



| JUMBO PRIME PROGRAM (FIXED) | | | | | | |
|--------------------------------|------------------|-----|------|-----------|----------------|------------------------------|
| Primary Residence | | | | | | |
| Purchase & Rate/Term Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$750,000 | 75% | 85% | 700 | 12 Months PITI | N/A |
| | \$2,000,000 | 80% | 80% | 700 | 12 Months PITI | |
| | \$2,500,000 | 75% | 75% | 700 | 24 Months PITI | |
| | \$3,000,000 | 70% | 70% | 700 | 24 Months PITI | |
| Condo | \$750,000 | 75% | 85% | 720 | 12 Months PITI | |
| | \$2,000,000 | 80% | 80% | 720 | 12 Months PITI | |
| | \$2,500,000 | 75% | 75% | 720 | 24 Months PITI | |
| | \$3,000,000 | 70% | 70% | 720 | 24 Months PITI | |
| | \$2,000,000 | 75% | 75% | 700 | 12 Months PITI | |
| | \$2,500,000 | 70% | 70% | 700 | 24 Months PITI | |
| | \$3,000,000 | 65% | 65% | 700 | 24 Months PITI | |
| 2 Units | \$2,000,000 | 75% | 75% | 700 | 18 Months PITI | |
| 3-4 Units | \$2,000,000 | 70% | 70% | 700 | 36 Months PITI | |
| Cash Out Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,500,000 | 70% | 70% | 720 | 12 Months PITI | >65% LTV/CLTV: \$400,000 |
| | \$2,000,000 | 65% | 65% | 720 | | <=65% LTV/CLTV: \$500,000 |
| Second Home | | | | | | |
| Purchase & Rate/Term Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$650,000 | 80% | 80% | 700 | 18 Months PITI | N/A |
| | \$1,000,000 | 75% | 75% | 700 | 18 Months PITI | |
| | \$1,500,000 | 75% | 75% | 700 | 24 Months PITI | |
| | \$2,000,000 | 70% | 70% | 700 | 24 Months PITI | |
| Condo | \$650,000 | 80% | 80% | 720 | 18 Months PITI | |
| | \$1,000,000 | 75% | 75% | 720 | 18 Months PITI | |
| | \$1,500,000 | 75% | 75% | 720 | 24 Months PITI | |
| | \$2,000,000 | 70% | 70% | 720 | 24 Months PITI | |
| | \$650,000 | 75% | 75% | 700 | 24 Months PITI | |
| | \$1,000,000 | 70% | 70% | 700 | 18 Months PITI | |
| | \$1,500,000 | 70% | 70% | 700 | 12 Months PITI | |
| | \$2,000,000 | 65% | 65% | 700 | 24 Months PITI | |



| Cash Out Refinance | | | | | | |
|--|------------------|-----|------|-----------|----------------|---------------|
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,000,000 | 75% | 75% | 700 | 18 Months PITI | \$350,000 |
| | \$1,500,000 | 65% | 65% | 720 | 24 Months PITI | |
| | \$2,000,000 | 60% | 60% | 720 | 25 Months PITI | |
| Investment Property | | | | | | |
| Purchase, Rate/Term Refinance & Cash Out | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,000,000 | 60% | 60% | 740 | 24 Months PITI | \$400,000 |
| | \$2,000,000 | 60% | 60% | 740 | 30 Months PITI | |



| JUMBO PROGRAM (ARM) | | | | | | |
|--|------------------|-----|------|-----------|----------------|------------------------------|
| Primary Residence | | | | | | |
| Purchase & Rate/Term Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$750,000 | 75% | 85% | 720 | 12 Months PITI | N/A |
| | \$2,000,000 | 80% | 80% | 720 | 12 Months PITI | |
| | \$2,500,000 | 75% | 75% | 720 | 24 Months PITI | |
| | \$3,000,000 | 70% | 70% | 720 | 24 Months PITI | |
| 2 Units | \$2,000,000 | 75% | 75% | 720 | 18 Months PITI | |
| 3-4 Units | \$2,000,000 | 70% | 70% | 720 | 36 Months PITI | |
| Cash Out Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,500,000 | 70% | 70% | 720 | 12 Months PITI | >65% LTV/CLTV: \$400,000 |
| | \$2,000,000 | 65% | 65% | 720 | | <=65% LTV/CLTV: \$500,000 |
| Second Home | | | | | | |
| Purchase & Rate/Term Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$650,000 | 80% | 80% | 720 | 18 Months PITI | N/A |
| | \$1,000,000 | 75% | 75% | 720 | 18 Months PITI | |
| | \$1,500,000 | 75% | 75% | 720 | 24 Months PITI | |
| | \$2,000,000 | 70% | 70% | 720 | 24 Months PITI | |
| Cash Out Refinance | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,000,000 | 75% | 75% | 720 | 18 Months PITI | \$350,000 |
| | \$1,500,000 | 65% | 65% | 720 | 24 Months PITI | |
| | \$2,000,000 | 60% | 60% | 720 | 25 Months PITI | |
| Investment Property ⁽¹⁾ | | | | | | |
| Purchase, Rate/Term Refinance & Cash Out | | | | | | |
| Units | Max. Loan Amount | LTV | CLTV | Min. FICO | Reserves | Max. Cash-Out |
| 1 Unit | \$1,000,000 | 60% | 60% | 740 | 24 Months PITI | \$400,000 |
| | \$2,000,000 | 60% | 60% | 740 | 30 Months PITI | |

(1) 7/1 and 10/1 ARMs Only



LOAN PURPOSE

REFINANCE OF LOANS WITH LESS THAN ONE YEAR SEASONING

If the first lien being paid off was a purchase transaction, and the original purchase price, as stated on the application, is less than the new appraised value the file should contain documentation supporting the increase in value (e.g. appraisal indicates increasing values for the market, appraisal comparable support increasing values, documented home improvements, or a copy of the original appraisal showing the original appraised value higher than the original sales price).

If the increase in value is unsupported, the underwriter should use the lower of the original purchase price or the new appraised value to determine LTV/TLTV/CLTV.

RATE/TERM REFINANCE

WinPrime Lending will consider transactions meeting the following criteria to be Rate/Term refinances:

- Payoff of the current mortgage (principal balance plus accrued interest, and any required prepayment penalty, only; other costs such as late fees and past-due amounts may not be paid with the new Loan)
 - If the first mortgage is a Home Equity Line of Credit (HELOC) a copy of the HUD1 Settlement Statement from the borrower's purchase of the subject property, or documentation of home improvements made to the property, must be provided evidencing the proceeds were used in their entirety to acquire or improve the subject property.
- Payoff (as defined above) of any subordinate mortgage lien used in its entirety to acquire or improve* the subject property
- Payoff (as defined above) any other mortgage lien against the subject, provided:
 - The lien has been open at least 12 months, and
 - Total draws in the past 12 months do not exceed 2% of the new first mortgage amount.
- Standard Loan fees (e.g., closing costs on the new mortgage; pre-pays, such as interest, taxes and insurance, etc. and points).
- Incidental cash to the borrower not to exceed 1% of the principal balance of the new Loan amount.

Note: Home improvement costs may include the following:

- Materials
- Architectural fees
- Supplies
- Labor
- Liability insurance on laborers
- Installation costs (water, sewer, well, etc.).
- Permits
- Nonrecurring costs of obtaining financing, including origination fees, discount points, title searches, recording fees.
- Temporary buy-downs are not allowed.

CASH-OUT REFINANCE:

Allowed. Any refinance transaction not meeting the requirements for a rate/term refinance is a Cash-out refinance.



▪ **Delayed Financing/Allowable Cash-out for Properties Recently Purchased with Cash**

If borrowers have purchased a primary or second home for cash within the preceding 90 days, an application may be considered to provide cash-out as a reimbursement of the borrower's cash investment providing all of the following are met:

- HUD1 or Closing Disclosure indicating cash purchase within 90 days prior to the application.
- Maximum LTV/CLTV based on the purchase LTV/CLTV matrix.
- Maximum DTI based on the purchase DTI requirements.
- Minimum Loan Score based on the purchase Loan Score requirements.
- The LTV/CLTV will be based off the lesser of the original purchase price or current appraised value.
- Borrower has exhibited a historic level of assets to support the cash purchase (supported by Schedule B of the last two years' tax returns) or other supportive documentation to verify receipt of such funds. A paper trail evidencing the funds used to acquire the subject property is acceptable as long as the funds had been on deposit at least 90 days prior to the date of the original transaction.
- Funds used for the original purchase cannot be borrowed, except by means of a fully secured Loan (for example, margin account, or other real estate). These will be treated on a case-by-case basis.
- Not allowed in Texas.
- The Loan must be registered and Closed as a Cash-out refinance since the borrower is already in title to the property. The Loan can be underwritten based on purchase transaction guidelines.

PROPERTY LISTED FOR SALE

WinPrime Lending will not provide financing on any refinance transaction secured by a ~~property~~ listed for sale, or

- Listed for sale within the six months prior to the Loan application.

OCCUPANCY

- Owner-Occupied
- Second Home
- Investment properties are allowed with the following restrictions:
 - Fixed, 7/1 & 10/1 ARM only - 5/1 ARM not allowed
 - Allowed on one unit properties only - Cooperatives not allowed
 - Two years property management experience required if rental income from subject is used to qualify
 - Maximum DTI of 38%

PROPERTY TYPE

ACCEPTABLE PROPERTY TYPES

- Single family detached or attached dwellings
- Condominiums/PUDs.
- Factory built except manufactured (mobile) homes
- Cooperatives.
- Properties with accessory units.

UNACCEPTABLE PROPERTY TYPES

- Timeshare
- projects



- Unimproved land
- Mobile home type manufactured housing
- Condotels/Resort Condominiums
- Hotel Condominium
- Log, earth or dome homes
- Hobby farms

PROPERTY FLIP TRANSACTIONS

- Not allowed

PROPERTIES WITH RESALE/DEED RESTRICTIONS

- Not allowed

PROPERTIES LOCATED ON ISLANDS

The following are considerations when making lending decisions on island properties:

- Regardless of where a property is located, it must be suitable for residential use and occupancy year-round. This is the area of greatest concern and the one most critical in determining acceptability. On some islands, public and private utilities such as water and electricity are not available year round, and the properties have no central heat source. These properties are ineligible for financing.
- The island should be accessible via public transportation. If a boat or ferry is the only means of access, it should be public, not private transportation. Public transportation is defined as that which is owned or controlled by local or state governing agencies or has been established for generations and is now considered public with assurance of public ownership should the business close.
- Due to location, access, and availability of utilities, the property may suffer limited marketability. Marketability must be demonstrated by sales of comparable properties.

PRODUCTS

- Fixed Rate 15 and 30 years
- 5/1, 7/1, and 10/1 LIBOR ARMs

ADJUSTABLE RATE DETAILS

- Interest rate adjustment caps
 - 5/1, 7/1 & 10/1 ARMs: Initial: 2% up/down; Subsequent: 2% up/down; Lifetime: 5% up
- Margin: 2.250
- Index: 1-Year LIBOR (London InterBank Offer Rate)
- Interest rate Floor: The interest rate Floor is equal to the Margin
- Change dates:
 - 5/1: The first Change Date is the 60th payment due date. There is a new Change Date every 12 months thereafter
 - 7/1: The first Change Date is the 84th payment due date. There is a new Change Date every 12 months thereafter



- 10/1: The first Change Date is the 120th payment due date. There is a new Change Date every 12 months thereafter
- Conversion Option: None
- Assumption: ARM products are assumable to a qualified borrower after the fixed term

QUALIFYING RATE & QUALIFYING RATIOS

QUALIFYING RATES FOR ARM PRODUCTS

- 7/1, 10/1 - Qualify at the greater of the fully indexed rate (index + margin) OR Initial Note rate, not to exceed the start rate plus lifetime cap.
- 5/1 ARM – Qualify at the greater of the Fully indexed rate (index + margin) OR Initial Note rate plus 2%

QUALIFYING RATIOS

| | Front End Ratio | Total Debt to Income Ratio | Occupant Borrower's Ratio w/ Non-occupant Co-borrower |
|--|-----------------|----------------------------|---|
| Fixed Rate, Primary Purchase and Primary Rate/Term Refi Transactions | 36% | 43% | 43% |
| Investment Properties | 36% | 38% | 38% |
| All Other Transactions | 36% | 40% | 43% |

LOAN AMOUNT

- Minimum: \$ 417,001 / Maximum: \$ 3,000,000

BORROWER ELIGIBILITY

- U.S. Citizens
- Lawful Permanent Residents
- Non-Permanent Residents must meet the following requirements
 - A-1, A-2, A-3, E-1, E-3, G Series, H-1, L-1, O-1A, O-1B, O-2, TN NAFTA , TC NAFTA Visas are accepted.
 - Minimum two year history of residence, employment and credit in the U.S., or Borrowing with a U.S. citizen or permanent resident alien.
 - A Borrower with an expired visa may be considered, subject to each of the following:
 - Visa classification is one of the eligible visas listed above.
 - Confirmation that the Borrower has submitted an application for extension of the visa or an application for a green card. Documentation includes, but is not limited to:



- ✗ USCIS Form I797 (Issued when an application or petition is approved)
 - ✗ USCIS Form I797C or I797E (must not state that the application has been declined)
 - ✗ application for extension of current visa (USCIS Form I539 or equivalent) or copy of application for green card (USCIS Form I485 or equivalent) and electronic verification of receipt from the USCIS web site.
- If the borrower is sponsored by the employer, the employer may verify that they are sponsoring the visa renewal.
 - All standards for determining stable monthly income, adequate credit history and sufficient liquid assets must be applied in the same manner to each borrower including borrowers who are nonpermanent resident aliens.
- Ineligible Borrowers included, but are not limited to:
 - Foreign Nationals
 - Diplomatic Immunity

NON ARMS LENGTH TRANSACTION

- Loans for second home or investment properties are not eligible for purchase by WinPrime Lending Funding if the transaction includes non-arm's length and/or at-interest characteristics.

PROPERTIES PURCHASED FOR OCCUPANCY BY A DIRECT FAMILY MEMBER

When the subject property is being purchased for occupancy by a direct family member (parents, siblings, children):

| If... | And the borrower's relationship is... | Then occupancy is considered... |
|---|--|---------------------------------|
| Only the occupant borrower's income is needed to qualify | N/A (borrowers do not have to be related) | Primary residence |
| Only the non-occupant borrower's income is needed to qualify | Direct family members (parent/child or siblings) | Second home |
| | Not direct family members | Investment property |
| Both the occupant and non-occupant borrowers' incomes are needed to qualify | N/A (borrowers do not have to be related; relationship does not impact occupancy type) | Investment property |

When qualifying using only the non-occupant borrower's income (i.e., the direct relative occupant is not required to be on the Loan), the following applies:

| If... | Then... |
|--|---|
| The primary income earner's Loan Score is ≥ 740 | The maximum LTV/CLTV is 5% below the second home policy. |
| The primary income earner's Loan Score is ≥ 700 and < 740 | The maximum LTV/CLTV is 10% below the second home policy. |



TITLE CHANGES

These are transactions where the borrowers have been transferred into title, perhaps by a quit claim deed, and may include a transfer from one individual to another or from an LLC or another business entity to an individual. The borrowers are attempting to refinance the existing mortgage from the previous owner's name to their name. This situation presents red flags for credit and transaction risk similar to the risks of a flip transaction.

