



Issue Date	June 6, 2012
Audit Report Number	2012-AT-1013

TO: Charles S. Coulter, Deputy Assistant Secretary for Single Family Housing, HU

FROM: //signed//
James D. McKay, Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: Universal American Mortgage Company, Miami, FL, Branch, Did Not Comply With HUD Regulations When Originating and Underwriting FHA Loans and Implementing Its Quality Control Program

HIGHLIGHTS

What We Audited and Why

We audited Universal American Mortgage, Co. LLC, located in Miami, FL, in accordance with our annual audit plan. Universal was selected for review because its default rate of 3.8 percent was higher than the Miami area default rate of 1.9 percent. Our objectives were to determine whether the lender followed U.S. Department of Housing and Urban Development (HUD) requirements when originating and underwriting loans and implementing its quality control program. In addition, we wanted to determine whether the loans reviewed contained improper restrictive covenants.

What We Found

Universal did not follow HUD requirements when it originated and underwrote three of the six loans reviewed. Specifically, it used inaccurate and unsupported income, credit, and asset information to qualify borrowers for three Federal Housing Administration (FHA) loans. This condition occurred because the lender did not exercise due care when it underwrote the loans. As a result, Universal increased the risk to the FHA insurance fund by \$442,703.

In addition, the lender did not fully comply with HUD requirements when implementing its quality control program. It did not (1) meet the requirements for credit reverification and (2) report a deficiency found in its quality control review. This condition occurred because Universal did not follow its controls to ensure compliance with HUD requirements. As a result, it increased the risk to the insurance fund because it did not have assurance regarding the accuracy, validity, and completeness of its loan origination and underwriting operations. We did not find any improper restrictive covenants placed on the properties reviewed.

What We Recommend

We recommend that the Deputy Assistant Secretary for Single Family Housing require the lender to (1) indemnify HUD for the three ineligible FHA-insured loans with an estimated potential loss of \$442,703, (2) reimburse the unallowable tax service fee charged to three borrowers, and (3) fully implement its quality control plan and follow up in 9 months to ensure that its quality control reviews are conducted in accordance with HUD regulations.

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

Auditee's Response

We provided the discussion draft report to Universal on April 24, 2012, and held the exit conference with lender officials on May 10, 2012. The lender provided written comments on May 9, 2012. It generally disagreed with finding 1; however, it agreed with finding 2. During the exit conference, the lender provided the indemnification agreement it executed with HUD pertaining to FHA case number 095-1727113, discussed in finding 1 and documentation showing it reported FHA case number 095-2007408 to HUD, as recommended in finding 2.

The complete text of the Universal's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

In 1934, Congress created the Federal Housing Administration (FHA), which provides mortgage insurance on loans made by FHA-approved lenders. Since its inception, it has insured more than 34 million properties, making FHA the largest insurer of mortgages in the world. Many lenders participate in the FHA mortgage insurance program since it provides lenders with protection against losses as the result of homeowners' defaulting on their mortgage loans. As a result, the lenders bear less risk because FHA will pay a claim to the lender in the event of a homeowner's default.

In 1965, FHA became part of the U.S. Department of Housing and Urban Development's (HUD) Office of Housing. Under HUD's FHA direct endorsement program, approved lenders may underwrite and close mortgage loans without prior FHA review or approval. Universal American Mortgage, LLC is a nonsupervised direct endorsement¹ lender that was approved on January 1, 1960, to originate FHA loans. Universal originates loans under the lender insurance program, which enables high-performing lenders to insure FHA mortgage loans without a preendorsement review by HUD.

Universal American Mortgage Company, LLC, Universal American Mortgage Company of California, North American Title Company, and Eagle Home Mortgage of California are all affiliates of Lennar Financial Services, LLC. Lennar Financial Services is a wholly owned subsidiary of Lennar Corporation, a national residential homebuilder. Universal's headquarters is located at 700 N.W. 107th Avenue, Miami, FL. It has 36 branches in 15 States across the Nation. Universal provides mortgage financing services primarily to purchasers of Lennar Corporation homes.

According to HUD's Neighborhood Watch Early Warning System, from the amortization period of October 2009 through September 2011, Universal underwrote 741 loans in the HUD Miami office jurisdiction. As of September 30, 2011, 28 of the 741 loans (or 3.78 percent) were in default with mortgage amounts totaling more than \$5.2 million.

Our audit objectives were to determine whether the lender followed HUD requirements when (1) originating and underwriting loans and (2) implementing its quality control program. In addition, we wanted to determine whether the loans reviewed contained restrictive covenants.²

¹A nonsupervised lender is a lending institution which has as its principal activity the lending or investing of funds in real estate mortgages. It may submit applications for mortgage insurance and may originate, purchase, hold, or service insured loans or sell mortgages.

² In September 2011, HUD's Office of Inspector General (OIG) in Region 9 issued a report on the Universal American Mortgage, Las Vegas, NV, branch and found that the lender did not follow HUD requirements in the origination or quality control review of FHA-insured loans. Specifically, it found that the 15 loans reviewed contained inappropriate restrictive covenants that affected the insurability of the loan. Thus, we reviewed whether the loans we selected from the Miami, FL, branch office contained restrictive covenants.

RESULTS OF AUDIT

Finding 1: Universal Did Not Follow HUD Requirements When Originating and Underwriting FHA Loans

Universal did not follow HUD requirements when originating and underwriting three of the six loans reviewed. Specifically, it used inaccurate and unsupported income, credit, and asset information to qualify borrowers for three FHA loans. This condition occurred because the lender did not exercise due care when it underwrote the loans. As a result, it increased the risk to the FHA insurance fund by \$442,703.

Three Loans Contained Underwriting Deficiencies

Universal did not follow HUD requirements when originating and underwriting FHA loans. Specifically, our review of six loan files identified three loans with underwriting deficiencies that included unsupported income, credit or debt, and asset information. All FHA lenders must follow all applicable statutes, regulations, and HUD’s written instructions, including program handbooks and mortgagee letters. Specifically, lenders must follow HUD Handbook 4155.1, “Mortgagee Credit Analysis for Mortgagee Insurance on One- to Four-Unit Mortgage Loans,” when using automated underwriting systems or manually underwriting FHA loans. The lender is responsible for eliciting a complete picture of the borrower’s financial situation, source of funds for the transaction, and intended use of the property. Its decision to approve the loan must be documented, supported, and verifiable.

The table below shows the summary of significant deficiencies identified with the three loans. The lender also found some of these deficiencies that it self-reported to HUD. All deficiencies are further discussed in appendix D.

FHA case number	Unsupported income	Inadequate credit analysis	Unsupported source of funds
095-1003547		x	x
095-1873522		x	x
095-1727113	x	x	x
Total	1	3	3

The following three sections discuss some examples of the originating and underwriting deficiencies.

On May 10, 2012, the lender provided the indemnification agreement it executed with HUD pertaining to loan 095-1727113. As a result, the lender has taken corrective action to address the recommendation for this loan. We reduced the amount of funds to be put to better use to account for the executed indemnification agreement.

Loans Contained Unexplained Mortgage Interest Deductions

The lender did not consider or clarify in its credit analysis a mortgage interest deduction in the tax returns for all three loans reviewed. HUD Handbook 4155.1 1.A 4.c requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial situation, and all information must be verified and documented. Obtaining an explanation was important because it may have impacted the approval of the loan. For example, in FHA case number 095-1873522, the cosigner claimed a mortgage interest deduction on his tax returns, which suggested that the cosigner had a mortgage loan that the lender should have considered when approving the loan. In addition, the loan file contained a letter indicating that the cosigner was going to refinance his property but did not. The lender did not consider this liability when underwriting the loan.

