

## **Attachment**

### **Requirements for borrowers using Self Employment income to qualify**

**Effective:** These policies remain effective for loans where the most recent tax return being used to document and support qualifying income is older than 2020.

#### **Income Analysis**

Self-employment income is variable in nature and generally subject to changing market and economic conditions. Whether a business is impacted by an adverse event, such as COVID-19, and the extent to which business earnings are impacted can depend on the nature of the business or the demand for products or services offered by the business. Income from a business that has been negatively impacted by changing conditions is not necessarily ineligible for use in qualifying the borrower. However, stability and reasonable expectation of continuance of income must be determined.

When 2020 federal tax returns are not available, obtain the following additional documentation to support the decision that the self-employment income meets our requirements:

- An audited year to date profit and loss statement reporting business revenue, expenses, and net income up to and including the most recent month preceding the loan application date; or
- And unaudited year to date profit and loss statement signed by the borrower reporting business revenue, expenses, and net income up to and including the most recent month preceding the loan application date, and three business depository account(s) statements no older than the latest three months represented on the year-to-date profit and loss statement.
  - For example, the business depository account statements can be no older than August, September, or October for a year-to-date profit and loss statement dated through October 31<sup>st</sup>.
  - The three most recent deposit account statements must be reviewed to support the level of business revenue reported in the current year-to-date profit and loss statement. Otherwise, an additional statement or other documentation to support the ongoing nature of the business revenue reported in the current year-to-date profit and loss statement must be obtained.

**Note:** *The year-to-date profit and loss statement must be no older than 60 days old as of the note date.*

The profit and loss statement, business depository accounts if required, and other relevant factors must be reviewed to determine the extent to which a business is still being impacted by COVID-19. The following guidance can be used when performing the assessment of business operations and stability and must complete the business income assessment based on the minimum additional documentation above. In some instances, it may be necessary to obtain supplemental documentation listed in the examples below.

Assessing the Impact of COVID-19	
Business Operations	<ul style="list-style-type: none"> <li>Have business operations been maintained or modified to support continued business income? <i>For example, review an updated business plan.</i></li> <li>Is the business continuing to operate in the current location or an alternated location suitable for business operations? <i>For example, perform an Internet search or verify through a third-party source.</i></li> <li>Is there a demand for the business's product or service currently offered? <i>For example, obtain current business receipts or purchase contracts.</i></li> <li>Is the business operation and/or revenue temporarily restricted due to state shelter in place, stay at home, or other similar state or local orders?</li> <li>Is the impact on the business operations negligible due to the nature of the business? <i>For example, obtain a written explanation from the business owner or confirmation that income is seasonal apart from the event timeline.</i></li> </ul>
Business Income	<p>A business income assessment must be completed by comparing the year-to-date net business income from the year-to-date profit and loss statement to historical business income calculated using the Cash Flow Analysis (Form 1084, or equivalent)) for a similar timeframe (such as monthly).</p> <ul style="list-style-type: none"> <li>Standard adjustments can be made to the business cash flow (net income on the profit and loss statement).</li> <li>If determined that the net business income is impacted, but profit and loss details are not sufficient to determine the income is stable at the reduced level, additional documentation can be obtained to supplement the profit and loss statement (such as a month-to-month income trending analysis) to make this determination. If stability cannot be confirmed, the income is not eligible for qualifying purposes.</li> </ul> <p><b>Example:</b>  <i>Historical monthly self-employment income calculated using Form 1084 (or equivalent) = \$2,000.</i>  <i>The current level of stable monthly Self Employment income as determined using details from the year-to-date profit and loss statement and other supplemental documentation = \$1,000</i>  <i>The impact of the COVID 19 pandemic on current business income results in a 50 decline from historical levels. See <u>Business Income Calculation Adjustment</u> below for steps.</i></p>

<b>Business Stability</b>	<ul style="list-style-type: none"> <li>• Does the profit and loss identify a significant imbalance between expenses and revenue that may impact financial stability? Or have modifications to current business operations been made to correct this imbalance? <i>Consider documenting with an updated business plan.</i></li> <li>• Do prior year business tax returns demonstrate ample financial liquidity due to a history of retained earnings?</li> <li>• Do current business account balances (excluding Paycheck Protection Program (PPP) or other similar COVID-19 related loans or grants) support the financial ability of the business to operate given current market and economic conditions?</li> </ul> <p>A current balance sheet may be used to support the determination of business stability in conjunction with the profit and loss statement.</p>
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### **Business Income Calculation Adjustment**

When it is determined current year net business income is still being impacted by the COVID-19 pandemic and is:

- Less than the historical monthly income calculated using Form 1084 (or equivalent) but is stable at its current level; the amount of qualifying income must be reduced to no more than the current level of stable income as calculated.
- More than the historical income calculated using Form 1084 (or equivalent), no more than the current stable level of income can be used to qualify the borrower.

In all cases, qualifying income must be supported by documentation, including any supplemental documentation, and must be included in the loan file.