SAN DIEGO HOUSING COMMISSION

Mortgage Credit Certificate

Comprehensive Program Manual

Effective May 31, 2018

San Diego Housing Commission
1122 Broadway, Suite 300
San Diego, CA 92101
www.sdhc.org

Table of Contents

PURPOSE OF THE MCC OPERATING MANUAL 4
GENERAL OVERVIEW 4
GENERAL DEFINITIONS 4
WHAT IS A MCC? 7
DIFFERENCE BETWEEN A “TAX CREDIT” AND A “TAX DEDUCTION” 7
PURCHASE PRICE AND INCOME LIMITATIONS 7
MCC TAX SAVINGS 7
INCREASE IN TOTAL NET INCOME 8
RECAPTURE TAX EXPLANATION 9
LENDER’S RESPONSIBILITY REGARDING RECAPTURE TAX 10
APPLICANT ELIGIBILITY REQUIREMENTS 12
FIRST TIME HOMEBUYER STATUS 12
TAX RETURNS: 12
INCOME CRITERIA 13
FULL TIME WAGE EARNER: 13
SELF-EMPLOYED: 13
SEASONAL EMPLOYEES: 13
PART TIME AND/OR SECOND JOB: 13
MILITARY PAY: 13
PART OR FULL TIME STUDENTS: 14
OTHER INCOME: 14
NO INCOME: 14
DEPENDANTS: 14
INCOME VERIFICATION: 14
MCC COMPUTATION VS. MORTGAGE UNDERWRITER’S COMPUTATION: 14
PENALTIES FOR APPLICANT MISREPRESENTATION: 14
ELIGIBLE FIRST TRUST DEED LOAN 15
ELIGIBLE PROPERTIES 15
TARGETED CENSUS TRACTS 15
OCCUPANCY REQUIREMENT:. 16
NO INTEREST PAID TO RELATED PERSONS: 16
APPLYING FOR AN MCC 16
REFINANCING: 16
MCC APPLICATION 17
LENDER CERTIFICATION 17
LENDER PROCESSING 17
FORMS: 18
POWER OF ATTORNEY: 18
INCOMPLETE PACKAGES: 18
PROCESSING TURN AROUND TIME 18
MCC COMMITMENT 19
MCC CLOSING AFFIDAVIT 19
MORTGAGE CREDIT CERTIFICATE ISSUANCE 19

FUNDING AVAILABILITY 19

CHANGES PRIOR TO THE CLOSE OF ESCROW 19

CANCELLATIONS: 19
EXPIRATION OF COMMITMENT: 19
TRANSFERRING MCC APPLICATION TO ANOTHER LENDER 20
ASSIGNMENT OF MCC COMMITMENT FOR FUNDING 20
CHANGING PROPERTIES DURING MCC APPLICATION PROCESS 20
CHANGES IN CURRENT INCOME: 20
CHANGES IN MARITAL STATUS: 20
If the applicant gets married after issuance of the Commitment and prior to closing, the spouse must satisfy the prior home ownership requirements contained in the MCC affidavit and the closing affidavit, and the lender must notify SDHC. Any income added to the household income because of the new spouse should be considered and may affect the validity of the Commitment. 20
CHANGES IN ACQUISITION COST: 20
CHANGES IN LOAN AMOUNT: 21
LENDER'S OBLIGATION TO NOTIFY SDHC OF MATERIAL CHANGES 21

REVOCATIONS 21

MCC TRANSFER 21

LENDER REQUIREMENTS 22

RECORD KEEPING AND FEDERAL REPORT FILING 22

POST AUDIT 22

MCC QUALITY POLICY 22

PURPOSE OF THE MCC OPERATING MANUAL

The purpose of this manual is to describe the program and set forth the role and requirements of the San Diego Housing Commission (SDHC), the lenders, and the program applicants. This document contains a description of the Mortgage Credit Certificate (MCC) program, processing procedures, and program administration. The applicant, purchase price, and mortgage underwriting requirements as set forth in state and federal regulations are also described. Loan processing forms are contained in a separate document. SDHC may revise these guidelines and processing forms from time to time. Public notice will be given only for significant program changes.

SDHC encourages all eligible applicants to apply for an MCC. Participating lenders are expected to be well-informed about all local, state, and federal restrictions contained in this manual so that all applicants are aware of these restrictions before the application is taken. The lender shall reject those applications where the submitted information indicates the applicant does not qualify for the MCC Program.

GENERAL OVERVIEW

The MCC Program, authorized by Congress in the Deficit Reduction Act of 1984, is an alternative to mortgage revenue bond-backed financing as a means of providing financial assistance for the purchase of a home. In 1985, the State adopted legislation authorizing local bond issuing agencies to make MCCs available in California. Our program is designed to benefit First Time homebuyers of new or existing homes throughout the *City of San Diego.*

GENERAL DEFINITIONS

As used in this MCC Operating Manual and all MCC Program documents, unless the context requires otherwise, the following words and terms have the meanings set forth below:

<u>ACQUISITION COST</u>: Derives its meaning from IRS Section 143(k)(3) and the regulations there under. The purchase price limit is set by the State of California law under Section 52020 <u>et seq.</u> of the Health and Safety Code. "Acquisition cost" is used interchangeably with "purchase price." Maximum purchase prices for resale and new homes are updated, according to a federal study, every 12-24 months.

<u>AFFIDAVIT</u>: An affidavit filed in connection with the program made under oath and subject to penalties of perjury.

<u>APPLICANT</u>: any person who applies for an MCC under the program.

<u>COMMITMENT</u>: is issued by SDHC based on review of the application, MCC affidavit and seller's affidavit once the requirements for issuance of a qualified MCC have been met. A Commitment will be valid for 60 days and must be issued before funding.

<u>DATE OF ISSUE</u>: the date the MCC is signed and executed by the Housing Commission.

