13.2.11 Subordination financing

For HELOCs, count monthly payment amount. If there is none, use current balance with current rate and current payment as detailed on the HELOC agreement or note. If interest only payment will change to fully amortized payment within 3 years, fully amortized payment for amortization period must be used to qualify. For example, if a HELOC only has 2 years of interest only payments remaining and will then change to a fully amortized payment for 15 years, the 15-year amortization period will be used at current rate to qualify.

14 Property Eligibility and Project Eligibility

14.1 Eligible Property Types

14.1.1 Single Family Residence (SFR)

An attached or detached single-family dwelling, including town homes and row homes.

14.1.2 Two-to-Four (2-4) Unit Property

A two-to-four unit property is a residential structure with more than one unit but not more than four units.

14.1.3 Planned Unit Development (PUD)

A PUD is a real estate project in which each unit owner has title to a residential lot and building and a nonexclusive easement on the common areas of the project. The owner may have an exclusive easement over some parts of the common areas (e.g., parking space).

14.1.4 Condominium

A condominium is a unit in a project in which each unit owner has title to their individual unit, an undivided interest in the project's common areas, and in some cases, exclusive use of certain limited common areas. A condominium project is created according to local and state statutes. The structure is two or more units with the interior airspace individually owned. The balance of the property (land and building) is owned in common by the individual unit owners.

For additional PUD/Condo requirements, see Project Eligibility section.

14.2 Ineligible Properties

- Vacant land or land development properties Properties that are not readily accessible by roads that meet local standards
- Agricultural properties, such as farms or ranches
- Boarding Houses
- Bed and breakfast properties
- Properties that are not suitable for year-round occupancy regardless of location
- Manufacture homes
- Mobile homes
- Properties in non-residential zoning
- Mixed use properties
- Title to the property not held as fee simple (leasehold)
- Co-Operatives

14.3 Condominium/PUD Project Eligibility & Review

All condominium & attached PUD projects require a Homeowners Association (HOA) Questionnaire. For LTV less than or equal to 50% on established condominiums, a limited HOA Questionnaire will be acceptable. For all other condominium loans including new construction, a full HOA Questionnaire must be completed. The completed questionnaire must confirm that the condo project is eligible.

14.3.1 Maximum Loan Concentration

The maximum number of loans that the NEXCAP may extend in a condominium or attached PUD project may not exceed 20% of the total units in the project.

14.3.2 New Condo Project

A new condo project is a project for which one or more of the following is true:

- fewer than 90% of the total units in the project have been conveyed to the unit purchasers;
- the project is not fully completed, such as proposed construction, new construction, or the proposed or incomplete conversion of an existing building to a condo;
- the project is newly converted; OR
- the project is subject to additional phasing or annexation

At least 70% of the total units in the project or subject legal phase must have been conveyed or be under contract for sale. At least 50% of the total units in the project must have been conveyed or be under contract for sale to principal residence or second home purchasers when subject is an investment property.

14.3.3 Ineligible Attached/Detached Condo & Attached PUD Projects

The following types of condominium projects are ineligible:

- Projects that contain commercial space exceeding 50%.
- Timeshare or segmented ownership projects.
- Manufactured homes.
- Condo-hotel.
- Houseboat projects.
- Projects that represent a legal, but non-conforming use of the land, if zoning regulations prohibit rebuilding the improvements to current density in the event of their partial or full destruction.
- Projects involved in any type of litigation
- Projects with owner-occupied occupancy ratio less than 50% when subject is investment property.
- Projects with more than 15% of the condo association dues delinquent.
- Projects that contains 8+ units with single entity owning more than 30% of the entire project.
- Projects that contains equal or less than 8 units with single entity owning more than 50% of the entire project.
- Projects subject to resale restrictions. (Age restriction is exempted for senior condo)
- Lender is liable for more than 6 months delinquent common charges.
- Lender is liable for more than 6 months for any delinquent common charges when a unit is taken over in Deed-In-Lieu or foreclosure.

- HOA owns or operates any non-incidental business operation.
- High Rise condominium project in Nevada: Due to the unknown risks surrounding super priority lien status in Nevada State Law NRS 116.3116, high rise condominiums in Nevada are not eligible at this time. Detached/attached condominiums in Nevada are acceptable.

