

**U. S. Department of Housing and Urban Development
Office of Inspector General**



**Evaluation of Mortgagee Review Board
Enforcement Actions**

**May 2009
IED-09-003**

Executive Summary

The Office of Inspector General, Inspections and Evaluations Division, conducts independent, objective examinations of U.S. Department of Housing and Urban Development (HUD) activities, programs, operations, and organizational issues.

In response to a request from Senator Charles Grassley, Ranking Member, Senate Committee on Finance, we conducted an evaluation of Mortgage Review Board (MRB/Board) enforcement actions as part of HUD's oversight of Federal Housing Administration (FHA) single-family mortgage lenders. Senator Grassley asked us to update a review of the MRB by the Government Accountability Office (GAO) in its 2004 report on FHA risk management. The evaluation focused on MRB rulings in fiscal year (FY) 2008 and the 10 specific questions that were asked in his letter. Our objectives were to identify the facts related to those questions and provide an independent assessment of the MRB's effectiveness in deterring abuse in FHA mortgage lending.

The MRB was established by statute in 1989 as an enforcement body at HUD authorized to take administrative sanctions against FHA approved lenders. These include letters of reprimand, probations and suspensions, withdrawals, and entering into settlement agreements with lenders. It is also authorized to impose civil money penalties against lenders for a set of violations specified in the regulations at 24 C.F.R. § 30.35. A description of and the cause for each administrative action taken by the Board is required, under 24 C.F.R. § 25.10, to be published in the Federal Register at least quarterly. The MRB's annual report indicated it ruled on 94 single-family lender referrals in FY 2008, 65 of which were administrative cases of noncompliance with FHA annual recertification requirements.

We reviewed 25 referrals (no administrative cases) to the MRB during FY 2008 for rulings on violations of FHA single-family regulations and policy.

The MRB's sanctions directly affected only a small number of lenders out of a possible 12,461 FHA approved single-family lenders. The violations for which the MRB cited lenders rarely warranted withdrawal of FHA lending authority. The sanctions and fines obtained against lenders were frequently mitigated. Elapsed time to complete Board action was slow, taking an average of 6.4 months following notice to the lender, and was prolonged by case development or settlement negotiations in many instances. The MRB's public visibility was also greatly reduced because the results of its rulings were not published in the Federal Register in FY 2008 as required or otherwise disseminated on HUD's Web site.

The MRB will remain marginal as an effective sanctioning body unless its enforcement actions include a much larger caseload. Its effectiveness will depend on FHA dedicating more resources to quality assurance monitoring and referring a greater number of targeted lenders to the MRB for sanctioning. A referral to the Board should

elicit the expectation of a maximum sanction that reach in a significant way to problematic lenders and serve as a strong deterrent to abusive practices. Imposed penalties should be viewed as of real financial consequence to the violating lender, rather than as a negotiable administrative cost of doing FHA mortgage business. For greater public impact and higher industry visibility, Board decisions and the adverse consequences of violating FHA lending standards must be timely disseminated through the Federal Register, the Department's and trade association Web sites.

If you have questions about this report, please contact Lester Davis, Deputy Assistant Inspector General for Investigations, at 202-402-0390.

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Introduction

Mortgagee Review Board

Established by the U.S. Department of Housing and Urban Development (HUD) Reform Act of 1989 (12 U.S.C. (United States Code) § 1708) and guided by the Code of Federal Regulations (24 C.F.R. Part 25), the mission of the Mortgagee Review Board (MRB/Board) is to protect the Federal Housing Administration (FHA) and its mortgage insurance funds from fraud and program abuse and to encourage compliance by FHA-approved lenders. 24 C.F.R. Part 25.4 specifically provides for Board membership. The voting members of the Board are the Assistant Secretary for Housing-Federal Housing Commissioner (Chairperson), General Counsel, the President of the Government National Mortgage Association (Ginnie Mae), the Assistant Secretary for Administration, the Chief Financial Officer, and the Director of the Departmental Enforcement Center. The Assistant Secretary for Fair Housing and Equal Opportunity is a member who may vote only on cases involving fair housing and equal opportunity issues. HUD's Inspector General and the Director, Office of Lender Activities and Program Compliance, serve as nonvoting advisors to the Board.

The Board rules on cases against FHA-approved single-family lenders where there is evidence of serious violations relating to loan origination, servicing activity and failure to comply with FHA operational guidelines. The Board can impose civil money penalties and administrative sanctions against FHA lenders who knowingly and materially violate FHA program statutes, regulations, and handbook requirements. The MRB has authority to enforce the provisions of the Fair Housing Act, the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act, and Executive Order 11063 as it applies to the origination or servicing of FHA-insured single-family and multifamily loans.

