Mid America Mortgage, dba 1st Tribal Lending, Pinole, CA

Section 184 Loan Guarantees for Indian Housing Program

Office of Audit, Region 9
Los Angeles, CA

Audit Report Number: 2020-LA-1005
September 3, 2020

To: Heidi Frechette
Deputy Assistant Secretary, Office of Native American Programs, PN

//SIGNED//
From: Tanya E. Schulze
Regional Inspector General for Audit, 9DGA

Subject: Mid America Mortgage, dba 1st Tribal Lending, Pinole, CA, Did Not Always Follow HUD's Section 184 Program Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Mid America Mortgage's, dba 1st Tribal Lending's, Section 184 program.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, appendix 8M, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at https://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at 213-534-2471.

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Mid America Mortgage, dba 1st Tribal Lending, Pinole, CA, Did Not Always Follow HUD's Section 184 Program Requirements

Highlights

What We Audited and Why

We audited Mid America Mortgage's, dba 1st Tribal Lending's, Section 184 Indian Home Loan Guarantee program based on a previous U.S. Department of Housing and Urban Development (HUD), Office of Inspector General, audit and corrective action verification of the Section 184 program, which determined that HUD lacked proper oversight of the program and lenders did not always underwrite loans in accordance with HUD's requirements. The lender was selected because it is the largest Section 184 program lender. Our audit objective was to determine whether the lender underwrote Section 184 loans in accordance with HUD's requirements.

What We Found

The lender did not always follow HUD's Section 184 program requirements. Specifically, it did not always (1) underwrite Section 184 loans in accordance with program requirements and (2) follow HUD's quality control requirements when reviewing loan files. This condition occurred because the lender did not always exercise due diligence when underwriting loans and did not strictly follow HUD's underwriting and quality control requirements. As a result, there was an increased risk to the Section 184 program and HUD's Loan Guarantee Fund. There were 11 loans with material underwriting deficiencies and we recommend indemnification for 7 of these loans. The seven loans had a total unpaid mortgage balance of $1.3 million with an estimated potential loss to HUD of $607,598.

What We Recommend

We recommend that the Deputy Assistant Secretary for Native American Programs (1) request indemnification for 7 of the 11 loans[1] that had material underwriting deficiencies and had an unpaid mortgage balance of $1.3 million with an estimated potential loss to HUD of $607,598, (2) require the lender to develop and implement enhanced policies and procedures to ensure electronic signatures from borrowers are properly supported, and (3) require the lender to fully implement its quality control plan with respect to reverifications and provide HUD with periodic reports for 12 months to ensure that its quality control reviews are conducted in accordance with the requirements.

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[1] One loan did not have a mortgage balance, and after the draft audit report was issued, the lender provided support to resolve deficiencies identified for three loans.

Table of Contents

Background and Objective

Under the provisions of Section 184 of the Housing and Community Development Act of 1992 and as amended by the Native American Housing Assistance and Self-Determination Act of 1996, the U.S. Department of Housing and Urban Development (HUD) was authorized to guarantee loans made by private lenders to Native Americans, Indian housing authorities or tribally designated housing entities, and tribes. The Section 184 Loan Guarantees for Indian Housing program is a home mortgage product specifically designed for American Indian and Alaska Native families, Alaska villages, tribes, or tribally designated housing entities. A borrower may use a Section 184 loan, both on and off native lands, for new construction, rehabilitation, purchase of an existing home, or refinance of single-family housing.

The Section 184 Loan Guarantee Program assures the lender that its investment will be repaid in the event of a foreclosure. The program is funded in part by annual appropriations and fees paid by borrowers that obtain loans through the program.

Section 184 loans are processed through direct guarantee lenders. The direct guarantee program is similar to the Federal Housing Administration's (FHA) direct endorsement program in that approved lenders underwrite and close loans before HUD issues the loan guarantee certificate. To participate in the program, lenders must be approved by HUD, receive Section 184 training, and initially go through a test case process to ensure that their loans comply with HUD's requirements.

Loans involving fraud, misrepresentation, or serious and material violations of HUD policies and procedures that significantly increase HUD's risk may result in a request for indemnification by the lender. Under the terms of an indemnification, the lender is required to:

- Abstain from filing an insurance claim; or
- If an insurance claim has been paid and the property has been conveyed to HUD, accept reconveyance of the property and reimburse HUD for any expenses or claims paid to date; or
- If an insurance claim has been paid to the lender or a subsequent holder of the loan, and the property has been sold to a third party, reimburse HUD for any financial loss suffered in disposing of the property.

HUD's Office of Loan Guarantee, within the Office of Native American Programs, guarantees mortgage loans made to eligible borrowers. As of November 2018, there were more than 42,000 loans insured for more than $7 billion under the Section 184 program.

Mid America Mortgage was established in 1940, under the name Frank A. Schmidt & Son's, and was located in Cleveland, OH. In 2010, the company relocated the corporate office to Addison, TX. In 2011, the company name was changed to Mid America Mortgage. The lender also does business as 1st Tribal Lending, located in Pinole, CA. This division focuses on Section 184 loans and has been the largest Section 184 program lender. The lender received approval to participate in the

Section 184 program in 2011 and from January 1, 2016, through December 31, 2018, originated 2,474 Section 184 loans totaling $477.9 million.

Our audit objective was to determine whether Mid America Mortgage, dba 1st Tribal Lending, underwrote Section 184 loans in accordance with HUD requirements.

Results of Audit

Finding: Mid America Mortgage, dba 1st Tribal Lending, Did Not Always Follow HUD's Section 184 Program Requirements

Mid America Mortgage, dba 1st Tribal Lending, did not always follow the requirements for the Section 184 program. Specifically, the lender did not always (1) underwrite Section 184 loans in accordance with program requirements and (2) follow HUD's quality control requirements when reviewing loan files. This condition occurred because the lender did not always exercise due diligence when underwriting loans and following HUD's quality control requirements. As a result, there was an increased risk to the Section 184 program and HUD's Loan Guarantee Fund. There were 11 loans with material underwriting deficiencies and we recommend indemnification for 7 of these loans. The seven loans had a total unpaid mortgage balance of $1.3 million with an estimated potential loss to HUD of $607,598.

Eleven Section 184 Loans Had Material Underwriting Deficiencies

We reviewed 30 Section 184 loans that were underwritten by the lender and determined that 8 (27 percent) had material underwriting deficiencies. We also reviewed 12 additional Section 184 loans underwritten by the lender to perform a limited review of borrower's signatures on the loan documents. We determined that 3 loans, 2 as part of the additional sample of 12 and 1 as part of the original 30 loans, contained borrower income, credit, or asset documents with questionable and unsupported borrower signatures that were not appropriately identified or resolved during the underwriting process.

Table 1 – Loans with material deficiencies

Case number	Deficiency type					Unpaid balance	Estimated potential loss to HUD[2]
	Income	Credit	Assets	Other	Signatures		
044-101639				■		$ 199,854	$ 93,931
265-100661	■	■				192,989	90,705
303-100496				■		210,587	98,976
405-116972		■				56,454	26,533
405-117477		■				194,683	91,501
451-100084	■	■	■			255,010	119,855
531-101910		■				183,186	86,097
Subtotals	**2**	**5**	**1**	**2**	**0**	**1,292,763**	**607,598**
463-100338		■				0	0
531-101818					■	364,474	171,303
531-101941					■	397,892	187,009
531-102058					■	301,322	141,621
Subtotals	**0**	**1**	**0**	**0**	**3**	**1,063,688**	**499,933**
Totals	**2**	**6**	**1**	**2**	**3**	**2,356,451**	**1,107,531**

2 Based on FHA's loss rate of 47 percent for single-family loans. The FHA loss rate was used because FHA sells the foreclosed-upon properties that were secured by a Section 184 loan guarantee.

