

# Underwriting Guidelines

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Earned Income Program's (EIPs), such as Buyers Account®, allow homebuyers to earn income that may be used towards a down payment on a home, closing costs, paying down debt, increasing cash reserves, etc.

Per the regulations set forth in the Fannie Mae Seller Guide for Single Family, the Freddie Mac Single Family Guide, and The HUD 4155.1 Handbook (revised), an EIP program such as Buyers Account®, meets the criteria for verifiable down payment funds as described below.

Specifically, the funds received through the program are **Earned Income** and are placed in a depository account prior to the settlement date. These funds are verified through the depository via a Letter of Account Verification or Request for Verification of Deposit - Form 1006 (VOD).

An EIP program is not a “non-profit gift program” and is not subject to the IRS Ruling 2006-27. The Buyers Account® may be used on any conventional, FHA, or sub-prime loan that allows income to be used toward the down payment.

#### **So why can “earned income” be used towards the down payment?**

Simply put, earned income is deposited in the purchaser's account, prior to settlement, and is verified in writing by the depository institution. Fannie Mae and Freddie Mac underwriting and purchasing guidelines allow these funds to be used towards down payment, closing costs, or cash reserves.

Buyers Account® is an Earned Income Program (EIP) that meets the guidelines for agency-eligible loans. Furthermore, Buyers Account® complies with all Federal and State regulations including the Real Estate Settlement Procedures Act (RESPA).

## **Fannie Mae Seller Guide Excerpt**

### **X, Chapter 6: Assets and Funds for Closing (07/03/00)**

The lender must verify that the borrower has sufficient cash deposits and other assets to complete the mortgage transaction, and also must confirm the level of reserves the borrower will have after closing. Generally, the borrower must have enough assets to cover the minimum required down payment that must come from his or her own funds (as discussed in Part VII, Section 104.07).

However, funds received from other acceptable sources may be used to supplement the minimum down payment from the borrower's funds, to pay the borrower's share of the closing costs and prepaid items that have to be paid by the property purchaser, and to satisfy any financial reserve requirement.

### **VII, 104.07: Minimum Down Payment (06/30/02)**

Generally, we require the borrower to use his or her savings or other liquid assets to make a minimum cash down payment of five percent. However, there are some mortgage products for which we require the borrower to pay a lesser amount from his or her own funds, as discussed in Section 113.01 (for Flexible 97 mortgages and Flexible 100 mortgages); Part VIII, Section 101.02 (for Fannie 3/2 mortgages); and Part VIII, Section 101.03 (for Fannie 97 mortgages).

Once our minimum down payment from the borrower's own funds requirement has been satisfied, the remainder of a larger down payment may come from other acceptable sources—such as a gift (or grant), trade equity, rent credit, a disaster relief grant or loan, an individual development account, **an employer**, premium proceeds from a mortgage revenue bond, etc. In some instances, we permit a borrower to obtain the entire down payment from these sources. See Part X, Chapter 6, for a full discussion of all acceptable sources of funds for the down payment and any exceptions to our requirement for the borrower to make at least five percent of the down payment from his or her own funds. *(Since the funds are "Earned Income" paid from the Independent Dealers employer the funds are approved for use.)*

### **X, 603: Sources of Borrower's Funds (01/31/06)**

The lender must obtain documentation for all sources for the funds that the borrower uses to make the down payment and to pay closing costs. Since a borrower who is not a U.S. citizen may maintain assets outside of the United States or may not invest his or her assets with financial institutions in the United States, a lender may consider funds that a non-U.S. citizen borrower recently deposited in a U. S. depository institution as an acceptable source of funds—as long as there is evidence that the funds were transferred from the country from which the borrower immigrated and it can be established that the funds were the borrower's before the date of the transfer. In this case, the sources of all funds used for closing should be verified just as they would for a borrower who is a U.S. citizen.

Typical sources of funds for a borrower's down payment, closing costs, and financial reserves are discussed in the following Sections.

**X. 603.04: Trust Accounts (06/30/02)**

Funds disbursed from a borrower's trust account are an acceptable source of the down payment, closing costs, and financial reserves if the borrower has immediate access to them. The lender should request the trust manager or trustee to verify the value of the trust account and to confirm the conditions under which the borrower has access to the funds. The lender also must document the effect (if any) that the withdrawal of funds from the account will have on any trust income that is used in qualifying the borrower for the mortgage.

