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Full-HELOC Guidelines

Effective 11/23/2023

Below are Underwriting Guidelines for Prime HELOC and Expanded HELOC.

Part Ⅰ ——Prime HELOC

COMPLIANCE WITH LAWS/REGULATIONS

These guidelines are intended to be consistent with all applicable legal and regulatory requirements regarding their subject matter.

STANDALONE HOME EQUITY UNDERWRITING STANDARDS

Prior to consummation, the underwriter must make a reasonable and good faith determination of the consumer's ability to repay the loan. This determination must be based on a consideration of the consumer's current or reasonably expected income, debt obligations, and assets (other than the value of the subject property) so that a monthly debt-to-income ratio or a monthly residual income amount, as appropriate, can be calculated.

All applications require manual underwriting. No automated underwriting systems (AUS) will be used for standalone home equity transactions.

All documentation submitted with the loan file is subject to review and may be considered during underwriting for qualification purposes regardless of the minimum documentation requirements addressed within these guidelines.

UNDERWRITING CONSIDERATIONS OUTSIDE OF STANDARD GUIDELINES

It is the responsibility of the underwriter to confirm that the credit underwriting information entered into the system is correct, that resources utilized are current and valid, and the decision is adequately supported as outlined within this document.

AAA Lendings reserves the right to reject any loan, regardless of the AUS response when applicable. AAA Lendings will evaluate all aspects of the loan file, including but not limited to, LTV/CLTV, ratios, program parameters, reserves, credit, property type and value. Although no one area of a particular loan may be weak enough to merit a denial, a compilation of several weak areas with no or limited strength to compensate can be sufficient to deny.

A loan file may be submitted to AAA Lendings for an exception to the guidelines. The exception can be reviewed only by a designated employee of the bank on a case by case basis depending on the overall loan file.

LOAN PURPOSE

Standalone Home Equity Lines of Credit (HELOC) are secured loans allowing individuals to refinance or obtain equity from a residential property.

SEGREGATION OF DUTIES

The person who originates the loan application cannot be the person making the credit decision. Applications will be taken by authorized personnel or via online banking. All credit decisions will be made by the Underwriting Department.

LOAN INTEGRITY

It is the responsibility of AAA Lendings to protect borrowers, our own company, investors, and insurers from becoming victim to mortgage fraud. Mortgage fraud is generally categorized as one of the following: fraud for housing, fraud for profit, or fraud for criminal enterprise. While the presence of one or more red flags in a file does not necessarily mean that there is fraudulent intent by parties involved in the transaction, red flags indicating a material misstatement, misrepresentation, or omission of information in relation to a mortgage loan, relied upon by AAA to meet the guidelines, must be addressed accordingly during the origination process.

LOAN VERIFICATIONS

All Verifications of Deposit (VOD), Verbal Verifications for Employment (VVOE), Written Verifications of Employment (WVOE [form 1005]), and Verifications of Mortgage or Rent (VOM) must be sent directly by the lender and received back directly to the lender without being transmitted through the applicant or any other party. We do not allow verifications to be hand carried. AAA Lendings reserves the right to verbally verify the information on a VVOE, WVOE, VOM or VOD with the borrower's employer/asset holder.

PRODUCT DESCRIPTIONS AND RATE SHEETS

Access the *Product Guidelines* page and *Price Indicator Sheets* on AAA TPO Portal for the most current product descriptions and rates.

LOAN REGISTRATION/LOCK

Refer to *Loan Registration and Locking a Loan* for registration and lock procedures. The addition or deletion of a borrower, a program change or a loan parameter change (loan amount, LTV, etc.) does not require an existing non-closed loan to be re-registered.

ADVERSE ACTION

A loan placed in a final HMDA status of Denied, Withdrawn or Cancelled may not reactivated. A new loan application must be submitted along with all the required documentation.

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ADJUSTABLE RATE MORTGAGE (ARM) DISCLOSURE

Per Federal Regulation Z it is required that an ARM disclosure is provided at time of application, or if application is taken by telephone or through a broker, must be mailed or delivered within 3 business days following receipt of application. In order to comply with this regulation, Underwriting will condition for the ARM disclosure prior to closing.

ELIGIBILITY

<u>GENERAL REQUIREMENTS</u>

AAA Lendings is committed to the fair and equal evaluation of credit applications. Discrimination based on the basis of the following factors is prohibited and will not be tolerated: race, color, religion, national origin, sex, marital status, family status, age (provided the applicant has the capacity to contract), disability status, sexual orientation, the fact that all or part of an applicant's income derives from any public assistance program or the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act (including Truth-in-Lending, Equal Credit Opportunity, Fair Housing Act, Fair Credit Reporting, Fair Debt Collection Practices and Consumer Leasing Acts.)

AAA Lendings will not lend to the following:

- Individuals and/or entities identified by the Office of Foreign Assets Control (OFAC) as prohibited.

- Irrevocable trusts
- Corporations, partnerships, estates or Life Estates, and Not-for-Profit Organizations, Schools, or Churches
- Non-resident aliens (i.e., foreign nationals)
- Persons with no legal residency status in the U.S.

ELIGIBLE BORROWERS

An applicant is defined as an individual who applies for secured financing with the obligation of paying the debt in full, with interest. A borrower is defined as the individual obligated to repay the secured loan in full, with interest. AAA Lendings will lend to the following for real-estate transactions:

- Individuals of legal age
- U.S. citizens
- Lawful Permanent and Non-Permanent Resident Aliens

BORROWER(S) AGE

The Borrower must have reached the age at which the mortgage note can be legally enforced in the jurisdiction in which the property is located. There is no maximum age limit for a borrower. All applicants are evaluated on their ability to meet our underwriting guidelines.

PERMANENT RESIDENT ALIEN

A permanent resident alien (immigrant) is an individual who is lawfully accorded the privilege of residing permanently in the United States. Permanent Resident Aliens must be employed in the U.S. for the last 12 months and document lawful residency as follows:

Documentation and Expiration

Permanent Resident Alien status must be documented with a copy of the borrower(s)' green card.

- Conditional 2-year green card- borrower must provide evidence of petition for permanent resident status if the card is expiring within 90 days of the application.
- Permanent green card with 10-year renewal- If the green card contains an expiration date, and will expire within 6 months of the application, the borrower must provide evidence of filing an I-90 form to replace the card. Note: an expired 10-year green card does not, in itself, impact the borrower's status to lawfully reside in the United States.

Refugees and Asylum Status

Refugees and others seeking political asylum, who are immigrating to and seeking permanent residency in the United States, are classified under the permanent resident alien status. The INS has special immigration programs that enable these individuals to seek and accept employment while they are in the process of obtaining their permanent resident alien status, which generally will take from two to three years.

Documentation and Expiration

- Refugees and asylees may provide valid form I-94 with the indicator of refugee or asylum admission status and copy of EAD card showing classification of A03 through A05.
- Refugee and Asylum status- If an EAD card expiration is within six months of the application the borrower must show evidence they have applied for an extension

DACA Status
For borrower's with DACA, a work status that is under a deferred action, an unexpired employment authorization status (EAD Card C33) is required.

Citizens of U.S. Territories
For Citizens of Micronesia, Marshall Islands or Palau, an unexpired employment authorization status (EAD Card A08) is required.

NON-PERMANENT RESIDENT ALIEN
Due to the inability to compel payment or seek judgment, transactions with individuals with diplomatic immunity who are not subject to United States jurisdiction are not eligible. Non-Permanent Resident Aliens must be employed in the U.S. for the last 24 months and document lawful residency as follows:

Documentation and Expiration
All nonpermanent resident alien borrower(s) must verify they are legally present in the United States with a copy of one of the following:
VISA
o If expiration is within six months of the loan application and the borrower has not changed employers, a copy of the employer's letter of sponsorship for visa renewal must be provided.
o If Visa has expired, a valid USCIS Form I-797 confirming submitted application to renew.
EAD Card
o If expiration is within six months of the application the borrower must show evidence they have applied for an extension or provide letter from the employer indicating they will continue to sponsor their employment
For residents of Canada or Mexico, H1-B status stamped on an unexpired passport For borrowers with income being used for qualification, see below for eligible VISA classifications.

VISA Eligibility for Borrower's with Income for Qualification		
Borrowers with any source of income being used for qualification must have one of the following VISA classifications and submit the appropriate documentation to support they are legally able to work within the United States. • Some VISAs automatically grant work authorization and an EAD will not be issued. • For certain VISA classes, spouses and dependents must be issued an EAD to work within the U.S. • When an EAD is provided it must be associated with one of the acceptable VISA classes notes below. • Refer to uscis.gov for the further guidance on associated VISA and EAD categories.		
VISA Series	**Acceptable VISA Class**	**Description**
A Series	A-1, A-2 and A-3 Must document that the borrower does not have diplomatic immunity.	Diplomat and foreign government official such as an ambassador, consular officer or other top government official, spouse, dependents and employees of a diplomat or official. A-2 can also classify as lower ranked foreign government employees.

		EAD class C01 issued to dependents.
E Series	E-1, E-2, E-3, E3D	Trade Treaty. International trader or investor, spouse and dependents. Employer Sponsored EAD class A17 issued to spouse. EAD class C02 may also be issued to dependents.
G Series	G-1, G-2, G-3, G-4, and G- 5 Must document that the borrower does not have diplomatic immunity.	Employees of International Organizations and NATO. Internationally recognized staff, spouse and dependents EAD class C04 issued to spouse and dependents
H Series	H-1B, H-1B1, H-1B2, H- 1B3, H-1C, and H-4	Temporary Work VISA. An individual who is in the U.S. performing services of a professional nature in a specific position for a sponsoring employer EAD class C26 issued to spouse
I Series	I	Foreign media representatives
K Series	K-1 and K-3	Finance or spouse of U.S. Citizen EAD class A06 issued to fiancé(e) or dependent of K-1. EAD class A09 issued to spouse or dependent of K-3
L Series	L-1A, L-1B, L-2	Temporary Work VISA. Intracompany transfer of an executive or an employee with specialized knowledge, spouse and dependents EAD Class A18 issued to spouses
NATO	NATO statuses 1 through 7 Must document that the borrower does not have diplomatic immunity.	Employees of International Organizations and NATO. Representative of member state to NATO, officials of NATO, support staff, spouse and dependents EAD class C07 issued to dependents
O Series	O-1 and O-2	An individual who possesses extraordinary ability in the sciences, arts, education, business, or athletics, or who has a demonstrated record of extraordinary achievement in the motion picture or television industry and has been recognized nationally or internationally for those achievements. Employer Sponsored.
R Series	R-1	Religious Workers. Employer Sponsored

TN	TN	Nonimmigrant NAFTA Professional visa (only issued to citizens of Canada and Mexico) Employer sponsored

INELIGIBLE BORROWERS

- Non-Resident Aliens
- Foreign Nationals
- Borrowers with diplomatic status
- Life Estates
- Non-Revocable Trusts
- Land Trusts
- Guardianships
- LLCs, Corporations or Partnerships
- Borrower(s) with any ownership in a business that is federally prohibited, regardless if the income is not being considered for qualifying, will be considered an ineligible borrower.

NUMBER OF BORROWERS

The maximum number of borrowers on a loan transaction is limited to four.

NUMBER OF FINANCED PROPERTIES

There is no limit to the number of financed properties the borrower(s) may own.

PRESENT ADDRESS

The borrower's present address must be within the U.S. territories, or APO military addresses located within the U.S.

POWER OF ATTORNEY

A Power of Attorney (POA) is a legal document giving one-person (described as the agent or attorney- in-fact) power to legally bind the borrower enacting the POA to the mortgage transaction.

Eligible Occupancy Types	Owner Occupied and Second Homes only. Investment properties are not eligible.
Borrower Eligibility	When multiple borrowers are on the transaction, at least one borrower must be present at closing.
Power of Attorney	• Must be specific to the transaction referencing the property address, unless the POA is a Military Durable POA. • Signatures on the POA must match signatures in the file to AAA Lendings's satisfaction (may not be eSigned). • POA must be notarized. • The POA must executed by the borrower prior to its use by the agent.
Application	The application and Purchase Agreement (if applicable) must be signed by all parties of the loan.

	A POA may sign the initial application only when the borrower is on military service servicing outside the U.S. or deployed on a U.S. vessel, as long as the POA expressly states the intent to secure a loan on the subject property
Eligible Agent/ Attorney in Fact	Family member of the borrower
Title	The title policy must not make any exceptions to the use of a POA.

CLOSING IN TRUST

The following guidelines must be met:

- An attorney's opinion letter stating all below warranties are met will be required on all loans closing in trust; or Certificate of Trust or equivalent form.
  - For California properties, a certificate of trust is acceptable in lieu of an attorney's opinion letter.
- The trust(s) must be a living revocable trust also known as a family trust or an inter vivos trust
- The title company must agree to insure over the trust with no exceptions for the trust or trustees
- A copy of the trust(s), or pertinent pages within the trust, must be included in the submission package
- The Settlor or grantor must be a natural person. The settlor must also be the trustee or one of the co-trustees
- The primary beneficiary of the trust must be the settlor or the grantor. If there is more than one settler or grantor, then there may be more than one primary beneficiary, as long as the income or assets of least one of the grantors or settlors will be used to qualify for the mortgage and that grantor or settlor will occupy the property and sign the mortgage instruments in their individual capacity
- The trust document must give the trustee or trustees the authority to mortgage trust assets, to incur debt on behalf of the trust, and to hold legal title to and manage trust assets.

OCCUPANCY AND PROPERTY

Inconsistencies in the loan file that raise questions about the authenticity of the proposed occupancy status as disclosed must be addressed to validate loan integrity. Examples may include significant or unrealistic commuting distance, close proximity between subject property and current primary residence. AAA, at its discretion, may determine the occupancy based on its current and best use. Properties occupied by a party other than the borrower will be considered an investment property.

<u>ELIGIBLE PROPERTIES</u>

- Primary Residence
  - The residential property physically occupied by the owner(s) as their principal home domicile.
- Second Homes
  - Must be located reasonable distance away from the borrower's principal primary residence
  - Restricted to 1-unit dwellings
  - Must be suitable for year-round occupancy
  - Must not be subject to any timeshare arrangement or other shared occupancy agreement
  - Property may not be rented or determined to be an investment property
- Residential Single-Family
- Owner-Occupied 2-4-unit Primary Residence
- Detached Condominiums and Condominiums, see below for additional requirements

- Planned Unit Developments (PUD)
- Modular Homes
- Leaseholds, see below for additional requirements
- Age-Based Resale Restricted properties

INELIGIBLE PROPERTIES

- Investment Properties
- Manufactured/Mobile Homes (single or double-wide)
- Cooperative properties
- Resale Deed Restricted properties (age-based restricted only eligible)
- Vacant Land
- Properties currently listed for sale
- Properties located in the state of Texas
- Properties located in the U.S. Virgin Islands
- Properties in less than Average condition (C5 and C6 are not eligible)
- Units is Transient Housing Condo projects (e.g. Condo-hotel)
- Properties under construction or renovation at time of loan closing
    - Construction/renovation cannot affect the safety, soundness or structural integrity of the subject property
- Properties titled as Life Estates or Land Trusts
- Properties located on Indian/Native American Tribal Land
- Unique properties including, but not limited, non-traditional property types such as barndominiums, berm earth houses, geodesic domes, container homes
- Properties without utilities (water, electric, gas, etc.) and/or utilities not meeting community standards (e.g. off-grid homes)
- Income producing properties with acreage, including but not limited to, working farms, ranches or orchards
- Properties located in Lava Zones 1 or 2
- Properties with environmental risk exposures to include, but not limited to, gas tanks, railroad tracks, high tension wires, UFFI, industrial areas, radon, mold, or Chinese Drywall.
- Properties that are not suitable for year-round occupancy, regardless of location
- Mixed-use properties, business use (primary function/modifications to property is non-residential in nature), included but not limited to:
    - Boarding Houses
    - Group Homes
    - Bed and Breakfasts
    - Daycare facility
    - Beauty/Barber Shops
    - Doctor Offices

U.S. TERRITORIES

AAA Lendings does not currently lend on properties located in the following U.S. Territories: Guam, Puerto Rico, American Samoa and Northern Mariana Islands.

