

AARMR BORROWER ABILITY TO REPAY STANDARD

Purpose

The purpose of this AARMR BORROWER ABILITY TO REPAY STANDARD (hereafter referred to as BARS) is to provide state regulators with a standardized examination procedure for examining a lender's determination that its borrowers have a reasonable ability to repay a loan. The BARS was developed to:

- Protect consumers by providing comprehensive examination procedures to ensure that lenders are adequately evaluating whether borrowers have the ability to repay the mortgage loans offered to them.
- Protect communities from the problems that are associated with lenders not adequately assessing the ability of borrowers to repay their mortgage loans, including foreclosures.
- Establish uniform standards applicable to multi-state examinations and enforcement actions or for review by one state of another state's reports of examination.
- Provide consistent and uniform guidance for use by lender in-house compliance and audit departments.

Background

A borrower's ability to repay is, in most cases, evaluated by a lender during the underwriting process. This process can be the most important step in loan origination because it controls the risk of foreclosure and other financial losses taken by both a borrower and a lender. Given the risks to consumers, communities and lenders alike, lenders must develop and implement cautious underwriting standards. However, implementing underwriting guidelines that are too restrictive would result in the lessening of available credit for riskier borrowers. A lender must weigh its appetite for risk against the potential harm to itself, as well as the consumers and communities it deals with, when setting its own policies for the ability to repay.

A lender should not extend a residential mortgage loan unless it has come to the conclusion, given the facts and their analysis, that the borrower will be able to make the payments on a timely basis and in full. However, AARMR understands that a lender must have flexibility built into its underwriting process and be allowed to make adjustments on a loan by loan basis based on all the factors used in the underwriting process.

Each lender evaluates, during the underwriting process, many facets of information about, and provided by, the borrower. It is usual and customary to examine the borrower's credit history; employment status, including future employment probabilities; income; occupancy; ratios and more.

Additionally, each lender may assign different weights to the different categories. These weights are where the biggest differences among lenders exist and these same weights comprise the lender's acceptable level of risk. This is why the examination work program must be flexible enough to adjust itself to each lender's risk level and therefore its underwriting processes. The examination work program is not intended to dictate these levels of risk since the result could be a lessening of available credit for certain types of borrowers.

Examination Process

Summary of the BARS

The BARS is comprised of three parts. The first is a questionnaire for the lender to complete at the onset of the examination to help provide the examiner with information about its ability to repay underwriting guidelines.

The second part, the *Policy Review Questionnaire*, provides guidance and explanation to the examiner in reviewing a lender's underwriting procedures regarding assessing a borrower's ability to repay. It also explains the main procedures used to determine the borrower's ability to repay.

The third part, the *Examiner's Loan Review Procedures*, focuses on individual loan review and assessing how well the lender has followed its own underwriting guidelines. This section also includes an Excel spreadsheet that will assist an examiner when reviewing individual loan files.

Examiner's Goals

It is very important at the beginning of the examination for an examiner to understand how the mortgage lender chooses to manage the ability-to-repay portion of its underwriting analysis. There is no one right way for a mortgage lender to conduct an ability-to-repay analysis. Each mortgage lender has a different business model that has built into it a certain amount of risk that its customers may default on their mortgage loans. The goal of mortgage regulation is to ensure that lenders manage this risk prudently. Although completely eliminating the risk of consumers defaulting on their mortgage loans is not our goal, keeping defaults low through prudent underwriting is. Once the examiner understands how the mortgage lender conducts its ability-to-repay analysis, judgments can be made about the assumptions underlying it as well as the procedures used by the company to comply with its own policy.

First Day Letter

Included in the examiner's first day letter to the mortgage lender should be a request for a detailed explanation about how the business conducts its ability-to-repay analysis and the underlying assumptions. Importantly, the examiner should specifically ask the mortgage lender in the first day letter:

- to discuss its “appetite for risk,” including its goals for default rates
- the specifics for how the business evaluates a customer’s ability to repay, including the key ratios and other information used

Included in the BARS is a sample first day letter addendum that can be used with the examiner’s existing letter or in conjunction with AARMR’s Manager Questionnaire. This addendum is intended to help the examiner answer the BARS Policy Review Questionnaire.

