PART IV – CREDIT GUIDELINES

SECTION 4000 – GENERAL

.01 INTRODUCTION

AHFC believes an underwriting program of high quality is an absolute necessity to accomplish its goal of stimulating the flow of funds to housing through the development and continuation of an effective secondary mortgage market. Thus, AHFC requires the Lender's qualified underwriter carefully evaluate the overall credit of the borrower and the property offered as security, and the Lender's underwriter and the Lender believe the mortgage is acceptable to private institutional investors. All information used to evaluate the credit worthiness of the borrower must be obtained before the date of the Note or applicable assumption agreement and must be supported by written documentation maintained by the Lender.

The following guidelines are used by AHFC in underwriting the borrower's ability to repay the mortgage debt. Credit underwriting guidelines must be applied consistently to each borrower regardless of race, color, religion, national origin, age, sex, marital status, familial status, or disability. All standards for determining stable monthly income must be applied in the same manner to each borrower.

The credit documentation should clearly demonstrate the borrower's ability and willingness to repay the loan and that the subject property is adequate collateral for securing the debt. Items such as adverse property conditions, limited liquidity or adverse credit conditions, such as previous foreclosures, deed-in-lieu of foreclosure, previous judgments, serious delinquencies, or other similar conditions, may constitute reason for less than maximum financing or possible declination. FHA/HUD loans must be underwritten according to FHA/HUD guidelines. However, it is essential to remember that both the borrower and property must meet all AHFC program requirements.

AHFC requires a full time employee of the Lender:

- Insure the application process is in conformance with FHA, HUD, VA and RD requirements, as applicable.
- Select an appraiser who must perform an inspection of the property.
- Order and receive the borrower's necessary credit documentation directly from the original sources.
- Make an underwriting determination of the entire credit and property package prior to recommending the mortgage to AHFC for purchase.

.02 AUTOMATED UNDERWRITING

All loans submitted to AHFC for commitment must have been submitted first to an automated underwriting system (AUS) as outlined below. The lender must use the most current version of the AUS. It is the lender's responsibility to ensure that the data entered into the automated system is accurate and that all supporting documentation is maintained in their loan file. The credit score, AUS identifier number and total debt ratios will be collected from the AUS feedback/findings submitted with the UND-3. A copy of the page of the feedback certificate/findings report that contains the results, credit score, and loan summary information for the loan must be included with all UND-3 submissions.

A. FNMA Desktop Underwriter (DU)

When the DU Findings Report reflects:

1. Approve/Eligible – The loan is acceptable to AHFC provided all the conditions of the findings report have been satisfied and the loan file has been documented according to the DU findings report. Lenders must meet all requirements outlined in the Verification Messages/Approval Conditions.

2. Approve/Ineligible – The loan is acceptable to AHFC provided the lender determines the criterion that makes the loan ineligible for FNMA does not also apply to AHFC.

3. All other findings – If the lender determines the mortgage is acceptable to AHFC, the loan must be manually underwritten and fully documented according to the criteria as set forth in Part IV of the AHFC Selling Guide. AHFC Form UND-1, Comprehensive Risk Assessment for Manual Underwriting loans must be completed for all manually underwritten loans and retained in the lender's file.

For loans approved using DU, the Lender must comply with all the requirements outlined in the most current FNMA Underwriter User's Guide and the Guide to Underwriting with Desktop Underwriter. The applicable warranties and waivers outlined in these guides will also apply to AHFC loans.

B. FHLMC Loan Prospector (LP)

When the LP Feedback Certificate reflects:

1. Accept/Eligible - The loan is acceptable to AHFC provided all the conditions of the findings report have been satisfied and the loan file has been documented according to the LP Feedback Certificate. Lenders must meet all requirements outlined in the Documentation Guidelines/Loan Processing Remarks of the FHLMC Feedback Certificate.

2. Accept/Ineligible - The loan is acceptable to AHFC provided the lender determines the criterion that makes the loan ineligible for FHLMC does not also apply to AHFC.

3. All other findings – If the lender determines the mortgage is acceptable to AHFC the loan must be manually underwritten and fully documented according to the criteria as set forth in Part IV of the AHFC Selling Guide. AHFC Form UND-1, Comprehensive Risk Assessment for Manual Underwriting must be completed for all manually underwritten loans and retained in the lender's file

For loans approved using LP, the lender must comply with all the requirements outlined in the most current Loan Prospector User Guide. The applicable warranties and waivers outlined in this guide will also apply to AHFC loans.

C. Rural Development Guaranteed Underwriting System (GUS)

When the GUS Underwriting Findings Report reflects:

Accept/Eligible - The loan is acceptable to AHFC provided all the conditions of the findings report have been satisfied and the loan file has been documented according to the GUS findings report. Lenders must meet all requirements outlined in the Lender's Required Conditions of the GUS Underwriting Findings Report.