15 Appraisal

NEXCAP requires an appraisal report for all residential mortgage loans. The purpose of valuation or appraisal review is to determine if a loan is secured by property that provides sufficient value to recover the investment if loan default occurs. Establishing the adequacy of the collateral for an investment quality loan requires an accurate assessment of the current fair market value and condition of the property. The appraiser must address any factors likely to affect the property's future value and provide a visual picture of the neighborhood, site, and improvements. The appraiser must use the comments section of the report to achieve this goal and attach additional documentation if necessary.

15.1 Appraiser Requirement

The appraiser must remain free of any outside influence in the valuation process. Appraisers must provide complete and accurate reports. The estimate of market value must represent the appraiser's professional conclusion, based on market data, logical analysis, and judgment.

15.2 Age of Appraisal

The effective date of the appraisal report must be dated within 120 days of the Note date. If the effective date of the appraisal report is more than 120 days but less than 180 days from the Note date, the appraiser must provide an update to the appraisal based on his or her knowledge of current market conditions. The appraiser must acknowledge that the value of the subject property has not declined since the effective date of the original appraisal. The update must be completed on Fannie Mae Form 1004D/Freddie Mac Form 442 and must be dated within 120 days prior to the Note date.

15.3 Appraisal Types

NEXCAP will accept the following types of appraisal forms:

- Uniform Residential Appraisal Report: (Fannie Mae 1004 / Freddie Mac 70)
- Individual Condominium Unit Appraisal Report: (Fannie Mae 1073 / Freddie Mac 465)
- Small Residential Income Property Appraisal Report (Fannie Mae 1025 / Freddie Mac 72)
- Appraisal Update or Completion Certificate (Fannie Mae 1004D / Freddie Mac 442)

15.4 Appraisal Review & Evaluation

As the underwriter evaluates a file to determine its eligibility for a loan, he/she considers the collateral property's marketability and justification of its value. Factors that affect marketability and value include the comparability of the subject property with surrounding structures and land use, condition and appeal of the property, quality of construction and equipment, characteristics of design, and the local home market real estate trends.

Information regarding these factors is documented on the appraisal, most inclusively on the Universal Residential Appraisal Report (URAR). There are three approaches generally used by the appraiser to establish value. These are the cost approach, the sales comparison analysis/market value analysis (market approach), and the income approach. For residential properties of 1-4 units, the market and cost approaches are the appraisal methods most widely used so therefore NEXCAP only accepts values based on these two approaches.

All residential appraisals and Evaluation reports should be made on an “as is” basis unless:

- The appraisal is made “subject to” repair alterations and/or conditions, which the appraiser lists in the comment section or by addendum.
- The property and appraisal is “subject to completion per plans and specifications.”

In both cases above, the appraiser must make a subsequent inspection of the subject and verify that such repairs, alterations or construction have been completed as represented in the appraisal, and the appraiser must complete an Appraisal Update and/or Completion Report (Fannie Mae Form 1004D/Freddie Mac Form 442) to verify compliance with his or her original appraisal conditions. A photograph attachment showing completion should be attached. When the appraiser makes the appraisal “subject to” any repairs, the repairs must be a requirement of loan approval. The repair work must be completed prior to funding, unless part of the approval funds is to be withheld to cover the cost of the repairs. Proof of completion of such repairs must be in writing in the funding, signed and dated by the appraiser.

15.4.1 Property Location

Rural properties may require additional analysis due to lack of available comparables and limited utilities and services. Any “fair” or “poor” ratings regarding the subject neighborhood should be explained.

15.4.2 Property Values

Declining property values represent higher, possibly unacceptable risk because of the potential for a loss in borrower equity. The rate of decline is a key factor.

15.4.3 Demand/Supply (Marketability)

An oversupply of housing units—within a neighborhood or citywide—may reflect problems with marketability. The reason for an oversupply and its effect on the property’s value requires explanation from the appraiser.

15.4.4 Occupancy

High-vacancy rates or an abundance of tenant occupants indicates that the neighborhood may be oriented to rental rather than owner-occupied housing.

15.4.5 Predominant Value

A property whose value falls outside the neighborhood price range or is at the extreme high or low end of the range may be a higher-risk property. Compatibility should be supported by use of similar properties from the same neighborhood and explained by the appraiser.

15.4.6 Land Use and Land Use Change

A strong residential base is important to overall neighborhood desirability.

