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Introduction

Summary

MSI provides these Underwriting Tips as a tool to assist Sellers in understanding the underwriting standards and requirements for selling loans to Mortgage Services III (MSI).

- ✓ They are neither legal advice, nor are they to be construed as a guarantee of loan purchase.
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Basics

MSI requires:

- ✓ **AUS - Each** loan delivered (with the exception of Government Streamline Refinance Loans) must utilize an Automated Underwriting system (DU or LP) **and** the results of the findings report must be delivered with the loan file.
 - The findings are not conclusive until an experienced underwriter evaluates and authenticates the findings against the documentation provided with the loan file.
 - Any material change to the data submitted must be resubmitted for evaluation prior to the loan delivery to MSI III.
 - ✓ An AUS does not “approve” the loan application. The AUS **evaluates** the risk associated with the application as presented.
 - It is the underwriter who makes the decision to approve the loan by evaluating the accuracy, integrity and validity of the information and documentation that supports the decision.
 - The underwriter is responsible for ensuring that each loan submitted has also been underwritten in accordance with Agency, State and Federal guidelines and restrictions, and that the loan supports all findings in the AUS report.
 - Additionally, to be salable to MSI, the underwriter must ensure that each loan meets the published MSI overlays/guidelines.
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Mortgage Services III, LLC

A Subsidiary of First State Bank Member FDIC

Quick Reference Sheet Delegated Underwriting Tips

Underwriting The Loan

Process

Underwriting is a process that requires attention to detail and suspicion of information that cannot be validated. Although each underwriter has their own personal process, the following steps outline the details that need to be considered by every good underwriter:

Step	Action
1	Analyze all the information provided by the applicant which includes comparing the initial signed/dated 1003 to the final 1003. <ul style="list-style-type: none"> ✓ With the new Mortgage Disclosure Improvement Act (MDIA), MSI does require that the initial 1003 be signed and dated by the Borrowers and the Interviewer to validate the date of application to ensure compliance.
2	Ensure that all the information on the application is fully supported by documentation. <ul style="list-style-type: none"> ✓ MSI has specific documentation requirements. See the Seller Guide for applicable details.
3	Ensure that all applicant's credit risk score (FICO) meets the minimum FICO for the product requested. <ul style="list-style-type: none"> ✓ The Seller Guide and/or Product Sheet provide the MSI minimum FICO requirements.
4	Ensure the accuracy of all data entry in to the AUS system: See Additional Notes and Comments . <ul style="list-style-type: none"> ✓ Income ✓ Assets ✓ Reserves after closing ✓ Payment of all liabilities which also includes documenting any other housing payments including all escrows (PITI) ✓ Appraisal and property type is accurate ✓ The appraised value fully supports the loan transaction
5	Clarify the omission or exclusion of debts on the AUS findings.
6	Accurately calculate the LTV and any applicable CLTV. <ul style="list-style-type: none"> ✓ It is critical that the closed loan delivered to MSI match the loan information locked and priced by MSI.
7	Ensure all the bullet points on the AUS findings are addressed. <ul style="list-style-type: none"> ✓ It is critical that the delivered closed loan is accurate to the AUS findings and validated documentation.
8	Address any "red flags" including potential fraud and/or identity theft. <ul style="list-style-type: none"> ✓ "Red Flag" listings and assistance is provided as a service by many of the Mortgage Insurance companies. ✓ MSI encourages the use of any fraud tool, social security number search or MERS check prior to your loan closing to assist in the discovery of any undisclosed liabilities or other pending undisclosed transactions for your protection.

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Underwriting The Loan, Continued