We determined the underwriting deficiencies were material because the lender did not follow the Section 184 processing guidelines and the deficiencies identified were significant enough that they affected the eligibility of the loan. The table above summarizes the loans and types of material deficiencies identified.[3]

Lenders must follow the Section 184 processing guidelines in order for HUD to guarantee a Section 184 loan (appendix C). The lender exhibited a lack of due diligence in determining whether the loan complied with program requirements or resolving the unusppported borrower signatures when it approved the 11 loans with the below cited deficiencies. The material underwriting deficiencies included inadequate determination or documentation of income, credit, assets, the appraisal report, and borrower signatures.

Income

The material underwriting deficiencies for two loans related to income included improper calculation of monthly income. For example, for loan 265-100661, the lender did not properly calculate the borrower's monthly per capita[4] income. The Section 184 processing guidelines state that per capita income may be used provided the tax returns show a 2-year receipt history and the income must be averaged over the 2 years (appendix C). However, it appeared that the lender calculated the income by averaging the reported amount received during the most recent 16.5 months. As a result, the borrower's monthly income was overstated by approximately $633, and the associated debt-to-income ratio increased from 38.26 to 43.53 percent, which exceeded HUD's required limit of 41 percent.

Credit

The material underwriting deficiencies for six loans related to credit included (1) improperly excluding liability accounts, (2) no evidence that collection accounts were paid in full, and (3) no explanation to address a significant increase in the borrower's projected housing expense. For example, for loan 531-101910, the lender did not verify that the borrower's three collection accounts were paid in full as required. Instead, the lender relied on a letter from the borrower's Tribe, which stated that it was in the process of paying off the collection accounts. The Section 184 processing guidelines state that all collections must show evidence of payment in full before the closing date (appendix C).

Assets

The material underwriting deficiencies for one loan related to borrower assets included gift funds that were not properly documented. For example, for loan 451-100084, the borrower received a $1,000 gift from a family member; however, the lender did not obtain the required gift letter from the donor, stating that no repayment was required. In this case, the gift funds were used as part of the borrower's cash required to close.

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3 We did not recommend indemnification for the four loans shaded in gray because one loan did not have a mortgage balance, and after the draft report was issued, the lender provided support to validate the questionable and unsupported borrower signatures for three loans.

4 Per capita income is a form of income commonly paid to tribal members from tribal trust income.

Other

The material underwriting deficiencies related to other items for two loans included (1) the loan-to-value ratio exceeding the required limit and (2) the debt-to-income ratio exceeding HUD's 41 percent limit without qualifying for two compensating factors. For example, for loan 303-100496, the debt-to-income ratio of 42.47 percent exceeded HUD's 41 percent limit, and the borrower did not qualify for two compensating factors as required. The lender used 6 months of borrower cash reserves as one of the compensating factors; however, the borrower did not have at least 6 months of reserves. The Section 184 processing guidelines state that a debt-to-income ratio of up to 43 percent may be acceptable if at least two of five compensating factors are presented. The guidelines list five compensating factors, such as a credit score of 700 or greater and substantial cash reserves after closing (6 months or greater) (appendix C).

Borrower Signautres

The material underwriting deficiencies for three loans related to questionable and unsupported borrower signatures. For example, for loan 531-102058, a letter that was purportedly from the borrower explaining the source of three bank deposits included an electronically printed signature that was inconsistent with other documents that had an electronic signature (that is, no document identification number or associated electronic signature certificate of completion). This discrepancy was not resolved and properly documented in the loan file. After the draft audit report was issued, the lender provided support to validate one loan document signature from each of the three loan files.

Quality Control Requirements Were Not Always Followed

The lender did not always follow HUD's quality control requirements when reviewing Section 184 loans. Our review of 12 Section 184 quality control files determined the lender did not reverify all of the required information for 3 loans. Specifically, the lender did not obtain a credit report for all borrowers on the loans as required by the Section 184 processing guidelines. We also noted that a reverification of rent was not conducted for four loans. This condition occurred because the lender did not conduct its due diligence to reverify credit and rent documents when it received the quality control loan files.

Conclusion

There was an increased risk to the Section 184 program and HUD's Loan Guarantee Fund because the lender did not always comply with HUD's Section 184 program requirements. We recommend indemnification for seven loans with material underwriting deficiencies. These seven loans had a total unpaid mortgage balance of $1.3 million and an estimated potential loss to HUD of $607,598. This occurred because the lender did not always exercise due diligence when underwriting loans and applying HUD's quality control requirements.

Recommendations

We recommend that Deputy Assistant Secretary for Native American Programs

1A. Request indemnification for the 7 of the 11 loans[5] that had material underwriting deficiencies (appendix D). The unpaid balance for these loans is $1.3 million and the estimated potential loss to HUD is $607,598.

1B. Require the lender to develop and implement enhanced policies and procedures to ensure electronic signatures from borrowers are properly supported.

1C. Require the lender to fully implement its quality control plan with respect to reverifications and provide HUD with periodic reports for 12 months to ensure that it conducts its quality control reviews in accordance with the requirements.

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[5] We did not recommend indemnification for four loans (see Table 1), because one loan did not have a mortgage balance, and after the draft audit report was issued, the lender provided support to validate the questionable and unsupported borrower signatures for three loans.

Scope and Methodology

We performed our audit field work from June to December 2019 at 1st Tribal Lending's office located in Pinole, CA, and remotely at the Office of Inspector General (OIG), Office of Audit, in Phoenix, AZ. Our audit period covered loans that were originated by the lender and guaranteed by HUD from January 1, 2016, to December 31, 2018.

To accomplish our objective, we

- reviewed applicable HUD requirements for the Section 184 program;
- interviewed appropriate management and staff from the lender and HUD;
- obtained and reviewed a report provided by HUD of all Section 184 loans originated by the lender and guaranteed from January 1, 2016, to December 31, 2018;
- obtained and reviewed a report provided by the lender of all Section 184 loans funded from January 1, 2016, to December 31, 2018;
- obtained and reviewed servicing reports from January 2018 to May 2019 provided by HUD and the lender;
- selected and reviewed 42 Section 184 loans that were underwritten by the lender and guaranteed by HUD;
- reviewed source documents in the loan files related to income, liabilities, assets, and the appraisal; and
- obtained the quality control logs from the lender for July to December 2018 and reviewed a sample of 12 quality control files.

We obtained a report from HUD of Section 184 loans originated by the lender and guaranteed by HUD from January 1, 2016, to December 31, 2018. During this period, there were 2,474 loans, which totaled $477.9 million in loan guarantees. We also obtained servicing reports and a report of Section 184 loans that were funded from January 1, 2016, to December 31, 2018, from the lender. From these reports, we selected a nonrepresentative sample of 30 loans that were targeted based on the delinquency status or indications that the loan did not comply with HUD's requirements, such as the loan-to-value ratio exceeding the required limit. We also selected a nonrepresentative sample of 12 loans to perform a limited review of the borrower's signatures on the loan documents. The sample was targeted based on loans that were originated by a specific loan officer because a loan file originated by that loan officer had an inconsistent borrower signature on a loan document. We determined the two samples selected above were sufficient to accomplish our objective. The audit results only apply to the sampled loans and cannot be projected to the larger universe.

For the quality control review, we obtained the quality control reports from the lender for July to December 2018. There were 70 quality control reviews of Section 184 loans during this period. We selected a nonrepresentative sample of 12 quality control loans to examine. We determined the sample was sufficient to accomplish our objective. The audit results only apply to the sample quality control loans and cannot be projected to the larger universe.