MRB enforcement actions are required to be reported in the Federal Register (24 C.F.R. § 25.10). The Board also advises the U.S. Department of Veterans Affairs, Freddie Mac, Fannie Mae, Ginnie Mae, and the U.S. Department of Agriculture's Rural Housing Service of the Board's administrative actions (24 C.F.R. § 25.12).

In FY 2008 the MRB placed three lenders on probation, suspended two others and withdrew FHA lending authority from four lenders, as the result of referrals from Departmental reviews.¹ Other sanctions included the imposition of \$137,000 in civil money penalties and \$602,431 in administrative fees. The Board also accepted offers to indemnify high risk loans during settlement negotiations. Official public notice of FY 2008 enforcement actions has not yet been published in the Federal Register, as required, or otherwise communicated to the mortgage banking community and the general public through HUD's Web site.

¹ Probation allows the lender to continue to originate FHA loans, suspension stops the lender temporarily, and withdrawal is final.

FHA Statistics

FHA experienced a substantial increase in single-family mortgage loan volumes in FY 2008. Single-family insurance endorsements totaled 1,199,624 or an increase of 125 percent over FY 2007. The increased loan volumes have continued in FY 2009. Between October 1, 2008 and March 31, 2009, FHA reported total endorsements of 867,716 versus 406,833 during the same period one year earlier, or an increase of 113 percent. As the endorsements have climbed along with FHA's market share of mortgage loans nationally, FHA insurance exposure and accompanying risks have also risen. FHA single-family insurance in force now stands at \$577.8 billion representing 4.9 million insured loans as of March 2009.

Scope and Methodology

To answer the questions posed, we obtained and reviewed documents related to FY 2008 MRB enforcement decisions, mapped the referral and negotiation process, and recorded and analyzed relevant data. We interviewed the Secretary of the Board; the Associate Counsel for Program Enforcement; and FHA oversight staff at headquarters and the Philadelphia Homeownership Center. The Office of Lender Activities and Program Compliance provided a summary statement addressing the ten questions, and we confirmed the source and reliability of the document. We also independently obtained related data and other information concerning MRB activities, reviewed referral documents and the case files. Our sample consisted of 25 FHA single-family referrals (no administrative cases) to the MRB during FY 2008 for rulings on violations of FHA regulations and policy.

We conducted the inspection in accordance with the Quality Standards for Inspections published by the President's Council on Integrity and Efficiency.

Answers to the Ten Questions Requested for Review

The MRB met in five sessions during fiscal year 2008. Documentation of those hearings and related information collected from the Office of Single Family Housing, Office of Lender Activities and Program Compliance, Office of General Counsel, and the Secretary of the Board formed the basis of our evaluation and response to the 10 questions set out in the incoming letter of request.

Question 1: How many mortgagees are reviewed by the MRB annually?

The number of referrals to the MRB has varied from year to year. We identified 222 case referrals acted on by the Board from FY 2004 through FY 2008. A breakdown by year shows a declining caseload referral paralleling the decline in FHA loan volumes during the subprime loan bubble. Board minutes recorded rulings on 53 referrals in FY 2004; 36 referrals in FY 2005; 21 referrals in FY 2006; 18 referrals in FY 2007; and 94 referrals in FY 2008.

We examined 25 cases from FY 2008. These cases involved lenders that were referred primarily as the result of Homeownership Center quality assurance monitoring. The Board also ruled on 65 cases² in which mortgagees or loan correspondents failed to comply with annual recertification requirements.

As a point of clarification, the MRB does not review mortgagees, monitor, or audit FHA lender performance. It only rules on referrals typically based on monitoring reviews or audits conducted through the Office of Housing, GNMA, the Office of General Counsel, and the Office of Inspector General. For each referral, the Board considers civil administrative actions, as it determines appropriate, against the lenders for violations of regulatory and FHA program policy.

Question 2: How often does the Board meet, and how often are mortgagee reviews conducted by the Board?

There is no required minimum number of Board meetings. From FY 2004 to FY 2008 the Board met 23 times. The Board met in five sessions in FY 2008. Again the MRB does not review mortgagees, monitor or audit FHA lender performance.

Question 3: What are the policies and procedures for overseeing these mortgagees, and are they implemented in a consistent, effective, and efficient manner?

