

For Arch MI and Arch MI For Credit Unions

Income Fundamentals 101

The First Step in Understanding
Acceptable Qualifying Income

a BACK TO BASICS course



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Objectives

Acceptable Income.

- Stability.
- Continuance.

Income Categories.

- Employment Income.
- Non-Employment Income.

Income Continuance.

- Expiration Date Not Defined.
- Expiration Date Defined.
- Other.

Taxable vs. Non-Taxable Income.



Overview of Acceptable Income



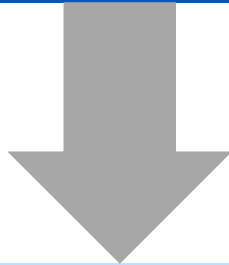
What Makes Income Acceptable?

Stability

Predictability

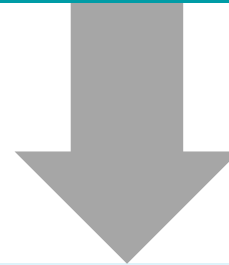


Stability



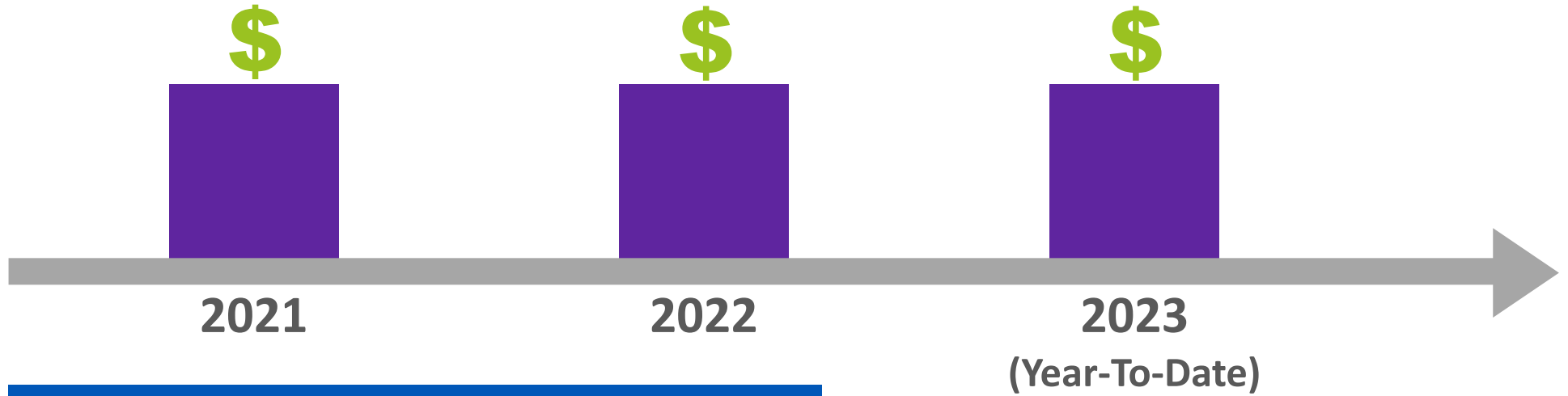
History

Predictability



Continuance

Income Stability



History
Two years.

Continuance
Three years.

Acceptable or Unacceptable?



Can you document it?

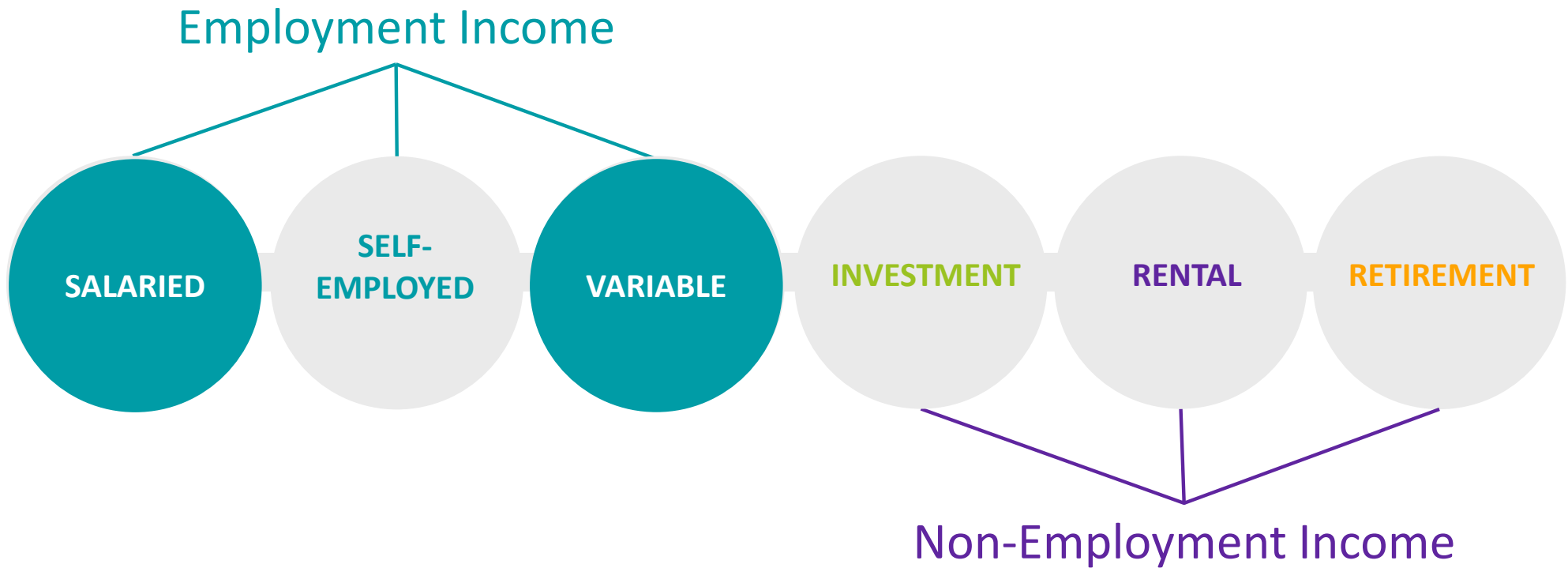
Is there a history?