While we did rely on reports from HUD and the lender to identify the universe of loans and target loans for the sample, we used the source documents from the loan files to determine whether the loans were underwritten and approved in accordance with HUD's requirements. Therefore, we did not rely on computer-processed data to reach our conclusions and did not assess the reliability of the data provided by HUD and the lender.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Internal Controls

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- effectiveness and efficiency of operations,
- reliability of financial reporting, and
- compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective:

- Controls intended to ensure that the lender underwrites (approves) Section 184 loans in accordance with HUD's requirements.
- Controls intended to ensure that the lender implements a quality control program that complies with HUD's requirements.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

Based on our review, we believe that the following items are significant deficiencies:

- The lender did not have adequate controls to reasonably ensure that loans were underwritten in accordance with HUD's requirements (finding).
- The lender did not have adequate controls to ensure that its quality control program complied with HUD's requirements (finding).

Appendixes

Appendix A

Schedule of Funds to Be Put to Better Use

Recommendation number	Funds to be put to better use 1/
1A	$607,598
Total	**607,598**

1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this instance, implementation of recommendation 1A to indemnify loans not approved in accordance with HUD's requirements will reduce HUD's risk of loss to the loan guarantee fund. The amount noted reflects HUD's calculation that FHA loses an average of 47 percent of the unpaid principal balance when it sells a foreclosed-upon property. The FHA loss rate was used because FHA sells the foreclosed-upon properties that were secured by a Section 184 loan guarantee. The 47 percent loss rate is based on HUD's Single Family Acquired Asset Management System's "case management profit and loss by acquisition" computation for the fourth quarter of fiscal year 2019 based on actual sales.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation | **Auditee Comments**

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MID AMERICA MORTGAGE, INC.

April 24, 2020

Ms. Tanya E. Schulze
Regional Inspector General for Audit
Office of Inspector General
300 N. Los Angeles Street, Room 4070
Los Angeles, CA. 90012

Via E-mail to tschulze@hudoig.gov

Re: Mid America Mortgage, Inc. HUD OIG Draft Audit Report

Dear Ms. Schulze:

Mid America Mortgage, Inc. ("MAM") is in receipt of the discussion draft audit report ("Report") from the U.S. Department of Housing and Urban Development ("HUD") Office of Inspector General ("OIG"). The Report is based upon a review of MAM's underwriting practices and procedures in connection with its Section 184 Indian Home Loan Guarantee program. A previous OIG audit of HUD's Native American Programs determined that HUD lacked proper oversight of these programs and lenders did not always underwrite loans in accordance with HUD's requirements. MAM, doing business as 1st Tribal Lending, was selected for audit because MAM is one of the largest, if not the largest, Section 184 program lenders.

Comment 1

The report contains two findings, alleging that MAM did not always underwrite Section 184 loans in accordance with HUD requirements or did not always follow HUD's quality control requirements. The OIG has provided MAM with the opportunity to submit a written response to the Report prior to preparation and publication of the final report. This response summarizes MAM's history with HUD's Native American housing and community development programs and addresses the findings in the Report. We appreciate the opportunity to comment on the OIG's findings and recommendations.

I. INTRODUCTION

In September of 2011, MAM formed its 1st Tribal Lending division ("1st Tribal"), with the goal of becoming a long term, committed ONAP program lender. That goal has been realized, as 1st Tribal is now one of the largest, if not the largest, Section 184 program lenders. As part of the evolution of this line of business, 1st Tribal has developed a unique set of cultural sensitivities to the ONAP market it serves. Further, to our knowledge, MAM/1st Tribal may also be the only nationwide lender which lends to the entire scope of the ONAP program. Most

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Comment 2

Section 184 lenders proceed cautiously by limiting their participation to high FICO score applicants, those with a fee simple interest in the real estate, or urban Indians. 1st Tribal, on the other hand, goes beyond those lower risk products and lends, when appropriate, against tribal trust properties and to low or no credit score borrowers. It is interesting to note that, notwithstanding 1st Tribal's broad-based willingness to extend credit through a wide array of ONAP programs, our servicing portfolio consistently outperforms the Federal Housing Administration universe, with lower delinquencies and defaults.

II. RESPONSE TO THE GENERAL FINDINGS

As previously noted, the Report contained two general findings. The first finding is that MAM did not always underwrite Section 184 loans in accordance with HUD requirements. The second is that MAM did not always follow HUD's quality control requirements for Section 184 loans.

A. First Finding Response – Underwriting.

Comment 1
Comment 3

MAM/1st Tribal concedes the likelihood that not all of its Section 184 loans were underwritten in strict conformity with the processing guidelines published by HUD/ONAP (the "Guidelines"). However, 1st Tribal asserts that all of its loans were underwritten consistent with oversight and guidance communicated by ONAP, in recognition of ONAP's unique products and programs. Because these are manually underwritten programs, which serve a population with cultural differences and without a long-term history of home ownership or rental obligations, ONAP has consistently communicated the need for flexibility in the application of common-sense underwriting practices. 1st Tribal understood this need and incorporated it into its underwriting practices, consistent with ONAP authorization and direction.

Comment 4

1st Tribal's position is based upon over nine years of frequent discussion and communication (both verbal and in writing) with Senior ONAP underwriting managers, as well as thousands of successful file endorsements by ONAP personnel. In the early years of the Section 184 program, ONAP personnel provided underwriting decisions and written guidance for specific loans when requested by lenders. Due to the growth of the program, ONAP's capacity was overwhelmed and the decision was made to delegate underwriting to lenders. ONAP was no longer permitted to decision specific files. However, 1st Tribal continued to consult with ONAP about complex scenarios or issues that were not clearly addressed in the Guidelines. MAM/1st Tribal was of the clear belief that ONAP empowered 1st Tribal to exercise discretion to make underwriting decisions on behalf of the ONAP programs, guided by and statutory rules relating to ONAP programs.

Comment 5

Recognizing confirmation of MAM's assertion may prove difficult given the recent retirement of both senior ONAP underwriters with whom 1st Tribal most frequently dealt, we

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reached out to [redacted], former and now retired Senior Loan Guarantee Specialist, HUD ONAP OLG. [redacted] is quite familiar with the working relationship we describe above and was kind enough to write a letter of explanation, which may further clarify MAM/1st Tribal's assertions. For convenience,attached is a copy of [redacted] letter, should OIG wish to review and give consideration to it.

B. Second Finding Response – Quality Control.

Comment 6

MAM outsources the post-closing quality control function. We became dissatisfied with the performance of the third party quality control vendor we contracted with during the time period the loans which are the subject of the Report, were originated. MAM/1st Tribal has retained a new vendor, which has resulted in a significant performance upgrade. We will continually monitor this vendor closely to ensure compliance with Section 184 post closing audit requirements. Also, our quality control program is audited annually.

III. RESPONSE TO SPECIFIC LOAN FINDINGS

MAM/1st Tribal has conducted its own stringent analysis of the loans which were the subject of the OIG's review. Based on MAM's diligent examination, the following addresses each finding with respect to specific loans.

Comment 7

Several of the eleven loans identified by OIG as containing underwriting deficiencies, were cited for "payment shock". With respect to these loans, we would like to point out that prior to underwriting each of them, 1st Tribal had been instructed by ONAP senior underwriting staff (not specifically as to these loans, but from a general underwriting perspective) that even if payment shock does not meet the Guideline standards, it should not be used as the sole basis for loan denial.

1. Case Number 044-101639

Comment 8

We concur with OIG's finding that the loan amount exceeded maximum loan-to-value ratio permitted under the program. The cause was an underwriter's inadvertent mathematical error, which resulted in the loan amount exceeding the maximum by $149. Based on our analysis, we do not believe the error was a material factor in the default of this loan, and propose the indemnification amount be reduced to amount of the error.