D. Standard Criteria

The following applies regardless of AUS findings/feedback (includes Conventional, VA, RD, FHA, and HUD 184 loans)

1. All loans with credit scores below 620 will be ineligible for purchase.

2. All loans with a total debt ratio exceeding 50% will be ineligible for purchase.

3. Regardless of loan type, lenders must use standard documentation to verify employment and income on income-restricted loan programs such as TEP, IRRLIB and RELP, and on the Teachers' and Health Care Professionals' Housing Loan Program. (Refer to Section 4003.01)

4. Alaska Statute prohibits AHFC from purchasing any loan when the borrower has a past due child support obligation. Borrowers must pay child support arrearages prior to loan closing. There are no exceptions. (Refer to Section 4005.07)

5. Automated underwriting **may not** be used on Rural Non-Owner Occupied loans or Type II Manufactured Home loans.

.03 Manual Underwriting

Manually underwritten loans must meet the criteria as set forth in Part IV of this guide with documentation that supports the underwriting decision. When properly applied, AHFC's underwriting requirements and guidelines will result in an evaluation of the Borrower's overall creditworthiness rather than an evaluation that focuses on minor exceptions to specific policies. AHFC Form UND-1, Comprehensive Risk Assessment for Manual Underwriting must be completed and retained in the lenders loan file for all manually underwritten loan files.

AHFC will consider documented compensating factors when granting credit approval to borrowers, who for example, have debt-to-income or total obligation ratios that exceed AHFC guidelines. Valid compensating factors offset (in part) the loan’s weakness and should represent particular strengths rather than the satisfaction of program requirements. Compensating factors **may not** be used to compensate for unsatisfactory credit.

Compensating factors include, but are not limited to:

- Excellent credit history
- Conservative use of consumer credit
- Minimal consumer debt
- Long-term employment
- Significant liquid assets after closing
- Large down payment
- Low loan-to-value
- Low debt-to-income ratio
- Little or no increase in housing expense
- High residual income
- Previous satisfactory homeownership

SECTION 4001 – RATIO OF DEBT-TO-INCOME

.01 TOTAL PAYMENT RATIO

The total monthly first mortgage payment (PITI) and, when applicable, any secondary financing, Homeowner's Association charges, and space rent should not exceed the following, unless there are fully documented compensating factors that justify using a higher ratio:

Conventional Loans	28% of allowable gross income
VA Loans	41% of allowable gross income
RD Loans	29% of allowable gross income
AHELP & IRRLIB Loans	33% of allowable gross income
FHA and HUD Loans	31% of allowable gross income

.02 TOTAL OBLIGATION RATIO

The total monthly obligations should not exceed 36% of allowable gross income on all conventional loans and 41% on VA, RD, AHELP and IRRLIB loans, and 43% on FHA and HUD loans , unless there are fully documented compensating factors that justify using a higher ratio. Total monthly obligations are defined as the total monthly mortgage payment, and any other monthly installment (including deferred payments Section 4006.12), and revolving obligations that extend beyond ten months. If ratios exceed the guidelines lenders must provide a written explanation justifying the underwriting decision. Under no circumstances should a total obligation ratio exceed 45%.

When revolving accounts with outstanding balances do not have minimum required payments shown on the credit report, payments are calculated at the greatest of three percent (3%) of the outstanding balance or $10 per month. The recent payoff of revolving debt will warrant a more conservative approach to underwriting the total debt ratio.

The treatment of contingent liabilities is handled on a case-by-case basis. When a borrower has co-signed a loan to enable another person (the primary obligor) to obtain credit, the payment may be excluded from the long-term debt-to-income ratio provided it can be verified the primary obligor has had at least a 12-month history of documented payments with no delinquencies. If timely payments by the primary obligor cannot be verified, the contingent liability must be included in the borrower's total debt ratio calculation.

.03 ENERGY EFFICIENCY EVALUATION/UNDERWRITING

Higher income ratios may be allowed if the property is energy efficient. Lenders may qualify borrowers using increased payment and total obligation ratios by two percent (2%) for homes with a Home Energy Rating of 4★+ and by three percent (3%) for homes with a 5★ (or better) rating. A copy of the energy rating must be included in the submission.

SECTION 4002 – STABILITY OF INCOME

.01 GENERAL

Stable monthly income is the borrower's verified gross monthly income from all verifiable sources that can reasonably be expected to continue for at least the next three years. All sources of income will be considered; however, each source of income will be analyzed to determine whether it has the required stability. The borrower's application and supporting documents must clearly demonstrate stability of income.

A question of stability of employment and income arises from time to time for those borrowers employed by companies whose financial stability and/or future employment plans have been the subject of various media reports. This becomes even more critical if the media has disclosed information regarding financial problems, layoffs, etc. occurring with the employer. Such information obligates a lender to review the employment information more stringently and ascertain if there is sufficient stability of income and probability of continued employment. Research into the availability of similar employment elsewhere, education or experience in another field, or availability of additional sources of funds to offset a loss of income should be considered. Approval of a loan to a borrower that may be faced with a loss of income or a serious reduction in income which would have a negative impact on ability to make payments does not benefit the borrower, the lender or AHFC and should be prevented, if possible. There may be individual situations with strong compensating factors that would allow approval such as the amount and strength of the co-borrower's earnings, large cash reserves, etc. Each loan must be considered on a case-by-case basis.

In the case of joint title to the property, the effective income of each borrower should be computed separately, then added together to provide a sum for total effective income.

.02 TWO-YEAR EMPLOYMENT HISTORY

All employment for the preceding two-year period must be verified. Refer to Section 8000.02.B for the required documentation of employment and earnings history. All periods of unemployment during the two-year period must be explained. If a borrower was in school for all or part of the preceding two years supporting documents such as college transcripts must be obtained.