Examination and Exit Meetings

The examination process in general should include on-going meetings with management to clarify and better understand how the mortgage lender conducts its business. In particular, examiners should communicate with management personnel as needed to fully understand the lender’s ability-to-repay analysis. Questions and concerns about the business’ ability-to-repay analysis should be brought to management’s attention and management should be provided with every opportunity to explain and justify its ability-to-repay program to the examiner including economic or geographic disparities, the effect of certain government programs on underwriting and the like.

The exit meeting with management should include a detailed discussion of any concerns the examiner has about the lender’s ability-to-repay program. Given the frequent communication between the examiner and the lender about the ability-to-repay program, management should not be surprised by any concerns raised by the examiner.

Loan File Selection

The examiner must review a sample of loan files to determine if the lender is following its ability to repay underwriting policies. To accomplish this, the examiner should first determine how large of a sample to review. The examiner should use the statistical sampling method outlined below for selecting the sample size. Once the sample size is known, the examiner must then choose which files should be reviewed. The examiner should either continue with the statistical sampling method or refer to the judgmental sampling method for guidance on selecting the actual files.

The judgmental sampling method necessitates that the examiner have sufficient information from the lender in order to be able to categorize the loans into different risk categories – high, medium, and low. If the examiner does not have sufficient information to do so, then the statistical method for selecting loan files should be used. The examiner may also have to use a combination of the two methods to obtain the appropriate sample size.

Statistical Loan Sampling

The examiner first ascertains the lender's total loan population from which to select samples. The following chart must be used to determine the total number of sample loans to select from any given population.

TOTAL UNIVERSE TABLE			
Number in Universe	Minimum	Plus:	Maximum
Under 99	20	Total universe if smaller	20
100-299	20	10% of number above 100	40
300-499	40	7% of number above 300	54
500-749	54	6% of number above 500	69
750-999	69	5% of number above 750	82
1000-1999	82	4% of number above 1000	122
2000-2999	122	3% of number above 2000	152
3000-4999	152	2% of number above 3000	192
5000-9999	192	1.5% of number above 5000	267
10000 or more	267	1% of number above 10000	

At this point, the examiner can switch to the judgmental sampling method or proceed with the statistical sampling method. To proceed with the sample loan selection under the statistical sampling method, the examiner must sort the entire loan population into the different loan products offered by the lender. The examiner must also determine the percentage of loans made by each product type. The table below illustrates how the percentage of each product group may differ by company.

Products Offered Table¹					
	First Mortgage Fixed	Second Mortgage Fixed	3/1 ARM	5/1 ARM	First Mortgage Fixed – Interest Only
Company 1		30%	70%		
Company 2	50%	50%			
Company 3	25%	25%		25%	25%
Company 4			100%		

¹ This table is for illustration purposes only. Not all possible product combinations are shown.

Company 5	10%	10%	40%	20%	20%
Company 6				50%	50%

For Example:

Using Company 3 from the Products Offered Table, if the total population of all four categories is 3000, then according to the Total Universe Table the total number of loans to be selected for the examination is 152. The 152 loans are then divided by four, which represents the number of loans (25%) to select from each category. Thus, 38 loans are selected from each category.