2. Case Number 265-100661

Comment 9

1st Tribal concurs that payment shock Guidelines were not strictly followed, but respectfully disagrees with the conclusion the debt-to-income ratio ("DTI") exceeded Section 184 processing Guidelines. To the contrary, our income calculation was reasonable and would

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Comment 10
Comment 3

pass generally recognized underwriting standards. Our underwriting decision was well documented, explained, and within 1st Tribal's delegated underwriting authority with respect to both payment shock and DTI. 1st Tribal respectfully requests reconsideration be given to indemnification for this loan.

3. Case Number 303-100496

Comment 11
Comment 3

We respectfully disagree with OIG's finding that the DTI exceeded 41% without the required two compensating factors. The underwriter used three compensating factors: excellent credit, greater than six months of reserves and additional income that could not technically be used, but would have dropped the DTI below 41%. 1st Tribal believes this to be a prudent exercise of its Section 184 delegated underwriting authority. Therefore, we respectfully request that this loan be removed from the indemnification list.

4. Case Number 405-116972

Comment 12
Comment 3
Comment 13

We respectfully disagree with OIG's conclusion regarding payment shock. 1st Tribal's assessment was well explained and documented. Kindly refer back to this documentation, which was provided to OIG during the course of the audit. However, even if OIG's payment shock assessment is correct, it falls well within 1st Tribal's delegated underwriting authority, as we understand it to be. The gap in employment was determined by our underwriters to be insignificant, immaterial and within our delegated underwriting authority. 1st Tribal respectfully requests reconsideration be given to indemnification for this loan.

5. Case Number 405-117477

Comment 14
Comment 3
Comment 15

1st Tribal acknowledges OIG's finding under the heading "Credit", but disagrees that the file lacked 24-month job history verification. Satisfactory employment history documentation was obtained and provided to OIG as part of the audit process. Also, the borrower's current employment as a school district administrator was considered very stable by the underwriter. The payment shock was carefully analyzed and was within our delegated underwriting authority.

6. Case Number 451-100084

Comment 16
Comment 3
Comment 17

1st Tribal disagrees with the finding that income was overstated and provided documentation to OIG in support of this position, during the course of the audit. We followed the Guidelines, as well as general underwriting principals to make a favorable credit decision under our delegated authority. Though a proper gift letter was not in the loan file, the gift was verified with the giftor's bank. We do not believe this was a material element in the borrower's default.

7. Case Number 463-100338

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This loan has been paid in full.

8. Case Number 531-101910

Comment 18

Comment 3

Comment 19

We respectfully disagree with OIG's assessment of collection risk. During the audit process, we provided a detailed explanation of our reasoning, in the context of the Guidelines. ONAP guidance to 1st Tribal has always provided more flexibility around medical collections due to disfunction within the Indian Health Services agency and tribal assistance which usually comes into play. We believe this decision to be well within our Section 184 delegated underwriting authority and immaterial to any default. 1st Tribal also disagrees with the revised DTI calculation by OIG and assert that our methodology falls within our delegated underwriting authority.

9. Case Number 531-101818; 10. Case Number 531-101941; & 11. Case Number 531-102058

Comment 20

1st Tribal acknowledges that proper e-sign certifications for the borrower(s)' letters of explanation were not obtained and forwarded by the mortgage broker. After identification by this audit, we obtained wet signatures on the relevant documents and have attached them to this response. In that the documents used to underwrite these loans have been obtained and because the documentation issue would not be a material factor in the default of this loan, we respectfully request that both of these loans be removed from the indemnification recommendations.

III. CONCLUSION

Comment 3

In summary, MAM/1st Tribal's thorough review of the findings in the Report indicates that not all of its Section 184 loans were underwritten in strict conformity with HUD requirements. However, all of the loans were underwritten in conformity with 1st Tribal's understanding of its Section 184 delegated underwriting authority. 1st Tribal's underwriting practices are constantly evolving, based upon guidance received from HUD/ONAP. Neither former nor current ONAP management has expressed disagreement with our underwriting approach. 1st Tribal strongly believes that its prudent exercise of Section 184 delegated underwriting authority has not and does not pose an increased risk to the Section 184 program or to HUD's Loan Guarantee Fund. To the contrary, 1st Tribal asserts that its application of Section 184 delegated underwriting authority is beneficial to the Section 184 program by broadening its scope, within the confines of sound lending practices, and by extending the reach of the program to the Native American communities it is designed to serve. On this basis, we respectfully request that OIG, HUD and ONAP reconsider each indemnification recommendation in the Report, for removal from the final report.

15301 Spectrum Dr., Suite 405, Addison, TX 75001 Phone: (866) 544-7013 Fax: (866) 740-0244

Ref to OIG Evaluation

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MID AMERICA
MORTGAGE, INC.

As a long- standing partner of HUD's ONAP, MAM/1st Tribal highly values its relationship with HUD and ONAP, and takes its responsibilities under the ONAP very seriously. We are dedicated to extending credit to qualified borrowers pursuant to HUD Guidelines, with the overlay of ONAP guidance. Our hope is that this audit process will provide some clarity to our role and responsibilities to ensure that unintended risk is not imposed upon HUD's Loan Guarantee Fund, ONAP, and MAM/1st Tribal. We look forward the long-term continuation of our ongoing, mutually beneficial relationship.

If you have any questions or need any additional information, please do not hesitate to contact Brett J. Robinson, 1st Tribal Managing Director at 510.856.2186, or me.

Thank you for your consideration.

Sincerely,

DocuSigned by:

Jeffrey E. Bode
President

15301 Spectrum Dr., Suite 405, Addison, TX 75001 Phone: (866) 544-7013 Fax: (866) 740-0244

OIG Evaluation of Auditee Comments

Comment 1 We appreciate the time and consideration put forth by Mid America Mortgage (lender) to review and respond to the audit report. Overall, the lender conceded that it likely did not always underwrite its Section 184 loans in strict conformity with the processing guidelines. The following comments respond to specific statements made by the lender in its response.

Due to privacy, we note that small portions of the lender's response were redacted (page 3 of the response) and the attachments (letter provided by a former HUD employee and three borrower-signed documents) were not included in this audit report but are available upon request.

Comment 2 We did not verify the lender's assertion that its servicing portfolio (of Section 184 loans) consistently outperformed the FHA loan universe. The audit objective and scope focused on the underwriting of certain Section 184 loans, as described in the scope and methodology section of the report, and did not include a review of or comparison to overall FHA loan performance.

Comment 3 The lender did not provide documented evidence to support its assertion that all of its loans were underwritten consistent with oversight and guidance communicated by ONAP. The audit report identified loans with material underwriting deficiencies that did not comply with the Section 184 processing guidelines and the lender did not provide evidence that ONAP authorized lenders the flexibility to deviate from the Section 184 processing guidelines.

The HUD OIG conducted a review of the HUD Office of Loan Guarantee Section 184 program in 2015 and determined that loans were not always underwritten in accordance with the Section 184 processing guidelines.[6] During that audit, ONAP agreed with the findings and at no time stated the Section 184 processing guidelines were flexible and that direct guarantee lenders were allowed to deviate from the guidelines.

Additionally, throughout its response, the lender refers to its delegated underwriting authority. The lender and ONAP (during the previously mentioned OIG audit in 2015) did not provide evidence that lenders were allowed the flexibility to deviate from the Section 184 processing guidelines.

Comment 4 The lender asserted that it continued to consult with ONAP about complex scenarios or issues that were not clearly addressed in the guidelines. We contend that the Section 184 processing guidelines directly addressed all of the

[6] Audit report 2015-LA-0002, issued July 6, 2015.

underwriting deficiencies identified in the loan summaries in appendix D of the audit report, and the identified deficiencies were not complex scenarios.

