



# Bankers Advisory

## COMPLIANCE MONITOR

August 25, 2015

### *Fannie Mae Updates Self-Employment Income and Other Rules*

By Anna DeSimone

August 25, 2015 Fannie Mae released Ann. SEL-2015-09: *Selling Guide* Updates. Below is the complete content from the announcement.

#### **Selling Guide Updates**

The Selling Guide has been updated to include changes to the following:

- Self-Employed Income
- Project Eligibility Review for Attached Planned Unit Developments
- HomeStyle® Renovation
- Cash Back Pair-offs on Mandatory Whole Loan Commitments
- Miscellaneous Selling Guide Updates

Each of the updates is described below. The affected topics (and specific paragraphs) are noted for each policy change. Lenders should review each topic to gain a full understanding of the policy changes. The updated topics are dated August 25, 2015.

#### **Self-Employed Income**

Fannie Mae has updated the self-employment income policies published in December 2014 regarding how to calculate and document self-employment income, including the parameters under which business income without a history of distribution may be included to qualify self-employed borrowers.

This policy update provides an alternative approach that lenders may follow for borrowers who do not show a history of receiving distributions of business income provided certain conditions are met. Specifically, in order to include business income to qualify a self-employed borrower who does not have a history of receiving business income, the lender must confirm the borrower has access to the business income and the business must have adequate liquidity to support the withdrawal of earnings.

The approach and instructions published in December 2014 for self-employed borrowers who can provide a documented history of receiving distributions of business income remains in effect, as another approach lenders may follow when qualifying these borrowers.

A minor clarification has been made to broaden a reference to “salaried income” in a section that addresses when lenders need to prepare a written evaluation of self-employment income. We now refer to borrowers who are qualified using only “income that is not derived from self-employment”. For example, when qualifying borrowers using only retirement income to qualify, no written evaluation of secondary self-employment income is required.

In addition to these updates, the Selling Guide has been updated to reflect that only the most recent year of individual and business federal income tax returns will be required for certain Desktop Underwriter® (DU®) loan casefiles,

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provided the tax returns show at least 12 months of self-employment income and the lender completes the Fannie Mae Cash Flow Analysis (Form 1084) or any other type of cash flow analysis form that applies the same principles. This flexibility will become available in DU in a future release, and will be communicated to lenders in the associated release notes.

Lastly, the December 2014 version of the *Cash Flow Analysis* (Form 1084) has been revised to incorporate these policy updates and improve ease of use.

### **Updated Selling Guide Topics**

- B3-3.1-09, Other Sources of Income (Schedule K-1 Income)
- B3-3.2-01, Underwriting Factors and Documentation for Self-Employed Borrower (Analysis of Borrower's Personal Income, Income Verification for Self-Employed Co-Borrowers)
- B3-3.2.1-01, General Information on Analyzing Individual Tax Returns (Removed Cash Flow Analysis Form 1084)
- B3-3.2.1-08, Income or Loss Reported on IRS Form 1065 or IRS Form 1120S, Schedule K-1 (Income or Loss Reported on IRS Form 1065 or IRS Form 1120S, Schedule K-1, Documentation Requirements)
- B3-3.2.2-01, Analyzing Partnership Returns for a Partnership or LLC (Evaluating the Business Income, Borrower's Proportionate Share of Income or Loss, Adjustments to Business Cash Flow, Income from Partnerships, LLCs, Estates, and Trusts)
- B3-3.2.2-02, Analyzing Returns for an S Corporation (Evaluating the Business Income, Borrower's Proportionate Share of Income or Loss, Adjustments to Business Cash Flow)
- B3-3.3-01, Income and Employment Documentation for DU (Self-Employment Income)

### **Effective Date**

On March 24, 2015, Fannie Mae delayed the mandatory implementation of the self-employed income policies announced in December 2014. Lenders had the discretion to choose to move forward with implementation of some or all of the changes. With these latest updates, lenders are now encouraged to implement all of the self-employed income policies immediately (with the exception of the DU update referenced above), but must do so for mortgage loans with application dates on or after February 1, 2016.

### **Project Eligibility Review for Attached Planned Unit Developments**

The current Planned Unit Development (PUD) review policy requires lenders to conduct a review of the ineligible project characteristics list to confirm that attached PUDs meet Fannie Mae's project eligibility requirements. Detached units in PUD projects are not subject to this review requirement. Fannie Mae re-evaluated this policy and is now aligning the requirements for attached and detached PUD projects. As a result of that effort, the requirement that attached PUDs be reviewed against the ineligible projects criteria has been removed.

### **Updated Selling Guide Topics**

B4-2.1-02, Ineligible Projects (List of Ineligible Project Characteristics)

B4-2.3-01, Eligibility Requirements for Units in PUD Projects

### **Effective Date**

This update is effective immediately.