.03 NEWLY EMPLOYED MORTGAGORS

If a borrower is newly employed (generally less than six months) or has had several jobs within the past two years, the loan application must demonstrate other stabilizing factors. These factors may include stability of co-borrower's employment, substantial liquid assets after closing, low LTV, or low debt-to-income ratios, or other compensating factors as described in Section 4000.02.

.04 TAX RETURNS

The two most recent years complete, signed federal tax returns must be provided for all borrowers who derive 25% or more of their income from commissions, a per job contract basis, fees, investments, trust funds, or is employed by the seller, realtor, relative or a family business, or is self-employed. Income restrictive programs such as Tax-Exempt and the Interest Rate Reduction for Low Income Borrowers require the most recent three years tax returns.

For any loan that requires tax returns, the loan file must contain the borrower(s)' written permission to request copies of their returns directly from the Internal Revenue Service in a form that is acceptable to the IRS, e.g. Form 4506 (Request for Copy of Tax Form), Form 4506-T (Request Transcript of Tax Form), or Form 8821 (Tax Information Authorization). When the lender completes the form, the "recipient" of the tax documents should be the lender's name or the name of the Servicer if servicing will be transferred. The form should indicate the request is for documentation concerning the year or years for which the borrower's tax return was used in underwriting the loan, and the form should be dated no earlier than the date of loan closing. If AHFC selects the loan for a Quality Control Audit, the Lender may be required to exercise the authorization and forward the tax information.

SECTION 4003 – EFFECTIVE INCOME

Effective income is current verified income of the borrower(s) at the time of application to AHFC for loan commitment. Income is underwritten to determine whether the circumstances reasonably indicate the income, jointly or severally, will continue in a manner sufficient to repay the debt under the terms of the Note and mortgage.

.01 VERIFICATION OF EMPLOYMENT

A. Standard Documentation

Lender's may use a Request for Verification of Employment (VOE) (FNMA Form 1005 or equivalent), sent directly to the borrower's employer, to document income from wages. The VOE must cover the most recent two-year period and include year-to-date earnings. If the borrower has been employed for less than two years or has had breaks in employment the file must demonstrate other stabilizing factors.

Lenders **must** use standard documentation for income-restricted programs such as TEP, IRRLIB and RELP, and on the Teachers' and Health Care Professionals' Housing Loan Program.

B. Alternate Documentation

Lenders **may not** use alternate documentation if the borrower is self-employed, derives more than 25% of his/her income from commissions, or if the seller, realtor, or a relative employs the borrower. Lenders may verify income with:

1. Pay stubs or payroll earnings statements covering wages for the most recent 30-day period. The pay stubs or earnings statements must be computer generated or typed (not handwritten), clearly identify the borrower as the employee, show the time period covered and show both the current period and year-to-date earnings;

2. A copy of the borrower's W-2 forms from the most recent two years; or

3. Lender's Telephone Verification of Employment, Form PRG-20; or

4. Third-party employment verification provided directly to the lender, supplemented by the borrower or borrower's employer if the verification contains missing information.

   Note: Pay stubs or payroll earnings statements faxed to the lender or that the borrower downloads from the Internet are acceptable

only if the document clearly identifies the employer's name and source of information.

.02 AVERAGED INCOME

In those fields where income fluctuates from year to year and cannot be verified as a constant figure, the verification of year-to-date and the previous two years income is averaged. However, if the pattern of income is not stable or increasing, a conservative view must be taken when calculating effective income.

.03 SELF-EMPLOYED

A borrower who has 25% or more ownership interest in a business is considered self-employed. The business must be analyzed to confirm it will continue to generate the income the borrower needs to qualify for the requested loan and to determine it will not negatively impact the personal income and assets of the borrower. Corporate, partnership or "S" Corporation income is considered only if the borrower has the legal right to draw additional income from the Corporation and can provide evidence of access to funds.

If a borrower has been self-employed for less than two full years, financing is generally not available through AHFC. Special circumstances may warrant financing at a reduced loan-to-value.

Signed federal income tax returns including all applicable schedules (personal, corporate, and partnership, when applicable) for the most current two years, a current year-to-date profit and loss statement (if the loan application is dated more than 120 days after the end of the business tax year), and a balance sheet for the previous two years is required. A self-employed income analysis (FNMA Form 1084A, 1084B or similar form) is to be completed by the Lender and included in the loan file. Income is averaged from the most recent two years tax returns, provided the returns evidence stable or increasing income. The year-to-date profit and loss should evidence the business is continuing to be profitable at or above the same level shown on the tax returns. If current year income has decreased from income reported on tax returns, the income used to qualify the borrower will generally be based on the lowest earnings, representing a conservative underwriting approach. A continuing large decline in gross income over two or three years may warrant declination of the application even if the current income and debt ratios meet acceptable guidelines. Generally, the profit and loss statement should be completed by an independent accountant and not by the borrower, a family member, or an employee. However, in some rural areas where an accountant may not be available, the borrower may complete the profit and loss statement.

A. Non-Cash Items

1. Individual Tax Returns

Non-cash items such as depreciation, depletion, and amortization may be added back to adjusted gross income on Schedule C. Documented, non-recurring losses, such as casualty losses, can also be added back, as well as loss carryovers from previous tax years.

2. Corporate Tax Returns

Depreciation, depletion, amortization, documented non-recurring losses (such as casualty losses) and loss carryovers from previous tax years may be added back to the corporate income. However, mortgages, notes and bonds payable in less than one year must be deducted from income. (These figures can be found on corporation balance sheets).