Comment 5 We reviewed the letter provided by the lender from the former ONAP employee and determined that it did not change the status of our findings.

Comment 6 The lender acknowledged performance issues with its third-party quality control vendor that was contracted during the time period of the indicated loan. The recommendation to ensure the lender fully implements the quality control plan remains unchanged and the lender can demonstrate to HUD during audit resolution that corrective action was taken.

Comment 7 The lender did not provide documentation or support for its assertion that ONAP instructed the lender that even if payment shock did not meet the guidelines that it should not be used as the sole basis for loan denial. However, we agree that a significant increase in the projected housing expense (payment shock) does not automatically require loan disapproval. The Section 184 processing guidelines state that lenders may document other reasonable compensating factors for loans that have a significant increase in the projected housing expense. For the loans identified in the audit report that had payment shock, the lender did not document reasonable compensating factors for loan approval. A list of compensating factors that could be used to allow for loan approval are provided in the Section 184 processing guidelines. While the list is not all inclusive, the lender should have included other reasonable compensating factors in addition to the base program eligibility requirements related to income, assets, and credit to support loan approval. The lender should address these loans with HUD during audit resolution.

Comment 8 The lender agreed that the loan amount exceeded the allowed maximum loan-to-value ratio but believes the underwriter’s mathematical error was not a material factor in the default of the loan. We did not question the deficiency as an element of the loan defaulting, but instead identified the exceeded maximum loan amount as a loan underwriting deficiency. The Section 184 processing guidelines and 12 USC (United States Code) 1715z-13a state that loans shall not exceed 97.75 percent of the appraised value. Lenders must follow these requirements in order for loans to be eligible for the Section 184 program.

Comment 9 We disagree with the lender’s response that its income calculation was reasonable and well documented. The Section 184 processing guidelines state that per capita income may be used, provided that tax returns support a 2-year receipt history, and the income must be averaged over the 2 years. The tax documents in the loan file showed the borrower received $48,000 and $62,400 over the past 2 years (2014 and 2015), which averages $4,600 per month. During the audit, the lender stated the borrower turned 18 in 2014 so they would not have received per capita payments until March 2014. Therefore, the lender determined the average monthly per capita income based on the prior year (2015) and current year to date per capita income, which resulted in $5,236 per month. However, the guidelines do not provide exceptions in calculating the per capita income.

Comment 10 We agree with the lender's response that the payment shock guidelines were not strictly followed but disagree that its underwriting decision was well documented, explained, and within a delegated underwriting authority. As stated in the audit report, the lender did not document or support that the borrower exhibited an ability to accumulate savings or that they had the ability to manage their financial affairs. The lender also did not document other reasonable compensating factors to offset the loan having a significant increase in the projected housing expense.

Comment 11 We disagree that the borrower qualified for two of the three compensating factors provided in the lender's response. Regarding the compensating factor of greater than 6 months of reserves, we determined the borrower had reserves of 5.87 months. The lender determined the borrower had verified assets of $12,892; however, we determined the assets totaled $11,615, an overstatement of $1,277. This overstatement was a result of the lender using assets of $1,958 from a verification of deposit for one of the borrower's bank accounts (Glacier Bank) that was dated May 25, 2016. However, a more recent bank statement in the loan file was dated June 16, 2016, and showed a balance of $681. Therefore, the verified assets of $11,615, less the cash required to close of $4,287 ($11,615 - $4,287 = $7,328), and a projected mortgage payment of $1,249 left reserves of 5.87 months ($7,328 / $1,249 = 5.87).

The third compensating factor (additional income that could not be used but would have dropped the debt-to-income ratio below 41 percent) was not listed or documented in the loan file. During the audit, the lender stated this was a third compensating factor; however, we determined the co-borrower was previously self-employed and the Uniform Residential Loan Application stated the dates of self-employment were from January 1, 1996, to July 29, 2014. The loan closed on July 13, 2016. Therefore, the loan file did not support that the co-borrower remained self-employed when the loan closed.

Comment 12 We disagree with the lender's explanation regarding payment shock that was provided during the audit and again referred to in its response. The lender stated the borrowers had a history of satisfactorily maintaining a similar level of housing expense and made rental payments of $650 from February 2017 through June 2017 (6 months). However, the documents showed the borrowers made a rental payment of $650 from only March 2017 through May 2017 (3 months).[7] The rental payments started on February 24 and a partial rent payment of $250 was made in June because the Tribe was assisting the borrowers by providing the

[7] The documents showed the rent charged for April 2017 was $650; however, there was no evidence that the full amount was paid by the borrowers. The documents showed only that $500 was paid.

remaining $400 for the last month prior to the loan closing. However, the Section 184 processing guidelines require that the lender document the borrowers' monthly housing expense amount over a 24-month period. The borrowers incurred a monthly housing expense for only 4 months immediately prior to the loan closing; the housing expense was not consistent during this period, as the borrowers paid rent of only $250 (plus a $35 late fee) in the last month; and the borrowers had not incurred housing payment costs from approximately February 2016 to March 2017 because they had resided in government-assisted housing that did not require rent. Therefore, we determined the projected housing expense of $425 was a significant increase from the most recent rent payment amount of $250, and also a substantial increase from the recent period of no rental payment. In addition, despite the borrowers receiving $400 in assistance for their final rent payment and taking out a second loan as part of the home purchase, the borrowers would have had only $245 after the loan closing.

During the audit, the lender also stated the borrowers had a previous history of devoting a higher percentage of income to their housing expense. Specifically, the borrowers had a mortgage with the lender on November 25, 2014, and the monthly payments were $374. However, this mortgage was terminated approximately 18 months before the closing of the subject loan. The longer and more recent period of no rental payments should have been considered when assessing for payment shock.

Comment 13 We agree that the gap in employment was not a material underwriting deficiency and it provided no impact on the recommendation for indemnification for this loan. We recommended indemnification because the projected housing expense significantly increased and the lender did not document or support that one of the borrowers had the ability to accumulate savings or otherwise manage their financial affairs.

Comment 14 We disagree that documentation of a satisfactory employment history was provided during the audit process. Part of the borrower's 24-month previous employment history included self-employment, but the documentation regarding self-employment was inconsistent. The lender stated the borrower was self-employed from August 2011 to August 2017; however, a letter from the borrower stated he was self-employed from October 2015 to February 2017. The loan file also contained an Internal Revenue Service Form W-2, Wage and Tax Statement, for 2015 from Verizon, and the Uniform Residential Loan Application stated the employment dates were from July 2013 to October 2015; however, the lender did not verify the employment dates with Verizon. The lender was required to document the borrower's 24-month employment history (from August 30, 2015, to August 30, 2017) but did not verify and document the employment history with Verizon from August 30, 2015, to October 25, 2015 (approximately 2 months).

Also, even though the lender stated that its underwriter considered the borrower's employment as a school administrator as very stable, the lender was still required to verify the most recent 24 months of previous employment history. However, this was not a material underwriting deficiency and it provided no impact on the recommendation for indemnification for this loan.

Comment 15 We disagree with the lender's response that the payment shock was carefully analyzed and within a delegated underwriting authority to approve the loan. As stated in the audit report, the lender did not document or support that the borrower exhibited an ability to accumulate savings or had the ability to manage their financial affairs. The lender also did not document other reasonable compensating factors to offset the significant increase in the projected housing expense.