The lender explained that this liability was not included since the cosigner's credit report did not reflect an outstanding mortgage. However, the credit report did not include the cosigner's spouse. As a result, the credit report may not have reflected all of the financial responsibilities that the cosigner may have had with his spouse. The lender should have inquired further about this mortgage deduction to obtain a complete picture of the cosigner's financial situation. Mortgagee Letter 2004-47, FHA TOTAL Mortgage Scorecard User Guide, states that if a mortgage debt does not appear on the credit report, the lender should obtain the most recent 12-month history and include the payment in the qualifying ratios. According to property records, the cosigner and his spouse owned an additional property. Therefore, this financial obligation may have affected the cosigner's ability to make payments and should have been considered when qualifying the borrowers for the FHA loan.

There Was an Unsupported Earnest Money Deposit

The lender did not determine the source of funds for an earnest money deposit. HUD Handbook 4155.1, paragraph 5.B.2.a, states that the lender must verify with documentation the deposit amount and source of funds if the amount of the earnest money deposit appears excessive based on the borrower's history of accumulating savings. For instance, in FHA case number 095-1727113, the HUD-1 settlement statement showed an earnest money deposit of \$3,000, which

the coborrower provided. Based on a bank slip, on May 13, 2010, the coborrower made a cash deposit of \$3,000 to his bank account, which had a beginning balance of \$114, and on the same day, the coborrower withdrew \$3,000 for the earnest money deposit. According to the coborrower's bank statements, from January 1 through April 30, 2010, the average balance in the account was approximately \$1,049. However, the lender did not determine the source of funds for the earnest money deposit, which appeared excessive based on the coborrower's bank statements. In addition, the borrower's bank statements for the period April 13 through June 10, 2010, did not support that the funds came from the borrower. As a result, the lender should have clarified the source of these funds to ensure that they came from an acceptable source.

Universal Charged an Unallowable Fee

The lender charged three borrowers an unallowable tax service fee. HUD Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. Two of the three borrowers whose loans contained underwriting deficiencies were charged this fee. In FHA case number 095-1873522, the lender said that the seller-paid closing costs included the tax service fee. However, the tax service fee was not included in the seller-paid closing costs; it was paid by the borrower. In addition to the two loans, one other loan also contained this unallowable fee; see the table below.

FHA case number	Tax service fee on HUD-1 settlement statement
095-1727113	\$73
095-1873522	\$85
095-1957849	\$85
Total	<u>\$243</u>

A Lack of Due Diligence Increased the Risk of Loss to the FHA Insurance Fund

Universal did not exercise due care when underwriting three loans for FHA insurance to ensure compliance with HUD requirements. Universal indicated that since it was understaffed, some of the deficiencies might have gone unnoticed. However, for two of the three questioned FHA loans, the lender identified some of the same deficiencies in its quality control review. As a result, the lender self-reported these deficiencies to HUD and took preventive measures to ensure that these deficiencies would not recur, see appendix D. As a direct endorsement lender, Universal was allowed to endorse a mortgage loan for FHA insurance without a

detailed technical underwriting review by HUD. However, in approving loans for FHA insurance, the lender certified that the mortgage loan documents were personally reviewed and the mortgage was found to be eligible for FHA insurance.

Conclusion

Universal did not follow HUD requirements when originating and underwriting three FHA loans. This condition occurred because Universal did not exercise due care to ensure that loans were originated and underwritten in accordance with HUD requirements. On May 10, 2012, the lender indicated that it executed an indemnification agreement with HUD pertaining to FHA case number 095-172113 for its self-reported deficiencies which includes the deficiencies identified in this report. Therefore, we reduced the amount of funds to be put to better use to account for the executed indemnification agreement. For the remaining loans, the lender placed the FHA insurance fund at risk of loss when it did not follow HUD's FHA regulations in the underwriting of two loans. The two loans had a total unpaid mortgage balance of \$431,479 with an estimated loss to HUD of \$284,776, see appendix C.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing require the lender to

- 1A. Indemnify HUD against any future losses on the two loans with underwriting deficiencies. The projected loss to HUD is \$284,776 based on HUD's loss severity rate of 66 percent of the unpaid balance of \$431,479.
- 1B. Reimburse the unallowable tax service fees charged to borrowers for FHA case numbers 095-172113, 095-1873522, and 095-1957849.
- 1C. Fully implement and enforce its policies and procedures to ensure that loans comply with HUD requirements and underwriting decisions are properly supported.

Finding 2: Universal Did Not Fully Comply With HUD Requirements When Implementing Its Quality Control Program

Universal did not fully comply with HUD requirements when implementing its quality control program. Specifically, the lender did not (1) meet the requirements for credit reverification and (2) report a deficiency found in its quality control review. These conditions occurred because Universal did not follow its controls to ensure compliance with HUD requirements. As a result, it increased the risk to the FHA insurance fund because it did not have assurance regarding the accuracy, validity, and completeness of its loan origination and underwriting operations.

As a condition of receiving and maintaining FHA approval, Universal must implement and continuously have in place a quality control program. HUD Handbook 4060.1, REV-2, paragraph 7-2, states that lenders must design their quality control program to meet the basic goals of (1) ensuring compliance with FHA’s and the lender’s origination and servicing requirements; (2) protecting FHA and the lender from unacceptable risk; (3) guarding against errors, omissions, and fraud; and (4) ensuring swift and appropriate corrective action. The lender’s quality control program contained deficiencies in its quality control reviews.

Universal Did Not Complete the Required Reverifications

Universal hired an external contractor to perform its quality control reviews during our audit period. The lender stated that its contractor conducted monthly random quality control reviews. Of the reviews conducted by its contractor, Universal reviewed 10 percent for compliance.

Universal conducted eight quality control reviews that were incomplete and did not meet HUD requirements. HUD Handbook 4060.1, REV-2, paragraph 7-6 (e), requires the lender to reverify employment and asset information of the borrower. We selected 16 quality control reviews, of which eight had missing reverifications. The eight reviews had missing reverifications of employment, assets, and a gift, as shown in the table below.

FHA case number	Incomplete reverifications		
	Employment	Assets	Gift
095-1608897	X		
095-1634930		X	
095-1848143		X	
095-1880733	X		
095-1874330	X	X	
095-2023192		X	
095-1983487		X	X
095-2189036		X	
Total	3	6	1

According to the lender, the deficiency occurred because of an oversight by its quality control contractor. The lender indicated that it was aware of this problem and was working with the contractor to address the issue. By not performing complete quality control reviews, the lender unnecessarily put HUD at risk for errors, omissions, and fraud.

Universal Did Not Report a Deficiency to HUD

Universal did not report to HUD a significant deficiency from its quality control review. One of the sixteen loans reviewed was rated nonquality by Universal's quality control contractor. The nonquality rating is provided to a loan if it fails to meet investor, agency, or regulatory guidelines to such degree that it affects the expected performance. FHA case number 095-2007408 was rated nonquality because the field review appraiser estimated the property value to be \$48,500 lower than the initial appraiser's valuation.

