# CHAPTER 11: RATIO ANALYSIS

## 11.1 INTRODUCTION

Ratio calculations are used to determine if the applicants' repayment income can reasonably be expected to meet the anticipated monthly housing expense and total monthly obligations involved in homeownership. The Agency has established standards for principal, interest, taxes, and insurance (PITI) and total debt (TD) ratios; however in some instances, there is flexibility to apply these standards when valid compensating factors are present.

## 11.2 THE RATIOS [7 CFR 3555.151(h)(1)(i)]

Ratios are calculated by utilizing the repayment income, as determined by the lender in Chapter 9, Section 2 of this Handbook. To qualify for a guarantee, borrowers must meet the Agency's standards for both the PITI and TD ratios.

### A. The PITI Ratio

Applicants are considered to have repayment ability if their proposed monthly housing expense does not exceed ~~29~~ 34 percent of their repayment income. Monthly housing expenses include:

- First Mortgage (P&I);
- Subordinate Lien(s);
- Homeowner's Insurance;
- Supplemental Property Insurance;
- Property Taxes;
- Mortgage Insurance (First –y~~Y~~ear annual fee monthly amount) Association/Project- Dues (Condo, Co-Op, PUD); and
- Other.

### B. The Total Debt Ratio

Applicants are considered to have repayment ability when their total debts do not exceed 41 percent of their repayment income.

The total debt ratio includes monthly housing expense (PITI) plus other monthly credit or debt obligations incurred by the applicants.

The lender must document the applicants' debts through various records including, but not limited to, credit reports, direct or third-party verifications, court documents, and verification of deposits. All open debts/accounts (including non-medical collection accounts and judgments) incurred through the closing date must be considered in the total debt calculation and documented in GUS ~~as well as~~and the loan application, as applicable. Amounts listed on the credit report will be used unless verification supports an alternate payment amount. If an amount other than that shown on the credit report is used, the lender will provide documentation of the amount utilized. This documentation will be uploaded with the final submission to Agency.

The following obligation expenses must be included in the monthly debts:

1. ***PITI***

   - First Mortgage (P&I), property taxes, homeowner's insurance, mortgage insurance (first year annual fee monthly amount), association/project dues, other.

2. ***Installment accounts***

   - Accounts that will be paid in full through a specified number of fixed payments such as auto, personal, secured/unsecured, etc. must have the monthly payment included.

   - If ten or less months of repayment remains per the credit report, creditor verification, etc., the monthly debt may be omitted if the payment does not exceed five percent of the monthly repayment income.

   - Installment debt may be paid down to ten months or less of remaining debt.

3. ***Revolving accounts***

   - Credit cards, lines of credit, secured/unsecured loans, etc. must include the minimum monthly payment documented on the credit report or other creditor verification in the total debts.

   - If the credit report shows an outstanding balance, but no minimum monthly payment, the payment must be calculated as five percent of the balance reported on the credit report.

   - The lender may obtain a current account statement or creditor verification to document the actual monthly payment and include that amount in the monthly debts.

- Revolving accounts with no outstanding balance on the credit report do not require an estimated payment to be included in the debt ratio.

- Revolving accounts with no outstanding balance are not required to be closed.

**4. *Open 30-Day Accounts***

- A 30-day account is a credit arrangement requiring the applicant to pay off the full outstanding balance on the account every month.

- The lender may utilize the credit report to document the applicant has paid the outstanding balance for the previous 12 months.

- If the credit report reflects late payments in the last 12 months, the lender must include five percent of the outstanding balance in the monthly debts.

- 30-day accounts that are paid monthly in full are not included in the total debt ratio.

**5. *Court Ordered Debts: Child support, alimony, garnishments, etc.***

- Court ordered debts must have the payment included in the total debt ratio unless the applicant has a release of liability from the court/creditor and acceptable evidence is documented.

- Lenders will utilize select pages from the applicable agreement/court order to document the required monthly payment due and the duration of the debt.

- Court ordered debts with ten or less payments remaining may be excluded if the payment does not exceed five percent of the monthly repayment income.

- For GUS transactions, the lender will manually enter the obligation(s) as a monthly liability. When the obligation account is entered as “other,” the lender will specify what the obligation is (i.e. court ordered child support~~.~~). A manual entry of this monthly obligation does not require an underwriting recommendation of “Accept” to be downgraded to a “Refer.”

- Lenders must confirm repayment agreements are current. Refer to Chapter 10 for court ordered debt guidance and program eligibility.

6. ***Child Care Expenses***

- Child care expenses are not required to be included in the monthly debt ratio.