Comment 16 We disagree with the lender's position that the borrower's income was properly determined. As stated in the audit report, the lender determined the borrower's monthly income based on 80 hours per 2-week pay period; however, only two of the three pay stubs in the loan file supported that the borrower worked 80 hours. The lender used only the two most recent pay stubs (dated February 9 and February 23, 2018) that showed the borrower worked 80 hours but disregarded the other pay stub (dated January 26, 2018) that showed the borrower worked only 53 hours. The loan file did not provide an explanation for the reduced number of hours for the pay stub dated January 26, 2018, and the lender did not document justification for not considering the pay stub with the reduced number of hours in determining the borrower's monthly income.

During the audit, the lender stated the borrower was on maternity leave for a portion of the previous year, so it disagreed with using an average of the previous year's income to determine the borrower's monthly income. Even if the average of the three pay stubs were used to determine the borrower's monthly income, the income would have been overstated by $456 and the revised debt-to-income ratio would have been 48.43 percent, which exceeds the required limit of 41 percent.

Comment 17 The lender agreed that a proper gift letter was not present in the loan file but asserted that the gift was confirmed with the donor's bank, and also stated that it did not believe that the missing gift letter was a material element in the borrower's default. We did not question the deficiency as an element of the loan defaulting, but instead identified the missing gift letter as a loan underwriting deficiency. We determined that the gift was material because the borrower had assets totaling $4,305 (including gift funds of $1,000) and the cash required to close was $3,551. Therefore, the $1,000 gift was necessary for the borrower to close on the loan. The Section 184 processing guidelines state that for funds to be considered a gift there must be no expected or implied repayment of the funds. Therefore, without the required gift letter, we were not able to determine if repayment of the gift funds was required.

Comment 18 During the audit, the lender stated that three collection accounts for the borrower were to be paid by the Tribe and provided a letter to that effect, and also stated the underwriter used the Section 184 processing guidelines regarding disputed ownership of accounts when approving the loan. The lender cited the following from the guidelines: "When a borrower disputes the ownership of accounts showing up on their credit report, or claim that collections, judgments, garnishments, or liens have been paid, the applicant must submit documentation that reasonably supports their assertions. An underwriter must determine if the applicant's documentation reasonably supports their contention that the item is disputed. If there is reasonable evidence that the dispute will be resolved in the applicants favor then the loan may proceed without seeking a waiver." The underwriter proceeded with loan approval based on the letter that the Tribe was in the process of paying the collections.

We disagree that the letter from the Tribe stating they were in the process of paying the collections was sufficient for loan approval. The guidelines state that all collections must show evidence of payment in full prior to the date of closing and the borrower did not provide evidence that supported a dispute of the accounts or that the claims were paid.

Also, the lender did not provide documentation to show that ONAP provided additional flexibility for unpaid medical collections. Further, we did not question the unpaid collections as an element of the loan defaulting, but instead identified the collections as a loan underwriting deficiency.

Comment 19 During the audit, the lender stated a third party (the borrower's employer) was paying the installment loan that was excluded from the borrower's liabilities. While we agree the documentation showed the borrower's employer was paying the installment loan, we disagree that the liability was properly excluded in calculating the debt-to-income ratio. As stated in the audit report, we determined the liability should have been included because the borrower was the primary obligor. The loan was only in the borrower's name and there was no evidence that the debt holder would not pursue debt collection against the borrower, as required by the Section 184 processing guidelines to exclude the liability.

Comment 20 The lender acknowledged that the proper e-sign certifications for the borrowers were not obtained when processing the loan. We reviewed the wet signatures provided by the lender in response to the draft audit report and agree that the documentation was sufficient to address the issues identified. As a result, we adjusted the audit report finding accordingly and removed the recommendation for indemnification for these three loans (531-101818, 531-101941, and 531-102058). However, the deficiency remains in the report and a recommendation has been added for the lender to develop additional controls to ensure electronic signatures are properly supported.

Appendix C

Criteria

Section 184 Processing Guidelines (Effective April 1, 2011)

Section 12.6H (Credit Report) – A new credit report must be obtained for each borrower whose loan is included in a quality control review unless the loan was a streamline refinance and exempted from this requirement.

Section 12.6.I (Credit Document Re-verification) – Documents contained in the loan file should be checked for sufficiency and subjected to written re-verification. Examples of items that must be re-verified include, but are not limited to, the mortgagor's [borrower] employment or other income, deposits, gift letters, alternate credit sources, and other sources of funds. Sources of funds must be acceptable as well as verified. Other items that may be re-verified include mortgage or rent payments.

Section 12.7 (Specific Elements for Quality Control Review of Production)

- Determine whether loan documents requiring signature (other than blanket verification releases) were signed by the mortgagor or an employee of the mortgagee [lender] only after completion; and that all corrections were initialed by the mortgagor or employee(s) of the mortgagee.

- Determine whether all conflicting information or discrepancies in the application file were resolved and properly documented in writing prior to submission of the loan for underwriting.

- Determine whether all items requiring documentation have been properly evidenced and retained in the file.

- Determine whether verifications of employment, verifications of deposit or credit reports are suspect due to handling by any interested third party or the mortgagor.

Public and Indian Housing Notice 2014-22

Section 4 (Debt Analysis, Collections) – All collections must show evidence of payment in full prior to the date of closing. In addition, the applicant must furnish a written letter of explanation and must have otherwise good credit.

Section 5A (Stability of Income) – The lender must verify the applicant's employment from all sources for the most recent 2 full years, and the applicant must: 1) explain any gaps in employment that span one or more months and 2) indicate if he/she was in school or the military for the recent 2 full years, providing evidence supporting this claim, such as college transcripts, or discharge papers.

Section 5D (Non-Employment Related Applicant Income, Per Capita Income) – This is a form of income commonly paid to tribal members from tribal trust income (the most common example is income derived from tribal gaming operations). Per capita income may be used provided that tax returns support a 2 year receipt history. This income must be averaged over the 2 years.

Section 6 (Types of Liabilities, Debt to Income Ratio Computation for Recurring Obligations) – The creditor must include the following when computing the debt to income ratios for recurring obligations: 1) monthly housing expense (including principal, interest, taxes, insurance, and condo/HOA [homeowner association] fees) and 2) additional recurring charges extending 10 months are more, such as payments on installment accounts, child support or separate maintenance payments, revolving accounts, and alimony.

Debts that will be paid in full in less than 10 months must be included if the amount of the debt affects the applicant's ability to pay the mortgage during the months immediately after loan closing, especially if the applicant will have limited or no cash assets after loan closing.

Section 6 (Types of Liabilities, Contingent Liability) – A contingent liability exists when an individual is held responsible for payment of a debt if another party, jointly or severally obligated, defaults on the payment. The contingent liability policies described in this topic apply unless the applicant can provide conclusive evidence from the debt holder that there is no possibility that the debt holder will pursue debt collection against him/her should the other party default.

Section 6 (Types of Liabilities, Contingent Liability on Cosigned Obligations) – Contingent liability applies, and the debt must be included in the underwriting analysis, if an individual applying for a mortgage is a cosigner/co-obligor on a car loan; student loan; mortgage; or any other obligation. If the credit obtains documented proof that the primary obligor has been making regular payments during the previous 12 months and does not have a history of delinquent payments on the loan during that time, the payment does not have to be included in the applicant's monthly obligations.

Section 7 (Determining Ability to Pay, Debt to Income Ratio) – Without compensating factors as discussed below, to qualify for a Section 184 loan, the ratio or the applicant's total monthly debt to total monthly income at the time of the loan applications cannot exceed 41 percent.

