

RD AN No. 4345 (1980-D)
March 28, 2008

TO: All State Directors
Rural Development

ATTENTION: Rural Housing Program Directors,
Guaranteed Rural Housing Specialists, and
Area Directors, and Area Specialists

FROM: Russell T. Davis
Administrator
Housing and Community Facilities Programs

SUBJECT: Single Family Housing Guaranteed Loan Program
Applicant Traditional and Nontraditional Credit History
Verification

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to elaborate upon the forms of credit history and current debt verifications acceptable for loans guaranteed under the Single Family Housing Guaranteed Loan Program (SFHGLP).

COMPARISON WITH PREVIOUS AN:

This AN replaces AN 4268 dated April 19, 2007. This AN further supplements RD Instruction 1980-D to clarify guidelines and standards for nontraditional credit history applicants.

EXPIRATION DATE:
March 31, 2009

FILING INSTRUCTIONS:
Preceding RD Instruction 1980-D

BACKGROUND:

An essential component to mortgage lending is to determine current debt payments a loan applicant is obligated to make, evaluate the applicant's credit history, and establish the applicant's willingness and ability to repay the additional credit obligation represented by the home mortgage loan.

Information lenders use to make applicant credit evaluations is typically obtained from one of the following sources:

- **In-File Credit Reports:** An in-file credit report is issued by one credit repository or credit reporting agency. It contains "as is" information as of the last date reported by the credit grantor subscribing or reporting to the credit repository. No information is updated or re-verified by the credit repository as a result of the mortgage credit inquiry. A minimum of two credit repository reports is required for Rural Development purposes.
- **Merged, Tri-Merged, or Multi-Merged Credit Reports (MMCR):** A MMCR is issued by a credit repository or consumer reporting agency and includes the in-file credit report information from at least two credit repositories. Merged credit reports are also known as tri-merge credit reports if the merged report contains in-file credit report information from three credit repositories (Equifax, Experian, and TransUnion).

The MMCR must identify all the credit repositories whose information was merged into the report. The credit information from each credit repository may be presented in its entirety on the MMCR, or the reporting agency may eliminate duplicate records through an automated merge process. Duplicate information need not be repeated. However, if the duplicate information is not exactly the same on each report, the MMCR must either repeat the information or include the most derogatory of the duplicate information that pertains to payment history and/or current payment status.

The MMCR, in effect, is an adaptation of the Residential Mortgage Credit Report (RMCR). Information supplied on an RMCR, which is not on a MMCR (i.e. income and employment verification), is obtained and verified independently by lenders under current procedures.

- **Residential Mortgage Credit Reports:** A RMCR contains merged credit information from at least two national repositories. The consumer reporting agency or bureau supplying the RMCR typically uses its best efforts to re-verify accounts directly with creditors. The consumer reporting agency also attempts to verify the applicant's employment and residence history. The consumer reporting agency interviews the applicants when the lender has incomplete information or when it discovers information that indicates the possible

existence of undisclosed credit obligations or public records.

NONTRADITIONAL CREDIT

The current mortgage market and ongoing evaluation of loan performance prompts Rural Development to provide guidance, which supplements RD Instruction 1980-D, for applicants who do not have a traditional credit history and rely upon nontraditional credit sources to qualify for a mortgage loan.

Nontraditional credit presents unique risk characteristics and possible misrepresentation challenges in accessing the borrower's ability and willingness to repay the proposed mortgage obligation.

A recent SFHGLP portfolio review of non-traditional credit loans and those with credit scores of 619 and below supports a thorough evaluation prior to extending mortgage credit:

- FICO score 619 and below:
 - * 17% of SFHGLP portfolio
 - * 39% of program losses
- No FICO score:
 - * 6% of SFHGLP portfolio
 - * 16% of program losses

Lenders may rely upon the following methods to verify nontraditional credit histories:

- Non-Traditional Mortgage Credit Reports (NTMCR): A NTMCR is designed to assess the credit history for borrowers without the types of trade references normally appearing on a credit report. NTMCRs are typically used for those prospective borrowers who have not yet established a credit history or who do not use traditional credit. A NTMCR may be used as a substitute for a RMCR or MMCR, for borrowers without a credit history through traditional credit grantors, or to supplement RMCR's or MMCR's that do not have sufficient traditional credit references reported. **A NTMCR may not be used to enhance the traditional credit history of borrowers with poor payment records.**

Rural Development will accept reports by various providers who develop bill payment histories, which may also include a score. Rental history, utility trade lines, and other non credit reporting debts may be verified through this third party service. The bill payment score is not a substitute for a FICO score, however it will lend credibility to the nontraditional tradelines verified.