7. ***Student loans***

- For outstanding student loans, regardless of the payment status, lenders must use:
  - The payment amount reported on the credit report or the actual documented payment, when the payment amount is above zero; or
  - One half (.50) percent of the outstanding loan balance documented on the credit report or creditor verification, when the payment amount is zero.
- Student loans in the applicant's name alone but paid by another party remain the legal responsibility of the applicant. The applicable payment must be included in the monthly debts.
- Student loans in a "forgiveness" plan/program remain the legal responsibility of the applicant until they are released of liability from the creditor. The applicable payment must be included in the monthly debts.
- Co-signed obligations are addressed below in ~~section~~paragraph 11.

8. ***Mortgages: Rental Property***

- A GUS Accept recommendation will not require a manual downgrade to a Refer when the net monthly rental income is negative.
- Income received from rents may only be counted for repayment if received for 24 months or more. Rental income received for less than 24 months should not be entered into GUS as rental income.
- If the credit report reflects late mortgage payments on the rental dwelling in the 12 months prior to loan application, the full mortgage liability and all associated costs must be included in the monthly debts.
- Refer to Chapter 9 for rental income guidance.

9. ***Mortgages: No Release of Liability***

- Mortgage liabilities disposed of through a sale, trade, or transfer without a release of liability (i.e.~~,~~ the borrower remains on the promissory note) must be included in the total debt ratio unless evidence can be obtained to confirm the remaining party/new owner has successfully made the payment for the previous 12 months prior to loan application.

- Evidence may be reported through the credit report or verification from the creditor/servicer to document the payment history has been current for the 12 months prior to loan application.

- If there are late payments in the previous 12 months prior to loan application, the full mortgage obligation must be included in the monthly debt.

**10.** ***Mortgages: Divorce***

- In the case of a divorce, the lender must obtain a copy of the legal separation agreement or divorce decree to document the remaining party/new owner is responsible to pay all mortgage debts from the effective date of the decree forward.

- To exclude the mortgage debt, the lender must document the previous 12 months have been paid as agreed prior to loan application through the credit report or verification from the creditor/servicer.

- If there are late payments in the previous 12 months prior to loan application, the full mortgage obligation must be included in the monthly debts.

**11.** ***Co-signed obligations***

- Co-signed debts refer to debts where the applicant may be a co-borrower, joint obligor, co-signer, guarantor, etc.

- Co-signed debts must be included in the monthly debts unless the applicants provide evidence another obligor (party to the debt) has successfully made the payment for the previous 12 months prior to loan application.

- Acceptable evidence includes, but is not limited to, canceled checks, money order receipts, and/or bank statements of the co-obligor.

- Late payments reported in the previous 12 months prior to application will require the monthly liability to be included in the monthly debts.

- If the applicant can provide conclusive evidence from the creditor that they will not pursue debt collection against the applicant should the other party default, the 12-month payment history of the additional party is not required.

- Debts identified as "individual" on a credit report must be included in the debt ratio regardless of who is making the monthly payment (e.g. parents paying car payments on behalf of applicant and the loan is solely in the applicant's name).

**12. *Business debts***

- Business debts (e.g. car loan) reported on the applicants' personal credit report may be omitted from the monthly debt if there is evidence the debt is paid through a business account.

- Acceptable evidence includes canceled checks or bank statements from a business account for the previous 12 months.

- Payments paid by the business must be included ~~Verification of an ongoing payment arrangement should also be present~~ on the cash flow analysis and/or profit and loss statement, when applicable. ~~for the business.~~

**13. *401(k) loans/personal asset loans***

- Loans pledging personal assets, such as a 401(k) account, retirement funds, savings account, or other liquid assets do not require a payment to be included in the monthly debts.

**14. *Debts of a non-purchasing spouse (NPS)***

- Applicants who currently reside or are purchasing in a community property state must include the debts of the NPS unless specifically excluded by state law.

- Approved lenders are responsible to confirm state laws are met.

**15. *Collection accounts***

- Refer to Chapter 10 for collection account guidance.

**16. *Judgment accounts***

- Refer to Chapter 10 for Federal and non-Federal judgment guidance.

**17. *Charge-off accounts***

- ~~Charge-off accounts are not required to have a payment included in the monthly debts.~~ Refer to Chapter 10 for charge-off account guidance.

**18.** ***Expense allowances (including Automobile Allowances)***

- An automobile or other expense allowance will not cancel out a monthly debt for an automobile or expense loan/debt.
- The full amount of the monthly debt associated with the expense (such as a car or equipment payment) must be included in the total debt ratio calculation.
- For guidance on calculating income for expense allowances, refer to Chapter 9.

**19.** ***Balloon/deferred payments.***

- Deferred debts and balloon debts that will require payment in full upon their due date must have a payment included in the monthly debts. When the balloon/deferred payment loan is due within 12 months, the lender must evaluate the complete loan application to make a determination regarding the applicants' repayment ability.
- If the actual payment on a deferred/balloon loan is unknown, the lender may obtain documentation from the creditor to establish a monthly payment that will be due on a documented payment date, or they must use five percent of the outstanding balance on the credit report or creditor verification.