Section 7 (Determining Ability to Pay, Compensating Factors) – A debt to income ratio up to 43 percent may be acceptable if at least two out of the five compensating factors listed below are presented. Compensating factors include, but are not limited to:

- Minimal housing increase (no more than 15 percent)
- Strong credit history (credit score of 700 or greater)
- The applicant has additional income that has not been included in qualifying that will, if used as qualifying income, reduce the debt to income ratio to below 41 percent
- The applicant has substantial cash reserves after closing (six months or greater)
- Loan to value ratio is 75 percent or less

Section 7 (Determining Ability to Pay, Projected Increase in Housing Expense) – The projected increase in the applicant's housing expense from his or her present housing expense must be carefully analyzed. If the new housing expense will significantly exceed the previous housing expense, then the lender must determine if the applicant has either exhibited an ability to accumulate savings or can otherwise show that he or she has the ability to manage financial affairs.

For example, if a person's rent payment was $50, and their proposed new mortgage is $800 a lender can favorably consider the applicant for approval if it can be shown that the applicant was able to save on a monthly basis the $750 difference between the present rent charge and the projected future mortgage payment for a period of time exceeding 6 months.

Lenders may also document other reasonable compensating factors to allow for loan approval, despite the significant increase in projected housing expense (however, the projected mortgage interest deduction on the applicant's federal income tax return, while beneficial to the applicants, is not a compensating factor and may not be included in the analysis).

Section 9 (Maximum Applicant Financing) – As dictated by the Section 184 statute, the maximum loan eligible for a guarantee can never exceed 97.75 percent of the appraised value of the property (or 98.75 percent if the value of the property is $50,000 or less).

However, the maximum mortgage amount that HUD will insure on a purchase transaction is calculated by multiplying the appropriate loan to value factor by the lesser of the property's 1) sales price subject to certain allowable adjustments or 2) appraised value.

Section 9B (Acceptable Source of Applicant's Funds, Verification of Earnest Money Deposit) – The lender must verify the deposit amount and the source of funds used by the applicant. Satisfactory documentation includes a copy of the applicant's cancelled check and a bank statement, as well as a verification of deposit or bank transaction statement dated after the earnest money deposit check has cleared.

Section 9E (Gift Funds) **–** The lender must document any gift funds through a gift letter, signed by the donor and applicant. The gift letter must show the donor's name; address; telephone number; specify the dollar amount of the gift; the nature of the donor's relationship to the applicant; and that no repayment is required.

Appendix D

Summaries for Loans With Material Underwriting Deficiencies

The following summaries provide details for each loan containing material underwriting deficiencies noted in the finding.

1. **Case number:** 044-101639
   Loan type: Purchase
   Closing date: 04/01/2016
   Unpaid balance: $199,854
   Delinquency status: 305 days past due

   We are recommending indemnification of this loan because the loan-to-value ratio exceeded the required limit.

   Other
   The loan-to-value ratio, as calculated by the lender and OIG, was 97.82 percent, which exceeded the required limit of 97.75 percent as stated in section 9 of Public and Indian Housing Notice 2014-22. The loan-to-value ratio exceeded the required limit because the lender did not use the lesser of the sales price and the appraised value.

2. **Case number:** 265-100661
   Loan type: Purchase
   Closing date: 08/25/2016
   Unpaid balance: $192,989
   Delinquency status: Foreclosure sale[8]

   We are recommending indemnification of this loan because (1) the projected housing expense significantly increased and the lender did not document or support that the borrower had the ability to accumulate savings or otherwise manage his financial affairs and (2) the revised debt-to-income ratio increased from 38.26 to 43.53 percent, which exceeded the required limit. The increase was a result of overstated income.

   Credit
   The projected housing expense significantly increased, and the lender did not document or support that the borrower had the ability to accumulate savings or otherwise manage his financial affairs as required by section 7 of Public and Indian Housing Notice 2014-22. The borrower was living rent free with family for 13 years, and the projected mortgage payment was $1,250. The borrower had an available bank account balance of $12,573 before loan closing; however, this amount included a loan of $10,000 received from the borrower's tribe.

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[8] Based on FHA's loss rate of 47 percent for single-family loans. The FHA loss rate was used because FHA sells the foreclosed-upon properties that were secured by a Section 184 loan guarantee.

Therefore, the borrower had only $2,573 that he saved on his own, despite living rent free for 13 years.

Section 7 of Public and Indian Housing Notice 2014-22 also states that lenders may favorably consider the applicant for approval if it can be shown that the applicant was able to save on a monthly basis the difference between the present rent charge and the projected future mortgage payment for a period exceeding 6 months. The documents in the loan file showed that the borrower was able to save the difference for only 1 month.

Income
The borrower's income was overstated by $633 because the lender did not average the per capita income over the past 2 years as shown on the tax returns and required by section 5 of Public and Indian Housing Notice 2014-22. We were not able to determine how the lender determined the borrower's income; however, it appeared that the lender used only the current and previous year, approximately 16.5 months.

3. **Case number:** 303-100496
Loan type: Purchase
Closing date: 07/13/2016
Unpaid balance: $210,587
Delinquency status: Current

We are recommending indemnification of this loan because the debt-to-income ratio of 42.47 percent exceeded the required limit of 41 percent and the borrowers did not qualify for two compensating factors.

Other
The debt-to-income ratio was 42.47 percent, exceeding the limit of 41 percent, and the borrowers did not qualify for one of the two compensating factors provided to establish eligibility as required by section 7 of Public and Indian Housing Notice 2014-22. The lender referenced a strong credit history (credit score of 700 or greater) and substantial cash reserves after closing (6 months or greater) as compensating factors. However, after paying the earnest money deposit and required cash to close the loan, the borrowers had less than 6 months of cash reserves after closing.

4. **Case number:** 405-116972
Loan type: Purchase
Closing date: 07/03/2017
Unpaid balance: $56,454
Delinquency status: 427 days past due

We are recommending indemnification of this loan because the projected housing expense significantly increased and the lender did not document or support that one of the borrowers had the ability to accumulate savings or otherwise manage his financial affairs. We also determined that the lender (1) did not obtain an explanation for a 39-day gap in employment and (2) did not verify the source of the earnest money deposit.

Credit

The projected housing expense significantly increased, and the lender did not document or support that the borrower's had the ability to accumulate savings or otherwise manage their financial affairs as required by section 7 of Public and Indian Housing Notice 2014-22. The projected housing expense was $425, and the borrowers paid zero rent through a housing authority for approximately 17 of the previous 20 months. The lender did not clearly document the housing expense that was paid by the borrowers for the 4 months before the loan closed. It appeared that the total rental amount for the most recent month was $650; however, the rental payment ledger from the loan file showed that another source paid $400, indicating the most recent month's housing expense paid by the borrowers was only $285 (including a $35 late fee). In addition, the borrower's bank statements did not support that the borrower funded the rental payment for 1 of the prior 4 months. Based on loan file documents, the borrower would have had only $245 after loan closing, demonstrating an inability to accumulate savings despite the 17-month period with no housing expense.

In addition, the lender did not document or support that the borrowers were able to save the difference between the present rent charge and the projected future mortgage payment for a period exceeding 6 months.

Income

The lender did not obtain an explanation for a 39-day gap in employment as required by section 5 of Public and Indian Housing Notice 2014-22. The borrower had a gap in employment from January 18 to February 26, 2016, and there was no explanation by the borrower in the loan file.

Assets

The lender did not verify the source of the $500 earnest money deposit made by the borrower as required by section 9B of the Public and Indian Housing Notice 2014-22. The bank statements from the loan file indicated a withdrawal of approximately $503 on March 31, 2017; however, the sales contract was dated 1 month later (April 30, 2017), and there was no documentation showing that these funds were available and used for the earnest money deposit. The loan file also indicates that a $500 rental payment was made for the previous housing expense on the same date as the $503 withdrawal.

5. **Case number:** 405-117477
Loan type: Purchase
Closing date: 09/01/2017
Unpaid balance: $194,683
Delinquency status: 152 days past due

We are recommending indemnification of this loan because the projected housing expense significantly increased and the lender did not document or support that the borrower had the ability to accumulate savings or otherwise manage his financial affairs. We also determined that the lender did not verify the borrower's employment for the most recent 2 full years.

