspection is required, a copy of the full report must be provided to Smartfi. All Section 1 and Section 2 items will be required to be repaired or corrected prior to closing. Clearance/Final Report is required once repairs and/or treatment are completed.

PRIVATE ROADS AND SHARED DRIVEWAYS

The subject property must be provided with vehicular and pedestrian access by a public or private road.

Private roads and shared driveways must be protected by permanent recorded easements or be owned and maintained by an HOA.

A maintenance agreement is not required as long as the appraiser notes the accessibility and condition.

EXCESS AND SURPLUS LAND

Excess Land refers to land that is not needed to serve or support the existing improvement. The highest and best use of the Excess Land may or may not be the same as the highest and best use of the improved parcel. Excess Land may have the potential to be sold separately.

Surplus Land refers to land that is not currently needed to support the existing improvement but cannot be separated from the Property and sold off. Surplus Land does not have an independent highest and best use and may or may not contribute to the value of the improved parcels.

The Appraiser must include the highest and best use analysis in the appraisal report to support the Appraiser's conclusion of the existence of Excess Land. The Appraiser must include Surplus Land in the valuation.

If the subject of an appraisal contains two or more legally conforming platted lots under one legal description and ownership, and the second vacant lot is capable of being divided and/or developed as a separate parcel where such a division will not result in a non-conformity in zoning regulations for the remaining improved lot, the second vacant lot is Excess Land. The value of the second lot must be **excluded** from the final value conclusion of the appraisal and the Appraiser must provide a value of only the principal site and improvements under a hypothetical condition.

When excess land is identified the borrower(s) have a choice to mortgage the entire parcel, but not receive a value benefit for the excess land or subdivide off the excess land.

Encumber the land;

- Nothing further is required.

Subdivide the land;

- A new survey including a legal description,
- The local governing authority must indicate if a new parcel number will be assigned for the encumbered lot. If a new parcel number cannot be assigned until the next tax roll the governing authority must state in writing it cannot be assigned at this time and it will be assigned for the next tax roll,
- Land may not be subdivided if this would limit or prevent the encumbered property from direct access to a public road, an acceptable water source, septic tank and leach/drain field unless the appropriate recorded easements are in place, and
- An updated title report with the new legal description.

EXTERNAL INFLUENCES / ADVERSE SITE CONDITIONS

Items such as railroad tracks, high voltage power lines, traffic noise, and proximity to commercial and/or industrial structures will be reviewed by the DE Underwriter. Acceptance of these influences will be determined by underwriting based on its impact on marketability, safety of the occupants, and the appraiser's ability to provide comparable sales with similar influences.

Externalities

Externalities refer to off-site conditions that affect a property's value. Externalities include heavy traffic, airport noise and hazards, special airport hazards, proximity to high pressure gas lines, Overhead Electric Power Transmission Lines and Local Distribution Lines, smoke, fumes, and other offensive or noxious odors, and stationary storage tanks.

The Appraiser must comment the presence of Externalities so that the Smartfi can determine eligibility.

The Appraiser must consider how Externalities affect the marketability and value of the Property, report the issue and the market's reaction, and address any positive or negative effects on the value of the subject Property within the approaches to value.

AIRPORT NOISE AND HAZARDS

The Appraiser must identify if the Property is affected by noise and hazards of low flying aircraft because it is near an airport. The Appraiser must review airport contour maps and analyze accordingly. The Appraiser must determine and report on the marketability of the Property based on this analysis.

SPECIAL AIRPORT HAZARDS

The Appraiser must identify if the Property is located within a Runway Clear Zone (also known as a Runway Protection Zone) at a civil airport or Clear Zone military airfield and consider the effect of the airport hazards on the marketability For Properties located in an Accident Potential Zone 1 (APZ 1) at military airfields, the Appraiser must require compliance with the Department of Defense (DoD) Guidelines and a buyer's acknowledgement.

PROXIMITY TO HIGH PRESSURE GAS LINES

The Appraiser must identify if the dwelling or related property improvement is near high-pressure gas or liquid petroleum pipelines or other volatile and explosive products, both aboveground and subsurface. The Appraiser must determine and report on the marketability of the Property based on this analysis.

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the Property is not located more than 10 feet from the nearest boundary of the pipeline Easement.

OVERHEAD ELECTRIC POWER TRANSMISSION AND LOCAL DISTRIBUTION LINES

Overhead Electric Power Transmission Lines refer to electric lines that supply power from power generation stations to Local Distribution Lines.

Local Distribution Lines refer to electric lines that commonly supply power to residential housing developments, similar facilities, and individual Properties.

Residential service drop line refers to an electric line that begins at the local distribution line and drops to the subject property.

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if any Overhead Electric Power Transmission Line(s) or Local Distribution Line(s) pass directly over any dwelling, structure, or related property improvement, including pools, spas, or water features. A residential service drop line (from street pole to subject property) may not pass directly over any pool, spa or water feature. It does not matter if the subject property is or is not located within an easement if there are any overhead or local power lines that pass directly over the dwelling, or any improvement(s) then the property is not eligible until the line has been relocated.

The Appraiser must also notify Smartfi of the deficiency of MPR or MPS if the dwelling or related property improvements are located within an Easement or if they appear to be located within an unsafe distance of any power line or tower.

The Appraiser must note and comment on the effect on marketability resulting from the proximity to such site hazards and nuisances. The Appraiser must also determine if the guidelines for Encroachments apply.

If the dwelling or related property improvements are located within the Easement area, we must obtain a certification from the appropriate utility company or local regulatory agency stating that the relationship (distance) between the improvements and local distribution lines conforms to local standards and is safe.

SMOKE, FUMES AND OFFENSIVE OR NOXIOUS ODORS

The Appraiser must notify Smartfi if excessive smoke, chemical fumes, noxious odors, stagnant ponds or marshes, poor surface drainage or excessive dampness threaten the health and safety of the occupants or the marketability of the Property.

The Appraiser must consider the effect of the condition in the valuation of the Property if the conditions exist but do not threaten the occupants or marketability.

STATIONARY STORAGE TANKS

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the subject property line is located within 300 feet of an aboveground stationary storage tank with a capacity of 1,000 gallons or more of flammable or explosive material. This includes domestic and commercial uses as well as automotive service station tanks. If the subject property is located within 300-feet, it is **NOT** eligible for FHA insuring.

SITE CONDITIONS

ACCESS TO PROPERTY

Adequate vehicular access to property refers to an all-weather road surface over which emergency and typical passenger vehicles can pass at all times.

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the Property does not have safe pedestrian access and adequate vehicular access from a public street or private street that is protected by a permanent recorded Easement, ownership interest, or is owned and maintained by an HOA. Shared driveways that are not part of an HOA must also meet these requirements.

The Appraiser must note whether there is safe pedestrian access and adequate vehicular access to the site and analyze any effect on value or marketability.

The Appraiser must report evidence of a permanent Easement.

The Appraiser must ask if a maintenance agreement exists and comment on the condition of the private road or lane.

TOPOGRAPHY

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the surface and subsurface water is not diverted from the dwelling to ensure positive drainage away from the foundation.

The Appraiser must make the appraisal subject to an inspection by a qualified individual or Entity if the purchase contract or any other documentation indicates, or if the Appraiser observes dampness because of a foundation issue. The Appraiser must report to the Lender any danger due to topographic conditions (e.g., earth and mudslides from adjoining properties, falling rocks and avalanches) to the subject Property or the adjoining land.

GRADING AND DRAINAGE

The Appraiser must check for readily observable evidence of grading and drainage problems. Proper drainage control measures may include gutters and downspouts or appropriate grading or landscaping to divert the flow of water away from the foundation.

The Appraiser must make the appraisal subject to repair if the grading does not provide positive drainage away from the improvements. The Appraiser must note any readily observable evidence of standing water adjacent to the foundation that indicates improper drainage. The Appraiser must report this in the “Site” section of the report, if the standing water is problematic.

OIL OR GAS WELLS

Operating or Proposed

The Appraiser must examine the site for the existence of any readily observable evidence of an oil or gas well and report the distance from the dwelling.

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the dwelling is located within 75 feet of an operating or proposed well. The distance is measured from the dwelling to the site boundary, not to the actual well site.

Abandoned

For an abandoned well, there must be a letter from a responsible authority stating that the well was safely and permanently abandoned, and the dwelling must be no closer than 10 feet from the abandoned well. If no letter is provided, the dwelling must be at least 300 feet from the abandoned well.

HYDROGEN SULFIDE

Hydrogen sulfide gas emitted from petroleum product wells is toxic and extremely hazardous. Minimum clearance from sour gas wells may be established only after a petroleum engineer has assessed the risk and state authorities have concurred on clearance recommendations for petroleum industry regulation and for public health and safety.

The Appraiser may only complete an appraisal on a property if the Lender has required an inspection by a qualified person and provided evidence that the minimum clearance has been established.

SLUSH PITS

A Slush Pit refers to a basin in which drilling "mud" is mixed and circulated during drilling to lubricate and cool the drill bit and to flush away rock cuttings.

If the Property has a Slush Pit, the Appraiser must make the appraisal subject to the removal of all unstable and toxic materials and the site made safe.

COASTAL BARRIER RESOURCES SYSTEM

The Appraiser must stop work and notify the Mortgagee of the deficiency of MPR or MPS if the Property is located within a Coastal Barrier Resources System (CBRS) designated area.

The Appraiser must review the FEMA FIRM to determine if a property is located within a CBRS. The FIRM will identify CBRS boundaries through patterns of backward-slanting diagonal lines, both solid and broken. If it appears that the Property is located in a CBRS, the Appraiser must review CBRS location maps to confirm.

