CMG FINANCIAL
Correspondent Lending

BULLETIN #2017-50

TO: Distribution

DATE: September 27, 2017

RE: CMG Financial Correspondent Lending Updates

EFFECTIVE: As noted below

CMG FINANCIAL CORRESPONDENT LENDING UPDATES

Topics Covered in this Announcement:

- Freddie Mac Conventional Conforming Updates- Rental Income
- Fannie Mae Disaster Related Limited Cash Out Refinance Flexibilities
- USDA FY2018- Lapse in Funding and "Subject to" Conditional Commitments

FREDDIE MAC CONVENTIONAL CONFORMING UPDATES- RENTAL INCOME

Summary: As previously announced in CMG Bulletin 2017-36 on August 23, 2017, Freddie Mac recently released selling guide bulletin 2017-12. This bulletin primarily addresses revisions to rental income requirements and guidance. The revisions include addressing evolving housing industry trends in the rental market such as short-term rental income and includes expanded requirements, additional specificity and guidance to support the determination of stability, reasonable expectation of continuance and calculation of rental income, resulting in continued support of purchase certainty. **In order to meet Freddie Mac's delivery requirements, December 29th will be the last day for CMG to purchase loans not meeting the revised requirements.** Updates are summarized below:

SHORT-TERM AND LONG-TERM RENTAL INCOME SOURCES: REFINANCE TRANSACTIONS FOR PROPERTIES OWNED IN THE PRIOR CALENDAR YEAR(S)

The changes below apply to refinance transactions when using rental income from properties owned in the prior calendar year(s) for:

- 2- to 4-unit Primary Residences
- 1- to 4-unit Investment Properties, and
- Non-subject investment properties

Short-term rental income sources:

- Added requirements and guidance to address the stability of rental income derived from short-term rental income sources (e.g., rental income from a source where a lease is not utilized) to support evolving housing industry trends in the rental market.rental income
- A two-year history of rental income from a short-term source is required.
- The income must be documented on Schedule E and the property must have been used for the purposes of producing rental income for this period of time.
- Short-term rental income is typically fluctuating so historical analysis of the associated degree of volatility and/or irregularity is necessary to determine income stability.

LONG-TERM RENTAL INCOME SOURCES

Updated requirements for traditional rental market income sources (e.g., rental income from a one year lease).

- A one-year term lease lends support to income stability and continuance, so a one-year history of rental income reported on Schedule E is acceptable.
- Lenders may determine that rental income is stable without obtaining a current lease when it is evident that the source of rental income is not short term based on the documentation provided.

INCOME FROM RENTAL PROPERTIES NOT OWNED IN THE PRIOR CALENDAR YEAR

For Borrowers who do not have a documented one-year history of investment property management experience, the lender may only consider net rental income in an amount up to 30% of the sum of the net rental income and all other stable monthly income that is used to qualify the Borrower.This change provides support to sustainable and successful homeownership by requiring a reasonable limitation upon the reliance on a newer type of income stream.

GUIDE FORM 1000 AND COMPARABLE RENT DATA

Freddie Mac is reintroducing Guide Form 1000, Comparable Rent Schedule, for all 1-unit subject Investment Properties and providing requirements for the analysis of comparable rent data in both Form 1000 and Form 72, Small Residential Income Property Appraisal Report. As a result, they are retiring Form 998, Operating Income Statement.

EXPANDED REQUIREMENTS, ADDITIONAL SPECIFICITY AND GUIDANCE

Additional revisions include, but are not limited to the following:

☐ **Accessory units**– Specifying rental income may be used for an accessory unit in a 1-unit subject Investment Property and non-subject investment property. Rental income requirements and subject property appraisal requirements must be met.

☐ **Leases** - Specifying that leases must be current and fully executed, with a minimum original term of one year (with an allowance for a month-to-month term if in the automatically renewable stage) for all transaction types.