3. "S" Corporation

Depreciation, depletion, amortization, documented non-recurring losses (such as casualty losses) and loss carryovers from previous tax years from the "S" Corporation's tax returns may be added back to the borrower's income (in proportion to the percentage of ownership). However, they must first be reduced by the borrowers proportionate share of the "S" Corporation's total obligations that are payable in less than one year.

4. Partnership

Depreciation, depletion, amortization, documented non-recurring losses (such as casualty losses) and loss carryovers from previous tax years from the partnership tax returns may be added back to the borrower's income (in proportion to the percentage of ownership). It is necessary, however, to first reduce this amount by the borrower's share of the partnership's total debts that are payable in less than one year.

B. Negative Earnings

Negative earnings from a business are treated as a loss to income, not as an additional debt.

C. Annual Payments

For those self-employed applicants who have large annual debt payments (such as fishermen with boat and/or permit payments), the effective gross income is derived by adding back the interest and subtracting the payment from the net profit/loss on the Schedule C of the tax returns. This obligation should be listed in brackets under the liability section of the application, showing the liability is acknowledged, but the amount is not used in calculating the debt ratios as it has already been considered in the income calculation.

.04 COMMISSION INCOME

As commission income may be subject to fluctuations from year to year, an average of the last two years' earnings should be used in evaluating the borrower's income qualifications. Commission income must be supported by signed federal income tax returns for the previous two years. Less than a two-year history of commission earnings is typically not acceptable unless there are **significant compensating factors.**

It is also important to establish an earnings trend for commission income. Annual earnings that are level or increasing from one year to the next are acceptable. However, if the earnings show a decline toward the current year, there must be strong offsetting factors for the commission income to be acceptable.

.05 RENTAL INCOME

A. Rental Income From Other Than Subject Property

Rental income must be verified by the most recent two years of tax returns, including Schedule E. The rental income is calculated from the borrower's tax returns by taking the net rental income/loss plus depreciation divided by 24 months. In some cases, the actual loss from rental properties may be larger than the loss the borrower is allowed to deduct for tax purposes. The actual loss, not the deductible loss, should be used in calculating loss. Any loss carryovers from previous years should be added to net income/loss. If the income has decreased in the most recent year, or if the losses have increased, a conservative underwriting approach should be taken. No more than 75% of the gross rental income less the payment is to be used unless the prior two years' tax returns clearly support the use of a higher percentage.

If the borrower did not own the property the previous year, copies of a signed lease are required. When determining rental income from lease agreements, AHFC will use the gross rental income multiplied by 75%, less the debt on the rental property.

Positive rental income is added as other income on the application and negative income is considered a debt and listed as a liability.

B. Rental Income From Subject Property

1. Owner Occupied Loans

Net rental income is calculated using 75% of gross rents, which is added as other income on the application (not subtracted from the proposed payment). Rental income should be documented by signed leases and supported by the appraisal.

2. Rural Non-Owner Occupied

The project must show a positive cash flow after debt service, allowance for operating expenses, and replacement reserves with a breakeven point of 85% or less when fully rented, and should generally have a minimum debt service coverage ratio of 1.15%.

The borrower should have remaining liquid assets after closing that would be used to supplement payments during vacancies (for at least six months) and to make regular and emergency repairs to the property as necessary.

.06 OVERTIME, BONUSES, AND OTHER EARNINGS

Income received for overtime work, bonuses, incentive plans, etc., may be included as effective income if it is established such earnings are characteristic of the employer, type of employment, and are of a continuing nature. If the history and the continuance of the income are established, AHFC will consider for qualifying purposes an average of the verified year-to-date and previous year's amount, or the current **guaranteed** overtime, bonus, etc., if an average is not applicable.

.07 SECOND JOBS

Income from a second job may be considered as effective income if the borrower has demonstrated a history of working a second job for at least two years in conjunction with other employment.

.08 CAR ALLOWANCE

A two-year history verified by tax returns and W-2 forms must be established for car allowance to be considered as effective income. The amount received in the past year and year-to-date must be provided. If the borrower has an auto liability that is paid from this allowance, AHFC will count the liability as a debt.

.09 CHILD SUPPORT OR ALIMONY

In instances where an applicant is relying on child support or alimony received as a portion of the monthly effective income, a copy of the divorce decree evidencing continuation for at least three years from the date of application must be provided. In addition, evidence the funds have been received in a timely manner for the last 12 months. Acceptable evidence includes canceled checks, court letter of payment, if paid through court system, or tax returns.

.10 DEFERRED INCOME

The amount of an employee's contribution into a deferred income plan is used in determining gross income. The VOE must show the amount of the employee's deferred income. The funds in the deferred account cannot be used as an asset available for down payment and closing costs, unless there is verification provided allowing use of these funds for purchase of a home.

.11 PERMANENT FUND DIVIDENDS

The State of Alaska Permanent Fund Dividend may be considered as effective income for qualifying purposes. An average of the most recent two years distribution is considered as effective income for payment ratio calculation, as well as calculating total annual income for specific income restrictive programs, such as Tax-Exempt, and IRRLIB.

.12 SOCIAL SECURITY

Income from Social Security benefits is considered as effective income providing the benefits are permanent, or if they contain a defined expiration date disclosing at least three years remaining at time of application. Acceptable verification is a photocopy of the Social Security Award Letter.