Process, Continued

Step	Action
9	<ul style="list-style-type: none"> ✓ Investigate if numerous inquiries reported on the credit report require an explanation from the applicant(s). ✓ Pursue to uncover if any new credit obligations resulted from the inquiries, (regardless whether or not the AUS findings address the issue; it is a matter of prudent underwriting to ensure that new debt will not cause the borrowers to default.)
10	<p>Address any findings of undisclosed debts by the applicant.</p> <ul style="list-style-type: none"> ✓ This should be addressed in writing, by both the applicant and the underwriter.
11	<p>Review the Tax Transcripts.</p> <ul style="list-style-type: none"> ✓ MSI requires the most recent 2-years tax transcripts, regardless whether the AUS required full (2-year) or reduced (1-year) income documentation. ✓ Review the processed tax transcripts for the following undisclosed or non-supported information: <ul style="list-style-type: none"> • Self-employment. • Property ownership. • Losses that can affect ability to repay the mortgage obligation. • Expenses or even the address history reflected on the filing that correlates to the address history applicants provided on the 1003. <p>Note: Quality control auditors in the secondary market expect that the tax transcripts substantially provide the same borrower(s) profile as provided on the initial and final 1003 and the documentation provided in the loan file.</p>
12	<p>Underwriter must sign the official approval document for our file retention.</p> <ul style="list-style-type: none"> ✓ MSI requires that the underwriter sign the final 1008 in Section III. Printed name is optional; however the signature must appear on the "underwriter" line in Section III.
13	<p>Perform the Verbal VOE</p> <ul style="list-style-type: none"> ✓ MSI provides requirements in the Underwriting Chapter of the Seller Guide. ✓ If the borrower(s) is no longer employed, or if there are significant discrepancies from the originally validated employment. <ul style="list-style-type: none"> • The loan must be re-reviewed to make sure the borrower(s) still qualify for the loan. The underwriter should provide written justification for approving the loan with the altered circumstance.

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Underwriting The Loan, Continued

Additional Notes and Comments

Data Integrity

Data integrity is key and the obligation for loan salability.

- ✓ Solid data integrity should help to eliminate any future potential loan buy-backs for AUS approvals without supporting documentation.
 - ✓ Not all situations can be accurately addressed in the AUS findings.
 - In those circumstances it is the underwriter's responsibility to address these issues **in writing** on the 1008, 2900LT or VA Loan Analysis so it is clear to any auditor that will review the loan file after the loan sale.
 - Situations can also include (but are not limited to) occupancy of the subject property.
 - A motivational letter from the borrowers can many times avoid issues with this situation.
 - ✓ It is the underwriter's obligation to justify the credit decision.
 - MSI does require a written document showing the calculation used to arrive at the qualifying income.
 - This is required for all borrowers, regardless of the type of income.
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Common Errors

Summary

MSI performs a quality control audit of each loan file delivered for purchase.

- ✓ The audit may be perfunctory or it may be an in-depth re-underwrite of the entire loan.
- ✓ Additionally, as the loan is sold through the secondary market, other quality control auditors may review the loan.
- ✓ Loans may be purchased and then be noted for "buy-back" based on these audits.

MSI provides the following listings of common errors based on feedback from the quality control audits in an effort to provide assistance to our business partners.

- ✓ In our opinion, if these errors are eliminated, the chance of loan non-purchase and/or buy-back is greatly reduced.
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Assets

Common Errors in Assets

- ✓ Minimum down payment requirement is not fully documented.
 - ✓ Seller tax credits were utilized in the calculation in the AUS and borrowers down payment not met.
 - ✓ Complete bank statements (all pages as required) were not included.
 - ✓ Assets were not properly calculated, (i.e., 60% of the vested amount of retirement accounts after reduction of any outstanding loans).
 - ✓ Gift funds are not fully documented, including transfer to the applicant(s).
 - ✓ Refinance transaction where assets needed to close on the HUD 1 but no verification of any assets in the file or the AUS.
 - ✓ Assets are duplicated, particularly earnest money that hadn't cleared the current assets but used as a credit in the AUS.
 - ✓ No documentation provided to support the source of large deposits.
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Common Errors, Continued

Income

Common Errors in Income

- ✓ Variable income sources only reflected as base pay, especially bonus and commissions which must be separately entered into the AUS.
- ✓ Averaging declining income or not utilizing lower year to date paycheck figures.
- ✓ Not annualizing bonus income calculation or documenting received 2 years from the same employer.
- ✓ Utilizing commission income without a minimum 2 year documented history in the same field with increasing or steady earnings trend.
- ✓ Utilizing qualifying income from 2 jobs without a minimum documented 2 history of applicant working 2 jobs with a steady or increasing earnings trend.
- ✓ Rental income utilized without support documentation when not reflected on prior tax return transcript.

DTI

Common Errors in DTI Ratios

- ✓ Incorrect calculation of the income or not accounting for valid losses or applicable deductions to income.
- ✓ Exclusion or omission of debts that will actually be remaining with a payment obligation after closing.
- ✓ Garnishments reflected on the paystubs but not identified or utilized in the qualifying.
- ✓ Failure to include the entire proposed housing debt accurately, principal and interest, accurate real estate tax assessment, HOA fees, monthly MI, hazard insurance in the ratio.
- ✓ Incorrect calculation of a HELOC payment.
- ✓ Inclusion of the full PITI on a retained property that isn't reflected on the tax transcripts.
- ✓ Elimination of deferred payments from the qualifying ratio when not allowed.