WARRANTABLE CONDOMINIUMS

- FNMA Warrantable Condos
- Limited Review Eligible
- Detached condos (i.e. site condo)

- Each condominium project must be reviewed and approved by AAA's Condo Review Department.

LEASEHOLDS

When the first mortgage was originated or is being serviced by AAA Lendings, no further documentation is required. If the first lien is not held or originated by AAA Lendings, or when the HELOC is taking first lien position, an attorney's opinion letter is required to verify the property is a FNMA eligible leasehold.

INELIGIBLE FIRST LIENS

Home equity transactions may not be closed behind the following ineligible first lien types:

- Land Contracts or Contracts for Deed
- Reverse Mortgages
- Negative Amortization Loans
  - Will be considered ineligible when disclosed as such by the applicant or if uncovered during the credit bureau investigation.
- Home Equity Lines of Credit or any other future advance liens (HELOCs in repayment period are eligible)

When the first lien type cannot be determined from the credit report or other credible source, a copy of the first mortgage note may be requested to verify it is not an ineligible lien.

INELIGIBLE PARTICIPANTS

If any of the participants associated to the loan transaction are listed on AAA Lendings's internal ineligible list, the loan may not be approvable.

ADDITIONAL SUBORDINATE FINANCING

An existing Home Equity lien or non-first mortgage financing on title may be re-subordinated to the new HELOC. The following requirements must be met:

- Provide documentation that the lien will subordinate to a second or third lien position, as applicable
- Must meet CLTV requirements
- Subordination agreement must be provided at closing

TRANSACTION TYPES

All transactions will be classified as cash-out transactions.

COMBINED LOAN TO VALUE

LTV/CLTV/HCLTV is generally calculated based on the appraised value or valuation of the property.

- Properties purchased within 120 days of application will use the lesser of the purchase price or appraised value to calculate LTV/CLTV/HCLTV, measured from the date on which the property was purchased to the disbursement date of the new mortgage loan.
- There are no seasoning requirements for LTV/CTLV/HCLTV calculations where an occupying borrower is added to the title on a primary residence. For second homes, see title requirements below for additional restrictions.

TITLE

AAA will originate refinance loans secured by residential single-family homes. It is the responsibility of the Underwriting department to ensure the Bank has a first or second lien position that is perfected in accordance with applicable state law.

The borrower must own the property in fee simple or leasehold interest. Title may also be held in a revocable "living" trust, also known as a family trust or an inter vivos trust. Land trusts are not acceptable.

For second homes, the borrower must be also be a Note holder on any first lien held against the subject property, unless the borrower is the spouse of the Note holder and is present on title.

SOLAR PANELS

Ownership and financing/leasing structure of the subject property solar panels must be determined by evaluating documents including but not limited to the credit report, copy of related solar panel documentation and title commitment to address if the related debt is reflected in the land records.

- The monthly lease must be included in the DTI unless the lease is structured to:
  - Provide delivery of a specific amount of energy at a fixed payment during a given period, and
  - Have a production guarantee that compensates the borrower on a prorated basis in the event the solar panels fail to meet the energy output required for in the lease for that period.
- The payment on financed loan for solar panels must be included in the borrower's obligations
- Property must maintain access to an alternative source of electric power that meets community standards.
- Only solar panels owned free and clear by the borrower may be included in the appraised value. Solar power leases, power purchase agreements and panels financed as personal property can be repossessed or removed from the property in the event of default.
- When financed as a fixture to real estate the loan must be included in the CLTV calculation and must obtain a subordination agreement or lien must be released,
  - Title confirmation or copy of UCC-1 Financing Statement may be required to determine if recorded against title to the Mortgaged Premises, creating a lien on the real estate itself (i.e., claiming an interest in both the solar panels and the real estate, not just the solar panels).
  - Financed solar panels where the lien takes priority position, in other words will not subordinate, are not eligible (e.g. select PACE loans) and must be paid off prior to or at closing

ESCROW REQUIREMENTS

Escrows for taxes and insurance are not allowed for standalone home equity transactions.

HAZARD

Refer to *Hazard Insurance Requirements*, for specific hazard insurance guidelines.

FLOOD

Refer to *Flood Insurance*, for specific prior to closing flood insurance guidelines.

MORTGAGE INSURANCE

Not Applicable

CREDIT

CREDIT REPORTS

Credit report must be a 3-file merged credit report. Every submitted credit bureau report must include the full name, address and social security number of each borrower. When the credit reporting agency has incomplete information, discovers that the borrower might not have disclosed all information that should be found in the public records or obtains other information that indicates the possible existence of undisclosed credit records, the credit reporting agency must interview the borrower(s) to obtain additional information that is needed to provide an accurate report or perform additional research to verify whether the purported undisclosed records actually exist.
Note: Credit must be dated within 120 days of the Note date.

EXTENDED FRAUD ALERTS OR ACTIVE MILITARY ALERTS

Applicants with credit reports containing Extended Fraud Alerts or Active Military Alerts will be contacted by a AAA employee prior to a commitment letter being issued.

CREDIT SCORING

FICO (Fair, Isaac and Company) scores are required to be obtained from the three national credit bureaus. Each borrower must have at least two credit scores.

- If there are (3) valid credit scores for a borrower, the middle score (numerical middle of the three scores) is used.
- If there are (3) valid scores for a borrower but two of the scores are the same, the duplicate score is used.
- If there are (2) valid scores for a borrower, the lower of the two scores is used.

If there is more than one borrower on a mortgage loan, the lowest of the median FICO scores for all borrowers (as calculated above) is used for credit qualification purposes.

FROZEN CREDIT

No more than one credit repository can have frozen credit information. The lower of the two available scores will be used for qualifying purchases

CREDIT ANALYSIS

CREDIT INQUIRIES

The report must list all inquiries that were made in the previous 120 days. All loan applicants will be required to provide an explanation for all inquiries that were made in the previous 90 days on their credit report and any new debt must be added to the liabilities section of the 1003 and be supposed by applicable documentation. All applicants will be required to provide an explanation for all credit inquiries found during the loan process. A written explanation from a borrower may be in the form of a letter, an email, or some other form of written documentation provided by the borrower.

TRADELINES

- Minimum 4 trade lines; one currently active and open for more than 12 months with a minimum high balance of $1,000, regardless of credit score
- Credit history showing 0x30 for all mortgages in last 12 months

TRADITIONAL CREDIT
Traditional credit is typically presented in the form of a credit report that provides sufficient information with which to make an underwriting decision.

Non-Traditional/Alternative Credit
Non-traditional/Alternative credit is not acceptable. Tradelines, or items such as collections, charge- offs, "authorized user" accounts, deferred loans with no payment history, transferred accounts, not traditionally reported obligations (e.g. utilities) are all considered non-traditional tradelines.

DISPUTED CREDIT INFORMATION
If a borrower indicates that any significant information in the credit file is inaccurate, such as reported accounts that do not belong to the borrower or derogatory information that is reported in error, the borrower should request the credit reporting company that provided that information to confirm its accuracy. If the credit reporting company confirms that the disputed information is incorrect, the information should be corrected and a new report obtained if the erroneous information significantly effects the underwriting of the file.

Disputed Tradelines
- All disputed tradelines with a balance must be included in the DTI if the account belongs to the borrower
- A disputed account with a zero balance and no late payments, can be disregarded.

VERIFICATION OF MORTGAGE REQUIREMENTS
A verification of mortgage is not required if the credit report reflects the payment history is reporting current as of the date of the application unless otherwise indicated below. Applies to all borrowers on the loan.
- If the borrower(s) has a mortgage(s) in the most recent twelve (12) months, a VOM must be obtained reflecting 0X30 in the last twelve (12) months from the date of application if mortgage is not reporting on credit.
  - VOM requirement applies even if the borrower is not the Note holder on first lien of the subject property (e.g. mortgage held by another party on title)
- Additional due diligence and documentation must be provided to support the 12-month payment history requirements on any mortgage containing the following:
  - The credit report reflects trending data indicating partial, missed payments within the last 12 months.
  - Credit report indicates an active forbearance
  - A mortgage or payoff statement indicates past-due or deferred balance owed or an active forbearance.

The documentation provided must support the accurate payment history of the borrower and will be accepted at the discretion of AAA Lendings. Borrower's actively late on their mortgage(s) at time of application are not eligible.

Loans with Prior COVID-Related Forbearance
Due to the stipulations of the CARES Act, partial or missed payments while a borrower was under a COVID-related forbearance are not be reported as late on a credit report. As such, the following will apply when documentation discloses missed or late payments on all loans held by the borrower and any mortgage on the subject property:

- Any missed or late payments documented within the last 12 months will be assessed according to the guidelines as a late, regardless of current or previous COVID forbearance status.
- Any outstanding deferred balances or servicer resolutions aged over 12 months, documented as occurring during a COVID-related forbearance on the subject, may be paid off with the proceeds of the new transaction.

SIGNIFICANT DEROGATORY CREDIT EVENTS

The presence of significant derogatory credit events dramatically increases the likelihood of a future default and represents a significantly higher level of default risk.

BANKRUPTCY, FORECLOSURE, DEED-IN-LIEU, SHORT SALE

The underwriter must determine the significance of the derogatory event and verify sufficient time has elapsed since the date of the last derogatory mortgage event based on the distribution date of the new loan.

Significant Derogatory Event	Recovery Time Periods for Re-Establishment of Credit with Financial Mismanagement	Recovery Time Periods for Re-Establishment of Credit with Extenuating Circumstances
Bankruptcy (Chapter 7 or 11)	A 4-year waiting period is required, measured from the discharge or dismissal date of the bankruptcy action	Primary Residence only A 2-year waiting period is permitted from the discharge or dismissal date of the bankruptcy action.
Bankruptcy (Chapter 13) A distinction is made between Chapter 13 bankruptcies that were discharged and those were dismissed.	2 years from the discharge date, or 4 years from the dismissal date	Primary Residence only A 2-year waiting period is permitted after a Chapter 13 dismissal, if extenuating circumstances can be documented. There are no exceptions permitted to the 2-year waiting period after a Chapter 13 discharge.
Multiple Bankruptcy Filings	For a borrower with more than one bankruptcy filing within the past 7 years, a 5-year waiting period is required from the most recent dismissal/discharge date.	Primary Residence only A 3-year waiting period is permitted if extenuating circumstances can be documented, and measured from the most recent bankruptcy discharge of dismissal date. The most recent bankruptcy filing must have been the result of extenuating circumstances
Foreclosure	A 7-year waiting period is required, and is measured from the completion date of the foreclosure action as reported on the credit report or other foreclosure documents provided by the borrower	All cash out transactions are prohibited

Deed-In-Lieu of Foreclosure, Pre-foreclosure Short sale, or Charge-off of mortgage account	4-year date of completion or sale	Primary Residence only 2 years date of completion or sale

Extenuating Circumstances for Bankruptcy, Foreclosure, Deed-In-Lieu, Short Sales
Extenuating circumstances are nonrecurring events that are beyond the borrower's control that result in a sudden, significant, and prolonged reduction in income or a catastrophic increase in financial obligations.

In order to support an extenuating circumstance and follow the reduced recovery time, listed above, the following requirements must be met:

- Documentation to support borrower's claim must be provided. Examples include:
  - Copy of divorce decree
  - Medical bills
  - Notice of job layoff or severance papers
  - Additional documents that illustrate an inability to resolve the derogatory event
    - Insurance paper or claim settlements
    - Property listing agreements
    - Lease agreements
    - Tax returns covering the periods to, during and after the loss of employment
- Letter from borrower explaining the relevance of the documentation and support claims of the extenuating circumstances that led to the event. Letter to illustrate the borrower had no reasonable options other than the default on their financial obligations.

PAST-DUE, COLLECTIONS AND CHARGE-OFFS OF NON-MORTGAGE ACCOUNTS

- Accounts that are reported as past-due, not reported as collection accounts, must be brought current prior to close.
- For 1-unit, owner-occupied properties, borrowers are not required to pay off outstanding collections or charge-offs, regardless of the amount, provided the collection will not threated first-lien position.
- For 2 to 4-unit owner-occupied properties and second homes, collections and charge-offs totaling more than $5,000 must be paid in full prior to or at closing.

Delinquent credit that has the potential to affect lien position or diminish the borrower's equity, must be paid off at or prior to closing.

JUDGMENTS AND LIENS
Open judgments, tax liens and all other outstanding liens must be paid off prior to or at closing. Documentation of the satisfaction of these liabilities, along will verification of funds sufficient to satisfy these obligations, must also be obtained if paid off prior to close or using funds outside of loan proceeds.

LIABILITIES

RECURRING OBLIGATIONS

AAA considers debt the borrower owes to be a liability. Debt is defined as borrowed money, the repayment of which may be either secured or unsecured, with various possible repayment schedules including but not limited to:

- All installment loans
- Revolving charge accounts
- Real estate loans
- Alimony
- Child support
- Other continuing obligations

Obligations to be considered as possible recurring debt may be identified on sources including but not limited to the application, credit report, paystubs, asset account statements, and legal orders.

DEBT TO INCOME (DTI) RATIO

The underwriter must include and verify the following when computing the debt to income ratios for recurring obligations:

- Monthly housing expense(s) including
  - Rent
  - Real Estate loans
  - Taxes
  - Insurance
  - Association Dues
- Additional recurring charges extending ten months or more, such as
  - Payments on installment accounts
  - Child support or separate maintenance payments
  - Revolving accounts
  - Alimony

If an installment debt does not extend beyond 10 months it may be excluded, however the underwriter must take into consideration whether the size and/or number of remaining payments will impact the borrower's ability to handle the new debt during the early part of the loan.

Monthly payments on revolving, open-ended and/or lease, regardless of the balance, are counted as a liability for qualifying purposes even if the account appears likely to be paid off within 10 months or less

PROPERTY DEBT OBLIGATIONS

- When the borrower(s) on the transaction is not a Note Holder to first lien mortgage, the mortgage payment does not need to be included in the borrower's DTI.
- Taxes, insurance and any association dues must be documented and included, regardless if included in the first mortgage payment held by another person. Documentation may include, but not limited to, the following:
  - Mortgage statement with breakdown of escrows, if applicable
  - Tax verification via title commitment, tax bills, evidence from local assessor office

- Insurance policy
- Current HOA/Association statement, verification from HOA, as applicable, if not provided on appraisal

REVOLVING CHARGE ACCOUNTS

Revolving charge accounts (e.g. credit cards) and lines of credit must be considered part of the borrower's recurring monthly debt obligations. If the credit report does not show a required minimum payment amount, one of the following must be applied:

- The minimum payment from a current statement, or
- the greater of $10 or 5% of current balance.