These transactions are ineligible, unless the:

Title change is due to marriage, divorce, or death, and

- Borrower must qualify under normal underwriting.
- Transaction may be considered as a rate-term or cash-out refinance (refer to eligible transaction requirements specified previously in this section).
- The reason for the title transfer must be explained.
- To evidence the relationship in this chain of title and to show that there is not an unrelated party entering the chain of title, one of the following must be met:
 - Appropriate legal documents (such as divorce decree, marriage certificate, or estate documents) must be obtained.
 - Status of the new title holders must be identified and fulfilled in Schedule B-1 of the title work.

OR

Borrower has been in title for more than six months, and

- Transaction may be considered according to the Requirements listed in Identity of Interest Transactions, along with the following additional requirements:
 - Transaction may be considered as a rate / term or cash-out refinance (refer to eligible transaction requirements specified previously in this section).
 - The reason for the title transfer must be explained.

CREDIT

BUSINESS CREDIT REPORTS

Business credit reports are not required; however, there are certain circumstances when it will be imperative to obtain a business credit report to determine the acceptability of a Loan.

When the Borrower's business entity is a corporation, subchapter "S" corporation or a partnership, it is at the sole discretion of the underwriter to determine the appropriate times to require a business credit report.

MINIMUM LOAN SCORE REQUIREMENTS

To be eligible for Jumbo financing, WinPrime Lending requires a minimum Loan Score of at least:

- Purchase and rate/term transactions with fixed rate product require a minimum Loan Score of 700
- All other transactions require a minimum Loan Score of 720
- Non-traditional credit is not allowed

Additionally, a housing payment history (mortgage, rental or combination of the two) covering the most recent 12 months (minimum) with no late payments must be verified either by the credit bureau or by direct verification.

BANKRUPTCY, FORECLOSURE, DEED-IN-LIEU, SHORT SALE, REPOSSESSION REQUIREMENTS AND LOAN MODIFICATIONS



Borrowers with a bankruptcy, foreclosure, deed-in-lieu, short sale, repossession, or Loan modifications are subject to the following requirements:

- LTV/CLTV greater than 70%: Not allowed
- LTV/CLTV less than or equal to 70% is allowed when:
 - The adverse Credit was due to extenuating circumstances and a minimum of 60 months re-establishment of credit since the discharged/dismissal/completion date, or
 - The Adverse Credit was due to financial mismanagement and 84 months re-establishment of credit since the discharged/dismissal/completion date.

CHARGE-OFF

- Individual, unpaid charge-off less than or equal to \$500 is allowed with no requirement to pay off.
- Individual, unpaid charge-off more than \$500 is not allowed.

MONTHLY DEBT OBLIGATIONS

PAYOFF VS. PAYDOWN

Accounts may not be “paid down” to less than 10 months to allow the borrower to qualify. Installment or mortgage accounts must be paid in full. Payoff of revolving accounts in order to qualify the borrower is not allowed.

HOUSING EXPENSE RATIO

The housing expense ratio equals the total monthly primary housing expense divided by the qualifying monthly income. The monthly housing expense is the sum of the following:

- Monthly principal and interest payment on the borrower’s primary residence.
- Monthly principal and interest payments are required for interest only HELOC payment calculations.

Note: See table under Liabilities – Revolving Accounts below for methods of calculating home equity line of credit (HELOC) payment.

- 1/12th of the annual real estate taxes (do not use a lot only tax figure for new construction).
- 1/12th of the annual hazard insurance premium (including flood, earthquake, or subsidence insurance if any)
- Monthly leasehold payments if applicable.
- Monthly homeowners association dues, condominium maintenance fees, or cooperative monthly assessments if applicable.

TOTAL DEBT RATIO

The total debt to income ratio is the sum of the monthly housing expense and all long-term debt divided by the qualifying monthly income.

The long-term debt (recurring obligations) is defined as the sum of all continuing monthly obligations including but not limited to:

- The total proposed monthly housing expense. Payments on all revolving accounts with a balance.
- Payments on all installment obligations with 10 or more monthly payments remaining until payoff.
- When calculating the DTI, full principal and interest payments are used for all other mortgages, including home equity lines of credits (HELOCs) on other real estate held by the borrower. See table under Liabilities Analysis – Revolving Accounts below for methods of calculating HELOC payment.



- For Closed End subordinate loans (not HELOCs) with an interest-only feature: Qualify using monthly principal and interest payment, based on full amortization over the term of the loan remaining as of the date the loan is or will be recast, at the fully indexed rate or any introductory rate, whichever is greater, not including any rate/payment discounts that will not apply over the term of the loan.
- Real estate loans (if not accounted for in rental income analysis).
- Child support.
- Other continuing obligations.

It is not acceptable to pay down installment debts to less than 10 months in order to qualify. Installment debts must be verified as paid-in-full at closing in order to exclude the debt from the borrower's qualifying ratios.

Debts lasting less than 10 months must be included if the amount of the debt affects the borrower's ability to pay the mortgage during the months immediately after Loan closing, especially if the borrower will have limited or no cash assets after Loan closing.

Some debts may be excluded from total obligations with additional documentation. See Liabilities analysis for additional information. All debts, including debts that are excluded from ratio calculations, should be listed on the application.

Obligations not considered long term debt, and therefore excluded from DTI, include:

- Federal, state, and local taxes
- Federal Insurance Contributions Act (FICA) or other retirement contributions, such as 401(k) accounts
- Commuting costs Union dues
- Automatic deductions to savings accounts
- Child care
- Voluntary deductions

Employment/Income Stability

The following analysis is required:

- Only income that is reasonably expected to continue for at least three years should be considered. For additional information, see BORROWER EMPLOYMENT AND INCOME ANALYSIS.
- Stability of employment must also be considered when determining if the income should be used in qualifying.
- For self-employed borrowers, stable income is generally considered to be a 24-month average of net income.
- When reviewing information from a tax return, a 24-month income average is used when two years' tax returns are required and a 12-month average when one year's tax return is required.

SUBORDINATE FINANCING

For transactions including subordinate financing, the following requirements apply:

- For HELOC and Closed End Loans: Negative amortization is not allowed; scheduled payments must be sufficient to cover at least the interest due.
- For Closed End Loans: Balloon payments are not allowed.
- For Closed End Loans with Interest-Only feature: see Total Debt Ratio above.

REVOLVING ACCOUNTS

Revolving accounts, including credit cards, department store accounts, equity lines and other open-ended accounts are accounts that do not fully amortize and have balances and payments that vary from month-to-month.



The minimum payment amount for all revolving accounts with a balance must be included in the total monthly obligations.

If the credit bureau does not reflect a payment on a current reporting liability, a payment should be calculated as follows:

- Revolving: The greater of \$10 or 5 percent of outstanding balance.
- Home equity line of credit (HELOC): When calculating the DTI, full principal and interest payments are used for all other mortgages, including home equity lines of credits (HELOCs) on other real estate held by the borrower. See the table below for methods of calculating HELOC payments. This is to account for loans that require less than a full principal and interest payment, including but not limited to Interest Only.

| Transaction | |
|---|---|
| <p>New HELOC on subject property or Cash-out refinance first lien – all subordinated HELOCs on subject property</p> | <p>When there is a payment reported on the credit bureau, use: Full credit line limit 20-year amortization term</p> <ul style="list-style-type: none"> - Current prime rate - + 1.5 margin - + 2.0 WinPrime Lending qualifying <p>Or, economic adjuster</p> <p>Obtain the Note and use:</p> <ul style="list-style-type: none"> - Full credit line limit - 20-year amortization term - Fully indexed rate (prime + margin) from the Note - + 2.0 WinPrime Lending qualifying economic adjuster <p>When no payment is reported on the credit bureau and the Note cannot be obtained, use the higher of:</p> <ul style="list-style-type: none"> - Full credit line limit - 20-year amortization term - Current prime rate - + 1.5 margin - + 2.0 WinPrime Lending qualifying <p>Or, economic adjuster</p> <p>- 5% of the outstanding balance</p> |
| <p>Rate/term refinance – Existing HELOC on subject property</p> | <p>When there is a payment reported on the credit bureau, use:</p> <ul style="list-style-type: none"> - Outstanding balance - 20-year amortization term - Current prime rate - + 1.5 margin - + 2.0 WinPrime Lending qualifying <p>Or, economic adjuster</p> <p>Obtain the Note and use:</p> <ul style="list-style-type: none"> - Outstanding balance - 20-year amortization term - Current prime rate - + 1.5 margin - + 2.0 WinPrime Lending qualifying economic adjuster |



| | |
|-----------------------------------|--|
| | <p>When no payment is reported on the credit bureau and the Note cannot be obtained, use the higher of:</p> <ul style="list-style-type: none"> - Outstanding balance - 20-year amortization term - Current prime rate - + 1.5 margin - + 2.0 WinPrime Lending qualifying economic adjuster <p>Or,</p> <ul style="list-style-type: none"> - 5% of the outstanding balance |
| <p>Non-subject property HELOC</p> | <p>When the HELOC is aged less than or equal to 12 months (calculated from open date to note date)</p> <ul style="list-style-type: none"> - Obtain the Note and calculate the qualifying payment based on: - Full credit line limit - 20-year amortization term - Actual rate/margin may be verified with a copy of the note - Do not include any rate/payment discounts that will not apply over the term of the line <p>When there is a payment on the credit bureau and a copy of the note is not available:</p> <ul style="list-style-type: none"> - Full credit line limit - 20-year amortization term - Current prime rate - + 1.50 margin - + 2.0 WinPrime Lending qualifying economic adjuster - Do not include any rate/payment discounts the will not apply over the term of the line <p>When no payment is reported on the credit bureau and the Note cannot be obtained, use the higher of:</p> <ul style="list-style-type: none"> - Outstanding balance or full credit line limit, as outlined above - 20-year amortization term - Current prime rate - + 1.5 margin <p>Or, - + 2.0 WinPrime Lending qualifying economic adjuster 5% of the outstanding balance or full credit line limit, as determined by above criteria</p> <p>If the borrower has sufficient liquid assets to pay off the full credit line limit amount in addition to standard policy requirements for post-closing reserves, the qualifying payment calculation may be based on outstanding balance rather than the full credit line limit.</p> <p>When the HELOC is aged more than 12 months (calculated from open date to note date)</p> <p>Obtain the Note and calculate the qualifying payment based on:</p> |



| | |
|---|--|
| | <ul style="list-style-type: none"> - Outstanding balance - 20-year amortization term - Actual rate/margin may be verified with a copy of the note <p>When there is a payment on the credit bureau and a copy of the note is not available:</p> <ul style="list-style-type: none"> - Outstanding balance - 20-year amortization term - Current prime rate - + 1.50 margin - + 2.0 WinPrime Lending qualifying economic adjuster <p>When no payment is reported on the credit bureau and the Note cannot be obtained, use the higher of:</p> <ul style="list-style-type: none"> - Outstanding balance or full credit line limit, as outlined above - 20-year amortization term - Current prime rate - + 1.5 margin <p>Or, - + 2.0 WinPrime Lending qualifying economic adjuster 5% of the outstanding balance or full credit line limit, as determined by above criteria</p> |
| <p>Non-subject property – first mortgage/lien</p> | <p>When calculating the DTI, full principal and interest payments are used for all first mortgage/lien on all real estate owned/held by the borrower.</p> <p>Note: This is accounts for Loans that require less than a full principal and interest payment, including but not limited to Interest Only.</p> |

Note: Prime rate can be found in the Wall Street Journal.

HELOCS ON REAL ESTATE OWNED OTHER THAN THE SUBJECT PROPERTY

For qualifying purposes, Mortgage payments included HELOCs, must use a fully indexed, fully amortized principal and interest payment calculation.

First mortgages on a non- subject property will use the following data to calculate a qualifying principal and interest payment:

- Outstanding principal balance
- Fully indexed note rate
- Existing amortization term

Borrowers should be qualified with a full PITI payment including Homeowner Association fees, if applicable.

When the borrower is the credit account owner on an authorized user account, the debt must be considered in the credit analysis and the monthly payment obligation must be included in the debt to income (DTI) ratio.



When the borrower is the authorized user and the account is being used as a tradeline, the debt must be considered in the credit analysis and the monthly payment obligation must be included in the debt to income (DTI) ratio.

Certain open-ended accounts (such as American Express) require payment in full monthly. For such accounts, one of the following options may be used for qualifying:

- Document sufficient assets to pay off the full balance (beyond cash required to close and reserves). In addition, use the greater of 5 percent of the balance or \$10 for a qualifying payment.
- If sufficient assets are not available, use the full balance for a qualifying payment; if a lower payment amount can be documented from the creditor, that amount may be used for qualifying purposes.
- Follow verbal verification requirements or obtain a written verification or account statement. Refer to Verbal Verification of Employment (VVOE) for documentation requirements.

INSTALLMENT ACCOUNTS

Installment accounts are accounts that fully amortize or have a balloon payment at a predetermined date. The account balance cannot be increased during the term of the loan. Payments are made on a regular basis and may be fixed or adjustable.

Whenever the installment debt's payment amount is not provided on the credit report then documentation of the payment amount must be obtained. Examples of documentation of the payment include but are not limited to:

- Direct verification from the creditor.
- Copy of the installment loan agreement.

Installment debts with less than 10 monthly payments remaining may be excluded from the qualifying ratios, but must be listed on the application. It is not acceptable to pay down installment debts to less than 10 months in order to qualify. Installment debts must be verified as paid-in-full at closing in order to exclude the debt from the borrower's qualifying ratios.

DEFERRED PAYMENTS, BALLOON PAYMENTS, AND SINGLE PAYMENTS NOTES (INCLUDING INTEREST ONLY PAYMENT NOTES)

Some debts may have deferred payments or are in a period of forbearance. These debts must be included in the qualifying ratios if scheduled to begin or come due within 12 months of the mortgage Loan closing. Examples of installment debts with deferred payments include:

- Debts on automobiles, furniture, and appliances for which the initial payment is delayed for a period of time as part of a promotional campaign by the retailer.

Some deferred payments must be included in the qualifying ratios even if deferred 12 months or more.

