



Last Reviewed: 01/09/2025

## TPO – FHA MANUAL UNDERWRITING QUICK SUMMARY

### OVERVIEW

FHA files may require manual underwriting or may need to be manually downgraded when specific file characteristics warrant the loan to be reviewed, by the lender, to determine its insurability is certain. This document provides reference information and materials regarding manual underwriting of FHA loans.

**For additional information regarding FHA loans and FHA manual underwriting guidelines, please refer to:**

- FHA 4000.1 Handbook
- FHA Manual Underwriting Guide
- UHM's Third Party Originator Lending Guide
- UHM TPO Overlays for GNMA Delivery
- Waiting Periods for Significant Derogatory Credit Events

### COMMON REASONS AN FHA WILL NEED TO BE MANUALLY UNDERWRITTEN

- "Total Scorecard" returns a 'Refer' recommendation.
- "Total Scorecard" returns a 'Approve Eligible' recommendation, but the loan requires a manual downgrade.
- There is specific information that cannot be evaluated by or submitted to "Total Scorecard."
- The cumulative amount of disputed accounts totals \$1,000 or more.
- Bankruptcy seasoning requirements have not been met.
- Foreclosure seasoning requirements have not been met.
- Short Sale or Deed in Lieu seasoning requirements have not been met.
- Payment History does not meet the minimum FHA late payment requirements.
- Business income shows more than a 20% decline over the course of the reviewed analysis period.
- Borrowers have NO credit scores or do not have enough satisfactory trade lines.
- Undisclosed financed properties.

For additional reasons that may warrant an FHA Manually Underwritten file, refer to the [FHA 4000.1 Handbook](#).

### CREDIT

Refer to this section for requirements on evaluating credit report late payments for an FHA loan.

**IMPORTANT:** All Borrower's credit must be reviewed to meet satisfactory FHA standards.

*For FHA loans that do not meet the minimum liability requirements, listed below, the UW must document the details proving the delinquency was due to an Extenuating Circumstance that should not re-occur and submit the file for an Underwriting Team Lead 2nd Level Review.*

- **Mortgage and Installment liabilities:** Zero 30-day late payments in the last 12 months and no more than two 30-day late payments in the last 24 months are acceptable.
- **Revolving Debt:** Zero 90-day late payments in the last 12 months and no more than two 60-day late payments in the last 12 months are acceptable.

| Liability Type            | 12 Months      | 24 Months |
|---------------------------|----------------|-----------|
| Mortgage and Installments | 0 X 30         | 2 X 30    |
| Revolving                 | 2 X 60; 0 X 90 | N/A       |

**Note:** Compensating factors cannot be used to offset a negative credit history.



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## Business Credit Reports

FHA requires a business credit report for all Corporations or S Corporations when:

- Loan is subject to manual underwriting, and
- The Borrower has 25% or greater ownership interest in the Corporations or S Corporations.

UHM requires the Borrower to provide the business credit report from one of the three major business credit bureaus: Dun & Bradstreet, Equifax, or Experian. The report must include, at a minimum:

- Company legal name, address, incorporation details, number of employees, sales, ownership, and subsidiaries,
- Public filings (liens, judgments, and UCC filings), and
- Trade Line payments, past payment history, and collections.

The business credit report is valid for 120 days.

## DEBT AND LIABILITY OVERVIEW

The following Credit Liability Review Chart provides FHA guidance on how to evaluate credit liabilities that may be found on a borrower's credit report when applying for an FHA mortgage.

**Important:** Always refer to the FHA section of the UHM GNMA Overlay to ensure all current policies and procedures are being upheld.

| CREDIT LIABILITY REVIEW CHART                |  |
|--|--|
| Liability Type                               | Payment Rules  |
| Installments or Close End Debts              | If there are less than 10 payments remaining AND the total cumulative payment amount for all debts that are less than 10 payments is equal to 5% or less than the borrower's gross monthly income, then the payment amount(s) may be excluded.   |
| Authorized User Accounts                     | This debt can only be excluded from the DTI if the primary account holder has paid the last 12 month's payments on time. If the account has been opened for less than 12 months, all payments must have been paid by the primary account holder with no less than 3 months payments proven; otherwise, debt cannot be excluded from unauthorized user's DTI.   |
| Child Support, Alimony, or Other Maintenance | The payment amount used must be the greater of the amount shown per a court ordered document OR the garnishment amount represented on the paystub.   |
| Deferred (Non-Student Loan) Debt             | Payments must be included. No exceptions. If no active or projected payment amount can be verified, the amount used must be gathered by calculating 0.5% of the outstanding balance  |
| Student Loans                                | Student Loan payments will never be excluded from the DTI, even when deferred. The payment amount must be calculated using of 0.5% of the outstanding balance, if the payment amount provided, via the credit report, is less than the of 0.5% calculation. The payment can be verified using actual loan documentation and it must confirm the payment is or will be fully amortized over the entire loan term. |
| Timeshares                                   | A timeshare MUST be underwritten as an Installment loan and will follow Installment loan rules.  |
| Non-30-day Revolving Accounts                | If the payment amount is not available on the credit report, it must be calculated using 5% of the outstanding balance or by using the payment shown on most recent account statement.   |
| 30-day Revolving Accounts                    | This account can be excluded from the DTI if there are no late payments in the last 12-months. Funds to close must support the payoff of this account in addition to the funds needed for closing and loan approval. If a late payment does exist, the payment should be calculated using 5% of the outstanding balance.   |
| Disputed Accounts                            | If there are less than \$1,000 in cumulative disputed accounts, these accounts can be excluded from the DTI.<br><b>Medical disputes are automatically excluded. Fraud accounts will require supporting documentation.</b>  |