Non-compatible land use (for example, a high percentage of commercial or industrial land usage) could negatively affect marketability. Change in land usage can have a significant effect, positively or negatively, on the long-range value of the property and requires explanation from the appraiser.

15.4.7 Neighborhood Comments

Factors that affect the marketability of the properties in the neighborhood, such as proximity to employment and amenities and employment stability and appeal to the market, require an explanation from the appraiser. Analysis could include economic trends, location influences and neighborhood amenities.

15.4.8 Market Conditions

Market conditions and trends should be supported by statistical information.

15.4.9 Zoning Compliance

The property should be zoned as "residential." Highest and best use as improved should be the "Present use." Properties with commercial zoning should exhibit no negative impact on marketability or habitability as residential properties and should not change the residential character or atmosphere of properties. The majority of the uses on the Subject Property's street must also be 1-4 family and at least two of the comparable sales must be from the Subject Property's immediate neighborhood and have the same zoning. Properties with agricultural zoning must be verified that property is residential in nature, its residential use is a permissible use under the zoning classification and its use does not primarily involve commercial activities such as farming or ranching. Residential properties with commercial and agricultural zoning should reflect the current usage as the highest and best use and be eligible to be rebuilt in the case of partial or total destruction and 100% rebuild letter from the city/county required.

15.4.10 Utilities

The source and type of all utilities should be identified. Utilities which are not typical for the area increase risk.

15.4.11 Off-site Improvements

Private road maintenance should be identified. If the condition or adequacy of a private road is not typical, an explanation is required.

15.4.12 Drainage/Flood Hazard

Drainage problems or the existence of a flood hazard condition require explanation from the appraiser. Such conditions or major problems may require physical correction or flood hazard insurance.

15.4.13 Site Comments

Adverse site conditions, including adverse easements, encroachments, or special assessments may affect the value or marketability and require explanation by the appraiser.

15.4.14 Improvements

A property's physical features should be most like other similarly sized dwellings in the market. If characteristics are not similar—for example, a room list that is not typical for the market, or heating that is unusual or not in good condition—they may affect market appeal. The affect the non-conformity has on value and marketability requires explanation from the appraiser. Construction components and special features should be similar to other properties in the marketplace. Amenities that do not meet market expectations may negatively affect marketability.

15.4.15 Condition of Improvements

Property improvements should be at least in average condition and should not negatively affect the livability or marketability of the property. Minor cosmetic deficiencies are not a major concern. The condition of the major components, including the roof, foundation, plumbing, electrical, and heating, may be an issue. Incurable structural factors that are not typical for the market—for example, a room list that is unusual or location of rooms that is not typical—may decrease the value and market acceptance of the property. Curable structural factors may be acceptable under certain conditions when properly justified.

Homes with energy efficiency improvements are eligible when marketability can be justified through comparable sales, and any additional cost is supported by the market. NEXCAP underwrites these properties based on the evaluation of the individual loan and does not generally have special documentation requirements or ratio guidelines for energy efficient properties except for Solar Panels.

For properties with solar panels, copy of purchase contract or lease agreement for solar panel must be reviewed to determine if there is any recurring monthly payment. Any monthly payment must be included in debt-to-income calculation. If solar panel contract is recorded as a lien against subject property, it cannot be in a first lien position. For purchase transaction, if borrower assumes the existing solar panel contact from the current owner/seller, assignment of lease or similar documents must be reviewed to determine the term and validity of transfer.

15.4.16 Adverse Environmental Conditions

Environmental items that have a negative effect on value—such as proximity to a hazardous waste site—must be identified and fully explained. Comparables should have similar environmental conditions. Generally, properties with material environmental hazards are ineligible for a loan. The effects of such hazards on the safety, value, and marketability of the property make it unacceptable collateral for low down payment lending. NEXCAP may require removal of such hazards as a closing condition

15.4.17 Property Condition and Quality of Construction of the Improvements

The Condition and Quality ratings must be based on a holistic view of the property and any improvements. When selecting the Condition and Quality ratings, an appraiser must:

- Consider all improvements to determine an overall Condition and Quality rating. The appraiser should select the rating that best reflects the property as a whole and in its entirety.
- Describe the subject property as of the effective date of the appraisal on an absolute basis, meaning the property must be rated on its own merits. The rating should not be selected on a relative basis, meaning it is not selected on how the property relates or compares to other properties in the neighborhood. Additionally, the Condition and Quality ratings for comparable properties must be made on an absolute basis, not on a relative basis, and reflect the property as of the date of sale of that comparable property.
    - Note: These requirements also apply to all other ratings or descriptions, including the View and Location

When an appraiser selects a rating and/or description of the subject property for a sales transaction, the selected rating and/or description must remain the same when reflecting that specific transaction. For example, if a C4 rating is selected for the sale of the subject property, then that property remains a C4 when using that specific sale as a comparable in future reports. The same expectation holds true for ratings and descriptions of comparable sales. When a comparable is used in a subsequent appraisal, the ratings and descriptions of that property should not change from one appraisal to the next when it reflects the same sale transaction.

- Note: Properties can have the same rating or description and still require an adjustment. It should be noted that this does not only apply to Conditions and Quality ratings and can apply to other ratings or descriptions as well. For example, all water views may not be equal. In this instance, an adjustment should be made and explained in the Additional Comments section of the form in an addendum.

Acceptable Property Condition and Quality Ratings are as follows:

- Condition Rating Range: C1 – C5
- Quality Rating Range: Q1 – Q5

15.4.18 Cost Approach

The cost approach is one of the ways an appraiser comes up with the final value of a home. The following applies to the cost approach method:

- **Site value:** The proportion of site value to the value of the residence must be in line with other values in the neighborhood. A property with a site value higher than the area norm may be considered a higher-risk property.
- **Estimated reproduction cost:** The estimated reproduction cost per square foot should not be higher than the area norm.
- **Depreciation:** The appraiser must make adjustments for physical, functional, and external depreciation when appropriate.

15.4.19 Sales Comparison Analysis/Market Value Analysis

Another method used by the appraiser to come to a final value of a home. The following applies to the sales comparison approach:

- **Comparable sales:** A minimum of 3 comparable sales is required for the market value analysis. Comparables should be similar to the subject property in size, room count, location, condition, etc. Comparable sales generally should have closed within 6 months of the appraisal date.
- **Location of comparables:** Except for rural locations, 2 of the 3 required comparables should be located within 1 mile of the subject property. Beyond that, an appraiser's explanation is required. Comparables for rural properties may fall outside the 1 mile range; therefore, it's important that the comparables be from locations that have the same influences, such as distance from schools, shopping, and employment Departments.
- **Source of comparables:** No more than 1 of the 3 comparables may be supplied by the lender or developer from its own files, unless justified by the appraiser. The 3 comparables must be closed sales, not listings. As alternatives, listings, offers and contracts can help support value; however, they may not accurately reflect market value since the details of the transaction could change prior to closing.
- **Adjustments:** Adjustments must be logical. The size of the adjustments indicates the extent of differences between the comparables and the subject property. Large adjustments should be fully explained. Large adjustments for site/view, design and appeal, quality of construction, age, or condition may be an indication that the comparables are not really comparable. Adjustments must be consistent for all comparables. Total net adjustments for any comparables used should not exceed 15% of the sales price. Total gross adjustments should not exceed 25%. Individual line adjustments for comparables should not exceed 10% of the sales price. If any of the net, gross, or individual line adjustments exceed these thresholds (15%/20%/10% respectively), the appraiser must address the adjustment, explain reason for use of comparable, and confirm comparable is the best available. One-directional adjustments will also need further explanation. Property value may be inflated when all of the comparables are significantly superior or inferior to the subject property. When all of the adjustments are positive or all negative, the valuation may be questionable.
- **Personal property/options:** Furniture, fixtures, and other personal property cannot be included in the market value of the property. Additional builder options on newly constructed properties should be reviewed and considered. For example, if the subject has $5,000 in options, such as upgraded wall coverings, carpeting and built-ins, the appraiser must evaluate that the costs of these items are truly reflected in the resale market. Often the options do not recapture dollar-for-dollar cost in market value. At least,

1 comparable sale should have options or extras similar to the subject's.

- **Prior sales activity:** The appraiser must identify and describe prior sales activity for the most recent 12 months for the subject and the comparables. Adverse value trends need to be identified and explained.