MINERAL, OIL, AND GAS RESERVATIONS OR LEASES

The Appraiser must analyze and report the degree to which the residential benefits may be impaired, or the Property damaged by the exercise of the rights set forth in oil, gas, and mineral reservations or leases.

The Appraiser should consider the following:

- The infringement on the property rights of the fee owner caused by the rights granted by the reservation or lease; **and**
- The hazards, nuisances, or damages that may arise or accrue to the subject Property from exercise of reservation or lease privileges on neighboring properties.

LEASED EQUIPMENT, COMPONENTS, AND MECHANICAL SYSTEMS

The Appraiser must **NOT** include the value of leased mechanical systems and components in the Market Value of the subject Property. This includes furnaces, water heaters, fuel or propane storage tanks, solar or wind systems (including power purchase agreements), and other mechanical systems and components that are not owned by the property owner. The Appraiser must identify such systems in the appraisal report.

Smartfi must review the terms of the lease on any equipment to ensure they do not contain any Legal Restrictions on Conveyance (Free Assumability).

Mechanical Components and Utilities

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if mechanical systems are not safe to operate; not protected from destructive elements; do not have reasonable future utility, durability, and economy; or do not have adequate capacity.

The Appraiser must observe the physical condition of the plumbing, heating, and electrical systems. The Appraiser must operate the applicable systems and observe their performance.

If the systems are damaged or do not function properly, the Appraiser must condition the appraisal on its repair or further inspection.

If the utilities are not on at the time of observation and the systems could not be operated, the Appraiser must:

- Render the appraisal as subject to re-observation;
- condition the appraisal upon further observation to determine if the systems are in proper working order once the utilities are restored; **and**
- Complete the appraisal under the extraordinary assumption that utilities and mechanical systems, and appliances are in working order.

The Appraiser must note that the re-observation may result in additional repair requirements once all the utilities are on and fully functional.

If systems could not be operated due to weather conditions, the Appraiser must clearly note this in the report. The Appraiser should not operate the systems if doing so may damage equipment or when outside temperatures will not allow the system to operate.

Electrical, plumbing, or heating/cooling certifications may be required when the Appraiser cannot determine if one or all of these systems are working properly.

HEATING AND COOLING SYSTEM

The Appraiser must examine the heating system to determine if it is adequate for healthful and comfortable living conditions, regardless of design, fuel, or heat source.

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the permanently installed heating system does not:

- Automatically heat the living areas of the house to a minimum of 50 degrees Fahrenheit in all GLAs, as well as in non-GLAs containing building or system components subject to failure or damage due to freezing;
- Provide healthful and comfortable heat or is not safe to operate;
- Rely upon a fuel source that is readily obtainable within the subject’s geographic area;
- Have market acceptance within the subject’s marketplace; and
- Operate without human intervention for extended periods of time.

Central air conditioning is not required but, if installed, must be operational. If the air conditioning system is not operational, the Appraiser must indicate the level of deferred maintenance, analyze, and report the effect on marketability, and include the cost to cure.

All habitable rooms must have a heat source. This does not mean that each room must contain a heating device, but that each room must receive sufficient heat (at least 50 degrees Fahrenheit). Heat rising from the first floor to the second-floor bedrooms is not acceptable unless a licensed HVAC professional certifies they have the dwelling’s heating system, and it adequately heats the entire dwelling to at least 50 degrees Fahrenheit, and the heating system meets local jurisdiction guidelines. If the dwelling’s heating system cannot adequately heat the second floor, an acceptable heating system must be installed on the second floor to count the rooms as finished square footage.

Exception: Homes located in Hawaii do not require heat if the lack of it is “typical” for the market area and does not adversely affect the marketability of the property.

Note: HUD minimum property standards state that a heat source is required when an outside temperature could fall below 55 degrees.

- Wood Stove and Solar Heating Systems: Dwellings with wood burning stoves or solar heating systems as a primary heat source must have a permanently installed conventional heating system that can maintain at least 50 degrees Fahrenheit in all living areas, and those containing plumbing systems. These systems must be installed in accordance with the manufacturer's recommendations.
- Floor/space heaters. Must be permanently affixed, properly vented, and meet local code. Plug-in space heaters are not acceptable.
- Non-Conventional Heating Systems: All non-conventional heating systems must comply with local jurisdictional guidelines. Often these are not acceptable as a primary source of heat. An inspection of the heating system and local code compliance may be required.
- Propane Tanks: Must be common and typical for the area, and not affect the

marketability of the subject property. Propane fired furnaces located in a crawl space area are NOT acceptable.

ELECTRICAL SYSTEM

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the electrical system is not adequate to support the typical functions performed in the dwelling without disruption, including appliances adequate for the type and size of the dwelling.

The Appraiser must examine the electrical system to ensure that there is no visible frayed wiring or exposed wires in the dwelling, including garage and basement areas, and report if the amperage and panel size appears inadequate for the Property. The Appraiser must operate a sample of switches, lighting fixtures, and receptacles inside the house and garage, and on the exterior walls, and report any deficiencies. The Appraiser is not required to insert any tool, probe or testing device inside the electrical panel or to dismantle any electrical device or control.

PLUMBING SYSTEM

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the plumbing system does not function to supply water pressure, flow, and waste removal.

The Appraiser must flush the toilets and operate a sample of faucets to check water pressure and flow, to determine that the plumbing system is intact, that it does not emit foul odors, that faucets function appropriately, that both cold and hot water run, and that there is no readily observable evidence of leaks or structural damage under fixtures.

The Appraiser must examine the water heater to ensure that it has a temperature and pressure-relief valve with piping to safely divert escaping steam or hot water.

If the Property has a septic system, the Appraiser must examine it for any signs of failure or surface evidence of malfunction. If there are deficiencies, the Appraiser must require repair or further inspection.

ROOF COVERING

The Appraiser must notify Smartfi of the deficiency of MPR or MPS if the roof covering does not prevent entrance of moisture or provide reasonable future utility, durability and economy of maintenance and does not have a remaining physical life of at least two years.

The Appraiser must observe the roof to determine whether there are deficiencies that present a health and safety hazard or do not allow for reasonable future utility. The Appraiser must identify the roofing material type and the condition observed in the "Improvements" section of the report.

The Appraiser must report if the roof has less than two years of remaining life and make the appraisal subject to inspection by a professional roofer.

When the Appraiser is unable to view the roof, the Appraiser must explain why the roof is unobservable and report the results of the assessment of the underside of the roof, the attic, and the ceilings.

ZONING

Zoning classifications must be residential in nature and must allow for the number of units contained in the subject property.

There are three options for zoning:

- If there is zoning, zoning compliance must be legal or legal non-conforming.
    - If zoning is legal non-conforming, we will need either appraiser confirmation that the property can be legally rebuilt "as is" if destroyed or Smartfi will require a letter from the zoning board stating that the home can be rebuilt if destroyed.
- If zoning is illegal, the file will be rejected.
- No zoning must be highest and best use of the subject property as improved.
- Commercial or Agricultural zoning: Allowed if the appraiser confirms the highest and best use is as improved, residential use is permitted and property conforms to the area. (Commercial influence is the surrounding area may still pose a marketability issue that may impact loan approval. The appraiser to provide a similar (same zoning and exterior influences) closed comparable sale to establish marketability).

NON-RESIDENTIAL USE OF PROPERTY

The non-residential portion of the total floor area may not exceed 49 percent. Total floor area refers to floor area of all residential spaces and the commercial/non-residential space.

Any non-residential use of the Property must;

- Be subordinate to its residential use, character, and appearance,
- May not impair the residential character or marketability of the Property, and

- Be legally permitted and conform to current zoning requirements.

The Appraiser must calculate the non-residential portion of any residential Property. Storage areas or similar spaces that are integral parts of the non-residential portion must be included in the calculation of the non-residential area. We will include the floor area of all outbuildings i.e., barn(s), stables, paddocks, shed(s), pole barn, etc. that support the non-residential use in order to determine that the nonresidential portion of the total floor area does not exceed 49%.

The Appraiser must comment on any non-residential use within the Property and state the percentage of the total floor area that is utilized as non-residential. The Appraiser must report whether the nonresidential usage is legal and in compliance with current zoning requirements.

Non-residential use may include commercial business, agricultural, floriculture, equestrian, livestock, poultry, fish, dairy, crops, orchards, tree farm, etc. When there is non-residential use of the property the borrower must be the individual using the property for non-residential purposes.

When the non-residential use is land use i.e., agriculture, equestrian, dog kennel, livestock, tree farm, etc. calculation of a total floor area may not be possible in order to determine property eligibility. The exterior areas i.e., acreage, riding or training arenas, riding tracks, training courses, kennels, etc. on the property that are used for or to support the non-residential use of those areas will be considered for Property eligibility.

When the appraisal or other information in the file indicates that the subject property is being used as a hobby farm the borrower's most recent 2 years federal tax returns (with all schedules) are required. Federal tax returns are required even if the income is not being used as effective income. The amount of annual income on the tax returns must support usage as a hobby. In all cases we must consider how the subject property can be utilized when non-residential use indicators are present to determine Property eligibility.

PRIVATE ROAD

If the road, street, and/or alley are private, and is not located in a PUD or Condo project that is acceptable provided that the following requirements are met:

- The subject property must be provided with safe and adequate vehicular and pedestrian access,
- The property is to be provided with an all-weather surface. An all-weather surface is a road surface over which emergency and typical passenger vehicles for the area can pass in all types of weather, and
- A recorded easement (non-exclusive and non-revocable easement without trespassing from the property to a public street) is required. If an easement does not exist then it can be created, executed by all parties, and sent for recording at the time of closing.

If a Shared driveway the above requirements must also be met.

PROPERTY LISTED FOR SALE

If the subject property is or has been listed for sale in the last 12 months, the following will be required:

- Proof of MLS Listing Cancellation/expiration; AND
- Explanation/documentation from the borrower(s) verifying that the intent is to occupy the property after refinancing and no longer wants/needs to sell the property; AND
- Prior to closing, the borrower(s) will be required to execute the Verification of Occupancy.