Authorized User Accounts

The payment is excluded from the DTI ratio.

OPEN 30-DAY CHARGE ACCOUNTS

An open 30-day account, account which the balance is required to be paid in full monthly (e.g. Amex), may be identified when the account does not reflect a revolving monthly payment on the credit report, lacks documentation in file to indicate a revolving monthly payment, or credit reflects the monthly payment is identical to the outstanding balance. The borrower must have sufficient verified liquid assets to pay off the balance and meet the reserve requirements for the loan program to exclude the payment from the qualifying DTI.

- If sufficient liquid assets are verified exclude the reported monthly payment from the DTI.
- If sufficient liquid assets are not verified obtain evidence that the account has been paid in full and exclude the reported monthly payment from the DTI, or include the monthly payment (equal to the outstanding account balance) in the calculation of the qualifying DTI.
- If the account provides for a monthly payment option other than the total outstanding balance, the account is not considered a 30-day charge account and these requirements do not apply.

INSTALLMENT LOANS

Installment debt, secured or unsecured, is borrowed money that is repaid in several successive payments, usually at regular intervals, for a specific amount and for a specific term.

- Installment debts with monthly payments that extend beyond 10 months should be included in the DTI ratio
- Even if the debt does not extend beyond 10 months, it must be noted whether the size and/or number of remaining payments will impact the borrower's ability to handle the new debt during the early part of the loan
- For purposes of qualifying, the borrower may pay off the installment debt

Timeshares

Timeshares to be considered installment debt and not classified as real estate owned, regardless if reported on credit as a mortgage loan.

LEASE PAYMENTS

The lease payments must be considered a recurring monthly debt obligation, regardless of the number of months remaining on the lease. This is because the expiration of a lease typically leads to a new lease or debt obligation.

GARNISHMENT
Garnishments, generally disclosed as a deduction on paystubs, with more than 10 months remaining must be included in the monthly debt obligations.

ALIMONY/CHILD SUPPORT/MAINTENANCE
When the borrower is required to pay under a legal written order or agreement, and the payments are required to continue to be made for more than 10 months the obligation must be included.

- Child support is treated as a liability.
- Alimony payments:
  - must be considered as part of the borrower's recurring monthly debt obligations, or
  - Reduced from the qualifying income by the amount of the alimony obligation in lieu of including it as a monthly payment in the calculation of the DTI ratio.

STUDENT LOANS
If a monthly student loan payment is provided on the credit report, the lender may use that amount for qualifying purposes. If the credit report does not reflect the correct monthly payment, the lender may use the monthly payment that is on the student loan documentation (the most recent student loan statement) to qualify the borrower.

If the credit report does not provide a monthly payment for the student loan, or if the credit report shows $0 as the monthly payment, the lender must determine the qualifying monthly payment using one of the options below.

- If the borrower is on an income-driven payment plan, the lender may obtain student loan documentation to verify the actual monthly payment. If the payment is $0 the borrower must qualify using one of the following:
- For deferred loans, loans in forbearance, or income-driven payment of $0 the lender must calculate
  - a payment equal to 1% of the outstanding student loan balance, or
  - a fully amortizing payment using the documented loan repayment terms.

DEFERRED LOANS (OTHER THAN STUDENT LOANS)
Deferred installment debt must always be included in the applicant's monthly recurring obligations. If the credit report does not indicate a monthly payment at the end of the deferment period, a payment of 2% of the outstanding balance will be calculated and included in the DTI ratio. If the loan is deferred beyond the term of the loan, the payment can be excluded from the DTI ratio.

DEMAND LOANS
A demand loan or balloon loan with no monthly payment, unsecured or secured, which it becomes due and is payable in full on a particular date must meet the following:

- If the note is due within the next 12 months:
  - If the applicant does have adequate reserves available to pay the obligation in full, the debt should not be included in the DTI ratio, or
  - A minimum payment will be included in the DTI ratio, calculated by dividing the outstanding balance by the remaining loan term.

Example- If the outstanding balance is $24,000 and the loan is due in full in 12 months, then the payment that will be included in the monthly DTI ratio is $2,000 [$24,000/12 = $2,000].

LOAN SECURED BY FINANCIAL ASSETS
A loan secured against the borrower's financial asset such as a 401K, IRA, CD, Stocks, etc.

- The loan is not considered as part of the borrower's recurring monthly debt obligations, as long as the lender obtains a copy of the applicable loan instrument, or other supporting documentation (e.g. paystub), that shows the borrower's financial asset as collateral for the loan.
  - Payments on debts secured by virtual currency, such as cryptocurrency, must be included in the debt-to-income ratio and are not subject to the provisions regarding installment debts secured by financial assets.
- The value of the asset must be reduced by the proceeds from the secured loan, and any related fees, to determine remaining funds which may be applied toward asset reserves

HOME EQUITY LINES OF CREDIT

HELOCs with a current outstanding balance with no payment reflected on the credit report may have the payment documented with a current billing statement. HELOCs with a current $0 balance do not need a payment included in the DTI unless using for the transaction

<u>OMITTING PERSONAL LIABILITIES</u>

BUSINESS DEBT IN BORROWER'S NAME

Non-mortgage business debts for which the borrower is personally liable (reporting on credit) may be excluded from the borrower's DTI when all of the following conditions are met:

- Copies of the most recent 12 month's canceled business checks or statements to show the business pays
- The account cannot have a history of delinquency within the last 12 months

RENTAL PROPERTY REPORTED THROUGH A PARTNERSHIP OR A S CORPORATION

When a borrower is personally obligated on a mortgage debt with the gross rents and related expenses reporting through a Partnership (1065) or S Corporation (1120s) a portion or all of the debt may be excluded as follows:

- Form 8825 from the business return(s) must be used to calculate the rental net cash flow of the property to offset the borrower's obligation, up to but not to exceed the PITIA.
- Any resulting loss from the calculation must be added to the borrower's total monthly obligations.
- No positive rental income may be given for the property in question.
- In order to determine business income or loss from the 1065 or 1120s, defer to self-employment requirements.

COURT ORDERED ASSIGNMENT OF DEBT

If the obligation to make payments on a debt has been assigned to another person by court order (e.g. divorce decree), the payment may be excluded from the DTI when the following requirements are met:

- Provide copy of court order or divorce decree
- For mortgage related debt:
  - a copy of the documents transferring title ownership of the property must be provided
  - If the borrower has not been released from title, any late payments associated with repayment of the mortgage debt must be considered per the guidelines.

CONTINGENT LIABILITIES (CO-BORROWER/CO-SIGNED DEBT)

Contingent Liabilities exist when an applicant co-signs another person's loan or is a co-borrower on an existing loan and may include auto, student, mortgage or other obligations. As a co-borrower/co-signer, the individual has equal responsibility in repaying the loan should the loan go into default.

In order to exclude a debt for which the borrower is a co-borrower/co-signer the following conditions must be met:
- Documentation to support the other party making the payments is obligated to the debt and
- Has been making timely payments over the last consecutive 12 months.
  - Acceptable documents include canceled checks, other party's bank statements showing monthly amounts disbursed, canceled cashier's checks, money order receipts.

If payments are not made on a timely basis, a person not obligated to the liability is making the payments, or cannot be sufficiently documented, the debt should be included as a recurring liability.

OBLIGATIONS NOT CONSIDERED DEBT

Obligations that are not considered debt, and therefore not subtracted from gross income, include:
- Federal, State, and local taxes (unless court ordered garnishments exist);
- Federal Insurance Contributions Act (FICA) or other retirement contributions, such as 401(k) accounts (including repayment of debt secured by these funds)
- Commuting costs;
- Union dues;
- Open accounts with zero balances;
- Automatic deductions to savings accounts;
- Child care (unless court ordered child support); and
- Voluntary deductions.

PAYOFF OF DEBT TO QUALIFY
- Paying down revolving debt and/or installment to qualify is not acceptable (e.g. cannot pay installment down to 10 payments or less)
- Lease payments may not be paid down or paid off for qualifying purposes
- Paying off revolving debt, installment loans, collections, judgments, or tax liens to qualify is allowed to be paid prior to or at time of closing
  - When paid off prior to close documentation must be provided to source funds when the total to payoff and funds needed to close is $3,000 or more and must confirm zero balance.

ASSETS

INTRODUCTION

Assets are an indicator of, and may be used to highlight an applicant's creditworthiness and financial strength. The applicant should have sufficient net worth – cash or other equity – in order to cover any costs associated with the new loan and/or to mitigate any shortfall in capacity to repay the loan.

Asset verification will be required in which the applicant must bring $3,000 or more to transaction/closing, or as deemed necessary per the underwriting guidelines.

ASSET DOCUMENTATION
- Monthly bank statements must be dated within 45 days of application.
  - If the latest bank statement is more than 45 days earlier than the date of the loan application, the borrower must provide a more recent supplemental bank-generated form that shows the account number, balance and date.
- Quarterly statements must be dated with 90 days of application.
- Depository and Investment accounts statement covering the most recent two-month period.

- The most recent retirement statement available.
- Asset statements must clearly identify the borrower as the account holder, include the account number, the transaction history from the time period covered by the statement(s) and the ending account balance.
- Verifications of source of funds may be dated up to 120 days before the date of the note.
- Documents that are "faxed" to the lender or that the borrower downloads from the Internet must clearly identify the name of the depository or investment institution and the source of the information (Fax number or URL) at the top of the document.

VERIFICATION OF DEPOSIT FORM

The *Request for Verification of Deposit* may be used to verify activity in the borrower's depository accounts. When the borrower authorizes the lender to obtain this information directly from the different depository institutions in which he or she has accounts by signing the Form 1006 or 1006(S), the depository institutions must complete, sign and date the form and return it directly to the lender. The Verification of Deposit should not be handled by the borrower. Rather than requiring the borrower to sign multiple verification forms, the lender may have the borrower sign a borrower's signature authorization form.

- When a *Verification of Deposit* (Form 1006 or Form 1006[S]) (VOD) is used and depository activity is not included, the lender must verify the source of funds for accounts opened within the last 90 days of the application date, and
- Account balances that are considerably greater than the average balance reflected on the VOD.

<u>TYPES OF ASSETS</u>

The following asset types may be used for closing costs. See additional guidelines for requirements when assets may be required for reserves (e.g. income or debt obligations).

DEPOSITORY ACCOUNTS

Checking, savings, money market, certificate of deposit are acceptable depository account types.

RETIREMENT ACCOUNTS

Retirement account statements must identify the borrower's vested amount and the terms and conditions for loans or the withdrawal of funds.

STOCKS, BONDS AND MUTUAL FUNDS

Stocks, government bonds and mutual funds are acceptable sources of funds if their value can be verified.

- The value of stocks, bonds and mutual funds (net of any margin accounts) may be verified by referencing the most recent monthly or quarterly statement from the depository or investment firm. A photocopy of the stock certificate, accompanied by a newspaper stock list that is dated as of or near the date of the loan application, may also be used to document stock ownership and value.
- The value of government bonds should be based on their purchase price unless the redemption value can be documented.
- When used for the down payment or closing costs, if the value of the asset (as determined above) is at least 20% more than the amount of funds needed for the down payment and closing costs, no documentation of the borrower’s actual receipt of funds realized from the sale or liquidation is required. Otherwise, evidence of the borrower’s actual receipt of funds realized from the sale or liquidation must be documented.

- Vested Stock Option are eligible source of borrower funds and reserves, and must be documented with the following:
  - Account statements covering a two-month period or direct account verification (i.e., VOD) confirming the number of vested shares and current value
  - If the borrower does not receive a stock/security account statement for the stock options, the originator must:
    - Provide a statement verifying the number of vested shares owned by the borrower
    - Provide the current stock price from a published source to determine the value

TRUST ACCOUNTS

Funds disbursed from a borrower's trust account are an acceptable source of funds if the borrower has immediate access to them. The trust manager or trustee must verify the value of the trust account and to confirm the conditions under which the borrower has access to the funds. The effect, if any is that the withdrawal of funds from the account will have on any trust income that is used in qualifying the borrower for the mortgage must also be documented.

<u>LARGE DEPOSIT</u>

When bank statements are used, the lender must evaluate large deposits, which are defined as a single deposit that exceeds 50% of the total monthly qualifying income (includes income derived from the asset calculation establishing the debt payment-to-income ratio) for the loan.

All large deposits should be reviewed for indications of recently opened liabilities resulting from borrowed funds or any indication that the funds used to cover closing costs, or reserves generated from an unacceptable source.

If funds from a large deposit are needed to complete the transaction, i.e., are used for closing costs, the lender must document that those funds are from an acceptable source. Occasionally, a borrower may not have all of the documentation required to confirm the source of a deposit. In those instances, the lender must use reasonable judgment based on the available documentation as well as the borrower's debt-to- income ratio and overall income and credit profile. Examples of acceptable documentation include the borrower's written explanation, proof of ownership of an asset that was sold, or a copy of a wedding invitation to support receipt of gift funds. The lender must place in the loan file written documentation of the rationale for using the funds.

- Verified funds must be reduced by the amount, or portion, of the undocumented large deposit, as defined above, and the lender must confirm that the remaining funds are sufficient for the down payment, closing costs, and financial reserves. When the lender uses a reduced asset amount, net of the unsourced amount of a large deposit, that reduced amount, must be used for underwriting purposes. When a deposit has both sourced and unsourced portions, only the unsourced portion must be used to calculate whether or not it must be considered a large deposit. See examples below:
  - Scenario 1:
    - Borrower has monthly income of $4,000 and an account at ABC bank with a balance of $20,000. A deposit of $3,000 is identified, but $2,500 of that deposit is documented as coming from the borrower's federal income tax refund.
    - Only the unsourced $500, the deposit of $3,000 minus the documented $2,500, must be considered in calculating whether it meets the large deposit definition.
    - The unsourced $500 is 12.5% of the borrower's $4,000 monthly income, falling short of the 50% definition of a large deposit.

- Therefore, it is not considered a large deposit and the entire $20,000 balance in the ABC bank account can be used for underwriting purposes.

- Scenario 2:
  - Using the same borrower example, a deposit of $3,000 is identified, but only $500 is documented as coming from the borrower's federal income tax refund, leaving $2,500 unsourced.
  - In this instance, the unsourced $2,500 is 63% of the borrower's $4,000 monthly income, which does meet the definition of a large deposit.
  - Therefore, the unsourced $2,500 must be subtracted from the account balance of $20,000 and only the remaining $17,500 may be used for underwriting purposes.

Note: If the source of a large deposit is readily identifiable on the account statement(s), such as a direct deposit from an employer (payroll), the Social Security Administration, or IRS or state income tax refund, or a transfer of funds between verified accounts, and the source of the deposit is printed on the statement, the lender does not need to obtain further explanation or documentation. However, if the source of the deposit is printed on the statement but the lender still has questions as to whether the funds may have been borrowed, the lender should obtain additional documentation.