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Common Errors, Continued

Credit

Common Errors with Credit

- ✓ Incorrect qualifying payments used on revolving accounts including HELOCs.
 - 90 days same as cash accounts or accounts with significantly low payments to balance need additional documentation to utilize an accurate payment for qualifying purposes if not utilizing the standard 5%.
 - ✓ Not identifying what are in fact mortgage accounts or verifying what properties they are attached to on the Schedule of REO on the 1003 or in the AUS findings.
 - ✓ Public records reflecting open judgments and satisfaction or payment on the HUD 1 not provided.
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Appraisal

Common Errors with the appraisal

- ✓ Current HVCC Compliance not provided.
 - ✓ Declining market conditions and 2 closed comps within 90 days are not provided.
 - ✓ Second appraisal not provided when required by the product.
 - ✓ Address isn't the same on the appraisal as reflected on the collateral and closing documents.
 - ✓ Government Case # not reflected on the document.
 - ✓ Refinance transaction where the appraisal reflects either a vacant property or a property listed in the previous 6 months, both which make the refinance ineligible for sale to MSI.
 - ✓ Allowing for an appraisal to be utilized that clearly indicates any condition less than fair.
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Common Errors, Continued

Appraisal, Continued

Fannie Mae Unacceptable Appraisal Practices (UAP)

MSI has provided below some examples of UAP; **discovery of UAP in a loan are grounds for a repurchase request by an investor:**

- ✓ **Neighborhood Description** – Parameters deliberately expanded to justify the use of superior market data as well as housing trends that conflict with available market data comparable to the subject.
- ✓ **Pending Sales Contract** – Not reporting a sales contract analysis for a purchase loan or not analyzing/disclosing significant sale concessions.
- ✓ **Property Condition** – Property conditions that significantly impact marketability or value are not disclosed/analyzed.
 - “AS IS” value concluded when subject property is not livable due to health, safety or structural soundness issues.
- ✓ **Declining Market Characteristics** – Not disclosing comparable data that clearly indicates a declining market.
 - Prior sales/listings of the subject property not disclosed that are either required or relevant due to declining market analysis as well as prior sales of comparable sales not disclosed for the same reasons.
- ✓ **Subject Sales/Listing history** – Not analyzing/reporting subject sales/listing history or not disclosing prior listing activity of the subject property that may indicate market resistance to the list price/overall lack of marketability.
- ✓ **Comparables** – All or majority of comparables presented are outside subject neighborhood when comparables within the neighborhood were available.
 - Location adjustments or lack of location adjustments when using comparables outside reasonable neighborhood boundaries are used without reasonable explanation or support.
- ✓ **Appraised Value** - Adjusted sales price is not within acceptable range or supported by the majority of comparables.
 - Over 20% higher than the reported predominant comparable sale prices.
 - Over 10% difference that the subject’s pending sales price.
- ✓ For more information on Fannie Mae’s Unacceptable Appraisal Practices, please visit <https://www.efanniemae.com/sf/guides/ssg/relatedsellinginfo/appcode/pdf/appraisalguidance.pdf>

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Common Errors, Continued

Owner Occupancy

Supporting Owner Occupancy

It is the Correspondent's obligation to provide any support documentation in the cases of questionable occupancy.

- ✓ Motivation letters, signed by the applicant(s) as to the occupancy of the subject property.
- ✓ Underwriter assessment of the subject property being an appropriate property and location being reasonable for owner occupancy due to commuting distance or family size.
- ✓ Documenting borrower's current property is listed through an MLS if the claim is the proposed or pending sale of the current, more superior residence.
- ✓ Reviewing the applicant's trend toward acquiring investment properties even through initial owner occupied presentation.
- ✓ Evidence of current occupancy with real estate tax exemptions claimed, mortgage interest deduction claimed, auto insurance address, utilities, etc.
- ✓ Occupancy of a significantly distressed property.
- ✓ Applicant that is a real estate or mortgage professional and an interested party to the transaction.
- ✓ Quick acquisition of properties and mortgages over a short duration of time.

HUD-1

A review of the HUD- 1 Settlement Statement, before loan disbursement, to ensure the data matches the AUS findings is also recommended.
