

# PFI Advisory

January 27, 2006

## Special Attention:

PFI's MPF Program Management, PFI's Origination Management, PFI's Servicing Management

## Subject: Guidance on Underwriting for Hurricane Katrina

In an effort to provide assistance to those borrowers affected by Hurricane Katrina, the MPF Program is offering temporary underwriting flexibility for borrower's credit reputation and capacity, revised collateral underwriting requirements, and guidance for appraisal valuation of properties in affected areas. This underwriting flexibility is a supplement to, not a replacement of, the MPF Program guidelines. The underwriting guidelines outlined in this PFI Advisory are extended to borrowers with mortgages secured by properties located in Major Disaster Areas ('Disaster Areas'), defined as those counties, municipalities or parishes, that have been declared by the President of the United States to be Major Disaster Areas as a result of Hurricane Katrina where federal aid in the form of individual assistance is being made available. These areas are named by the Federal Emergency Management Agency (FEMA) on its web site at [www.fema.gov](http://www.fema.gov). **The underwriting guidelines outlined in this PFI Advisory apply only to mortgages with note dates on or after August 30, 2005 through December 31, 2006.** To be eligible for these guidelines, a mortgage must meet the following criteria:

1. The property type must be:
  - The borrower's existing primary residence located in a Disaster Area;
  - A new primary residence for relocated borrowers whose previous primary residence was located in a Disaster Area; or
  - A temporary primary residence defined as a borrower indicating that the home is being purchased with the intent to move back to the previous home located in a Disaster Area once damages are repaired. These temporary primary residences must be underwritten as second homes and delivered under the MPF Program as second homes.
2. The loan purpose must be a purchase or a no cash-out refinance. For all purchase transactions, the PFI must represent and warrant that, as of the MPF funding date, there are no outstanding insurance claims on the mortgaged property, including flood insurance claims, as applicable.

### Qualifying Ratios

When a borrower is purchasing a new primary residence and has an outstanding mortgage obligation on a previous primary residence located in a Disaster Area, any mortgage obligation on that previous primary residence` can be excluded from the qualifying ratio (total debt ratio) calculation provided that:

- The borrower intends to inhabit the new property as a new primary residence instead of as a temporary primary residence as defined above under eligible property types;
- The property is uninhabitable due to heavy damage, or was completely destroyed or condemned as documented by an originator obtained property inspection; and
- Information is provided to the originator indicating that the borrower is working with the servicer to address the mortgage obligation and the servicer's documentation indicates that the borrower has agreed any property insurance proceeds will be applied directly to the mortgage on the damaged home. **All documentation acquired by the servicer should be maintained in the mortgage file.**

### **Credit History**

Due to hardships caused by Hurricane Katrina, many borrowers' credit will be negatively affected due to expenses incurred and / or possible income reduction due to job loss. It is therefore beneficial to analyze a borrower's credit history by considering credit performance both before and after the disaster occurred. Accordingly, the MPF Program is offering flexibility in analyzing an affected borrower's credit history. If a mortgage has received an "Approve / Eligible" from Desktop Underwriter<sup>®</sup> or an "Accept and Eligible to Purchase" from Loan Prospector<sup>®</sup> it is considered acceptable according to the requirements of Underwriting Guide Chapter 2.17. If a loan is manually underwritten, a borrower's credit history containing adverse or derogatory information is acceptable providing the following criteria is met:

- The underwriter and the borrower both provide explanations detailing that any derogatory information is directly attributed to Hurricane Katrina and not representative of the borrower's customary credit performance. Both the underwriter's assessment on the Uniform Underwriting and Transmittal Summary (FNMA Form 1008 / FHLMC Form 1077) and the borrower's letter of explanation detailing this information should be maintained in the mortgage file;
- The credit report and other credit documentation contained in the file indicates that the Borrower's credit is current;
- Bankruptcy, foreclosure or a deed-in-lieu within the most recent 24 months will **not** be considered acceptable, making the mortgage ineligible for delivery under the MPF Program; and
- The borrower's mortgage or rent payment history for the most recent 12 months immediately prior to, and the period after, Hurricane Katrina shows no late payments that are not directly attributed to Hurricane Katrina. In the event that the borrower's rental or mortgage payment history was not reported to the credit repositories, the mortgage file contains other documentation showing that the borrower's mortgage or rent payment history for the most recent 12 months immediately prior to, and the period after, Hurricane Katrina shows no late payments that are not directly attributed to Hurricane Katrina.

### **Income**

As many borrowers' employers that were located in areas affected by Hurricane Katrina are facing difficulty in producing income documentation and verifying current employment, the MPF Program is offering relief both in the use of alternative forms of verification and the acceptance of alternative sources of income. Originators can utilize current employment and future employment to qualify

borrowers by using the alternative verification sources listed below. Only income that the borrower is either currently receiving or is under contract to receive can be used as qualifying income. Gaps in income directly attributed to Hurricane Katrina can be disregarded. Self-employed borrowers whose business is not currently in operation may not use forecasted income from that business to qualify. Also, a borrower is not to be qualified with income from temporary employment benefits, severance pay or contract funds received from federal and local governments or FEMA, as these are not on-going and are often received in one lump sum.