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| Collections                      | <p>If there is less than \$2,000 in cumulative collections, these accounts can be excluded from the DTI. <b><i>Medical and Fraud collections are automatically excluded and are not a part of the \$2,000 calculation.</i></b></p> <p>If the non-medical collection payments total \$2,000 or more, the payment amount must be obtained from a documented payment arrangement or by calculating 5% of the outstanding balance for each collection. File must document all collections with an extenuating circumstance, medical included.</p> <p>The Borrower must provide an LOE, which is supported by documentation, for each outstanding collection account.</p> |
| Charge-Offs                      | <p>Charge offs may be excluded from the DTI. The file must document all collections with an extenuating circumstance, medical included.</p> <p>The Borrower must provide an LOE, which is supported by documentation, for each outstanding charge-off account.</p>   |
| Co-signer/Contingent Liabilities | <p>Payments must be included unless it is documented that the primary account holder has made the most recent 12 months payments on time OR if the debtor can document they will pursue the co-signer if the primary account holder defaults on the loan.</p>  |
| Business Related Debts           | <p>Where business-related debts are listed under the borrower's credit report, the debt should reflect no late payments in the last 12 months and the lender must confirm payments are made from business funds and not personal funds.</p>  |
| Verification of Rent (VOR)       | <p>A formal Verification of Rent (VOR) is required for all manually underwritten FHA loans.</p>  |

## DEROGATORY CREDIT OVERVIEW

**Important:** Significant Derogatory Credit Events require a minimum Waiting Period to be satisfied, prior to entering into an FHA mortgage transaction. The credit file must be reviewed and documented according to FHA's underwriting standards.

| FHA'S WAITING PERIODS FOR DEROGATORY CREDIT EVENTS |  |
|--|--|
| Event Type   | Seasoning Rule   |
| <b>Chapter 7 Bankruptcy</b>                        | <p>2-year Wait Period from the discharge date.</p> <p>1- year Wait Period with extenuating circumstance documented and acceptable re-established credit history.</p>   |
| <b>Chapter 13 Bankruptcy</b>                       | <p>1-year Wait Period with satisfactory payment history and permission from trustee or judge.</p>  |
| <b>Foreclosure, Deed in Lieu</b>                   | <p>3-year Wait Period from the transfer of title.</p> <p>2-year Wait Period with FHA acceptable Extenuating Circumstance and acceptable re-established credit history.</p>   |
| <b>Short Sale</b>                                  | <p>3-year Wait Period, if prior mortgage has one or more late payments incurred in the 12 months preceding the short sale.</p> <p>If no late payments were incurred on the mortgage for the last 12 months prior to the short sale, and all installment debt payments for the same time period were also made within the month due, then NO WAIT PERIOD is required.</p>   |
| <b>Loan Modification</b>                           | <p>For both purchases and no cash-out refinances, a mortgage that has been modified must utilize the payment history in accordance with the modification agreement for the time period of modification in determine late housing payments. In addition, where a mortgage has been modified, the borrower must have made at least six payments under the modification agreement to be eligible for a no cash-out refinance.</p> |



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|                                  | Where a mortgage reflects payments under a modification or Forbearance Plan within the 12 months prior to case number assignment, the Mortgagee must obtain: <ul style="list-style-type: none"> <li>• A copy of the modification or Forbearance Plan; and</li> <li>• Evidence of the payment amount and date of payments during the forbearance term.</li> </ul> |
| <b>Extenuating Circumstances</b> | All files requiring an Extenuating Circumstance will also require an UW 2 <sup>nd</sup> Level Review Signature.  |

**See Reference Materials:** UHM's GNMA Overlays and Waiting Periods for Significant Credit Events for full procedures regarding how to review significant Derogatory Credit Events on FHA loans at UHM.

## EXTENUATING CIRCUMSTANCES

Extenuating Circumstances are significant events where a severe credit or financial distress has occurred and is considered beyond the borrower's control. These events are determined as unlikely to re-occur or repeat.