Board guidance and procedures are set out at 12 U.S.C. § 1708; 24 C.F.R. Part 25; and HUD Handbook 4060.2, REV-2. The authorities provided in the statute and regulations empower the MRB to impose sanctions on lenders for 32 specific violations listed at 24 C.F.R. § 25.9 (2008). The Board can take administrative actions against mortgagees including withdrawal, suspension, probation, letters of reprimand, and “cease and desist” notices. The Board also has the power to impose civil money penalties³ as well as enter into settlement agreements.

The Referral Process

Board enforcement actions flow from a step-by-step process, starting with a notice of violation to the lender and ending with an MRB ruling.

Step 1. Notice of Violation.

The Notice of Violation (Notice) is an official document from the MRB Secretary advising lenders that HUD has obtained evidence of irregularities in the lender’s FHA

² Until FY 2008 when a HUD Administrative Law Judge decision became effective, the MRB did not entertain or rule on cases of non-payment of annual lender fees or other administrative non-compliance issues.

³ Civil money penalties are penalties or fines which HUD may impose against a mortgagee or loan correspondent for “knowing and material” violations of certain FHA regulatory and program requirements. Civil money penalties are currently capped at \$7,500 per violation and can be imposed by following the procedures specified in 24 C.F.R. Part 30.

loan origination or loan servicing practices. This document is typically drafted by the HOC Quality Assurance Division (QAD) staff that prepares the referral packages for submission to the Secretary of the MRB. Before issuance it is also reviewed by OGC Program Enforcement for legal sufficiency and by the Office of Lender Activities and Program Compliance. The notice lists specific violations related to individual loan originations and sets forth the maximum penalties related to each violation. Lenders are given 30 days to provide a written response.

Step 2. Lender Response to the Notice of Violation and MRB staff evaluation.

If the lender provides a formal written response to the Notice, MRB staff and the HOC QAD review and evaluate the response and modify the referral package based on the evaluation. The referral package, as modified, is then again reviewed by OGC for legal sufficiency.

Step 3. Options Meeting.

This meeting is conducted as a conference call between the MRB Secretary and staff, OGC attorneys, the Director of Headquarters Office of Lender Activities and Program Compliance, and the four HOC QAD Directors. Collectively, these staff makes final decisions on case referrals and the penalty amounts to be recommended for each violation (the discussions usually involve more than one lender referral package).

Step 4. Settlement Negotiations.

Following the Options Meeting, the Office of General Counsel for Program Compliance can entertain offers of settlement from the lenders, and negotiate on behalf of the Board. If the negotiations result in an offer that, as determined by MRB staff, warrants Board consideration, the settlement provisions will be presented to the Board for ruling and resolution.

Step 5. Board Ruling.

The MRB Secretary prepares and presents a written case history including MRB staff recommended sanctions (typically a civil money penalty), an administrative fine, or, if the irregularity warrants, suspension or withdrawal of FHA lending authority. The Board then, after discussion, decides or rules by majority vote on the case and recommended sanctions.

Board Sanctions

The Board does not follow a written formula or matrix to determine the type of sanction or penalty. However, each violation cited in the referral documents carries a staff-recommended penalty amount.⁴ A civil money penalty for not performing quality control reviews, for example, could warrant the maximum sanction of \$7,500. Not observing FHA third-party restrictions on loan originations could carry a \$1,000 per loan penalty. Misleading advertising to solicit FHA “brokered” business could bring a \$3,500 penalty and a 6-month suspension. Our document review found consistency in the staff recommendations, on a violation by violation basis, for 15 of the 25 referrals without a negotiated settlement.

For the 10 referrals in which the lender and MRB staff negotiated a settlement, the Board accepted the staff recommendations, without material change, in most cases. As explained to us by Board staff, OGC Office of Program Enforcement staff negotiates settlements that include agreements to indemnify HUD on some number of mortgages and to impose civil money penalties or administrative fines. Settlement actions also include agreed to corrective actions that commit the lender to comply with FHA requirements. This commitment can be revisited by the MRB later if the lender defaults on terms of the settlement agreement. Our review of documentation supporting the 10 settlement agreements indicated that staff followed a thorough, consistent, and reasoned review process.