<u>ELIGIBLE APPLICANT</u>: any person meeting the criteria for an eligible applicant set forth in this manual who is in the process of securing financing for the purchase of an owner occupied single family residence, condominium, or townhome.

<u>ELIGIBLE DWELLING</u>: real property located within the City of San Diego which includes newly constructed units or existing homes. The home can be a single family dwelling, condominium, or townhome which meets the criteria set forth in this manual.

<u>EXISTING HOME (also RESALE HOME)</u>: a dwelling unit that has been previously occupied prior to loan commitment.

FIRST TIME HOMEBUYER: Means a person who has not owned a home during the three year period prior to the purchase of a home using assistance from SDHC. This timeframe includes those 36 months previous to the date the mortgage is executed.

INCOME (Household): income of the applicant and any other person who is expected to live in the residence being financed and/or be secondarily liable. All income derived from any source including income from wages (gross pay, overtime, pension, veterans compensation, bonuses, public assistance, alimony, net rental income, dividends and interest, assets, etc.) of all the members of the household (other than minors) who contribute to the expenses of the household and will occupy the dwelling should be included. Maximum applicant income figures are updated, according to a federal study, every 12-18 months.

IRS: the Internal Revenue Service.

ISSUER: means the City of San Diego exercising bond issuing authority SDHC.

LENDER: a financial institution, whether broker, retail or wholesale, which is licensed to do mortgage business in the State of California and has met all of the requirements established by SDHC to participate as a lender in the MCC Program.

LOAN: an extension of credit to which an MCC applies, provided to an eligible applicant to finance the purchase of an eligible dwelling which meets SDHC requirements set forth in this manual.

LOW-INCOME SET-ASIDE: means that 40% of the allocation SDHC receives is designated specifically for those households with income not greater than 80% of the area median income. This set-aside designation is a requirement by the State of California.

MCC PROGRAM: means the MCC Program established by the City Council of San Diego by Resolution and administered by the SDHC pursuant to the rules and regulations included in the MCC Operating Manual.

MORTGAGE CERTIFICATE RATE: means the rate specified by the Housing Commission in the MCC. For this program, the mortgage certificate rate is either 15% or 20%.

MORTGAGE CREDIT CERTIFICATE (MCC): a tax credit certificate issued by SDHC pursuant to Section 25 of the Internal Revenue Code of 1986, as amended, and applicable by state and local requirements.

NEW HOME: a dwelling unit that is newly constructed or an existing home not previously occupied.

OWNERSHIP: means any of the following interests in residential real property:

- fee simple interest
- joint tenancy
- tenancy in common
- interest of a tenant-shareholder in a cooperative
- life estate
- interest held in trust for the applicant that would constitute a present ownership interest if held by the applicant

Ownership does not include a remainder interest, a lease with or without an option to purchase, or any interest acquired on the execution of the purchase contract.

PRIMARY RESIDENCE: Residence must be occupied as the primary home of the applicant and be defined as one of the following types of residences: 1) single-family house; 2) condominium unit; or 3) town home unit.

PURCHASE PRICE: the cost of acquiring the residence excluding usual and reasonable settlement or finance cost, and the value of services performed by the lender in completing the acquisition of the residence.

RELATED PERSON: allied by nature, origin, kinship, marriage, etc.

SDHC: the San Diego Housing Commission (also referred to as "Housing Commission").

SINGLE FAMILY RESIDENCE: The term single-family residence is a home intended and used for occupancy by one household.

TARGETED AREA: a census tract in which 70% or more of the households have an income which is 80% or less of the statewide median family income, or an area designated as an area of chronic economic distress. These specific areas are not subject to the prior home ownership restriction.

WHAT IS A MCC?

The MCC operates as an IRS tax credit. With an MCC, the qualified applicant becomes eligible to take a federal income tax credit of 20% of the annual interest paid on the mortgage. This credit reduces the federal income taxes of the applicant, resulting in an increase in the applicant's net earnings. An increase in income results in an increase in purchasing power to buy the proposed principal residence.

DIFFERENCE BETWEEN A "TAX CREDIT" AND A "TAX DEDUCTION"

A tax credit entitles applicants to subtract the amount of the credit from their total federal income tax liability, receiving a dollar for dollar savings. A tax deduction is subtracted from the adjusted gross income *before* federal income taxes are computed. Therefore, with a deduction, only a percentage of the amount deducted is realized in savings.

The following example in Table I-1 illustrates how a credit is considerably more valuable than a deduction.

TABLE I-1
VALUE OF A TAX CREDIT VS. TAX DEDUCTION

	TAX CREDIT	TAX DEDUCTION
Total Income	$ 60,000	$ 60,000
Tax Deductions	0	– 2,000
TOTAL TAXABLE INCOME	$ 60,000	$ 58,000
Federal Income Tax Liability	11,350	10,850
Tax Credit	– 2,000	0
TAXES PAID	**$ 9,350**	**$ 10,850**

Table I-1 shows that for the same dollar value, a $2,000 credit reduces federal income taxes paid by $1,500 more than the $2,000 deduction. ($10,850 minus $9,350 equals $1,500.)

PURCHASE PRICE AND INCOME LIMITATIONS

Table I-3 shows the current purchase price and income limitations for the MCC program, which are reviewed and adjusted every 12-24 months. The applicant will be entitled to take a 20% tax credit which is described as follows:

TABLE I-2

Income Limit:	
1 - 2 persons	$116,760 (2018 / 2019 limit)
3 + persons	$136,220 (2018 / 2019 limit)
Sales Price Limit:	
Targeted	$731,177 (2018/2019 limit)
Non-Targeted	$598,235 (2018/2019 limit)

MCC TAX SAVINGS

An applicant receiving an MCC credit loses 20% of his/her normal interest paid deduction with respect to interest paid on the mortgage loan. However, the applicant may continue to deduct the remaining 80% of the annual mortgage interest payment not claimed as a credit. Although the interest deduction is reduced from 100% to 80%, the holder of the MCC still pays considerably less in taxes. See Tables I-2(A) and I-2(B). Assume an applicant with a $100,000 annual income buys a home for $540,000 at a 4% interest rate; the interest paid the first year will be approximately $19,440.