Now the examiner selects the particular loans within each category. Using the Company 3 example above, if there are 750 fixed first mortgages, 750 fixed second mortgages, 750 5/1 adjustable rate mortgages, and 750 fixed rate interest only first mortgages, you would start with the 750 fixed first mortgages and divide by 38 to get the interval that each loan is selected. Approximately every 20th loan is selected. Then the examiner does the following:

- Pick any starting point between zero and twenty, say row 10.
- Starting with row 10, count the items until the interval number (20) is reached. The loan that corresponds with that row (30) will be the first item selected for the sample.
- Starting with the next consecutive row (31) as number 1, count until the number corresponding with the interval (row 50) is reached and select that loan for the sample.
- Repeat above steps throughout the entire universe.
- If for some reason the item pulled does not fit the characteristics of the sample (different state property, wrong date, or business loan) pull the item then begin counting with the next row. This ensures that items are sampled uniformly.
- To ensure that the results of the sample are statistically valid, the EIC must strictly adhere to the procedures for the sampling method selected.
- The EIC should verify that the sample sizes are able to be accomplished within the time allowed for an examination. The initial sample size may need to be reevaluated to get a new sample size.

Judgmental Loan Sampling

Judgmental sampling, like statistical sampling, involves an in-depth analysis of only a portion of a group. The basic purpose of the sampling is to draw conclusions about a “population” by testing a portion of that population. The feature that distinguishes

judgmental from statistical sampling is that each item in the population does not have an equal chance of being selected. Items are not selected randomly because a predetermined hypothesis has been made after reviewing the loan data from the lender.

The examiner should select the sample of loans as follows:

1. *High Risk*

50% of sample from programs with at least one of the following characteristics:

- a. Total debt-to-income ratios of 50% or higher
- b. High risk of “payment shock”
- c. Credit scores of 640 and below
- d. Short-term teaser rates
- e. Loan-to-value ratios higher than 90%
- f. Stated income/low-doc/no-doc programs
- g. Yielding the most money to loan officers, the lender, or mortgage brokers
- h. Loans which were required to be bought back

If examiners have access to servicing-related information, then the following should be considered in the high risk sample: (Examiners will need to look for naturally occurring breaks in default and foreclosure rates within each loan program to help determine which should fall into the high, medium, and low risk categories. Examiners should also consider any national or regional default or foreclosure rate information that is available.)

- i. Highest default rates
- j. Highest percentage collection activities
- k. Early payment defaults
- l. Highest foreclosure rates

2. *Medium Risk*

30% of sample from programs with at least one of the following characteristics:

- a. Total debt-to-income ratios from 40% to 50%
- b. Credit scores between 640 and 686
- c. With loan-to-value ratios between 80% and 90%

If examiners have access to servicing-related information, then the following should be considered in the medium risk sample:

- d. Slow pays
A portfolio exhibiting 20% or more slow pays is at higher risk for default and should be examined for potential underwriting errors.
- e. Next level of default rates
- f. Next level of early payment defaults
- g. Next level of foreclosure rates

3. *Low Risk*

20% of sample from programs with all of the following characteristics:

- a. Total debt-to-income ratios below 40%

- b. Loan to value ratios under 80%
- c. Credit scores above 686

Examination Conclusions

By the end of the examination, the examiner should be able to make conclusions about the following:

1. The mortgage lender's appetite for default risk
2. The quality of the mortgage lender's ability-to-repay analysis, including:
 - a. Whether the lender uses preferred ratios and other metrics in their ability to-repay analysis
 - b. Whether the lender weights the factors it considers appropriately
 - c. Whether the lender follows its own policies through appropriate procedures and internal controls
 - d. Whether the lender appropriately monitors its default ratios and adjusts its ability-to-repay analysis accordingly
 - e. Whether the lender's ability-to-repay analysis presents unreasonable risk of default to consumers in the future or at present
 - f. Whether the lender appropriately connects employee compensation and evaluation to loan performance
3. Recommended changes to a lender's ability-to-repay analysis
4. Recommended rating assigned to a lender's ability-to-repay analysis
A sample rating system follows that allows for a rating of 1 to 5 based on the examiner's findings
5. Recommended levels of administrative action

Rating Definitions

Rating of "1":

The company adheres to strong extensive written policies and procedures and extensive internal training that focus on the consumer's ability to repay across all product lines. Management properly weighs loan product features which prevent accepting unacceptable risks. Management actively monitors and conducts a delinquency analysis on respective loan programs and makes modifications as deemed necessary. As a result delinquency and foreclosure rates across all products lines are lower than industry averages.

