

Documentation Requirements for Retirement Reserves

About The Author

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In the past before the market changed, it was common practice to list retirement funds on the 1003 at either 70% of the vested account value for conventional loans or 60% of the vested value if a government loan. As long as the borrower wasn't utilizing the account funds for their downpayment or closing costs, we didn't need to document the terms of withdrawal. However, dependent upon the type of retirement account in question, we may need documentation in our file justifying the amount of funds listed for reserve. This is particularly important when the difference between an AUS approval or referral is due to the amount of reserves listed on the 1003.

Listed below are the retirement funds documentation requirements for the agencies.

Fannie Mae Requirements

Fannie Mae defines liquid financial reserves as those liquid or near liquid assets that are available to a borrower after the mortgage closes. Liquid financial reserves include cash and other assets that are easily converted to cash. Examples of liquid financial assets that can be used for reserves include:

- checking or savings accounts;
- investments in stocks, bonds, mutual funds, certificates of deposit, money market funds, and trust accounts;
- the amount vested in a retirement savings account;
- the cash value of a vested life insurance policy.

The following **cannot** be counted as part of the borrower's reserves:

- funds that have not been vested;
- funds that cannot be withdrawn under circumstances other than the account owner's retirement, employment termination, or death;
- stock held in an unlisted corporation;
- stock options and non-vested restricted stock;
- unsecured borrowed funds;
- interested party contributions (IPCs); and
- cash proceeds from a cash-out refinance transaction.

When funds from retirement accounts are used for reserves, Fannie Mae does not require the funds to be withdrawn from the account(s). However, lenders must exercise caution when considering retirement accounts as effective reserves because these accounts often feature significant penalties for early withdrawals, allow limited access, or have vesting requirements.

To account for withdrawal penalties and estimated taxes, lenders must include only 60% of the vested amount in its determination of the borrower's available reserves. If the retirement account only allows withdrawals in connection with the borrower's employment termination, retirement, or death, the lender should not consider the vested funds as effective reserves.

Therefore, depending on the type of account being listed as reserve, we as the lender must verify the potential terms of withdrawal in order to effectively prove that (1) the funds can be liquidated if needed; and (2) to verify the amount that CAN be liquidated.

Freddie Mac Requirements

Streamlined Accept Documentation Requirement

Account Type is a Personal IRA and SEP-IRA accounts that are owned by the Borrower, 401(k), KEOGH, 403(b) and other IRS-qualified employer plans

Required Documentation is: Most recent statement reflecting the vested balance or the percent of vesting, any outstanding loans, the ending balance as of the end of the statement and conditions under which the funds may be withdrawn or borrowed. If the assets are required for closing, proof of liquidation

Standard Documentation Requirements:

Account Type is a: Personal IRA and SEP-IRA accounts that are owned by the Borrower, 401(k), KEOGH, 403(b) and other IRS-qualified employer plans

Required Documentation is: Most recent two months statements reflecting the vested balance or the percent of vesting, any outstanding loans and the ending balance as of the end of the statement and conditions under which the funds may be withdrawn or borrowed. If the assets are required for closing, proof of liquidation is required.

FHA Requirements

If the loan application is rated as an “Accept/Approve”, document the borrower’s assets to close and cash reserves, if any, using the following:

Cash Reserves---Verify all cash reserves available after closing that are submitted to the AUS. Note that cash reserves after closing are not required on FHA mortgages (except when purchasing 3- or 4-unit properties) but are evaluated in determining the risk classification of the loan.

Cash reserves may include certain retirement accounts. To account for withdrawal penalties and taxes, only 60% of the vested amount of the account may be used. The lender must document the existence of the account with the most recent depository or brokerage account statement. In addition, evidence must be provided that the retirement account allows for withdrawals for conditions other than in connection with the borrower's employment termination, retirement, or death. If withdrawals can only be made under these circumstances, the retirement account may not be included as cash reserves. If any of these funds are also to be used for loan settlement, that amount must be subtracted from the amount included as cash reserves.

Retirement Accounts---Obtain the most recent statements for each account to verify sufficient funds to close. Document the terms and conditions for withdrawal and/or borrowing and that the borrower is eligible for these withdrawals. Use only 60 percent of the amount in the account unless the borrower presents documentation supporting a greater amount after subtracting any taxes or penalties for early withdrawal. Evidence of liquidation is not required.

If the loan application is rated as a “Refer”, document the borrower’s assets to close and cash reserves, if any, using the following:

Cash Reserves---Verify all cash reserves available after closing that are submitted to the AUS. Note that cash reserves after closing are not required on FHA mortgages (except when purchasing 3- or 4-unit properties) but are evaluated in determining the risk classification of the loan.

Cash reserves may include certain retirement accounts. To account for withdrawal penalties and taxes, only 60% of the vested amount of the account may be used. The lender must document the existence of the account with the most recent depository or brokerage account statement. In addition, evidence must be provided that the retirement account allows for withdrawals for conditions other than in connection with the borrower's employment termination, retirement, or death. If withdrawals can only be made under these circumstances, the retirement account may not be included as cash reserves. If any of these funds are also to be used for loan settlement, that amount must be subtracted from the amount included as cash reserves. Note: To be considered as a compensating factor when manually underwriting, there must be three months’ worth of such reserves.

Retirement Accounts---Obtain the most recent statements for each account to verify sufficient funds to close. Document the terms and conditions for withdrawal and/or borrowing and that the borrower is eligible for these withdrawals. Use only 60 percent of the amount in the account unless the borrower presents documentation supporting a greater amount after subtracting any taxes or penalties for early withdrawal. Evidence of liquidation is not required.

VA Requirements

VA does not address the documentation requirements of retirement accounts in either the VA Lender’s Handbook or the DU User’s Guide for VA Loans but I feel it safe to assume that the documentation requirements would be the same as we can see they are according the other agencies.

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