TABLE I-3

	With MCC	**Without MCC**
Annual Income (Household Size – 1)	$ 100,000	$ 100,000
Personal Exemption	-$ 4,000	-$ 4,000
Standard Deduction	-$ 6,300	$ 6,300
Real Estate Taxes	-$ 6,750	$ 6,750
Interest Deduction	-$ 15,552	-$ 19,440
Taxable Earnings	$ 67,398	$ 63,510
Tax from Tax Table	$ 12,638	$ 11,675
1st Year's MCC Credit	-$ 3,888	$ 0
Total Income Tax Liability	**$ 8,750**	**$ 11,675**

The MCC will reduce the amount of federal income taxes otherwise due to the federal government from the applicant. However, the IRS will not pay out more than should have been paid in. Therefore, the benefit in any one year cannot exceed the amount of federal taxes owed for that year, after other credits and deductions have been taken into account.

INCREASE IN TOTAL NET INCOME

The applicant should consider adjusting his/her federal income tax withholding to receive the benefit from the credit on a monthly basis. The applicant may file a new W-4 form with his/her employer reflecting the MCC credit savings. By taking this action, the number of exemptions will increase, reducing the amount of taxes withheld and increasing the applicant's net income.

The applicant also has the option to wait until the end of the year and realize the tax credit savings in one lump sum when filing the federal income tax return.

Regardless of whether the W-4 form is adjusted or not, the tax credit must be listed when filing the federal income tax return, in order to receive the tax credit savings. The applicant should consult a qualified tax preparer to determine the best way to realize the MCC savings.

- If the amount of the MCC exceeds the total tax liability reduced by any other personal credits for the tax year, the unused portion of the credit can be carried forward to the next three tax years or until used, whichever comes first. The applicant will have to keep track of the unused credit each year. The current year credit is applied first and then the oldest amount of unused credit is applied next.

RECAPTURE TAX EXPLANATION

According to Section 143(m) of the Internal Revenue Code of 1986, applicants with loans closing after January 1, 1991, who receive an MCC may be subject to a "recapture tax" if they sell or transfer their home within nine years after the closing. A number of factors determine the amount of tax, if any, that must be paid; computation of the tax is somewhat complicated.

Some MCC holders who sell their home within nine years will not be subject to any recapture tax. Generally, there are four tests to be met in order to incur a recapture tax:

- The home must be sold or transferred within nine years
- The sale or transfer must result in a gain
- The transfer must not be due to death or divorce
- The income of the seller must exceed an amount which equals an increase of 5% per year over the qualifying income in effect when the home was first purchased with the MCC. (This maximum income amount is referred to as the "Income Threshold".)

Further, if the seller's income exceeds the income threshold by less than $5,000, the seller is entitled to a reduction in the recapture tax.

There are several conditions which can exempt the seller from the recapture tax. These include:

- A sale due to death or divorce
- An insufficient increase in the income of the seller (MCC holder) between the time of purchase and the time of sale.

The applicant will receive detailed information on the recapture tax from the lender and will be asked to sign a statement at time of application that he/she is aware of the tax.

The tax, if any, will always be the lesser of half the gain from the sale of the home or a tax based on a somewhat complicated formula which takes into consideration:

- the original principal amount of the home mortgage;
- the number of complete years that pass before the home is sold;
- the median family income for the buyer's area at the time he/she bought the home;
- the applicant's modified adjusted gross income at the time the home is sold.

In no case will the recapture liability exceed 50% of the gain from the sale of the residence. The liability will always be the lesser of half of the gain from the sale of the home, or the recapture tax, as computed through the following formula:

$$PRT = 6.25\% \times P \times H \times \frac{M - (IL \times 1.05^{Y})}{5000}$$

PRT = Potential Recapture Tax

P = original principal amount

H = holding period percentage

M = mortgagor's adjusted gross income at time of sale

IL = original income limit

Y = number of complete years mortgagor owned home

NOTE: If "M - (IL x 1.05 ^{Y})" is greater than $5,000, that amount is treated as equal to $5,000.

There are two basic steps in computing the recapture tax:

- Compute the basic tax by multiplying the original principal balance by a percentage assigned to the year in which the home is sold; and
- If the seller's income exceeds the threshold by less than $5,000, reduce the tax computed by multiplying it times the excess income divided by $5,000.

EXAMPLE

The following is an example of how to compute the recapture tax in a situation where the MCC holder is selling the home between the first and second year after the mortgage closing, the original loan amount is $100,000, and the seller's income exceeds the threshold by $3,000.

STEP 1

First, the loan amount of $100,000 is multiplied by 2.5%, the percentage in the table below which is assigned to a sale between the 1st and 2nd year after closing.

	MAXIMUM POTENTIAL RECAPTURE TAX (MPRT)	
Date of Sale or Transfer of Home (or Prepayment of Mortgage if Earlier)	Percentage of Original Mortgage	Dollar Amount Based on Original Mortgage of:
Before:		**$ 100,000.00**
1 year after Mortgage Closing:	1.25%	$ 1,250.00
1 or more years, but less than 2 years after Mortgage Closing:	2.50%	$ 2,500.00
2 or more years, but less than 3 years after Mortgage Closing:	3.75%	$ 3,750.00
3 or more years, but less than 4 years after Mortgage Closing:	5.00%	$ 5,000.00
4 or more years, but less than 5 years after Mortgage Closing:	6.25%	$ 6,250.00
5 or more years, but less than 6 years after Mortgage Closing:	5.00%	$ 5,000.00
6 or more years, but less than 7 years after Mortgage Closing:	3.75%	$ 3,750.00
7 or more years, but less than 8 years after Mortgage Closing:	2.50%	$ 2,500.00
8 or more years, but less than 9 years after Mortgage Closing:	1.25%	$ 1,250.00

STEP 2

Multiply the tax computed in Step No. 1 ($2,500) by $3,000 (excess income) divided by $5,000.

$$\$2{,}500 \times \frac{\$3{,}000}{\$5{,}000} = \$2{,}500 \times 60\% = \$1{,}500$$

FINALLY

The seller's tax will be $1,500 or half the gain from the sale of the home, whichever is less.