EMPLOYMENT & INCOME

INTRODUCTION

Employment and income are essential for loan repayment. Qualifying income should be stable, predictable, and likely to continue. The applicant must demonstrate the financial wherewithal to repay the proposed loan transaction as well as other obligations.

SOURCES OF INCOME

ACCEPTABLE SOURCES OF INCOME

Sources of income/liquidity/repayment may vary. Some receive primary income from only one source, while others have a diversified portfolio and may receive income from several sources. Acceptable sources which demonstrate ongoing sufficiency of repayment capacity and that can be utilized in the analysis of a borrower's income projections include:

- Wage-Earner Income: All non-self-employed applicants who receive a W-2 at year end to summarize total earnings – includes hourly, weekly, biweekly, part-time, seasonal, bonus, commission, and tips/gratuity.
- Self-Employed Income: Sole proprietorship, Partnership, Corporations, and S-Corporations
- Other Non-Employment Income: Alimony/Child Support/Maintenance, Unemployment/Public Assistance, Disability/Worker's Compensation, Retirement/Pension, Social Security, Annuity, IRA, Military/VA Benefits, Trust, Interest & Dividend, Inheritance/Guaranteed Income, Note Receivables, Mortgage Differential/COLA & Rental
- Readily Convertible Assets: Bank Deposits, Money Market, Marketable Securities, Mutual Funds, Annuities, and Bonds

UNACCEPTABLE SOURCES OF INCOME

- Income based on future earnings (unless documented from a source such as social security income or retirement account/annuity/disability or other sources of protected income based upon reliability and regularity of income where the source and term are verifiable).
- Draw Income
- Capital Withdrawals
- VA Education Benefits
- Income from Mortgage Certificates

- Illegal Income/Income not listed on tax returns
- Any income that cannot be documented and verified
- Room/Boarder rent from subject property
- Income derived from an activity that is prohibited by federal, state or local law, rules and regulations cannot be considered. This applies to both W2 and self-employment, regardless if reporting income or loss. Income sources may include, but not limited to:
  - Foreign shell banks
  - Medical marijuana dispensaries
  - Any business or activity related to marijuana or CBD (e.g. growing, processing, distribution, etc.) even if legally permitted under state or local law.
  - Businesses engaged in any type of internet gambling.
- Income derived from virtual currency, such as cryptocurrency, including but not limited to:
  - Income paid to or earned by the borrower in the form of cryptocurrency
  - Assets to establish income continuance such as retirement distributions, trust or dividend/interest income
  - Use in assets as a basis for repayment of obligations
  - Rental payments. When a lease is necessary the payment on the lease must be reflected in U.S. dollars.

FOREIGN INCOME

Foreign income is income earned from a foreign corporation or a foreign government and is paid in foreign currency. Borrowers may use foreign income to qualify if the following requirements are met:

- All income must be converted to US dollars based on the exchange rate at the time of underwriting for qualifying purposes.
- All written communication must be presented in English or translated to English by a certified translator.

<table>
<tr><th colspan="4">Foreign Income – US Citizen Resident Alien (Green Card)</th></tr>
<tr><th>Residency</th><th>Occupancy</th><th>Verification</th><th>Ineligible</th></tr>
<tr><td rowspan="3">May live abroad, but must still maintain a present address within the US</td><td rowspan="3">Subject to underwriter's discretion</td><td>Copies of his or her signed federal income tax returns filed with the IRS for the past two years that include foreign income verified with 4506C</td><td rowspan="2">Self-employed borrower who earns the self-employments income from a country other than the United States and is not reported on Schedule C or Schedule E of the borrowers 1040's.</td></tr>
<tr><td>Foreign earned pension converted to US currency</td></tr>
<tr><td>Documentation to satisfy the standard documentation requirements</td><td>Unlawful aliens not eligible</td></tr>
</table>

Foreign Income – Non-Permanent Resident Alien (Visa)			
Residency	Occupancy	Verification	Ineligible
Must currently and lawfully reside in the US	Subject to underwriter's discretion	Copies of his or her signed federal income tax returns filed with the IRS for the past two years that include foreign income verified with 4506C	Self-employed borrower who earns the self-employments income from a country other than the United States.

		Foreign earned pension converted to US currency	Previously self- employed borrowers are not eligible
		Documentation to satisfy the standard documentation requirements	Unlawful aliens not eligible

INCOME DOCUMENTATION

HELOC – LOAN AMOUNTS ≤ $150,000

Scenario	Paystub OR The Work Number with verification of income	Previous year's W-2(s) OR The Work Number with verification of income	Most recent year's personal and business tax returns	Tax transcripts
Hourly/Salary Base Only	X			
Hourly/Salary with OT or Bonus	X	X		
Commission	X	X		
Self-Employed			X	X

HELOC – LOAN AMOUNTS > $150,000

Scenario	Paystub OR The Work Number with verification of income	Previous year's W-2(s) OR The Work Number with verification of income	Most recent two year's personal and business tax returns	Tax transcripts
Hourly/Salary Base Only	X	X		
Hourly/Salary with OT or Bonus	X	X		
Commission	X	X		
Self-Employed			X	X

HELOC – ALL LOAN AMOUNTS

See Other Non-Employment Income for additional income requirements not included below.

Scenario	*One of the Following:*			
	1099	Award Letter or Pension Statement	Bank statement with Direct Deposit	Most recent year's personal tax returns[1]
Social Security (SSI and SSD)	X	X	X	X
Pension	X	X	X	X

1 When tax returns are used to determine income, tax transcripts are required

EMPLOYMENT

The applicant's past employment record and the employer's confirmation of current, ongoing employment status should be examined when analyzing employment. AAA should confirm applicant has been employed for the past 2 years (hourly/salaried/commissioned/self-employed). The depth and breadth of employment and income verification should be commensurate with the type and size of the transaction, and the applicant's credit risk profile.

Applicants with non-consecutive and/or non-reoccurring employment histories must have financial strengths in order to be considered for maximum financing. Applicants who work in certain industries may experience frequent job changes due to the nature of the work (e.g. seasonal or unskilled labor). In these instances, applicants will be considered if they are able to demonstrate the ability to maintain a steady income despite the changes.

EMPLOYMENT DOCUMENTATION

This section addresses the sources of documentation that may be used to verify salary/wage earner income and the principle methods of validating authenticity.

Telephone Verification (VVOE)
The phone number the applicant provided as their employer's number must be independently confirmed by using the phone book, or other source, such as the internet. Contact with the employer must be documented in writing, or captured in the underwriting system and include the name of person contacting the employer, company name, name and title of the person confirming the information, date of contact, and information that was verified.

Pay Stubs
Must be computer generated and include the following information in order for it to be considered an acceptable form of verification: company's name or employer Tax I.D. that matches the W-2, name and/or social security number of the employee, the pay period covered, the year-to-date gross earnings, list all deductions. Paystubs must be dated within 120 days of the Note date.

W-2's
A W-2 form is a summary of earnings statement that the employer prepares and sends to its employees at the end of the year.

Loan amounts over $150,000, a copy of the most recent year W-2 is required to verify annual income and employment for each borrower.

Form 4506/4506-C
If pay stubs do not contain all required information and tax returns are used to verify income, the applicant must also sign a 4506 form. The form may be required at application or closing.

Verification of Employment (WVOE) Form
A written VOE showing year-to-date income may be substituted for a verbal VOE, pay stub(s) and W-2(s), provided it contains year-to-date earnings and the prior year's earnings. The VOE must be completed, signed, and dated by the owner, partner, or Human Resources representative, along with the date and phone number. Forms completed by the applicant will not be accepted.

Internet Verifications
Downloads from the Internet are acceptable provided they meet all general guidelines outlined in this section. The existence of the web site from which the documents were derived must be verified. Printed web pages must show the uniform resource locator (URL) address and the date and time printed.

EMPLOYMENT VERIFICATION

VERIFICATION OF EMPLOYMENT (VOE)

The phone number the applicant provided as their employer's number must be independently confirmed by using the phone book or other source, such as, the internet. Contact with the employer must be documented in writing, or captured in the underwriting system, and include the name of person contacting the employer, company name, name and title of the person confirming the information, date of contact, and information that was verified.

Income Type	Requirements
Wage Earner	Verbal verification of employment is required on currently employed wage earners when: • the loan amount is greater than $100,000; OR, • the loan amount is greater than $75,000 AND the CLTV is greater than 80%. The VVOE must be dated within 10 business days of the Note date unless the following applies: • If a borrower is in the military, a military Leave and Earnings Statement (LES) dated within 30 days of the closing is acceptable in lieu of a verbal or written VOE. • Because third party vendor databases are typically updated monthly, the verification must evidence that the information in the vendor's database was not more than 35 days old as of the Note date
Self-employed borrower	The existence of the business must be documented within 120 days prior to the note date. The existence of the borrower's business must be verified from a third- party source. Acceptable third- party sources include the following: • CPA, regulatory agency, or the applicable licensing bureau, if possible, or • By verifying a phone listing and address for the borrower's business using the internet or directory assistance.

TAX TRANSCRIPTS

When tax returns are used to document the qualifying income, the most recent (1) year tax transcripts results will be required regardless of the number of applicable years required unless the following apply:

- Transcripts are not required if the borrower is an existing AAA customer with one of the following:
  - Transcripts were previously obtained/provided to AAA for most recent year used for qualification
  - There is no significant increase (defined as 10%) to the income source based on the last available transcript for the borrower
  - Borrower has a satisfactory mortgage payment history of at least 12 months with AAA
- In the case where the most recent tax year has been filed and the tax transcripts are not yet available from the IRS, the tax returns may be used for qualification when the following are met:
  - The IRS response to the request must reflect “No Record on File”.
  - The most recent tax year does not represent a large increase, defined as greater than 10% of the previous year’s income. If large increase is needed for qualification, third-party transcripts must be obtained.
  - Additional required prior year(s) and amended tax returns must obtain third-party tax transcript(s), regardless of the tax year, as applicable
  - Alternative Documentation must be provided to document tax filing for the most recent year with one of the following:
    - ✓ Borrower-obtained tax transcripts for the applicable year, or
    - ✓ A bank account statement reflecting amount received from or paid to the IRS that aligns with the amount reflected on the most recent year returns. The information reflected on a bank statement is subject to standard asset review requirements. The IRS printout “Where’s My Refund” or Record of Account confirming refund or payment will also be acceptable in lieu of a bank statement

EMPLOYMENT STABILITY

INCOME ADEQUACY & CONTINUANCE

The applicant should have a history of generating steady income for at least 2 years*. Qualifying income must be:

- Recurring;
- Received regularly
- Received in cash (includes check, wire-transfer, etc.) and paid tax on the income as evidenced by a U.S. tax return;
- Reasonable based on the source

The applicant must be receiving income if it is to be included as qualifying income. However, the potential to increase income may be considered a strong compensating factor if the applicant has recently completed education and/or training to enhance job opportunities/income. Income should be expected to continue during the entire term of the Note.

BORROWER EMPLOYED BY FAMILY MEMBER

Provide the most recent two (2) years personal tax returns with all schedules to determine stability of income and potential ownership interest to document less than 25% ownership.

EMPLOYMENT GAP

Explain any gaps in excess of 60 days during the past two years.

- Allowances can be made for seasonal employment gaps beyond 60 days, typical for the building trades and agricultural, if documented.
- Income received from secondary employment or multiple job sources, there may be no gap greater than 30 days in the last 12 months.

NEWLY ENTERING THE WORKFORCE

For a Borrower who has less than a two-year employment and income history, the Borrower's income may be qualifying income if the Mortgage file contains documentation to support that the Borrower was either attending school or in a training program immediately prior to their current employment history. School transcripts must be provided to document.

WAGE EARNER INCOME

Wage earner income is defined as compensation for services paid by a person, business, or organization at specified intervals is commonly referred to as salary or wage earner income. The pay schedules of wage earners can be classified into four general categories:

Full Time
The applicant is a permanent employee of a company and works a standard work week, usually totaling 35 to 40 hours a week.

Part Time
The applicant is a permanent employee of a company but the number of hours is not standardized, usually totaling less than 30 hours per week.

Temporary
The applicant is not a permanent employee of the company and therefore is not part of the company's permanent staff. Temporary employees usually work for contracted, or "as needed" period of time.

Occasional/Seasonal
The applicant works for a specified period of time on a specific job or project. Once completed, the applicant is on "standby" until he/she receives their next assignment (e.g. roofers, landscapers, and migrant farm workers)

If a wage earner intends to use income from other sources to qualify, the income may be considered stable to the extent that it is consistent and it is expected to continue based on the required documentation.

CONSUMERS RETURNING TO WORK AFTER AN EXTENDED ABSENCE

A consumer's income may be considered effective and stable when recently returning to work after an extended absence if he/she:

- Is employed in the current job for six months or longer; and
- Can document a two-year work history prior to an absence from employment using:
- Traditional employment verifications; and/or
- Copies of IRS Form W-2s or pay stubs.

Note: An acceptable employment situation includes individuals who took several years off from employment to raise children, then returned to the workforce. Important: Situations not meeting the criteria listed above may not be used in qualifying. Extended absence is defined as six months.

CALCULATING EMPLOYMENT INCOME

CONVERTING FROM PART TIME TO FULL TIME

When a borrower is converting from part time to full time with the same employer, the income must be documented with a paystub reflecting 30 days year-to-date earnings of full-time employment along with a WVOE to document the date the borrower transitioned to full time in order to use the current wages.

PRIMARY EMPLOYMENT LESS THAN 40 HOURS

When an applicant's primary employment is less than a typical 40- hour work week, the underwriter should evaluate the stability of that income as regular, on-going primary employment.

For example, a registered nurse may have worked 24 hours per week for the last year; although this job is less than the 40-hour work week, it is the applicant's primary employment and should be treated as such for qualifying purposes.

CALCULATING WAGE EARNER INCOME

Individuals either receive a fixed regular annual income, usually paid monthly, semimonthly, biweekly, or weekly, or they may work and get paid by the hour, day, or week. All receive regular compensation in the form of a paycheck and year-end income is reported via W-2. Each type of qualifying income is calculated differently.

Non-Fluctuating Employment Earnings	
Pay Period	**Calculation of Income**
Annual Salary	Annual rate of base pay divided by 12 (without overtime, bonus, or commission)
Monthly Salary	Monthly base pay as shown (without overtime, bonus, or commission)
Semi-monthly Salary	Base pay rate x 24 / 12
Bi-weekly Salary	Base pay rate x 26 / 12
Weekly Salary	Base pay rate x 52 / 12
Hourly	Rate of Pay x # Hours worked per week x 52 / 12

OTHER TYPES OF EMPLOYMENT-RELATED INCOME

OVERTIME & BONUS

Overtime is money paid to individuals who earn additional wages for time worked above and beyond the normal workday or workweek. A Bonus is money paid in addition to regular wages. Sometimes bonuses are paid on a regular basis throughout the year, and some employees receive a "guaranteed" bonus as part of an incentive plan.

Overtime and Bonus income can be used to qualify if it has been received for the past two years and documentation submitted for the loan does not indicate this income will likely cease.
A two-year average of bonus or overtime income must be used; periods of overtime and bonus income less than two years may be acceptable, provided the underwriter can justify and document in writing the reason for using the income for qualifying purposes. Note: 'projected' bonus income must also be verified in writing by the employer and scheduled to begin within 60 days of loan closing.