REMAINING ECONOMIC LIFE (REL)

Any property with less than 30 years Remaining Economic Life (REL) may be ineligible. The appraiser will need to provide a list of repairs/updates that must be completed in order for the subject property to have at least 30 years REL. Repairs/updates must be completed and an Appraisal Completion Report or Compliance Inspection Report, as applicable, is required prior to closing. If repairs/rehabilitation cannot be done prior to closing the property is not eligible.

REPAIR REQUIREMENTS

When examination of New or Existing Construction reveals non-compliance with MPR and MPS, the Appraiser must report the repairs necessary to make the Property comply, provide an estimated cost to cure, provide descriptive photographs, and condition the appraisal for the required repairs.

If compliance can only be affected by major repairs or alterations, the Appraiser must report all readily observable property deficiencies, as well as any adverse conditions discovered performing the research involved in completion of the appraisal, within the reporting form.

Any structures on the subject property must meet FHA's minimum property requirements and standards, be safe, sound, and secure, and cannot pose any health or safety issues.

This applies even if the Appraiser does not give value to an outbuilding. The Appraiser is responsible for inspecting all structures on any part of a property and is required to observe, analyze, and report.

Regardless of the Appraiser's suggested repairs, the Lender will determine which repairs are required.

Installation of smoke, carbon monoxide, double straps on hot water heaters are items that are required by local, or state code and those items must be completed and re-inspected prior to closing.

REPAIR SET ASIDE

FHA permits for a repair set aside to be established in an amount equal to 150% of the estimated cost of repairs when such required repairs do not exceed 15% of the Maximum Claim Amount.

Smartfi will use the Appraiser's cost to cure for minor repair items i.e., missing handrails, minor scraping & painting. A written estimate from a qualified contractor is required for all other required repairs i.e., roof replacement, major exterior scraping & painting. If a contractor must be licensed as per State requirements, then estimates must be from an actively licensed contractor.

REPAIRS COMPLETED PRIOR TO CLOSING

Any repairs determined to pose an immediate health/safety risk to the occupants are required to be completed prior to closing.

Repairs that are to be completed prior to closing include but are not limited to:

- Structural deficiencies that pose immediate safety issue,
- Defective paint surfaces in the home AND there are children under the age of six (6) living in the home,
- Window security bars on bedroom(s) with no safety/quick release latches,
- Missing smoke detectors,
- Missing carbon monoxide detectors,
- Hot water heater not double strapped. In addition to Alaska & California, areas of Nevada, Idaho, Wyoming, Montana, Oregon, Washington & Hawaii also fall under the Uniform Codes' seismic zones 3 & 4, where water heaters are specifically required to be anchored.
- Inadequate direct exterior egress from bedroom(s).

The property must be re-inspected prior to closing. An Appraisal Update and/or Completion Report (1004D) or Compliance Inspection Report (CIR)(Form HUD-92051), as applicable, with photos must be obtained, that certifies the required repairs are complete. Photos must be provided by the appraiser, not the borrower or any other interested party.

Items required by State law, smoke and/or carbon monoxide detectors, hot water heater double strapped, etc. must be completed prior to closing, and an Appraisal Completion Report Form 1004D or Compliance Inspection Report, as applicable, with photos is required.

REPAIR SET-ASIDES AT CLOSING

In instances where it is not otherwise prohibited, the amount necessary to complete the required repairs can be withheld from the proceeds as a repair set-aside, and then paid toward repairs within twelve (12) months.

The total cost of required repairs cannot exceed 15% of the maximum claim amount. The Repair Set Aside amount will be equal to 1.50 times (x) cost to cure/contractor estimate.

An Appraiser's cost-to-cure may be used for a set-aside if the repairs are considered minor and do not require an expert in the field. Smartfi may require contractor estimates on minor repairs if the appraiser notes he/she is not qualified to provide a cost to cure or at the discretion of the DE Underwriter.

For more detailed and/or major repairs, a contractor proposal will be required when repairs will be completed as a repair set aside i.e., foundation, roof, and/or plumbing repairs. If the Property state requires for a Contractor and/or Tradesmen (Electrician or Plumber) to be licensed, then proposals must come from a licensed Contractor/Tradesmen.

LIMITED REQUIRED REPAIRS

The appraiser must limit required repairs to those repairs necessary to:

- Maintain the safety, security, and soundness of the property,
- Preserve the continued marketability of the property, and
- Protect the health and safety of the occupants.

AS-IS CONDITION AND COSMETIC REPAIRS

The Appraiser may complete an as-is appraisal for existing Properties when minor property deficiencies, which generally result from deferred maintenance and normal wear and tear, do not affect the health and safety of the occupants or the security and soundness of the Property. Cosmetic or minor repairs are not required, but the Appraiser must report and consider them in the overall condition when rating and valuing the Property.

Cosmetic repairs include:

- missing handrails that **do not** pose a threat to safety,
- holes in window screens,
- cracked window glass,
- defective interior paint surfaces in housing constructed **after** 1978,
- minor plumbing leaks that do not cause damage (such as a dripping faucet),
- and other inoperable or damaged components that in the Appraiser's professional judgment do not pose a health and safety issue to the occupants of the house.

If an element is functioning well but has not reached the end of its useful life, the Appraiser should not recommend replacement because of age.

RURAL PROPERTIES

Special attention will be paid to rural properties.

Rural properties often have larger lot sizes, and their locations can be relatively undeveloped. As a consequence, there may be a shortage (or absence) of recent comparable sales in the immediate vicinity.

This may cause the appraiser to select comparable sales that are located a considerable distance from the subject property. In those instances, the appraiser must use his/her knowledge of the area and apply good judgment in selecting comparable sales that are the best indicators of value for the subject property. In these situations, the appraiser must include an explanation of why the particular comparable sales were selected.

Only closed (settled) sales may be used as comparable sales 1, 2, or 3. If a sale over six (6) months old is used, an explanation must be provided.

No sales over one (1) year old are permitted except as “additional comparable sales” and would be identified as comparable sale(s) 4, 5, or 6. Properties under contract may also be submitted as additional comparable sales 4, 5, or 6 to support trends or value conclusions observed.

SALES HISTORY

The appraiser is required to provide a 36-month sales history on the subject property.

The appraiser must comment on any prior transfer or sale of the subject property or comparable sale. If any transfer or sale occurred within the prior 12 months the appraiser will need to provide detailed comments for the increase in sales price when there is a significant increase in sales price, 35% or more, from the prior transfer or sale to the most recent sale. (i.e., what upgrades/renovations were completed, was prior sale an arms-length transaction, prior sale a foreclosure/short sale, etc.).

SWIMMING POOLS

The Appraiser must report readily observable defects in a non-covered pool that would render the pool inoperable or unusable. If the pool water contains algae and is aesthetically unappealing, but the Appraiser has no evidence that the pool is otherwise contaminated, no cleaning is required. Swimming pools must be operational to provide full Contributory Value.

The Appraiser must condition the appraisal report for pools with unstable sides or structural issues to be repaired or permanently filled in accordance with local guidelines, and the surrounding land re-graded if necessary.

If the swimming pool has been winterized, or the Appraiser cannot determine if the pool is in working order, the Appraiser must complete the appraisal with the extraordinary assumption that the pool and its equipment can be restored to full operating condition at normal costs.

An empty swimming pool can pose a health and safety risk. At minimum, swimming pools must comply with all local ordinances (perimeter fencing, covers, etc.) and, if empty or non-functioning, the pool must be secured by a cover that would be sufficiently sturdy to prevent a person from falling in the pool or through the cover. Non-functioning pools (and related equipment) which are not covered must be repaired.

We must obtain satisfactory evidence that any health or safety issues have been corrected prior to closing.

PUBLIC WATER SUPPLY SYSTEM

The lender must confirm that a connection is made to a public or community water system whenever feasible and available at a reasonable cost. If connection costs to the public or community system are not reasonable, the existing onsite systems are acceptable provided they are functioning properly and meet the requirements of the local health department.

WELL/SEPTIC

- Appraiser must confirm that a well and/or septic system is typical for the market area and meets FHA minimum guidelines.
- Appraisal must also comment regarding access to public utilities
- If access for hookup is available and cost is less than 3% of the appraised value, then hookup is required. If costs exceed 3% of appraised value hookup is not required. The cost estimate **MUST** be provided by a licensed contractor.
- If connection costs to the public or community system are not reasonable, the existing onsite systems are acceptable, provided they are functioning properly and meet the requirements of the local health department.
- If the appraiser is unable to identify the location of the well and/or septic system a survey may be required **OR** an inspection from a qualified individual to determine the location and separation distances from well to septic tank, well to septic drain/leach field, and well to any property line.

INDIVIDUAL WATER SUPPLY SYSTEMS

An Individual Water Supply System refers to a potable water source providing water to an individual Property.

When an Individual Water Supply System is present, water quality must meet the requirements of the health authority with jurisdiction. If there are no local (or state) water quality standards, then water quality must meet the standards set by the EPA, as presented in the National Primary Drinking Water Regulations in 40 CFR 141 and 142.

Soil poisoning is an unacceptable method for treating termites unless satisfactory assurance is provided that the treatment will not endanger the quality of the water supply.

Requirements for the location of wells for FHA insured properties are located in 24 CFR 200.26d (f) (3)

When the Appraiser obtains evidence that any of the water quality requirements are not met, the Appraiser must notify the Lender and provide a cost to cure.