LENDER'S RESPONSIBILITY REGARDING RECAPTURE TAX

The Internal Revenue Service requires that the lender:

- Has a basic understanding of the recapture tax and explains it to the MCC applicant before collecting the MCC application fee.

- Has the MCC applicant sign the form entitled "Initial Notice to Mortgagor Regarding Potential Recapture Tax." This form is included in the MCC application package to the Housing Commission.

In an effort to clearly and adequately explain the recapture tax, the Housing Commission has designed a form entitled "Notice to Mortgagor/Information Regarding Potential Recapture Tax." This form is generated by the Housing Commission and is tailored to reflect the particular loan amount and income threshold. SDHC forwards it to the applicant along with the MCC after loan closing.

APPLICANT ELIGIBILITY REQUIREMENTS

Borrower eligibility requirements are set by both federal and state law. These requirements are subject to change periodically. SDHC will notify the lenders when those changes take place, including the effective date of each change. There are two primary applicant eligibility requirements:

- First-Time Homebuyer Status
- Income Criteria

FIRST TIME HOMEBUYER STATUS

Applicants applying for a MCC cannot have had an ownership interest in a primary residence at any time during the preceding three years ending on the date the mortgage is executed. In the case of a married couple as applicant, both parties must meet this requirement. The lender must obtain from the applicant an affidavit to the effect that the applicant had no ownership interest in a primary residence at any time during the three year period prior to the date on which the mortgage for the MCC is executed. The First Time Homebuyer requirement does not apply to acquisition of units in targeted census tracts.

- Primary residence includes a single-family house, condominium unit, manufactured home (as defined by federal law), share of a housing cooperative, or occupancy of a unit in a multifamily building owned and occupied by the applicant. Ownership interest means ownership by any means, whether outright or partial, including property subject to a mortgage or other security interest. Ownership interest also means a fee simple ownership interest, joint ownership interest by joint tenancy, tenancy in common, or tenancy by the entirety, an ownership interest in trust, a life estate interest, and purchase by land contract under the MCC Program.

<u>TAX RETURNS:</u>
To demonstrate compliance with this requirement, applicants must complete and sign the MCC affidavit, the MCC Program application, the closing affidavit, and provide copies of their last three (3) years signed federal tax returns (or acceptable alternative exhibits - see below).

- If the applicant can produce the signed 1040A, 1040EZ, or 1040 federal income tax returns for the three preceding years with all schedules showing no deductions for mortgage interest or real estate taxes for a primary residence, then these forms shall be submitted to the lender and forwarded to the Housing Commission with the complete MCC application package. The tax returns must be signed and dated in blue ink by the applicant.

- If the applicant has filed the short form 1040A, 1040EZ, or 1040 federal income tax for the last three (3) years, completes and signs the required affidavits, but is unable to produce copies of the signed returns, or if applicant is unable to locate their tax return copies, then they can contact their tax preparer for copies or obtain either Form 4506 (Request for Copy of Tax Return) or Form 4506T (Request for Transcript of Tax Return) from the IRS to request a copy or transcript of their tax returns. If the address on the tax returns filed is different from the current address, then the applicant should also provide a handwritten note (signed by all applicants) indicating the previous returns had been filed at a different address.

- In the event the applicant was not obligated to file federal income tax returns for any of the preceding three (3) years, then it will be necessary for the lender to obtain from the applicant a completed and signed Income Tax Affidavit which is required in place of the documents listed in items above. This document is forwarded to SDHC along with other program affidavits in the application package. It must also include an explanation of why the tax return was not included.

- When the Commitment is issued during the period between January 1 and February 15, and the applicant has not yet filed his/her Federal income tax return for the preceding year with the IRS, the Housing Commission may, with respect to such year, rely on an affidavit of the applicant that the applicant is not entitled to claim deductions for taxes or interest on indebtedness with respect to property constituting his/her principal residence for the preceding calendar year. ***After February 15, the preceding year tax return will be required.***

- If the tax returns indicate the applicant took a deduction for mortgage interest or real estate taxes on property claimed not to be the primary residence, then documentation would be required to show proof of the applicant's rental during that period (i.e., rent receipts, canceled checks).

INCOME CRITERIA

The "gross income" of an applicant, as defined by the Revenue Ruling 86-124 of the Internal Revenue Code, is the applicant's annualized gross income. Annualized gross income is the sum of monthly gross income multiplied by 12. Gross monthly income includes the gross amount, before payroll deductions, of wages, salaries, overtime, commissions, tips, bonuses, sick pay, and flex benefits; dividends and interest; severance pay; insurance payments; death benefits; winnings/prizes; disability; annuities; fees; part-time employment; royalties; pensions; veterans compensation; net rental income; alimony; child support; foster care support; adoption care support; public assistance; social security benefits; unemployment compensation; and income derived from trusts, business activities or investments. The income to be taken into account in determining "gross income" is income of the applicant and any other person who is expected to live in the residence being financed and/or be secondarily liable on the mortgage.

For married couples, income includes the income of both spouses, whether or not on title. Co-applicants that will not occupy the property are not permitted.