.13 RECEIVABLE INCOME

Income from seasoned receivables is considered as effective income if there has been a minimum 12-month history of timely receipt of payments and there is at least three years remaining on the contract. Documentation to verify this income should include a copy of the note disclosing the terms, verification of the current balance, and a 12-month payment profile.

.14 RETIREMENT INCOME

Retirement earnings must be documented to include completion of a standard verification of employment or an awards letter that clearly stipulates the duration and amount of benefits the borrower will receive.

For retired military borrowers, a copy of the DD-214 evidencing 20 or more years of active duty service and a copy of the most recent retirement check is sufficient documentation.

.15 INTEREST AND DIVIDEND INCOME

Interest and dividend income may be used if it is properly documented and has been received for the past two years and is anticipated to continue for at least the next three years. The Lender must develop an average of the income for the last two years to use in evaluating the borrower’s income qualifications. Photocopies of tax returns or account statements may be used to verify this income. Any funds used for down payment or closing costs must be subtracted before the interest is calculated.

.16 NON-TAXABLE INCOME

Verified non-taxable income that is likely to continue into the near future, such as certain military allowances, may be “grossed up” when calculating the debt-to-income ratios. Current income tax withholding tables should be used to determine an amount, which can be prudently employed to adjust or “gross up” the borrower’s actual income. The Lender must document and support its analysis for any case in which this special consideration is necessary in order to qualify the borrower.

.17 FOSTER CARE INCOME

Income from a state or locally sponsored organization for the temporary care of children may be considered as stable income provided the borrower has a two-year history of providing foster care services under a recognized program and is likely, in the foreseeable future, to continue to provide such services at a level that supports the amount of income needed for qualifying for the mortgage. The Lender must average the income for the last two years and verify whether the borrower has any extraordinary expenses (such as medical) because of caring for the foster child

.18 PUBLIC ASSISTANCE

Income from public assistance may be considered as acceptable stable income if it is properly documented, has been received for the past two years, and is expected to continue to be received for at least three years from the date of the mortgage application. Letters or exhibits from the paying agency that state the amount, frequency, and duration of the benefit payments should document public assistance income.

SECTION 4004 – AGE OF BORROWER

Generally, the age of borrowers is evaluated in accordance with the following guidelines:

A. Legal Majority

Borrowers must have attained legal majority as defined by Alaska Statutes (AS 25.20).

B. Favorable Consideration

All borrowers, regardless of age, are favorably considered when there are circumstances involving sufficient guaranteed income from cash assets, investments, continuing life insurance benefits, retirement benefits, etc. which reasonably assure an adequate ratio of debt-to-income.

SECTION 4005 – BORROWER'S CREDIT RATING

.01 ATTITUDE TOWARD OBLIGATIONS

The manner in which the borrower has paid his or her obligations is an important criterion in determining acceptability. The information furnished by the Lender and other creditors provides a basis for making this determination.

.02 CREDIT REPORT

AHFC will accept the use of automated "merged" credit reports that electronically combine information from "in file" credit reports from three different repositories into a single report, provided these reports are acceptable to insurers/guarantors. Such reports must be provided by a consumer-reporting agency that is not affiliated with the lender in any way. Some cases of reports showing numerous late or delinquent payments, bankruptcies, foreclosures, etc., may warrant a full Standard Factual Mortgage Credit report be ordered.

A legal records search (judgments, foreclosures, garnishments, bankruptcies, divorce actions) for seven years is required. The most current two years may be obtained from searching court records in each locality where the borrower lived or reported from accumulated and regularly filed records from qualified legal reporting services. The remaining five years may be obtained from a consumer-reporting agency. All credit reports for conventional and VA loans must disclose at least two specific sources of public records information used for that report.

AHFC will not require a Credit Report legal search in foreign countries or APO/FPO addresses. However, if the borrowers maintained a "home" address in the United States while stationed or living out of the country, this "home" address should be listed for the credit agency's research.

A. Credit Score

Although a credit score cannot predict which borrowers will default, or what percentage of borrowers, a higher credit score is indicative of a lower default risk and a lower credit score is indicative of a greater risk of default. Underwriters can use credit scores as a measurement of risk in analyzing the borrower's creditworthiness.

On all loans, AHFC requires a minimum "representative" credit score of 620. For underwriting and evaluating the mortgage the Lender must obtain at least two credit scores for every borrower. The "representative" credit score is the lower of two credit scores, or the middle score of three. In the case of multiple borrowers, the borrower with the lowest score or lowest middle score is used to determine the "representative" credit score.

Credit scores below 660 warrant careful consideration of whether the derogatory contributing factors were the result of circumstances beyond the borrower's control (such as prolonged illness or loss of employment) and not the result of poor financial management. The Lender must obtain a written explanation from the borrower along with supporting documentation.

If no credit score is available because of a lack of trade items, an alternative credit history is permitted. A satisfactory Verification of Rent (VOR) covering the previous year and a minimum of three other sources each with a 12 month record of satisfactory payment is required. However, if the credit score is zero or unavailable due to recent inactivity, lenders must evaluate prior derogatory credit as outlined in Section 4005.03 (C) below.

Note: AHFC will call for a post purchase audit on all manually underwritten loan files where no credit score is available or the credit score is below 660.

B. Inquiries

The lender must determine whether additional credit was granted because of any inquiries made within the last 90 days. Written verification from the creditor should be obtained to establish whether additional credit was granted. If such verification is unobtainable, a signed statement from the borrower addressing the reason for the inquiry must be provided.