Conditions for Individual Water Supplies

The Appraiser must note the deficiency of MPR or MPS if the subject Property contains a well located within the foundation walls of an existing dwelling and there is no evidence that the local jurisdiction recognizes and permits such a location, that it is common for the market area, and does not adversely affect marketability unless the well is located within the foundation walls of a New Construction dwelling in an arctic or sub-arctic region.

The Appraiser must report when water to a property is supplied by dug wells, cisterns or holding tanks used in conjunction with water purchased and hauled to the site. The Appraiser must report whether such systems are readily accepted by local market participants and that the water supply system may violate MPR or MPS.

The Appraiser must note the deficiency of MPR or MPS if the subject Property has a water source that includes a mechanical chlorinator or is served by springs, lakes, rivers, sand-point, or artesian wells.

A pressure tank with a minimum capacity of 42 gallons must be provided.

However, pre-pressured tanks and other pressurizing devices are acceptable if delivery between pump cycles equal or exceed that of a 42-gallon tank. Tanks must be equipped with a clean-out plug at the lowest point and a suitable pressure relief valve.

The Appraiser must note any readily observable deficiencies regarding the well and require test or inspection if any of the following apply:

- The water supply relies upon a water purification system due to the presence of contaminates;
- Corrosion of pipes (plumbing);
- Areas of intensive agricultural uses within one quarter (1/4) mile;
- Coal mining or gas drilling operations within one quarter (1/4) mile;
- A dump, junkyard, landfill, factory, gas station, or dry-cleaning operation within one quarter (1/4) mile; or
- An unusually objectionable taste, smell, or appearance of well water.

The Appraiser must also be familiar with the minimum distance requirements between private wells and sources of pollution and, if discernible, comment on them. The Appraiser is not required to sketch or note distances between the well, property lines, septic tanks, drain fields, or building Structures but may provide estimated distances where they are comfortable doing so. When available, the Appraiser should obtain from the homeowner or Lender a copy of a survey or other documents attesting to the separation distances between the well and septic system or other sources of pollution.

Individual Water Supply System for Minimum Property Requirements for Existing Construction

- Property line/10 feet
- Septic tank/50 feet
- Drain field/100 feet
- Septic tank drain field reduced to 75 feet if allowed by local authority

- **5** If the subject Property line is adjacent to residential Property, then local well distance requirements prevail. If the subject Property is adjacent to non-residential Property or roadway, there needs to be a separation distance of at least 10 feet from the property line.

Note: Distance requirements of local authority prevail if greater than stated above.

Water Wells Minimum Property Requirements for Existing Construction

- Existing wells must deliver water flow of 3 to 5 gallons per minute
- No exposure to environmental contamination
- Continuing supply of safe & potable water
- Domestic hot water
- Water quality must meet requirements of local jurisdiction, or the EPA is no local standard

SHARED WELLS

A Shared Well refers to a well that services two to four homes where there is a binding Shared Well Agreement between the property owners that meets FHA requirements.

If the Property has a Shared Well, the Appraiser must report it and note any readily observable deficiencies. The Appraiser must also obtain a Shared Well Agreement and include it in the appraisal report so that the Lender may review the agreement to determine eligibility. The Appraiser must also require an inspection under the same circumstances as an individual well.

Smartfi must confirm that a Shared Well:

- Serves existing Properties that cannot feasibly be connected to an acceptable public or Community Water supply System;
- Is capable of providing a continuous supply of water to involved Dwelling Units so that each existing Property simultaneously will be assured of at least three gallons per minute (five gallons per minute for Proposed Construction) over a continuous four-hour period. (The well itself may have a lesser yield if pressurized storage is provided in an amount that will make 720 gallons of water available to each connected existing dwelling during a continuous four-hour period or 1,200 gallons of water available to
- Each proposed dwelling during a continuous four-hour period. The shared well system yield must be demonstrated by a certified pumping test or other means acceptable to all agreeing parties.);
- Provides safe and potable water. An inspection is required under the same circumstances as an individual well. This may be evidenced by a letter from the health authority having jurisdiction or, in the absence of local health department standards, by a certified water quality analysis demonstrating

that the well water complies with the EPA's National Interim Primary Drinking Water Regulations;

- Has a valve on each dwelling service line as it leaves the well so that water may be shut off to each served dwelling without interrupting service to the other Properties; and
- Serves no more than four living units or Properties.

For both proposed and existing Properties, Smartfi must ensure that the shared well agreement complies with the guidance provided and include the **22 points** below:

1. Require that the agreement is binding upon signatory parties and their successors in title, recorded in local deed records when executed and recorded, and reflects joiner by any borrower holding a Mortgage on any Property connected to the Shared Well.
2. Permit well water sampling and testing by the local authority at the request of any party at any time.
3. Require that corrective measures be implemented if testing reveals a significant water quality deficiency, but only with the consent of a majority of all parties.
4. Ensure continuity of water service to "supplied" parties if the "supplying" party has no further need for the shared well system. ("Supplied" parties normally should assume all costs for their continuing water supply.)
5. Prohibit well water usage by any party for other than bona fide domestic purposes.
6. Prohibit connection of any additional living unit to the shared well system without:
   1. the consent of all parties;
   2. the appropriate amendment of the agreement; and
   3. Compliance with item 3.

7. Prohibit any party from locating or relocating any element of an individual sewage disposal system within 75 feet (100 feet for Proposed Construction) of the Shared Well.
8. Establish Easements for all elements of the system, ensuring access and necessary working space for system operation, maintenance, improvement, inspection, and testing.
9. Specify that no party may install landscaping or improvements that will impair use of the Easements.
10. Specify that any removal and replacement of preexisting site improvements, necessary for system operation, maintenance, replacement, improvement, inspection, or testing, will be at the cost of their owner, except for costs to remove and replace common boundary fencing or walls, which must be shared equally between or among parties.
11. Establish the right of any party to act to correct an emergency in the absence of the other parties onsite. An emergency must be defined as failure of any shared portion of the system to deliver water upon demand.

12. Permit an agreement amendment to ensure equitable readjustment of shared costs when there may be significant changes in well pump energy rates or the occupancy or use of an involved Property.
13. Require the consent of a majority of all parties upon cost sharing, except in emergencies, before actions are taken for system maintenance, replacement, or improvement.
14. Require that any necessary replacement or improvement of a system element(s) will at least restore original system performance.
15. Specify required cost sharing for:
    1. The energy supply for the well pump;
    2. System maintenance, including repairs, testing, inspection and disinfection;
    3. System component replacement due to wear, obsolescence, incrustation or corrosion; and
    4. System improvement to increase the service life of a material or component to restore well yield or to provide necessary system protection.
16. Specify that no party shall be responsible for unilaterally incurred shared well debts of another party, except for correction of emergency situations. Emergency correction costs must be equally shared.
17. Require that each party be responsible for:
    1. Prompt repair of any detected leak in this water service line or plumbing system;
    2. Repair costs to correct system damage caused by a resident or guest at their Property; and
    3. Necessary repair or replacement of the service line connecting the system to the dwelling.
18. Require equal sharing of repair costs for system damage caused by persons other than a resident or guest at a property sharing the well.
19. Ensure equal sharing of costs for abandoning all or part of the shared system so that contamination of ground water or other hazards will be avoided.
20. Ensure prompt collection from all parties and prompt payment of system operation, maintenance, replacement, or improvement costs.
21. Specify that the recorded agreement may not be amended during the term of a federally insured or -guaranteed Mortgage on any Property served, except as provided in items 5 and 11 above.
22. Provide for binding arbitration of any dispute or impasse between parties with regard to the system or terms of agreement. Binding arbitration must be through the American Arbitration Association or a similar body and may be initiated at any time by any party to the agreement. Parties to the agreement must equally share arbitration costs.

COMMUNITY WATER SYSTEMS

A Community Water System refers to a central system that is owned, operated, and maintained by a private corporation or a nonprofit property owners' association.

If the Property is on a Community Water System, the Appraiser must note the name of the water company on the appraisal report.

The Appraiser must report on the availability of connection to public and/or Community Water System or sewer system, and any jurisdictional conditions requiring connection.

Water Portability Testing

- Well must meet standards of local or state health authority, as applicable. If none, water must be tested for lead and acute contaminants in accordance with Mortgagee Letter 1995-34
- Water purification systems are **NOT** permitted.

Water testing is **NOT** required UNLESS:

- Mandated by state or local jurisdiction
- Well is believed to be contaminated
- Relies on purification system due to contaminants
- Unusual taste, smell, or appearance
- Corrosion in pipes
- Located within ¼ mile of intensive agricultural, coal mining, gas drilling, landfill, junk yard, factory, gas station, or dry cleaning.

ONSITE SEWAGE DISPOSAL SYSTEMS

An Onsite Sewage Disposal System refers to wastewater systems designed to treat and dispose of effluent on the same Property that produces the wastewater. The Appraiser must note the deficiency of MPR or MPS and notify Smartfi if the Property is not served by an off-site sewer system and any living unit is not provided with an Onsite Sewage Disposal System adequate to dispose of all domestic wastes in a manner that will not create a nuisance, or in any way endanger the public health.

The Appraiser must visually inspect the Onsite Sewage Disposal System and its surrounding area. The Appraiser must require an inspection to ensure that the system is in proper working order if there are readily observable signs of system failure. The Appraiser must report on the availability of public sewer to the site.

Sewage System

The Lender must confirm that a connection is made to a public or community sewage disposal system whenever feasible and available at a reasonable cost. If connection costs to the public or community system are not reasonable, the existing Onsite Sewage Disposal

Systems are acceptable provided they are functioning properly and meet the requirements of the local health department.

When the Onsite Sewage Disposal System is not sufficient and an off-site system is available, Smartfi must confirm connection to an off-site sewage system.

When the Onsite Sewage Disposal System is not sufficient and an off-site system is not available, Smartfi must reject the Property unless the Onsite Sewage Disposal System is repaired or replaced and complies with local health department standards.