Universal took corrective measures without notifying HUD. Mortgagee Letter 2011-2 requires management to report to HUD all corrective actions taken in response to instances of serious material deficiencies. The lender indicated that based on the appraisal rebuttal and reviews of additional loans appraised by the initial appraiser, it did not consider this isolated incident to constitute a pattern of serious deficiencies. Therefore, the lender did not notify HUD of this deficiency as required. Although the lender took corrective measures, it should have reported this deficiency to HUD, along with the corrective actions taken.

Based on our recommendation, the lender provided a print out from neighborhood watch showing it reported FHA case number 095-2007408 on May 10, 2012 . Therefore, the lender has taken corrective actions to address recommendation 2B.

Conclusion

Universal did not follow HUD requirements when implementing its quality control program. These conditions occurred because Universal did not follow its controls to ensure compliance with HUD requirements. By not having an effective quality control program, the lender increased HUD's risk for errors, omissions, and fraud. As a result, HUD had no assurance regarding the accuracy, validity, and completeness of the lender's underwriting operations.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing require the lender to

- 2A. Fully implement its quality control plan and follow up in 9 months to ensure that its quality control reviews are conducted in accordance with HUD requirements.
- 2B. Report the deficiency associated with FHA case number 095-2007408 to HUD via Neighborhood Watch.

SCOPE AND METHODOLOGY

Our audit objectives were to determine whether the lender followed HUD requirements when (1) originating and underwriting loans and (2) implementing its quality control program. In addition, we wanted to determine whether the loans reviewed contained restrictive covenants.

To accomplish the audit objectives, we

- Reviewed applicable HUD handbooks and mortgagee letters;
- Reviewed Universal's policies and procedures for processing and underwriting loans;
- Reviewed Universal's FHA-insured loan files;
- Verified the accuracy of the information from the loan files with the borrowers and borrowers' employers;
- Reviewed Universal's written quality control plan;
- Reviewed Universal's post-quality control reviews; and
- Interviewed Universal's employees, management, and external quality control contractor.

We accessed Neighborhood Watch to obtain information about the lender and its loans. Universal underwrote 741 loans within the jurisdiction of the Miami HUD office between the amortization dates of October 1 and September 30, 2011. As of September 30, 2011, 28 loans with mortgage amounts totaling \$5.2 million were in default. Of the 28 defaulted loans, we selected 5 loans to review based on various risk factors, including loans that defaulted with 6 or fewer payments, loans with gift donors, and loans with high mortgage amounts. The original mortgages of the five loans totaled approximately \$1 million, and the unpaid principal balances totaled \$998,064. The results of our review apply only to the loans reviewed and cannot be projected to the universe of the loans.

One of the loans that contained underwriting deficiencies involved an employee of the Lennar Corporation. Universal is a subsidiary of Lennar. As a result, we expanded our review to include loans involving employees and associates of the Lennar Corporation or its subsidiaries. Of the 28 defaulted loans, we identified 1 additional loan involving an employee of the lender. The original mortgage amount of this loan totaled \$235,551 with an unpaid principal balance of \$230,121.

Universal's external post-quality control contractor reviewed 85 loans from the Miami branch office for our scope period of October 1, 2009, through September 30, 2011. Of these 85 loans we selected 16 loans. We selected loans reviewed by the quality control vendor for the months of March 2010, September 2010, March 2011, and September 2011. We reviewed these 16 loans for review of timeliness, desk appraisal, and credit document reverification, as well as corrective actions taken on material findings cited in the quality control review reports. In addition, we determined whether Universal complied with the frequency and early payment default requirements for our scope period and the sample size and field appraisal in 2010.³ The

³The lender's fiscal year is from December through November, which covers 1 full year (2010) of our scope period of October 1, 2009, through September 30, 2011. Therefore, to test the sample size and field appraisals, we focused on the lender's 2010 fiscal year.

results of our review apply only to the quality control reports reviewed and cannot be projected to the universe of reports.

We used data maintained in Neighborhood Watch to obtain background information and the universe of loans and their status. This system is designed to highlight exceptions so that potential problems are readily identifiable. In particular, the system gives the ability to identify and analyze patterns, by geographic area or originating lender, in loans which became delinquent during the first 2 years. We did not rely on the data as a basis for our conclusion.

During the course of the audit, we clarified HUD regulations and discussed potential issues with the Atlanta Homeownership Center's Quality Assurance Division. We also discussed the findings with the lender.

We classified \$284,776 as funds to be put to better use. This is 66 percent of the total unpaid principal balances of \$431,479 for the two loans as of February 29, 2012. We used 66 percent because it has been determined that upon the sale of the mortgaged properties, FHA's average loss was about 66 percent of the unpaid principal balance.

Our review generally covered the period October 2009 through September 2011 and was extended as necessary during the audit. Our review was conducted from November 2011 through March 2012 at Universal Mortgage Company, LLC, located at 700 N.W. 107th Avenue, Miami, FL, and at various other locations in the Miami-Dade area to conduct interviews with the borrowers.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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 objectives:

- Program operations - Policies and procedures that management has implemented to provide reasonable assurance that a program meets program objectives.
- Compliance with laws and regulations - Policies and procedures that management has implemented to provide reasonable assurance that program implementation is in accordance with laws, regulations, and provisions of contracts or grant agreements.

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:

- Universal did not follow HUD requirements when originating and underwriting FHA loans (see finding 1).
- Universal did not fully comply with HUD requirements when implementing its quality control program (see finding 2).

APPENDIXES

Appendix A

SCHEDULE OF FUNDS TO BE PUT TO BETTER USE

<u>Recommendation number</u>	<u>Funds to be put to better use 1/</u>
1A	<u>\$284,776</u>

- 1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (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.

Implementation of our recommendation to require Universal to indemnify HUD for the two ineligible loans will reduce the risk of loss to the FHA insurance fund. The amount above reflects HUD's estimated loss of 66 percent of the loans' unpaid principal balance of \$431,479 as of February 29, 2012.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

UAMC™

UNIVERSAL AMERICAN MORTGAGE COMPANY

May 9, 2012

James D. McKay
Regional Inspector General for Audit
Region 4, Office of Inspector General
Office of Audit, Box 42
U.S. Department of Housing and Urban Development
Richard B Russell Federal Building
75 Spring Street, SW, Room 330
Atlanta, GA 30303-3388

Re: Universal American Mortgage Company, LLC, Miami, Florida
Draft Audit Report Dated April 24, 2012

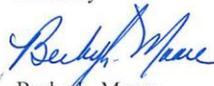
Dear Mr. McKay:

Universal American Mortgage Company, LLC (UAMC) acknowledges receipt of your draft findings report for the OIG audit of our office in Miami, Florida, and appreciates the opportunity to provide a written response. UAMC continually strives to originate quality mortgage products and audit reports such as yours assist us in furthering our initiatives for quality.

We have completed our review of your draft of the proposed audit report findings and are providing responses and supporting documentation to address each of the exceptions. Where corrective action was warranted, we have initiated the appropriate action and the action is noted in the detailed response. We trust that the information and documentation herein provided adequately addresses your findings and that any findings found to be resolved will be removed.

We thank you for your time and consideration. If you have any questions or need further clarification on the information or documentation submitted, please contact me at 305-229-6561 or via email at beckymoore@uamc.com.

Sincerely



Becky L. Moore
Vice President, Quality Assurance

Enclosures



Finding 1: Universal Did Not Follow HUD Requirements When Originating and Underwriting FHA Loans

Universal American Mortgage Company, LLC (“UAMC”) appreciates the opportunity to respond to the draft audit report of findings in the audit of our Miami, Florida office by HUD’s Office of Inspector General. The draft audit report cites three loans as having significant deficiencies in origination and underwriting. We will respond to the alleged specific deficiencies in separate attachments, labeled by HUD case number.