C. Rental Payment History

If the rental payment history is not listed on the credit report as verified by the landlord, a separate credit letter from the landlord is required. If it is not possible to obtain a credit letter, a memo stating the reasons should be retained along with copies of canceled checks and a copy of the rental agreement. If the borrowers paid rent in cash, copies of bank statements showing withdrawals each month may be used.

D. Mortgage Loans

The Lender must verify all previous mortgages within the last seven years and all current mortgages. The following documentation is acceptable.

1. Direct written verification from the mortgagee.

2. Reference contained in the credit report (covering at least 12 months activity).

3. Mortgage payment history (must be computer generated and show all pertinent mortgage data).

4. If items 1 through 3 above cannot be obtained, canceled checks may be provided to cover the most recent 12-month period (both sides of check must be provided and must be legible).

It is recognized some firms will not or cannot provide verification of older, paid mortgages. If verification cannot be obtained, an explanation addressing the reason should be provided in the loan file. If the mortgage has been paid off for over two years and the credit report states “unable to verify,” no further verification or explanation is needed.

An explanation must be obtained from the borrower for any delinquent mortgage payments made within the last two years or any other derogatory credit, if applicable.

.03 ANALYZING THE BORROWER’S CREDIT

A. Lack of Credit History

A credit history for borrowers who normally do not use credit or do not have the type of credit history that will appear on a credit report can be established by verification of current and previous rent history, utility payments, telephone bills or from other sources of credit for which the borrower has (or had) a regular financial obligation. In addition to a satisfactory Verification of Rent (VOR) covering the previous year, a minimum of three other sources each with a 12-month record of satisfactory payment is required.

B. Manner of payment

AHFC does not look for the isolated case of unsatisfactory or slow payment of an account, but for the general pattern of payment. The credit report and credit letters must clearly establish a proper regard for contractual obligations.

C. Delinquent Accounts

1. The Lender must obtain an explanation from the borrower for adverse credit ratings, including mortgage payments made consistently after the 15th of the month. Generally, a written explanation for a minor, isolated instance of poor credit or a late payment is not required.

2. Reports of foreclosure, numerous slow payments, collections, court suits, or other adverse ratings may disqualify the borrower from further consideration unless valid and verified reasons can be established to minimize the probability of reoccurrence. Where it can be established that any adverse rating was caused by circumstances beyond the borrower’s control (such as prolonged

family illness or loss of employment) and the borrower has re-established his credit, favorable consideration may be given to receive loan approval. (See Section 4005.10) However, it is not realistic to expect the re-establishment of credit can be accomplished in less than one year.

3. AHFC will not require collection accounts to be paid off at or prior to loan closing if an individual account balance is less than $250, or if the total of all such accounts is $1,000 or less. Any collection account with balances above $250 and all judgments, garnishments, liens, and child support arrearages (See .07 below) must be paid at or prior to loan closing.

.04 PREVIOUS FORECLOSURES AND DEEDS-IN-LIEU OF FORECLOSURE

Report of previous foreclosures or deeds-in-lieu within the preceding five years will typically warrant declination of the loan request unless valid and verifiable reasons can demonstrate it was beyond the borrower’s control (such as prolonged family illness or loss of employment) and the probability of a reoccurrence is unlikely.

.05 PRESALES (SHORT SALES)

If a borrower had a previous mortgage loan that required a presale agreement to sell the property, a detailed explanation from the borrower must be obtained. The reason for the presale must establish that the circumstances were beyond the borrower’s control and the likelihood of reoccurrence is minimal. A mortgage history profile for at least the 12 months prior to the presale is required. If a repayment plan is in effect to reimburse the mortgage insurer to cover the losses paid on the borrower’s behalf, a payment profile must be included in the loan package showing all payments have been made in an acceptable manner (minimum 12-month history is required). Any debt still existing requiring repayment is included in the borrower’s total obligation ratio.

.06 BANKRUPTCY

A bankruptcy must be fully discharged and the borrower must re-establish good credit and demonstrate his or her ability to manage financial affairs. A five-year period should have elapsed between the discharge of the bankruptcy and application date for the loan. A shorter period may be considered if the bankruptcy was the result of circumstances beyond the borrower’s control (such as prolonged family illness or loss of employment) and would receive more favorable consideration than one that occurred because of poor financial management. The Lender must obtain a written explanation from the borrower along with copies of the bankruptcy petition, schedule of debts, and discharge.

.07 ARREARS ON CHILD SUPPORT PAYMENTS

(Form UND-22)

AS 18.56.096 (a) prohibits AHFC from the purchase of a mortgage loan to a person who has a past due child support obligation. The Lender must verify no individuals applying for an AHFC loan are in arrears on their child support obligations by sending the Child Support Verification (Form UND-22) to the Child Support Enforcement Agency. If an arrearage exists, the borrower is ineligible for an AHFC loan unless the arrearage is paid in full prior to closing. This applies to all child support arrearages, regardless of the state in which the arrearage has been declared or whether payments are being collected.

.08 NON-SUFFICIENT FUNDS CHECKS

Evidence of NSF checks in the file should be treated as any other adverse credit and a full explanation should be obtained.