☐ **Net rental income calculations**– Separating by documentation type (e.g., lease, comparable rent schedule, tax returns). Rental income calculation for subject 1- to 4- unit Investment Property and non-subject investment property is being revised to reflect calculation based on net rental income less the Mortgage payment rather than the net aggregate calculation. This calculation takes the monthly Mortgage principal payment into account. Adding Form 92, Net Rental Income Calculations – Schedule E, to the Guide for use when calculating the net rental income using Schedule E.

☐ **Establishment of debt payment-to-income ratio**– Separating requirements by occupancy and property type and specifying treatment of multiple non-subject investment properties.

☐ **Subject Investment Property** – Removing the requirement to verify operating expenses when rental income is not used to qualify.

☐ **Non-subject investment properties** – Specifying the property type may be non-residential.

☐ **Internal Revenue Service (IRS) Form 8825, Rental Real Estate Income and Expenses of a Partnership or an S Corporation**

- Adding a cross-reference to Chapter 5304 in Section 5306.1(e) for the treatment of all rental real estate income reported on IRS Form 8825, as announced in Bulletin 2016-19.
- Updating Sections 5306.1(e) and 5304.1(d) to specify that all rental real estate held in a partnership or S corporation is treated as self-employed income, regardless of the Borrower's ownership interest in the business.

Action to Take: Additional detail is available in the full Bulletin and its Attachment A.

Effective Date: The change may be implemented immediately. In order to meet Freddie Mac's delivery requirements, December 29th will be the last day for CMG to purchase loans not meeting the revised requirements.

Link: http://www.freddiemac.com/singlefamily/guide/bulletins/pdf/bll1712.pdf

FANNIE MAE POST DISASTER LIMITED CASHOUT REFINANCE FLEXIBILITIES

Summary: Fannie Mae provides flexibilities to standard limited cash-out refinance policies for borrowers who have been impacted by a natural disaster. These guidelines:

- permit the refinance of non-purchase money subordinate mortgage loans obtained to finance disaster-related property repairs, and ☐
- provide for a higher cash-out amount to reimburse borrowers for documented out-of-pocket expenses related to disaster-related property repairs.

This below topics outline the specific eligibility requirements for these additional flexibilities in accordance with the Fannie Mae selling guide.

LOCATION OF PROPERTY

- These flexibilities may be applied to mortgage loans on properties located in any counties, cities, or parishes that are designated by the Federal Emergency Management Agency (FEMA) as eligible for Individual Assistance as a result of a natural disaster (these areas are referred to as "FEMA Disaster Areas").

OCCUPANCY STATUS

- These guidelines are applicable only to mortgage loans secured by the borrower's principal residence, and may not be used in connection with second homes or investment properties.

TRANSACTION TYPES

A borrower may obtain:

- a limited cash-out refinance to consolidate non-purchase money subordinate financing used for repair of disaster-related property damage to his or her principal residence. To be eligible, the subordinate financing, including any draws on an existing HELOC, must post-date the disaster. However, the borrower may pay off the entire HELOC through the limited cash-out refinance, provided that a portion of the amount was used for disaster-related expenses to repair property damage to the principal residence.
- cash-out for reimbursement of documented out-of-pocket expenses for the completed repair of disaster-related property damage to his or her principal residence in an amount not to exceed the lesser of 10% of the balance of the new refinance mortgage loan or $15,000.
- All existing guidelines and requirements for limited cash-out refinance transactions continue to apply, including those for Texas 50(a)(6) mortgages.

DOCUMENTATION OF ELIGIBLE DISASTER-RELATED EXPENSES AND FINANCING

The lender must document that the subordinate financing (or a portion of the HELOC) or the entire requested cash-out amount represents funds used for completed disaster-related property repairs.

- Generally, documentation includes copies of receipts, work orders, canceled checks, etc., related to the cost of materials and labor.
- The borrower may not receive any reimbursement for amounts representing his or her sweat equity in connection with the repairs.