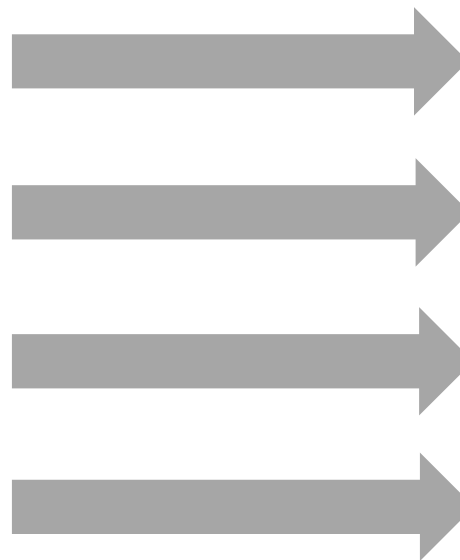
Is it likely to continue?

Income Categories



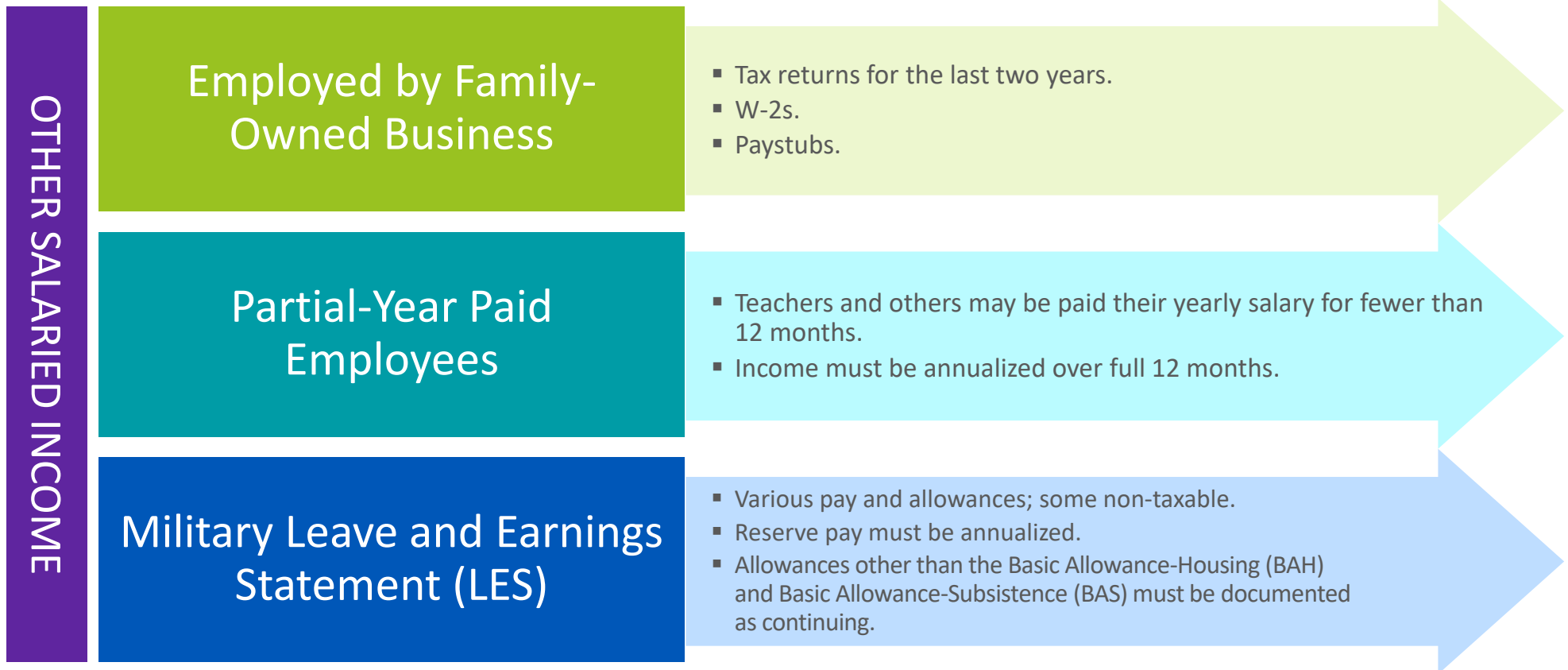






- History.
- Continuance.
- Documentation.
- Income Calculation.

Employment Income — Special Consideration



Employment Income — Special Consideration

OTHER SALARIED INCOME

Automobile Allowance

- Required two-year history of receipt.
- Must be added to income (not used to offset payment).

Seasonal Unemployment Compensation

- Required two-year history of receipt.
- Must be annualized.
- Must be verified as likely to continue

\$1,200/month
for 3 months.

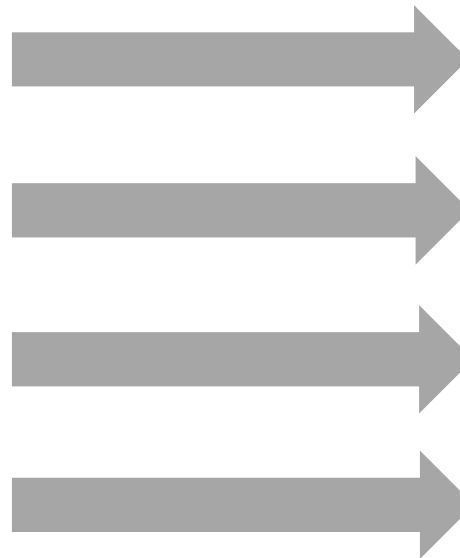
$\$1,200 \times 3/12$
= $\$300$.

Postal Service Income

- 26 pay periods listed in format 00-00.
- First set of numbers refers to the pay period; second set of numbers refers to the year.