Sanctions against individual lenders can be effective especially for lenders who engage in egregious and repeated violations of FHA origination standards. It can mean removal and suspension of FHA lending authority. This was evident in the lenders’ formal responses to notices of violations in FY 2008 and documentation of ensuing settlement negotiations. However, the MRB ruled on so few referrals that, as an enforcement body, its overall deterrent effect on FHA mortgage lending was *de minimis*, especially when viewed from the perspective that FHA loan volumes exceeded 1 million endorsements in FY 2008.

Question 4: How many penalties have been assessed over the years, against whom, and how much money was collected? Does the Board settle cases for less than the penalty amount? If so, what are the implications of that action(s)?

Penalties Assessed

According to FHA staff, the MRB assessed monetary sanctions totaling \$28.26 million from FY 2004 through FY 2008 against FHA lenders. However, the sanctions included negotiated settlements of \$3.2 million with KB Homes Corporation and \$16.8 million with ABN AMRO Corporation.

⁴ Staff-recommend adjustments upward or downward based on these additional factors: the history of prior offenses, the ability to pay the penalty, the injury to the public, any benefits received by the violator, the extent of potential benefit to other persons, the deterrence to future violators, the degree of the violator’s culpability, and such other matters as justice may require.

Collections

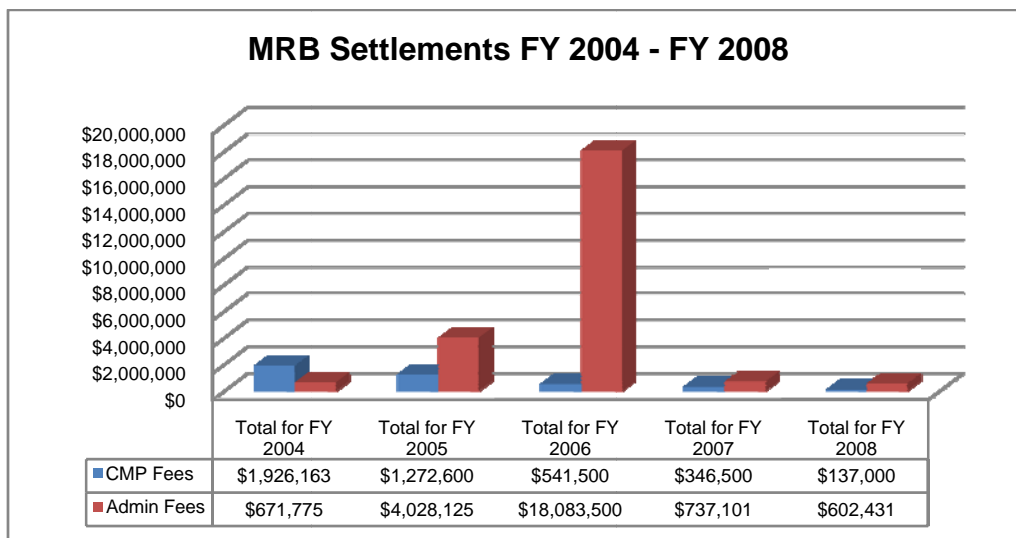
HUD’s Financial Operations Center (FOC) in Albany NY currently serves as the collection resource for Board sanctions involving settlement agreements. Formerly, staff from OGC, Office of Program Enforcement monitored collections.

In FY 2007 and FY 2008, FOC records indicated it collected \$599,503 in FY 2007 and \$4,481,714 in FY 2008 in civil money penalties and administrative fees based on MRB rulings. In addition, the MRB approved settlement agreements with lenders that included mortgage loan indemnifications. These lenders agreed to indemnify or reimburse HUD for FHA’s losses on paid and future claims against the insurance fund. However, because FOC’s debt servicing system does not track indemnification receivables separately by source (MRB rulings, QAD monitoring, Homeownership Center post endorsement technical reviews), the FOC could not provide collection amounts involving MRB sanctions against lenders that included indemnification agreements.

Settlements

In some instances, the Board will enter into a settlement agreement with a lender that would result in the lowering of the amount of a penalty imposed and/or the mitigating of a penalty to an administrative payment. In FY 2008 the Board agreed to change proposed civil money penalties to administrative fees, mostly as a result of negotiated settlement offers from the lenders. As MRB staff explained to us, by negotiating an administrative fee instead of a civil money penalty, the lender can avoid state regulatory reporting and disclosure in annual financial statements.

The following chart illustrates MRB settlement agreements FY 2004 through FY 2008 and the breakdown of civil money penalties and administrative fees.



The FY 2005 and FY 2006 MRB settlements reflect multimillion-dollar agreements with KB Homes Corporation (\$3.2 million) and ABN AMRO Corporation (\$16.8 million).