An earnings trend must be established and documented for overtime and bonus income. If either type of income shows a continual decline, a sound rationalization must be documented in writing for including the income when qualifying the applicant; the applicant will be qualified using the lower amount. A period of more than two years must be used in calculating the average overtime and bonus income if the income varies significantly from year to year.

TIPS/GRATUITY

Tips or gratuity income is compensation received in addition to the employee’s straight salary or hourly wage. This type of income can be used to qualify if it is established and expected to continue.

COMMISSION INCOME

Verification of Commission Income:

- A minimum history of 2 years of commission income is recommended; however, commission income that has been received for 12 to 24 months may be considered as acceptable income, as long as there are positive factors to reasonably offset the shorter income history.
- One of the following must be obtained to document commission income:
    - a completed Request for Verification of Employment (Form 1005 or Form 1005(S)), OR
    - The borrower’s recent paystub and IRS W-2 forms covering the most recent two-year period

If the income is declining/has declined, the applicant will be qualified using the lower amount.

AUTO ALLOWANCE

The full amount of an automobile allowance received for at least the last two consecutive years may be included as income and the lease or financing expenditure must be included as a debt in the calculation of the debt-to-income ratio.

HOUSING/PARSONAGE INCOME

A housing or parsonage allowance may be considered qualifying income if there is documentation that it has been received for the most recent 12 months and the allowance is likely to continue for the next three years. The housing allowance may be added to income but may not be used to offset the monthly housing payment.

PART-TIME/SEASONAL/SECONDARY

Part-time or secondary income may be used to qualify if it can be documented that the applicant has worked the part-time job uninterrupted for the past two years, and is expected to continue. Verification of part-time or second-job income must be supported by IRS W-2 forms. If a borrower who has historically been employed on a part-time basis indicates that he or she will now be working full-time, written confirmation must be obtained from the borrower's employer.

Occasionally, an applicant who has less than a 2-year history of receiving income from part-time or multiple-job employment may need that income to qualify for the mortgage. There is flexibility of accepting less than a 2-year history, but no less than a 12-month history for a borrower if there is a strong likelihood that the borrower will continue to receive that income and the lender develops an average monthly income for the part-time or multiple jobs.

Situations in which a shorter history of receiving income from a part-time job may be acceptable include those in which there are two borrowers, one who has always been a full-time employee and one who had recently returned to work on a part-time basis; those in which a full-time employee took on a second, part-time job to offset the loss of income from overtime pay that was no longer available from his or her primary source of employment; etc.

When a borrower relies on the income from a second job to qualify for a mortgage, it should be determined if there has been any change in the borrower's overall employment status that might jeopardize the continuance of income from the second job. For example, if a borrower recently accepted a new primary job, but arranged to continue working at his or her old job as a second job, the borrower would have a history of receiving income from what is now considered a second-job, but there would be no history of his or her ability to handle two jobs on a continuing basis. For that reason, the income from this second job would not be acceptable to use in qualifying the borrower.

Seasonal, part-time or second job income (including seasonal unemployment compensation) can be considered as stable income if the borrower has worked in the same job (or line of seasonal work) for the past two years and the borrower's employer indicates that there is a reasonable expectation that the borrower will be rehired for the next season. Examples of borrowers who have seasonal jobs include outdoor laborers (landscapers, construction workers, etc.), income tax preparers, supplemental department store personnel who work during the Christmas shopping period or another holiday period, etc. Seasonal unemployment compensation should not be used to qualify the borrower unless it is appropriately documented, clearly associated with seasonal layoffs, expected to recur and reported on the borrower's federal income tax returns.
For qualifying purposes, “part-time” income refers to employment taken to supplement the applicant’s income from regular employment; part-time employment is not a primary job and it is worked less than 40 hours.

TEMPORARY LEAVES OF ABSENCE (INCLUDING MATERNITY LEAVE)

Temporary leave from an employer may encompass various circumstances (e.g. family and medical, short-term disability, maternity, other temporary leaves with or without pay). Temporary leave is generally short in duration. The period of time that borrower is on temporary leave may be determined by various factors such as applicable law, employer policies and short-term insurance policy and/or benefit terms. Leave ceases being considered temporary when the borrower does not intend to return to the current employer or does not have a commitment from the employer to return to employment.

During a temporary leave, a borrower’s income may be reduced and/or completely interrupted. The lender must determine that during and after the temporary leave the borrower has capacity to repay the HELOC and all other monthly obligations.

Determining qualifying income and borrower capacity to meet obligations while on temporary leave:

- For borrowers returning to their current employer prior to the first home equity payment due date:
  - The lender may use for qualifying income the borrower’s gross monthly income amount that will be received upon the borrower’s return to their current employer.
- For borrowers returning to their current employer after the first payment due date the lender must determine the income amount that will be received upon the borrower’s return to their current employer. The lender must take into account any temporary reductions in income when determining qualifying income, as follows:
  - The lender may use for qualifying income the Borrower’s gross monthly income amount being received during the temporary leave. In the event that the income has been reduced or interrupted, the lender may use for qualifying income the monthly reduced amount (this amount may be zero) being received during the temporary leave combined with the partial or complete income supplement up to the amount of the income reduction.
  - The total qualifying income must not exceed the gross monthly income that will be received upon the borrower’s return to current employer.

- Assets that are required for the transaction, e.g., closing costs, financing costs, may not be considered as available assets to supplement the income.

Documentation Requirements
The following documents must be retained in the loan file:

- Verification of the Borrower's pre-leave income and employment
- Documentation from the current employer confirming the borrower's statutory right to return to work, or the employer's commitment to permit the borrower to return to work. The confirmation date of return, and the borrower's post leave employment and income.
- Written statement signed by the borrower confirming that the borrower will return to their current employer stating the confirmation date of return that has been agreed upon between the borrower and the employer.

In addition, the following documentation is required for borrowers returning to the current employer after the first mortgage payment due date:

- Documentation evidencing amount, duration, and consistency of all temporary leave income sources being used to qualify the borrower, e.g., short-term disability benefits or insurance, sick leave benefits, temporarily reduced income from employer, that are being received during the temporary leave
- All available liquid assets used to supplement the reduced income for the duration of the temporary leave must meet requirements of and be verified.

RESTRICTED STOCK (RS) AND RESTRICTED STOCK UNITS (RSU)

Employers increasingly include RS and RSU as a component of employee compensation. RS are grants of company shares which represent equity interest in the company. RSU are grants valued in terms of company shares that do not represent equity interest in the company. Both RS and RSU are subject to a restriction period during which recipients are not permitted access to granted shares until vesting requirements are met. Vesting requirements are based on varying criteria but the most common types are:

- Performance-based (e.g., a certain percentage of total granted shares vest based on individual or corporate performance), and
- Time-based (e.g., a certain percentage of total granted shares vest after a pre-determined period of employment)

Documentation Requirements
RS and RSU may be used to qualify the Borrower for the Mortgage, provided the following requirements have been met:

Income Type	**Stable Monthly Income Requirements**	**Documentation Requirements**
RS and RSU subject to performance-based vesting provisions	History of receipt: • Two years, consecutive • To be considered for history of receipt, RS and RSU used for qualifying must have vested and been distributed to the Borrower from their current employer, without restriction	All of the following: • YTD paystub(s) documenting all YTD earnings, including payout(s) of RS or RSU, W-2 forms for the most recent two calendar years and a 10- dayprior to close verbal verification of employment. Income verification obtained through a third-party

Income Type	Stable Monthly Income Requirements	Documentation Requirements
	Continuance: Must be likely to continue for at least the next three years. The underwriter is not required to obtain documentation to verify income continuance, absent any knowledge, information or documentation that the income is no longer being received or is likely to cease.	verification service provider is not permitted. Or all of the following: • Written VOE documenting all YTD earnings (including payout(s) of RS or RSU) as well as earnings for the most recent two calendar years, and a 10-day prior to close verbal verification of employment. Income verification obtained through a third-party verification service provider is not permitted. Additional documentation requirements applicable to all documentation levels: • Evidence the stock is publicly traded • RS and/or RSU agreement • Most recent vested schedule(s) detailing past and future vesting • Evidence of receipt of previous year(s) payout(s) of RS/RSU (e.g., year-end paystub, employee-provided statement paired with a brokerage or bank statement showing transfer of shares or funds) that must, at a minimum, include: o Date(s) of the payout(s) The number of vested shares or its cash equivalent distributed to the Borrower (pre-tax)

Calculation

SUBJECT	REQUIREMENT AND GUIDANCE
RS and RSU subject to performance-based vesting provisions	Based on the form in which vested RS or RSU are distributed to the borrower (i.e., as shares or its cash equivalent), the seller must use the applicable method(s) below to calculate the monthly income: RS or RSU distributed as shares: Multiply the 52-week average stock price as of the application received date by the total number of vested shares distributed (pre-tax) to the borrower in the past two years, then divide by 24.

SUBJECT	REQUIREMENT AND GUIDANCE
	(e.g. if 200 vested shares were distributed (pre-tax) in the past two years and the 52-week average stock price as of the application received date is $10, multiply 200 x $10 then divide by 24=$83.33 monthly income) RS or RSU distributed as cash equivalent: Use the total dollar amount distributed (pre-tax) from the cash equivalent of vested shares in the past two years and divide by 24. Refer below for more information about fluctuating earnings.
RS and RSU subject to time-based vesting provisions	Based on the form in which vested RS or RSU are distributed to the Borrower (i.e., as shares or its cash equivalent), the Seller must use the applicable method(s) below to calculate the monthly income: RS or RSU distributed as shares: Multiply the 52-week average stock price as of the Application Received Date by the number of vested shares distributed (pre-tax) to the Borrower in the past year, then divide by 12. (e.g., if 50 vested shares were distributed (pre-tax) in the past year and the 52-week average stock price as of the Application Received Date is $10, multiply 50 x $10 then divide by $12=$41.67 monthly income) RS or RSU distributed as cash equivalent: Use the total dollar amount distributed (pre-tax) from the cash equivalent of vested shares in the past year and divide by 12. Refer below for more information about fluctuating earnings.

Analysis of Income Fluctuation and Stability

The determination of stability for RS and RSU income used to qualify must include analysis of changes in the company's stock price as well as past and future distributions detailed in a vesting schedule. If the YTD earnings are consistent with the previous year(s) earnings or trending upward, then the underwriter must use the applicable calculation method(s) below to determine the monthly income. If the earnings are not consistent (i.e., the value of vested shares distributed decreases substantially year-over-year), additional analysis is required and additional documentation may be necessary to determine income stability and develop an accurate calculation of qualifying income.

Eligible Asset
Stock with limitations on its accessibility (e.g., restricted stock which has not vested and been distributed to the recipient) is not eligible source of borrower funds and may not be used for closing costs.

SELF-EMPLOYMENT INCOME

GENERAL

A consumer with a 25 percent or greater ownership interest in a business is considered self-employed. The following factors must be analyzed before approving a home equity transaction for a self-employed borrower:

- The stability of the borrower's income,
- The location and nature of the borrower's business,
- The demand for the product or service offered by the business,
- The financial strength of the business, and
- The ability of the business to continue generating and distributing sufficient income to enable the borrower to make the payments on the requested mortgage.

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

- Sole proprietorships;
- Corporations;
- Limited liability or "S" corporations; and
- Partnerships.

MINIMUM LENGTH OF SELF-EMPLOYMENT

Income from self-employment is considered stable, and effective, if the consumer has been self- employed for two or more years.

Due to the high probability of failure during the first few years of a business, the requirements described in the table below are necessary for consumers who have been self-employed for less than two years.

If the period of self-employment is:	Then:
Between one and two years	For the individual's income to be effective, the individual must have at least two years of documented previous successful employment in the line of work in which the individual is self-employed, or in a related occupation. A combination of one year of employment and formal education or training in the line of work the individual is self-employed or in a related occupation is also acceptable.
Less than one year	The income may not be considered when qualifying the borrower

INCOME OR LOSS REPORTED ON SCHEDULE K-1 (IRS FORMS 1065 OR 1120S)

Business income reported on Schedule K-1 may be used to qualify only when the borrower has a documented history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify.
Caution must be used when including income that the borrower draws from the borrower's partnership or S corporation as qualifying income. Ordinary income, net rental real estate income, and other net rental income reported on Schedule K-1 may be included in the borrower's cash flow provided:

- The borrower can document ownership share (may use Schedule K-1), and
- The business has adequate liquidity (e.g. working capital) to support the withdrawal of earnings. A written evaluation of the business income must be retained in the file.

If…	Then…
The Schedule K-1 reflects a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify,	No further documentation of access to the income or adequate business liquidity is required. The Schedule K-1 income may then be included in the borrower's cash flow.
The Schedule K-1 does not reflect a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify,	The lender must confirm the following to include the income in the borrower's cash flow: o The business has adequate liquidity (working capital) to support the withdrawal of earnings.
The borrower has a two-year history of receiving "guaranteed payments to the partner" from a partnership or an LLC,	These payments can be added to the borrower's cash flow
Business tax returns are required,	The underwriter must consider the type of business structure and analyze the business returns

DOCUMENTATION

Self-employed documentation requirements differ based on the loan amount:

- Most recent one to two years of signed individual federal income tax returns—IRS Form 1040.
  - Tax transcript(s) obtained directly from the IRS may be used in lieu of signed tax returns.
- Most recent one to two years of IRS Schedule K-1.
- Most recent one to two years of signed business federal income tax returns (IRS Form 1065 or IRS Form 1120S).
- In cases where the most recent tax year has not year been filed, between the tax filing date (typically April 15) and the extension period date (typically October 15) a copy of the filed tax extension must be provided. The applicable number of prior year(s) tax returns must be provided.
- All applicants whose income is verified with tax returns, must sign IRS Form 4506 – Request for Copy of Tax Return – (or 4506-C Request for Transcript of Tax Returns) for the individual, and if applicable, for the business.
- See Tax Transcript Section for additional requirements

If an applicant has submitted required income documentation with an existing or pending First Mortgage and/or Commercial Relationship, the underwriter may relay on the following:

First Mortgage Relationships:

- Residential first mortgage derived income may be used; AND
- IDM may be used as repository for income docs/assets.

ANALYZING TAX RETURNS FOR A PARTNERSHIP, LLC AND S CORPORATION

Evaluating Business Income for Partnership, LLC and S Corporation

When the borrower has 25% or more ownership interest in the business and business tax returns are required, the underwriter must perform a business cash flow analysis and evaluate the overall financial position of the borrower's business to determine whether:

- Income is stable and consistent, and

- Sales and earnings trends are positive.

If the business does not meet these standards listed above, business income cannot be used to qualify the borrower.

Borrower's Proportionate Share of Income/Loss for a Partnership and LLC
The borrower's proportionate share of income or loss is based on the borrower's partnership percentage of Ending Capital in the business as shown on the IRS Form 1065, Schedule K-1. Only the borrower's proportionate share of the business income or loss after making the adjustment to the business cash flow can be used when qualifying the borrower for the mortgage loan.