Rating of "2":

The company has satisfactory written policies and procedures and training programs that focus on the consumer's ability to repay across all product lines; and the company generally follows these policies, procedures and programs. The company has developed various lending programs which include loan features which enable the company to accept more risk when evaluating the consumer's ability to repay. The aggressive lending programs and adherence to satisfactory risk management policies, procedures and

programs have resulted in delinquency and foreclosure results which would be considered to meet industry averages.

Rating of “3”:

The company has less than satisfactory policies and procedures or does not consistently follow its policies and procedures when determining if the consumer has the ability to repay their respective loans across all product lines. The company has developed various lending programs with loan features that are considered more “risky” and doesn’t consistently and actively consider the consumer’s ability to repay their respective loan. The aggressive loan programs have led to higher than average delinquency and foreclosures. Management fails to actively monitor and adjust loan programs. Insufficient policies and procedures coupled with lack of effective training plans needs immediate attention by management

Rating of “4”:

The company hasn’t developed policies and procedures or the policies and procedures have no bearing on the products offered. Therefore the company cannot properly determine if the consumer has the ability to repay the loans across all product lines. Controls and monitoring of all loan programs are considered inadequate. Management hasn’t monitored delinquency and consumer complaints. There is evidence of predatory lending and financial loss to consumers and the company warrants immediate policy reviews and revisions. The company needs immediate supervisory guidance to prevent further deterioration.

Rating of “5”:

The company has failed to develop any loan programs that address the consumer’s ability to repay their loan. There is evidence of extensive predatory lending and financial losses to the consumer and the company. The company warrants immediate regulatory enforcement to force the company to cease offering the risky products or cease operations.

Remedies

Examining a lender’s ability-to-repay analysis should be done in a thoughtful, iterative way with abundant opportunity for management to explain what they do. Unless circumstances warrant otherwise, AARMR recommends that the primary method used to enforce compliance with a state’s standards for a lender’s ability-to-repay analysis be the candid comment and criticism between lender and regulator more commonly used in the regulation of depository institutions. Unless consumers are significantly at risk through a mortgage lender’s weak ability-to-repay analysis, AARMR recommends that progressive discipline be used to address exceptions to an ability-to-repay analysis and related items such as board resolutions, memoranda of understanding, orders, and fines with license revocations and suspensions used as last resorts.

Similarly, less frequently used tools in the world of non-depository mortgage regulation may yield beneficial results such as:

- Having non-portfolio lenders study their default rates by tracing loans or contacting consumers
- Off-site monitoring programs to report default rates quarterly to a regulator when an ability-to-repay analysis is determined to be weak
- Requiring mortgage lenders to increase capital or net worth or to fund Allowance for Loan and Lease Loss Accounts when ability-to-repay analyses are insufficient

Definitions

Combined Loan-to-Value (CLTV):

The total of 1st and any subordinate lien loan amounts divided by the lesser of the selling price or the appraised value.

Credit Score:

A single numerical score, based on information in an individual's credit report, which measures that individual's creditworthiness.

Early Payment Default

A delinquency occurring usually within the first, second, or third payment owing.

Fully Amortizing Payment:

The monthly mortgage payment which, if unchanged through the remaining life of the loan at the then-existing interest rate, will pay off the loan at term.

Fully Indexed Rate:

On an Adjustable Rate Mortgage (ARM), the index rate prevailing at the time a residential mortgage loan is made, plus the margin that will apply after the expiration of an introductory interest rate.

Loan to Value (LTV):

The loan amount divided by the lesser of the selling price or the appraised value.

Negative Amortization:

If the loan payment made is less than the interest incurred, the remaining balance of the loan increases.

Payment Shock

A scenario in which monthly mortgage payments on an adjustable rate mortgage rise so high that the borrower may not be able to afford the payments. Consumer protection guidelines regarding extremely low initial "teaser" rates, lifetime ceilings, and annual caps are designed to prevent payment shock.