Question 5: Are there mortgagees who violate applicable law on more than one occasion; if so, who are they, and please review what action the Board takes with repeat offenders?

There are instances in which a mortgagee has come before the Board on more than one occasion.

According to staff, the Board takes into account its prior actions when ruling on FHA lenders that have been referred for repeat violations. Case documentation showed that the Board moved swiftly, for example, to remove one lender for originating five loans based on falsified bank statements and others for failure to indemnify or pay penalties as agreed. More examples of quick action involve cases of non-performance with provisions of settlement agreements and non-payment of MRB imposed civil money penalties and administrative fees.

Question 6: What are the sources of the Board's referrals?

The Board responds to referrals from the Office of Housing, Homeownership Centers, which are within the QAD, the Office of Lender Activities and Program Compliance, Ginnie Mae, and the Office of General Counsel for Program Enforcement, and the Office of Inspector General.

Question 7: Are there FHA mortgagees that have never been reviewed? What happens to other mortgagees with issues that do not make it to review by the MRB? Are violations being settled early?

The vast majority of FHA approved lenders are not reviewed by the MRB. From FY 2004 to FY 2008 the MRB ruled on 157 lender referrals, excluding the 65 administrative rulings, out of a possible 12,461 FHA approved single-family lenders. During the same period 2,958 mortgagees and loan correspondents were reviewed by FHA's Quality Assurance Division. FHA follows a risk-based selection process in selecting its monitoring targets and, therefore, focuses primarily on poor performers who are mortgagees that represent the highest potential for loss exposure to the insurance fund. Additionally, about 4 percent of new loan originations are chosen for technical (underwriting and appraisals) review by Homeownership and contractor staff. HUD's default servicing system also requires all lenders to report loan performance monthly.

QAD Lender Targeting and Findings Resolution

Before the start of each fiscal year, QAD staff prepares an annual lender targeting plan. The plan is generated by analyzing and evaluating high levels of lender defaults and claims, insurance processing, loan type, and volume spikes. As stated, the QAD conducted 2,958 lender monitoring reviews from FY 2004 through FY 2008.

HUD's QAD staff resolves most violations identified during on-site lender monitoring without referral to the MRB. Remedies to the on-site monitoring findings included developing policies or procedures to ensure against similar future deficiencies,

paying down the principal balance of overinsured loans, refunding inappropriate fees, and indemnifying HUD for potential future losses. According to staff, indemnification may be sought when a lender fails to comply with HUD's policies and procedures and this noncompliance subjects the FHA insurance fund to unreasonably high risk of loss. This is done in cases where the QAD determines that the findings do not merit referral to the MRB. If the lender agrees to execute the indemnification agreement(s) and the violations do not merit an MRB referral, the violations are resolved without escalating to the MRB.

Other HUD Monitoring and Deterrence

All FHA-approved lenders are subject to "oversight" through HUD's automated quality control systems. Automated monitoring is conducted at least quarterly through the use of one or more oversight or risk management tools available to HUD. For example, the QAD performs a quarterly analysis of the default and claim rate for each lender branch (approximately 27,000 branches) through Credit Watch monitoring, comparing it with average rates for all lenders located in each HUD field office jurisdiction. Those lenders with a relative compare ratio of greater than 200 percent are subject to proposed termination. The default rates of these lenders are published on the Internet (<https://entp.hud.gov/sfnw/public/>) and thereby serve as a source of information by which other lenders and interested parties can judge a lender's performance.

Question 8: Does the Board maintain a database or other mechanism to track its reviews, actions, and other processes?

The MRB currently uses both the Approval/Recertification/Review Tracking System (ARRTS) and Microsoft Excel to track Board cases and actions but is transitioning to the sole use of the ARRTS system. The QAD uses ARRTS to track lender reviews. Documents related to these reviews are stored in the Quality Assurance Document Library.

Question 9: On average, how long does it take from the time a violation is noticed to the time action is taken against a lender? During this period, is the lender limited in its operation?