Borrower's Proportionate Share of Income or Loss for an S Corporation
The borrower's proportionate share of income or loss is based on the borrower's (shareholder) percentage of stock ownership in the business for the tax year as shown on IRS Form 1120S, Schedule K-1. The cash flow analysis should consider only borrower's proportionate share of the business income (or loss), taking into account any adjustments to the business income that are discussed below. Business income may only be used to qualify the borrower if the lender obtains documentation verifying that:

- The borrower has ownership of the income (Schedule K-1 may be used to document ownership share)

Alternatively, the lender can obtain documentation verifying that:

- The business has adequate liquidity (e.g. working capital) to support the withdrawal of earnings.
  - A written evaluation of the business income must be retained in the mortgage file.

Earnings from a Corporation (1120)
It is only required to document access to business income if the borrower is less than 100% owner of the business (i.e. 1120) and the income is not reporting on the borrower's personal tax returns.

ADJUSTMENTS TO BUSINESS CASH FLOW

Partnership, LLC and S Corporation

Items that can be added back to the business cash flow include depreciation, depletion, amortization, casualty losses, and other losses that are not consistent and recurring. The following items should be subtracted from the business cash flow:

- Meals and entertainment exclusion,
- Other reported income that is not consistent and recurring, and
- The total amount of obligations on mortgages or notes that are payable in less than one year.

These adjustments are not required for lines of credit or if there is evidence that these obligations roll over regularly and/or the business has sufficient liquid assets to cover them.

Income from Partnerships, LLCs, Estates, and Trusts
Income from partnerships, LLCs, estates, or trusts can only be considered if the lender obtains documentation verifying that:

- The borrower has ownership of the income (Schedule K-1 may be used to document ownership share), and
- The income was actually distributed to the borrower.

- Alternatively, the lender can obtain documentation verifying that:
- The borrower has access to the income through a partnership agreement, LLC operating agreement, or other documentation that the lender determines is appropriate, unless the borrower(s) own 100% of the business in which case confirmation of access to the income is not required; and
- The business has adequate liquidity (e.g. working capital) to support the withdrawal of earnings. A written evaluation of the business income must be retained in the file.

OWNERSHIP IN THE BUSINESS < 25%

For borrowers who have less than 25% ownership of a partnership, S corporation, or limited liability company (LLC), ordinary income, net rental real estate income, and other net rental income reported on IRS Form 1065 or IRS Form 1120S, Schedule K-1 may be used in qualifying the borrower provided:

- The borrower can document ownership share (may use Schedule K-1),
- The borrower can document access to the income, and
- The business has adequate liquidity (e.g. working capital) to support the withdrawal of earnings. A written evaluation of the business income must be retained in the file.

If…	**Then…**
The Schedule K-1 reflects a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify,	No further documentation of access to the income or adequate business liquidity is required. The Schedule K-1 income may then be included in the borrower's cash flow.
The Schedule K-1 does not reflect a documented, stable history of receiving cash distributions of income from the business consistent with the level of business income being used to qualify,	The lender must confirm the following to include the income in the borrower's cash flow: o The business has adequate liquidity (working capital) to support the withdrawal of earnings.
The borrower has a two-year history of receiving "guaranteed payments to the partner" from a partnership or an LLC,	These payments can be added to the borrower's cash flow
Business tax returns are required,	The underwriter must consider the type of business structure and analyze the business returns

An exception to the two-year requirement of receiving "guaranteed payments to the partner" is if a borrower has recently acquired nominal ownership in a professional services partnership (for example, a medical practice or a law firm) after having an established employment history with the partnership. In this situation, the lender may rely upon the borrower's guaranteed compensation. This must be evidenced by the borrower's partnership agreement and further supported by evidence of current year- to-date income.

Documentation Requirements – For Schedule K-1 documentation requirements, the borrower must provide the most recent two years of signed individual federal income tax returns and the most recent two years of IRS Schedule K-1. If the K1 does not reflect a documented stable history of receiving cash distributions of income, two years business returns will be required to demonstrate the business has adequate liquidity (e.g. working capital) to support the withdrawal of earnings.

SECONDARY SELF-EMPLOYMENT INCOME

It is not required to account for self-employment loss when the borrower is qualified using only income that is not derived from self-employment and self-employment is a secondary and separate source of income (or loss). Examples of income not derived from self-employment include salary and retirement income.

RENTAL INCOME-

CALCULATING MONTHLY NET RENTAL INCOME OR LOSS

When the subject property is a 2-4-unit principal residence, you must calculate rental income as follows:

Rental Income from the Subject Property		
Does Borrower Have History of Receiving Rental Income from Property?	**Documentation Requirements**	**Calculate Monthly Net Rental Income (or Loss)**
Yes	Document the rental cash flow by obtaining a copy of the most recent year filed tax return, pages 1 and 2 and Schedule E	Analyze the borrower's cash flow and calculate the net rental income (or loss) per month from the returns
No	Leases can only be used if a property is not listed on Schedule E because it was acquired subsequent to filing the tax return).	The gross rental income from the property is equal to the lesser of the market rent established by the appraiser or the current rent based on the existing lease agreement(s). Net rental income equals 75% of the gross rent; the remaining 25% of the gross rent is absorbed by vacancy losses and ongoing maintenance expenses.

When the borrower owns additional property that is rented, calculate the monthly net rental income (or loss) in accordance with the following table:

Rental Income from Property Other Than the Security Property		
Does Borrower Have History of Receiving Rental Income from Property?	**Documentation Requirements**	**Calculating Monthly Net Rental Income (or Loss)**
Yes	Document the rental cash flow by obtaining a copy of the most recent year filed tax return, pages 1 and 2 and Schedule E	Analyze the borrower's cash flow and calculate the net rental income (or loss) per month from the returns
No	Obtain copies of current lease agreements (only if a property is not listed on Schedule E because it was acquired subsequent to filing the tax return).	Net rental income is 75% of the gross rent from the lease agreements, with the remaining 25% being absorbed by vacancy losses and ongoing maintenance expenses.

Treatment of the Income (or Expense)
The amount of monthly net rental income (or loss) that is considered as part of the borrower's total monthly income (or expenses) and its treatment in the calculation of the borrower's total debt-to- income ratio will vary depending on whether the borrower occupies the rental property as his or her principal residence.

If the net rental income (or loss) relates to the borrower's principal residence:
- The monthly net rental income (as defined above) must be added to the borrower's total monthly income.
- Any net rental loss must be added to the borrower's total monthly obligations.
- The full amount of the mortgage payment (PITIA) must be included in the borrower's total monthly obligations when calculating the debt-to-income ratio.

If the net rental (or loss) relates to a property other than the borrower's principal residence:
- The monthly net rental income (as defined above, but excluding the full amount of the related mortgage payment) must be added to the borrower's total monthly income.
- Any monthly net rental loss must be added to the borrower's total monthly obligations.
- The full PITIA for the rental property is factored into the amount of the net rental income (or loss), therefore, it should not be counted as a monthly obligation.
- The full PITIA for the borrower's principal residence must be counted as a monthly obligation.

When Schedule E is used to calculate rental income, the full PITIA must be accounted for. Any listed depreciation, interest, taxes, insurance, or HOA expenses will be added back to the borrower's cash flow. Please refer to the Fannie Mae Rental Income Worksheets Forms 1037 or 1038 or the Freddie Mac Rental Income Worksheet Form 92.

When the borrower is using rental income to qualify for the mortgage the entire PITIA of the property must be considered when evaluating property cash flow regardless of the obligated party.

<u>OTHER NON-EMPLOYMENT INCOME</u>
GENERAL
If the applicant intends to use income from other non-employed/non-self-employed sources to qualify, the income may be considered stable to the extent that it is consistent and it can be established that income appears to be sustainable for a specified period of time or the loan term based on the required documentation. Factors that should be considered in determining the likelihood of consistent payments include, but are not limited to the following:
- Whether the payments are received pursuant to a written agreement, court decree, or law;
- The length of time the payments have been received;
- Eligibility criteria governing the continued receipt of the income, such as age of dependents or accumulation of assets.

DOCUMENTATION
If other non-employed income is used to qualify, the applicant must have a history of receiving the income regularly, and demonstrate that the income appears to be sustainable, and/or will continue for a specific period of time or the loan term. In order to verify the duration in which the applicant has

received, and will continue to receive other non-employed income, the following documentation may be obtained:

- Most recent award letter, pension statement, court order/agreement, asset statement from which the income is generated, notes receivable, agreements etc. confirming the amount, frequency, duration of payment, and what if any portion is tax free, or;
- Tax returns with all schedules from previous two years, most recent 1098 and/or most recent 1099, or;
- Most recent bank statements showing receipt of income.

Evidence in the file shall demonstrate that the applicant income was considered to the extent that it is reliably and regularly received.

ALIMONY/CHILD SUPPORT/SEPARATE MAINTENANCE

In order for alimony or child support to be considered as acceptable, stable income, the applicant must have received the income for at least 12 months and it must be expected to continue for at least 3 years as specified by the court order, final divorce decree, legal separation agreement, voluntary payment agreement or an attorney's letter specifying the individuals and issues.

Child support may be "grossed up" by 25% to account for tax deductions.

We will accept as verification that alimony or child support will continue to be paid. A photocopy of the divorce decree, or separation agreement if the divorce is not final, that provides for the payment of alimony or child support and states the amount of the award and the period of time over which it will be received; any other type of written legal agreement or court decree that describes the payment terms for the alimony or child support; or any application of state law that requires alimony, child support, or maintenance payments may be used as income.

FOSTER CARE

Income that a borrower receives from a state or county-sponsored organization for providing temporary care for one or more children may be considered as acceptable stable income as long as the borrower has a 2-year history of providing foster-care services and is likely, in the foreseeable future, to continue to provide such services at a level that supports the amount of income needed for qualifying for the loan. If a borrower has not been receiving this type of income for 2 full years, we may nevertheless count the income as stable income, as long as the borrower has at least a 12-month history of providing foster care services and this income does not represent more than 30% of the total gross income that is used to qualify the borrower for the mortgage.

Foster-care income may be verified by:

- Letters from the organizations providing the income,
- Copies of the borrower's signed federal income tax returns that were filed with the IRS, or
- Copies of the borrower's deposit slips or bank statements that confirm the regular deposit of the payments.

CAPITAL GAINS INCOME

Income received from a capital gain is generally a one-time transaction; therefore, it should not usually be considered as part of the borrower's stable monthly income. However, if the borrower needs to rely on the income from capital gains to qualify for the mortgage, copies of the borrower's signed federal income tax returns that were filed with the IRS for the past two years, including the related Capital Gains and Losses (Schedule D to IRS Form 1040) must be obtained. When the borrower's tax returns show that he or she has realized capital gains for the last two years, develop an average income from capital gains and use that amount as part of the borrower's qualifying income, as long as the borrower provides evidence that he or she owns additional property or assets that can be sold if extra income is needed to make future mortgage payments.

The sale of real estate is not acceptable to be used as qualifying income unless documentation can establish that the borrower does this for a living.

UNEMPLOYMENT BENEFITS

Unemployment benefits, such as those received by seasonal workers, may be considered as acceptable income if the income is properly documented, has been received for the past 2 years and is predictable and likely to continue (as discussed for seasonal unemployment compensation). Copies of the borrower's signed federal income tax returns that were filed with the IRS for the past 2 years should be used to establish a history of the receipt of these benefits.

DISABILITY/WORKER'S COMPENSATION

Disability benefit payments should be treated as acceptable income unless the terms of the disability policy specifically limit the stability or continuity of the benefit payments. Benefits that have a defined expiration date must have a remaining term of at least three years from the date of the mortgage application in order to be used for qualifying the borrower. For example, if a borrower is receiving disability benefits that are scheduled to be discontinued when he or she reaches a certain age and the borrower will reach that age within three years of loan closing, the lender should not count the disability benefit as stable income. When a borrower is currently receiving short-term disability payments that will decrease to a lesser amount within the next three years because they are being converted to long-term benefits, the lender must use the amount of the long-term payments in determining the borrower's stable income.

Generally, long-term disability will not have defined expiration date and must be expected to continue. The requirement for re-evaluation of benefits is not considered a defined expiration date.

Verification of long-term disability must be documented with one of the following:

- Obtain a copy of the borrower's disability policy or benefits statement from the benefits payer (insurance company, employer, or other qualified disinterested party) to determine:
  - The borrower's current eligibility for the disability benefits, and
  - The amount and frequency of the disability payments, and
  - If there is contractually established termination or modification date
- Social Security income for long term disability will not have defined expiration date and must be expected to continue. Verification of income must be documented with one of the following:
  - A copy of the Social Security Administration's award letter; or
  - Copies of signed federal income tax returns; or
  - Social Security Benefit Statement (Form SSA-1099); or
  - Copies of the borrower's recent bank statements.

NOTES RECEIVABLE

Payments on notes receivable must continue for at least 3 years from the date of the mortgage application in order to be considered as acceptable stable income. We require a copy of the note to establish the amount and length of payment. Borrowers must provide evidence the funds have been received for the past 12 months. Acceptable evidence includes deposit slips, copies of signed federal income tax returns that were filed with the IRS or copies of the borrower's bank statements that show consistent deposits of these funds.

RETIREMENT, GOVERNMENT, AND PENSION INCOME

Individual retirement account (such as 401K or 403b), or annuity income is similar to pension and social security income except that it may not be payable for life. A copy of the most recent updated individual retirement account or annuity renewal statement showing the effective date, amount, frequency, and duration of the benefit payments showing the income will continue for at least 3 years must be obtained.

Document regular and continued receipt of the income as verified by

- Letters from the organizations providing the income,
- Copies of retirement award letters,
- Copies of retirement award letters,
- IRS W-2 or 1099 forms, or
- Proof of current receipt

If retirement income is paid in the form of a distribution from a 401(k), IRA, or Keogh retirement account, determine whether the income is expected to continue for at least three years after the date of the mortgage application. In addition

- The borrower must have unrestricted access without penalty to the accounts; and
- If the assets are in the form of stocks, bonds, or mutual funds, 70% of the value (remaining after any applicable costs for the subject transaction) must be used to determine the number of distributions remaining to account for the volatile nature of these assets.

If the retirement income is newly established, verification of current receipt is not required. Document the finalized terms of the newly established income including, but not limited to, the source, type, effective date of income commencement, payment frequency and pre-determined payment amount with the benefit verification letter, notice of award letter or other equivalent documentation from the payor that provides and establishes these terms. The income must commence prior to or on the first Mortgage payment due date.

All retirement income must be likely to continue for at least the next three years

Distributions from retirement accounts recognized by the Internal Revenue Service (IRS) (e.g., 401[k], IRA) that are not subject to penalty (e.g., early withdrawal penalty) may be considered stable monthly qualifying income. Evidence of the income source, type, distribution frequency, distribution amount(s), current receipt (as applicable) and history of receipt (as applicable), must be documented.

If distributions are being taken in accordance with certain IRS rules, such as the Required Minimum Distributions (RMD) rule (i.e., excise tax penalty applies if distributions are not taken), and evidence of current receipt of the required minimum distribution amount is obtained, history of receipt is not required for the income to be considered stable.