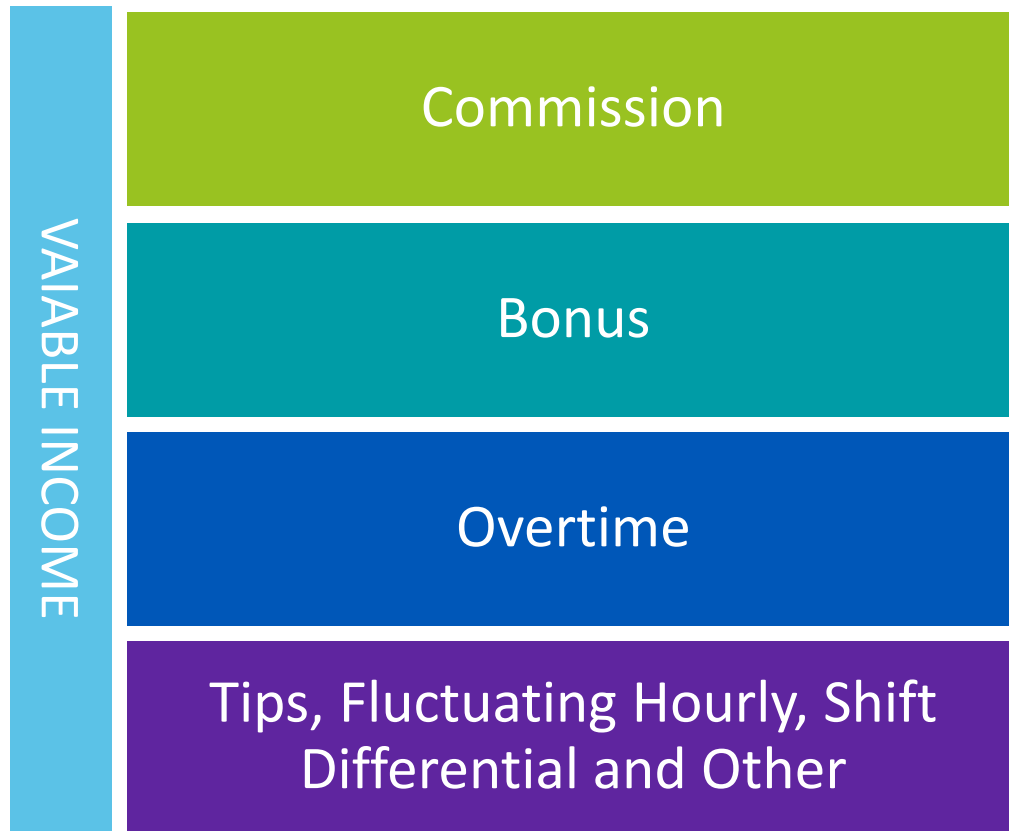
Paystubs and Earnings Statements





- History.
- Continuance.
- Documentation.
- Income Calculation.

Employment Income — Variable



A complete income picture must include historical income. Since this income fluctuates, qualifying income is generally averaged using current and historical earnings.

**Self-
Employment**

25% or greater
ownership interest
in a business.

Five
different
business
structures.

Tax returns
are
required.

Knowledge Check One

Which of the following is true regarding Seasonal Unemployment Compensation:

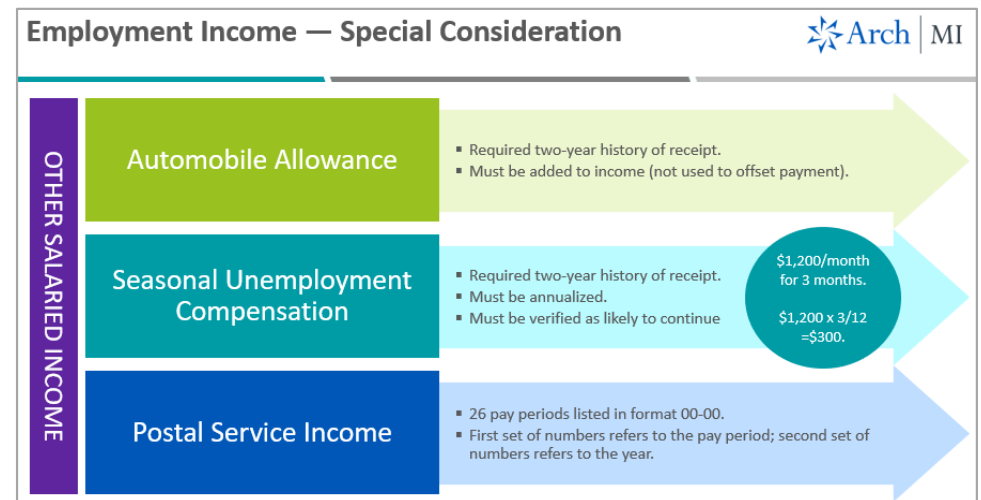
1. Requires a two-year history of receipt.
2. Must be annualized.
3. Must be verified as likely to continue.
4. All the above.



Check Your Understanding One

The correct answer is *4. All the Above.*

- *Seasonal Unemployment requires a...*
 - *Two-year history of receipt, AND*
 - *It must be annualized, AND*
 - *It must be verified as likely to continue.*



Non-Employment Income



Non-Employment Income Types



Mortgage Differential

Royalty

Mortgage Credit Certificate

Foster Care

Housing or Parsonage

Trust

Retirement or Pension

Notes Receivable

Rental Income

Dividends and Interest

Capital Gain

Disability

Alimony or Child Support

Public Assistance

Social Security

Boarder Income

Non-Employment Related

Possibly Employment Related

Investment or Asset Related

Benefit Related

Rental

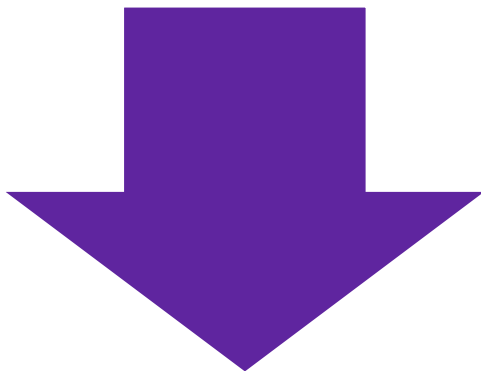
Retirement

Social Security

Alimony and Child Support



Sometimes, you must **prove** continuance of Qualifying Income.



Other times, you can **assume** continuance of Qualifying Income.

Three Years Continuance (?)



Non-Employment Income — Possibly Employment-Related

Royalty

Income received from allowing someone to use your property. Royalty payments for the use of patents, copyrighted works, natural resource are most common.

Many times, the person using the property does so to generate revenue. Royalties are usually legally binding.

Income received from providing foster-care services. Typically, a two-year history of receipt is required.

Foster Care

Or borrower has 12+ months providing service and the income is less than 30% of total gross qualifying income.

Non-Employment Income — Possibly Employment-Related *(Continued)*

Mortgage Differential

Often used in conjunction with corporate relocations. Are used as income, not as a mortgage payment offset.

An employer subsidy used to pay all or part of interest differential between employee's present and proposed mortgage payment.

Housing or Parsonage

May be considered qualifying income if documentation for most recent 12 months exist and the allowance is likely to continue for the next three years.