.09 RE-ESTABLISHED CREDIT

Regardless of the reason for prior poor credit, an applicant's re-established credit history must reveal a payment record that illustrates the borrower now has the willingness and ability to manage his or her finances over time. The time required for re-established credit may vary depending on the severity and the cause, but in most cases a minimum of at least one year is required. Some individuals may attempt to avoid a recurrence of their credit problems by not re-establishing the types of credit accounts that led to their previous difficulties. Complete avoidance of traditional credit sources does not demonstrate the applicant has acquired successful credit management skills. AHFC requires at least one of the accounts under the re-established credit be from a traditional source of credit, (such as a fixed payment installment account). In no instance will credit from a non-traditional source be considered to offset delinquencies for traditional credit accounts.

.10 CONSUMER CREDIT COUNSELING

When applicants have used the services of a consumer credit counseling agency, such an arrangement entered into prior to any delinquency will not be considered as negative. However, the loan file must contain evidence the payment plan was successfully completed. If the applicant's credit was already damaged prior to entering into a credit counseling agreement, in addition to evidence of successful completion of the plan, the loan file must demonstrate a minimum of one year with no derogatory credit since completion of the plan.

.11 DEFERRED PAYMENTS

Payments on installment debts such as student loans that are in deferment must be included in the borrowers monthly obligations. If the deferred payments are not shown on the borrower's credit report, the lender must obtain a copy of the payment letter or agreement in order to determine the payment amount.

SECTION 4006 – DOCUMENTATION OF REQUIRED FUNDS

The documentation must clearly establish the borrower has sufficient liquid funds without resorting to unsecured borrowed funds for the required down payment and all additional costs incidental to closing. The source of any funds needed to close the transaction, or funds considered as an offsetting factor, should be clearly established. If the required funds are held in a recently opened (within 180 days) account, the source of funds in the new account is to be documented.

.01 MINIMUM DOWN PAYMENT

The borrower must invest a minimum down payment of five percent (5%) into the transaction from his/her own cash assets on all conventional loans. This must be established and verified prior to and in addition to the receipt of any gift funds used in the transaction. The minimum down payment requirement is waived when gift funds and any down payment, is equal to or greater than 20% of value (the lesser of the sales price or appraised value). Gift funds that meet the requirements outlined in Section .06 below may be used for the balance of the required down payment, closing costs, and prepaid items on conventional loans. For FHA, HUD, VA, and RD loans follow the applicable insurer/guarantor requirements.

Note: A portion of the minimum five percent (5%) may come from certain preapproved down payment assistance grant programs. The provider of the grant must be a governmental entity or other entity in the business of increasing home ownership. **Assistance from the seller of the subject property either directly or indirectly is prohibited.** All grant funds and any matching contribution by the borrower must be applied to the transaction as down payment and closing costs, with no funds retained by the borrower for personal use.

On Type II Manufactured Home Loans see Section 5007.

.02 CASH RESERVES

The borrower must have a minimum of two months payments in cash reserves on a single-family residence (not required on Type II manufactured home loans). This requirement is waived when the down payment is 20% or more and has come from the borrower’s own unencumbered assets. For duplex, triplex or fourplex loans and Rural Non-Owner Occupied Loans, the borrower must have remaining liquid assets after closing months (6 months PITI) that could be used to supplement payments during vacancies and to make regular and emergency repairs to the property as necessary. Gift funds are acceptable for these reserves. Certain retirement accounts, adjusted for any early withdrawal penalties, are also acceptable for these reserves.

.03 DEFINITION OF CASH

A. Acceptable

The following sources of cash are acceptable for use as down payment and closing costs:

1. Verified funds on deposit in the borrower's checking, savings, or investment accounts;
2. A gift as outlined in Section 4006.06;
3. Proceeds of a loan fully secured by the borrower's owned assets; or
4. A cash deposit toward the purchase, the source of which is verifiable.

B. Not Acceptable

The following sources of cash are **NOT** acceptable:

1. Proceeds of a personal or unsecured loan;
2. A gift that must be repaid in full or in part;
3. A cash advance on a revolving charge account or unsecured line of credit; or
4. Cash for which the source cannot be verified.

.04 FUNDS ON DEPOSIT

If the required funds are being held in a deposit account, the verification of deposit must indicate the average balance. In lieu of the standard verification of deposit, bank statements, showing the previous three months balances may be provided. The statements must be computer generated or typed, identify the issuing institution, identify the account owner(s), identify the account number, show all transactions on the account, show the period covered, and ending balance or cash value. Documentation of excess liquid assets is not required, with the following exceptions.

- The funds are being considered as an offsetting factor.
- The source of funds is suspect and could represent a corresponding debt.

.05 SALE OF ASSETS

If the required funds are proceeds from the sale of personal property, the value may be established with a blue book listing, an appraisal, or a letter of opinion by an individual in the business of determining value of the item. Settlement statements or evidence of sale must identify the asset, identify the borrower as the seller of the asset, show the net proceeds to the seller, show the disposition of all liens against the asset, and be signed by the buyer and seller, or their authorized agents.

.06 GIFT FUNDS

Gifts (or grants) are acceptable from a relative, domestic partner, fiancée, a church, municipality, state or federal agency, non-profit organization or Alaska Regional Native Association. Contributions from the seller of the subject property, either directly or indirectly is prohibited. There may not be any conditions placed upon the gift and no repayment must be expected. (Refer to Minimum Down Payment section above).

A. Gift Letter Information

The gift letter must be signed by the donor and contain the following information.

