

**Greater Minnesota Housing Fund  
Single Family/Building Better Neighborhoods  
Gap Loan Program**

**Need-Based Loan Program  
Procedure Manual**

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**Updated Spring 2003**

This manual was prepared by the Greater Minnesota Housing Fund for use by organizations administering a GMHF need-based gap loan program and their lender partners.

## **CHAPTER ONE PROGRAM ELIGIBILITY**

### **I. ELIGIBLE APPLICANTS**

All individuals and families with verified household incomes below the program income limits are eligible to participate in the GMHF gap loan program. There are no restrictions on the geographical location or tenure (i.e., owner or renter) of applicants.

### **II. PROGRAM INCOME LIMITS**

The maximum household income for buyers is 80 percent or less of statewide median income (as determined by HUD) and adjusted for family size. The maximum household income will be adjusted annually to reflect current HUD figures. Current GMHF income limits are attached.

### **III. CALCULATION OF APPLICANT ELIGIBILITY INCOME**

The first mortgage lender will verify all sources of household income for the current year and project the current household income ahead for the remainder of the year. Household gross income cannot exceed the program eligibility limit. Sources of income that must be included in the household income calculation are attached.

### **IV. GMHF GAP LOAN PROGRAM**

The program will provide qualified applicants with a need-based deferred gap loan. The deferred loan is intended to help fill the gap between the price of the new home and the amount of mortgage the applicant can afford to pay.

The maximum dollar amount of gap assistance per household may not exceed \$15,000. Borrowers may obtain additional downpayment, closing cost and monthly payment assistance from MHFA or other sources.

The amount of the gap loan will be based on the following factors:

- Household income (adjusted for family size).
- Home sale price. The maximum total development cost (TDC) for GMHF-financed homes is adjusted each year. See the attached GMHF TDC limit guidelines for more information.
- Affordability of first mortgage product (e.g., borrower with a market rate loan receives more gap financing than a borrower with a subsidized mortgage to offset the difference in interest rates).
- Amount of other housing expenses, including taxes, homeowners insurance, private mortgage insurance, and closing costs (determined/estimated by the program administrator).
- Amount of downpayment/closing assistance and monthly payment assistance from MHFA or other public sources.

- Amount of borrower contribution for downpayment and closing costs. Minimum borrower contribution **from personal funds** is 1 percent of the home purchase price.
- Amount of equity from a previous sale or other cash reserves. Borrowers are allowed to retain up to \$5,000 of equity or other cash reserves. Any amount above \$5,000 must be applied toward the purchase of the homes.
- The minimum housing expense ratio used for the final gap calculation must be at least 25 percent. The buyer may opt for a gap loan based on a 25 percent housing expense ratio even if the first mortgage product allows for a higher front-end ratio.
- GMHF funds may not be used to pay for prepaids. The buyer or another source must cover prepaid expenses due at closing. Prepaid expenses are in addition to the minimum downpayment from personal funds required by GMHF.
- The gap loan **will not** be adjusted based on the level of other debt (e.g., car loans, credit cards, etc.) accumulated by the borrower.

#### **V. EXTRAORDINARY MEDICAL EXPENSES/OTHER EXTENUATING CIRCUMSTANCES**

At the discretion of GMHF, extraordinary medical expenses can be considered in determining the amount of the gap loan. Extraordinary medical expenses will be determined by utilizing an MHFA Extraordinary Expense Form.

The gap loan amount may be adjusted due to extenuating circumstances. The request for an adjustment must be in writing and approved by the Greater Minnesota Housing Fund. The adjustment must result in the applicant's ability to obtain a first mortgage. The adjustment is at the sole discretion of GMHF.

#### **VI. HOME STRETCH HOME BUYER EDUCATION**

Gap loan recipients must attend homebuyer training provided by a certified Home Stretch organization before closing on a gap loan. Proof of completion should be retained in the applicant's file.

#### **VII. GAP LOAN TERMS**

The minimum amount of a gap loan is \$2,000. Applicants who meet all income and program guidelines but do not qualify for a need-based award may still receive a program minimum loan of \$2,000. The maximum gap loan amount is \$15,000.

Gap loans must be repaid according to the provisions of the Gap Financing Loan Note. The gap loan will be coterminous with the borrower's first mortgage. Conditions that trigger repayment of the mortgage include:

- If a sale of the property occurs or if the property is transferred, including by gift or in the event of death.
- If the first mortgage is satisfied or foreclosed.