Some acceptable examples of Extenuating Circumstances are:

- Serious illness
- Involuntary loss or an employment layoff of a wage earner
- Death of a wage earner

**Note:** Divorce, job relocation/transfer, or the inability to sell a current home does not qualify and are not considered extenuating circumstances.

**Disclaimer:** For additional information regarding FHA Loans and FHA Manual Underwriting Guidelines, please refer to FHA 4000.1 Handbook, the FHA Manual Underwriting Guide, or the UHM's Third Party Originator Lending Guide.

## ASSETS

FHA manually underwritten files require a minimum number of reserves, based on the unit count. Refer to the chart below.

**Important:** AUS "Total Scorecard" documentation relief is not permitted for manually underwritten files.

| RESERVE REQUIREMENTS BASED ON UNIT COUNT |  |
|--|--|
| # of Units                               | Minimum Reserve Requirements<br>(When Not Used as a Compensating Factor) |
| 1-2 Units                                | 1 months' PITIA reserves   |
| 3-4 Units                                | 3 months' PITIA reserves   |

See the [Compensating Factors section](#) below for asset requirements when using assets as a Compensating Factor.

## COMPENSATING FACTORS

Compensating Factors provide a means to support a file for approval where it may present some weaker loan characteristics and risk levels. Refer to the FHA Acceptable Compensating Factors chart below regarding when and what Compensating Factors are required based on FHA minimum credit score(s) and maximum ratio thresholds.

**Important:** Compensating Factors cannot be used to offset a negative credit history.

UHM requires both FHA Compensating Factor Requirements as well as UHM Compensating Factor Requirements for loan files that meet any of the FICO Ratio Tiers on the following table. This table is strictly for the purposes of providing Compensating Factor guidance on FHA loans. UHM GNMA Overlay Policies are still required and mandated.

The maximum Total Mortgage Payment to Effective Income Ratio (PTI) and Total Fixed Payments to Effective Income Ratio (DTI) applicable to manually underwritten loans are summarized in the matrix below.

The qualifying ratios for Borrowers with no credit score are computed using income only from Borrowers occupying the property and obligated on the Mortgage. Non-occupant co-borrower income may not be included.



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| FHA ACCEPTABLE COMPENSATING FACTORS CHART |  |   |
|---|--|---|
| If the Credit Score is:                   | AND the Max Qualifying Ratios (DTI) are: | Then the Compensating Factor Requirements are:<br>(Refer to UHM GNMA Overlays that may apply, in addition to the below requirements)  |
| 500-579                                   | 31/43*                                   | Not applicable. Borrowers with credit scores below 580 may not exceed 31/43 ratios. NOTE: Credit scores below 580 are generally ineligible at UHM, unless approved by the Pre-App Express Desk. Refer to UHM's GNMA Overlays for additional requirements.   |
| No Credit Score Borrowers                 | 31/43*                                   | Not applicable. Borrowers with no credit score may not exceed 31/43 ratios.   |
| 580 and above                             | 31/43*                                   | Compensating Factors are not required.  |
| 580 and above                             | 37/47                                    | <b>At least one of the following Compensating Factors is required:</b> <ul style="list-style-type: none"> <li>• Payment shock is not more than \$100 or &lt;5%, whichever is less</li> <li>• Verified Cash Reserves (three months for 1-2 units and six months for 3-4 units)</li> <li>• Residual income that meets VA residual income requirements</li> </ul>  |
| 580 and above                             | 40/40                                    | <b>**No Discretionary debt may be cited as a compensating factor subject to the following requirements:</b> <ul style="list-style-type: none"> <li>• The borrower's housing payment is the only open account with an outstanding balance not paid off monthly; and</li> <li>• The credit report shows established credit lines in the borrower's name open for at least 6 months; and</li> <li>• The borrower can document these accounts have been paid off in full monthly for at least the past 6 months.</li> </ul> |
| 580 and above                             | 40/50                                    | <b>At least two of the following Compensating Factors are required:</b> <ul style="list-style-type: none"> <li>• Payment shock is no more than \$100 or &lt;5%, whichever is less</li> <li>• Verified Cash Reserves (three months for 1-2 units and six months for 3-4 units)</li> <li>• Residual Income meets VA guidelines</li> <li>• Additional Income received at least one year that is not being used for the effective income calculation</li> </ul>   |

**\* Energy Efficient Mortgages (EEM) permitted to 33/45**

**\*\* No Discretionary Debt** - Borrowers who have no established credit other than their housing payment, no other credit lines in their own name open for at least six months, or who cannot document that all other accounts are paid off in full monthly for at least the past six months, do not qualify under this criterion. Credit lines not in the Borrower's name but for which they are an authorized user do not qualify under this criterion.