An allowance paid for use toward housing expenses, such as that received by clergy. Not military quarters allowance.

Non-Employment Income — Investment- or Asset-Related

Capital Gains

If two-year history exists and documented evidence of like-assets can be sold in the future, average historical income can be used to qualify.

When a capital asset is sold for more than the purchase price. One-time transaction should not be used as qualifying income.

Notes Receivable

Formed when a loan is made, and a promissory note is signed. Reported on a personal tax return as “installment sale income” on Form 6252.

Example: I sell you my car (I owned free and clear) and I hold the note for you, that is Notes Receivable Income.

Trust Income

Verify income stability w/copy of trust agreement (amount, payment frequency and duration) and verify income continuing for three more years.

Income received from money that has been placed in a Trust Account from which the beneficiary receives a distribution (e.g., inheritance).

Non-Employment Income — Investment- or Asset-Related *(Continued)*

Dividends and Interest

Two-year history
required and income must
continue for three more
years.

Earning generated from
investments such as
savings accounts and
certificates of deposit, or
stock ownership.
Considered income for that
tax year rather than a
capital gain.

Employment- Related Assets

Income calculation = $\text{Balance} - (\text{Penalties} + \text{market fluctuation considerations} + \text{monies used for mortgage}) / \text{Mortgage term}$.

Monthly income stream
calculated using
employment-related assets
(severance package,
retirement package/
account that borrower has
full access to, and
distributions are not set up.

Non-Employment Income — Benefit-Related

Disability

Benefit from a disability policy. Borrower's disability benefit eligibility, amount, payment frequency must be determined.

Contract termination/modification date must be beyond three years. Long-term disability usually does not have defined expiration date.

Mortgage Credit Certificate

State or local government certificate that allows a tax credit for mortgage interest. Not a tax deduction.

Mortgage lender will often use the estimated amount of the credit on a monthly-basis as additional income to help the potential borrower qualify for the loan.

Non-Employment Income — Benefit-Related *(Continued)*

Public Assistance

Acceptable source of qualifying income when it continues for three or more years. Paying agency letters/exhibits stating amount, frequency and duration of benefit payment required.

Program designed to help needy families achieve self-sufficiency. Often referred to as Temporary Assistance for Needy Families (TANF).

Housing Choice Voucher Program

Acceptable source of qualifying income that does NOT require history of receipt or payment evidence. Copy of voucher must show monthly payment amount and whether it is non-taxable.

Federal government program assisting very low-income families, the elderly, and the disabled to afford housing. Also known as Section 8 (named for Section 8 of the U.S. Housing Act of 1937).

Non-Employment Income — Rental

Rental Income

Income received for renting either a residential or commercial property. Subject property can be a 2-4 unit primary residence or 1-4 investment property.

Review Schedule E of tax return when property has history of generating rental income. A lease can be used for newly acquired/rented properties.

Boarder Income

Income received from boarders/roommates renting shared living space in the principal residence or second home. **Acceptable ONLY** when (1) there is a live-in personal assistant to a borrower with disabilities, (2) Fannie Mae's HomeReady program.

Personal assistants (can be a relative of borrower) are typically paid by Medicaid waiver Funds. Rental payments can be considered as acceptable stable income in an amount up to 30% of total gross qualifying income.

Non-Employment Income — Retirement

Retirement Accounts

Post-retirement pay received from employer in the form of distributions from asset accounts, e.g., 401(K), individual retirement account, Keoghs, simplified employee pension.

Asset-based distribution accounts must have sufficient funds for the distributions to continue for three more years.

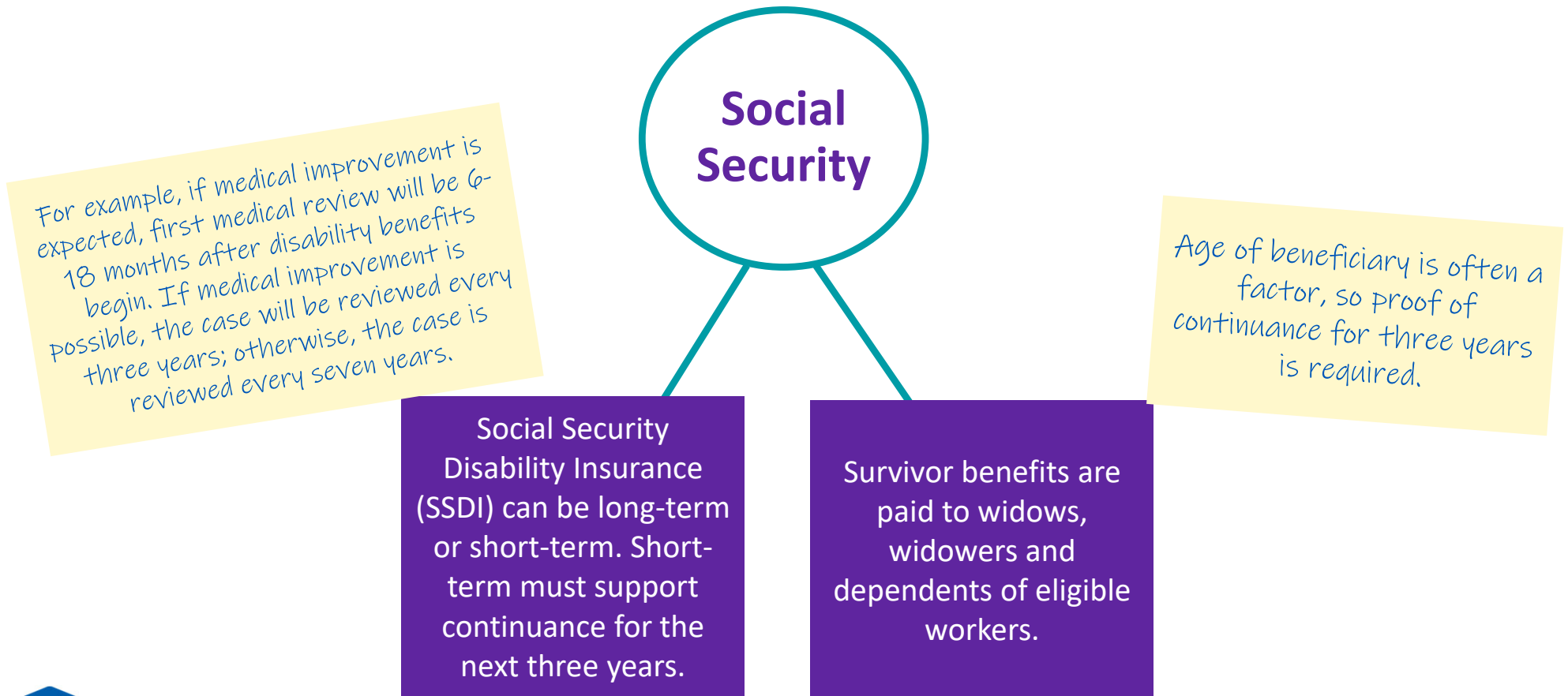
Continuance is typically not required.