DISASTER AREA DECLARATIONS

The Federal Emergency Management Agency (FEMA) announces/publishes when the President declares an area as a federal disaster area.

The full effect of an incident may not be known at the time of FEMA's initial publication, so the list of individual counties may expand as the incident progresses, and damage is re-evaluated.

The FEMA website must be checked immediately following an event, at time of approval, and prior to closing to ensure that the subject property has not been impacted. Major Disaster Declarations can be found at https://www.fema.gov/disasters

For loans that are not closed prior to the disaster declaration date where the inspection report reveals property damage, the appraisal validity period is extended from 180 days to a maximum of 1 year from the effective date of the original appraisal. In no instance will an appraisal be acceptable for a loan closing that has an effective date beyond 1 year.

Property Inspection and Condition Report

- The inspection report must be performed by an FHA approved appraiser,
- When available the FHA Appraiser that completed the appraisal report should complete the reinspection report for the disaster. If the original Appraiser is not available, then another FHA Appraiser in good standing with geographic competence in the affected market may be used may complete the re-inspection. We must provide a copy of the original appraisal report to the
- Appraiser.,
- Must have a damage inspection report that identifies and quantifies any dwelling damage, and
- FHA does not require the Appraiser to ensure utilities are on at the time of this inspection if they have not yet been restored for the area.

Declared Disaster Area Re-Inspection Requirements

All Properties with pending Mortgages or endorsements in Presidentially Declared Major Disaster Areas (PDMDA) designated for individual assistance must have a damage inspection report that identifies and quantifies any dwelling damage, and the report must be dated after the Incident Period (as defined by FEMA) or 14 days from the Incident Period

start date, whichever is **earlier**. FHA does not require a specific form for a damage inspection report. If the effective date of the appraisal is on or after the date required above for an inspection, a separate damage inspection report is not necessary.

Smartfi will attempt to keep partners updated with communication applicable to each specific disaster.

Loan not closed, "Property Inspection or Condition Report" with an interior/exterior inspection with photos is required for:

- Any property that is in a Federal Disaster Area where assistance to Individuals and households is being provided by FEMA, **AND**
- The appraisal report has an effective date that is on or before the date of the Incident period.

Note: Where a damage inspection report reveals property damage, the appraisal validity period is extended from 180 days to a maximum of one (1) year from the effective date of the original appraisal. In no instance will an appraisal be acceptable that has an effective date beyond one (1) year and a new appraisal is required.

If there is damage:

- Below $5,000 and property is habitable then we can establish a repair set aside permitting that the repair costs are within 15% of Max Claim Amount.
- Above $5,000 or the property is not habitable the repairs must be completed prior to closing.
- All damages must be repaired by licensed contractors or per local jurisdictional requirements.

All damages, regardless of amount, must be repaired and the Property restored to pre-loss condition with appropriate and applicable documentation.

Loan closed/funded but not yet insured a drive-by exterior inspection with photos is required for:

- Any property that is in a Federal Disaster Area where assistance to individuals and households is being provided by FEMA, **AND**
- The appraisal report has an effective date that is on or before the date of the Incident period.

If there is damage:

- Below $5,000 and property is habitable then complete repairs and submit for insuring.

- Above $5,000 or the property is not habitable the repairs must be completed prior to the loan being insured.
- All damages must be repaired by licensed contractors or per local jurisdictional requirements.
- All damages, regardless of amount, must be repaired and the Property restored to pre-loss condition with appropriate and applicable documentation.

Potentially Impacted Areas (not yet declared a disaster)

If an area has not yet been declared a disaster, but has been declared a state of emergency, Smartfi will publish a list of locations that must follow the Declared Disaster Area Requirements above.

As FEMA declares disaster areas, Smartfi may add or remove counties from the list that must adhere to the Disaster Area Requirements.

INSURANCE GUIDELINES

Each submission package must include proof of insurance. The policy must be effective at time of funding and be in effect for 45 days past the funding date or a renewal policy will be required.

The policy must be paid at least 60 days past closing. If the loan is closing in the name of Smartfi, all declaration pages must contain the following mortgagee clause prior to closing:

MORTGAGEE CLAUSE

Smartfi Home Loans, ISAOA/ATIMA
3636 Nobel Dr. Ste 210
San Diego, CA 92122

All declarations pages must include evidence of payment status.

Property insurance for a home mortgage must show the property is protected against loss or damage from fire and other perils covered by the standard extended coverage endorsement.

Hazard binders that limit or exclude coverage, in whole or in part, from windstorm are not acceptable unless additional insurance policy that provides coverage over wind.

GENERAL COVERAGE REQUIREMENTS

The policy must reflect:

- All borrower names (NBS names acceptable to reflect on policy)
- Correct property address (must match loan file documents)

- Effective date and Expiration date should cover 12 months and must have 60 days remaining after funding
- Dwelling coverage amounts
- Deductible
- Annual premium
- Mortgagee clause
- Loan Number

The hazard insurance dwelling coverage must be greater than or equal to the lesser of one of the following replacement amounts:

- Maximum Claim of the HECM loan
- Total Estimate of Cost New
- Appraised Value minus the Site Value
- Replacement cost estimator (RCE) provided by insurance agent.
    - Must list property address
    - Dwelling coverage must be greater than or equal to the estimated replacement cost
    - Demolition and debris removal

COVERAGE

Standard Extended Coverage Endorsement is required.

Declaration page must specifically state the policy includes wind coverage in coastal areas. Currently, 19 states, plus Washington, D.C., mandate windstorm and hurricane deductibles: Alabama, Connecticut, Delaware, Florida, Georgia, Hawaii, Louisiana, Maine, Maryland, Massachusetts, Mississippi, New Jersey, New York, North Carolina, Pennsylvania, Rhode Island, South Carolina, Texas, and Virginia.

Exclusion of earthquake coverage is permissible unless the Appraiser comments that the Property is in a seismic zone.

Policy should list "All perils" deductible. If states "covered perils" the agent will need to confirm all perils in standard HO-3 are covered. The required Perils include:

- Fire or lightning
- Windstorm or hail
- Explosion
- Riots
- Aircraft
- Vehicles
- Smoke
- Vandalism
- Theft
- Falling objects
- Weight of ice, snow, or sleet

- Accidental discharge or overflow of water or steam
- Sudden and accidental tearing, cracking, burning, or bulging
- Freezing
- Sudden and accidental damage due to short circuiting
- Volcanic Eruption

DEDUCTIBLE

Unless a higher maximum deductible amount is required by state law, the maximum allowable deductible is 5% of the face amount of the insurance policy.

Additional Requirements for Condo & PUD master policies:

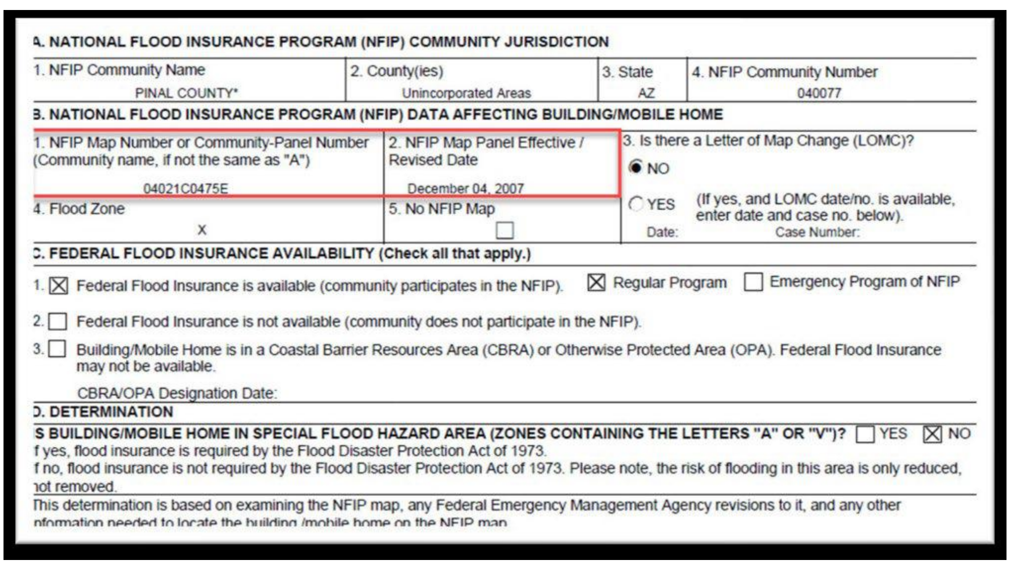
The policy must cover all the general and limited common elements that are normally included in coverage including fixtures, building service equipment, and common personal property and supplies belonging to the homeowner's association.

Commercial and general liability coverage for condominiums must be at least $1 million for bodily injury and property damage per single occurrence.

Note: Actual Cash Value policies are not acceptable.

FLOOD CERTIFICATION

A Flood Certificate is required on every loan submitted to Smartfi for underwriting. All Flood Certificates should have the National Flood Insurance Program (NFIP) map number and date completed. All Flood Certificates are good for the life of the loan:



A. NATIONAL FLOOD INSURANCE PROGRAM (NFIP) COMMUNITY JURISDICTION

1. NFIP Community Name	2. County(ies)	3. State	4. NFIP Community Number
PINAL COUNTY*	Unincorporated Areas	AZ	040077

B. NATIONAL FLOOD INSURANCE PROGRAM (NFIP) DATA AFFECTING BUILDING/MOBILE HOME

1. NFIP Map Number or Community-Panel Number (Community name, if not the same as "A") 04021C0475E	2. NFIP Map Panel Effective / Revised Date December 04, 2007	3. Is there a Letter of Map Change (LOMC)? ◉ NO
4. Flood Zone X	5. No NFIP Map ☐	◯ YES (If yes, and LOMC date/no. is available, enter date and case no. below). Date: Case Number:

C. FEDERAL FLOOD INSURANCE AVAILABILITY (Check all that apply.)

1. ☒ Federal Flood Insurance is available (community participates in the NFIP). ☒ Regular Program ☐ Emergency Program of NFIP

2. ☐ Federal Flood Insurance is not available (community does not participate in the NFIP).