Examples include:

- Deferred payments must be included if the amount of the debt or payment affects the borrower's ability to pay the mortgage after Loan closing, especially if the borrower will have limited or no cash assets after Loan closing, (such a borrower with high ratios / no or low cash assets after closing with a sizable debt event that is just outside of the 12 month window for inclusion in ratios).
- Deferred payments on student loans and deferred payments on revolving accounts must be included in the total debt ratio.
- Balloon and single payment Notes must be considered in the underwriting analysis:
 - If sufficient liquid assets (excluding assets used to meet reserve (post-closing liquidity)/down payment/closing costs requirements) can be verified to pay off Note, the Note does not need to be

included in the ratios.

- If sufficient liquid assets cannot be verified, verify the term of the Note, and include a payment in the ratios based on amortization over remaining term of the Note.

When the credit report does not include a payment on the debt, documentation of the payment amount must be obtained. Examples of documentation of the payment include but are not limited to:

- Direct verification from the creditor.
- Copy of the installment loan agreement.
- Student loan certification from the financial institution holding the loan.

LEASE PAYMENTS

The monthly payment associated with a lease must be included in the total monthly obligations regardless of the number of payments remaining until the end of the lease term.

BUSINESS DEBT

Business debts for which the borrower is personally liable are usually included in long term debt according to the requirements for revolving or installment accounts. Installment debts with 10 or more monthly payments remaining and revolving debts may be excluded if the account has a satisfactory payment history and all of the following is provided as evidence that the business is paying the debt:

- The account does not have a history of delinquency.
- Minimum of 12 months of consecutive canceled checks from the business.
- The cash flow analysis of the business takes the payment obligation into consideration.

CHILD SUPPORT

Child support payments must be documented with a copy of the court order (such as a divorce decree).

Child support payments with less than 10 monthly payments remaining may be excluded from the qualifying ratios. A copy of the court order is required.

Alimony and separate maintenance payments to be paid policy must be followed. See Borrower – Employment and Income Analysis – Other Income - Alimony and Separate Maintenance Payments to be Paid.

NET RENTAL LOSS

If the analysis of rental income on an investment property as described in employment and income analysis indicates a loss, the monthly net rental loss is included in the long term debts.

SALE OF PRIOR HOME

The borrower's previous mortgage payment does not have to be included in long term debt as long as one of the following can be provided:

- A copy of the HUD-1 or Closing Disclosure from the sale of the real estate.
- Departure Residence Policy is met. See Departure Residence Policy.

BRIDGE LOANS

The payment on a bridge loan may be excluded from the total debt ratio when the following documentation is provided:

- A copy of the fully executed sales contract for the previous residence.
- A lender's commitment to the buyer of the previous residence (if the executed sales contract includes a financing contingency).
- Documented reserves of six months' payments covering all liens on the previous residence.



RENTAL OF PREVIOUS RESIDENCE LISTED FOR SALE

See Departure Residence Policy.

SUBORDINATE FINANCING

Payments on closed end subordinate financing (installment loan) must be included in the monthly housing expense or in long term debt if there are 10 or more monthly payments remaining.

Payments on any HELOC with an outstanding balance must be included in the monthly housing expense or in long term debt (depending on whether the primary residence of other real estate secures the line).

READY RESERVE ACCOUNTS

Any ready reserve (overdraft protections or extended credit option) on a checking account with a balance must be treated as a revolving account.

LOANS SECURED BY A FINANCIAL ASSET

Payments on loans secured by a borrower's financial asset (such as, SIP, IRAs, or stocks) are not included in long term debt because they are voluntary payments. However, the underwriter must consider these payments in terms of their possible impact on cash flow and debt ratios. The borrower must indicate plans for debt repayment if the inclusion of a loan payment in the monthly debts results in a high total obligation to income ratio or negative cash flow.

LOANS FROM 401(K), 403(B), AND KEOGH PLANS

Payments on loans from 401(k), 403(b), and KEOGH plans must be included in qualifying ratios unless there are sufficient liquid assets to pay off the debt. If sufficient liquid assets exist then the payment can be excluded.

MARGIN ACCOUNTS

If the borrower discloses the existence of a margin account on the application or it is indicated on brokerage account statements, repayment must be considered and included in total monthly obligations unless the value of the stock exceeds the amount of the Loan.

GROUP SAVINGS

If the borrower is part of a group savings plan with a remaining obligation period of 10 months or more, the monthly contribution to the account must be included in the total obligations to income ratio.

CONTINGENT LIABILITIES

Contingent liabilities are debts in which the borrower has become a cosigner / guarantor with another person. A contingent liability exists when an individual is held responsible for payment of a debt if another party defaults on the payment. These could be a present co-signed loan, a loan that was assumed, or a loan assigned to another party by court order. Contingent liabilities must be included in liabilities if there are 10 or more monthly payments remaining.

COSIGNED LOANS

The monthly payment on a cosigned loan with 10 or more monthly payments remaining may be excluded from long term debt if there is documentation that the primary obligor has been making regular payments during the previous 12 months and does not have a history of delinquent payments on the loan during that time. If the payments have not been paid on time or if there is no evidence that someone other than the borrower is making payments, the cosigned loan is treated as borrower's own obligation. Copies of canceled checks for the most recent 12 months or a statement from the creditor are acceptable documentation.



The above applies to:

- A car loan
- A student loan
- A mortgage
- Any other obligation

ASSUMPTIONS

Contingent liability must be considered when the borrower remains obligated on an outstanding mortgage (including conventional, FHA insured, VA guaranteed, or any other mortgage or line of credit) secured by property that:

- Has been sold or traded within the last 12 months without a release of liability; or
- Is to be sold on assumption without a release of liability being obtained.

If a property has been sold on assumption, the following documents are required:

- Copy of the documents transferring ownership of the property.
- The assumption agreement executed by the transferee.

When a mortgage is assumed, the contingent liability may be excluded from the total monthly obligations, if:

- A payment history from the servicer of the assumed loan is obtained showing that the mortgage has been current during the previous 12 months; or
- Value of the property, as established by an appraisal or the sales price on the HUD-1 Settlement Statement or Closing Disclosure from the sale of the property, results in a LTV/CLTV ratio of 75 percent or less.

PREVIOUSLY PAID IN FULL

The monthly payment on a debt may be excluded from the total monthly obligations if the borrowers can document that they no longer owe the debt. The following documents are required:

- Copy of the documents detailing debt paid in full.
- Copy of the documents releasing liability.

COURT ORDER

If the obligation to make payments on a debt has been assigned to another person by a court order such as a divorce decree, the payment may be excluded from the total monthly obligations regardless of the number of payments remaining. The following documents are required:

- A copy of the court order or divorce decree.
- For mortgage debt, a copy of the documents transferring ownership of the property.

Any late payments associated with loans on the property should be taken into account when reviewing the borrower's credit profile.

BANKRUPTCY

If a debt has been included in a court order such as a bankruptcy, the payment may be excluded from the total monthly obligations regardless of the number of payments remaining. The following documents are required:

- A copy of the bankruptcy papers detailing the debt to be excluded.
- For mortgage debt, a copy of the documents transferring ownership of the property.

Any late payments associated with loans on the property should be taken into account when reviewing the borrower's credit profile.



PENDING LAWSUITS

If the application, title, or credit documents reveal that the borrower is presently involved in a lawsuit or pending litigation, a statement from the borrower's attorney must be requested and reviewed. The statement must explain the circumstances of the lawsuit or litigation and discuss the borrower's liability and insurance coverage. A copy of the complaint and answer may also be required.

EMPLOYMENT

JOB CHANGES

A borrower who changes jobs frequently to advance within the same line of work should receive favorable treatment if this can be verified. Frequent job changes without advancement or in different fields of work should be carefully reviewed to ensure consistent or increasing income levels and likelihood of continued stable employment.

EMPLOYMENT GAPS

The borrower must provide a detailed two year employment history. Obtain a written explanation from the borrower for any gaps in employment that span one or more months. Gaps in employment due to the borrower attending training or schooling for a specific profession should be favorably considered. Verification of the schooling (for example, diploma, or transcripts) must be provided.

EMPLOYMENT BEGINNING AFTER SUBJECT LOAN CLOSING

Loans may close prior to the start date with a New Employer provided the following requirements are met:

- Primary residence and 1unit only.
- Maximum 80% LTV.
- Purchase transactions only.
- Salaried borrowers only.
- Fully executed non-contingent employment contract or offer letter indicating salary and start date is required. The contract must be fully guaranteed and non-revocable.
- The time period between closing date & commencement of employment must not exceed 60 days.
- Borrower must have adequate cash reserves to cover PITI during employment gap plus two additional months over and above any other reserve requirements that may apply.
- Post Close verbal Verification of Employment and Paystub not required.
- Documentation evidencing all contingencies have been satisfied must be provided prior to closing.

EMPLOYMENT LESS THAN TWO YEARS THE FOLLOWING APPLY:

- For borrowers who are reentering the workforce after an absence of six months or more, the borrower's income may be qualifying income if the borrower has been at the current employer for a minimum of six months and can document a two year work history prior to an absence from employment using traditional employment verifications and/or copies of IRS form W2s or pay stubs.
- A move from dependence on public assistance to reliance on employment and earned income should be viewed as a positive factor.

Note: One, but not the only example of an acceptable employment situation, includes individuals who took several years off from employment to raise children and then returned to the workforce.



CONTINUANCE OF INCOME

Income sources that may have a finite period of receipt such as the income types listed below must have a continuation period of at least five (5) years. The continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.

- Alimony or separate maintenance payments
- Child support
- Note income
- Trust Income
- IRA/401K/Keogh income
- Certain types of retirement income, such as annuities (excluding social security income)
- Social Security survivor benefits for children
- Foreign income
- Certain types of benefit income, such as worker's compensation
- Public assistance income
- Mortgage differential
- Relocation compensation
- Royalty income

Effective income for borrowers planning to retire during the first three year period must include the amount of:

- Documented retirement benefits
- Social Security payments or
- Other payments expected to be received in retirement.

DECLINING INCOME POLICY (SELF-EMPLOYMENT, BONUS, OVERTIME, COMMISSION, RESTRICTED STOCK)

- When income has declined less than 20 percent or greater decline in self-employed, bonus, overtime, commission and restricted stock income in the past two years or year to date, risk/offset factors, underwriters will use judgment to determine whether similar assessment is warranted (for example, Loans with debt ratios at or near maximum allowed could be impacted with even small income declines). The list of risk/offset factors include but are not limited to the following:
 - Is the decline an isolated or a onetime occurrence?
 - Has the decline been addressed and expectations for non-recurrence documented /supported?
 - Are the bonus or commission income programs being used to qualify still in place?
 - Has it been verified that the amount of income used to qualify will continue?
 - Is the proportion of declining income relative to total income?
 - Self-employment income is frequently more volatile and less stable than other professional income sources.
 - Additional years of income trending may be required to support stability and expected continuance.
- If the self-employed, bonus, and commission income has declined more than 20%, then:
 - The lower income must be used in qualifying.
 - Income cannot be averaged with previous higher years' income or current income unless both of the following apply:
 - Decline is an isolated, onetime occurrence.
 - The reason for onetime decline has been satisfactorily addressed and documented to support a strong expectation of non-recurrence or further decline in income.



- If there have been declines over multiple years or further declines are possible, an additional risk offset of one of the following is required:
 - DTI ratio at least 5% less than required.
 - Housing ratio less than 36%.
 - Reserve (post-closing liquidity) over minimum required.
 - For self-employed borrowers, the CPA must be contacted to provide documentation and support for income trends and continuance.
 - For borrowers with bonus or commission income, the employer must be contacted for income trends and continuance as well as verification the employee is still eligible and that programs are ongoing:
 - If a publicly held company, earnings reports can be used to evidence favorable business trends.

Note: Reserve (post-closing liquidity) exceptions with declining income are generally not available. Loans that do not meet all the declining income guidelines may not be eligible for approval as submitted.

INCOME ANALYSIS - RESTRICTED STOCK

Restricted stock refers to stock of a company that is not fully transferable until certain conditions have been met. Upon satisfaction of those conditions, the stock becomes transferable to the person holding the grant. Restricted stock should not be confused with stock options. Restricted stock must be vested as well as received on a regular, recurring basis.

The following documentation is required:

- Issuance agreement or equivalent (part of the benefits package), and
- Schedule of distribution of units (shares), and
- Vesting schedule, and
- Evidence that stock is publicly traded, and
- Evidence of payout of the restricted stock (e.g., YTD pay stub and 2 years W2s)

Calculation of income:

- To determine the restricted stock price use the lower of: current stock price, or the two year stock price average.
- Qualifying income will be calculated using an average of the restricted stock income for the past two years, and year to date stock earnings. The average stock price should be applied to the number of stock units vested each year. If stock income is declining, refer to DECLINING INCOME POLICY (SELFEMPLOYMENT, BONUS, OVERTIME, COMMISSION, and RESTRICTED STOCK).
- Future vesting must support qualifying income.

INCOME ANALYSIS - SELF-EMPLOYED BORROWERS

Borrowers are considered self-employed when their income is derived from a business in which they maintain a majority owner interest or can otherwise exercise control over the business' activities. Generally, a 25% or greater ownership interest in the business is considered a majority. There are circumstances where borrowers may be considered self-employed if they own less than 25% of a business.

Example: In partnerships with each of five general partners owning 20%, the borrower is considered self-employed if this 20% ownership is the borrower's major source of income.



Increased Risk Consideration

Self-employed borrowers present a greater credit risk than salaried borrowers because their income is directly linked to the success of their business. The following additional risks are associated with self-employed borrowers:

- Difficulty in verifying actual income/cash flow.
- Cash flow may not be regular because it is affected by marketplace fluctuations.
- Business may decline if borrower becomes ill.
- Borrower may be liable for business debts.
- Business may suffer from inadequate control or dissension among partners.
- Maximum financing for a borrower self-employed less than two years.

Two- year history

Income from self-employment may be considered stable if the borrower has been self-employed two or more years. Stable income is the average income for the previous two years. Any income from self-employment earned by the borrower must be documented with tax returns or financial statements prepared by the borrower's accountant.

Income of a borrower with at least one year, but less than a two-year history of self-employment may be considered stable if both of the following requirements are met:

- Borrower must have had at least two years of previous successful employment in the same occupation.
- Borrower must be able to document a reasonable probability of business success based on market feasibility, research, or studies and pro forma financial statements.

The following factors must be carefully considered when a borrower has been self-employed for at least one year, but less than two years:

- The borrower's training and experience.
- The location and nature of the business.
- The demand for that type of business in the area.

Less than one-year history

Income from a self-employment of less than one year may not be considered effective income.

SOLE PROPRIETORSHIP

A sole proprietorship is a business owned by one person. It is the least expensive and simplest form of business to establish. As long as the establishing individual uses his own name, no fees, registrations, agreements, or taxes are involved.