Predatory Lending:

Unsavory lender practices calculated to take advantage of unsuspecting borrowers. This would include, but not be limited to, a borrower paying more for a mortgage than they should, related to their risk profile.

Slow Pays

A mortgage payment that is made late enough to generate a late fee but is less than 30 days late.

Statistical Loan Sampling:

A method of selecting a portion of a population, by means of mathematical calculations and probabilities, for the purpose of making scientifically and mathematically sound inferences regarding the characteristics of the entire population.

Total Debt to Income (Total DTI):

Total DTI should include household debt such as property tax; homeowner's insurance; condo or homeowner association fees; PMI; secondary or subordinate mortgages; as well as, other debt such as credit card; motor vehicle; or other contractual obligations.

Underwriting:

The process of collecting and verifying the information and qualifications about a borrower that will lead a lender to approve or deny a mortgage loan application.

**FIRST DAY LETTER / QUESTIONNAIRE ADDENDUM
INFORMATION REQUEST**

BORROWER'S ABILITY TO REPAY

1. Does management have a written policy concerning evaluation of the borrower's ability to repay? Yes No

If yes:

Provide a copy of the policy for each loan program.

Was the written policy developed internally by the company?

Yes No

2. Have any complaints been filed against the institution related to the borrower's ability to repay? Yes No

If yes, provide copies of the complaints.

3. What appetite for risk does management assume and specifically what is the default rate management is willing to assume?

4. Does the company have a policy that includes standards for third party originators? Yes No

If yes:

Are the originators provided with a copy of the policy? Yes No

Are the originators informed of the consequences of their failure to abide by the policies? Yes No

5. Does the policy address the appropriate due diligence of third-party originators including pre-relationship review, verifications of borrower information, responsibility for post-closing reviews? Yes No

6. What is the policy for third party compensation?

7. Does the compensation policy to loan originators correlate to the default pattern of loans that they have originated?

Yes No don't have access to default information

If yes, explain.

8. Does the policy require a regular review of third party loan transactions to determine compliance with underwriting standards? Yes No

If yes, how many? How often? Is there a record of the reviews?

9. What notification is required to be given to borrowers in regard to prepayment penalties?

10. Are exceptions to prepayment penalties allowed? Yes No

If yes, explain.

11. Does management believe that it adheres to its policies in determining the borrower's ability to repay? Yes No

12. Does the policy require management to review its delinquency report to determine if the policy in use adequately supports management's acceptable level of risk associated with each product type?

Yes No don't have access to default information

13. Does the company have loan delinquency information? Yes No

If yes:

Are delinquency reports available by product type, loan originator, and early payment defaults?

Yes No

POLICY REVIEW QUESTIONNAIRE

A. Step One (Documentation Request)

		Y	N	Comments regarding repayment policies
A.1	Does management have a written policy concerning evaluation of the borrower's ability to repay?			
A.2	Have complaints been filed against the institution related to the borrower's ability to repay? <i>(Review complaints received by your agency as well as the institution's complaint logs.)</i>			

B. Step 2 (Review of Policy)

		Y	N	Comments regarding repayment policies
B.1	Does the policy demonstrate that management has a clear understanding of its responsibilities related to the borrower's ability to repay? <i>(Policy should identify all areas necessary to evaluate the ability to repay)</i>			
B.2	Is the policy developed by the lender? If not, by whom?			
B.3	Does the policy address qualifying standards that evaluate the borrower's ability to repay the debt by final maturity at the fully-indexed rate?			
B.4	Does the policy assume a fully-amortizing repayment schedule in determining the borrower's ability to repay?			
B.5	Does the policy address reasonable limitations on potential payment shock at expected payment change dates? <i>(Is the index used a standard index or a more volatile one? Are there "teaser" rates that are significantly below market? Is there a reasonable cap on changes over the life of the loan?)</i>			
B.6	Does the policy address negative amortization features related to the borrower's ability to repay?			
B.7	Does the policy address how the company will verify the borrower's income, including the borrower's current employment and reasonably expected future income, for repayment ability? <i>(Examiners should consider the use of IRS W-2's, tax returns, payroll receipts, financial institutions records, credit report or payment history on existing mortgage.)</i>			
B.8	Does the lender's policy allow for the			