<u>FULL TIME WAGE EARNER:</u>

For the purpose of computing the gross income of a W-2 wage earner, the salary or base pay will be calculated by multiplying the hourly rate by the number of hours, then by the number of pay periods and divided by 12 months. If the applicant does not consistently work the same number of hours per pay period, the salary or base pay will be averaged over the previous two years, plus current year-to-date income. The applicant must have a two year work history in order to include the income for underwriting purposes. Overtime, double-time, commissions, and bonuses etc., will be averaged over the previous two years and current year-to-date income. The applicant must have a two year history of overtime, double-time, commissions, and bonuses etc in order to use the income for underwriting purposes.

<u>SELF-EMPLOYED:</u>

The income for self-employed workers is calculated by averaging the previous two years adjusted gross income, plus depreciation and/or depletion claimed on schedule C. A year-to-date signed and dated profit and loss statement is required.

<u>SEASONAL EMPLOYEES:</u>

The income for seasonal workers is calculated by averaging the previous two years income as stated on the W-2 and/or signed and dated verification of employment. For unemployment benefits received in the off season of work, the gross income will be calculated by averaging the previous two years benefits. If in the off season during the period of application, then proof of unemployment benefits must be provided.

<u>PART TIME AND/OR SECOND JOB:</u>

The monthly income is calculated by averaging the previous two years gross income as indicated on the W-2, plus the current year-to-date income. For the purpose of computing the gross income for underwriting, the applicant must have a two year history of the part time, or second job.

<u>MILITARY PAY:</u>

For the purpose of computing the gross monthly income, the "total entitlement" shown on the applicant's most recent monthly leave and earnings statement, including all regular pay, special pay and allowances including housing allowance. The "total entitlement" is <u>not</u> grossed up. Certain categories of pay, which may be received only sporadically, will be considered on a case-by-case basis. The special pay to a family member serving in the Armed Forces who is exposed to hostile fire is excluded from gross income calculation.

<u>PART OR FULL TIME STUDENTS:</u>
Adult members (18 and older) enrolled in a vocational, community college, or university must provide evidence of current enrollment status and a copy of their Financial Aid Award letter. For the purpose of computing the gross income of any person(s) identified as an adult student and a member of the household, only the first $480 of the student's monthly income is included in the calculation of household income. The $480 limit does not apply to a student who is head of household or a spouse, in this case the full income must be counted.

<u>OTHER INCOME:</u>
Sources of income other than wages must be documented by third party verifications. In cases where the third party fails to respond, acceptable alternative sources of documentation can be determined on a case-by-case basis and should follow standard income verification guidelines.

<u>NO INCOME:</u>
Adult members, 18 years and older, of the household who have no income must complete and sign the Declaration of No Income form.

<u>DEPENDANTS:</u>
A Declaration of Household Size must be provided if any persons claimed on federal tax returns within the past three years are not identified as a household member on the application. A Declaration of Household Size must also be provided if any person not claimed on the federal tax returns within the last three years, is identified as a household member on the application. The borrower must provide proof as an established household for a minimum of one year. Acceptable sources of documentation include bank statements, driver license, identification card, utility bills, etc.

<u>INCOME VERIFICATION:</u>
The Lender bears the burden of proving the buyer's income is within the program guidelines. The computation should be clear, complete, and documented. Include any written explanation, including calculator tapes, which demonstrate your computation. In cases where the buyer is employed, an acceptable source of documentation to verify the buyer's <u>current</u> income is a recent pay stub with year-to-date earnings. A verification of employment (VOE) from all employers within the previous 2 years is required. All VOEs must include income and be signed & dated by the employer.

<u>MCC COMPUTATION VS. MORTGAGE UNDERWRITER'S COMPUTATION:</u>
The lender should understand that the applicant's income will be computed one way to qualify for the MCC and possibly a second way to qualify for the first mortgage. There are two major differences:

- <u>Current Income</u>: The MCC figure represents CURRENT income, while the lender's figure represents income AVERAGED over the last few years; and

- <u>Income Sources</u>: The IRS requires that <u>every</u> source of income, taxed or untaxed, be included in the MCC computation, while the underwriter for the mortgage may choose not to honor sources of income which are sporadic and lack a strong track record.

<u>PENALTIES FOR APPLICANT MISREPRESENTATION:</u>

Strict penalties may be imposed on any applicant making a material misstatement, misrepresentation or fraudulent act on documents submitted to obtain an MCC. Any person making a negligent material misstatement or misrepresentation in any affidavit or certification made in connection with the application for or the issuance of an MCC shall be subject to all applicable fines and penalties.

ELIGIBLE FIRST TRUST DEED LOAN

MCCs can only be used with original first mortgage financing which includes 30 year fixed-rate conventional loans, FHA, and VA loans. MCCs are not available with bond-backed loans such as California Housing Finance Agency (CalHFA), Cal Vet loans, adjustable rate and negative amortization loans. First trust deed loans will be underwritten by the lender and not SDHC.

An MCC cannot be issued in conjunction with acquisition or replacement of an existing mortgage or land contract. The lender and the applicant, using the program affidavits, state that the mortgage being acquired in connection with the certificate will not be used to acquire or replace an existing mortgage or land contract.

For loans involving MCCs, the conventional underwriting standards should be modified to reflect recognition of the MCC-derived mortgage interest credit in determining housing expense and indebtedness ratios. The secondary mortgage market and the mortgage insurance industry have established underwriting policies for MCC-linked loans. These are available as policy statements from the mortgage lending industry.

ELIGIBLE PROPERTIES

An MCC can only be used for new or resale single-family homes, including single family detached homes, condominiums, or townhomes in the City of San Diego. Duplexes, triplexes, or four-plexes do not qualify as eligible structures. Two-on-one units also do not qualify as eligible structures.