1. The dollar amount of gift and date the funds are being transferred.
2. The donor’s name, address, telephone number and relationship to the borrower.
3. A statement that no repayment is expected.

B. Verification

Written evidence of the transfer of the gift funds from the donor to the borrower must be provided. If funds are not transferred prior to closing, a copy of a certified check for the gift from the donor must be provided.

A gift (or grant) from a church, municipality, non-profit organization, etc. must be evidenced by either a copy of the letter awarding the gift or grant to the borrower or a copy of the legal agreement that specifies the terms and conditions of the gift or grant. This supporting document must include language indicating that no repayment of the gift or grant is expected and an indication of how the funds will be transferred (to the borrower, the lender or the closing agent). The lender must include in the individual mortgage file evidence of the transfer of the funds—such as a copy of the donor’s canceled check or a settlement statement showing receipt of the check.

Refer to the Manufactured Home Program Section 5007.05.D for gift fund guidelines on Type II manufactured home loans.

.07 EARNEST MONEY DEPOSITS

Earnest money deposits in excess of two percent (2%) of the sales price must be substantiated by a copy of the canceled check or copy of a bank statement evidencing that the funds have cleared. If the documentation cannot be provided, the amount of the earnest money may be deducted from the sales price to determine the LTVR.

.08 RENT CREDIT

Rent credit (the difference between rent paid and market rent) is an acceptable source of funds for use as down payment and closing costs provided the following criteria is met.

- Rent payments were made under a documented rental purchase agreement that had a minimum original term of at least twelve months.
- The market rent must be determined by an appraiser, property manager, or other acceptable independent source.
- The allowable rent credit cannot exceed the difference between the market rent and actual rent paid.
- Evidence of rent paid must be documented and a copy of the rental agreement is to be provided.

.09 EXCHANGE OF ASSETS-TRADES

The minimum down payment and closing costs must be from the borrower's own cash assets. Additional down payment may be in the form of trade equity. When the transaction involves an exchange of assets other than cash (i.e., equity in other real estate, vehicles, stocks, gold, etc.) such assets may be considered as the equivalent of additional cash investment to the extent of the stated consideration or the market price, whichever is less. The equity is determined by subtracting the outstanding balance on the asset being traded, and any transfer costs, from the lesser of appraised value or trade-in value agreed to by both parties. The seller must provide proof of title transfer and satisfaction of any existing mortgage liens for which the borrower had been liable. The transfer deed must be recorded.

AHFC will require an appraisal (by a disinterested qualified third party) of the asset being traded be provided.

A. Residence

If the asset being traded is a residence, a full residential appraisal report is required. When warranted (such as is the case in rural areas of the State), an acceptable broker's opinion of value or other reliable independent source may be provided in lieu of a full appraisal report.

B. Land

A letter of opinion with comparables must be provided from an appraiser. When warranted (such as is the case in rural areas of the State), an assessor's value or other acceptable valuation may be provided.

C. Escrow

An appraisal from an independent source in the business of buying escrows is required.

D. Services

If the borrower is providing services and/or labor (not on the subject property), the application must evidence the borrower's ability to perform the work and provide at least two outside bids.

E. Personal Property

An appraisal or letter of opinion by an individual in the business of determining the value of the item is required.

On transactions involving the sale or trade of real estate, a short title search or preliminary title report is required to show who is in title to the property and any outstanding liens on the property.

.10 BORROWER EQUITY

The minimum down payment and closing costs must be from the borrower's own assets. However, labor actually to be performed or materials to be furnished by the borrower on the subject property may be considered as the equivalent of additional cash investment. The sales agreement must state the amount of credit being given to the buyer.

A. Sweat Equity

1. The application must evidence that the borrower has the ability to perform the work and that it can be accomplished satisfactorily within a reasonable period. It is not reasonable to expect that a borrower who has regular full time employment can complete a

substantial amount of work in a short time. The appraiser must certify completion of the work in a skillful, competent manner.

2. Two outside bids from an individual/company in the business of performing the same type of work that the borrower will be completing must be provided.

3. AHFC considers services that are normally performed by a new homeowner; i.e., cleaning the windows, yard and house, planting grass, etc., to have no real value.

Note: Sweat Equity is not allowed as a cost on owner/builder transactions. State statutes prohibit the use of credit for the borrower's labor (sweat equity) on Rural Program loans.

B. Materials

Materials furnished by the borrower on the subject property may be considered an acceptable cash investment. Documentation must be provided to verify that the funds are from the borrower's own assets, the materials have been delivered to and made part of the subject property, and the purchase of the materials has occurred within the last 12 months from date of application.

.11 BRIDGE LOANS

Bridge (or swing) loans are collateralized by the borrower's present home, which is usually for sale. By using funds from a bridge loan, the borrower can close on a new house before selling his or her existing house

A. Payments

The purchaser has the ability to carry the payment on the new home, the payment on other obligations, the payment on the current home, and the payment on the bridge loan. If the bridge loan's repayment schedule is not monthly, it must be converted to a monthly amount for qualifying purposes.

B. Security

The bridge loan is not cross-collateralized against the new property.

.12 REAL ESTATE COMMISSION

When the purchaser of the property is a real estate agent, the applicant's share of the commission is **not** acceptable as part of the down payment, closing costs or prepaid items. The application must clearly evidence that the borrower has sufficient cash to close, exclusive of the amount of the real estate commission.