Sole proprietorship liability

In a sole proprietorship, the individual owner is personally liable for all debts of the business, and, therefore, has unlimited liability. No distinction is made between the owner's personal assets and the assets used in the business. Either may be taken by creditors to satisfy business obligations.

Sole proprietorship death of owner

With a sole proprietorship, the death of the owner would terminate the business and place the assets into probate, delaying the disposition of assets to creditors and heirs. There is no legal provision for continuity of sole proprietorships.

Sole proprietorship risks

Management control of the business is concentrated in the owner. While this is useful for rapid decision making, continuity of the business may be endangered by:

- A lack of checks and balances.



- Illness or long absence of the owner.
- Inability to raise adequate capital.

Sole proprietorship taxes

The business income or loss is reported on Schedule C, Internal Revenue Service (IRS) Form 1040, and included with the individual owner's tax return.

Sole proprietorship qualifying income

Income based on the individual tax returns, IRS Form 1040, for the previous two years is averaged. If the earnings trend for the previous two years is downward and the most recent tax return or P&L is less than the prior year's tax return, the borrower's most recent year's tax return or P&L must be used to calculate his/her income.

PARTNERSHIP

A partnership is basically a sole proprietorship multiplied by the number of people involved. A partnership is based upon a contractual relationship formed to carry on a trade or business.

- In a general partnership, each partner is personally liable for the total debts of the business.
- In a limited partnership, a limited partner is liable only to the extent of his own investment in the business.

▪ **GENERAL PARTNERSHIP**

General partnership liability

A general partnership is formed so that each partner is personally liable for the debts of the whole business. Therefore each partner is responsible for the actions of every other partner. This can create significant control problems and the necessity for a written partnership agreement. The personal liability to partnership creditors exists even after the partnership is dissolved.

General partnership dissolution

Unless specified in the partnership agreement, a partnership is dissolved immediately upon the death, withdrawal, incompetence, or insolvency of any one partner.

General partnership risks

There may be a lack of prompt and centralized control particularly where loose assignment of responsibilities exists. The concept that equal partners have equal voice may produce more reasonable judgment but may also cause more frequent arguments.

Generally, large amounts of capital are difficult to obtain because of the relative instability of this form of organization.

General partnership taxes

Partnerships are treated like sole proprietorships. Although the partnership is not subject to taxation, it is required to calculate and report partnership income on IRS Form 1065, United States Partnership Return of Income. The net income distributable to each partner is reported on Schedule K1 of IRS Form 1065 and on the individual's Schedule E, Part II.

Partners then pay taxes on their proportionate share of net partnership income at their individual tax rate, whether or not the income was actually withdrawn from the partnership.

General partnership qualifying income

Refer to EVALUATING PARTNERSHIP TAX RETURNS (IRS FORM 1065) AND SCHEDULE K1 below.

▪ **LIMITED PARTNERSHIP**

Limited partnership liability



Limited partnerships are usually formed for the purpose of investing money. Limited partners usually take a loss on this invested money. In turn, this reduces their taxable income. Limited partners have limited decision making opportunities and their liability is limited to the amount they invest. Unlike general partners, a limited partner's death or withdrawal does not terminate the partnership.

Limited partnership capital

Limited partnerships raise capital by attracting investors in the form of limited partners. As a result, limited partners are an excellent source of capital for the general partners without any loss of management control.

Limited partnership taxes

Limited partnerships carry the same tax implications as general partnerships and sole proprietorships. Both the limited and general partners in a limited partnership pay taxes on their proportionate share of net income as reported on their individual tax returns. Limited partners report their income or loss to the IRS on Schedule K1 of Form 1065 and the individual Schedule E, Part II.

Limited partnership qualifying income

Refer to EVALUATING PARTNERSHIP TAX RETURNS (IRS FORM 1065) AND SCHEDULE K1 below.

CORPORATION

Corporations are state chartered businesses owned by stockholders. The stockholder is not personally responsible for the debts of the corporation. The corporation's profits (retained earnings) are put back into the business or are distributed to stockholders as dividends. A corporation may choose to do both. The ultimate legal control of a corporation rests with its owners, the shareholders. These shareholders delegate their control to an elected board of directors. The board of directors, in turn, elects the officers of the corporation who are responsible for the day-to-day operations of the business.

Corporation taxes

Corporations report their income and losses on the United States Corporation Income Tax Return, Form 1120. Schedule L of IRS Form 1120 presents the current year corporation balance sheet. Income to the officers is reported by a W2 and is reflected on IRS Form 1040.

Corporation qualifying income

Qualifying income is determined by using a two-year average of income reported on W2s. Refer to Evaluating Corporate Tax Returns (IRS Form 1120) below.

Corporation additional income

For an analysis of corporate tax returns, refer to Corporation qualifying income below. For an analysis of financial statements in this document, refer to Financial Statements Analysis below.

Subchapter S Corporation

This entity is formed as a result of an elective provision of the federal law, which permits certain small business corporations and their shareholders to elect special income tax treatment. It has the characteristics of a corporation, except for the special tax treatment.

Subchapter S corporation substantial risk

Because S corporations are generally small, startup businesses, which are taxed like partnerships, they are in the developmental stage and present a substantial underwriting risk.

This is particularly true because the limit on the number of shareholders allowed affects sources of borrowing and limits management options.



Subchapter S corporation taxes

S corporations pass gains and losses onto their shareholders, who are then, taxed at the tax rates for individuals. Income is detailed on IRS Form 1120S (U.S. income tax return for an S corporation), and is transferred to the individual shareholder's personal returns by the Schedule K1. The owners' salaries are reported on W2s.

Subchapter S corporation qualifying income

Refer to Evaluating S Corporation Tax Returns (IRS Form 1120s) And Schedules K1 below.

REQUIRED INCOME DOCUMENTATION

The following documents are required for all self-employed borrowers on loans that require documentation of income:

VERBAL VERIFICATION OF EMPLOYMENT – SELF-EMPLOYED REQUIRED DOCUMENTATION

If any borrower on a loan is self-employed, a verbal Verification of Employment must be completed not more than 30 calendar days prior to the date printed on the note. Employment needs to be verified by analyzing tax returns and financial statements.

The Seller must perform additional diligence to verify income stability and continuance including but not limited to:

- Confirm with a disinterested third party, for example, a CPA, regulatory agency, contractor or professional organization and
- Provide supporting documentation verifying the existence of the business including, but not limited to:
 - Yellow page ads.
 - Copies of business licenses.
 - Internet websites. Acceptable Internet websites include the borrower's business website and government, union, and professional association websites or accessing LexisNexis.

The verification must be documented in writing, including:

- Independently-verified source of the employment information.
- Name and title of the person who verified the borrower's employment

TAX RETURNS

Copies of signed individual income tax returns for the past 2 years including all applicable schedules are used to document income.

The following are acceptable documents:

- Tax returns signed by borrower(s), regardless of date, or
- Form 8879 indicating that e-signatures are filed, or
- Tax return signed, stamped, or letterhead by CPA.

If the borrower is self-employed and the self-employment income is not used to qualify, the Self-employed borrower must provide a copy of the first page of the most recent individual federal tax return to determine whether there was a business loss that negatively impacts the borrower's ability to repay. When that is the case, additional documentation about the Self-employed borrower's business income is needed to fully evaluate the impact of the business loss.



▪ CORPORATIONS, S-CORPORATIONS, PARTNERSHIPS

The following additional documentation is required if the business is a corporation, Subchapter S corporation, or partnership:

Business Income Tax Returns

Copies of signed federal business income tax returns for the previous two-years with all applicable schedules attached:

- Corporation - IRS 1120.
- S corporation – IRS Form 1120S and Schedule K1.
- General partnership- IRS Form 1065, and Schedule K1.
- Limited partnership – IRS Schedule K1.

Financial statements

The individual preparing financial statements cannot be an immediate relative of the applicant.

A year-to-date profit and loss (P&L) statement and balance sheet are required if more than four months have lapsed since the last fiscal year end. Since balance sheet information is not included on the Schedule C, balance sheets are also required for sole proprietorships when less than four months have lapsed since the last fiscal year end.

The individual preparing or reviewing the financial statements must be an appropriate third party:

- An unrelated and qualified individual (e.g. accountant / bookkeeper), including employee of the applicant's business, particularly if that employee has filed tax documents with the IRS.
- An appropriate third party who has reviewed the document or other record prepared by the consumer is also acceptable.

Additional reviewed or audited financial statements prepared by a certified public accountant may be required at the discretion of the underwriter. Cases which may warrant reviewed or audited financial statements are:

- An applicant who has been self-employed for less than two years.
- Excessive variation in income or expenses from year to year.
- Reported delinquencies on the business credit report.

▪ SOLE PROPRIETORSHIP

The following additional documentation may be required if the business is a sole proprietorship:

Balance sheet

A balance sheet for the previous two years may be required at the underwriter's discretion if the business has significant assets, employees other than family members, and regularly prepares separate business financial statements.

Request for tax returns from IRS (Form 4506T)

Seller to obtain fully executed IRS Form 4506T from the borrower for each business tax return that was used in the Loan decision.

EVALUATING TAX RETURNS

INCOME CALCULATION METHODS

Two approaches to income calculation must be considered:

- WinPrime Lending Cash Flow Method - considers distributions that the borrower is taking from the business.
- Baseline Method - considers the net income from the business.



Calculations for each method are shown below. The lowest income figure resulting from these calculations must be used to qualify.

INTRODUCTION

To determine the income of the self-employed borrower, personal and business tax returns must be obtained and evaluated.

AVERAGING

Because self-employment income may change each year, an average better approximates the borrower’s long-term earning ability.

EARNINGS TREND

Establish the borrower’s earnings trend. Annual earnings that are level or increasing are acceptable. However, a large decline in gross income over two or three years may result in an unacceptable income source, even if the borrower’s current income and debt ratios meet the guidelines.

- Earnings trends from the previous two years are established using the tax returns. If borrower: Provides quarterly tax returns, the income analysis may include income through the period covered by the tax filings, or
- Is not subject to quarterly tax returns, or does not file them, then the income shown on the P&L statement may be included in the analysis, provided the income stream based on the P&L is consistent with the previous years’ earnings.

If the P&L statements submitted for the current year show an income stream considerably greater than what is supported by the previous year’s tax returns, base the income analysis solely on the income verified through the tax returns.

If the consumer’s earnings trend for the previous two years is downward and the most recent tax return or P&L is less than the prior year’s tax return, the borrower’s most recent year’s tax return or P&L must be used to calculate his/her income.

INCOME SOURCE

Give particular attention to the actual income source, not just the total income. For example, the adjusted gross income (AGI) may be increasing annually due to income not related to the business, such as real estate capital gains, while the business income may be declining.

Only sources of income that are likely to continue may be used for qualifying.

SCHEDULE C

Business income or loss

This is the business income or loss for a sole proprietorship. Income is calculated as follows:

| | Baseline Method | WinPrime Lending Cash Flow Method |
|--|---|--|
| Schedule C - Profit or Loss From Business (Sole Proprietorship) | Net profit + depletion + depreciation | Net profit + expenses for business use of home + depletion + depreciation - meal and entertainment exclusion + amortization/casualty loss |

Note: Qualifying income will be the lesser of the two calculation methods above.



SCHEDULE D

Capital gain or loss

Capital gains or losses generally occur only one time, and should not be considered when determining effective income. However, if the individual has a constant turnover of assets resulting in gains or losses, the capital gain or loss must be considered when determining the income. Three years’ tax returns are required to evaluate an effective earning trend. If the trend:

- Results in a gain, it may be added as effective income, or
- Consistently shows a loss, it must be deducted from the total income.
- Anticipated continuation of income must be documented through verified assets.

SCHEDULE E

- **Part I** (For self-employed borrowers who also have rental income) Refer to INCOME ANALYSIS – RENTAL INCOME.
- **Part II** Income or loss from partnerships and S corporation income or loss is determined by reviewing the business tax returns.

SCHEDULE F

Farm income or loss

This is the profit or loss from farming. Income is calculated as follows:

| | Baseline Method | WinPrime Lending Cash Flow Method |
|---|-------------------------------------|--|
| Schedule F - Farm Income or Loss | Net profit (loss) + depreciation | Net profit (loss) - nonrecurring other income/loss + depreciation + amortization/casualty loss + expenses for business use of home + Non-Tax Portion Ongoing Coop and CCC Payments |

Note: Qualifying income will be the lesser of the two calculation methods above.

EVALUATING CORPORATE TAX RETURNS (IRS FORM 1120)

Purpose of review

The primary purpose for reviewing business tax returns is to analyze the financial strength of the business and to confirm that it will continue to generate the income the borrower needs to qualify for the requested Loan. When the individual tax return confirms sufficient borrower income and the business tax return indicates a viable company, the corporation need not be investigated any further.

Additional income

Qualifying income is determined by using a two-year average of income reported on W-2s. However, if the borrower needs (and has the legal right) to draw additional income from the corporation to qualify for this Loan, further evaluation is necessary to verify that the business is capable of contributing additional income.

The following are required:

- Borrower has the legal right to withdraw income from the corporation, per corporate resolution or comparable document.
- Withdrawal of additional income will not impact the business operations, based on careful analysis of the corporate financial statements.
- The business has positive sales and earnings trends.



Verify right to business funds

Before proceeding with the analysis of additional income, it should be verified that the owner / borrower has a right to these funds. Verification includes corporate resolution or other comparable document.

Calculation

Income is calculated as follows:

| | Baseline Method | WinPrime Lending Cash Flow Method |
|-----------------------|---|---|
| C- Corporation | Officer's compensation (W-2) + Borrower's share of: taxable income - tax liability + depreciation + depletion | Officer's compensation (W-2) + dividends/distributions + loans to shareholders - loans from shareholders - unreimbursed employee expenses |

Note: Qualifying income will be the lesser of the two calculation methods above.

Fiscal year

Many corporations operate on a fiscal year that is different from a calendar year. In these cases, a time adjustment is necessary to relate the corporate income to the individual tax return because the individual return is on a calendar year.

Individual percentage of ownership

- The borrower's percentage of ownership can be determined from the Compensation of Officers section of the corporate tax return.
- If this information is not provided, other evidence of the borrower's ownership must be obtained for this business income to be considered. A statement by the corporation's accountant is satisfactory evidence.
- This percentage should be applied to the total of the above figures to determine the borrower's share of corporate after-tax income and non-cash expenses.

EVALUATING S CORPORATION TAX RETURNS (IRS FORM 1120S) AND SCHEDULES K-1

Calculation

The gains or losses of an S corporation are passed on to the shareholders who are then taxed at the tax rates for individuals. This income or loss is reflected on Schedule K-1 (IRS Form 1120S) and transferred to Schedule E of the individual tax return.