	borrower's assets, credit score, net worth or equity in their primary residence to be used when determining the borrower's ability to repay? If so, explain.			
B.9	Does the policy allow the institution to determine the borrower's ability to repay, based solely on guidelines provided by a federal agency, such as Fannie or Freddie?			
	TOTAL Debt to Income (Total DTI)	Y	N	Comments regarding repayment policies
B.10	Does the policy outline an acceptable range for the borrowers total DTI based on the loan type? (<i>Examiner should consider industry standard percentages based on loan type and risk.</i>)			
B.11	Does the policy's total DTI ratio include all of the borrowers' contractual obligations?			
B.12	Does the lender's policy address counseling borrowers on the impact of their decision to accept a mortgage with an adjustable rate, balloon payment, or other alternative mortgage product? (<i>Counseling should include how their standard of living might change, and the potential loss of their home.</i>)			
	Indirect Originations (use of brokers or other lenders)	Y	N	Comments regarding repayment policies
B.13	Does the policy include standards for using third party originators? (<i>Are the originators provided with a copy of the lender's policy? Are the originators informed of the consequences of their failure to abide by the policy?</i>)			
B.14	Does the policy address the appropriate due diligence of third-party originators, including pre-relationship review, verifications of borrower information, and post-closing reviews?			
B.15	Does the institution's policy establish criteria for third-party compensation designed to avoid providing incentives for originations? (<i>Does the policy dictate the type of fees allowed or is the maximum amount of the fees allowed commensurate with the work performed including use of YSPs according to HUD guidelines?</i>)			
B.16	Does the lender's policy address compensation to loan originators that correlates to the default pattern of loans that they have originated? (<i>Is there any type of breakdown in the payment of commissions, for example 50% at closing and the remaining after 30-60 days if the loan has not defaulted?</i>)			

B.17	Does the institution's policy require a regular review of a reasonable sample of its loan transactions to determine compliance with underwriting standards? <i>(If so, how often? How many? Is it sufficient? Is there a record of the review?)</i>			
	Multiple Concurrent Transactions	Y	N	Comments regarding repayment policies
B.18	Does the policy address a borrower who may be applying for multiple transactions, simultaneously or within a 60 day period?			
	Prepayment Penalty Clauses	Y	N	Comments regarding repayment policies
B.19	Does the policy require both verbal and written notification to borrowers regarding any potential prepayment penalty?			
B.20	Does the policy allow for exceptions to charging the prepayment penalty such as: a refinance by their institution or subsidiary; or a refinance due to a bona fide emergency of the borrower?			
	Examination (Sampling Loan Transactions)	Y	N	Comments regarding repayment policies
B.21	Does the policy require that the lender review the delinquency report to determine if the policy adequately supports the risk associated with each product type? Does the lender's delinquency report track by loan originator, product type, or early payment default? Based on the information provided in the delinquency report, does the institution's policy address the ability to make changes to their policy? <i>(Are the delinquencies significantly higher than industry average for the product and risk? Are there particular originators whose loans are responsible for the increase?)</i>			

EXAMINER'S LOAN REVIEW PROCEDURES

	LOAN REVIEW PROCESS	EXAMINER'S COMMENTS
	Before beginning to evaluate each borrower's ability to repay, the examiner should:	
LR.1	Review and evaluate lender underwriting standards, including loan policies through the Policy Review Questionnaire.	
LR.2	Determine the validity of the income documentation and verify that the amounts used are correct.	
LR.3	Ensure that all debts are documented and disclosed in full as per the borrower's application. Overlooked debt may greatly affect the ratios calculated during the initial underwriting process possibly to the extent of a change in the loan approval status.	