**X. 603.25: Anticipated Savings (06/30/02)**

The lender may preliminarily qualify the borrower on the basis that his or her anticipated savings will be sufficient to meet the funds needed for closing. The use of "anticipated savings" does not relieve the lender of the responsibility for verifying that the savings are actually accumulated by the borrower before loan closing. The estimate for "anticipated savings" that the borrower can be expected to save over the time remaining until loan closing must be realistically developed. For example, if the borrower has no previous history of a consistent savings pattern or the ability to reduce or eliminate unnecessary expenses, it is not realistic to estimate that all of his or her pay over a two-month or three-month period can (or will) be directed entirely to savings. To determine the potential funds that are available for savings, the lender should reduce the borrower's expected "after tax" income for the period by his or her existing housing expenses, monthly debt expenses (based on data from the credit report), and expected living expenses (food, transportation, etc.) for that same period.

**X. 603.02: Checking and Savings Accounts (06/30/02)**

Funds held in a checking or a savings account may be used for the down payment, closing costs, and financial reserves. The lender should use either a Request for Verification of Deposit (Form 1006 or 1006(S)) or the borrower's bank statements for the most recent two months to verify checking and savings accounts. The lender must investigate any indications of borrowed funds—such as a recently opened account, a recently received large deposit, or an account balance that is considerably greater than the average balance over the previous few months. When there is a recently opened account or a large increase in an existing account, the source of funds must be explained by the borrower and verified by the lender. Unverified funds are not acceptable sources for the down payment or closing costs unless they satisfy our requirements for borrowed funds (as discussed in Section 603.15).

## **Freddie Mac Single-Family Seller Guide Excerpt**

### **26.1: Borrower Funds (09/09/02)**

All funds paid by the Borrower in connection with the property purchase or Mortgage financing must be from cash or other equity.

### **26.2: Cash (06/10/05)**

“Cash” is considered to be any of the following:

1. Funds on deposit in the Borrower’s checking, savings, money market or certificate of deposit account or other depository account.
2. A gift that is from a Related Person of the Borrower, that does not have to be repaid and is documented according to Section 37.20. A gift of Equity from a Related Person is allowed provided it meets the requirements of this Section and Section 37.20. If a gift from a Related Person is used with a Mortgage with a loan-to-value (LTV) ratio greater than 80%, the gift is permitted only if the Borrower has made a down payment of at least 5% from other sources of cash or other Equity unless provided for otherwise in this Single-Family Seller/Service Guide (Guide).
3. A gift or grant from An Agency that does not have to be repaid, is given pursuant to an established program and meets the requirements of Section 37.20 provided the agency is not an interested party (as described in Section 25.3) and the funds were not obtained from an interested party either directly or through a third party. This source of gift does not require a 5% down payment from other sources of cash or other Equity.
4. Proceeds of a loan fully secured by the Borrower’s owned assets
5. Proceeds from the sale of the Borrower’s assets
6. A cash deposit toward the purchase, the source of which is verifiable
7. Funds disbursed from a trust if documented according to Section 37.20.
8. Funds on deposit in an Individual Development Account (IDA) meeting the requirements of Sections 26.6 and 37.20 and matching funds provided by An Agency
9. Funds on deposit in a Community Savings System that are deposited by the Borrower and documented according to Section 37.20
10. Pooled funds on deposit from Related Persons who reside with the Borrower meeting the requirements of Section 26.4, if they are verified and documented according to Section 37.20
11. For purchase transactions, proceeds from an unsecured loan meeting the requirements of Section 26.6.1 that is an Employer Assisted Homeownership (EAH) Benefit meeting the requirements of Section 26.6.2. If an unsecured loan is used with a mortgage with a loan-to-value (LTV) ratio greater than 80%, the unsecured loan is permitted only if the Borrower has made a down payment of at least 5% from other sources of cash or other Equity unless provided for otherwise in this Guide.

**FHA / HUD 4155.1 (rev.) Excerpt**

P. Commission from Sale. If the borrower is a licensed real estate agent entitled to a real estate commission from the sale of the property being purchased, that amount may be used for the cash investment with no adjustment to the maximum mortgage required. A family member entitled to the commission also may provide gift funds to the homebuyer.