TARGETED CENSUS TRACTS

Sixty-six census tracts in the City of San Diego were designated by the Census Bureau as "low income". In these areas, the applicant can be, but does not have to be, a First Time Homebuyer to qualify for an MCC, but must sign an affidavit of intent to occupy the property. In accordance with federal guidelines, twenty percent (20%) of the Housing Commission's MCC allocation is set aside for purchases in targeted census tracts.

All of San Diego is divided into numbered census tracts. Thomas Brothers Maps publishes a census tract edition which clearly designates the boundaries of each of these tracts. Lenders and applicants can determine a properties census tract by logging on to www.ffiec.gov/geocode/default.aspx.

The following is a complete listing of the census tracts within the City of San Diego which are federally targeted for special treatment under the MCC Program. These tracts are:

12	16	22.01	22.02	23.01	23.02
24.01	24.02	25.01	26.01	26.02	27.02
27.07	27.08	27.09	27.10	27.12	28.01
29.04	30.01	30.04	31.05	31.11	33.01
33.03	33.04	33.05	34.03	34.04	35.01
35.02	36.01	36.02	36.03	39.01	39.02
40	41	47	48	49	50
51	52	53	57	58	65
66	83.05	83.39	83.41	83.43	83.61
83.63	86	90	94	100.05	100.09
100.13	101.03	101.06	101.11	101.12	170.35

OCCUPANCY REQUIREMENT:
The applicant must use the home being purchased with the MCC-linked mortgage as a principal residence. The lender must obtain from the applicant, using the program affidavits, a statement of the applicant's intent to use the residence as his/her primary residence within 60 days after the MCC is issued. This affidavit further states that the MCC holder will notify the lender and SDHC if the residence ceases to be his/her principal residence.

NO INTEREST PAID TO RELATED PERSONS:
No interest on the mortgage (or certified indebtedness) amount may be paid to a person who is a related person as that term is defined under the Internal Revenue Code and applicable regulations. The lender must obtain from the applicant, using the program affidavits, a statement to the effect that no related person has or is expected to have, an interest as a creditor in the certified indebtedness amount.

APPLYING FOR AN MCC
Applicants shall apply for an MCC through a SDHC participating lender. A list of the lenders can be obtained from the SDHC website.

Eligible applicants apply for MCCs when applying for a mortgage loan through the participating lender. The applicant should apply for the MCC at the same time he/she makes a formal application for a mortgage loan. The applicant should be ready to supply credit information, employment data, and other information to the lender for both the mortgage and the MCC applications.

REFINANCING:
If an applicant obtains an MCC in connection with a first mortgage, and subsequently pays off and refinances that original mortgage, the applicant will no longer be eligible to take the tax credit unless a Reissued Mortgage Credit Certificate is applied for. The RMCC program is administered by SoCal RMCC at http://socalrmcc.com/. Refinancing does not trigger the recapture tax.

MCC APPLICATION

The MCC processing procedures are designed to coincide with the standard mortgage loan processing and underwriting procedures that are in place at most mortgage lending institutions. Recognizing there are procedural variations among the participating lenders, the procedures outlined here are meant to serve as guidelines with respect to the sequence of events. However, all the elements of the processing sequence outlined in this manual must at some point be completed, regardless of sequence, by the lender, applicant, seller, and SDHC.

Lenders will work with applicants on a first-come, first-served basis. There is no direct allocation of MCCs to a lender. During the processing of the mortgage application, the lender will submit an MCC application package to SDHC on behalf of the applicant. Once the applicant and property are determined to be eligible, the Housing Commission will issue a Commitment to the lender. This reserves an MCC for that particular purchase transaction. The actual MCC is issued to the applicant after the close of escrow. Since the MCC processing is concurrent with the loan processing, it should not extend the length of escrow.

LENDER CERTIFICATION

The lender will be required to submit certifications which it will certify to the best of its knowledge no material misstatements appear in the application and program documents. If the lender becomes aware of misstatements, whether negligently or willfully made, it must notify SDHC immediately. The Housing Commission will take all lawful actions to correct or mitigate the problem.

The lender should also be aware and inform the applicant of criminal penalties provided by federal and state law if a person makes a false statement or misrepresentation in order to participate in this program. In an attempt to ensure that all requirements are clear, an MCC affidavit is required by each applicant and must be included in the MCC application package submitted to SDHC.

LENDER PROCESSING

The lender discusses parameters of the MCC Program with the applicant and determines eligibility.

The lender will inform the applicant of the non-refundable MCC application fee to the Housing Commission of:

- $620

The lender determines if the applicant is an eligible candidate for an MCC, based on income, purchase price, prior home ownership, tax liability and other factors. The lender uses published SDHC income and purchase price limitations. The lender requests three prior year's tax returns from the applicant and prepares to have the Seller Affidavit forwarded with instructions to the Seller.

The lender gives the applicant the MCC application package which explains the program and contains consumer information. The package should include:

- MCC Information Packet (available on SDHC's website).
- Copy of Recapture Tax Notice #1 signed by applicant;
- MCC affidavit

The lender and applicant together review, complete, and execute the MCC Program application and the MCC affidavit. These documents serve as the application and contain certifications required by the MCC Program regulations and requirements as follows:

- Certification that the property will be used as principal residence and that the MCC holder must notify SDHC when the home ceases being their principal residence.
- Certification that the applicant has not had an ownership interest in a principal residence during the preceding 3-year period from date of application (not required for a targeted area).
- Certification that the purchase price does not exceed purchase price limits.
- Certification that this is a new mortgage loan, as defined in Internal Revenue Service regulations.
- Certification that the loan applied for does not constitute a prohibited mortgage.
- Certification that the applicant was not forced to apply through a particular lender.
- Certification that the applicant's gross annual household income does not exceed permitted income limits.
- Certification that no interest is being paid to a related person.
- Certification that the MCC cannot be transferred without the prior written approval of the RMCC program.
- The lender transmits to the Housing Commission an MCC application package containing all applicable items listed on the checklist in the submission packet which can be downloaded from the SDHC website.