For the 25 cases for FY 2008 that we reviewed, the MRB met and ruled on the violations within an average of 6.4 months following notice of the violation. According to the Board Secretary, the lender is not limited in its operation if a mortgagee has been issued a notice of violation because HUD is not permitted by law and regulation to take adverse action without affording due process.⁵

HUD officials acknowledged that the MRB referral process can be time consuming. We mapped the process to reflect staff descriptions and case file records. Once a response to a notice of violation is received, the referring office and the Office of General Counsel for Program Enforcement determine whether factual or legal issues are present that would weaken HUD's findings. This deliberative process is followed

⁵ 12 U.S.C. § 1708 and 24 C.F.R. § 25.6.

routinely and, as explained to us, is an important step to ensure that HUD is in a legally defensible position and that the lender is being afforded its required due process. A meeting is held for the MRB staff to determine the level of sanctions to be recommended for consideration. As GAO noted in its 2004 report, some processing delays occur in cases where the Office of Inspector General requests that the MRB withhold action in support of a criminal investigation. MRB rulings may also be delayed due to a bankruptcy filing by the mortgagee. Board action may be terminated if the lender is no longer in business.

Question 10: How many mortgagees are on probation as a result of the Board's action(s), and how is the probation monitored?

Currently three lenders are on probation as a result of FY 2008 MRB enforcement actions. Probation generally lasts for 6 months to 1 year. The reason for the probation determines how it is monitored and by which office. Usually probation is monitored by QAD, either in headquarters or in the appropriate Homeownership Center, and tracked in ARRTS. The Board also withdrew FHA authority from four lenders, excluding the administrative terminations for failure to recertify, and suspended two lenders in FY 2008.

Observations on the MRB's Effectiveness as an Enforcement Body

- 1. Few lenders were referred to the MRB, and mostly for violations that did not warrant removal of FHA lending authority.**

Factual Matters

We reviewed 25 cases where the Board sanctioned FHA single-family lenders for violations of FHA mortgage lending regulations (24 C.F.R. Part 25). Referred primarily as the result of Homeownership Center quality assurance monitoring, these lenders were formally cited for violations of FHA underwriting standards, programmatic policy, and, in two instances cited below, for material misrepresentations and falsehoods. The Board removed FHA loan origination authority from four lenders, and imposed civil money penalties or administrative fines on the other offenders. Examples of the violations and recommended penalties included:

Technical, underwriting deficiencies

Failure to calculate the maximum mortgage amount properly, resulting in an overinsured mortgage	Penalty = \$3,000 per loan
Failure to properly verify source of funds for earnest money deposits and gift funds	Penalty = \$3,000 per loan
Failure to include a nonpurchasing spouse in the credit analysis	Penalty = \$3,000

Technical, programmatic policy

Failure to perform quality control review of early loan defaults	Penalty = \$3,500 to \$6,500
Failure to comply with FHA restrictions on identity-of-interest business relationships in the origination process	Penalty = \$5,000 per loan

Material, misrepresentations and falsehoods

Submitted falsified documentation to the sponsoring lender to obtain FHA insurance	Penalty = \$3,000
Submitted a false certification on application for FHA lending authority	Penalty = \$7,500 per loan

With the exception of falsified documentation and material misrepresentation, the violations ruled on by the Board differ little from typical findings identified during a QAD on-site monitoring review. Such violations also do not always constitute an unacceptable increase in insurance risk, especially when viewed within the context of the cited lender's overall FHA portfolio performance.

Evaluation

We believe the Board should be focusing on lenders whose irregular loan origination and servicing practices represent a significant risk to the FHA insurance fund.

2. Civil Money Penalties were frequently mitigated to administrative fines.

Factual Matters

The MRB is authorized at Section 536 of the National Housing Act (12 U.S.C §1735(f)-14) to impose civil money penalties. However, as a matter of practice in FY 2008 and prior years, the Board frequently agreed to recharacterize the civil money penalty as an administrative fine. This condition occurred for 10 of the 25 lenders referred to the Board in FY 2008, and, in some cases, reflected a settlement offer from the lender to make payment without an admission of fault or liability. Administrative fees, like civil money penalties, are subject to public disclosure in the Federal Register but do not carry the penalty implications of misconduct or irregularity. Additionally, by negotiating for an administrative fee instead of a civil money penalty, the lender can avoid state regulatory reporting and disclosure in annual financial statements.

Example #1: W.R. Starkey Mortgage, LLP, Plano, TX (WRS)

WRS was cited for seven violations of FHA requirements. These violations included understating proposed housing payments in qualifying borrowers for FHA new construction loans (six mortgages), approving one borrower who had delinquent Federal debt, failing to ensure that Construction-Permanent Mortgage Program requirements were met (54 mortgages), and allowing documents in the processing/underwriting of loans to pass through a prohibited third party (14 mortgages). MRB staff proposed civil money

penalties in the amount of \$143,500. WRS offered to settle the matter by making an administrative payment to HUD of \$144,431 and indemnifying for insurance losses on seven loans. The MRB accepted the settlement offer.