**1-9: CASH INVESTMENT (07/91)**

The applicant must make a cash investment in the property at least equal to the difference between the total cost of acquisition and the amount of the mortgage to be insured. The total acquisition cost is the total cost to the buyer, including the sales price, cost of any required repairs, alterations or additions, plus total closing costs. Total acquisition cost does not include non-realty items, prepaid expenses, seller concessions, including seller-paid closing costs, and excessive seller contributions.

A. Source. Generally, this cash investment must be from:

- 1) the applicant's own assets, or
- 2) gifts from a relative, **employer**, longstanding friend not involved in the transaction, government agency, charitable organization, or
- 3) loans secured against marketable assets owned by the applicant other than the subject property, or
- 4) secured loans from a State or local government agency (subject to HUD approval), or
- 5) sweat equity.

B. Mortgagor's Certification. No part of the minimum investment can be borrowed as an unsecured loan, except for applications under Section 203(i) or borrowers at least 60 years old applying under Section 203(b). In all other cases, mortgagors are required to certify that they do not and will not have any unpaid contractual obligation remaining as a result of their cash payment.

Asset Verification. Our documentation requirements for verifying a borrower's assets to close include obtaining verification of deposits (VODs) backed up with the most recent bank statements, or, if using the alternate documentation procedures, original bank statements covering the most recent three month period; these requirements are further described in paragraph 3-1F of the mortgage credit handbook.

## **ON DETERMINING IF THE BUYERS ACCOUNT, LLC PROGRAM VIOLATES THE REAL ESTATE SETTLEMENT PROCEDURES ACT (RESPA)**

The Buyers Account, LLC program does not violate RESPA because the sale of the membership is not related to settlement services of the real estate transaction and the commission is reasonable consideration for the sale of the membership.

RESPA was enacted by congress after seeing a significant need of reforms in the residential real-estate settlement process. 4 key items were. 12 U.S.C §2601.

1. To bring about more effective advance disclosure of settlement costs to home buyers and sellers.
2. To eliminate kickbacks and referral fees that tended to increase the cost of settlement services.
3. To reduce sums that home buyers were required, by lenders, to place in escrow accounts to insure payment of real estate taxes and insurance.
4. To significantly reform and modernize local record keeping of land title information.

In order to prohibit kickback and referral fee arrangements RESPA's "fee-splitting" provision was created. This provision prohibits any payment that is made or thing of value that is furnished for referral of real estate settlement business, and to prohibit a person that provides settlement services from giving or rebating any portion of a charge to any other person except in return for services actually performed. *Welch v. Centex Home Equity Co., LLC*, 262 F.Supp.2d 1263

Pursuant to RESPA

*"the term "settlement services" includes any service provided in connection with a real estate settlement including, but not limited to, the following: title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the originator of a federally related mortgage loan (including, but not limited to, the taking of loan application, loan processing, and the underwriting and funding of loans), and the handling of the processing, and closing or settlement."*

12 U.S.C §2602(3).

RESPA does not prohibit the payment of a reasonable fee for services actually performed. The services provided by Buyers Account, LLC is independent of the real estate transaction and does not constitute "Settlement Services" as defined by RESPA.

**Simply put; the Buyers Account, LLC program does not violate RESPA because all fees charged are equitable and reasonable in an open market economy.**

**ON DETERMINING THE LENDERS ABILITY TO EXCLUDE THE “EARNED INCOME” COMMISSION AS A PROPER SOURCE OF FUNDS FOR A DOWN PAYMENT**

Income from Part-Time Employment can not be discounted or excluded by lenders under the Equal Credit Opportunity Act.

The use of a “Earned Income” commission for a down payment is consistent with the Equal Credit Opportunity Act. Under the Equal Credit Opportunity Act, 15 USCA § 1691, a lender may consider the amount and probable continuance of any income, but may not discount or exclude from consideration income from part-time employment. It was found in the case of U.S. v. Household Finance Corp., 1988 WI 893886 (N.D.Ill. 1988), the United States District Court prohibited “discounting or excluding from consideration income from part-time employment except as provided by the ECOA and Regulation B, 12 CFR §202.6(b)(5)”.

Rules of that regulation regarding the evaluation of applications state:

(b) Specific rules concerning the use of information. (1) Except as provided in the Act and this regulation, a creditor shall not take a prohibited basis into account in any system of evaluating the creditworthiness of applicants.