FORMS:
MCC applications, affidavits, and disclosures are to be fully executed. It is imperative that the submission instructions be followed. The loan submission packet on the SDHC website is in excel format and contains the required documents.

- All forms must be signed
- Checklist – check each blank for the document being forwarded. Any item which is not applicable is to be marked N/A.
- Upon completion of the application worksheet, "click" each worksheet/document and verify that all necessary information was completed accurately.
- After all worksheets have been properly completed and verified, print and put the loan application package together according to the stacking order shown on the checklist.
- Send the complete application package in hard copy to: San Diego Housing Commission, 1122 Broadway, #300, San Diego, CA 92101, ATTN: Melissa Holt

POWER OF ATTORNEY:
Signatures under Power of Attorney are acceptable, provided they are accompanied by a copy of the recorded Power of Attorney. If not recorded prior to loan closing, then it must be provided with the recording date and document number as part of the closing phase package.

INCOMPLETE PACKAGES:
Incomplete packages and packages which are not in stacking order will be rejected. The lender will be asked to pick up the package.

PROCESSING TURN AROUND TIME
The Housing Commission accepts and reviews the MCC application package and determines the applicant's eligibility. SDHC staff date-stamps the package and reviews it in the order in which it is received. The approximate turn-around time for reviewing and sending an MCC Status Report is 3-7 business days.

MCC COMMITMENT
Upon receipt of requested conditions, SDHC will issue a Commitment to the lender, which designates a unique MCC reservation number for the applicant. This reservation number is used to identify and track the file. The Commitment is valid for a period of 60 days.

Prior to the Commitment expiration date, the lender must either:

- Submit the fully executed MCC Closing Affidavit and Final HUD;
- Submit written notice of MCC cancellation; or
- Request a 30-day extension.

MCC CLOSING AFFIDAVIT
SDHC will issue a MCC Closing Affidavit. The affidavit is to be signed and dated by the applicant's and loan officer. Immediately following the close of escrow the following documents are to be submitted to SDHC:

- Original Closing affidavit signed by the lender and the applicant
- Final HUD-1

MORTGAGE CREDIT CERTIFICATE ISSUANCE
Upon receipt of the MCC Closing Affidavit and final HUD, SDHC issues the following documents to the applicant:

- Mortgage Credit Certificate
- Completed Recapture Tax Notice #2
- A letter explaining how to use the MCC certificate
- A copy of the IRS Form 8396 to be filed with the applicant's federal income tax returns.

A copy of the MCC will be emailed to the lender for their records.

FUNDING AVAILABILITY
The Housing Commission maintains a cumulative-to-date total of mortgage amounts reserved to monitor the amount of expected mortgages and aggregate amount of MCCs to be issued. SDHC will notify lenders via email and the SDHC web page regarding the status of available certificates.

CHANGES PRIOR TO THE CLOSE OF ESCROW

<u>CANCELLATIONS:</u>
The lenders must adhere to the time frame of the MCC processing period, promptly notifying the Housing Commission in writing of any MCC cancellations and/or requests for reservation or Commitment extensions. In cases where a decision is made not to continue with an MCC application, written notice must be received at the Housing Commission prior to the expiration of the Commitment. The notice must include the reason for the cancellation and be signed by both the lender and the applicant.

<u>EXPIRATION OF COMMITMENT:</u>
Before the Commitment has expired, the lender must submit the closing phase package, submit a request for a 30-day extension and check for $25 *or* submit a notice of cancellation as described above. The following action is to be taken by the lender if the Commitment expires:

- If loan has closed, then the lender submits closing phase package and $175 payment.

- If loan has not closed, then the lender submits request for extension, estimate of closing date, and $175 payment.

- If 120 days have passed since the Commitment was issued, then the lender submits an entirely new MCC application with current income verification and payment of $175.

- If loan was canceled, then the lender submits a cancellation notice as described above and payment of $175.

In all cases, expiration of the Commitment without the required action by the lender will result in the lender being placed on inactive status. Inactive status means the lender may not submit new MCC applications until the issue is resolved plus a $175 payment from the lender which is not to be passed on to the applicant. A failure to comply may result in the lender's removal from the program.

TRANSFERRING MCC APPLICATION TO ANOTHER LENDER
If an applicant has a pending MCC application and decides to change from one participating lender to another, the Housing Commission will honor the original expiration date as long as all other conditions are unchanged. The new lender must verify the Commitment documents. The transfer will be recognized by SDHC only after written notification is received. The new lender must be an SDHC participating lender.

ASSIGNMENT OF MCC COMMITMENT FOR FUNDING
If a lender packages a loan with an MCC and assigns the loan to another MCC participating lender for funding, the original lender must forward to SDHC in the application package an MCC letter of assignment using the Housing Commission form provided for this purpose. The MCC will be issued in the funding lender's name. The funding lender will also be responsible for the reporting that particular loan on IRS Form 8329.

CHANGING PROPERTIES DURING MCC APPLICATION PROCESS
If an applicant has a pending application and changes the property he/she is purchasing, the lender must submit a new signed sales agreement and indicate by transmittal whether the mortgage amount has changed. If the applicant has already been issued a Commitment, the following documents should be revised and re-submitted to reflect the new property address and any change in mortgage amount:

- Home Buyer Program Application
- Sales Contract
- Seller Affidavit

The Commitment is re-issued with the original expiration date.

CHANGES IN CURRENT INCOME:
The eligibility of the applicant for an MCC is based upon the applicant's current income. The MCC Program will issue the Commitment based on facts pertaining to income as of the date the Commitment is issued. The income verified for the Commitment is valid as long as the loan closes within four months after the financial information was originally submitted and there are no additional sources of income that were not previously reported.