The primary source of income for an owner of an S corporation comes from W-2 wages, which are traced to the Compensation of Officers line of the IRS Form 1120S and reported on IRS Form 1040. However, if the borrower needs (and has the legal right) to draw additional income from the corporation to qualify for this Loan, further evaluation is necessary to verify that the business is capable of contributing additional income. The following are required:

- Documentation of ownership and access to income.
- The business must have adequate liquidity to support the withdrawal of earnings. The business must have positive sales and earnings trends.

If the borrower meets the above requirements, calculate income as follows:



| | Baseline Method | WinPrime Lending Cash Flow Method |
|-----------------------|--|--|
| S- Corporation | Officer's compensation (W-2) + Borrower's share of: Ordinary income/loss + net rental real estate income (loss) + depreciation + depletion - total obligations payable in <1 year | Officer's compensation (W-2) + cash distributions + loans to shareholders - loans from shareholders - unreimbursed employee expenses |

Note: Qualifying income will be the lesser of the two calculation methods above.

The Schedule K-1 (IRS Form 1120S) must be reviewed to determine the borrower's percentage of ownership.

EVALUATING PARTNERSHIP TAX RETURNS (IRS FORM 1065) AND SCHEDULE K-1

All Partnerships

Both general and limited partnerships use the IRS Form 1065 federal income tax return. The gains or losses of a partnership are passed on to the partners who are then taxed at the tax rates for individuals. This income or loss is reflected on Schedule K-1 (IRS Form 1065) and transferred to Schedule E of the individual tax return.

If the borrower is a general partner and needs (and has the legal right) to draw additional income from the partnership to qualify for this Loan, further evaluation is necessary to verify that the business is capable of contributing additional income. The following are required:

- Documentation of ownership and access to income.
- The business must have adequate liquidity to support the withdrawal of earnings.
- The business must have positive sales and earnings trends.

If the borrower meets the above requirements, calculate income as follows:

| | Baseline Method | WinPrime Lending Cash Flow Method |
|--------------------|---|---|
| Partnership | Partner's share of: Ordinary income/loss + net rental real estate income (loss) + guaranteed payments + depreciation + depletion - total obligations payable in < 1 year | Guaranteed Payments to Partner - capital contributed during year + withdrawals and distributions + loans to partners - loans from partners - unreimbursed partnership expenses |

Note: Qualifying income will be the lesser of the two calculation methods above.

The Schedule K-1 (IRS Form 1065) is used to determine the borrower's percentage of ownership.

RE-EVALUATION OF BUSINESS INCOME

Introduction

Once the additional business income has been credited to the borrower, the overall business financial position must be re-evaluated.

Recent withdrawals

Additional borrower withdrawals of cash may have a severe negative impact on the business and may lead to negative cash flow. When this occurs, it may not be possible to confirm the stable, on-going income needed to approve the mortgage.



The taxable income line must be reduced by the amount of the borrower’s withdrawal.

To determine the impact on the business, income and expenses for the previous two-years must be compared with year-to-date income and expenses. In addition, a current balance sheet should be reviewed to determine that the business has adequate funds to cover short-term liabilities.

FINANCIAL STATEMENTS ANALYSIS

Purpose of analysis

Self-employed borrowers’ ability to repay the mortgage Loan depends on the stability and success of their business because the net income from that business will be used to repay the mortgage.

Financial statements of the business should be reviewed if there are any doubts about the continued stability of the business. Income statements and balance sheets can be evaluated for solvency (the ability to repay debts) and profitability (the ability to achieve monetary gain).

By reviewing financial statements for two or more years, the underwriter can develop a historical view of operations.

The two principal business statements that reveal the financial status of a company are:

- Balance sheet: An overview of a business, which shows a company’s financial position at one point in time.
 - Income statement: The short-term (one year or less) look at a business, which shows the income realized and expenses incurred over that period.

The balance sheet

The balance sheet presents what a company or individual owns and owes at a specific point in time, usually the last day of the year. The balance sheet is an indicator of the individual’s or company’s financial strength.

Balance sheet organization

The balance sheet has two sides and lists the general ledger account balances in three main categories:

Assets are things of value owned by the company or individual and are shown on the left side of the balance sheet.

Liabilities are debts owed by the company or individual to its creditors in exchange for goods and services required to operate the business. They are shown on the right side of the balance sheet.

Stockholder’s equity, sometimes called capital, is the value of the financial interest put into the business by its stockholders, owners, or both and is shown on the right side of the balance sheet.

Must balance

Both sides of the balance sheet must be equal as shown in the following formula:

Assets = liabilities + stockholder’s equity.

Typical balance sheet categories

| Assets | Liabilities |
|--|--|
| Current assets: Cash - Accounts receivable - Inventory - Prepaid expenses - Marketable securities Fixed assets: Property, plant, and equipment (less accumulated depreciation) | Current liabilities: - Accounts payable - Notes payable (current portion) - Federal income tax payable Long-term liabilities: - Mortgages - Notes payable - Bonds |



| | |
|--|---|
| Intangibles and other assets: - Goodwill - Patents - Trademarks - Copyrights | Stockholder's equity |
| | - Capital stock - Capital surplus - Retained earnings |

Assets

The assets column lists all the goods and property owned. It also shows amounts to be collected. There are three major sections: current assets, fixed assets, and other (intangible) assets.

Current assets

Current assets can be converted to cash quickly within a current year. Current assets are in a constant cycle of being changed into cash to pay debts and operating expenses. The test usually applied to distinguish current assets from fixed assets or other assets is whether the business will consume these assets within the operating cycle of the business.

Current assets include:

- Cash: all money on deposit or in petty cash.
- Accounts receivable: money owed to the business for goods and services.
- Inventor: finished goods, goods-in-process or raw materials.

Fixed assets

Fixed assets are of a relatively permanent nature. They are the assets the business needs to operate its ongoing activities. Fixed assets last longer than the current operating cycle and are depreciated over their useful lives to allow for normal wear and tear. Fixed assets are items such as buildings, furniture, fixtures, and automobiles.

Other assets

Other assets are long-term rights and privileges which are intangible but add value to a business because of their worth. These include:

- Copyright: Exclusive rights to publish and sell a musical, literary, or artistic piece of work for a number of years.
- Patent: A document granting a privilege to someone who has invented a product or a concept.
- Goodwill: Accrues when a business's rate of expected future earnings is greater than the rate of earnings normally realized in the industry.
- Trademark: The right to use an identifying name or mark given exclusively to a company (for example, Coca-Cola®).

Liabilities

Liabilities are the debts owed by an individual or corporation in exchange for goods and services. The two categories of liabilities are:

- Current liabilities: All amounts owed and due within the coming year. The portion of a long-term liability, such as a mortgage, that is due within the coming year is classified as a current liability.
- Long-term liabilities: Debts due more than one year from the balance sheet date.

Stockholder's equity

The stockholder's equity is the third section of the balance sheet and is also known as the capital section. It reflects the business's net worth and is equal to the assets minus the liabilities.

There are three categories:

- Capital stock: A share of interest or ownership in a company. There are two types: Common stock & Preferred stock.



- Capital surplus (sometimes called additional paid-in capital): This is the excess of market value over the stated (par) value of stock paid by shareholders.
Example: If the par value of a company’s stock is \$6 and one share is purchased for \$10, the capital surplus has a balance of \$4 and the capital stock account has a balance of \$6.
- Accumulated retained earnings is the amount of after-tax earnings that is put back into the business to conduct ongoing operations. Retained earnings cannot be used as income to qualify or as cash to close.

Income statement

The income statement presents the income and expenses over a 12-month period. The net profit or loss for the year is shown on the income statement. By reviewing the income statements for two or more years, the underwriter can develop a historical review of operations, especially in terms of net profit and net loss, and be better able to predict how the business might perform in the future.

Organization

- The income statement is made up of two major sections: Inflow of revenue.
- Outflow of expenses.

Matching concept

The accounting principle, matching concept, refers to matching expenses with the revenue they help generate. Expenses are subtracted from revenues. Net profit or net loss for the year is what remains.

| Sample Income Statement | |
|---|---------|
| Sales (revenue, including returns and allowances) | \$0,000 |
| Less: cost of goods sold | (000) |
| Gross profit on sales | \$0,000 |
| Less: | |
| selling expenses | (000) |
| general administrative expenses | (000) |
| other expenses | (000) |
| Other sources of income | \$0,000 |
| Less: federal income taxes | (000) |
| Net income | \$0,000 |

INCOME DEFINITION

Sales

Sales are generally the major source of revenue for the business. Gross sales are reduced by sales returns and allowances. The result is referred to as net sales.

Cost of goods sold

Cost of goods sold is the cost of materials used to produce the goods sold or cost of items to be resold during the accounting cycle. This account may be inappropriate if the business sells a service or other intangible item such as insurance.

Gross profit on sales

Gross profit on sales is also called gross margin, the results from subtracting the returns and cost of goods sold from the gross sales.

Expenses

Selling expenses

Selling expenses are incurred to produce the sales revenue. Included in the selling expenses are



commissions and salaries to salespeople, advertising, and travel and entertainment.

- **General and administrative expenses**

General and administrative expenses include office expenses, staff salaries, and other overhead expenses, which are unrelated to directly producing sales revenues.

- **Other expenses**

Other expenses are the expenses incurred outside of the main operations of the business. These include dividend and interest expense.

Federal income tax

Federal income tax is generally the last expense deducted from income.

INCOME ANALYSIS – SALARIED INCOME

A salaried worker is paid on a regular, recurring basis by an employer. Income is reported to the Internal Revenue Service (IRS) on a W-2 form. The borrower has minimal (less than 25%) or no interest in the business.

INCOME IS VERIFIED WITH ONE OF THE FOLLOWING:

- Verification of Employment (VOE) form, completed by the employer.
- Current pay stubs, a verbal VOE (Exhibit 3), not more than 20 business days prior to the date printed on the Note, and most recent two years of W-2 forms.
- Employment verification for the most recent two full years must be documented.
- A borrower with a 25% or greater ownership interest in a business is considered self-employed and is evaluated as a self-employed borrower for underwriting purposes. See INCOME ANALYSIS – SELF-EMPLOYED BORROWERS – Definition/risk/stability for circumstances when borrowers may be considered self-employed if they own less than 25% of a business.

OVERTIME INCOME

Overtime may be used as stable monthly income if the employer verifies:

- Two year history of receipt
- Probability of continued receipt
- Dollar amount of overtime paid in the last two years

If the employment verification states that the overtime income is unlikely to continue, it may not be used in qualifying.

The underwriter will develop an average of overtime income for the past two years. Periods of overtime income less than two years may be acceptable, provided the underwriter can justify, document and confirm in writing the reason for using the income for qualifying purposes.

To document, obtain all of the following:

- Most recent YTD paystub or salary voucher documenting at least one month of income.
- W-2s covering the most recent two years
- Verbal VOE (Exhibit 3) not more than 20 calendar days prior to the date printed on the Note.

BONUS INCOME

Bonuses may be used as stable monthly income if the employer verifies all of the following:

- Two-year history of receipt.
- Probability of continued receipt.
- Dollar amount of bonuses paid in the last two years.



If the employment verification states that the bonus income is unlikely to continue, it may not be used in qualifying.

The underwriter will develop an average of bonus income for the past two years. Periods of 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.

To document, obtain all of the following:

- Most recent YTD paystub or salary voucher documenting at least one month of income.
- W-2s covering the most recent two years.
- Verbal VOE (Exhibit 3) not more than 20 calendar days prior to the date printed on the Note.

Refer to Assets – Down Payment for additional requirements when using bonus income as qualifying income and as cash to close.

COMMISSIONED BORROWER

Borrowers who received commissions must provide all of the following:

- The most recent two years' federal tax returns to verify commissions earned and expenses incurred.
- Current paystub.
- Most recent two years' W-2 forms.
- Verbal VOE (Exhibit 3) not more than 20 business days prior to the date printed on the Note.

Commission income must be averaged over the previous two years. Commission income earned for less than one year is not considered effective income unless the underwriter can verify and document in writing that the borrower's compensation changed from salary to commission within a similar position with the same employer.

Borrowers whose commission income was received for more than one year, but less than two years, may be considered favorably if the underwriter can do both of the following:

- Document the likelihood that the income will continue.
- Soundly rationalize accepting the commission income.

Commission income received for a minimum of two years from similar positions with different employers within the same industry may be considered if the underwriter can soundly rationalize accepting the commission income.

If the borrower is self-employed, for documentation requirements see INCOME ANALYSIS – SELF-EMPLOYED BORROWERS.

INCOME ANALYSIS – RENTAL INCOME

ELIGIBLE RENTAL INCOME

The following are acceptable sources of rental income:

- Rent received from investment properties or other units of an owner-occupied multifamily property may be considered stable income.
- Rents received from a live-in aide, generated from a disabled borrower's 1 unit, primary residence may be used for qualifying purposes, in an amount up to 30% of the total gross income that is used to qualify the borrower for the mortgage.

Typically, a live-in aide will receive room and board payments through Medicaid waiver funds from which the live-in-aide then makes rental payments to the borrower. This source of income is non-taxable and is not reported on the borrower's personal tax returns.

This income source may be considered stable monthly income, if both of the following are met:



- The borrower has received rental payments from a live-in aide for the past 12 months on a regular basis.
- The live-in aide plans to continue to reside with the borrower for the foreseeable future.

INELIGIBLE RENTAL INCOME

The following are ineligible rental income types:

- Rent from boarders in a single-family property that is also the borrower's primary residence. Income from a live-in aide may be allowed.
- Rent from a property that is the borrower's second home.

SUBJECT PROPERTY

The following documentation is required for all investment properties if rental income is to be used:

- The operating income statement (Fannie Mae 216 / Freddie Mac 998) is required for 2-4-unit primary or 1-unit investment properties. The Single-family Comparable Rent Schedule (Fannie Mae 1007 / Freddie Mac 1000) is required for 1-unit investment properties.
- Income used to qualify must be supported by Operating Income Statement / Comparable Rent Schedule.

In addition, when the subject property has been owned for at least 12 months:

- The borrower's prior year complete and filed federal individual tax return including Schedule E.
- Rental income from commercial rental properties requires two years' complete and filed federal individual tax returns, including schedule E.

When property has been owned less than 12 months and is not reflected on the borrower's most recent, filed federal individual tax returns, the following is required:

- Copies of the present, signed leases may be used only if the borrower has a two-year history of property management experience as evidenced by the most current two years' filed and signed federal IRS 1040 tax returns.
- Three months of canceled checks or bank statements verifying receipt of rental income.