Retirement income can also be in the form of a traditional pension. Corporate and government pensions continue for the lifetime of the recipient.

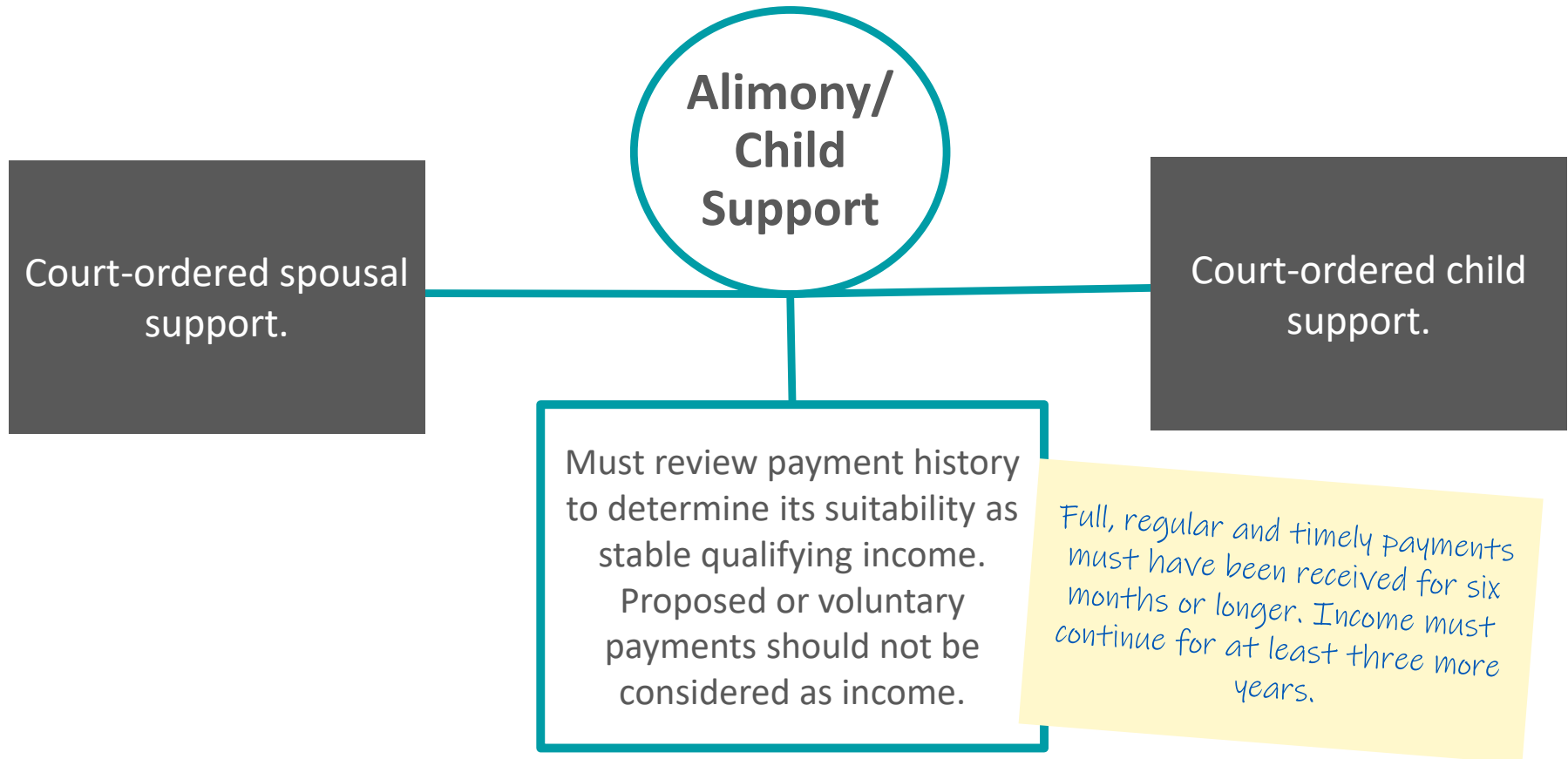
Pension

Non-Employment Income — Social Security *(Continued)*





Non-Employment Income — Alimony/Child Support



Knowledge Check Two

Is the following **True** or **False**?

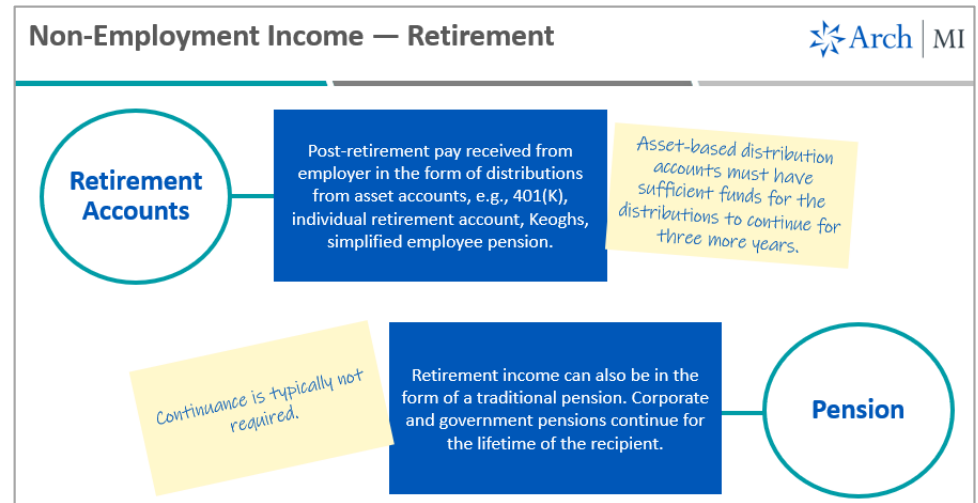
- All retirement and pension accounts require documentation to prove the distributions will continue for three more years.