15.4.20 Changes to the Appraised Value

Particular attention and extra due diligence must be instituted for those loans in which the appraised value is believed to be excessive or when the value of the property has experienced significant appreciation in a short time period since the prior sale. Any appreciation within 12 months greater than 20% of the previous sale value, will require additional explanation from the original appraiser. If the appreciation occurred in under 6 months, a Field Review will be required.

15.4.21 Final Value

Final value must reflect the most reliable sales data, not an average of comparable.

15.5 Additions without Permits

If the appraiser identifies an addition(s) that does not have the required permit, the appraiser must comment on the quality and appearance of the work and its impact, if any, on the market value of the subject property.

15.5.1 Attached Un-Permitted Additions

When reviewing a property with an attached un-permitted addition, the appraiser should address and comment on the following items:

- Describe the un-permitted work and whether is it common for the area.
- Is there a health or safety issue?
- Does zoning permit the type of work that was done?
- Was value given to the un-permitted addition? If value is given, it must be supported by comps.
- What is the effect of the un-permitted addition on the marketability of the property?
- If a permit was required for the work done, state what the consequences/penalties of not having obtained a permit for the work are.

15.5.2 Detached Un-Permitted Additions

When reviewing a property with a detached un-permitted addition or accessory dwelling unit that does not comply with zoning, the property may be eligible if the appraiser and/or lender address and comments on the following items:

- The current use conforms to the subject neighborhood and to the market.
- The property is appraised based upon its current use.
- The appraisal must report that the improvements represent a use that does not comply with zoning.

15.6 Third Party Appraisal Review

NEXCAP will utilize **AVM** to validate the value of the property. If the AVM is failed, the seller must order an appraisal desk review product for each loan from a vendor listed on the Approved Appraisal Desk Review Vendors.

- CDA report from Clear Capital
- ARR from ProTeck
- ARA from Computershare

A copy of the appraisal desk review report should be submitted in the loan file. The review must not be over 120 days old from the date of the Note.

If the desk review produces a value in excess of a 10% negative variance to the appraised value, the loan is not eligible for purchase; provided, the seller has the option to then ask the NEXCAP to order a Field Review to support the appraised value. If the field review also produces a value in excess of a 10% negative variance to the appraised value, then the loan will remain ineligible for purchase.

All appraisals are reviewed for eligibility as well as value support. However, the use of an appraisal review product does not relieve the seller of its representations and warranties relating to the property and the appraisal including the underwriting thereof.

15.7 Home Equity Combined Loan-to-Value (HCLTV)

The HCLTV is calculated by adding the first lien amount to the combined total of the junior liens. (adding the outstanding balance of loans, the remaining balance of lines in repayment without ability to make new draws, and the greater of the line amount or outstanding balance for lines of credit that are active where the borrower continues to have the ability to make new draws). When a junior lien is present, payment must be included when calculating the qualifying ratios, and the HCLTV must not exceed program guidelines.

15.8 Value Seasoning

If borrower has less than 12 months ownership in the property, LTV/CLTV is calculated on the lower of the purchase price or appraised value. If the borrower has owned property for more than 12 months, LTV/CLTV is based on the appraised value.

15.9 Loan Amount

The maximum loan amount is contained in the applicable product eligibility matrix.

15.10 Insurance Requirements

15.10.1 Flood Insurance

Flood insurance consistent with standard Fannie Mae/Freddie Mac requirements must be in place.

15.10.2 Hazard Insurance

Hazard insurance consistent with standard Fannie Mae/Freddie Mac requirements must be in place.

15.10.3 Title Insurance

Title insurance consistent with standard Fannie Mae/Freddie Mac requirements must be in place.

16 Legal and Regulatory Requirements

Loans must be originated in accordance with applicable federal, state, and local laws and regulations.

17 Age of Documentation

Credit Documentation: All credit documentation must be dated within 90 days of closing.

Asset Statements: The most recent asset statement to verify the source of funds or reserves must be dated no more than 45 calendar days earlier than the date of the loan application, and not more than 90 days earlier than the date of the Note. Quarterly statements are permissible.

Income Documentation: No income document should be included in the loan file.

CPA letter/Verification of Employment: no more than 90 days of closing.

Appraisal: Eligible appraisals must be dated within 120 days from the Note date.

Title & CPL: Eligible Title & CPL must be dated within 90 days of closing.