Comment 1

UAMC has been very concerned about our rate of delinquency and we have taken significant steps to address internal policies and underwriting quality over the past year. In 2010, there were a total of six underwriters and two managers in the Underwriting Department. As of January 2012, there were thirteen underwriters and two managers. Since January 2012, an additional six experienced underwriters have been hired with plans to add one more underwriter, for a total of 20 underwriters. We have also expanded our training program and created a new Risk Management Department.

In March of 2011, the Risk Management Department was created which is independent of the Underwriting Department as part of UAMC’s effort to strengthen underwriting quality. The Risk Management Department was further expanded in November of 2011. This Department provides a second level of underwriting review for loans with identified high risk characteristics to evaluate the borrower’s capacity and willingness to repay. Exceptions are approved only when strong compensating factors are present that support the borrower’s ability and willingness to repay. This process is designed to enable qualified borrowers to become successful homeowners. The associates in the Risk Management Department are senior, management level underwriters with extensive experience managing credit risk.

The Risk Management Department also provides support to the underwriting staff. The Department performs periodic reviews of underwriting files to ensure underwriting policies are being followed, accuracy of data and documentation exists, and decisions are consistently applied. If errors are found, the Risk Management Department will review all loan decisions by the underwriter in question until they have at least five successful “passes.” In an effort to give the Underwriting Department more tools, UAMC’s Risk Management Department has taken on the monthly review of the FHA Connection Underwriting Performance Reports and reviews in detail its findings and observations in monthly meetings with the full underwriting staff. The Risk Management and Underwriting Departments conduct quarterly training calls with production staff to review issues found in the QC Audits, deficiency letters from FHA, guideline changes, as well as to answer questions from the production area. The Risk Management Department also publishes periodically the “UAMC Underwriting Buzz” which gives guidance on important issues to all of UAMC’s production staff.

In 2012, the “Underwriting Signature Authority Process” was implemented. Underwriting associates are granted tiered signature authority, based on training and performance levels.

- New underwriting associates must satisfactorily complete a UAMC training program.
- Underwriters must satisfactorily complete five live test cases for each loan type including conventional, FHA and VA.
- Test cases are reviewed and signed off on by Risk Management or Underwriting Management.
- After successful completion and nomination, underwriters are granted approval level to \$417,000.
- Increase in approval level to \$750,000 requires an additional five test cases with loan amounts above \$417,000.

Loan amounts greater than \$750,000 require a second signature by the Risk Management Department, Underwriting Management or Senior Underwriter approved for that authority.

**Finding 2: Universal Did Not Fully Comply with HUD Requirements
When Implementing Its Quality Control Program**

Comment 2

Universal (“UAMC”) acknowledges the cited shortcoming in its follow-up process to ensure every effort was made to obtain the required re-verifications during the time period under review and has made several improvements in the area of quality control since this audit period. These shortcomings have been brought to the attention of our QC contractor, who was directed to perform a self audit. In addition, UAMC staff reviewed all random audits during 2011 to identify and attempt to obtain any missing re-verification documents. We have also hired one additional Quality Control staff member who concentrates solely on the re-verification process. Reports are being utilized to track outstanding re-verification requests and additional staff is assigned to assist during peak periods. We are finding that our continued oversight of the Quality Control contractor has resulted in more consistent, thorough reviews by that vendor. Loans with significant findings are further reviewed by senior audit staff, as well as UAMC risk management personnel and discussed with senior management to identify areas of concern that require further action. Loans with unresolved significant findings are reported to HUD via FHA Connection.

Comment 3

As recommended by this report, UAMC has reported the deficiency associated with FHA case number 095-2007408 to HUD via Neighborhood Watch. This loan was rated non-quality by the quality control analyst because the field review appraiser estimated the property value to be 22% lower than the original appraiser’s value conclusion. We also appreciate the opportunity to explain the measures that were taken to properly evaluate the appraiser’s work and determine the accuracy of the field reviewer’s findings. As with many lenders, UAMC does not automatically consider a field reviewer’s differing opinion of value to be an automatically reportable deficiency since the market value provided by the appraiser and field reviewer are just that, opinions. It has been our practice to provide the original appraiser an opportunity to respond to a field reviewer’s report and then evaluate the appraiser’s response. Depending on the circumstances, we may also ask the field reviewer for additional information. If we still need more information in order to make a determination, we might order an additional field review from a third appraiser. Importantly, as stated in your findings, UAMC took additional measures in the cited case to carefully evaluate the differing opinions and make a determination regarding the most probable correct value conclusion. Based on the additional information obtained, UAMC determined that the original appraiser was more likely to be correct and that the incident was not a reportable incident. We would not have considered the measures taken to be corrective measures, but rather the gathering of information needed in order to make a determination about whether or not a deficiency existed in this case. UAMC believes that the actions it took to determine the appraisal value conclusion were reasonable and prudent.

LOAN DETAILS FOR THE THREE PURCHASE LOANS

FHA case #: 095-1003547

██████ - UAMC #0005400445

Mortgage Amount: \$226,816

Date of loan closing: 12/17/2009

Unpaid principal balance: \$225,309

Loan purpose: Purchase- existing

Default status: Special forbearance

Cited Asset Deficiency:

The lender did not adequately document the transfer of gift funds. HUD Handbook 4155.1, Paragraph 5.B.5.b., requires that if the gift funds are provided at closing and are in the form of an official check, the lender must have the donor provide a withdrawal document or cancelled check for the amount of the gift showing that the funds came from the donor's personal account. The borrower received \$4,900 in gift funds. According to the gift letter, the funds would be provided at closing. The lender's file included a copy of the donor's account summary report and official check to the closing company. However, none of the documents showed that the withdrawal came from the donor's account. To ensure that the borrower did not receive funds from an unacceptable source, the lender should have obtained documentation showing the money coming from the donor's account.

UAMC Response:

We are unable to determine with certainty the reason that this file does not contain documentation of the actual withdrawal of gift funds from the donor's account. Gift funds were transferred at closing and the funds were recognized as a gift on the HUD-1. The file did contain a copy of the donor's bank statement dated 12/15/2009 which showed sufficient funds for the gift, a copy of the cashier's check dated 12/17/2009 drawn on the donor's bank and made payable to the closing agent and a gift letter from the donor. The gift funds were clearly provided to the borrower by the donor.

Credit Deficiency:

The lender approved an ineligible loan by not considering a final judgment of foreclosure that occurred less than 3 years before the loan closing. HUD Handbook 4155.1, paragraph 4.C.2.f, states the HUD does not insure borrowers that had their principal residence foreclosed upon in the previous 3 years. Based on the borrower's 2007 tax return, the borrower claimed a mortgage interest deduction for a property. Public records show that on July 23, 2007, the borrower had a property that was issued a final judgment of foreclosure. According to the

Comment 4

borrower, due to financial challenges, the borrower was unable to make the mortgage payments on the borrower's principal residence, which led to the final judgment of foreclosure. To avoid the completion of the foreclosure process, the borrower remained on the property and leased it from the investor. In December 2009, the borrower repurchased this property within 3 years of the foreclosure with an FHA loan. Therefore, the borrower was ineligible to receive an FHA-insured loan due to the previous foreclosure.