While a NTMCR from a consumer reporting agency is preferred, a lender may develop its own nontraditional credit history for a proposed applicant. In either case, at least three (3) non-traditional credit references should be developed. The following guidelines are provided to assist lenders in creating their own nontraditional credit histories:

- Additional layers of risk are not advised for applicants who rely on nontraditional credit references.
- Payments made to relatives for credit sources (i.e. personal loans) are not eligible non-traditional credit references.
- Nontraditional credit may not be used to offset derogatory references found in the borrower's traditional credit information, such as late payments, collection accounts, and judgments.
- Rent or housing payment history should be given the most consideration when evaluating nontraditional credit histories. Cancelled checks or money order receipts over the past 12 months should be provided as proof of timely payment. Rental references from management companies with a payment history over the past 12 months may be used in lieu of cancelled checks.
- In addition to rent or housing payment history, a 12 month payment record from the following are acceptable sources lenders may verify to prove the applicant's ability and willingness to meet debt obligations:
 - Utility payment records (if utilities were not included in the rental payment) including gas, electricity, water, or telephone cell phone service, cable TV, etc.
 - Insurance payments (excluding those paid through payroll deductions) including medical, automobile, life, household, or renter's insurance
 - School tuition
 - Payments to retail stores (i.e. department, furniture, appliance stores, specialty stores, etc.)

Acceptable verification for proof of payment includes canceled checks, money order receipts, and written verification from independent third parties (not relatives). Written verification should include creditor name, date the account was opened, balance of that account, monthly payment, and payment history reported in 0x30, 0x60, etc. format. Subjective statements should not be used to verify payment history such as "satisfactory" or "acceptable".

- Only one 30 day delinquency is allowed on one nontraditional credit reference within the last 12 months

- 60 and 90 day delinquencies, and reports of disconnect notices are not acceptable

An additional non-traditional credit reference includes documenting the applicant's ability to make steady periodic savings deposits over a 12 month period accumulating a cash reserve of at least 2 months worth of housing expense payments.

IMPLEMENTATION RESPONSIBILITIES:

Rural Development staff reviewing requests for guarantees under the SFHGLP should accept MMCRs, NTMCRs, RMCRs, and lender prepared nontraditional credit histories which contain sufficient information as outlined for purposes of RD Instruction 1980-D, section 1980.353(e)(4).

RMCRs, MMCRs and NTMCRs that meet the standards of Fannie Mae, Freddie Mac, Housing and Urban Development (HUD) and the Department of Veteran Affairs (VA) are acceptable for Rural Development purposes. In the case of MMCRs, tri-merged reports are preferred because they contain in-file credit report information from three separate credit repositories. Dual-merged credit reports are acceptable only if that is the extent of the data available for the borrower. If only one in-file report is available for the borrower, the lender must obtain an RMCR.

While a MMCR should prove sufficient for processing most loan applications, other circumstances that require ordering a RMCR include:

1. The borrower disputes accounts on the MMCR as belonging to someone else; **or**
2. The borrower claims that collections, judgments, or liens reflected as open on the MMCR have been paid and cannot provide separate documentation supporting this; **or**
3. The borrower claims that certain debts shown on the MMCR have different balances or payments and cannot provide current statements (less than 30 days old) attesting to this fact; **or**
4. The lender's underwriter determines that it would be prudent to utilize a RMCR in lieu of a MMCR to properly underwrite the loan.

Questions regarding this AN should be directed to Joaquín Tremols at (202) 720-1452 or Kristina Zehr at (309) 452-0830 ext. 111. Their respective email addresses are joaquin.tremols@wdc.usda.gov and kristina.zehr@wdc.usda.gov.