3. ☐ Building/Mobile Home is in a Coastal Barrier Resources Area (CBRA) or Otherwise Protected Area (OPA). Federal Flood Insurance may not be available.

CBRA/OPA Designation Date:

D. DETERMINATION

IS BUILDING/MOBILE HOME IN SPECIAL FLOOD HAZARD AREA (ZONES CONTAINING THE LETTERS "A" OR "V")? ☐ YES ☒ NO

If yes, flood insurance is required by the Flood Disaster Protection Act of 1973.

If no, flood insurance is not required by the Flood Disaster Protection Act of 1973. Please note, the risk of flooding in this area is only reduced, not removed.

This determination is based on examining the NFIP map, any Federal Emergency Management Agency revisions to it, and any other information needed to locate the building /mobile home on the NFIP map.

When an area has not been mapped, or if NFIP is not available, the following chart may be used to verify if a property is eligible:

Mapping Refer to box 1, 2 or 5	Flood Zone Refer to box 4	NFIP Participation Refer to boxes C1 & C2	Eligible Property?
Mapped	In a flood zone	NFIP Available	Eligible
Mapped	In a flood zone	NFIP Not Available	Ineligible
Mapped	Not in a flood zone	NFIP Not Available	Eligible
Not Mapped	Undetermined	NFIP Available	Lender Discretion
Not Mapped	Undetermined	NFIP Not Available	**Manufactured:** Ineligible **Stick-built:** Lender Discretion

The Underwriter will review the flood zone and flood insurance availability sections on every flood certificate. If the property is located within a SFHA and the National Insurance Program (NFIP) is not available within the community, the property is not eligible.

If the chart above indicates "Lender Discretion" the underwriter will review the area for local bodies of water, annual rain fall, last flood, and availability of NFIP coverage to determine if the property is eligible. Flood certification must not be expired as of funding date and should reflect Smartfi Home Loans as the Lender if the closing will be in our name. If property is in a special flood hazard area, indicated by Flood Zones containing the following designations: A, AO, AH, A1-30, AE, A99, VO or V1-30, VE or V, these zones require flood insurance.

Note: Properties within zones B and C do NOT require flood insurance.

FLOOD INSURANCE

The flood certification determines whether flood insurance is needed, and if so, whether flood insurance is available. When required, the flood policy must reflect:

- Policy is a National Flood Insurance Program (NFIP) policy
- All borrower names (NBS names acceptable to reflect on policy)
- Correct property address (must match loan file documents)
- Effective date and Expiration date (must have 60 days remaining after funding)
- Dwelling coverage amounts
- Deductible
- Annual premium
- Mortgagee clause
- Loan Number

For properties in Flood Zones A, AO, AH, A1-30, AE, A99, VO or V1-30, VE or V:

- If the Borrowers do not currently have flood insurance, a new policy must be obtained.
- The disclosure entitled "Notice to a Borrower in a Special Flood Hazard Zone" must be signed & dated by the Borrower at least ten days prior to loan closing.
- Adequate proof of insurance is required before the loan is cleared to close.
- The Borrower must provide a copy of the declarations page showing the appropriate insurance coverage.

If the loan is closing in the name of Smartfi, the mortgagee clause must reflect the following loss payee endorsement and the loan number:

MORTGAGEE CLAUSE

Smartfi Home Loans, ISAOA/ATIMA
3636 Nobel Dr. Ste 210
San Diego, CA 92122

GENERAL COVERAGE REQUIREMENTS

The policy must be a National Flood Insurance Policy (NFIP). The policy must be effective at time of funding and be good through 60 days past the funding date or the renewal will be required. The flood insurance must be greater than or equal to one of the following replacement amounts, up to the maximum allowable NFIP limit of $250,000:

- Maximum Claim of the HECM loan
- Total Estimate of Cost New Maximum Deductible: The lesser of $5,000.00 or 5% of the coverage amount.

Note: Manufactured homes located in a flood zone, or a partial flood zone are ineligible.

See chart below for additional info regarding special circumstances:

	New / Proposed Construction	Existing Construction	Manufactured Homes	Condo Projects	All Other Properties
Life-of-Loan flood zone determination certificate	Required	Required	Required	Required	Required
Property within Coastal Barrier Resource System (protected areas)	Ineligible for FHA insurance	Ineligible for FHA insurance	Ineligible for FHA insurance	Ineligible for FHA insurance	Ineligible for FHA insurance
Property within Special Flood Hazard Areas (SFHA)	Ineligible for FHA insurance	Adequate flood insurance for term of loan. If National Flood Insurance Program (NFIP) insurance is not available, property is ineligible.	Ineligible for FHA insurance	Adequate flood insurance for term of loan. If National Flood Insurance Program (NFIP) insurance is not available, property is ineligible.	Adequate flood insurance for term of loan. If National Flood Insurance Program (NFIP) insurance is not available, property is ineligible.
Exceptions	**New / Proposed Construction**	**Existing Construction**	**Manufactured Homes**	**Condo Projects**	**All Other Properties**
Letter of Map Amendment (LOMA) or Letter of Map Revision (LOMR)	Property is eligible for FHA insurance. No flood insurance required	No flood insurance required.	Property is eligible for FHA insurance. No flood insurance required.	No flood insurance required.	No flood insurance required.
FEMA National Flood Insurance Program (NFIP) Elevation Certificate (FEMA Form 81-31) indicating property is above Base Flood Elevation.	Property is eligible for FHA insurance. Flood insurance is required if property is in SFHA.	Flood insurance is required if property is in SFHA.	Loan is ineligible. Urban does not lend on Manufactured Homes in a flood zone.	Flood insurance is required if property is in SFHA.	Flood insurance is required if property is in SFHA.

Note: It is acceptable for New Construction to be in a flood zone if we can be provided with an Elevation Cert that confirms the lowest portion of the structure, including basement (if applicable) is above the 100-year flood plain.

HECM FOR PURCHASE PROGRAM

For purchase transactions only, the Maximum Claim Amount will be the lesser of the final appraised value (as determined by the DE Underwriter), sales price or FHA HECM National Mortgage Limit.

BUYER ELIGIBILITY

- All HECM borrowers must be listed as buyers on the sales contract.
- If there is a non-borrowing spouse on the loan, s/he may be listed as a buyer on the purchase contract, but this is not a requirement.
- Any party listed as a buyer on the purchase contract who will also be vested on title may remain a buyer on the purchase contract even if they will not be a borrower.
- If a person listed as a buyer on the purchase contract will not be a vested owner of the property, an addendum to the purchase contract will be required to remove this person from the contract.

PROPERTY ELIGIBILITY

The following property types are eligible for FHA insurance under the HECM Purchase Program:

- Single family
- FHA approved condominiums
- 2-4-unit properties where the borrower(s) will occupy one of the units as an owner-occupant
- Manufactured homes

Eligible property types must meet the following criteria:

- A valid h4p has been issued prior to the close of the loan to certify that construction has been completed as defined in 4000.1
- The property is held as fee simple
- The purchase transaction will be an arm’s length transaction

The property must not have transferred in the 90 days prior to the date of the real estate purchase contract (subject to exceptions as outlined in Section Property Flipping / Seasoning)

TERMITE REQUIREMENTS

For New Construction and/or Construction Completed in the last year, unless shown on HUD’s published list, Termite Treatment Exception Areas, the following is required regarding termite inspections:

- Builder is required to complete form NPMA 99A: Subterranean Termite Protection Builder’s Guarantee
- If the Builder indicates on the NMPA 99A that a pest control company applied treated (see box 1), form NPMA 99B: New Construction Subterranean Termite Service Record will also be required.
- If the building is constructed with steel, masonry or concrete building components with only minor interior wood trim and roof sheathing, no treatment is needed but the builder must note on the NPMA 99A form that the construction is masonry, steel or concrete and sign and date the form.

REQUIRED DOCUMENTATION FOR HECM FOR PURCHASE (H4P)

- Fully executed purchase contract with all addenda:
    - all signature lines must be signed and dated within compliance.
- Amendatory/Escape Clause & Real Estate Certification: these disclosures can be an addendum to the sales contract, included in the sales contract (exact verbiage required) or available in the application package. Both forms must

be signed and dated by all parties prior to the note date. The parties can sign separate forms if all parties sign on, or before, the note date.

    - The purpose of the Amendatory/Escape Clause is to expressly give the buyer an out if the property does not appraise for the sales price. It also requires the seller to give the buyer notice of any changes to the property. This form is signed again at closing to certify that there were no changes to the terms of the sale that were not fully disclosed to all parties, including the lender and FHA, and that there are no separate agreements outside of the closing.

- Lead Based Paint seller's disclosure & Important Notice to Homebuyer
- Seller's Property Condition Disclosure: provided by the realtor and signed by the selling party, if required per the real estate purchase contract
- Schedule of Real Estate Disclosure: must reflect all properties owned, including the departure residence
- Valid source and paper trail of funds to close
- Earnest money deposit (EMD): Copies of cancelled checks and/or wire receipts for all deposits (including construction deposits) that will be applied toward the purchase price balance (must match cumulative deposits per the purchase contract & amount per estimated HUD)
- Verification of EMD: required only if cumulative deposits exceed 1% of the sales price.
- NMPA 99A&B forms as applicable (see Termite Requirements for New Construction)
- Credit Report: borrower(s) CANNOT currently be late on any FHA insured mortgage tied to the retained residence or any other property. Late payments must be brought current before closing.
- If the sales price exceeds the appraised value, the borrower(s) must write a letter acknowledging that the appraised value is less than the sales price and express their intent to proceed with the HECM for Purchase at the sales price. DE Underwriter to determine eligibility
- Copy of Estimated HUD from subject transaction to ensure no seller credits/incentives
- Copy of Grant Deed to confirm new vesting

INSPECTIONS

A home or pest inspection is not typically required unless requested at underwriter discretion or when required by any of the following:

- State regulations
- Signed Purchase Contract
- Appraiser

If any of the above applies, or if the contract or HUD indicate that the borrower opted for a home or pest inspection, the inspection report must be provided to us for review and repairs may be required.