## HomeStyle Renovation

The HomeStyle Renovation product allows Fannie Mae-approved lenders to deliver HomeStyle Renovation loans prior to completion of the renovation work provided the loan is delivered with recourse. Going forward, Fannie Mae will begin documenting lender approval to deliver HomeStyle Renovation mortgages in the addendum to the Master Selling and Servicing Contract (MSSC). Therefore, a master contract and credit variance will no longer be required to deliver HomeStyle Renovation loans. For lenders who are already approved to deliver HomeStyle Renovation mortgages, the Fannie Mae account team will update the Master Agreement before or at the time of contract renewal. There will be no impact to a lender's ability to deliver these loans. As a result of this change, the documentation requirements for removing recourse have been added to the Selling Guide. In addition, Fannie Mae currently requires the lender to obtain a certification of completion from the appraiser documented on Fannie Mae's HomeStyle Completion Certificate (Form 1036). In order to provide lenders with additional flexibility, the Selling Guide has been updated to permit the use of either the Appraisal Update and/or Completion Report (Form 1004D) or Form 1036 as evidence of completion.

To improve content organization, the sections concerning HomeStyle Renovation LTV Ratios and Limited Cash-out Transactions have been moved from B5-3.2-03, HomeStyle Renovation Mortgages: Collateral Considerations, to B5-3.2-02, HomeStyle Renovation Mortgages: Loan and Borrower Eligibility. Also, some topic and section titles have changed to more clearly describe contents.

### Updated Selling Guide Topics

- A2-4-01, Master Agreement Overview (Mortgage Loan Types that Require a Master Agreement)
- B5-3.2-01, HomeStyle Renovation Mortgages (Removal of Recourse)
- B5-3.2-02, HomeStyle Renovation Mortgages: Loan and Borrower Eligibility
- B5-3.2-03, HomeStyle Renovation Mortgages: Collateral Considerations
- B5-3.2-05, HomeStyle Renovation Mortgages: Completion Certification

### Effective Date

Lenders may implement these policy changes immediately. The DU message regarding the certification of completion will be modified in a future release to reference the new options. Until that time, lenders may disregard the certification of completion form requirement in DU and comply with the updated *Selling Guide* requirements to submit either Form 1004D or Form 1036.

### Cash Back Pair-offs on Mandatory Whole Loan Commitments

The option of providing lenders cash back on a pair-off of a mandatory whole loan commitment if the market has moved in the lender's favor has only been available to certain lenders on a negotiated, contractual basis. As part of Fannie Mae's effort to simplify offerings and provide greater certainty to lenders, this option will be a standardized process and has been added to the *Selling Guide*, no longer requiring that lenders engage in special negotiations or execute additional contracts.

Under the cash back pair-off process, if the lender is unable to meet the terms of a mandatory whole loan commitment and, because of market fluctuations, the applicable whole loan price at commitment is greater than the price at the time of pair-off, Fannie Mae will provide the lender with cash back.

### Updated Selling Guide Topics

- C1-1-01, Execution Options (Volume Limitations, Whole Loan Sale Commitments)
- C2-1.1-02, Pricing, Fees, and Pricing Adjustments (Up-front Commitment, Extension, Overdelivery, Pair-off and Other Fees; Additional Resources [new block])

- C2-1.1-04, Mandatory Commitment Extensions and Pair-Offs (Lender-Requested Pair-offs, Fannie Mae-Implemented (Automatic) Pair-offs, Additional Resources [new block])
- E-3-03, Glossary of Fannie Mae Terms: C
- E-3-16, Glossary of Fannie Mae Terms: P

### **Effective Date**

This update is effective for all mandatory whole loan commitment pair-off requests made on and after August 31, 2015.

### **Miscellaneous Selling Guide Updates**

A2-5.1-02, Individual Mortgage Loan Files (Contents of a Mortgage Loan File). In June 2015, Fannie Mae updated the Selling Guide to include references to the new Closing Disclosure form that becomes effective for mortgage loan applications dated on or after October 3, 2015. This update included a requirement that the lender use the applicable version of the Closing Disclosure form for the transaction (the standard version or the alternate version for refinances). This requirement aligned with information Fannie Mae and Freddie Mac have communicated as part of the Uniform Closing Dataset (UCD) requirements. Fannie Mae has received feedback from a number of lenders that they are not prepared to implement both the standard version and the alternate version at this time. To address this concern and help ease implementation of the new Disclosure, the Selling Guide is being updated to remove the requirement for the alternate form at this time. Fannie Mae encourages the use of the alternate form for refinances now, and will communicate its mandatory usage and delivery in UCD at some point next year.

B4-2.1-02, Ineligible Projects (Non-Incidental Business Arrangements). The examples of non-incidental business income have been revised. Income earned by the homeowners' association that is the result of lease agreements with telephone, cable, and Internet companies has been removed as an example of non-incidental income, as this income does not meet the definition of active ownership or operation of amenities or services available to unit owners and the general public. Therefore, the 15% cap (relative to the project's operating budget) does not apply to this type of income.

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