	Using the Ability to Repay Spreadsheet, the examiner should enter information requested in each category. Calculations are done electronically	EXAMINER'S COMMENTS
S.1	Enter Lender's Name	
S.2	Enter Lender's Address	
	Locate the "Enter the Lender's Underwriting Standards Below" (after the blank column, at the bottom of the spreadsheet) The examiner will need to create a new worksheet for each loan program, as the underwriting standards will be different.	EXAMINER'S COMMENTS
S.3	Enter the qualifying ratios the lender uses in its underwriting standards. These ratios should be found within the underwriting policy: <ul style="list-style-type: none"> • Primary Housing Expense-to-Income • Total Debt-to-Income 	

	<ul style="list-style-type: none"> • Loan-to-Value • Combined Loan-to-Value 	
	Monthly Income	EXAMINER'S COMMENTS
S.4	<p>Enter the income amounts listed on the borrower's application and which have been verified through additional documentation. Enter:</p> <ul style="list-style-type: none"> • Base Income - Borrower • Other Income – Borrower • Base Income – Co-Borrower • Other Income – Co-Borrower 	
	Total Monthly Housing Payments	EXAMINER'S COMMENTS
S.5	<p>Housing projections based on <u>Fully Indexed Rate</u> or on <u>Highest Interest Rate</u> (ceiling) as permitted by the Promissory note and attachments to the note. Enter each of the following as found within the closed loan documents:</p> <ul style="list-style-type: none"> • First Mortgage P & I • Second Mortgage P & I • Hazard Insurance • PMI (Mortgage Insurance) • Real Estate Taxes • HOA Fees • Lease/Ground Rent • Other housing expense 	
	Total Debts	EXAMINER'S COMMENTS
S.6	<p>The following will describe and help to classify all debt that must be considered in qualifying borrowers.</p> <p>In computing the total debts for the <i>debt-to-income ratios</i>, include the new total monthly housing payment and all other additional recurring charges <i>extending 10 months or more</i>, including payments on installment accounts, child support or separate maintenance payments, revolving accounts and alimony, etc.</p> <p>For <i>revolving account</i> payments, calculate using the greatest of 5 percent</p>	

	<p>of the balance or \$10, unless the account shows a specific minimum monthly payment.</p> <p>In the file, observe additional possible contingent liabilities (example: co-signed on accounts for others or a company obligation), projected obligations (example: student loan) scheduled to begin with twelve (12) months of the loan closing.</p> <p><u>Obligations not to be considered debt</u> (or subtracted from gross income) include federal, state and local taxes; FICA or other retirement contributions such as 401(k) accounts (including repayment of debt secured by these funds); commuting costs; union dues; open accounts with zero balances; automatic deductions to savings accounts; child care; and voluntary deductions.</p> <p>Enter: The total of All Other Monthly Payments</p>	
	Final Spreadsheet Entries	EXAMINER'S COMMENTS
S.7	<p>Enter the following items which will complete the spreadsheet and calculate the final ratios:</p> <ul style="list-style-type: none"> • Appraised Value • First Mortgage Loan Amount • Second Mortgage Loan Amount 	

When the spreadsheet is complete and combined with other sampling evaluations, the examiner will gather information to evaluate and determine if the underwriting ratios or mitigation circumstances applied to the sampled loans correlate with the lender's underwriting standards.

The examiner may review the historical performance of the lender's loan portfolio (default rates on each loan product) to determine if mitigating circumstances exist for certain products or are otherwise justified.

Excessive variations, mitigating or otherwise, may show an avoidance of mandated policies and may indicate a lack of internal control of the lender and should be brought to the attention of the appropriate management. Management may be able to show why such extreme variances exist. If not, the lender may be driven to perform its own evaluation to see where its policies are being ignored.

Underwriting policies are the key to determining that borrowers have the ability to repay their mortgage loan. Lenders need to ensure that their underwriting policies are sufficient and most importantly, followed completely and properly.