18 Additional Requirements

18.1 Escrow Waivers

- Property tax and insurance escrows may be waived.
- Individual state laws may supersede this requirement.

18.2 Escrow Holdback

Escrow Holdback is not eligible.

18.3 Section 32: High-Cost Loans

High-cost loans (Section 32) as defined by applicable state and/or local regulations are not permitted.

18.4 Section 35: Higher Priced Mortgage Loan (HPML)

NEXCAP will purchase loans that are defined as HPML only if all of the requirements listed below are met along with applicable product guidelines;

- QM Points and Fees audit must pass
- Escrows/Impounds are required for property taxes and homeowner's insurance (including flood insurance)
- All federal and state guidelines are met

Use the FFIEC Rate Spread Calculator to help determine Higher Priced Mortgage Loan (HPML) status: https://www.ffiec.gov/ratespread/newcalc.aspx

The calculator requires: Lock-In Date, APR, and the fixed term of the mortgage (in years).

A loan is "higher priced" if:

- It is a first-lien mortgage (other than a jumbo loan) with an Annual Percentage Rate (APR) that exceeds the published Average Prime Offer Rate (APOR) at the time the APR is set (lock date) by ≥ 1.5 percentage points
- It is a first-lien jumbo loan with an APR that exceeds the APOR at the time the APR is set (lock date) by ≥ 2.5 percentage points

Property Flipping with HPML is Ineligible

- Limitations on HPML loans for resale transactions within 180 days
- When a second appraisal is required per the TILA HPML Appraisal Rule the loan is considered on a case by case basis

For principal residences where the price reflected in the buyer's purchase agreement is higher than the amount listed below compared to the seller's acquisition price, a second appraisal will be required.

The amounts are as follows:

- More than a 10% increase if the seller acquired the property in the past 90 days;
- More than a 20% price increase if the seller acquired the property in the past 91 to 180 days
- See the CFPB TILA HPML Appraisal Rule for exemptions from this requirement.

18.5 State Restrictions

Refer to eligible states at http://www.NEXCAPgroup.com/licensing
Texas refinance loans that must close under Section 50(a) (6) requirements are not eligible.

18.6 Legal Documentation

Available Fannie Mae security instruments, notes, riders/addenda, and special purpose documents can be utilized for loan documentation. In the case when Fannie Mae doesn't offer current documentation such as interest only, a document vendor should be utilized for forms.

18.7 Fraud Prevention

All loans are underwritten with fraud prevention and detection as part of the lending decision process. The following fraud prevention requirements are used for all transactions as applicable which include but are not limited to:

- Internal Fraud Prevention Tools (CoreLogicTM or FraudGuard® Reports).
- Ineligible Party List search requirements.
- Verbal Verification of Employment requirements.
- MERS search prior to closing.
- Internal settlement agent and title company approval process.
- Soft-pull credit report in compliance with Fannie Mae's LQI to determine if the borrower may have taken out new credit prior to closing.
- Originators are required to originate loans in compliance with all applicable federal, state, and local laws, rules, and regulations, including the USPAP and the FACT Act.

The Fraud Report is reviewed by the Underwriter at initial approval and again prior to issuing a clear to close if the report is more than 30 days old. All variances noted on the Fraud report must be reviewed and mitigated with comments and supporting documentation, if necessary, before the final clear to close can be issued.

Clearing Variances on Fraud Report: Underwriters must note how they mitigated the Moderate and High Risk Variances on the Fraud report by making notes on the report. Supporting documentation should be included in file before the final clear to close be issued.

FraudGuard® scores above 800 from CoreLogicTM require management review and approval by the Underwriting Manager in order to proceed with the loan.

Underwriters to confirm by reviewing the Fraud Tools, if any of the companies or individuals involved in the origination, underwriting, or servicing of the mortgage transaction are on any of the following lists:

- General Services Administration (GSA) Excluded Party List

- HUD Limited Denial of Participation List (LDP List)
- OFAC List
- Freddie Mac Exclusionary List

Regardless of the reason or the scope for the party being excluded, any party to the transaction included on either list will result in the loan being ineligible for delivery.

18.8 Pre-Funding Audit

NEXCAP strongly recommends but does not require that lender’s implement a pre- funding audit process (such as those prescribed by Fannie Mae and Freddie Mac) to improve loan origination quality.