- If the property is no longer the primary residence of the borrower.

For further information, consult the Gap Financing Loan Note.

The gap loan mortgage will be filed with the County Recorder's Office as a second mortgage on the property. If the borrower has a HAF equity contribution loan, the GMHF gap loan will be a third mortgage.

## **VIII. REFINANCE AND SUBORDINATION POLICIES**

GMHF has recently adopted a gap loan subordination policy. GMHF will subordinate for borrowers who refinance to a lower interest rate but receive no cash from the refinancing. The lender must contact GMHF for the subordination agreement. If the borrower obtains a home equity loan or gets cash from a refinancing, the cash may only be used for qualified home repairs or improvements.

Important: All cash proceeds from the refinancing or home equity loan must be paid directly at closing to a valid title company or bank and managed by an escrow agent. The funds will be held in the escrow account until payments are approved by the local administrator. No improvements may be started before the escrow account is established. Cash cannot be paid directly to a homeowner at closing. The local administrator must agree to authorize escrow payments and may charge a fee for this service. GMHF does not require administrators to provide this service.

No wrapping in of other debt to the new first mortgage is allowed. GMHF will only subordinate once to each homeowner during the life of the loan. Please review the complete policy included with the project award letter for additional information.

## **IX. HANDICAPPED-ACCESSIBLE MODIFICATIONS**

GMHF will provide up to an additional \$10,000 of need-based gap loan assistance (maximum gap loan of \$25,000) to assist households with documented handicapped-accessibility needs. To provide additional gap financing, GMHF requires documentation of the disability from the family and the cost of required modifications from the builder/developer. An itemized list of modifications must be approved by GMHF before construction can begin on the house. Additional gap financing cannot be provided to retro-fit/modify a new house that has already been completed. Technical/design assistance for accessibility modifications is available from GMHF upon request.

## **X. FIRST MORTGAGE LOANS**

Gap loan assistance must be combined with an affordable first mortgage product that meets the GMHF guidelines. These guidelines are designed to ensure that low- and moderate-income homebuyers receive first mortgages that meet their needs and promote long-term affordability. GMHF gap loans are typically not available to buyers who cannot obtain a first mortgage

consistent with these guidelines. Exceptions to these guidelines are at the sole discretion of GMHF.

The program administrator will provide information to buyers about participating lenders; however, it is the responsibility of the applicant to contact lenders, shop for the best product to address their needs and provide the necessary documentation to secure the first mortgage loan.

The program administrator should provide interested lenders with the GMHF guidelines for affordable mortgage products and the gap loan program and underwriting guidelines.

Affordable first mortgages must meet all of the following requirements:

- Fixed-rate loan, minimum amortization of 30 years, and a minimum term of 15 years. Note: The GMHF gap loan is co-terminus with the first mortgage.
- Downpayment required by product cannot exceed 5 percent of sale price. (Note: This guideline does not preclude a buyer from making a larger downpayment if additional personal funds are available.)
- GMHF preference is for below-market or market-rate loan products. The buyer's first mortgage interest rate cannot exceed current market rate plus 1 percent. Current market rates are available from the Freddie Mac Weekly Mortgage Market Survey at <http://www.freddiemac.com>.
- Housing expense and debt to income ratios of at least 28/36 allowed by the loan product (e.g., 29/41 is acceptable). Lenders are encouraged to use community homebuyer products with flexible underwriting guidelines.
- Closing costs (excluding prepaids) cannot exceed 3.5% percent of the loan amount. Note: This does not preclude buyers with liquid assets above \$5,000 from using their excess funds to buy down the interest rate.
- Roll over loans are not acceptable. Roll over loans have a fixed interest rate, short maturity, and a term to be negotiated.

## **XI. MHFA CASA PROGRAM**

MHFA has agreed to provide CASA funding for Building Better Neighborhoods subdivisions. CASA provides funding for below-market first mortgages. MHFA participating lenders should contact the agency to apply for CASA funds.