**20.** ***Tax repayment agreements***

- Include Federal or State income tax repayment plan payments in the monthly debt.
- If ten or less months of repayment remains per the plan, the monthly debt may be excluded if the payment does not exceed five percent of the monthly repayment income.
- Refer to Chapter 10 for Federal Income Tax agreement eligibility.

**21.** ***Lease payments***

- Auto, solar, energy, and additional lease payments must have the payment included in the monthly debt regardless of months remaining to pay on the contract.

**22.** ***Debt management plans***

- Include the monthly payment amount due from the counseling plan.
- Refer to Chapter 10 for guidance on credit exception and documentation requirements.

## 11.3 DEBT RATIO WAIVERS AND COMPENSATING FACTORS [7 CFR 3555.151(h)(3)]

The applicants' ~~PITI ratio may exceed 29 percent and the~~ Total Debt ratio may exceed 41 percent if the lender determines that strong compensating factors demonstrate that the household has higher repayment ability. No waivers are permitted to increase the PITI ratio above 34 percent for purchase transactions.

**A. Purchase Transactions: Debt ratio waivers**

**1. *GUS Accept loans:***

GUS files that receive an Accept or Accept Full Documentation underwriting recommendation do not require a debt ratio waiver~~s~~.

**2. *GUS Refer, Refer with Caution, and manually underwritten loans without GUS assistance:***

The lender must document eligible compensating factors to support a debt ratio waiver. Agency approval of a lender's request for the Total Debt ratio to exceed 41 percent ~~debt ratio waiver may be~~ may be granted if all of the following conditions are met:

- Acceptable ratio thresholds are met:
  - The maximum PITI ratio cannot exceed ~~32~~ 34 percent, and
  - The maximum TD ratio cannot exceed 44 percent;
- The validated credit score of all applicants is 680 or greater;
- At least one of the acceptable compensating factors listed below is identified. Supporting documentation is provided to the Agency and

maintained in the lender's permanent file. Acceptable Compensating Factors and Supporting Documentation:

- Accumulated savings or cash reserves available post loan closing are equal to or greater than three months of PITI payments. Documentation may include a verification of deposit (VOD) or bank statements that meet the requirements of Chapter 9. Cash on hand is not eligible for consideration as a compensating factor.

- The applicant(s) (all employed applicants) has been continuously employed with their current primary employer for a minimum of two years. A *Request for Verification of Employment* (VOE) (Form RD 1910-5, comparable HUD, FHA, VA or Fannie Mae form, or other equivalent), or a VOE prepared by an employment verification service (e.g.~~,~~ The Work Number~~.~~) must be provided. Applicants that have received Social Security benefits or retirement income for two years may utilize this compensating factor with documentation to support the history of receipt of benefits. This compensating factor is not applicable for self-employed applicants.

- The proposed PITI does not exceed the ~~is equal to or less than the~~ applicant's current verified housing expense by more than $100 or 5 percent, whichever is less, for the 12-month period preceding loan application. Verification of housing expenses may be documented on a V~~v~~erification of R~~r~~ent (VOR), Verification of Mortgage (VOM), -or credit report, as noted in Chapter 10 of this Handbook. The VOR, VOM, -or credit report must include the actual payment due and report no more than one 30 day late payments ~~or delinquency~~ for the previous 12 months. Rent or mortgage payment histories from a family member or interested party will not be considered unless 12 months of canceled checks, money order receipts, or electronic payment confirmations are provided. A history of less than 12 months will not be considered an acceptable compensating factor.

- The ~~dwelling~~subject property- is an energy efficient home based on the International Energy Conservation Code (IECC) standards, defined as:

  - For new construction, the dwelling ~~is energy-efficient in accordance with the Rural Energy Plus provision. The dwelling must be a new construction property that~~ meets or exceeds the IECC in effect at the time of construction. ~~the energy efficiency standards outlined in the most current edition of the International Energy Conservation Code.~~ The lender is responsible for verifying ~~that~~ the home meets the IECC standards, ~~and~~with evidence ~~of this requirement must be~~maintained in the lender's permanent loan file ~~at the time of construction~~. Refer to Chapter 12 for guidance in documenting thermal standards for new construction dwellings.

- ~~o~~ For existing dwellings, the dwelling meets or exceeds the current IECC. Existing dwellings that have been retrofitted to meet the current IECC standards are eligible. The lender is responsible for verifying the home meets the current IECC standards, with evidence maintained in the lender's permanent loan file.