CLOSING COSTS – BUYER/SELLER RESPONSIBILITIES

The borrower must pay for all closing costs typically associated with purchasing a property and obtaining financing, and the seller must pay for all costs typically associated with selling a property. Fees required to be paid by a seller under state or local law or customarily paid by a seller in the subject property locality, including real estate agent commissions or fees, and the purchase of the Home Warranty policy by the seller are already permitted under 24 CFR 206.44(c) (1) and will be excluded from the six percent interested party contribution limit.

INTERESTED PARTY CONTRIBUTIONS

Interested Parties refer to sellers, real estate agents, builders, developers, Mortgagees, Third-Party Originators (TPO), or other parties with an interest in the transaction.

Interested Party Contribution refers to a payment by an Interested Party or combination of parties, toward the Borrower's origination fees, other closing costs including any items Paid Outside Closing (POC), prepaid items, and Discount Points.

(b) Standard

Interested Parties may contribute up to 6 percent of the sales price toward the Borrower's origination fees, other closing costs, prepaid items, and Discount Points. The 6 percent limit also includes:

- Interested Party payment for permanent and temporary interest rate buydowns; and
- payment of the IMIP.

Exceptions

Premium Pricing credits from the Mortgagee or TPO are excluded from the 6 percent limit provided the Mortgagee or TPO is not the seller, real estate agent, builder, or developer.

PERSONAL PROPERTY

Any personal items beyond the "typical and customary" items may require a third (3rd) party estimate, and reduction from lenders accepted sales price. Exceptions to this rule include fridge, oven, range, dishwasher, washer/dryer, or any item that would cause damage to remove.

Alternately, if the buyers do not wish to obtain a 3rd. party estimate, personal property may also be removed from the purchase contract via a fully executed addendum.

OCCUPANCY REQUIREMENT

The HECM Borrower has 60 days from the close of escrow to occupy the dwelling.

BANKRUPTCY CHAPTER 7 & CHAPTER 13

Chapter 7

Bankruptcy (liquidation) does not disqualify a mortgagor from consideration for a HECM for purchase if, at the time of case number assignment, at least two years have elapsed since the date of the bankruptcy discharge.

- During this time, the borrower must have:
  - re-established good credit; or
  - chosen not to incur new credit obligations.
- An elapsed period of less than two years, but not less than 12 months, may be acceptable, if the borrower:
  - can show that the bankruptcy was caused by Extenuating Circumstances beyond the borrower's control; and
  - has since exhibited a documented ability to manage his or her financial affairs in a responsible manner.

If the credit report does not verify the discharge date or additional documentation is necessary to determine if any liabilities were discharged in the bankruptcy, Smartfi must obtain the bankruptcy and discharge documents.

Smartfi must also document that the borrower's current situation indicates that the events which led to the bankruptcy are not likely to recur.

Chapter 13

Bankruptcy does not disqualify a mortgagor from consideration for a HECM for purchase if at the time of case number assignment at least 12 months of the pay-out period under the bankruptcy has elapsed.

Smartfi must determine:

- Payment performance has been satisfactory and on time
- File contains written permission from the court to enter a HECM for purchase transaction.
- If the court ordered payoff of chapter 13, this cannot be paid as a mandatory obligation.
  - Borrower must pay off with properly sourced and seasoned funds

Smartfi must include the payment amount in the court-approved payment plan in the borrower's expenses when calculating residual income.

If the credit report does not verify the discharge date or additional documentation is necessary to determine if any liabilities were discharged in the bankruptcy, Smartfi must obtain the bankruptcy and discharge documents.

Smartfi must also document that the borrower's current situation indicates that the events which led to the bankruptcy are not likely to recur.

REPAIRS

All repair items noted in the appraisal and/or termite inspection must be completed prior to closing. The seller will typically pay for repairs. Repair set-asides are not allowed on the HECM for Purchase program.

For new construction, Smartfi must obtain a copy of the CO or its equivalent issued by the local jurisdiction, ICC, RCI, or CI.

Existing Less than One Year

For Properties in the Existing Less than One Year status at time of appraisal, Smartfi must obtain one of the following prior to closing and provide the applicable documentation in the case binder:

- copy of the CO (or equivalent); or
- a final inspection issued by the local authority with jurisdiction over the Property or by an ICC certified RCI or CI; or
- in the absence of such ICC certified RCI or CI, the Mortgagee may obtain a final inspection performed by a disinterested third-party, who is a registered architect, a structural engineer, or a qualified trades person or contractor, and has met the licensing and bonding requirements of the State in which the property is located.

PROPERTY FLIPPING (SEASONING)

To be eligible for FHA financing, any re-sale of a property may not occur 90 or fewer days from the last sale date of the property. FHA defines the seller's date of acquisition as the date of settlement on the seller's purchase of that property. The resale date is the date of execution of the sales contract by the buyer that will result in a mortgage to be insured by FHA.

EXCEPTIONS TO 90-DAY RESTRICTION

The following sales are exempt from the time restrictions:

- Sales by HUD of its Real Estate Owned

- Sales by other United States Government agencies of single-family properties pursuant to programs operated by these agencies.
- Sales of properties by nonprofits approved to purchase HUD-owned single-family properties at a discount with resale restrictions.
- Sales of properties that are acquired by the sellers by inheritance.
- Sales of properties purchased by employers or relocation agencies in connection with relocations of employees.
- Sales of properties by state and federally charted financial institutions and Government Sponsored Enterprises.
- Sales of properties by local and state government agencies.
- Upon FHA's announcement of eligibility in a notice, sales of properties located in areas designated by the President as federal disaster areas, will be exempt from the restrictions of the property-flipping rule. The notice will specify how long the exception will be in effect and the specific disaster area affected.

If the resale date is between 91 and 180-days following acquisition by the seller, the lender is required to obtain a second appraisal from another appraiser if the resale price is 100 percent or more over the price paid by the seller when the property was acquired. If the Lender suspects the senior has become a victim to a Property Flipping scam, the Processing and Underwriting Division of the local HOC should be contacted.

ASSET VERIFICATION (FUNDS TO CLOSE)

Prior to closing, Smartfi requires verification of the source of all funds needed to close. Borrower funds will be applied to satisfy the difference between the HECM principal limit and the sale price and mandatory obligations for the property plus any HECM loan related fees that are not financed into the loan.

The earnest money deposit will be deducted from the required funds to close once evidence has been if escrow is in receipt of the EMD and that all checks have cleared.

Smartfi requires 2 months of bank statements, or a 60-day transaction history paired with a recent bank statement for all sources of funds to close.

Note: Deposits must be sourced and properly paper trailed.

ACCEPTABLE SOURCE OF FUNDS

Prospective borrowers must use their own funds (funds obtained from sale of assets, sale of current home, and sale of personal property) or gift funds for the required funds to close.

Acceptable sources in funds to close may include, but are not limited to:

- Checking/Savings accounts
- Cash on Hand

    - Smartfi must verify that the borrower’s cash on hand is deposited in a financial institution.
    - Smartfi must obtain an explanation from the Borrower describing how the funds were accumulated and the amount of time it took to accumulate the funds.
- Business checking/savings accounts, only if:
    - Borrower is 100% owner of business and evidence of this is documented
    - CPA letter is provided stating use of funds will not negatively affect the business in anyway
- Certificates of deposits – must be liquidated
- Stock, Bonds, Mutual Funds – most must be liquidated
- Sale of borrower owned Real Estate
- Gift funds
- Sale of Personal Property – requires adequate paper trail
    - Proof borrower owns personal property (copy of title, receipt from purchase etc.)
    - Third party valuation
    - Copy of fully executed bill of sale
    - Copy of check from buyer to seller
    - Proof funds deposited to borrower’s account
- Savings Bonds – must be liquidated
- IRA’s - most must be liquidated, not borrowed against
- 401(k) and Keogh Accounts - most must be liquidated, not borrowed against
- Thrift Savings Plans - most must be liquidated
- Life Insurance Policies – must be fully surrendered, not borrowed against

When borrower(s) are required to bring funds to the closing table, regardless of the amount that is needed, satisfactory documentation must be obtained to ensure the borrower(s) have sufficient and acceptable funds.

A family member entitled to the commission may provide commission as a Gift, in compliance with the standard gift requirements.

A Borrower who also serves as the licensed real estate agent on a HECM for Purchase transaction may use the real estate commission to satisfy the required monetary investment.

Smartfi must verify and document that the borrower, or family member giving the commission a Gift, is a licensed real estate agent, and is entitled to a Real Estate Commission from the Sale of the Subject Property being purchased.

Note: For jointly held accounts with someone other than a co-borrower, Smartfi requires a signed letter from that individual stating the borrower has 100% access to the funds in their joint account (must list bank and acct number).