Due to the multiple variables inherent with distributions from retirement accounts, including, but not limited to, fixed and fluctuating income amounts, the history of receipt necessary to justify a stable monthly qualifying income amount may vary. This may include a range of history from zero to 24 months, depending upon the individual circumstances. As with all income, the underwriter (or “it” can be acceptable) must determine that the source and amount of the income are stable. Factors that the underwriter must consider when determining that the income used to qualify the Borrower is stable, and when determining the history of receipt necessary to justify a stable monthly qualifying income amount include, but are not limited to, the following:

- Frequency and regularity of receipt of the distributions
- Length of time the distributions have been taken and whether or not they establish a stable pattern of receipt over a given period of time. For example, consider whether or not the distributions are fixed amounts occurring with regular frequency or are fluctuating amounts occurring with or without regular frequency. For fixed amounts occurring with regular frequency, a lesser history of receipt may be needed in order to determine the amount and stability of the qualifying income than would be needed for fluctuating amounts. For fluctuating amounts, it may be necessary to obtain a longer history of receipt in order to determine the amount and stability of the qualifying income while taking into consideration whether or not the overall payments are similar when viewed year over year or with another similar measure, such as quarter over quarter.
- Rules governing distributions (e.g., IRS rules governing exceptions to early withdrawal penalties and Required Minimum Distributions (RMD), employer retirement plan rules and designs governing scheduled distribution terms). Certain rules may provide support for the frequency and regularity of receipt as well as continued receipt, thereby enabling a lesser amount of history to justify a stable monthly qualifying income amount.

Documentation Requirements:

- Most recent retirement account statement(s), documentation from financial institution holding retirement account that verifies regularly scheduled distribution arrangements, 1099(s) and/or other equivalent documentation showing income source, type, distribution frequency, distribution amounts and history of receipt (as applicable), and
- Bank statement(s) or other equivalent documentation evidencing current receipt (as applicable), and
- Evidence of sufficient assets to support the qualifying income

If the retirement distributions are not scheduled monthly payments (e.g., annual, semi-annual, quarterly), the most recent distribution verified through a retirement account statement, 1099 and/or other equivalent documentation, as applicable, is sufficient in lieu of current receipt; however, verification of receipt of multiple distributions may be necessary to determine frequency of distributions, history of receipt and amount of stable monthly qualifying income. Sufficient assets remaining after closing must be documented to support continuance of the retirement account distributions as income for at least the next three years.

A written rationale explaining the analysis used to determine the qualifying income must be provided, regardless of the underwriting path.

ANNUITY INCOME

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

SOCIAL SECURITY INCOME

Supplemental Security Income (SSI) may be considered as qualifying income that has a reasonable expectation of continuance unless there is evidence that the benefits will not continue. Pending or current re-evaluation of medical eligibility for benefit payments is not considered an indication that the insurance and/or benefit payment will not continue. Social Security benefits received on behalf of another beneficiary or under another's Social Security account or work record may not necessarily continue for three years. In these instances, documentation of continuance will be required.

MILITARY/VA BENEFITS

Military personnel may be entitled to different types of pay in addition to their base pay. The following may be considered stable income provided there is documentation verifying the income will continue for at least three years:

- Flight Pay
- Hazardous Duty Pay
- Rations
- Clothing Allowance
- Housing Allowance

Education benefits used to offset education expenses are not acceptable.

Obtain a copy of the borrower's last Leave and Earnings Statement (LES) to verify allotments, allowances, estimated time in service, and the amount of net and gross pay. Also, obtain and verify the following information from the borrower's latest Leave and Earnings Statement (LES):

- Military Rank
- Social Security Number
- Military Address
- Length of active service to date

The tax-free income from housing (BAQ), rations, uniforms, food, flight pay, etc., can be used as income to qualify for the loan. Grossing up of this income is subject to standard. The LES statement must show at least 12 months remaining for time in service, otherwise the tax-free income cannot be used to qualify for the loan. As long as there is at least 12 months remaining before the borrower's "out date" (as verified on the LES), a verbal verification of employment is not needed.

INTEREST & DIVIDENDS

Average interest and dividend income received for the last 2 years may be used to calculate the qualifying income. Before calculating the projected interest or dividend income, the underwriter will need to subtract any funds that are derived from these sources, or are required for the cash investment. Asset statements must be provided to support a three-year continuance. Asset statements must be provided to support a three-year continuance.

ROYALTY PAYMENTS

If the borrower needs to rely on income from royalty payments to qualify for the mortgage, the following documentation must be provided:

- Royalty contact, agreement, or statement confirming amount, frequency, and duration of the income; and
- Borrower's most recent signed federal income tax return, including the related IRS Form 1040, Schedule E.

Documented evidence showing that the borrower has received royalty payments for at least 12 months and will continue to receive them for at least three years after the date of the mortgage application is required in order to use the payments as qualifying income, and documentation of receipt of income.

TRUST INCOME

Income from a trust may be used if constant payments will continue for at least the first three years and is properly documented via a copy of the Trust Certificate or other trustee statement confirming the amount of the trust, frequency of distribution and duration of payments.

Trust account funds may be used for the required cash investment if the applicant provides adequate documentation that the withdrawal of funds will not negatively affect income.

EMPLOYMENT-RELATED ASSETS AS QUALIFYING INCOME

All of the following loan parameters must be met in order for employment-related assets to be used as qualifying income:

Parameter	Transaction Requirements
Maximum LTV/CLTV/HCLTV	70% for borrowers < age 62 80% for borrower = > age 62
Loan Purpose	Cash-out refinance only
Number of units	1-4 units
Income Calculation/Payout Stream	Divide “Net Documented Assets” by amortization term of the loan (in months)
Asset Ownership	Borrower(s) must match asset ownership

Asset Requirements

Assets used for monthly income stream must be owned individually by the borrower, or the co- owner of the asset must be a co-borrower of the subject property. Assets must be liquid and available to the borrower with no penalty.

- Non-self-employed severance package or non-self-employed lump sum retirement package (i.e., a lump sum distribution) must be documented with a distribution letter from the employer (1099R) and deposited to a verified asset account.
- 401(k) or IRA, SEP, KEOGH retirement accounts, the borrower must have unrestricted access to the funds in the accounts and can only use the account if distribution is not already set up or the distribution amount is not enough to qualify. The account and is composition must be documented with the most recent monthly, quarterly or annual statement.
- If a penalty would apply to a distribution of funds form the account made at the time of calculation, then the amount of such penalty applicable to a complete distribution from the account (after costs for the transaction) must be subtracted to determine the income stream from these assets.
- If the employment–related assets are in the form of stocks, bonds, and mutual funds, 70% of the value (remaining after costs for the transaction and consideration of any penalty) must be used to determine the income stream to account for the volatile nature of these assets.
- A borrower shall only be considered to have unrestricted access to a 401(k) or IRA, SEP, Keogh retirement account if the borrower has, as of the time of calculation, the unqualified and unlimited right to request a distribution of all funds in the account (regardless of any possible tax withholding or applicable penalty applied to such distribution).

Ineligible Assets

Non-employment related assets (e.g. stock options, non-vested restricted stock, lawsuits, lottery winnings, sale of real estate, inheritance, divorce proceeds, etc.)

Net Documented Assets
"Net documented assets" are equal to the sum of eligible assets minus:
- the amount of the penalty that would apply if the account was completely distributed at the time of calculation;
- the amount of funds used for down payment, closing costs, and required reserves;
- 30% of the remaining value of any stocks, bonds, or mutual fund assets (after the calculation in (b)).

Example: Calculation of net Documented Assets	
IRA (made up of stocks and mutual funds)	$500,000
Minus 10% of $500,000 ($5000,000 x .10) (assumes the borrower is not yet 59 ½ years of age at the time this income is being calculated; therefore, it is subject to a 10% penalty for early distribution. This penalty must be levied against any cash being withdrawn for closing the transaction as well as the remaining funds used to calculate the income stream.)	(-) $50,000
Total eligible documented assets	(=) $450,000
Minus funds required for closing (down payment, closing costs, reserves)	(-) $100,000
(a) Subtotal	(=) $350,000
Minus 30% of $350,000 ($350,000 x .30) (assumes funds are in the form of stocks, bonds, and mutual funds)	(-) $105,000
(b) Net Documented Assets	(=) $245,000
Monthly income calculation ($245,000/360 (or applicable term of loan in months)) See Income Calculation/Payout Stream in table below	$680.56/month

NON-EMPLOYMENT-RELATED ASSETS AS QUALIFYING INCOME
When the borrower has liquid assets that are not employment-related, the assets may be used to qualify the borrower if the following terms are met:

Parameter	Transaction Requirements
Maximum LTV/CLTV/HCLTV	60%
Occupancy	Primary Residence only
Loan Purpose	Cash-out refinance only
Number of units	1-2-unit properties only (3 to 4 units not eligible)
Asset Ownership	Borrower(s) must match asset ownership

Income Verification
To determine whether the borrower qualifies for the home equity transaction, the underwriter may convert the borrower's Other Financial Assets into an income stream as described in the Monthly Income Stream Calculation section below.

The income derived from the monthly income stream calculation must be entered as "Other Income" on the Uniform Residential Loan Application. Other Financial Assets used in the conversion technique shall not be considered as assets available for closing costs or reserves.

Interest, dividends, and capital gains from Other Financial Assets (reported on the borrower's tax return) cannot be used as additional income.

Reserves

The borrower's minimum reserve requirements may not be satisfied using any of the Other Financial Assets that are being converted into an income stream.

Asset Requirements

- Other Financial Assets must be owned individually by the borrower, or the co-owner of the assets must be a co-borrower of the HELOCs.
- Other Financial Assets used for the calculation of the monthly income stream must be liquid and available to the borrower with no penalty.
- If the Other Financial Assets are in the form of stock, bonds, mutual funds, or U.S. savings bonds, 70% of the value (remaining after costs for the transaction) must be used to determine the income stream to account for the volatile nature of these assets.
- If assets are in the form of demand deposit account, savings account or certificate of deposit, 100% of the value may be used to determine the income stream.
- Net documented assets are equal to:
  - The sum of eligible documented Other Financial Assets minus any funds that will be used for closing or required reserves, and
  - Minus 30% of the remaining value of any stocks, bonds, mutual funds, or U.S. savings bonds assets (after the calculation in (a)).

Example:
Checking and savings accounts $40,000
IRA - made up of stocks and mutual funds $500,000
Funds required for closing - Down payment, closing costs, reserves (- $100,000)

Remaining IRA assets ($500,000 - $60,000 used at closing)
$440,000
Minus 30% 132,000
$308,000 Net documented assets

Minimum Asset Amount

The minimum amount of the Other Financial Assets required is as follows:

- The lesser of one- and one-half times the original UPB or $500,000.00.

Minimum Seasoning of Assets

The minimum seasoning of the Other Financial Assets is 24 months

Eligible Asset Types

Assets Eligible as Other Financial Assets:

- The same eligible liquid financial assets that may be used for the borrower's reserves, which includes: o Checking and savings accounts;
  - Investments in stocks, bonds, mutual funds, CD's, money market funds, and trust accounts; and
  - Cash value of a vested life insurance policy
- Funds from the sale of investment properties.

Assets Ineligible as Other Financial Assets:

Assets that are ineligible as borrower's reserves, which includes:

- Funds that have not been vested;

- Funds that cannot be withdrawn under circumstances other than the account owner's retirement, employment termination, or death;
- Stock held in an unlisted corporation;
- Non-vested stock options and non-vested restricted stock;
- Personal unsecured loans; and
- Cash proceeds from a cash-out refinance transaction on the subject property

Monthly Income Stream Calculation
Convert the borrower's net documented assets by the amortization terms of the Mortgage (in months).

Example of Calculation:
- Present Value: $1,000,000
- 30-year Mortgage: 360
- Income: $2777.77

<u>TAX EXEMPT INCOME</u>
When needed for qualification, if income is verified to be nontaxable and its tax-exempt status are likely to continue, the following requirements must be met to gross up the income:
- Income must be from a non-taxable source such as social security, retirement payments, child support, disability, workers compensation benefits, or certain public assistance payments
- A copy of the complete federal individual tax return for the most recent one year, or other documentation evidencing the income, or a portion of, is tax exempt must be provided.
- The non-taxable portion of the income may be grossed up by using a calculation of either
  - 25% of the tax-exempt portion of the income
  - The current federal and state income tax withholding tables

COLLATERAL & APPRAISAL GUIDELINES
<u>INTRODUCTION</u>
An essential part of the underwriting process is an accurate value of the real property comprising the loan security. The appraisal report summarizes the valuation process for the property; and establishes whether the property's value is adequate security for the proposed loan. The appraisal report must convey a thoroughly documented and well-supported impartial estimate of value as of a precise date. Appraisals prepared for AAA must be of high quality, nondiscriminatory, and prepared in accordance with all relevant professional standards and regulatory agency requirements. Appraisers must be independent of any influences – financial or otherwise – that would in any way detract from the objectivity of their reports.

Use of appraisals or other valuations must conform to AAA's appraisal policies and regulatory requirements.

COLLATERAL EVALUATION
The appraisal report/evaluation forms are designed to provide a concise format for presenting both the appraiser's description of the subject property and the valuation analysis that leads to the opinion of market value. All forms and documentation must be completed in a manner that will clearly reflect the thoroughness of the appraiser's investigation and analysis, and provide the rationale for the opinion of market value.

There are a number of ways to determine that the collateral is acceptable for the transaction. The forms vary depending on the underwriting method and the type of property. Collateral valuation is determined as described in the following sections.

RESIDENTIAL PROPERTIES

On-site inspections completed by licensed or certified appraisers, statistical database modeling, or other appropriate methods approved by the Chief Residential Appraisal Officer as long as they comply with all regulations. The value will be equal to the lesser of the appraised value or purchase price. The value for properties purchased within the prior 120 days will be equal to the lesser of the appraised value or purchase price plus the documented cost of improvements, if applicable.

ORDERING THE APPRAISAL

When an appraisal is ordered for a residential property, the appraiser should be provided with all information that may affect the appraiser's estimate of value or marketability. The appraisal order must include the name and phone number of a contact who can provide the appraiser with necessary information, and access to the property. The person ordering the appraisal cannot also be involved in underwriting the loan.

AGE OF APPRAISALS AND OTHER VALUATIONS

Appraisal reports and other valuations are good for up to 120 days preceding the date of the note. If the appraisal or other valuation is more than 120 days old at the time of application, the current appraised value will be used for the property valuation. Properties purchased within 120 days of application will use the lesser of the purchase price or appraised value to calculate LTV/CLTV/HCLTV, measured from the date on which the property was purchased to the disbursement date of the new mortgage loan.

STANDARD APPRAISAL GUIDELINES

Standard appraisal requirements establish the value based on a thorough evaluation of both the interior and exterior of the subject property. It includes a quantitative sales comparison analysis and requires the assignment of a dollar value to reflect the market's reaction to any features of a comparable sale that differs from those of the subject property.

Appraisals must generally be completed 'As Is".