- Debt Ratio Waiver Request and Agency Approval:

  - Debt ratio waivers must be requested and documented by the approved lender. The lender requests Agency concurrence with the debt ratio waiver by submitting an ~~signed~~ underwriting analysis that cites one or more of the above acceptable compensating factors. Lenders may utilize Fannie Mae 1008 / Freddie Mac 1077, *Uniform Underwriting and Transmittal Summary*, or similar form. Evidence of the compensating factor, such as a VOR, VOD, and/or VOE, must be submitted to the Agency for approval.

  - The issuance of the Conditional Commitment for a Loan Note Guarantee represents Agency approval of the ratio waiver.

**B. Refinance Transactions: Debt ratio waivers**

**1. *GUS Accept loans:***

- GUS files that receive an Accept or Accept Full Documentation underwriting recommendation do not require debt ratio waivers.

**2. *GUS Refer, Refer with Caution, and manually underwritten loans without GUS assistance:***

- GUS files that receive a GUS recommendation of Refer, Refer with Caution, or are not supported by GUS require debt ratio waivers, and supporting documentation must be submitted to the Agency.

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- Streamlined-assist refinance loans do not require debt ratio calculations, and therefore no debt ratio waiver.

- Debt ratios for refinance loans are not limited to the maximum purchase debt ratio thresholds.

- The following are examples of acceptable compensating factors for debt ratio waiver requests:

  - Validated c~~C~~redit score of 680 or higher for all applicants.

  - The proposed PITI does not exceed the borrower's current verified mortgage payment by more than $100 or 5 percent, whichever is less, for the 12-month period preceding loan application.

  - Accumulated savings or cash reserves available post-closing are equal to or greater than three months of the proposed PITI payment. Cash on hand is not eligible for consideration as a compensating factor.

  - Continuous employment with the current primary employer.

  - The subject property is an energy efficient home, defined as a dwelling which ~~An existing dwelling that~~ meets~~s~~ or exceeds~~s~~ the current International Energy Conservation Code (IECC)~~energy efficiency standards outlined in the most current edition of the International Energy Conservation Code~~. Existing dwellings that have been retrofitted to meet the current IECC standards are eligible. The lender is responsible for verifying ~~that~~ the home meets the current IECC standards, with evidence maintained in the lender's permanent loan file. ~~and supporting documentation must be obtained at the time of submission to the Agency.~~

- The issuance of the Conditional Commitment for a Loan Note Guarantee represents Agency approval of the ratio waiver.

## 11.4 MORTGAGE CREDIT CERTIFICATES

Authorized State or local housing finance agencies may issue a mortgage credit certificate (MCC) that provides a federal income tax credit to a qualified first-time homebuyer and/or low- or moderate-income homebuyer. Refer to Chapter 9 for MCC guidance and GUS data entry.

## 11.5 FUNDED BUYDOWN ACCOUNTS

Funded buydown accounts are designed to reduce the borrower's monthly payment during the initial years (temporary buydown) or the full life (permanent buydown) of the loan. Permanent buydowns are fully funded and paid for at loan closing. The interest rate is fixed and will not change for the life of the loan. Temporary buydowns are eligible when the ~~applicable~~ following guidelines are met:~~.~~

- ~~Temporary buydown account requirements:~~

- The mortgage loan must be underwritten at the full note rate. Both the full note rate and the initial buydown rate must be entered into GUS;~~.~~

- Buydown funds may come from the seller, lender or other third party;

- Buydown funds may not come from the borrower;

- The buydown must not reduce the interest rate more than two percent below the full note rate;

- The assistance may increase no more than one percent annually;

- The borrower must agree in writing that the temporary buydown funds will be placed in an escrow with a financial institution supervised by a federal or state agency and paid directly to the lender each month to reduce the monthly mortgage payment;

- The buydown account must be fully funded at origination; and

- A copy of the executed escrow agreement must be retained in the lender's permanent loan file.

## 11.6 SECTION 8 HOMEOWNERSHIP VOUCHERS

Section 8 Homeownership Vouchers may be used for qualifying applicants. Refer to Chapter 9 for voucher guidance and GUS data entry.

## 11.7 OBLIGATIONS NOT INCLUDED IN DEBT-TO-INCOME RATIOS

Obligations not considered or included in total debt-to-income ratio calculations include:

- Medical collections;
- Medical payments;
- Federal, state, and local taxes, unless a payment plan is in place;
- Federal Insurance Contribution Act (FICA) contributions;
- Other retirement contributions such as 401(k) accounts, including the repayment of loans secured by 401(k) funds;
- Automatic deductions to savings accounts, mutual funds, stocks, bonds, certificates of deposit, including the repayment of loans secured by such funds;

- Collateralized loans secured by depository accounts;
- Utilities;
- Insurance, other than property insurance;

- Commuting costs;
- Union dues;
- Open accounts with zero balances;
- Child care; and

Voluntary deductions.

All liabilities disclosed by the applicant should be listed in GUS. The lender may "omit" liabilities as permitted.