INELIGIBLE SOURCE OF FUNDS

The following funding sources MAY NOT be used:

- Bridge Loan/Gap Financing
- Loan(s) against other real estate owned (REO)
- Subordinate liens
- Personal/Unsecured Loans
- Cash withdrawals from credit cards
- Seller financing
- Any other lending commitment
- Loans against borrower(s) assets (401k accounts, life insurance policies, brokerage accounts)
- Sweat Equity
- Trade Equity
- Rent Credit
- Down payment assistance programs (DAP)
- Cash or its equivalent, in whole or in part, from the following parties, before, during, or after loan closing:
  - The seller or any other person or entity that financially benefits from the transactions
  - Any third (3rd) party or entity that is reimbursed, directly or indirectly, by any of the parties described in the previous bullet
- Foreign funds

BRIDGE LOAN/GAP FINANCING

HECM Borrowers may not obtain a bridge loan (also known as "gap financing") or engage in other interim financing methods to meet the monetary investment requirement or payment of closing costs needed to complete the transaction.

This restriction includes, but is not limited to:

- Subordinate liens
- Personal loans
- Loan discount points
- Interest rates buy downs
- Closing cost assistance
- Builder incentives
- Gifts or personal property given by the seller or interested parties related to the transaction (i.e., real estate agents, builder, etc.)
- Cash withdrawals from credit cards
- Seller financing
- Any other lending commitment that cannot be paid off (satisfied) at closing with seasoned funds
- Maximum Claim Amount Calculation

GIFT FUNDS

If the funds are gifted, the transfer of the funds from the donor to the Borrower must be documented.

Acceptable donors include:

- A relative of the borrower
- The employer of the borrower; documentation to support this relationship is required.
- A close friend with a clearly defined and documented interest in the borrower.
    - Documentation to support this relationship is required.

Donor deposits funds into borrower’s account prior to closing

- Donor provides:
    - Most recent bank statement prior to date of check showing donor had sufficient funds for the gift.
    - Copy of cancelled check/wire receipt/withdrawal slip showing amount & source of funds being gifted. In cases where the donor provides the funds in the form of a cashier's check, provide a withdrawal slip showing the donor's account number along with a copy of the cashier's check
- Borrower provides:
    - Copy of bank statement and/or transaction history showing deposit of funds from donor as well as available balance
- Additional requirements:
    - Fully executed gift letter

Donor provides funds directly to escrow

- Donor provides:
    - Most recent bank statement prior to date of check showing donor had sufficient funds for the gift.
    - Copy of cancelled check/wire receipt/withdrawal slip showing amount & source of funds being gifted. In cases where the donor provides the funds in the form of a cashier's check, provide a withdrawal slip showing the donor's account number along with a copy of the cashier's check
- Additional requirements:
    - Evidence escrow has received the funds from the donor’s verified account
    - Fully executed gift letter

Gift Letter Requirements

The loan file must also contain a gift letter specifying the following items:

- The dollar amounts
- The name of the donor
- The name of the donor's bank and account number
- The donor's signature
- The donor's address
- The donor's telephone number
- The donor's relationship to the Borrower
- The names of the Borrowers and their signatures
- That no repayment is required

Note: In the case of a HECM Purchase transaction, the funds cannot have been made available to the Borrower or donor from any person or entity with an interest in the sale of the property.

DEPARTURE PROPERTY

A departure property exists when the borrower(s) intends to retain their existing primary residence as a rental property. To qualify the borrower(s) must:

- Continue to make the mortgage payment, taxes, insurance, HOA dues, and special assessments on the existing mortgage.
- Be relocating to an area more than 100 miles from borrower's primary residence.
- File must contain documented mortgage payment, property tax, insurance, and homeowners' association (HOA) dues to be included in financial assessment.

If rental income is being derived from the property being vacated by the borrower, and used to qualify, the borrower must provide the following documents:

- A lease agreement of at least one year's duration after the mortgage is closed **and**;
- Evidence of the security deposit or first month's rent
- An appraisal of the departure property dated no more than 120 days old at time of disbursement, evidencing current market rents, and a minimum of 25% equity.
    - The appraisal of the departure property must be completed on the appropriate form, **and**
    - The appraisal does not have to be completed by an FHA roster appraiser.

Note: Example of appraisal form, for single family residence, a 216/1007.

To calculate the income from the subject property, the lender must use the lesser of:

- The monthly operating income reported on Fannie Mae Form 216, or
- Seventy-five percent (75%) of the lesser of:
  - Fair market rent reported by the appraiser.
  - The rent reflected in the lease or other agreement.

BORROWER SELLING CURRENT RESIDENCE

- If the sale is closing prior the closing of the HECM for Purchase, a final, fully executed HUD-1 Settlement Statement/Closing Disclosure will be required prior to closing.
- If proceeds from the sale of the current residence are being used for closing funds on the HECM for Purchase, we require copies of disbursement checks and/or wires.
- Depending upon the timing from sale of the current residence to closing of the HECM for Purchase evidence of deposit of sale proceeds may be required.
- If the sale will not close before the closing of the HECM for Purchase, follow the "Borrower Retaining Current Residence" guidelines above.
- A satisfactory 24-month property charge payment history (taxes, HOA dues, ground rent) evidencing no payments made in arrears.

Note: If the borrower has an existing FHA-insured loan on his/her primary residence, it must be satisfied prior to or simultaneously to the closing on the subject property.

BUY AND BAIL

Buy and bail is **buying** a new home with the intention of **bailing** on the old home. This practice is considered unacceptable and is typically done as a result of the borrower not making payments on their current residence. If a buy and bail is discovered, either at the time of the loan application or during the loan process, the result is an automatic loan decline. This practice is unacceptable, and it renders the loan uninsurable by FHA.

LAND CONTRACTS

A "land contract" (sometimes known as a "contract for deed," "agreement for deed," "land installment contract" or an "installment sale agreement") is a contract between a seller and buyer of real property in which the seller provides financing to buyer to purchase the property for an agreed-upon purchase price.

If the borrower(s) will use HECM proceeds to complete payment on a land contract, contract for deed, or other similar type financing agreement in which the borrower(s) do not have title to the property, the new mortgage **MUST** be processed as a HECM for Purchase.

Equity in the property (original sales price minus the amount owed) may be used for the borrower(s) down payment.

The following documentation must be obtained:

- Copy of the **Recorded**, fully executed, Land Contract. It must be recorded.
- Satisfactory evidence of the last 12 months of payments.:
    - 12 months cancelled checks (front & back),
    - copy of 12 months bank statements showing direct withdrawal,
    - 12-month payment receipt history from CPA/Legal Counsel/Managing Agent.

Obtaining a written statement from the Seller(s) or Seller(s) agent will not be sufficient. It must be supported by adequate documentation.

Sales Price

If the sales price exceeds the appraised value, the borrower(s) must write a letter acknowledging that the appraised value is less than the sales price and express his/her/their intent to proceed with the HECM for Purchase at the sales price.

Land Contract-Refinance

If the land contract is recorded on title and the borrower is already vested on title, the loan must originate as a refinance transaction.

STATE SPECIFIC REQUIREMENTS

The following is a list of some states and their basic state requirements. Additional requirements for the below states and other states may be required once file has been completely underwritten.

CALIFORNIA

- State Specific Counseling Requirements regarding CA Cooling Off Period.
- Carbon Monoxide Detector and Smoke Detectors are required
- Water heaters are required to be double strapped per CA Code
- Reverse Mortgage Worksheet Guide & Important Notice to Reverse Mortgage Loan Applicant disclosures are required to be given to borrower(s) prior to receiving counseling.

FLORIDA

- Survey Affidavit will be required to be fully executed at close.
- Estimator is acceptable to provide evidence of sufficient coverage where current policy does not meet Smartfi requirements for minimum dwelling coverage.

ILLINOIS

- Cooling Off Period, once commitment is signed, the loan cannot close for three business days (excluding Saturday). The day starts when borrower signs the disclosure. This requirement cannot be waived.

MARYLAND & DISTRICT OF COLUMBIA

Maryland and the District of Columbia require the following be sent to the borrower:

- Financing agreement: to be provided to the borrower at the time of application.
- Loan commitment: to be provided to the borrower by the closing department after the file has been cleared for docs. There is a three-day rescission period that will apply from the time the commitment is sent to the borrower to the time the loan funds.

> **Note:** ***This is only applicable for Purchases. Refinances only require the commitment letter to be included in the doc package*.**

MINNESOTA

- Counseling must be done before application.
- The state of Minnesota requires that we provide the borrower(s) with a commitment letter and there is a 7- day cooling off period from the date that the borrower(s) execute the MN Cooling Off Disclosure sent with the commitment letter until the closing can occur.
- There is a 7-day cooling off period from the date that the borrower(s) execute the commitment letter.

NEW MEXICO

- Survey required

OHIO

- Survey Affidavit will be required to be fully executed at close.

SOUTH CAROLINA

Proof that The Advisability of Counseling Notice has been given to the borrower(s) upon initial contact from the borrower(s) is required.

The Attorney and Insurance Preference Form must be signed and dated prior to closing.

TEXAS

- INBS is currently acceptable.
- ENBS is not acceptable.
- If the borrower(s) counseling is completed outside 180 days at the time of closing, re-counseling is required, and the borrower(s) are required to wait a minimum of 5 days after the re-counseling was completed in order to close.
- Confirm the T-19 endorsement and T-47 affidavit are issued at the close of escrow for all SFR's, PUD's, and Manufactured Homes.
- Important Notice to Borrower(s) – mandatory 12 calendar day waiting period between date the disclosure is signed by all borrowers and the date of closing.
- Review of the Title and closing package are required by an Attorney that is licensed in the state of Texas.
- Cannot close in Trust or Life Estate.

UTAH

- The state of Utah requires that we provide the borrower(s) with a commitment letter.
- There is a 5-day cooling off period from the date that the borrower(s) execute the commitment letter.

REVISION HISTORY

DATE	REVISIONS MADE
1/27/2025	Max Claim increased
	New section: legally blind signature requirements.
	Note added to Insurance, Actual Cash Value policies are not allowed