Check Your Understanding Two

The correct answer is **False**.

- *Asset based distribution retirement accounts must have sufficient funds for the distributions to continue for three more years.*
- *Pension funds typically do not require continuance.*

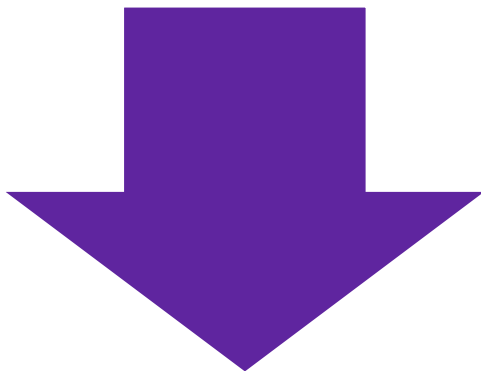


Income Continuance





Sometimes, you must **prove** continuance of Qualifying Income.



Other times, you can **assume** continuance of Qualifying Income.

Three Years Continuance (?)



Expiration date is **NOT** defined.

Proof of Continuance **NOT** Required.

Evidence of Ability to Continue is Required.

Dependent upon the Depletion of an Asset.

Expiration date **IS** defined.

Proof of Continuance **IS** Required.

Evidence of Ability to Continue is Required.

Other

Expiration Date Is NOT Defined

DO NOT
need to
document a
three-year
continuance.

Automobile allowance.

Base salary.

Bonus, overtime, commission, or tip income.

Corporate retirement or pension.

Long-term disability income.

Military income (including Base Pay, BAH and BAS).

Mortgage Credit Certificates.

Part-time, second job or seasonal income.

Rental income.

Social Security, VA or other government retirement.

Expiration Date IS Defined

MUST
document a
three-year
continuance.

Alimony or child support.

Mortgage differential payments.

Notes receivable.

Public assistance.

Royalty payments.

Social Security (not including retirement or long-term disability).

Trust income.

VA benefits (not including retirement or long-term disability).

Dependent Upon Depletion of an Asset

MUST
document
ability of a
three-year
continuance.

Interest income.

Dividend income.

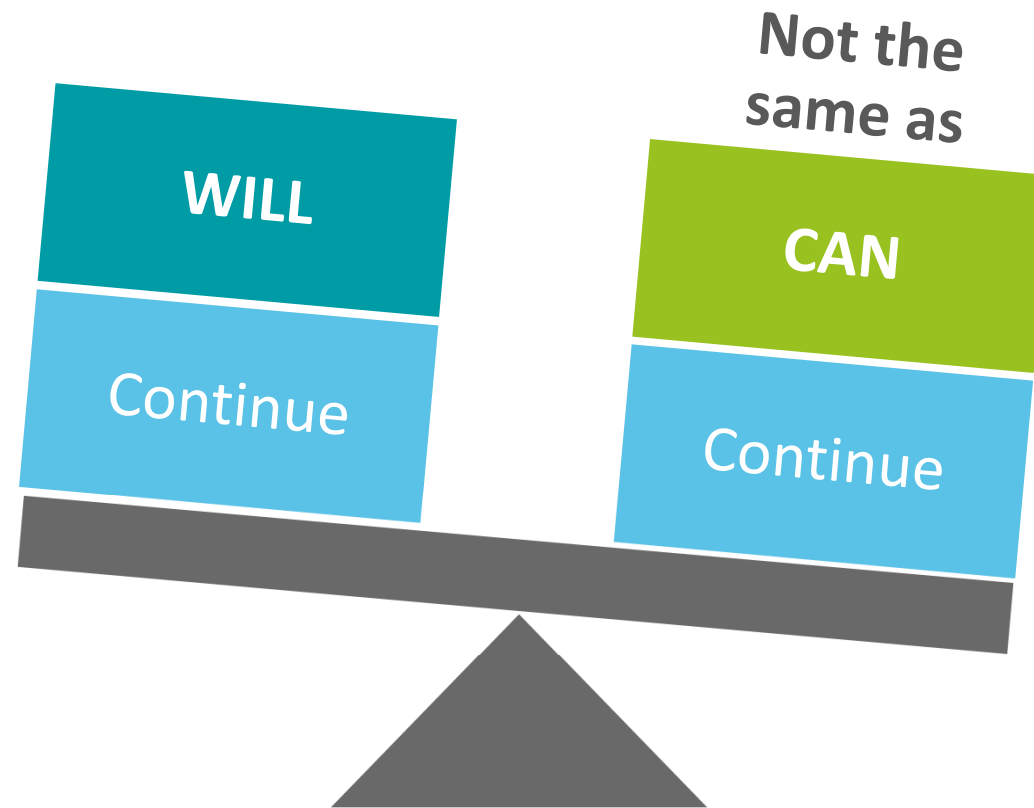
Employment-related asset depletion.

Distributions from retirement accounts (401(K), IRA, Keogh, SEP).

MUST
document
ownership of
additional
property or
assets.

Capital gains.

Continuance: Will vs. Can



Knowledge Check Three

Is the following **True** or **False**?

- You must ALWAYS prove continuance of Qualifying Income.




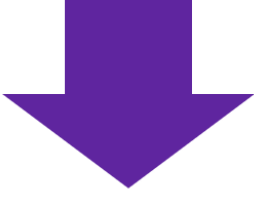
Check Your Understanding Three

The correct answer is **False**.

- *Sometimes you must prove continuance of Qualifying Income and other times, you can assume continuance of Qualifying Income.*

Continuance Arch | MI

 Sometimes, you must **prove** continuance of Qualifying Income.

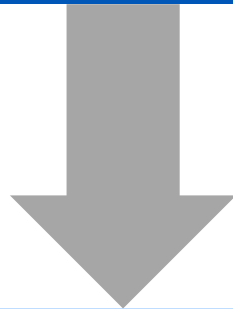
 Other times, you can **assume** continuance of Qualifying Income.