Property Management Experience – 1 Unit Investment Property

When the subject property is a 1-unit investment property and rental income from the subject property is being used to qualify, two years' property management experience must be documented with the most current two years' filed and signed federal IRS 1040 tax returns.

Insurance Requirements

Rent loss insurance covers rental losses that are incurred during the period that the property is being rehabilitated following a casualty.

Rent loss insurance is required:

- For 1-unit investment property where borrowers are relying on rents from the units they will not be occupying.
- If the income from those units is used to qualify the borrowers.
- The insurance must provide coverage for an amount equal to a minimum of six months of the rental income.

Operating Income Statement (Fannie Mae Form 216/Freddie Mac Form 998)

For 1-unit investment property, use the net cash flow found on the operating income reconciliation section of the form unless income/loss used to qualify is supported by another acceptable source of documentation:

- If net cash flow is a positive figure, it should be included in qualifying income.
- If net cash flow is a negative figure, it should be included with the long-term debts.



The monthly housing expense is already accounted for in the net cash flow so it should not be added to the long-term debts.

Investment income/loss on the subject property cannot be aggregated or netted with other real estate owned.

PROPERTY OTHER THAN SUBJECT PROPERTY

The stability of the rental income must be documented through one of the following:

- A current lease;
- An agreement to lease, or
- A rental history over the previous 24 months. Gaps greater than 3 months require an explanation from the borrower.

Qualifying Rental Income

When the rental income is derived from property other than the subject property, the qualifying rental income is the net cash flow. Net cash flow must be established by the following:

- When the property has been owned for at least 12 months:
The most recent complete personal tax return (1040) including Schedule E.
- When the property has been owned less than 12 months and is not reflected on the borrower's most recent, filed federal individual tax returns:
Current lease agreements may be used only if the borrower has a two-year history of property management experience as evidenced by the most current two years' filed and signed federal IRS 1040 tax returns.

If net cash flow is to be determined by Schedule E of IRS Form 1040 tax return or current lease agreements, see below for calculation information.

There are two methods for calculating rental income from the Schedule E: Baseline method and Cash Flow method. Both methods must be calculated. Use the lesser of the two methods to qualify the borrower.

▪ **Cash Flow method**

Make the following adjustments to the net income shown on Schedule E to determine the monthly operating income:

| | |
|---|---|
| | Net Income |
| + | Depreciation, mortgage interest, real estate taxes, insurance and homeowners association fees, if any |
| - | Unallowed losses, if any |
| + | Loss carry-overs from previous years, if any |
| = | Annual operating income |
| ÷ | Annual operating income 12 months |
| = | Monthly operating income |

Positive net rental income from Schedule E of the borrower's tax returns or positive net cash flow from Freddie Mac 998/Fannie Mae 216 or Freddie Mac 1000/Fannie Mae 1007 may be considered stable monthly income.

Negative net rental income from Schedule E of the borrower's tax returns or negative net cash flow from Form Freddie Mac 998/Fannie Mae 216 or Freddie Mac 1000/Fannie Mae 1007 must be considered a liability for qualification purposes.

When using rental income to qualify from a 2-4 unit primary residence that is not the subject property:



- The current monthly principal, interest, taxes, insurance (PITI) payment on the borrower’s primary residence must be included in the qualifying ratios.
- The monthly operating income should be included in qualifying income.

For an investment property, subtract the monthly housing expense from the monthly operating income to determine the net cash flow.

- If net cash flow is positive, include it in qualifying the income.
- If net cash flow is negative, include it with the long-term debts.

Aggregate net rental income may be counted as stable monthly income, provided the reliability of receipt is clearly supported by the documentation in the file.

Aggregate net rental loss from investment properties and 2-4 unit primary residences must be considered a liability for qualification purposes.

The monthly housing expense is already accounted for in the net cash flow so it should not be added to the long-term debts.

▪ **Baseline method**

Only Depreciation shown on Schedule E may be added back to the net income or loss. Positive rental income is considered gross income for qualifying purposes, while negative income must be treated as a recurring liability.

▪ **Lease Agreements**

Deduct a 25% maintenance expense/vacancy factor from the monthly rent stated on the lease agreements to determine the monthly operating income.

When using rental income to qualify from a 2-4 unit primary residence that is not the subject property:

- The current monthly PITI payment on the borrower’s primary residence must be included in the qualifying ratios.
- The monthly operating income should be included in qualifying income.

For 1-4 unit investment property, subtract the monthly housing expense. From the monthly operating income to determine the net cash flow.

- If the net cash flow is positive, include it in the qualifying income.
- If net cash flow is negative, include it with the long-term debts.

The monthly housing expense is already accounted for in the net cash flow, so it should not be added to the debts

INCOME ANALYSIS – OTHER INCOME

SECOND JOBS/PART-TIME INCOME

For qualifying purposes, "part-time" income refers to employment taken to supplement the borrower’s income from regular employment; part-time employment is not a primary job and it is worked less than 40 hours.

Note: When a borrower’s primary employment is less than a typical 40-hour work week that income should be evaluated as regular, on-going primary employment.

A part-time/second job is considered stable income if:

- The borrower’s primary profession lends itself to a second job.
- Income can be verified as having been received and uninterrupted for at least two years.
- Income is expected to continue for at least three years.

-



To document provide all of the following:

- Most recent YTD pay stub covering one month,
- W-2s covering the two most recent tax years, and
- A Verbal Verification of Employment (Exhibit 3) within 20 business days prior to the date printed on the Note.

Part-time income not meeting the qualifying requirements may not be used in qualifying.

SEASONAL INCOME

Seasonal part-time or seasonal second job income can be considered as stable income when the borrower has a two-year history of receipt in the same line of work, there is a reasonable expectation that the borrower will be rehired the next season, and that the income is likely to continue for the next three years.

To document, obtain all of the following:

- Seasonal employment income must be reported on the borrower's two most recent years' federal tax returns.
- Year-to-date (YTD) paystub or salary voucher documenting at least one month of income.
- W-2s covering the two most recent years.
- Verbal VOE (Exhibit 3) within 20 business days prior to the date printed on the Note.

Every attempt should be made to obtain a VVOE. However, if the VVOE is unattainable due to business closure during specified times of the year the underwriter should use judgment to determine if the income source will continue. The borrower does not have to be currently employed in order to use seasonal income, if received for the last two years and reasonably expected to continue.

SEASONAL EMPLOYMENT WITH ASSOCIATED UNEMPLOYMENT COMPENSATION

Seasonal employment with associated unemployment compensation can be considered as stable income when the borrower has a two-year history of receipt in the same line of work, there is a reasonable expectation that the borrower will be rehired the next season, and that the income is likely to continue for the next three years.

To document, obtain all of the following:

- Seasonal employment and unemployment income must be reported on the borrower's two most recent years' federal tax returns.
- YTD paystub or salary voucher documenting at least one month of income.
- W-2s covering the two most recent years.
- Verbal VOE (Exhibit 3) within 20 business days prior to the date printed on the Note.
- Proof of receipt of unemployment compensation for two years.

Every attempt should be made to obtain a VVOE. However, if the VVOE is unattainable due to business closure during specified times of the year the underwriter should use judgment to determine if the income source will continue. The borrower does not have to be currently employed in order to use seasonal income, if received for the last two years and reasonably expected to continue.

UNEMPLOYMENT COMPENSATION

Income derived from unemployment compensation is generally not to be considered stable due to the limited duration of its receipt. Seasonal unemployment compensation income may be used when an applicant is employed.

To document Seasonal Income with Unemployment Compensation include the following:

- Two most recent years' federal tax returns.



- YTD paystub or salary voucher documenting at least one month of income. Borrower expects to be rehired next season.
- W-2s covering the two most recent years.
- Verbal VOE within 20 business days prior to the date printed on the Note. Proof of receipt of unemployment compensation for two years.

BORROWER'S INCOME PER JOB/CONTRACT BASIS

Borrowers whose income per job/contract basis is equal to or greater than 25% of their total income are considered to be self-employed. See INCOME ANALYSIS – SELF-EMPLOYED BORROWERS.

AUTOMOBILE ALLOWANCE

An automobile allowance may not be used for qualifying and may not be used to offset a car payment.

CAPITAL GAIN INCOME

Income received from capital gains is generally a one-time transaction; therefore, it should not be considered as part of the borrower's stable monthly income. However, if the borrower needs to rely on income from capital gains to qualify, the income must be verified in accordance with the following requirements:

- Must have a two-year consecutive history of receipt and likely to continue for the next three years.

RESTRICTED STOCK

Restricted stock refers to stock of a company that is not fully transferable until certain conditions have been met. Upon satisfaction of those conditions, the stock becomes transferable to the person holding the grant. Restricted stock should not be confused with stock options.

To document restricted stock income include the following:

- Issuance agreement or equivalent (part of the benefits package)
- Schedule of distribution of units (shares)
- Vesting schedule
- Stock must be publicly traded
- Evidence of payout of the restricted stock (e.g., YTD pay stub and 2 years W2s)

Calculation of income:

- Stock price should be averaged.
- In most cases the lower of current price or the price of the stock averaged (generally a minimum of 2-years) should be used to support qualifying income. The average stock price should be applied to the number of stock units vested each year.
- Qualifying income will be calculated using an average of the restricted stock income for the past two years, and year to date stock earnings. If stock income is declining, refer to DECLINING INCOME POLICY (SELF-EMPLOYMENT, BONUS, OVERTIME, COMMISSION, RESTRICTED STOCK).

Future vesting must support qualifying income. Value of future vesting should be based on the lower of current value or the average of stock price.

EMPLOYMENT BY RELATIVES OR TRANSACTION PARTICIPANTS

If the borrower is employed by a relative, a closely held family business, the property seller, real estate agent, or any party to the real estate transaction, the following documentation must be obtained:

- Borrower's signed and completed personal federal income tax returns for the most recent two years.
- If business is a corporation, obtain either of the following:
 - A signed copy of the corporate tax return showing ownership percentage.



- A signed letter from the corporation accountant stating the borrower has no ownership interest in the corporation.
- Most recent two years' W-2 forms. Year-to-date pay stubs covering 30 days.
- Verbal verification of employment (Exhibit 3) within 20 business days prior to the date printed on the Note.

Current income reported on the pay stub may be used if it is consistent with W-2 earnings reported on the tax returns. If the tax returns do not include W-2 earnings or income is substantially lower than the current pay stubs, further investigation is needed to determine whether income is stable.

MILITARY INCOME

Military Income – Active Duty Personnel – Within 12 Months of Release from Active Duty

The date that the in-service borrower is scheduled to be released from active duty must be verified. The date of separation is on the enlisted personnel's Leave and Earnings Statement (LES). An officer's LES does not show a date of separation. In most cases, a copy of the Statement of Service is satisfactory verification of continued service.

When the separation date is verified by a VOE, LES, and Officer's Orders, or other documentation, and indicates the veteran will be released from active duty within 12 months of the projected date upon which the Loan will be closed, the file must include one of the following:

- Documentation that the service member has reenlisted or extended the period of active duty to a date beyond the 12-month period following the projected Loan closing date.
- Verification of civilian employment following the release from active duty (with all pertinent underwriting documentation, such as job position, rate of pay, start date, number of hours scheduled per week, and probability of continued employment).
- A statement from the borrower indicating the intention to reenlist or extend active duty to a date beyond the 12-month period and a statement from the veteran's commanding officer confirming that the service member is eligible to continue on active duty and the commanding officer has no reason to believe the reenlistment or extension of active duty will not be granted.
- Other strong positive underwriting factors that minimize the effect of the possible discharge such as a non-military spouse's income being so high that only minimal income from the active duty member is needed to qualify, along with evidence that the veteran and spouse will be remaining in the community in which the property is located. A down payment of at least 10% and exceptional cash reserves would also minimize the effect of a possible release from active duty.

Military Income – Probability Of Continued Employment

If an employer declined to indicate the probability of continued employment on a verification of employment, the lender is not required to make any further attempt to get such a statement.

Military Income – Non-Taxable Income

Some military income is non-taxable. Other military income is partially taxed. Examples include:

- Base pay is the only income taxed for social security on in-service personnel.
- Base pay, Propay, sea pay, and flight pay are federally and state taxed.

Quarters allowance, variable housing allowance, clothing allowance, and rations are not taxed. See Other Income – Non-Taxable Income.

Military Income – Reservist or National Guard (Called To Duty) Obligation

Broker must ask every applicant, whose income is being used to qualify for a Loan, if their income is subject to change due to participation in a reserves/national guard unit due to activation.



When the answer is yes, broker must determine what the applicant's income may be if activated. If the income is:

- Reduced – carefully evaluate the impact the reduction may have on the borrower's ability to repay the loan.
- Increased – consider the likelihood the income will continue beyond a 12-month period.

Underwriters will evaluate all aspects of each individual case, including credit history, accumulation of assets, and overall employment history and make the best decision for each Loan regarding the use of income in qualifying for the Loan.

It is very important that Loan files be carefully and thoroughly documented, including any reasons for using or not using reservist income in these situations.

Weigh the desire to provide veterans their benefit with the responsibility to ensure the veterans will not be placed in a position of financial hardship.

To accomplish this, a statement must be obtained that affirms that a veteran-applicant's status relative to membership in the Reserves or National Guard has been ascertained and considered. The statement should be made as part of the origination package.

Military Income – Military Reserve Income

For income to be used for qualifying purposes, substantiate income by documenting all of the following:

- The continuity of employment and income history for the two years that precede the date of the mortgage application.
- YTD LES documenting at least one month of income.
- W-2s covering the most recent two years.
- Verbal VOE (Exhibit 3) within 20 business days prior to the date printed on the Note. (In lieu of a verbal VOE, a military LES within 30 days prior to the date printed on the Note date is acceptable).
- Provide proof that entitlements are expected to continue over a three-year period.

MORTGAGE DIFFERENTIAL INCOME

An employer may subsidize an employee's mortgage payments by paying all or part of the interest differential between the employee's present and proposed mortgage payments.

When calculating the qualifying ratio, the differential payments are added to the borrower's gross income.

The payments may not be used to directly offset the mortgage payment, even if the employer pays them to the mortgage lender rather than to the borrower. Two-year history is not required. The payments must be likely to continue for the next five years; However, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.

PUBLIC ASSISTANCE/GOVERNMENT ASSISTANCE INCOME

In order to be included in the borrowers' qualifying income, income from public assistance programs must be verified as received for the past two months and must reasonably be expected to continue for at least five years; however, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income. Public assistance income should be documented by letters or exhibits from the paying agency that state the amount, frequency, and duration of the benefit payments.

DISABILITY INCOME – LONG-TERM

General Requirements

Permanent/Long-term disability benefits may be paid to the applicant by a Federal agency, such as the Social Security Administration or Veterans Administration, a State agency, a private insurance company, workers



compensation insurance, an employer, or other disinterested third party.