The lender was unaware of and did not consider this foreclosure because it was not reflected in the credit report. Mortgagee Letter 2004-47, FHA Total Scorecard User guide, explains that in the event that derogatory or delinquent credit items are revealed during the processing that are not reflected in the credit report, the lender must downgrade to a "refer" and manually underwrite the loan. Derogatory credit items include foreclosure, judgments, and so forth. If it is a foreclosure, the lender should follow HUD Handbook 4155.1, paragraph 4.C.2.f, Previous Mortgage Foreclosure.

When we informed the lender that the borrower was ineligible to receive an FHA loan, the lender disagreed because it believed that the property was not foreclosed upon since according to public records, the property was sold within 30-day redemption period. Although the property was sold within 30-day redemption period, the borrower's inability to make payments contributed to the foreclosure, and the lender should have questioned the mortgage interest deduction and considered the borrower's ability to make the mortgage payments

HUD indicated that the lender, having firsthand information, should have discovered and analyzed the information and followed HUD Handbook 4155.1, paragraph 4.C.2.f, Previous Mortgage Foreclosure.

UAMC Response:

We respectfully disagree that the UAMC loan underwriter would have had a reason to suspect that the borrower had any recent foreclosure activity. To our knowledge, the underwriter did not have any firsthand information about a previous foreclosure. The borrower stated that she did not have any previous foreclosure on her loan application which was dated November 12, 2009. Also, the credit report did not report any foreclosures, comments or other derogatory mortgage payment history, aside from a previous Wells Fargo mortgage loan with a history of two 30-day delinquencies, the most recent being April of 2005. The credit report also states "No Public Record Information found." Additionally, the credit report shows five previous mortgage loans with good payment histories, the most recent having been paid off in February 2007. This would have explained the mortgage interest deduction on the borrower's 2007 income tax return. There is no reasonable basis for UAMC to have known of any foreclosure activity.

Comment 5

**LOAN DETAILS FOR THE THREE PURCHASE LOANS
FHA Case # 095-1727113**

██████ – UAMC #6011944	Mortgage Amount: \$240,236
Date of closing: 8/31/2010	Unpaid principal balance: \$239,283
Loan purpose: Purchase – existing	Default status: Delinquent

Cited Credit Deficiency:

The lender did not ensure that all liabilities were included in its analysis. HUD Handbook 4155.1, paragraph 4.C.2.c, requires that a borrower provide a satisfactory explanation for any significant debt that is shown on the credit report but not listed on the loan application. The borrower's initial loan application and credit included a student loan with a balance of \$191,432, or a payment of \$980 per month. However, the final loan application did not include this student loan. The lender indicated that this student loan was not considered since a later credit report reflected that the loan was closed. Although the report stated that the loan was closed, it indicated that the account had been consolidated with a new account. Given that the amount was significant, the lender should have obtained further clarification regarding this account.

UAMC Response:

A credit report supplement had been obtained that reflected this loan as closed and having a zero balance. It also showed two new student loans opened having balances of \$98,271 and \$7,194 respectively. However, as the total amount does not match with the reported balance of the original student loan, we agree that the underwriter should have asked for further clarification regarding this account.

Cited Asset Deficiency

Earnest money deposit: The lender did not determine the source of funds for an earnest money deposit. HUD Handbook 4155.1, paragraph 5.B.2.a, states that the lender must verify with documentation the deposit amount and source of funds if the amount of the earnest deposit appears excessive based on the borrower's history of accumulating savings. The HUD-1 settlement statement showed an earnest money deposit of \$3,000, which the co-borrower provided. Based on the bank slip, on May 13, 2010, the co-borrower made a cash deposit of \$3,000 to the co-borrower's bank account, which had a beginning balance of \$114, and on the same day, the co-borrower withdrew \$3,000 for the earnest money deposit. According to the co-borrower's bank statements from January 1 through April 30, 2010, the average balance in the account was approximately \$1,049. However, the lender did not determine the source of funds for the earnest money deposit, which appeared excessive based on the co-borrower's bank statements. In addition, the borrower's bank statements for the period April 13 through June 10, 2010, did not show that the funds came from borrower. As a result, the lender should have clarified the source of these funds to ensure that they came from an acceptable source.

Comment 6

Seller contribution exceeding 6 percent threshold: Based on the HUD-1 settlement statement, the seller credits total \$15,923, which exceeded the maximum allowable contribution of \$14,610. According to HUD Handbook 4155.1, paragraph 2.A.3.b, the third party may contribute up to 6 percent of the property's sales price toward the buyer's closing costs, prepaid expenses, discount points, and other financing concessions. The lender explained that the builder's fee credit of \$3,630 was not a part of the seller's contribution, as the fee was not tied to the financing and was paid to the seller directly. However, HUD indicated that the builder's fee credit would be included since the 6% seller's contribution is all inclusive. Therefore, seller credit exceeded the maximum allowable by \$1,313.

Unallowable Fee: The lender charged the borrowers an unallowable fee. HUD Handbook 4155.1, Paragraph 5.A.2. a, states that borrowers may not pay a tax service fee. The lender said that the tax service fee was paid by seller. However, the settlement indicated that the \$73 tax service fee was charged to the borrower.

UAMC Response:

Comment 7

Earnest money deposit: The file did contain evidence of a withdrawal of \$4,000 from the donor's account on the same day as the \$3,000 earnest money deposit, but as the amounts do not match. Additional documentation should have been obtained. Sufficient verification of assets has been the subject of many recent trainings, emails and underwriting meeting discussions. UAMC will continue to stress this with our underwriting associates.

Comment 8

Seller contribution exceeding 6 percent threshold: Our review of the file found that in this particular case, the seller agreed to waive a standard builder fee for this purchaser. This fee was not an expense tied to the financing of the property and as such was not considered in the 6% contribution limit.

Comment 9

Unallowable Fee: All of the borrower's closing costs were paid by the seller, therefore the seller paid the \$73 Tax Service Fee in this case.

Deficiencies That Were Self-Reported by the Lender for FHA Case #095-1727113

UAMC Response

Comment 10

We have previously provided HUD with an executed indemnification letter as requested by HUD in response to our self-report of the stated deficiencies.

LOAN DETAILS FOR THE THREE PURCHASE LOANS
FHA case# 095-1873522

██████████: UAMC #0006477343 Mortgage Amount: \$207,209

Date of Closing: 10/19/2010 Unpaid principal balance: \$206,170

Loan purpose: Purchase- existing Default status: Delinquent

Cited Credit Deficiency:

The lender did not consider or clarify in its credit analysis a mortgage interest deduction in the co-signer's tax returns. HUD-Handbook 4155.1.A.4c requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial situation, and all the information must be verified and documented. Based on the final loan application, the cosigner lived rent free. However the co-signer had a mortgage loan interest deduction on their tax returns, which suggested that the co-signer had a mortgage loan that the lender should have considered when approving the loan. In addition, the loan file contained a letter indicating that the cosigner was going to refinance his property but did not go through with it. According to property records, the cosigner and his wife owned another property. Obtaining an explanation was important because it may have impacted the approval of the loan.

The lender explained that this liability was not included since the cosigner's credit report did not reflect an outstanding mortgage. However the credit report did not include the cosigner's spouse. As a result, the credit report may not have been reflected all of the cosigner's financial responsibilities that he may have had with his spouse. The lender should have inquired further about this mortgage deduction to obtain a complete picture of the cosigner's financial situation. According to Mortgagee Letter 2004-47 FHA totals Mortgager Scorecard User Guide, if a mortgage debt appears on the credit report the lender should obtain the most recent 12 month-history and include the payment in the qualifying ratios.