Example #2: AAA Worldwide Financial Company, Addison, TX (AAA)

AAA was cited for nine violations of FHA requirements. These violations included failing to implement an adequate quality assurance plan, not remitting mortgage insurance premiums in a timely manner (472 mortgages), late endorsement submissions (376 mortgages), and other underwriting deficiencies. The MRB proposed civil money penalties in the amount of \$115,500. AAA offered to settle the matter by indemnifying HUD on five mortgages, buying down five mortgages in the total amount of \$40,126, refunding \$2,217 to one borrower, and making an administrative payment in the amount of \$115,500. The MRB accepted the settlement offer.

Evaluation

Congress established the MRB as an enforcement authority holding sole power⁶ to impose civil money penalties on lenders that violate regulations and guidelines in originating and servicing FHA insured mortgages. The MRB should be more consistently assertive in enforcing its enforcement mandate, especially in cases where lenders are found to have deliberately violated FHA regulations and requirements. Instead, the MRB has followed a pattern of mitigation, compromise, and willingness to accept lender offers of settlement that can diminish the Board's stature and its effectiveness.

In the cited examples, the MRB, in response to staff recommendations, accepted the lenders' settlement offers if the civil money penalties were paid as administrative fee. In both cases the lenders had substantial net worth and ability to pay the negotiated amount of the settlements, including indemnifying FHA for the highest risk loans. At a minimum, by paying an administrative fee, these two lenders avoided the negative consequence of a publicly reported irregularity in the Federal Register and potential disclosure to State regulatory authorities. The effect of reducing the civil money penalties to administrative fees diminished the impact of the MRB's enforcement power and its overall deterrent influence.

3. The MRB referral process was slow to deter or stop noncompliant lending practices.

Factual Matters

The Government Accountability Office (GAO)⁷ in 2004 criticized the length of time that the Board took to review cases and impose sanctions against lenders or took to

⁶ Absent fraud against the Federal government, such as provided for in Program Fraud Civil Remedies Act. (5 C.F.R § Part 185).

⁷ GAO's findings (GAO-05-13, November 12, 2004).

enter into settlement agreements with them. From a sample of 32 cases, GAO found that it took an average of 6.7 months to withdraw lenders' FHA approval (10 lenders) following Notice of Violation and an average of 11.1 months to negotiate settlement agreements.

We analyzed the timeliness of 25 case referrals to the Board. It took an average of 6.4 months from the Notice of Violation to Board ruling in these 25 cases. Four of these cases resulted in withdrawal of FHA lending authority (average elapsed time was 8.4 months from Notice of Violation to withdrawal of FHA lending authority). Ten cases included agreed to settlements that resulted from MRB staff negotiations. For these cases, the average elapsed time was 8.8 months.

To explain the referral process in greater detail, we provide a timeline of a recent decision to remove FHA lending authority from a New Jersey mortgage company. The timeline records the year-long effort required to complete a monitoring review of loan cases, prepare case histories and referral documents, recommend sanctions, and present for MRB ruling. MRB action in this case was recommended based on suspected fraud in the loan documents prepared for FHA insurance requirements and, for the branch office in question, a claim and default rate of 22 percent (82 of 368 loans).

Quality assurance monitoring at lender	01/23/2008
Post monitoring case preparation complete	04/07/2008
Notice of violation to lender	05/09/2008
Referral of potential fraud cases to OIG	05/21/2008
Referral of potential fraud cases to OIG	07/31/2008
Credit Watch suspension (NJ branch office)	08/12/2008
Notice of violation - response from lender	09/20/2008
Office of General Counsel completed review of	
Lender's response	12/03/2008
MRB ruling and removal	01/16/2009

The MRB "Notice of Administrative Action/Immediate Withdrawal for a Period of Five Years" also imposed a civil money penalty of \$151,500 and advised that the lender would receive a copy of HUD's complaint with respect to the proposed civil money penalty.

Evaluation

Our review found little difference from GAO's 2004 observations on the timeliness of MRB rulings. However, as outlined in the statute, case referrals to the Board do involve serious matters of irregularity and abuse in FHA lending. We recognize that FHA has an obligation to thoroughly investigate these allegations and determine legal sufficiency before any action is taken. We do believe that this process should be streamlined and a "sense of urgency" should be established to minimize additional damage and loss to FHA. The deterrent effect of the decisions of the MRB has been diminished by its current practices.