Taxable vs. Non-Taxable



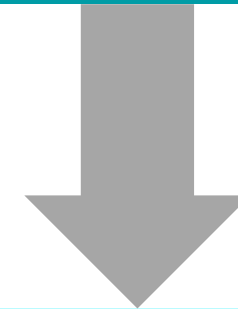
Non-Taxable Income

Taxable



\$4,000 Gross
\$3,000 Net

Non-Taxable



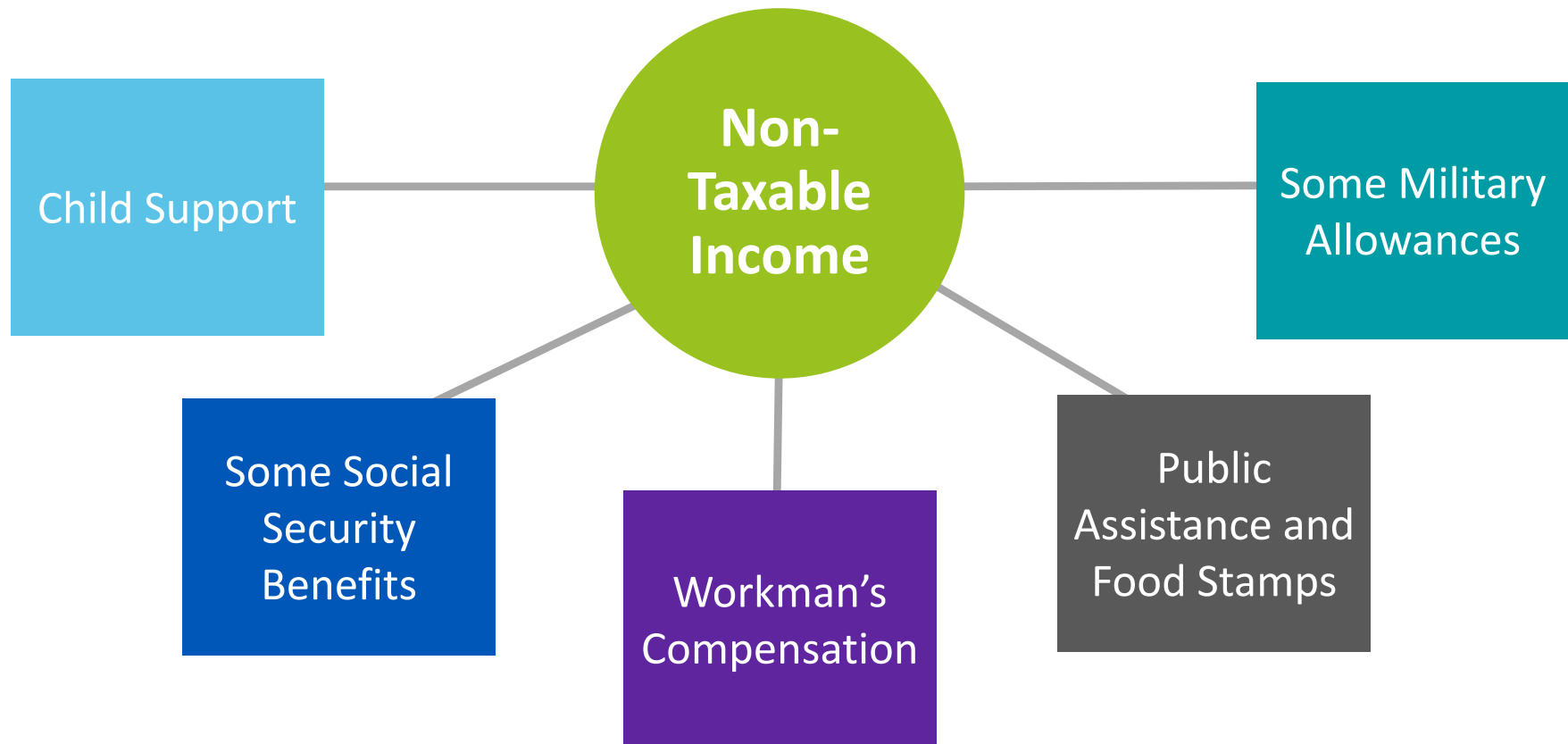
\$4,000 Gross
\$4,000 Net

Grossing Up Income

Standard Factor of 25%

$$\$4,000 \times 125\% = \$5,000$$

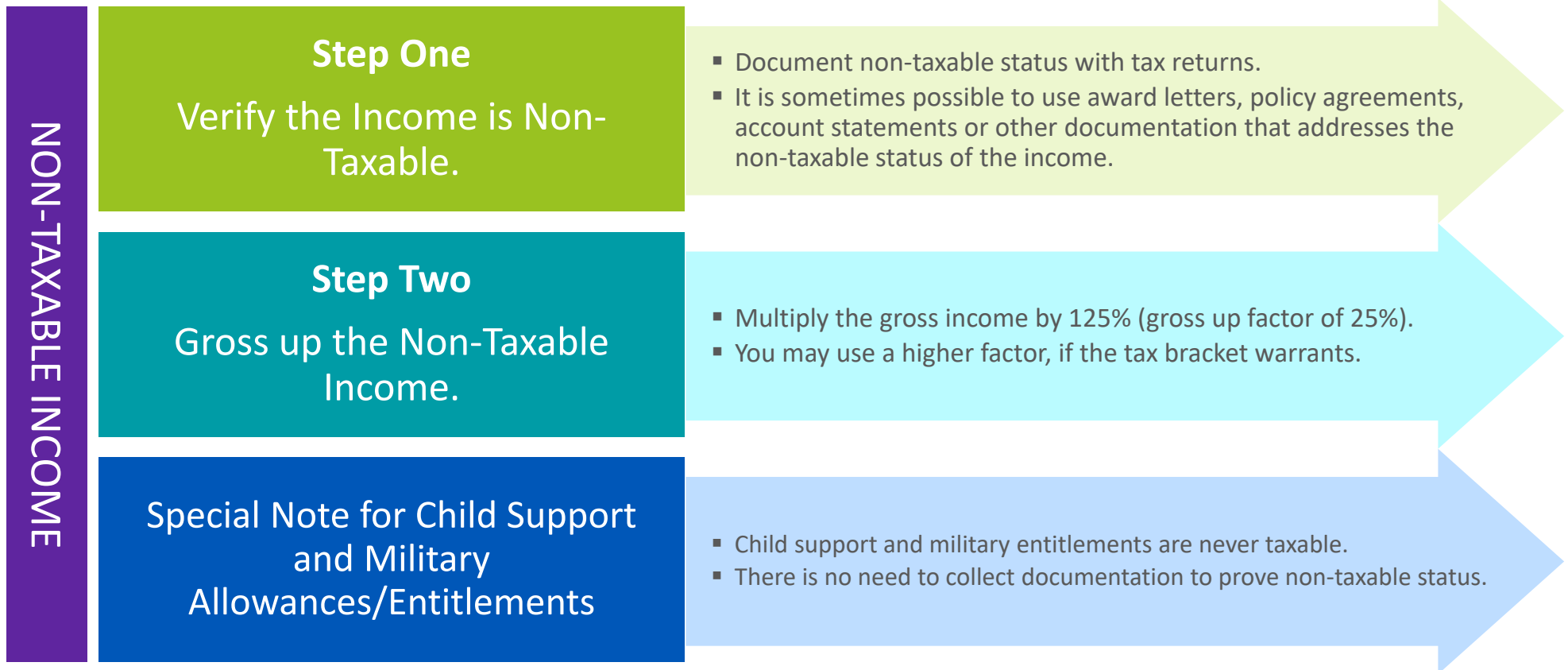
Non-Taxable Income



Non-Taxable Income

Income							
Attach Form(s) W-2 here. Also attach Forms W-2G and 1099-R if tax was withheld. If you did not get a Form W-2, see instructions.	1a	Total amount from Form(s) W-2, box 1 (see instructions)		1a			
	b	Household employee wages not reported on Form(s) W-2		1b			
	c	Tip income not reported on line 1a (see instructions)		1c			
	d	Medicaid waiver payments not reported on Form(s) W-2 (see instructions)		1d			
	e	Taxable dependent care benefits from Form 2441, line 26		1e			
	f	Employer-provided adoption benefits from Form 8839, line 29		1f			
	g	Wages from Form 8919, line 6		1g			
	h	Other earned income (see instructions)		1h			
	i	Nontaxable combat pay election (see instructions)		1i			
	z	Add lines 1a through 1h		1z			
	Attach Sch. B if required.	2a	Tax-exempt interest	2a		b Taxable interest	2b
3a		Qualified dividends	3a		b Ordinary dividends	3b	
Standard Deduction for— • Single or Married filing separately, \$12,950 • Married filing jointly or Qualifying surviving spouse, \$25,900 • Head of household, \$19,400 • If you checked any box under Standard Deduction, see instructions.	4a	IRA distributions	4a		b Taxable amount	4b	
	5a	Pensions and annuities	5a		b Taxable amount	5b	
	6a	Social security benefits	6a	24,972	b Taxable amount	6b	13,798
	c	If you elect to use the lump-sum election method, check here (see instructions)		<input type="checkbox"/>			
	7	Capital gain or (loss). Attach Schedule D if required. If not required, check here		<input type="checkbox"/>	7		
	8	Other income from Schedule 1, line 10			8		
	9	Add lines 1z, 2b, 3b, 4b, 5b, 6b, 7, and 8. This is your total income			9		
	10	Adjustments to income from Schedule 1, line 26			10		
	11	Subtract line 10 from line 9. This is your adjusted gross income			11		
	12	Standard deduction or itemized deductions (from Schedule A)			12		