Continuance

Continuance is not required for Social Security Disability Income (SSDI). For all other types of long-term disability income, the income must be likely to continue for the next 5 years. The continuance requirement may be reduced to 3 years if this income source contributes 25% or less of the qualifying income.

- If documentation does not contain any indication that the income will terminate within the next 5 years, assume income will continue for the next 5 years.
- If documentation indicates a termination date or conditions for termination of the payment, the termination must not occur within the next 5 years.

Note: If the documentation indicates the borrower's benefits are subject to periodic reviews or evaluations, this is not an indication that the income is unlikely to continue and does not require additional documentation for determining likelihood of continuance.

- If documentation indicates an expiration or modification date (such as reaching a certain age, etc.), verify that the remaining term is for at least 5 years.

Documentation

An Award Letter or equivalent written documentation confirming the source, amount, frequency, and borrower as the recipient of the payments must be provided.

Calculation Requirements

- Use the actual monthly amount received unless disability income is non-taxable. Refer to Other Income - Non-Taxable Income requirements in this Section regarding grossing up income.
- If the documentation indicates a reduction of the payment, use the lowest income indicated during the next 5-year period.

TEMPORARY LEAVE/SHORT-TERM DISABILITY/FAMILY LEAVE INCOME

Temporary Leave

Temporary leave from employment is typically short in duration and may be for many reasons, including parental (maternity or paternity) leave, short-term disability, and family leave. It may be taken with or without pay.

A borrower that is on, or scheduled to be on, temporary leave may still qualify for approval. A Loan with a borrower on temporary leave, including parental leave, is not ineligible for purchase merely because of such leave status. WinPrime Lending may purchase a Loan with a borrower on temporary leave provided:

- The application meets applicable underwriting and regulatory requirements
- AND
- The income used to qualify the borrower is sufficient to meet applicable debt-to-income ratios

The borrower must state they intend to return to work. The borrower is not required to return to work prior to closing.

If a borrower will not return to active work status on or before the first mortgage payment due date, temporary income received (if any) during the leave period and verified liquid assets after closing and reserves may be evaluated for use as qualifying income.

Calculation Requirements

For borrowers returning to work with their current employer prior to or on the first Mortgage payment due date:

- Qualify using pre-leave regular gross monthly employment income unless the borrower or employer has provided information about a reduction in that income upon the borrower's return to active work status.



For borrowers that will not return to work prior to or on the first Mortgage payment due date:

- Qualify using the lesser of:
 - The borrower’s temporary leave income (if any) combined with any available supplemental asset income.
 - OR
 - Pre-leave regular gross monthly employment income unless the borrower or employer has provided information about a reduction in that income upon the borrower’s return to active work status.
- If the temporary leave income is less than the borrower’s pre-leave regular gross monthly employment income, available verified liquid assets may be used as a partial or complete income supplement to the temporary leave income if all of the following requirements are met:
 - Only verified liquid assets can be used to supplement temporary leave income.
 - Assets that are required for the subject transaction (e.g., down payment, closing costs, and reserves) may not be used to supplement the borrower’s temporary leave income.
 - Supplemental asset income amount must be calculated as follows:
 - Available, verified liquid assets divided by the number of months of supplemental asset income.
 - The number of months of supplemental asset income is determined by the number of months from the first Mortgage payment due date to the date the borrower will begin receiving regular employment income after returning to work (i.e. pre-leave income unless the borrower or employer has provided information about a reduction in that income upon the borrower’s return to active work status), rounded to the next whole number. (See example provided in table below)

Note: If using assets to supplement income, manually reduce the assets before data entry of assets to avoid counting the same portion of these assets for both income and assets.

- Written rationale explaining the analysis used to determine the qualifying income.

| Supplemental asset income calculation example: | |
|--|---|
| Preleave income amount | \$6,000 per month |
| Temporary leave income | \$2,000 per month |
| Total verified liquid assets | \$30,000 |
| Funds needed to complete the transaction | \$18,000 |
| Available liquid reserves | \$12,000 (\$30,000 - \$18,000 = \$12,000) |
| First payment date | July 1 |
| Date borrower will begin receiving regular employment income | November 1 |
| Supplemental income | \$12,000/4 = \$3,000 |
| Total qualifying income | \$3,000 + \$2,000 = \$5,000 |

Documentation Requirements

All of the following:

- Verbal verification of employment. If the employer confirms that the borrower is currently on temporary leave, WinPrime Lending considers the borrower employed.
- Documentation of the borrower’s pre-leave income and employment, regardless of leave status. And,
- Written statement from the borrower confirming he or she intends to return to active work status at the



current employer and the intended date of return (must be consistent with employer-generated document). And,

- Documentation generated by current employer confirming the borrower's eligibility to return to the current employer after temporary leave and the duration or end date of the leave period.
 - ✓ Acceptable forms of employer documentation include, but are not limited to:
 - An employer-approved leave request, or
 - A Family Medical Leave Act (FMLA) document, or
 - Other documentation generated by the employer or a third-party verifier on behalf of the employer

AND

The following documentation is required if the borrower will not return to work prior to or on the first Mortgage payment due date AND where the borrower relies upon temporary leave income (not limited to short term disability benefits) for qualification purposes:

- Award Letter or equivalent written documentation confirming the following:
 - The amount and duration of the temporary leave income, and
 - The borrower as the recipient of the payments, and
 - The name of the payer (insurance company, employer, agency, or other qualified and disinterested party)
- If liquid assets are used to supplement income, assets must be verified and meet documentation requirements.

ROYALTY PAYMENTS

Royalty payments must have a 12-month history of receiving payments on a regular basis and must have a continuation period of at least five years; however, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.

Obtain completed, signed, individual federal tax returns for the most recent two years, including Supplemental Income and Loss and Schedule E, and a signed 4506-T.

SECTION 8 HOMEOWNERSHIP ASSISTANCE/HOMEOWNERSHIP SUBSIDIES

A monthly subsidy may be treated as income, if the borrower is receiving subsidies under Section 8 housing choice voucher home ownership option from a public housing agency (PHA). There is no requirement for the payments to have been received for any period of time prior to the date of the mortgage application. Section 8 voucher payments must be reasonably expected to continue for at least five years from the date of the mortgage application; however, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.

The monthly subsidy must be treated as income in determining the homebuyer's qualifying ratios when the monthly subsidy is remitted to the borrower.

RETIREMENT INCOME

Retirement income may be used if properly verified.

Acceptable documentation is:

- Most recent two months of bank statements, and one of the following:
 - Written verification from former employer
 - Federal tax returns
 - IRS 1099-R form



SOCIAL SECURITY INCOME

Social security income may be used if properly verified. Examples of acceptable documentation are:

- Most recent two months of bank statements.
- Social Security Administration benefit verification letter (sometimes called a proof of income letter, budget letter, benefits letter, or proof of award letter).

TIP INCOME

Tip income must be verified with two-year history of receipt.

To document, obtain all of the following:

- Most recent YTD paystub or salary voucher documenting at least one month of income.
- W-2s covering the most recent two years.
- Verbal VOE (Exhibit 3) within 20 business days prior to the date printed on the Note. The employer must verify that the tip income is expected to continue in the written VOE or in a separate statement.

FOSTER CARE INCOME

Income derived from foster care payments may be considered if written verification can be obtained that the income is regular, recurring, and continued receipt is likely. A two-year history of providing foster care services under a recognized program from a state- or county- sponsored organization is required. Income used to qualify must be averaged over this two- year period. Projected income may not be used. The income must be likely to continue for the next three years.

CHILD SUPPORT, ALIMONY, OR MAINTENANCE INCOME

Child support, alimony, or maintenance payments may be used as income only if this information is volunteered by the applicant, and if there is evidence that the court-ordered amount has been received on a continual basis for the most recent 12 months. In order to be used as income, these payments must reasonably be expected to continue for a five-year period; however, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.

If the payor has been obligated to make payments for less than 12 months, if the payments are not for the full amount, or are not received on a consistent basis, the income may not be considered for qualifying.

Required documentation:

- Final divorce decree
- Legal separation agreement
- Court order
- Voluntary payment agreement that has been approved by a court or is government- enforceable (for example, administered by a state agency) and acceptable evidence that payments have been received during the last 12 months, such as:
 - Canceled checks
 - Deposit slips or deposit receipts
 - Bank or other account statements
 - Tax returns
 - Court records

ALIMONY AND SEPARATE MAINTENANCE PAYMENTS TO BE PAID

Required alimony and separate maintenance payments must be deducted from income and should not be included in monthly liabilities. Alimony and separate maintenance payments must be documented with a copy



of the court order (such as a divorce decree).

Required Alimony or separate maintenance with less than 10 monthly payments remaining does not need to be deducted from income. A copy of the court order is required.

NON-TAXABLE INCOME

Special consideration can be given to regular sources of income that are non-taxable such as: Child Support

- Disability benefits
- Retirement income
- Worker's Compensation benefits
- Military allowances
- Other income that is documented as being exempt from Federal income taxes

To be considered as qualifying income, the underwriter must obtain documentation verifying that:

- The particular source of the income is non-taxable
- Both the income and its non-taxable status are likely to continue

Acceptable documentation includes tax returns and/or awards letters. If the income meets these requirements, the amount of tax savings attributable to the non-taxable income may be added to the borrower's income to develop an adjusted gross income. The adjusted gross income is used in calculations for the income and debt ratios. Standard qualifying ratios should not be exceeded when using grossed up income.

The following method must be used to determine the amount of tax savings that can be added back to the borrower's income:

- Add 25% of the non-taxable income to the borrower's qualifying income. This adjustment must be made whenever the non-taxable income source(s) is needed to qualify the borrower.

INTEREST OR DIVIDEND INCOME

Interest and dividend income may be used in calculating the qualifying income if the assets generating the income are verified and the interest income has been received for at least two years consecutively.

Complete, signed, individual tax returns for the most recent two years and a 4506-T must be used to verify this income.

The income must be averaged over 24 months. Subtract any funds used for down payment, closing costs, or as collateral for a Loan before calculating the interest at the rate of return received over the past 24 months.

Interest and dividend income must be expected to continue for three years if included in qualifying income.

NOTES RECEIVABLE, INSTALLMENT SALES AND LAND CONTRACTS

Secured or Unsecured

A copy of the Note is required to establish the payment amount and length of payment.

- Notes receivable payments must continue for at least five years; however, the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income.
- Installment sales and land contracts must continue for at least three years beyond the date of the mortgage application.

Evidence that these payments have been consistently received for the last 12 months must be verified through one of the following:

- Bank deposit slips or deposit receipts
- Canceled checks
- Bank or other account statements



- Tax returns

If the borrower is not the original payee on the Note, validate that the borrower is able to enforce the Note.

TRUST INCOME

Trust income may be used if the trust income will continue for at least five years; however the continuance requirement may be reduced to three years if this income source contributes 25% or less of the qualifying income. A photocopy of the trust agreement or the trustee's statement confirming the amount, frequency, and duration of the payments should be obtained to verify the income and continuance of the income.

Trust account funds may be used for the required down payment, closing costs, and reserve (post-closing liquidity) if the borrower provides adequate documentation that the withdrawal of funds will not negatively affect income. The borrower may use funds from the trust account for the required cash investment, but the trust income used to determine repayment ability cannot be affected negatively by its use.

If trust agreement or trustees statement does not provide historical level of distributions, most recent two years of tax returns must be obtained.

FOREIGN INCOME

Foreign income, for borrowers who do not qualify under the borrower requirements, is acceptable only if the income can be verified on United States personal tax returns.

Foreign income should be paid in United States currency. However, income paid in foreign currency may be considered on a case-by-case basis if it is converted into United States currency.

The following documentation requirements must be met:

Funds in foreign accounts: Must be transferred to U.S. account. Completed Verification of Deposit (VOD) or the two most recent months' bank statements for U.S. account.

Foreign Source – Employment Income:

- Most recent two years complete personal tax returns (IRS Form 1040).
- For Foreign National borrower only: Form W-8 (If borrower does not have tax ID number) or Form W-9 (If borrower has tax ID number) and letter from employer (translated into English) with:
 - annual income for most recent two years,
 - current monthly income,
 - current employment status,
 - name and title of person providing information,
 - borrower's job title, and
 - term of employment.
- A Verbal VOE (Exhibit 3) within 20 business days prior to the date printed on the Note is required.
- Tax transcripts from processed 4506-T may be used in lieu of tax returns provided by the applicant.

Foreign Source – Interest/Dividend Income:

- Most recent two years individual federal income tax returns (IRS Form 1040).

UNACCEPTABLE INCOME

The following types of income or compensation cannot be included when calculating the borrower's qualifying income:

- Expense account payments. Automobile allowances.



- VA education benefits – education benefits used to offset education expenses are not acceptable.
- Retained earnings in a company.
- Rent from boarders living in the borrower’s primary residence or second home. Proceeds from a reverse mortgage or other financing.
- Gambling income.

DEPARTURE RESIDENCE POLICY

CURRENT PRINCIPAL RESIDENCE IS PENDING SALE BUT WILL NOT BE SOLD (CLOSED) PRIOR TO THE NEW TRANSACTION:

Both the current and the proposed mortgage principal, interest, taxes and insurance (PITI) payments must be used to qualify the borrower for the new transaction, unless the following requirements can be met:

- A copy of the fully executed non-contingent sales contract for the departure residence (cash sale of the departure residence is not allowed), and
- A lender’s commitment from a regulated institution to the buyer of the departure residence with all financing contingencies cleared, and
- Standard reserve requirements plus an additional six months PITI for departure residence. Borrower is required to have a 20% equity position in the departure residence based on contracted sales price. Further documentation may be required if there is a significant difference between the sales price and estimated property value.

When the departure residence will not be sold at the time of closing and is in a negative equity position, the following may be required to reduce the overall risk:

- Additional reserves to cover the negative equity of the departure residence, OR
- Pay down the lien on the departing residence to eliminate the negative equity.

EXISTING PRINCIPAL RESIDENCE CONVERTING TO SECOND HOME

- Both the current and the proposed mortgage PITI payments must be used to qualify the borrower for the new transaction, and,
- Reserve requirements are the greater of six months PITI for both properties or the standard post-closing/reserve requirements.

EXISTING PRINCIPAL RESIDENCE CONVERTING TO INVESTMENT PROPERTY

If there is documented equity of at least 30 percent in the departure property, 75 percent of rental income may be used to offset the mortgage PITI payment in qualifying when:

- Reserve requirements are the greater of six months PITI for both properties or the standard post-close liquidity, and
- Rental income is documented with a fully executed lease agreement when the borrower’s tax returns reflect a two-year history of managing investment properties, as evidenced by the most current two years filed and signed Federal IRS 1040 tax returns, and
- Proof is provided that a security deposit was received from the tenant and deposited into the borrower’s account.