UAMC Response:

We noted that although the co-signer's income tax returns did reflect mortgage interest paid, the returns had been jointly with the co-signer's non-purchasing spouse and there was no mortgage liability reported on the co-signer's credit report. Importantly, the property was located in the state of Florida, which is not a community property state, the co-signer's spouses debt was not considered in this loan application as per 4155.1.4.A.5b Non-Purchasing Spouse Debt. As the mortgage debt did not appear on the credit report, it was our opinion that Mortgagee Letter 2004-47 did not apply to this situation and UAMC properly performed its credit analysis of this loan.

Comment 11

Cited Asset Deficiency:

Gift fund: The lender did not properly document the gift provided to the borrower. The loan file included a gift letter indicating a gift of \$500 and a transaction detail report that reflected a posting of \$507. However, the transaction detail report did not state the account holder's name. Therefore, we were unable to confirm the withdrawal of funds from the donor's account. The lender stated that since funds were given before initial loan application and submission to the automated system, documentation of the gift was not required. However, HUD Handbook 4155.1, paragraph 5.B.4.d, states that regardless of when the gift funds are made available to a borrower, the lender must be able to determine that the gift funds were not provided by an unacceptable source and were the donor's own funds.

Unallowable fee: The lender charged the borrower an unallowable fee of \$85. HUD Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. The lender said that the seller- paid closing costs included the tax service fee. However, the tax service fee was not included in the seller paid closing costs: it was paid by the borrower.

UAMC Response:

Comment 12

Gift fund: The file contained a gift letter and a copy of the cashier's check given by the donor to the seller for the earnest money deposit which was dated the same date as the withdrawal posted to the donor's account according to the bank printout submitted to UAMC. Although the printout showing this withdrawal does not reference the donor's name, we would like to point out that this documentation was obtained in an abundance of caution, as actual transfer of gift funds would not have been required in this case, according to our understanding. HUD Handbook 4155.1, paragraph 5.B.5.b. states the following about transfer of gift funds: "The borrower must list the name, address, telephone number, relationship to the homebuyer, and the dollar amount of the gift on the loan application or in a gift letter for each cash gift received. If sufficient funds required for closing *are not* already verified in the borrower's accounts, document the transfer of the gift funds to the homebuyer in accordance with instructions described in HUD Handbook 4155.1." Since the borrower did document sufficient cash to close with a Verification of Deposit from Bank of America, it was our understanding that the actual transfer of the additional \$500 in gift funds was not required to be fully documented.

Comment 13

Unallowable fee: The borrower brought \$3,237.05 to closing from their own funds. That entire amount was used to pay off debts as reflected on line 1305 of the HUD-1 Settlement Statement. The seller paid all of the borrower's closing costs, therefore the seller also paid the Tax Service Fee of \$85.00.

OIG Evaluation of Auditee Comments

Comment 1: Universal stated that due to its rate of delinquency, it has taken significant steps to address its internal policies and underwriting quality over the past year. As a result, Universal (1) hired more underwriters, (2) expanded its training program, and (3) created a Risk Management Department.

We acknowledge Universal's efforts in strengthening its controls over the underwriting process.

Comment 2: Universal acknowledged its shortcoming in its follow-up process to ensure that every effort was made to obtain the required re-verifications during the audit period. The lender indicated that since the audit period, it has made several improvements in the area of quality control. The improvements include reviewing all 2011 random QC reviews and attempting to obtain missing re-verifications, and hiring a quality control staff who concentrates solely on the re-verification process.

We recognize Universal's efforts in strengthening its controls over the quality control process, and to ensure the effectiveness of its process, we recommended that HUD review the lender's operations within nine months.

Comment 3: As recommended in our report, the lender reported the deficiency associated with FHA case number 095-2007408 to HUD via neighborhood watch.

The lender has taken corrective action to address recommendation 2B of our report.

Comment 4: Universal acknowledged that the file did not contain the withdrawal of the gift funds from the donor's account. However, it believed that the file had sufficient documentation to determine that the donor provided the gift funds because the gift funds was recognized on the HUD-1, the bank statement showed sufficient funds for the gift, and the file contained a copy of the cashier's check.

Although the HUD-1 indicates a gift of \$4,900; it is not a withdrawal document that shows the funds came from the gift donor. The file did not contain the donor's bank statement; it contained a summary report that only indicated the donor had an available balance of \$5,189. Although the donor's summary report indicated that the donor may have had sufficient funds, it did not show that the funds were withdrawn from the donor's account. When the gift funds are provided at closing and are in the form of an official check, HUD Handbook 4155.1 5.B.5.b requires that the lender obtain the donor's withdrawal document or cancelled check for the amount of the gift, showing that the funds came from the donor's personal account. As stated by the lender, it did not know the reason the file did not contain adequate documentation on the withdrawal of the gift funds.

Therefore, Universal did not support that the gift funds came from an acceptable source.

Comment 5: Universal disagreed that the underwriter would have a reason to suspect that the borrower had any recent foreclosure activity. The loan application did not state that the borrower had a previous foreclosure. In addition, the credit report did not report any foreclosures, comments or other derogatory mortgage payment history, aside from one mortgage loan that had two 30-day delinquencies, the most recent in 2005. However, the credit report showed five previous mortgage loans with good payment histories, the most recent having been paid off in February 2007. This explained the mortgage interest deduction on the borrower's 2007 income tax return.

The loan application did not correspond with documentation in the loan file that indicated the borrower's recent foreclosure. For example, the borrower claimed a mortgage interest deduction in 2007 although the loan application signed in 2009 indicated that the borrower had (1) been renting the FHA property for 15 years and (2) no ownership interest in a property in the last three years. The underwriter should have questioned these inconsistencies; and thus would have discovered the borrower's recent foreclosure.

Based on the credit report, the five previous mortgages were opened between 1997- 2004. Having five mortgages in a seven year period does not denote a good pattern of stability although the borrower may have been paying timely. The credit report indicated that the most recent mortgage credit line was reported in February 2007, not that it was paid off.

According to County records, the borrower purchased the FHA property in 2001. The borrower refinanced this property at least annually from the time of purchase until it was foreclosed in July 2007, which suggests financial instability. In addition, the credit report did not show (1) that the borrower had a property until July 2007 or (2) the late payments that contributed to the foreclosure. The borrower indicated having hired a company that would help rebuild the borrower's credit. Therefore, the credit report may not have been complete to evaluate the borrower's credit worthiness.

The borrower's file had sufficient indicators that alluded to the borrower's foreclosure and other information that the underwriter should have considered when determining the borrower's ability and capacity to repay the mortgage debt. Therefore, this loan was not underwritten in accordance with HUD requirements.

Comment 6: The lender agreed that the underwriter should have asked for further clarification regarding the student loan with a balance of \$191,432. The lender explained that the credit report supplement reflected this loan as closed and having a zero balance. It also showed two new student loans opened having balances of

\$98,271 and \$7,194 respectively; since these amounts did not match the reported balance of the original student loan, the lender agreed with our conclusion.

Comment 7: The lender agreed that it should have obtained additional information to support the earnest money deposit. Although the file contained the donor's withdrawal of \$4,000, it did not agree with the \$3,000 earnest deposit. The lender explained that sufficient verification of assets has been the subject of its trainings, emails and underwriting discussions and will continue to emphasize the importance of obtaining sufficient documentation.

We encourage the lender to continue strengthening its controls in the area of verification of assets.