## **XII. MHFA ECHO AND HAF PROGRAMS**

Gap loan borrowers are strongly encouraged to apply for entry cost assistance through the ECHO or HAF programs offered by MHFA. Qualified CASA buyers may also receive an equity contribution loan through the HAF program. The amount of HAF and ECHO assistance will be used to reduce the amount of GMHF gap loan assistance. **Buyers using CASA must receive all HAF assistance (entry cost, monthly payment assistance, and equity contribution loan) that they are eligible for before receiving any GMHF gap loan funds.**

### **XIII. Layering Gap Financing Programs**

GMHF encourages developers to obtain a wide range of financing assistance for income-qualified buyers. However, GMHF funds may not be layered with awarded funds from MHFA or DTED (e.g., CRV or Small Cities programs) if the total amount of awarded gap funds exceeds \$15,000 per buyer. This rule does not apply to MHFA HAF funds, which are available on a pipeline basis through participating lenders.

## **CHAPTER TWO**

### **LOAN PROCESSING STEPS/PROCEDURES**

#### **I. APPLICATION**

The application process requires buyers to complete a series of steps to receive financial assistance. This process is a guideline for local administrators. It may be adjusted to meet the needs of the local program.

- A. Determine preliminary eligibility. The applicant meets with the gap loan administrator (or its designee) to determine preliminary program eligibility. If the applicant is income-eligible, the administrator will provide information about the program, obtaining a first mortgage, and the requirements for homebuyer education.
- B. Obtain first mortgage credit approval. The applicant is responsible for obtaining first mortgage credit approval. The first mortgage must meet GMHF standards for affordable mortgage products.
- C. Enroll in homebuyer education. The applicant should enroll in a Home Stretch homebuyer training course if he/she has not yet completed homebuyer education. Proof of completion must be provided before closing.
- D. Receive gap loan estimate and preliminary reservation of funds. The administrator will collect all of the paperwork received from the applicant and his/her lender. If the applicant's first mortgage meets program guidelines, the administrator will provide him/her with a preliminary reservation of funds. The reservation of funds is based on the applicant's verified income, terms of the first mortgage, and other factors.
- E. Find a home and sign a purchase agreement. The applicant's next step is to find a home to purchase. The purchase agreement should include a contingency for the applicant receiving a certain level of gap loan funds. The applicant is responsible for returning the signed purchase agreement to the administrator.
- F. Receive final gap loan approval. The administrator will review the purchase agreement received from the applicant. After addressing any questions, the administrator will provide the applicant with a final gap loan approval. The final gap approval will be mailed to the applicant and builder after all required documentation is received. The final gap loan amount is based on the price of the home and the information already collected from the first mortgage lender. However, the applicant will not receive a final gap loan approval until he/she has provided proof of completion of a homebuyer education class.
- G. Schedule closing and notify the administrator. The applicant is ready to close on a new home. The applicant or his/her realtor is responsible for notifying the

administrator of the date of the loan closing at least 10 business days before the close date.

- H. Close on mortgage loans. Current homeowners must sell their homes and before closing on a new house. A preliminary settlement statement from the sale must be provided one week before the gap loan closing. If all documentation has been received, the applicant completes the closing process and moves into a new home.

## II. VERIFICATIONS

The program administrator will require the following verifications:

### A. Eligibility Income

The participating financial institution will be responsible for verifying eligibility income. Gross annual income will be verified in accordance with MHFA guidelines. Sources of income are included in Appendix B. GMHF strongly recommends that the following verifications be collected from each applicant:

- Previous 2 years income tax returns (1040, W2s)
- Check stubs for the past month for each place of current employment
- Third party verification of all other income
- Self employed individuals must supply the last two years income tax returns and year-to-date profit and loss statement

**Important: Household income includes all adult individuals living in the home (except for full-time students), whether or not they will be included on the deed or the mortgage application.**

The financial institution will provide the program administrator with a copy of the income verifications and the program administrator will also calculate gross annual income to ensure accuracy.

### B. Equity from Previous Home

Equity from a home sold within the previous two years must be verified through a settlement statement.

Equity from a home still owned by the applicant must be verified through a preliminary settlement statement. The equity amount will be adjusted, if necessary, at the time of sale. The applicant must sell their previous home to be eligible for the gap loan program.

#### C. First Mortgage Verification

The financial institution must provide verification of the loan approval and a Good Faith Estimate of all pertinent information such as term, interest rate, mortgage product, etc.

#### D. Family Size Verification

Upon the local program administrator's request, the applicant must provide documentation of family size. The requested documentation will be in accordance with MHFA requirements.