The appraiser must supply the following exhibits with all appraisal reports:

- Street map to scale that shows the location of the subject property and all comparable sales used
- Exterior building sketch of the improvements that indicates the dimensions
- Gross living area calculations must be shown
- Exterior Photographs of the subject property that show the front, back, sides, street and any amenity or obsolescence that adds or detracts value, as well as a picture of the front of each comparable sale
- Interior Photographs of the subject property that show the main living area, kitchen, all bathrooms, and amenity or obsolescence that adds or detracts value
- Condominium projects general information as it relates to the project itself such as management, number of phases and completion, common elements, etc.
- Any other data that is necessary to provide an adequately supported opinion of value

APPRAISAL FORMS

The forms required to document appraisal information, which is listed below, is dependent upon the property type, loan amount, and CLTV.

- Form 1004/URAR – Uniform Residential Appraisal Report: Used for interior inspections on 1-4-unit properties, PUD's and site condominiums.
- Form 1073/Individual Condominium Unit Appraisal Report (interior inspections)
- Evaluation – integrated valuation model or collateral valuation report analysis.

VALUATION METHODS

Charted below are the guidelines for determination of property values:

Appraisal Type	Loan Amount
3rd Party Collateral Evaluation	≤ $250,000 (see below for cases requiring a full appraisal for ≤ $250,000)
1004/1073, as applicable	> $250,000

A full appraisal must be ordered through AAA TPO Portal and be completed by a AAA approved Appraisal Management Company (AMC), regardless of AIR Compliant status in lieu of an evaluation in the following situations:

- Adequate subject property and/or comparable data is not available;
- Properties with any of the following characteristics: o Recently remodeled or extensively renovated o Properties with excess acreage (15+ acres)

o Unique design or amenities (berm/dome/log home or atypical amenities such as private tennis court, multiple outbuildings, etc.).

USE OF APPRAISAL FOR A SUBSEQUENT TRANSACTION

The use of an origination appraisal for a subsequent transaction is acceptable if the following requirements are met:

- The appraisal report must not be more than 12 months old on the note date of the subsequent transaction. If the appraisal report is greater than 4 months old on the date of the note and mortgage, then an appraisal update is required. Age of Appraisal and Appraisal Update Requirements, for requirements for completing an appraisal update, must be met.
- The property has not undergone any significant remodeling, renovation, or deterioration to the extent that the improvement or deterioration of the property would materially affect the market value of the subject property.
- The borrower and the lender/client must be the same on the original and subsequent transaction.
- Appraisal Review must review appraisal.

ACCEPTING AN APPRAISAL FROM ANOTHER LENDER

All requests to accept an appraisal that was ordered from another lender should be sent to appraisal@aaalendings.com.

Product Guidelines	
Target Market	Home Equity Line of Credit (HELOC) Product may be originated as a standalone (also see Standalone HELOC Documentation sheet) or as a piggyback combined with a conventional Agency first mortgage to avoid non-conforming loan amounts or combined with an Agency first mortgage product to reduce down payment below 20%.
Term/Amortization	30 Year Term: 2, 3, 5 or 10 year Draw Period with a 10 Year Interest Only Draw Period followed by 20 Year Amortization
DU/LPA Eligibility	Piggyback's must have DU/LPA Approve/Eligible/Accept or Approve/Accept/Ineligible due to loan size for non-conforming 1st liens; Standalones are manually underwritten and must be locked prior to submission to Underwriting.
Eligible Transactions	Purchase, Rate/Term or Cash-out refinance
Max Credit Limit	Maximum Credit Limit $250,000 to 89.99% HCLTV, $300,000 to 80% HCLTV, $350,000 to 70% HCLTV on Owner Occupied Maximum Credit Limit $250,000 to 80% HCLTV, $300,000 to 70% HCLTV on Second/Vacation homes
Max Combined Liens	$1.5MM
Max CLTV/HCLTV	• Owner Occupied – 89.99% purchase • Owner Occupied - 85% refinance (rate/term or cash-out) • Second Home – 80%; see Geographic Restrictions
Minimum Line/Draw	$25,000; minimum draw the lesser of $50,000 or 75% of the line
Eligible Properties	1 unit primary residence a. SFD / PUD / townhouse / rowhome b. Low-rise condominium (Fannie/Freddie Warrantable) c. High-rise condominium (Fannie/Freddie Warrantable) 1 unit second / vacation home a. SFD / PUD / townhouse / rowhome
Ineligible Properties	• Condotels • Non-warrantable condos • Manufactured • Co-Ops • Multi Unit (2-4) • Unique properties • Log Homes • Working or Hobby Farms • Tracts greater than 10 acres (larger properties considered on a case-by-case basis) • Properties subject to completion or repairs (without satisfactory certification of completion)
Occupancy	• Owner Occupied • Second/Vacation homes • Non-owner occupied home are ineligible • Non-occupant co-borrowers are ineligible
Eligible Borrowers	Follow Fannie Mae Seller Guide except: • No non-occupant co-borrowers • No E-2 investor visas

	• No tax IDs in lieu of valid social security numbers • See section for Self Employed Borrowers
Eligible First Lien Programs	• Agency & Government Fixed Rate and ARM's with initial fixed rate term ≥ 5 years • Non-Conforming Fixed Rate and ARM's with initial fixed rate terms ≥ 5 years • AUS approval required (DU/LPA) for piggybacks • Interest Only, Negative Amortization and other High Risk product features are ineligible Standalones: provide current mortgage statement (or CD if recently closed on 1st mtg); copy of 1st Mortgage Note may be requested by AAA Underwriter, if needed.

Credit	• Minimum underwriting credit score is 680
	• Credit limits: $250,001-$300,000 require minimum score of 700
	• Credit limits: $300,001-$350,000 require minimum score of 720
	• Underwriting score is determined as the middle of three indicator scores or the lower of two. For multiple borrowers, the lowest middle score for all borrowers is used. Non-traditional credit scoring is ineligible.
	• For piggybacks, credit document age must follow the AUS requirements
	• For standalones, credit documents must be no older than 120 days old on the note date
	• If there are past due unpaid Federal income taxes, provide installment agreement with the IRS, payment history showing at least 1 payment being made and that the borrower is current, and include the monthly payment in the borrower's debt obligations. Proof of income tax payment may be required to verify there are no past due taxes.
	• Tax liens must be paid off at or before closing
	• No mortgage delinquency (0x30) in the last 24 months
	• For any mortgage forbearance or payment deferral agreements that occurred during the COVID-19 pandemic time period, borrower(s) must have made at least 6 consecutive separate on-time monthly housing payments and at least 6 months must have elapsed since the forbearance/deferment arrangement ended
	• Borrower(s) must be current on all mortgage debt
	• No judgements, repossessions, or charge offs in the past 60 months
	• The following are considered severe delinquency, regardless of AUS feedback; *Borrowers with these profiles are ineligible until a period of 7 years has passed since occurrence and credit has been re-established.*
	  ○ Bankruptcy
	  ○ Foreclosure / Deed in Lieu of Foreclosure
	  ○ Short Sale or Short Payoff
	  ○ Mortgage modification, forbearance, or deferment (excluding COVID-19 related)
	• Borrowers with extenuating, isolated, one-time circumstances may be considered on a case-by-case basis, as determined by underwriting.
	• When borrower is not on the Note of the First mortgage of the subject property, the PITI must be included in the DTI calculation. The mortgage payment history must be provided and meet AAA posted guidelines.

Qualifying Ratios/DTI	45.00% DTI maximum on credit limits <= $250,000 36.00% DTI maximum on credit limits over $250,000
Qualifying Factor	Note Rate + 2% P&I over 30 year amortization
Income/Employment	• Piggybacks: follow first lien requirements. See Self Employed Borrowers section for additional restrictions. • Standalones: for salaried borrowers, most recent paystub dated within 30 days of application containing at least 30 days of YTD earnings and most recent year's W-2 or WVOE (follow FNMA guidelines for other types of income). See Eligible Borrowers Section for additional details. • Third party verifications of income, debts, and assets are acceptable

Self Employed Borrowers	• Minimum income documentation:
	    ○ Piggybacks: follow AUS for tax return requirements and Year to Date P&L
	    ○ Standalones: 2 years tax returns (business and personal) with all schedules and Year to Date P&L
	• For businesses impacted by pandemic, follow FNMA seller guide, including Lender Letters (such as LL-2020-03) and all updates
	• Maximum Credit Limit $250,000 to Maximum HCLTV 85% on Owner Occupied
	• Maximum Credit Limit $250,000 to Maximum HCLTV 70% on Second/Vacation Homes
	• Minimum underwriting credit score is 720
	• Complex ownership structures, business models (multiple affiliates or entities), or borrowers with significant contingent liabilities are ineligible (inquire with your BDM for scenarios)

Assets/Funds to Close/Reserves	• Piggybacks: follow first lien requirements • Standalones: no asset verification is required if borrower is receiving cash-out (otherwise provide at least one month liquid asset statements showing sufficient funds to close)
Interested Party Contributions	• See first lien eligibility

Appraisal/Property Valuation	• Piggybacks: follow FNMA/FHLMC guidelines (based upon the applicable AUS feedback type provided) except AAA will not accept value acceptance (appraisal waivers). If AUS permits a value acceptance, then instead provide: 1) AVM and exterior minimum property condition report (including photos) dated within 60 days of the note date or 2) an appraisal (can be a desktop, exterior inspection and/or interior inspection) completed by a licensed/state certified appraiser dated within 120 days of note date.
	• Standalones (First and Second Liens): 1) AVM and exterior minimum property condition report (including photos) dated within 60 days of the note date or 2) an appraisal (can be a desktop, exterior inspection and/or interior inspection) completed by a licensed/state certified appraiser dated within 120 days of note date or 3) FIRREA and USPAP compliant hybrid valuation may be acceptable.
	• For credit limits > $250,000, a full appraisal with interior & exterior inspection containing color photos is required.
	• AVM requirements:
	    ○ Completed by a rating agency approved provider for Residential Mortgage Backed Securities (RMBS).
	    ○ Confidence Score 90 or higher **and** forecasted standard deviation (FSD) maximum of 10 (.10).
	• 1004D Completion Alternatives are ineligible.
	• If property is located in a PUD, a HOA statement must be provided if an AVM is provided for valuation.

Disasters	• For properties located in individual assistance designated areas that have been declared a major disaster by FEMA after an appraisal/property inspection has been completed, then an exterior minimum re-inspection report (including a post-disaster photo) prepared by an independent third party dated after the disaster declaration date with confirmation that the property has not been adversely affected by the disaster is required.
Geographic Restrictions	• Properties located in AK, HI, [TX] and NY are ineligible • For TN, interest rate set at time of lock may not exceed Maximum Effective Interest Rate listed here: https://www.tn.gov/content/tn/tdfi/tdfi-how-do-i/info/mortgage-rate-of-interest/max-effective-interest-rate-history.html For NC properties total lender fees may not exceed 1% of credit limit
Property Insurance	Follow FNMA Selling Guide. Mortgagee clause for appropriate lien must be in the name of the creditor, ISAOA, ITIMA.
Title Policy	Full ALTA (for first liens) or Junior ALTA required. Lender's title insurance in the amount of the credit limit is required (final policy must be separate from 1st lien title policy). Both short form and long form policies are acceptable. ALTA Endorsements are not required. Closing protection letters are not required. For second lien Standalone transactions, a title report is acceptable.

Escrows	First lien HELOC's with collateral located in a FEMA designated Flood Zone require an Escrow/Impound account for Flood Insurance. Additionally, follow applicable state laws regarding Escrow/Impound accounts on first liens.
Trusts	Title may not be held in the name of a trust
Power of Attorney	POAs are permitted for all transaction types but must cover the appropriate lien transaction if utilized
Lien Position	Loan may be in first or second lien position
Conversion	Non-convertible
Assumability	Not assumable
High Cost Loans	May not be defined as High Cost by any applicable agency
Prepayment Penalty	None
Leasehold	Not eligible
Payment Date	Payment will be due on the 15th of each respective month
Late Charges	5% late fee will be assessed on the payment due date + 15 days (unless there is a more restrictive state requirement)
Annual Fee	No Annual Fee
Minimum Payment	None
Lifetime Max Rate	18% or state maximum
Lifetime Rate Floor	2.500%
Disbursement Documents	HELOC Revolving Disbursement Schedules, ALTA Settlement Statements or HUD-1 Settlement Statements are required (open-end loans are not subject to TRID so CDs should not be used) and must be specific to the subject lien
Rescission Notice	Notice of Right to Cancel is required for both purchases and refinances of primary residences
E-Signatures	In accordance with the ESIGN Act and with evidence of ESIGN consent provided within each loan file, electronic signatures are permitted on all initial disclosures and closing documents except for the following that must be wet/ink signed: • HELOC agreement with endorsement/Allonge • Any document that has to be recorded including security instruments with riders, property deeds, POAs, etc. • Notice of Right to Cancel Remote online notarization (RON) and Remote ink-signed notarization (RIN) are not permitted.
UAD/Loan Closing Advisor	Not required
UCDP/SSRs	Not required
Other Guidelines	If not addressed, follow FNMA selling guide. Additional documentation may be required in addition to AUS required documentation.

Secondary/Post Closing/Servicing Information	
Rates/Margin/Pricing/Incentive	See rate sheet
Fees	$150.00 Administration Fee (for principal balances < $150.00, fee must be paid prior to purchase). $10.00 life of loan flood certificate. First lien HELOC's require a real estate tax contract of $90.00.
Lock Period	Initial registrations will be priced and honored for 45 days
Extensions	• Will be assessed by Secondary Marketing as needed • Limit of 2 – 15 day extensions with a maximum of 30 total days (see rate sheet for applicable costs) • More days requires exception from Secondary Marketing Manager
Expired Registrations	Expired registrations may be renewed. For the first 30 days post-expiration (or post cancelation, whichever is earlier), the registration will be renewed on a worst case scenario. On the 31st day, a registration will move to current market (start over). Off sheet pricing may be required; contact AAA.
Shipping/Delivery	• Credit and legal files should be submitted to AAA • Loan files must be delivered within 10 days of note date and prior to registration expiration • Original Note address contact AAA
Purchase Review Conditions	• Conditions will be posted to our website. They must be uploaded to our website within 30 calendar days from date of first request.
MERS	• Loans must be delivered on MERS instruments • TOS/TOB to Org ID # 1010309 must be completed within 3 business days after purchase
Final/Trailing Documents	Final title policy and recorded security instrument must be delivered to AAA within 180 days of purchase or a $25 per document late fee will apply
Payment Histories	If not purchased by the 15th of the month in which a payment is due, then a pay history showing timely receipt of the payment is required prior to purchase
Servicing Transfers	If purchased after the 20th of the month preceding a payment due date, then correspondent will be responsible for collecting this upcoming payment and loan will be purchased at an amortized balance with payment first due to AAA the month after
Servicing/Payments	Forward customer payments to: AAA Capital Investment, Inc. Attn: Loan Servicing, 117 S. Garfield Ave, Alhambra, CA 91801
Early Payment Default (EPD)	If any payment required to be made by a Borrower within ninety (90) days after the loan purchase date has not been made on or prior to the date which is thirty (30) days after the related due date, Seller shall repurchase such Mortgage Loan at the Repurchase Price within fifteen (15) days of Purchaser's written request.
Early Pay Off (EPO)	If any loan pays off or makes principal curtailments in excess of 20% of the purchased balance within ninety (90) days of purchase date, any premiums or over par pricing will be subject to recapture by AAA.