(5) *Income.* **A creditor shall not discount or exclude from consideration the income of an applicant or the spouse of an applicant because of a prohibited basis or because the income is derived from part-time employment** or is an annuity, pension, or other retirement benefit; a creditor may consider the amount and probable continuance of any income in evaluating an applicant’s creditworthiness. When an applicant relies on alimony, child support or separate maintenance payments in applying for credit, the creditor shall consider such payments as income to the extent that they are likely to be consistently made.

Simply put; When applying this provision to the Buyers Account, LLC system, the use of an “Earned Income” commission for a down payment is acceptable under the Equal Credit Opportunity Act.

## **ON DETERMINING THE PROPER CLASSIFICATION OF THE COMMISSION PAID TO THE INDEPENDENT DEALER**

The commission paid to the Independent Dealer for services rendered in the sale of memberships to the Property Service Alliance is properly defined as “Earned Income” as currently defined by the US Internal Revenue Service.

In the past and present the Federal and State Supreme Courts have rejected narrow and strict definitions of “Income” in favor of a more broad interpretation of the term. In *Rickel v. Commissioner*, 900 F.2d 655, 657 (3d Cir.1990); and *United States v. Connor*, 898 F.2d 942, 943 (3d Cir.), cert. denied, 497 U.S. 1029, 110 S.Ct 3284, 111 L.Ed.2d 793 (1990), as well as numerous other courts of Appeals have uniformly upheld a broad definition of “income.” See; *Commissioner v. Miller*, 914 F.2d 586, 590 (4<sup>th</sup> Cir.1990) (“Exclusions to income are to be construed narrowly.”); *Herbert v. United States*, 850 F.2d 32, 34 (2d Cir.1988) (“The Supreme Court has consistently given this definition of gross income a liberal construction in recognition of the intention of Congress to tax all gains except those specifically exempted.”); *In re Carmel*, 134 B.R. 890, 896 Bankr.N.D.Ill.1991) (“This broad definition [of income] operates to tax all gains except those specifically excluded by statute.”); *In re Osborne*, 159 B.R. 570 (Bankr.C.D.Cal.1993), aff’d 167 B.R. 6998 (9<sup>th</sup> Cir. BAP 1994). The present IRC, the definition of income is very broad, *e.g.*, [except] as otherwise provided...., gross income means all income from whatever source derived, including (but not limited to) the following items:

1. Compensation for services, including fees, commissions, fringe benefits, and similar items
2. Gross income derived from business.

26 U.S.C §61(a)(emphasis added).

Simply put; the Buyers Account program properly defines the commission paid to the Independent Dealer as “Earned Income” and is consistent with the Federal and State Supreme Courts broad definition of “income.”

## **ON DETERMINING IF THE BUYERS ACCOUNT, LLC PROGRAM COMMITS MORTGAGE FRAUD**

The Buyers Account, LLC program does not commit mortgage fraud because there are **NO** knowingly false statements being made for the purpose of obtaining a mortgage.

18 U.S.C. §1010. Department of Housing and Urban Development and Federal Housing Administration transactions, provides that:

*Whoever, for the purpose of obtaining any loan or advance of credit from any person, partnership, association, or corporation with the intent that such loan or advance of credit shall be offered to or accepted by the Department of housing and Urban Development for insurance, or for the purpose of obtaining any extension or renewal of any loan, advance of credit, or mortgage insured by such Department, or the acceptance, release, or substitution of any security on such a loan, advance of credit, or for the purpose of influencing in any way the action of such Department, makes, passes, utters, or publishes any statement, knowing the same to be false, or alters, forges, or counterfeits any instrument, paper, or document, or utters, publishes, or passes as true any instrument, paper, or document, knowing it to have been altered, forged, or counterfeited, or willfully overvalues any security, asset or income, shall be fined under this title or imprisoned not more than two years or both.*

Three elements of proof are required to substantiate the offence of making a false statement in application for a Federal Housing Administration Loan.

1. Making of a false statement in application.
2. Knowing it to be false.
3. For purpose of obtaining loan from lending institution and influencing Administration.