Note: All documentation must post-date the disaster and be directly related to completed repairs of damage to the property resulting from the disaster.

LIMITED CASH-OUT REFINANCE DU REQUIREMENTS

Certain messages on the DU Underwriting Findings Report will not apply to mortgage loans originated under the disaster-related limited cash-out refinance requirements.

When the mortgage loan complies with the requirements of this section, lenders may disregard the following messages:

- This case is ineligible because the amount of cash taken out of the subject property equity exceeds the limit of 2% of the loan amount or $2,000 for limited cash-out refinances.
- If any subordinate lien that was not used to acquire the subject property is to be paid off with first mortgage proceeds, the loan is ineligible as a limited cash-out refinance. The loan must be resubmitted as a cash-out refinance.
- If subordinate liens are being paid off with the first mortgage proceeds, obtain written documentation that the subordinate lien was used to acquire the subject property.

APPRAISAL REQUIREMENTS

- The appraisal for the property must follow standard requirements.
- Those guidelines allow an appraisal to be based on the "as is" condition of the property provided there are no conditions that affect the safety, soundness, or structural integrity of the property. If

those conditions do exist, the property must be appraised subject to completion of the specific alterations or repairs (“as repaired”) and a completion report must be obtained from the appraiser prior to closing.

POST DISASTER TIME PERIOD ELIGIBILITY & CMG FUND/PURCHASE BY DATE

All CMG loans must be purchased no later than 20 months from the date of the disaster declaration by FEMA in order for CMG to meet Fannie Mae delivery restrictions.

SPECIAL FEATURE CODES

- Mortgage loans delivered under these guideline flexibilities must include SFC 416.

Effective Date: These flexibilities are in placed based on eligibility noted above.

Fannie Mae Selling Guide Link: https://www.fanniemae.com/content/guide/selling/b5/4/02.html

USDA FISCAL YEAR 2018- LAPSE IN FUNDINGS AND "SUBJECT TO" CONDITIONAL COMMITMENTS

Summary: At the beginning of each fiscal year, funding for the guaranteed loan program is not available for a short period of time –approximately two weeks. USDA anticipates this brief lapse in funding to continue for FY 2018. FY 2018 will begin October 1, 2017 and ends at the close of business September 30, 2018.

For standard USDA products CMG will fund Rural Development loans for eligible applications that are issued “subject to the availability of commitment authority”. For any bond/HFA loans, HFA and master servicer must both permit the closing and purchase of USDA with “Subject to” conditional commitments. Requirements may vary and must be confirmed prior to closing.

Issuance of Conditional Commitments: During the temporary lapse in funding, Rural Development will issue Conditional Commitments (Form RD 3555-18/18E) “subject to the availability of commitment authority” for purchase and refinance transactions. The Rural Development application processing workflow is as follows:

- Rural Development will continue to accept complete guaranteed loan applications for purchase and refinance loan transactions from approved lenders;
- Rural Development will process, approve, and issue Conditional Commitments for those applications that are eligible “subject to the availability of commitment authority”;
- Lenders may close loans as scheduled;
- When funds become available, Rural Development will obligate (reserve) funds for Conditional Commitments that were issued for loans subject to the availability of commitment authority;
- Once loans are obligated, Rural Development may process lender’s Loan Note Guarantee requests when the loan closing is verified and all conditions of the Conditional Commitment are satisfied;
- Lenders assume all loss default risk for the loan until Rural Development is able to obligate the loan and issue the Loan Note Guarantee.

Please refer to the Unnumbered Letter: Conditional Commitments Issued during the Beginning of Fiscal Year 2018 for more information.

Fee Amounts for FY 2018: The upfront guarantee fee of 1.00 percent and an annual fee of .35 percent will apply to both purchase and refinance transactions for FY 2018.

Please contact your Correspondent National Sales Manager or your Correspondent Liaison with any questions.

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