Credit

The projected housing expense significantly increased, and the lender did not document or support that the borrower had the ability to accumulate savings or otherwise manage his financial affairs as required by section 7 of Public and Indian Housing Notice 2014-22. The borrower's previous housing expense was $850, and the projected mortgage payment was $1,392, an increase of $555, or 65.3 percent. The borrower had an available balance of $8,771 and retirement savings of $1,394 before loan closing; however, the balance included gift funds of $8,000. Therefore, the borrower had only $1,608[9] that he had saved on his own when the loan closed, and the housing expense was going to increase by $555 per month.

Section 7 of Public and Indian Housing Notice 2014-22 also states that lenders may favorably consider the applicant for approval if it can be shown that the applicant was able to save on a monthly basis the difference between the present rent charge and the projected future mortgage payment for a period exceeding 6 months. The documents in the loan file showed that the borrower was not able to save the difference for any month.

Income

The lender did not verify the borrower's employment for the most recent 2 full years as required by section 5 of Public and Indian Housing Notice 2014-22. The lender verified only approximately 22 of the prior 24 months.

6. **Case number:** 451-100084
   Loan type: Purchase
   Closing date: 05/14/2018
   Unpaid balance: $255,010
   Delinquency status: 152 days past due

   We are recommending indemnification of this loan because (1) the gift was not properly documented and (2) the revised debt-to-income ratio increased from 38.21 to 49.86 percent, which exceeded the required limit of 41 percent. The increase was a result of overstated income and understated liabilities.

Income

The borrower's income was overstated by $573 because the lender improperly determined the borrower's monthly income based on working 80 hours per 2-week pay period. There were three pay stubs in the loan file, and only two supported that the borrower worked 80 hours. The third pay stub showed that the borrower worked only 53 hours. Also, the earnings for the previous year from the verification of employment indicated that the

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[9] The retirement savings of $1,394 was multiplied by 60 percent. Section 9B of Public and Indian Housing Notice 2014-22 states that up to 60 percent of the value of retirement accounts may be included in the underwriting analysis unless the applicant provides conclusive evidence that a higher percentage may be withdrawn.

borrower did not work 80 hours per pay period. The pay stubs provided only the year-to-date income through February for the current year. Therefore, we used the previous year's income to determine the borrower's gross monthly income ($4,017).

Credit

The borrower's liabilities were understated by $249 because the lender improperly excluded the payment for one account. It appeared that the payment was excluded because there were approximately 8.5 months left to pay. Section 6 of Public and Indian Housing Notice 2014-22 states that recurring charges extending only 10 months or more should be included when computing the debt-to-income ratios. However, the notice also states that debts that will be paid in full in less than 10 months must be included if the amount of the debt affects the applicant's ability to pay the mortgage during the months immediately after loan closing. The payment for the account should have been included in the liabilities because it would have affected the borrower's ability to pay the mortgage. The borrower's revised debt-to-income ratio was 49.86 percent, and she also had limited cash assets after closing (approximately $754 and the mortgage payments were $1,618).

Assets

The borrower received a gift of $1,000 from a family member, which was used to close on the loan; however, the lender did not obtain a gift letter from the donor as required by section 9E of Public and Indian Housing Notice 2014-22.

7. **Case number:** 463-100338
Loan type: Purchase
Closing date: 06/30/2017
Unpaid balance: $0
Delinquency status: 427 days past due

We are not recommending indemnification for this loan because the unpaid mortgage balance was $0. However, we identified material underwriting deficiencies, which included that the projected housing expense significantly increased and the lender did not document or support that the borrowers had the ability to accumulate savings or otherwise manage his financial affairs.

Credit

The projected housing expense significantly increased, and the lender did not document or support that the borrowers had the ability to accumulate savings or otherwise manage their financial affairs as required by section 7 of Public and Indian Housing Notice 2014-22. The borrowers' previous housing expense was $750, and the projected mortgage payment was $1,196, an increase of $446, or 59.5 percent. The borrowers had an available balance of $5,621 before loan closing; however, the balance included gift funds of $5,080. Therefore, the borrowers had only $541 that he had saved on his own when the loan closed and his housing expense was going to increase by $446 per month.

Section 7 of Public and Indian Housing Notice 2014-22 also states that lenders may favorably consider the applicant for approval if it can be shown that the applicant was able to save on a monthly basis the difference between the present rent charge and the projected future mortgage payment for a period exceeding 6 months. The documents in the loan file showed that the borrowers were able to save the difference for only 2 months.

8. **Case number:** 531-101910
   Loan type: Purchase
   Closing date: 11/20/2017
   Unpaid balance: $183,186
   Delinquency status: 244 days past due

We are recommending indemnification of this loan because (1) there was no verification that all collection accounts were paid and (2) the revised debt-to-income ratio increased from 39.74 to 46.61 percent, which exceeded the required limit of 41 percent. The increase was a result of understated liabilities.

Credit

The borrower's credit report showed four collection accounts, and the lender did not verify that three of the accounts totaling $930 were paid in full before loan closing as required by section 4 of Public and Indian Housing Notice 2014-22. Instead, the lender relied only on a letter from the borrower's tribe, stating that it was in the process of paying the collection accounts.

In addition, the borrower's liabilities were understated by $382 because the lender improperly excluded the payment for one account. The lender excluded the liability because the payments were made by the borrower's employer. However, we determined that it should have been included because the borrower was the primary obligor. The liability was for a secured note in the amount of $9,000 that was in the borrower's name. A document of explanation by the borrower stated the loan was put into the borrower's name to build credit and the payments were made by her employer. Although the lender was able to document that the employer was making the payments for the loan, there was no evidence that the debt holder would not pursue debt collection against the borrower in the future. Section 6 of Public and Indian Housing Notice 2014-22 states that contingent liability policies apply unless there is conclusive evidence that there is no possibility that the debt holder will pursue debt collection against the applicant should the other party default.

9. **Case number:** 531-101818
   Loan type: Purchase
   Closing date: 09/07/2018
   Unpaid balance: $364,474
   Delinquency status: 62 days past due

We are not recommending indemnification for this loan because after the draft audit report was issued, the lender provided support to validate the questionable and unsupported borrower signatures.

Three letters, purportedly from the borrower, explaining employment and credit history included questionable electronically printed signatures that were inconsistent with other lender file documents because they did not include an associated document identification number or electronic signature certificate of completion. This discrepancy was not appropriately identified or resolved during the underwriting process.

10. **Case number:** 531-101941
Loan type: Purchase
Closing date: 02/22/2018
Unpaid balance: $397,892
Delinquency status: Current

We are not recommending indemnification for this loan because after the draft audit report was issued, the lender provided support to validate the questionable and unsupported borrower signatures.

Two letters, purportedly from the borrower, explaining derogatory credit items and bank account overdrafts included questionable electronically printed signatures that were inconsistent with other lender file documents because they did not include a document identification number or associated electronic signature certificate of completion. This discrepancy was not appropriately identified or resolved during the underwriting process.

11. **Case number:** 531-102058
Loan type: Purchase
Closing date: 08/13/2018
Unpaid balance: $301,322
Delinquency status: Current

We are not recommending indemnification for this loan because after the draft audit report was issued, the lender provided support to validate the questionable and unsupported borrower signatures.

A letter, purportedly from the borrower, explaining the source of three bank deposits included a questionable electronically printed signature that was inconsistent with other lender file documents because it did not include a document identification number or associated electronic signature certificate of completion. This discrepancy was not appropriately identified or resolved during the underwriting process.