The Buyers Account, LLC program does not involve any of those three required elements. In Fact, the Buyers Account, LLC program goes above and beyond the requirements for proving it is legal by the following:

1. The property value as defined by the 3<sup>rd</sup> party appraisal is never exceeded.
2. The Independent Dealer properly provides his primary and part-time employment information on the loan application.
3. The home buyer correctly identifies the source of his down payment.
4. The home seller purchases the membership in a transaction separate from the real estate sale.
5. All information regarding the program, membership and payments are fully disclosed to all parties.
6. All U.S. laws regarding taxing of individual income are complied with.

**Simply put; the Buyers Account, LLC program does not commit mortgage fraud because all information is fully disclosed to all parties.**

## **ON DETERMINING IF THE BUYERS ACCOUNT, LLC PROGRAM IS COMPLIANT WITH HUD**

HUD does not prohibit seller concessions but in 1999, HUD proposed a rule that would prohibit borrowers from obtaining down payment assistance from organizations that received reimbursements from sellers. (Proposed Rule, The U.S. Department of Housing and Urban Development, 24 C.F.R. Part 203, 64 F.R. 49956 (Sept. 14, 1999).) This proposed ruling was later withdrawn after receiving almost 2,000 public comments on the proposed rule; with over 99% of those comments being opposed to the new rule. (111405, GAO Report “Mortgage Financing: Additional Action Needed to Manage Risks of FHA-Insured Loans with Down Payment Assistance”, page 23)

HUD does permit seller-funded down payment assistance because it does not compromise FHA guidelines prohibiting homebuyers from directly using funds from property sellers and other interested parties toward a down payment. FHA does prohibit sellers from directly providing down payment funds. But, HUD provides that the seller’s concessions for a buyer’s closing costs are allowed for up to 6% of the sales price.

The Buyers Account, LLC program is consistent with FHA policy which also does not prohibit sales concessions, but requires that appraisers report sales concessions and properly address and account for sales concessions in the appraisal. “FHA guidelines require mortgagees to provide appraisers with all financing data and sales concessions for properties to be security for an FHA-insured loan.” (010405 Mortgage Letter 2005-2.)

As defined above the Buyers Account, LLC program is NOT a seller’s concession and does comply with the FHA guidelines because the contract shows that the property will be enrolled in the Property Service Alliance and all financing data, including the down payment is properly disclosed.

Simply put; the Buyers Account, LLC program is NOT mortgage fraud because all information is fully disclosed to all parties and no knowingly false statement is presented for the purpose of obtaining a mortgage.

## **CONCLUSION**

Buyers Account, LLC is a qualified Earned Income program (EIP) that benefits both the seller and buyer in a real estate transaction and fully discloses all aspects of the membership and real estate purchases. Simply put, sellers can gain the benefit of adding value to the property much like a home warranty; making the home sell quicker and attracting more qualified buyers. Buyers earn commissions through standard employment. They use those commissions to purchase a home but not qualify for the loan to get the home. Buyers also must pay all tax debts associated with that additional Earned Income. Home values are preserved and not over estimated because they never go above the appraised value. Since the key to the Buyers Account® program is the sale of a multi-year membership in the Property Service Alliance. The buyer also benefits as the membership conveys with the property at settlement.

The Property Service Alliance provides a valuable set of goods and services to the homeowner at substantial discounts. It also provides access to service providers, contractors, utility providers, and local governments. The Alliance provides members with a voice in Tallahassee, FL and works to protect homeowner rights.

The Buyers Account, LLC program meets the underwriting guidelines for Fannie Mae, Freddie Mac, FHA/HUD, and all published Federal housing regulations. Buyers Account, LLC also works with most sub-prime loan programs.

The Buyers Account, LLC program is significantly different from non-profit down payment assistance programs (DPA's). Buyers Account, LLC is a for-profit entity that pays its dealers a taxable commission for selling a membership to a sister organization. These funds are "Earned Income" and can be used as the dealer wishes. The program provides a process for wiring these funds from the dealer's account to the closing table as a service to our commissioned dealers. This service is provided as a courtesy as many of our dealers choose to sell a membership to the owner of the home they are purchasing.

The Buyers Account, LLC program never over inflates property values it only uses the un-used equity that exists when a seller is willing to take less than what their property will appraise for.

The full details of the transactions are disclosed to all parties and all parties must sign contracts for the property enrollment, sale of the membership, commissions earned, taxes due and declaration of individuals with their respective roles defined.