Comment 8: According to Universal, the seller agreed to waive a standard builder fee for the purchase of the property. Therefore, the lender believes that this fee was not tied to the financing of the property, hence it was not considered in the six percent contribution limit.

There was no documentation in the file that indicated the seller waived the standard builder fee for this purchase. Because the builder's fee is a standard fee charged for the purchase of the property it is part of the sale of the property and included in the 6 percent seller contribution. HUD also stated that the builder's fee credit is included since the 6 percent seller's contribution is all inclusive and includes all costs paid by the seller. Therefore, the seller credit for the builder's fee as reflected on the HUD-1 is included in the 6 percent seller contribution. As a result, the lender exceeded the 6 percent threshold.

Comment 9: The lender explained that the borrower's closing costs were paid by the seller therefore; the seller paid the \$73 tax service fee.

The tax service fee was included in the loan origination fees charged to the borrower. HUD Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. Therefore, the tax service fee should not have been included as part of the borrower's loan origination costs charged to the borrower. Since this fee was not the responsibility of the borrower, the lender needs to refund the tax service fee.

Comment 10: The lender indicated that it provided HUD with an executed indemnification letter in response to the lender's self-reported deficiencies.

The lender has taken corrective action to address the deficiencies associated with this loan. HUD required indemnification of FHA case number 095-172113 based on deficiencies reported by the lender that coincide with the deficiencies we identified during our audit. As a result, we will reduce the amount of questioned costs to account for the executed indemnification agreement.

Comment 11: The lender indicated that although the cosigner's income tax return reflected a mortgage interest deduction, the tax returns had been filed with the cosigner's non purchasing spouse. Furthermore, the credit report did not report a mortgage liability. Therefore, the lender believed that the liability may have been the cosigner's spouse and since Florida is not a community property state, the cosigner's spouse's debt should not have been included.

Although the cosigner's credit report did not indicate the cosigner had a mortgage liability, the file included a letter from the cosigner explaining that he planned to refinance his property, but did not go through with it. Since the file contained indicators of the cosigner's potential liability, the lender should have clarified whether the cosigner had a mortgage liability. HUD Handbook 4155.1.A.4.c requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial position. Therefore, the lender did not underwrite this loan in accordance with HUD requirements.

Comment 12: Universal agreed that the bank printout used to support the donor's gift did not identify the donor's name. The lender indicated that the donor's documentation was obtained in an abundance of caution. It was Universal's understanding that since the borrower had sufficient funds to close according to the verification of deposit; it did not need to fully document the transfer of gift funds to the borrower's accounts.

The borrower's verification of deposit showed that the borrower had sufficient funds to close; however, the lender was still responsible to verify that the gift funds were withdrawn from the donor's account to ensure that it came from an acceptable source. According to HUD Handbook 4155.1 5.B.4.c and 4155.1 5.B.4.e, the lender has the responsibility to ensure that funds given by the gift donor are not provided by a person or entity with an interest in the sale of the property, such as the seller or real estate agent. The transaction detail report used to support the gift did not state the account holder's name. HUD Handbook 4155.1 1.B.1.i, requires that asset information obtained from an internet website for depository accounts must provide the account's holder's name, number, transaction history, and balance.

Although the lender indicated that documentation was obtained in an abundance of caution, not completing the verification diminishes its preventive measures. Therefore, the lender should ensure that the information obtained is complete and adequately documented.

Comment 13: According to the lender, the seller paid all of the borrower's closing costs, which included the tax service fee of \$85.

The loan file did not support that the seller paid all of the borrower's closing costs. The HUD-1 shows the tax service fee was charged to the borrower. HUD

Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. Therefore, the tax service fee should not have been included as part of the closing costs charged to the borrower. Since this fee was not the responsibility of the borrower, the lender needs to refund the tax service fee.

Appendix C

SCHEDULE OF INDEMNIFICATION AND REPAYMENT

No.	FHA case no.	Original mortgage amount	Unpaid mortgage balance	Indemnification amount (a)	Status of loan as of February 29, 2012
1	095-1727113	\$240,236	\$239,283	\$157,927	Delinquent
2	095-1003547	\$ 226,816	\$225,309	\$148,704	Special forbearance
3	095-1873522	\$207,209	\$206,170	\$136,072	Delinquent
	Sub total	\$674,261	\$670,762	\$442,703	
	095-1727113	(\$240,236)	(\$239,283)	(\$157,927)	HUD indemnified loan
	Total	\$434,025	\$431,479	\$284,776	
<p>a. On May 10, 2012, the lender provided the indemnification agreement it executed with HUD pertaining to FHA case number 095-1727113. As a result, we reduced the indemnification amount for this loan and classified \$284,776 as funds to be put to better use. This is 66 percent of the \$431,479 in unpaid principal balances for the two loans as of February 29, 2012. The 66 percent is the estimated percentage of loss HUD would incur when the FHA property is foreclosed upon and resold as supported by the HUD Single Family Acquired Asset Management System's case management profit and loss by acquisition as of December 2011.</p>					

Appendix D

LOAN DETAILS FOR THE THREE PURCHASE LOANS

FHA case #: 095-1003547

Mortgage amount: \$226,816

Date of loan closing: 12/17/2009

Unpaid principal balance: \$225,309

Loan purpose: Purchase - existing

Default status: Special forbearance

Asset Deficiency

The lender did not adequately document the transfer of gift funds. HUD Handbook 4155.1, paragraph 5.B.5.b, requires that if the gift funds are provided at closing and are in the form of an official check, the lender must have the donor provide a withdrawal document or cancelled check for the amount of the gift showing that the funds came from the donor's personal account. The borrower received \$4,900 in gift funds. According to the gift letter, the funds would be provided at closing. The lender's file included a copy of the donor's account summary report and the official check to the closing company. However, none of the documents showed that the withdrawal came from the donor's account. To ensure that the borrower did not receive funds from an unacceptable source, the lender should have obtained documentation showing the money coming from the donor's account.

Credit Deficiency

The lender approved an ineligible loan by not considering a final judgment of foreclosure that occurred less than 3 years before the loan closing. HUD Handbook 4155.1, paragraph 4.C.2.f, states that HUD does not insure borrowers that had their principal residence foreclosed upon in the previous 3 years. Based on the borrower's 2007 tax return, the borrower claimed a mortgage interest deduction for a property. Public records showed that on July 23, 2007, the borrower had a property that was issued a final judgment of foreclosure. According to the borrower, due to financial challenges, the borrower was unable to make the mortgage payments on the borrower's principal residence, which led to the final judgment of foreclosure. To avoid the completion of the foreclosure process, the borrower sold the property to an investor within the 30-day redemption period.⁴ The borrower remained on the property and leased it from the investor. In December 2009, the borrower repurchased this property within 3 years of the foreclosure with an

⁴The final judgment of foreclosure stated that the owner of the property had approximately 30 days in which to pay the amount owed on the property and other fees.

FHA loan. Therefore, the borrower was ineligible to receive an FHA-insured loan due to the previous foreclosure.

The lender was unaware of and did not consider this foreclosure because it was not reflected in the credit report. Mortgagee Letter 2004-47, FHA TOTAL Mortgage Scorecard User Guide, explains that in the event that derogatory or delinquent credit items are revealed during the processing that are not reflected in the credit report, the lender must downgrade to a “refer” and manually underwrite the loan. Derogatory credit items include foreclosure, judgments, and so forth. If it is a foreclosure, the lender should follow HUD Handbook 4155.1, paragraph 4.C.2.f, Previous Mortgage Foreclosure.