- **Previous employment:** If the business is currently in operation, income may be verified with a verbal verification of employment (VVOE). If the originator confirms that the business is not currently in operation, the income and business information must be stated on the mortgage application. The information provided on the mortgage application for previous employment is acceptable as income verification if it appears reasonable to the originator.
- **Present employment:** A verbal or written verification of the borrower's start date, previous year's income, year-to-date earnings and current salary along with a post-Hurricane Katrina pay stub are sufficient for income verification. In the case of a self-employed borrower who has lost all tax documentation, the originator must obtain tax information directly from the IRS, using IRS Forms 4506 or 4506-T.
- **Future employment:** An executed permanent employment contract may be used both to arrive at the salaried amount for qualifying purposes and to provide verification for the employment source.

## Assets

As many borrowers are having difficulty documenting asset accounts in cases where asset verification information was destroyed by Hurricane Katrina, affected borrowers can document these existing asset accounts with a Verification of Deposit (VOD) form or reissued bank statements. Accounts established after Hurricane Katrina must be documented according to the requirements of Underwriting Guide Chapter 4. To purchase a new property, borrowers may use Hurricane Katrina relief funds received from the following sources for the down payment and closing costs:

- Federal, state and local governments;
- FEMA; and
- Gift funds

Insurance proceeds may only be used in whole or in part toward the down payment or closing costs on a new mortgaged property either when excess proceeds remain after paying off unpaid principal balance of the mortgaged property affected or when the insurance proceeds received are for a property which the borrower owned free and clear.

## Appraisals

### Property Appraisals in Disaster Areas

Property location is a vital component in determining market value. When appraising properties located in Disaster Areas, appraisers must continue to consider neighborhood characteristics when

determining value and marketability. In accurately assessing value on a property in a Disaster Area, appraisers must use post-Hurricane Katrina comparable sales to support the value opinion. We realize that for some areas, there may be limited post-Hurricane Katrina comparable sales available; therefore, the appraiser may need to utilize pre-Hurricane Katrina comparable sales to supplement the post-Hurricane Katrina comparables provided. If the appraiser cannot arrive at an accurate assessment of market value as derived through analysis of both the property and neighborhood characteristics, the mortgage will not be eligible for delivery under the MPF Program.

### Short-Term Appreciation

Some areas are experiencing marked short-term appreciation resulting directly from shifts in market supply and demand following Hurricane Katrina. The MPF Program will accept mortgages secured by properties in areas which are experiencing this appreciation. However, the appraiser's adjustments to the comparable sales must be representative of the market and documented in the appraisal. If the appraiser is unable to support the subject property value with available comparables, the mortgage will not be eligible for delivery under the MPF Program.

### 'As-Is' Versus 'As-Repaired' Appraisals

Properties located in areas affected by Hurricane Katrina must be appraised based on exterior and interior inspections. If no conditions exist that affect the habitability or structural integrity of the property, the appraisal can be based on the 'as-is' condition of the property. Appraisers are not required to be qualified in the field of assessing environmental hazards. However, the appraiser is expected to report any adverse conditions found during the appraisal report process. Additionally, if the appraiser believes he / she has found any condition concerning the subject property to be hazardous, but does not feel qualified to make a determination, the appraiser is required to appraise the property subject to an inspection by a qualified professional. If conditions exist that the appraiser determines do affect the habitability or structural integrity of the property, the property must be appraised subject to completion of certain alterations or repairs ('as repaired'). The appraiser must clearly estimate the cost of repairs in the appraisal report, and the originator must obtain a completion report from the appraiser indicating that all repairs have been completed prior the mortgage being delivered under the MPF Program. In the event that such repairs cannot be completed prior to the mortgage's delivery, an escrow for completion can be established according to the provisions of Underwriting Guide Chapter 2.8.

### Appraisals with Supplemental Statements or Limiting Conditions

Natural Disasters such as Hurricane Katrina at times have had seemingly undeterminable effects on the stability of market value in affected areas, compelling appraisers to add additional limiting conditions to their appraisals. If the appraiser cannot arrive at an accurate assessment of market value as derived from thorough analysis of property and neighborhood characteristics, the mortgage will not be eligible for delivery under the MPF Program. Be advised that the MPF Program will not recognize limiting conditions beyond those which are standard to industry appraisal forms.

### Flood Damage and Repairs

For mortgages where the mortgaged property is located in a Disaster Area and the insurable improvements were damaged by floodwater, the loan is still eligible for delivery subject to the PFI

representing and warranting that the property is no longer flooded and that all damage (inclusive of mold damage) to the property resulting from floodwater has been repaired. If the mortgaged property is located in a Special Flood Hazard Area (SFHA), flood insurance must be maintained as required by Origination Guide Chapters 15.3, 15.9 and 27.9. If the mortgaged property is located in an SFHA and does not contain the proper flood insurance, it will not be eligible for delivery under the MPF Program.

### **MPF Data Elements**

#### Documentation Type

PFI's must deliver the Documentation Type code that represents the level of income and employment documentation used to qualify the borrower(s) based upon the time period covered by the documentation. The Documentation Type used should reflect the lowest level of income and employment documentation obtained for any borrower. (See the Instructions for Completing the Credit Enhancement Request Form (Form OG3)).

#### Special Feature Code

For Quality Assurance review purposes, PFI's should deliver Special Feature Code 300 for every loan delivered under the MPF Program using the provisions of this PFI Advisory.

**If you have any general questions about the information above, please contact your MPF Bank Representative or call the MPF Customer Support Desk at 877-INFO-MPF (877-463-6673).**