4. The message from MRB rulings was not published in the Federal Register or otherwise disseminated on HUD's Web site in FY 2008.

24 C.F.R. Part 25.12 provides that the Secretary shall publish, in the Federal Register, a description of and the cause for each administrative action taken by the Board against a mortgagee.

Factual Matters

Official public notice of MRB enforcement actions during FY 2008 has neither been published in the Federal Register nor otherwise communicated to the mortgage banking community and the general public through HUD's Web site. For FY 2004 through FY 2007 the Board published the summary results of its rulings in five notices in the Federal Register.

Evaluation

Decisions of the MRB need to receive quick and widespread public exposure, as contemplated by the regulations. Offenders levied with civil monetary penalties and/or punitive judgments, such as suspension and removal, are periodically cited in the Federal Register (none cited in FY 2008). However, disclosing adverse publicity about noncompliant lending practices in this official Federal publication cannot be expected to reach potential FHA consumers. HUD's Web site, www.hud.gov, offers advice and counsel to potential homebuyers and recently announced an initiative to encourage borrowers to seek housing counseling services as the number of foreclosure rescue scams increase in response to the Nation's housing crisis. The Web site, however, has made no mention of MRB findings in FY 2008. Industry advocates, such as the Mortgage Bankers Association (MBA), provide consumers with current data on loan originations, defaults, and foreclosures and actively advise the Congress on housing finance policy to discourage predatory lending. However, the MBA and others depend on HUD public disclosure of Board rulings before reporting the findings in their trade journals.

5. Board Workload Increased in FY 2008

Factual Matters

During FY 2008 Board workload increased due to the need to deliberate and vote on sanctions and on proposed settlement agreements involving mortgagees that were non-compliant with annual FHA renewal requirements. These renewal requirements included payment of annual fees, submission of informational verification reports and, in cases where lenders are non-supervised, submission of acceptable audited financial statements. Previously, such matters had been administratively handled by FHA program staff. This change in procedures resulted from a recommended decision issued by a HUD Administrative Law Judge (ALJ) in November 2007 and later upheld by a HUD hearing officer. In order to bring its procedures into compliance with this ruling, HUD thereafter

began submitting all cases involving mortgagees' failure to meet recertification requirements to the Board. In January of 2009, FHA issued Mortgagee Letter 09-01 which officially instituted the revised policies and procedures.

Board workload and that of its staff at OGC Office of Program Enforcement increased substantially due to this change. Cases involving recertification matters increased from zero in 2007 to 65 cases in 2008. Although the Board itself could and did consider these cases in groups at its meetings, each case had to be individually prepared for submission by the Board and DEC staffs. Many included cases where the mortgagees had failed to recertify; and, either had no interest in further participation in FHA programs or had already agreed to settle with HUD by paying the required fees and/or submitting the required reports.

Evaluation

HUD should propose legislative changes that would reverse the adverse workload impact of the HUD Administrative Law Judge's recommended decision. Procedural changes requiring the MRB to rule on each referral involving lenders who failed to meet recertification requirements are threatening to overwhelm the Board and its small staff assigned to prepare cases. Although the Board ruled on 65 recertification cases in FY 2008, there was a backlog of 520 similar cases at year end.

Conclusion

The statutory mission of the Mortgagee Review Board is to protect FHA and its mortgage insurance funds from fraud and program abuse and to deter noncompliance and mortgage lending irregularities. However, as pointed out in our review, the MRB ruled on few cases and often after a lengthy referral process. It sanctioned mostly technical violations of FHA policy. It imposed penalties, but most were without substantive financial consequence to the lenders. It imposed the strongest sanction of withdrawal mostly on routine cases of failure to recertify.

Unless its enforcement rulings include a much larger referral caseload, the MRB will remain marginal as an effective sanctioning body. To fully meet its statutory mandate, a stronger MRB will require greater willingness by FHA to dedicate more resources to quality assurance monitoring and to refer a greater number of targeted lenders to the Board for ultimate settlement of monitoring and audit findings. Referrals should also carry the expectation of maximum sanctions that reach in a significant way to problematic lenders and serve as a strong deterrent to abusive practices. Imposed penalties should be viewed as of real financial consequence to the violating lender, rather than as a negotiable administrative cost of doing FHA mortgage business. And, for greater public impact and higher industry visibility, Board decisions and the adverse consequences of violating FHA lending standards must be timely disseminated through the Federal Register and HUD's Web site.