	13	Qualified business income deduction from Form 8995 or Form 8995-A			13		
	14	Add lines 12 and 13			14		
	15	Subtract line 14 from line 11. If zero or less, enter -0-. This is your taxable income			15		

—	24,972
—	13,798
—	11,174
×	11,174
×	125%
—	13,968
+	13,798
+	13,968
—	27,766



Acceptable or Unacceptable?



Can you document it?

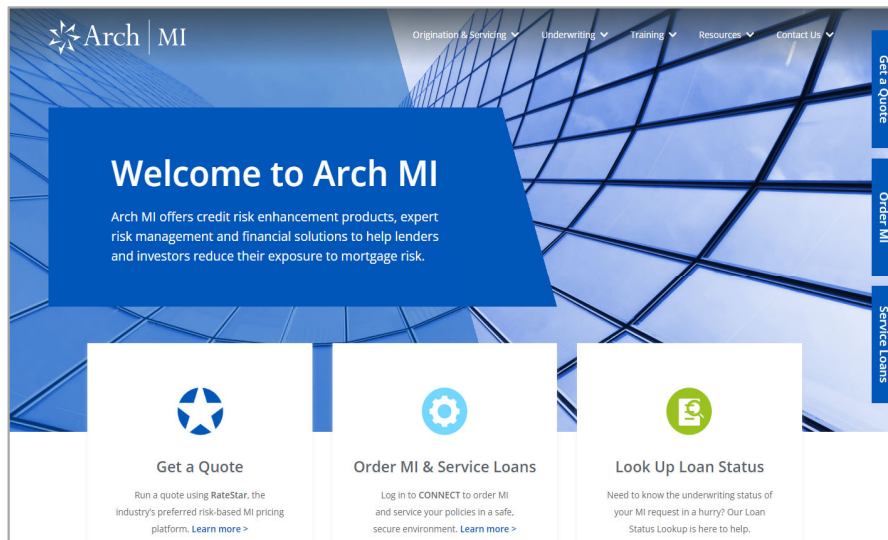
Is there a history?

Is it likely to continue?

Resources



ArchMI.com for Mortgage Lenders



The screenshot shows the ArchMI.com homepage for mortgage lenders. The header includes the Arch MI logo and navigation links: Origination & Servicing, Underwriting, Training, Resources, and Contact Us. A blue banner reads "Welcome to Arch MI" and states: "Arch MI offers credit risk enhancement products, expert risk management and financial solutions to help lenders and investors reduce their exposure to mortgage risk." A vertical sidebar on the right contains links for "Get a Quote", "Order MI", and "Service Loans". The main content area features three white cards: "Get a Quote" (with a star icon), "Order MI & Service Loans" (with a gear icon), and "Look Up Loan Status" (with a document icon). Each card includes a brief description and a "Learn more" link.

ArchMICU.com for Credit Unions



The screenshot shows the ArchMICU.com homepage for credit unions. The header includes the Arch MI logo, a "For Credit Unions" tag, and navigation links: Origination & Servicing, Underwriting, Training, Resources, and Contact Us. A teal banner reads "Welcome to Arch MI" and states: "Arch MI offers credit risk enhancement products, expert risk management and financial solutions to help lenders and investors reduce their exposure to mortgage risk." A vertical sidebar on the right contains links for "Get a Quote", "Order MI", and "Service Loans". The main content area features three white cards: "Get a Quote" (with a star icon), "Order MI & Service Loans" (with a gear icon), and "Look Up Loan Status" (with a document icon). Each card includes a brief description and a "Learn more" link.



THANK YOU

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