CHANGES IN MARITAL STATUS:
If the applicant gets married after issuance of the Commitment and prior to closing, the spouse must satisfy the prior home ownership requirements contained in the MCC affidavit and the closing affidavit, and the lender must notify SDHC. Any income added to the household income because of the new spouse should be considered and may affect the validity of the Commitment.

CHANGES IN ACQUISITION COST:
If the total acquisition cost of the residence purchased in connection with the MCC increases so as to exceed the acquisition cost limitations set forth herein, the Commitment shall be revoked. For a

change in acquisition cost after the Commitment and prior to closing which does not exceed maximum price guidelines, the lender will be required to complete and submit a new version of:

- Home Buyer Program Application
- Amended escrow instructions
- Seller Affidavit

CHANGES IN LOAN AMOUNT:

Any changes to the loan amount which occur before or after Commitment is issued must be reported to the SDHC immediately by phone, and followed up in writing. Indication of the change (with a brief explanation) on the completed transmittal form is sufficient for the written requirement. A change to the loan amount affects the amount of the MCC and must be reported to SDHC prior to the close of escrow. The lender will be required to submit the following new documents:

- 1st Trust Deed Application (1003)
- Transmittal Summary (1008)
- 1st Trust Deed Approval

LENDER'S OBLIGATION TO NOTIFY SDHC OF MATERIAL CHANGES

The decision to issue an MCC Commitment is based (in part) upon the applicant's and seller's affidavits and the lender's certification that the requirements necessary for issuance of a qualified MCC have been met. The lender must immediately notify SDHC in writing (by using the Transmittal Form) of any change in the circumstances upon which the Commitment was issued.

REVOCATIONS

Automatic revocation of an MCC occurs when:

- The residence for which the MCC was issued ceases to be the MCC holder's primary residence.
- The MCC holder is not in compliance with the requirements for a qualified MCC.
- Discovery by the Housing Commission or a participating lender of any material misstatement, whether negligent or fraudulent.

MCC TRANSFER

The MCC is not assumable. It can be used only by the applicant named on the original certificat

LENDER REQUIREMENTS

For the MCC Program, a "lender" is any corporation licensed to make first mortgage loans in the State of California. All brokers, retail and wholesale lenders who wish to participate in the MCC Program in any way must be enrolled in the program. To enroll and maintain active status in the MCC Program a lender must:

1. Complete and sign a Lender Participation Agreement perform in accordance with the MCC Quality Policy.
2. Designate a contact person for each branch office participating in the MCC program.
3. Pay a $400 enrollment fee and $400 annual renewal fee. Request to add additional branches during participation year will be charged $25 per branch.
4. All lending personnel involved in the MCC program are required to attend the MCC training course with SDHC.
5. Provide the MCC Operating Manual to all MCC processors.
6. Cooperate with the Housing Commission in providing the best possible service to the City's first-time homebuyers.
7. Provide the MCC Information Packet to all MCC applicants.

RECORD KEEPING AND FEDERAL REPORT FILING

The lender must file an annual report, using IRS Form 8329. For six years, the lender must retain:

- Name, mailing address, and TIN (social security number or tax identification number) of the MCC holder.
- Name, mailing address, and TIN of SDHC (95-3390896).
- Date of loan (date of issuance), certified indebtedness (mortgage) amount, and credit rate of 20%.

SDHC must make quarterly reports on IRS Form 8330, beginning with the quarter in which the election is made. The report must include:

- Name, address, TIN of SDHC, and date of election.
- The sum of the products of the certified indebtedness amount (mortgage amount) and the MCC credit rate for each MCC issued.
- Name, address, and TIN of each MCC holder whenever an MCC was revoked.

SDHC shall make an annual report for each year beginning July 1 and ending June 30. The report must include:

- Number of MCCs by Income and Acquisition Cost;
- Volume of MCCs by Income and Acquisition Cost; and
- MCCs for qualified Home Improvement and Rehabilitation Loans. (This is not applicable for this program.)

POST AUDIT

SDHC retains the express authority to perform annual random case post audits of any participating lender's records.

MCC QUALITY POLICY

The San Diego Housing Commission invites the entire San Diego mortgage lending community to participate in the Mortgage Credit Certificate program. Participation will continue to be open to those mortgage lenders who uphold the following work standards.

Lending company personnel follow MCC training manual instructions and other training materials; MCC lender update letters including attachments and revised forms

MCC packages have less than four errors per package. A "correction package" which repeats the errors of the original package will not receive a second opportunity for correction.

Each lender enrolled in the program designates an MCC contact person for each participating branch. The contact's responsibilities include: (1) making Lender Update letters (including attachments) available to all MCC-related personnel in a timely manner; (2) notifying the Housing Commission of any re-assignment regarding their role as contact person.

A notice of expiration of the Commitment without the required paperwork having been submitted is to be responded to by the lender in a timely manner, with payment of the $175 late fee, and submittal of the necessary documentation to bring the delinquent file current or close it out.

The lender obtains the Housing Commission's commitment to issue the MCC before funding the loan.

Each funding lender ensures that the closing or funding department of their company is aware of their obligations under the MCC program and are prepared to submit all necessary closing documentation in a timely manner.

Applicants are treated fairly, receiving a full and accurate explanation about the MCC and the recapture tax. For questions which the lender cannot answer, the applicant is referred to the Housing Commission.

EQUAL HOUSING OPPORTUNITY

The San Diego Housing Commission (SDHC) is committed to affirmatively furthering fair housing by promoting fair and equal housing opportunities for individuals living in the City of San Diego. This commitment extends to all housing programs managed or owned by SDHC and to all grant-funded programs provided by SDHC. It is the policy of SDHC to provide services without regard to race, color, religion, national origin, ancestry, age, gender, familiar status or physical/mental disability. For more on our commitment to affirmatively furthering fair housing visit our website at www.sdhc.org