If rental income will not be used to offset the mortgage payment to qualify, the following reserve requirements must be met:

- The greater of six months PITI for both properties or the standard post-closing/reserve requirements.

If 30 percent equity in the departure property cannot be documented, or the borrower does not have a two-year history of managing investment properties as evidenced by the most current two years filed and



signed Federal IRS 1040 tax returns, rental income may not be used to offset the mortgage PITI payment in qualifying and:

- Both the current and the proposed mortgage PITI payments must be used to qualify the borrower for the new transaction; and
- Reserve requirements are the greater of six months PITI for both properties or the standard post-closing/reserve requirements.

DEPARTURE RESIDENCE CONVERTING TO INVESTMENT PROPERTY EQUITY POSITION

To document equity position in the departure property converting to an investment property, a full appraisal must be obtained.

The appraisal must be dated within 120 days of the date printed on the Note of the current transaction.

ASSET

BONUS INCOME USED FOR CASH TO CLOSE

A borrower's recent bonus may be used for cash to close when the impact to borrower's qualifying income is analyzed.

It may be required to deduct the bonus from qualifying income when it is used as cash to close if the Underwriter determines that the borrower is unable to meet all financial obligations and living expenses until the next bonus payout. Considerations may include, but are not limited to:

- How often is the bonus paid (i.e. quarterly, semi-annual, annual) and what is the date of the last bonus payout?
- What is the amount of the bonus used for cash to close?
- Are base income and liquid reserves sufficient to allow borrower to meet all obligations and living expenses until the next bonus is received?
- Are liquid reserves sufficient to ensure the borrower has the ability to repay obligations in a timely fashion and to support the borrower's overall income profile for acceptable risk?

Refer to Cash Assets for additional requirements for cash assets used for down payment and closing costs.

USE OF CREDIT CARD FOR PAYMENT OF FEES

A credit card may be used to pay fees associated with the Mortgage. Acceptable fees are:

- Appraisal
- Credit Report
- Origination fee
- Commitment fee
- Lock-in fee
- Extended Lock fee

Acceptable credit cards are:

- Visa
- MasterCard
- Discover

The Loan must meet all of the following requirements:

- Borrower must have sufficient liquid assets to pay the amount charged (in addition to all other Closing costs).
- The maximum amount charged or advanced may not exceed 2 percent of the Mortgage amount.
- Under no circumstances may credit card financing be used for the down payment.



- The amount charged or advanced must be included in the borrower's total outstanding debt and the repayment of that amount must be included when determining qualifying ratios (greater of \$10 or 5 percent of the outstanding balance).
- A copy of the charge receipt must be included in the Loan file.
- The HUD-1 or Closing Disclosure must reflect a paid outside/before Closing (POC) credit to the borrower for the amount charged.

USE OF PREMIUM PRICING

For all transactions, the funds derived from premium pricing (Credit for Interest Rate Chosen, CFIRC), are only allowed to be used to pay the borrower's typical Closing costs and/or prepaid expenses.

Typical prepaid items paid by the borrower:

- Interest charges covering any period after the settlement date.
- Real estate taxes covering any period after the settlement date.
- Hazard insurance premiums.
- HOA dues

Typical Closing costs paid by the borrower:

- origination fee
- discount points
- appraisal fees
- title searches and surveys
- title insurance
- taxes
- deed-recording fees
- credit report charges

CFIRC may not be used to pay any portion of the borrower's down payment, personal debts (ex: revolving debt), collection accounts, judgments, escrow shortages or any other item that is not considered a typical prepaid item or typical Closing cost paid by the borrower as listed above. Other property improvement expenses not related to the transaction or not required by the purchase contract are not allowed.

For transactions where CFIRC exists, cash back to the borrower as a result of the premium pricing is restricted to the lesser of 1% of the Loan amount or \$2500.

GIFT FUNDS

For primary homes, the full down payment may be from a gift when the LTV/CLTV is 80 percent or less.

USE OF BUSINESS FUNDS

When a borrower has insufficient personal liquid assets to qualify or close, but has sufficient verified funds in a 100 percent owned business, the business funds may represent an adequate source of down payment and reserves (post-liquidity) if both of the following conditions are met:

- Business average annual cash flow is greater than the amount to be withdrawn/reserves.
- Cash on company year-end balance sheet for each of the previous three years is greater than the amount to be withdrawn/reserves. This information is found on line 1 of the schedule L for the Partnership, S-Corporation and the Corporation. A three-year history of a balance greater than or equal to the amount being considered for reserves (post-closing liquidity) or down payment is required. Two years of the schedule L will show three years of cash on hand for the company.



Full analysis of the business must consider the effect of the withdrawal of the assets and how it will impact the strength and viability of the business in the future.

The following questions need to be considered:

- What is the pattern of company cash flows? Do we have declining gross or net income?
- Do we have concerns about the type of business? Is the business experiencing a downturn?

Extreme care needs to be taken when considering business use of funds and in some cases even though a business is profitable, it may not be prudent to use the business assets in our transaction.

PROCEEDS FROM SECURED LOANS

Subordinate Financing

Subordinate financing, Closed End or HELOC, is allowed subject to the guidelines in Subordinate Financing.

The maximum LTV/CLTV* may not exceed the guideline limits for the product and occupancy type shown in Jumbo LTV Matrix.

*For Jumbo Loans, the CLTV is calculated by adding the first mortgage amount to all subordinate financing and dividing that sum by the value of the mortgaged premises. When subordinate financing is a HELOC, the credit line limit – rather than the amount of the HELOC in use – must be used.

IRA, 401(K), SEP, KEOGH, 403(B), AND IRS-QUALIFIED EMPLOYER PLANS

IRA, 401(k), SEP, KEOGH, and other IRS-qualified employer plans may be used for down payment and closing costs, up to the post-tax and post-penalty amount available to the borrower for distribution.

A copy of the plan statements for the most recent two months is required. The statement should be reviewed to determine the borrower's vested amount in the plan.

If there is a penalty for withdrawal, discount the asset by the applicable amount. Verification of liquidation is required.

TRADES

Equity from trading a borrower's existing property is acceptable after the borrower has made a five percent cash down payment. The amount of equity is determined by subtracting the outstanding Loan balance of the property that is being traded, plus any transfer costs, from the lesser of that property's appraised value or its trade-in value, as agreed to by both parties.

A separate written appraisal for the property that is being taken in trade is required. A search of the land records to verify ownership of the property and to document if there are any existing liens on the property is also required.

1031 TAX DEFERRED EXCHANGES

Refer to Other Assets For Down Payment.

STOCK, BONDS, MUTUAL FUNDS, U.S. GOVERNMENT SECURITIES AND PUBLICLY TRADED SECURITIES

Allowed. Refer to Cash Assets.

PUBLICLY TRADED STOCKS, BONDS, MUTUAL FUNDS, U.S. GOVERNMENT SECURITIES

A copy of the account statement for the most recent two months/quarter is required; proof of liquidation is required provided that the existence of these accounts is fully documented. When the asset is needed to complete the transaction, verify:

- the borrower's ownership of the asset,



- the value of the asset at the time of sale or liquidation, and
- the borrower’s actual receipt of funds realized from the sale or liquidation.

RESTRICTED STOCK SUBJECT TO U.S. SECURITIES AND EXCHANGE COMMISSION (SEC) RULE 144

Many executives receive a portion of their compensation in the form of company stock. When using vested company stock that is subject to SEC Rule 144 the following documentation is required:

- When stock is used for down payment provide proof of liquidation.
 - When stock used for reserves provide:
 - Evidence that stock is eligible for resale as defined by the SEC Rule 144,
 - A letter from the company which includes:
 - Vesting statement
 - Eligibility to liquidate stock
 - Current stock price
 - Addresses any additional restrictions on liquidating stock other than those imposed under SEC Rule 144
- Refer to SEC website for the current Trading Volume Formula for calculating eligible value.

DEPOSITORY ACCOUNTS

For all transactions, generally, single deposits that are greater than 50 percent of the borrower's monthly qualifying income should be explained and documented. Consideration will also be given to total monthly income, type of employment, total amount of all assets and reasonableness based on borrower’s overall credit and transaction profile.

INELIGIBLE ASSETS

The following assets are not allowed: Sweat equity

- Group Savings
- Pooled Funds
- Saving cash to close
- Stock options in a qualified plan but not fully vested
- Stock options in a non-qualified plan
- Assets held in a UGMA (Uniform Gift to Minors Act) or UTMA (Uniform Transfers to Minors Act)

RESERVES/ POST-CLOSING LIQUIDITY (PCL)

▪ Primary Residence Reserve/PCL Requirements

| Loan Amount/Adjusted Combined Loan Amount ¹ | Single Family Detached/Attached, PUD, Co-op, Condo | 2-unit | 3- to 4-unit |
|--|--|----------------|----------------|
| Up to \$1,000,000 | 12 months PITI | 12 months PITI | 36 months PITI |
| >\$1,000,000-\$2,000,000 | 12 months PITI | 18 months PITI | |
| >\$2,000,000-\$4,000,000 | 24 months PITI | | |

1. Adjusted combined loan amount (total of all loans/outstanding line balances against the subject property) applies when secondary financing exists. (i.e., when subordinate financing is a line of credit, the outstanding balance is used).



▪ Second Home – Reserve/PCL Requirements

| Loan Amount/Adjusted Combined Loan Amount ¹ | Single Family Detached/Attached, PUD, Co-op, Condo |
|---|--|
| Up to \$1,000,000 | 18 months PITI |
| >\$1,000,000-\$2,000,000 | 24 months PITI |
| >\$2,000,000-\$4,000,000 | 36 months PITI |
| 1. Adjusted combined Loan amount (total of all loans/outstanding line balances against the subject property) applies when secondary financing exists. | |

▪ Investment Property – Reserve/PCL Requirements

| Loan Amount/Adjusted Combined Loan Amount ¹ | Single Family Detached/Attached, PUD, Co-op, Condo |
|---|--|
| Up to \$1,000,000 | 24 months PITI |
| >\$1,000,000-\$2,000,000 | 30 months PITI |
| 1. Adjusted combined Loan amount (total of all loans/outstanding line balances against the subject property) applies when secondary financing exists. | |

Liquid assets verified to meet the reserve (PCL) requirements may be in the form of:

- Cash equivalents (checking, savings, or money market accounts)
- 100% of the vested value of publicly traded stocks, mutual funds, and government securities may be used.
- Cash surrender value of life insurance (less outstanding loans, if repayment not included in debt ratio calculation)
- Retirement funds may be used to meet up to 50 percent of the minimum reserve requirements.
- Gross retirement funds must be discounted by 30 percent to account for tax consequences (less any outstanding loan balances) to determine the actual funds available for reserve requirements.
 - There must be an additional 10% reduction if an early withdrawal penalty exists.
- 100% of Roth IRA (less outstanding loans)
- Equity proceeds from the sale of a residence.
- Funds held in business accounts may be eligible for use if the requirements detailed in Asset Section are met.

The following assets are ineligible for purposes of meeting the minimum reserve (PCL) requirement:

- Gift funds
- Borrowed funds
- Stock in a closely held corporation
- Proceeds from the sale of assets other than the sale of a residence. Proceeds from a cash-out refinance transaction.

INTERESTED PARTY CONTRIBUTIONS

| Property Type | LTV | Contribution ⁽¹⁾ |
|--|------|-----------------------------|
| Primary Residence | ≤80% | 6% |
| 1. HOA fees/dues prepaid by any party other than the borrower are not allowed. | | |



MULTIPLE FINANCED PROPERTIES

- The following guidelines apply to the number of 1-4 unit financed properties owned by all borrowers on the Loan transaction, not just the primary borrower.

| Property Type | Then the maximum number of 14 unit properties that may be financed with WinPrime Lending is: | and the total maximum number of financed 14 unit properties with all lenders including WinPrime Lending is: |
|---------------|--|---|
| Primary | 4 | 4 |
| Second Home | 4 | 4 |
| Investment | 4 | 4 |

- When aggregate financing for all properties owned by borrower exceeds \$3 million one of the following is required: Min. reserve (post-closing liquidity) is 36 months PITI or Max. 50% LTV/CLTV.
- There are no restrictions on the number of properties that a borrower owns free and clear.

APPRAISALS

- All appraisals must be completed by WinPrime Lending Approved Appraiser

| Total Loan Amount | CLTV | Appraisal Documentation Required | | |
|------------------------------|-----------|---|---|---|
| | | Median Home Price Multiple | | |
| | | ≤4 times Median Home Price | >4 ≤10 times Median Home Price | >10 times Median Home Price |
| ≤ 1,000,000 | All | One full appraisal ⁽¹⁾ | One full appraisal ¹ | One full appraisal ¹ |
| >\$1,000,000 ~ ≤ \$1,500,000 | ≤70% | One full appraisal ⁽¹⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ |
| | >70% ≤80% | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | | |
| >\$1,500,000 ~ ≤ \$2,000,000 | All | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ |
| >\$2,000,000 | All | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ | One full appraisal ⁽¹⁾ completed by a certified appraiser ⁽²⁾ and a Residential Valuation Services (RVS) Desk Review ⁽³⁾ |



1. A full appraisal is one prepared on form 1004/70, 2090, or 1073. A PIA/PIW, 2055, 1075 or 2095 Summary Report is not acceptable.
2. All appraisals must be completed by a WinPrime Lending Approved appraiser
3. RVS review products will be ordered by Investor. LTV/CLTV will be based on the lower of the reviewed value or the sales price.

HIGH DOLLAR APPRAISAL ADDENDUM

A high dollar appraisal addendum is required when the total Loan amount provided by WinPrime Lending is greater than \$2,000,000 and the property value is greater than \$2,500,000 as evidenced by the purchase price or the owner's estimate of value stated on the application. The high dollar appraisal requirement is not based on the appraised value.

The high dollar appraisal addendum must include all of the following:

- A summary of sales located in the subject's immediate neighborhood even if the sales are not considered comparable by the appraiser and even if they are not used in estimating the subject's market value.
- Days on market (DOM) for each comparable sale.
- Marketing time required to realize the market value estimated for the subject property.
- Include a market analysis for all properties priced within 25% of the subject's estimated value that addresses each of the following three factors:
 - In the selected price range, how many sales have occurred in the last 12 months?
 - In the selected price range, how many properties are currently listed for sale?
 - In the selected price range, how many properties have had listings expire or be withdrawn in the last 12 months?
- For purchase transactions, also include:
 - Names and phone numbers of the listing and selling agents.
 - Total listing period for the subject property (include list price decreases, if any).

HIGHER-PRICED COVERED TRANSACTIONS

Qualified Mortgages defined as "Higher-priced covered transactions" under the ability to repay provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which amended the Truth in Lending Act (TILA), are ineligible.