#### E. Purchase Agreement/Contract with Contractor

The applicant must provide a purchase agreement or contract that stipulates the price of the home and all terms associated with the sale. The purchase agreement or contract must be signed by the buyers and the sellers. The purchase agreement should be contingent on the buyer's receipt of gap loan funding.

#### D. Related Costs Verification

The formula to determine a gap loan includes taxes, homeowners insurance, private mortgage insurance and closing costs. All of these costs will be estimated/determined by the local program administrator based on the best available information.

### **III. ELIGIBILITY AND QUALIFYING INCOME**

For purposes of the gap loan program, lenders must determine if an applicant's eligibility income is less than the limits established by the program. However, there may be cases where income included for the eligibility determination cannot be used to underwrite the first mortgage loan. For example, an applicant with a one-year history of overtime would have the overtime included in the calculation of eligibility income, but an underwriter typically requires a two-year history to use the income for loan qualification.

In cases where the eligibility and qualifying incomes are different, the first mortgage underwriter should document and explain the differences. If the explanation is reasonable and consistent with normal underwriting guidelines, the local program administrator can adjust the gap loan calculation so it is based on the qualifying income.

### **IV. CITY WATER AND SEWER REQUIREMENT**

GMHF requires that all funded units are connected to city sewer and water. This requirement applies to both subdivisions and scattered site units. The program administrator should determine that the property has city services before approving gap financing.

## **V. APPROVAL OF PROPERTY**

The contractor must provide the local program administrator with a sworn construction statement and contract sales price. The program administrator will review this information to ensure that program guidelines are being met. The program administrator will certify that each property meets the guidelines before final calculation of the gap loan amount.

## **VI. CLOSING/DOCUMENT PREPARATION**

The buyer should inform the administrator of the closing date, time and place at least 10 business days before closing. The gap loan request must be received by GMHF at least 5 business days prior to closing. All documentation will be reviewed to ensure all information is still valid and the gap loan amount is correct.

The documents to be prepared for the closing include:

- Gap Financing Form
- Gap Financing Mortgage
- Gap Financing Loan Note
- Request for Notice of Foreclosure
- Repayment Agreement
- GMHF Privacy Policy

Buyers are responsible for paying filing fees associated with gap loan legal documents.

The Greater Minnesota Housing Fund is exempt from the mortgage registration tax.

## **VII. INSPECTIONS**

Home inspections during the construction process and upon completion of the home will be the responsibility of the financial institution providing the first mortgage.

**ATTENTION:**  
**Greater Minnesota Housing Fund**  
**2003 Income Limits**  
**(80% of Statewide Median)**  
**Adjusted for Family Size**

<b>Family Size</b>	<b>GMHF Income Limits</b>
1	\$36,500
2	\$41,700
3	\$46,900
4	\$52,100
5	\$56,300
6	\$60,450
7	\$64,650
8	\$68,800

These income limits are guidelines you must follow when the Greater Minnesota Housing Fund provides financing to your housing project. If you do not follow these guidelines you put funding for your development at risk, as well as potential for future funding. Projects with other additional funding sources must also comply with the income limits set by those programs.

If you have questions about these guidelines, please call the Greater Minnesota Housing Fund at 1-800-277-2258 or 651-221-1997.

## Eligibility Income Information

All of the following sources must be considered in the calculation of the household's gross eligibility income. This information should be collected by the first mortgage lender and copies of verification should be provided to the gap loan program administrator.

<b>Enter Gross Annual Income for Each:</b>	<b>Co-Applicant 1</b>	<b>Co-Applicant 2</b>	<b>Co-Applicant 3</b>
Gross Salary			
Overtime Pay			
Commissions			
Bonuses			
Part-time Employment Earnings			
Interest			
Dividends			
Tips			
Gains on Sale of Property or Securities			
Annuities			
Pensions			
Royalties			
Veterans Administration Compensation			
Net Rental Income			
Alimony			
Child Support			
Public Assistance			
Sick Pay			
Social Security			
Business Activity or Investment Income			
Unemployment Compensation			
Estate or Trust Income			
Other			
<b>TOTAL</b>	(CALCULATION)	(CALCULATION)	(CALCULATION)

Total Gross Annual Household Income: (CALCULATION)

**To:** GMHF-funded organizations  
**Date:** February 3, 2003  
**Re:** Updated Total Development Cost Limits

This document outlines GMHF's new total development cost (TDC) limits, as well as some key definitions to clarify how TDC is calculated. Please review carefully and contact GMHF with any questions at 800.277.2258 or 651.221.1997. You can also reach the program officer assigned to your project at:

Stephanie Omersa, [somersa@gmhf.com](mailto:somersa@gmhf.com)  
 Dan Jenney, [djenney@gmhf.com](mailto:djenney@gmhf.com)  
 Paige Kahle, [pkahle@gmhf.com](mailto:pkahle@gmhf.com)

### **GMHF 2003 Single-Family TDC Limits**

In response to rising development costs and the needs of larger families, Greater Minnesota Housing Fund (GMHF) has developed a tiered total development cost (TDC) limit for single-family homes receiving GMHF interim and/or homebuyer gap financing. These limits apply to GMHF's entire service area.

<b>Number of Children in Household</b>	<b>Total Development Cost Limit</b>	<b>Minimum Space to Finish<sup>1</sup></b>
<u>0 —1 Child</u>	<u>\$131,000</u>	<u>2 bedrooms, 1 bath OR 3 bedrooms, 1 bath</u>
<u>2 Children</u>	<u>\$135,000</u>	<u>3 bedrooms, 1 bath OR 2 bedrooms, 2 bath</u>
<u>3 Children</u>	<u>\$140,000</u>	<u>4 bedrooms, 1 bath OR 3 Bedrooms, 2 bath</u>
<u>4+ Children</u>	<u>\$144,000</u>	<u>4 bedrooms, 2 bath<sup>o</sup></u>

Please note the following guidelines regarding this increase:

- 1) Basic appliances a refrigerator and a range, at a minimum are now required for all homes financed with GMHF financing (interim and/or gap). These items must be included in the applicable total development cost limit.
- 2) The new limit applies to homes with purchase agreements signed in 2003. If the purchase agreement was signed in 2002, last year's limit of \$126,000<sup>2</sup> still applies even if the sale will close in 2003.
- 3) Many buyers using GMHF gap financing also obtain a CASA mortgage loan through MHFA. MHFA has recently changed its policy to allow the buyer or seller to pay the required two points for CASA loans. GMHF encourages developers to include the CASA

<sup>1</sup> If costs allow, additional space can be finished off. This would need to be arranged through agreement between the homebuyer and the builder.

<sup>2</sup> \$128,000 for those developments in the First Homes service area.

points within the TDC limit. If this is not possible, CASA points may be in addition to the TDC price limit.

- 4) Buyer closing costs are not subject to the TDC limit. However, costs that are typically included in the purchase price, such as realtor fees and appliance packages, should be part of the TDC and not included in closing costs. Please review your project award packet for more information about closing costs.
- 5) For a limited number of projects, GMHF and developers have agreed on lower TDC limits. This increase does not affect those agreements. However, most projects will be subject to the new TDC limit. If you have questions about the status of your project, please contact a program officer at GMHF.

We hope that these increases will help you address the challenge of rising housing development costs in greater Minnesota and that the tiered structure makes the program more attractive to families with children.

*Note: New 2003 Income Limits are expected from HUD in February. You will receive the updated limits as soon as they are available.*

## The Difference between Total Development Cost & Sales Price

There is often confusion about the difference between total development cost and sales price. The fact that different funders sometimes use different guidelines to set cost limits can make it more confusing. As an example, GMHF's single-family programs have a Total Development Cost limit, while MHFA's CASA program has a Home or Acquisition Cost limit, which most often equates to a Sales Price.<sup>3</sup>

Given that funding sources are often layered, it is important to understand the distinction and apply the more restrictive cost limit when layering funding. Below are definitions, as well as an example, that are meant to clarify these terms and how they relate to the financing of a single-family home.

**Total Development Cost (used by GMHF to establish a cost limit)** Include ALL costs associated with development, regardless of funding source, such as TIF or abatement or gap. Include costs of land, infrastructure, hard construction costs and soft costs, such as developer fees, insurance, interest, etc. TDC does not include buyer closing costs or prepaids (insurance, loan fees, etc.).

**Sales Price** This number is the TDC less any local financial contributions, such as TIF or abatement, that have the effect of reducing the cost of the house to the buyer. (Most often equates to MHFA's Home or Acquisition Cost limit for the CASA program.)

### EXAMPLE:

Total Development Cost	\$125,000
less TIF	-7,000
Sales Price	\$118,000

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<sup>3</sup> For a precise definition of acquisition cost, please contact MHFA.