When we informed the lender that the borrower was ineligible to receive an FHA loan, the lender disagreed because it believed that the property was not foreclosed upon since according to public records, the property was sold within the 30-day redemption period. Although the property was sold within the 30-day redemption period, the borrower’s inability to make payments contributed to the foreclosure, and the lender should have questioned the mortgage interest deduction and considered the borrower’s ability to make the mortgage payments.

HUD indicated that the lender, having firsthand information, should have discovered and analyzed the information and followed HUD Handbook 4155.1, paragraph 4.C.2.f, Previous Mortgage Foreclosure.

FHA case #: 095-1873522

Mortgage amount: \$207,209

Date of loan closing: 10/19/2010

Unpaid principal balance: \$206,170

Loan purpose: Purchase - existing

Default status: Delinquent

Credit Deficiency

The lender did not consider or clarify in its credit analysis a mortgage interest deduction in the cosigner's tax returns. HUD Handbook 4155.1 1.A 4.c requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial situation, and all information must be verified and documented. Based on the final loan application, the cosigner lived rent free. However, the cosigner claimed a mortgage interest deduction on his tax returns, which suggested that the cosigner had a mortgage loan that the lender should have considered when approving the loan. In addition, the loan file contained a letter indicating that the cosigner was going to refinance his property but did not go through with it. According to property records, the cosigner and his wife owned another property. Obtaining an explanation was important because it may have impacted the approval of the loan.

The lender explained that this liability was not included since the cosigners' credit report did not reflect an outstanding mortgage. However, the credit report did not include the cosigner's spouse. As a result, the credit report may not have reflected all of the cosigner's financial responsibilities that he may have had with his spouse. The lender should have inquired further about this mortgage deduction to obtain a complete picture of the cosigner's financial situation. According to Mortgagee Letter 2004-47, FHA TOTAL Mortgage Scorecard User Guide, if a mortgage debt does not appear on the credit report, the lender should obtain the most recent 12-month history and include the payment in the qualifying ratios.

Asset Deficiency

Gift fund: The lender did not properly document the gift provided to the borrower. The loan file included a gift letter indicating a gift of \$500 and a transaction detail report that reflected a posting of \$507. However, the transaction detail report did not state the account holder's name. Therefore, we were unable to confirm the withdrawal of funds from the donor's account. The lender stated that since funds were given before the initial loan application and submission to the automated underwriting system, documentation of the gift was not required. However, HUD Handbook 4155.1, paragraph 5.B.4.d, states that regardless of when the gift funds are made available to a borrower, the lender must be able to determine that the gift funds were not provided by an unacceptable source and were the donor's own funds.

Unallowable fee: The lender charged the borrower an unallowable fee of \$85. HUD Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. The lender said that the seller-paid closing costs included the tax service fee. However, the tax service fee was not included in the seller-paid closing costs; it was paid by the borrower.

FHA case #: 095-1727113

Mortgage amount: \$240,236

Date of loan closing: 8/31/2010

Unpaid principal balance: \$239,283

Loan purpose: Purchase - existing

Default status: Delinquent

Credit Deficiency

The lender did not ensure that all liabilities were included in its analysis. HUD Handbook 4155.1, paragraph 4.C.2.c, requires that a borrower provide a satisfactory explanation for any significant debt that is shown on the credit report but not listed on the loan application. The borrowers' initial loan application and credit report included a student loan with a balance of \$191,432, or a payment of \$980 per month. However, the final loan application did not include this student loan. The lender indicated that this student loan was not considered since a later credit report reflected that the loan was closed. Although the report stated that the loan was closed, it indicated that the account had been consolidated with a new account. Given that the amount was significant, the lender should have obtained further clarification regarding this account.

Asset Deficiency

Earnest money deposit: The lender did not determine the source of funds for an earnest money deposit. HUD Handbook 4155.1, paragraph 5.B.2.a, states that the lender must verify with documentation the deposit amount and source of funds if the amount of the earnest deposit appears excessive based on the borrower's history of accumulating savings. The HUD-1 settlement statement showed an earnest money deposit of \$3,000, which the coborrower provided. Based on the bank slip, on May 13, 2010, the coborrower made a cash deposit of \$3,000 to the coborrower's bank account, which had a beginning balance of \$114, and on the same day, the coborrower withdrew \$3,000 for the earnest money deposit. According to the coborrower's bank statements from January 1 through April 30, 2010, the average balance in the account was approximately \$1,049. However, the lender did not determine the source of funds for the earnest money deposit, which appeared excessive based on the coborrower's bank statements. In addition, the borrower's bank statements for the period April 13 through June 10, 2010, did not show that the funds came from the borrower. As a result, the lender should have clarified the source of these funds to ensure that they came from an acceptable source.

Seller contribution exceeding 6 percent threshold: Based on the final HUD-1 settlement statement, the seller credits totaled \$15,923, which exceeded the maximum allowable contribution of \$14,610. According to HUD Handbook 4155.1, paragraph 2.A.3.b, the third party may contribute up to 6 percent of the property's sales price toward the buyer's closing costs, prepaid expenses, discount points, and other financing concessions. The lender explained that the builder's fee credit of \$3,630 was not a part of the seller's contribution, as the fee was not tied to the financing and was paid to the seller directly. However, HUD indicated that the builder's fee credit would be included since the 6 percent seller's contribution is all inclusive. Therefore, seller credit exceeded the maximum allowable by \$1,313.

Unallowable fee: The lender charged the borrower an unallowable fee. HUD Handbook 4155.1, paragraph 5.A.2.a, states that borrowers may not pay a tax service fee. The lender said that the tax service fee was paid by the seller. However, the settlement statement indicated that the \$73 tax service fee was charged to the borrower.

Deficiencies That Were Self-Reported by the Lender for FHA Case #095-1727113

The following are deficiencies that we found; however, the lender had previously self-reported these deficiencies to HUD and taken preventive measures to ensure that these deficiencies would not recur.

Income deficiency: The lender obtained insufficient documentation to support the coborrower's employment information. HUD Handbook 4155.1, paragraph 4.D.2.d, states that part-time employment can be used to qualify the borrower if the lender documents that the borrower has held the part-time job uninterrupted for the past 2 years and documents the likelihood of the employment to continue. The lender obtained a letter from the employer that accounted for only 1.8 months of employment and did not indicate the likelihood that employment would continue. In addition, the coborrower's pay stub for the full-time employment included a required deduction of \$510 biweekly, which was not addressed in the file.

The lender took corrective actions by counseling the staff that worked on the file and reminded its underwriters to carefully review the pay stubs.

Credit deficiency: The lender did not consider or clarify in its credit analysis a mortgage interest deduction in the coborrower's tax return. HUD Handbook 4155.1, paragraph 1.A.4.c, requires the lender to ask sufficient questions of the borrower to get a complete picture of the borrower's financial position.

The coborrower's 2009 tax return showed that a mortgage interest deduction was claimed. The lender did not clarify whether the coborrower had an interest in a property or was making mortgage payments. The lender should have inquired about this mortgage because it may have had an effect on the qualifying ratios.

The lender took corrective actions by counseling the staff that worked on the file and reminded its underwriters to carefully review the tax returns.

Asset deficiency: The lender did not properly document a gift provided to the borrower. HUD Handbook 4155.1, paragraph 5.B.5.b, requires that the lender document borrower gift funds through a gift letter and verify the transfer of funds. Specifically, if the gift funds are in the borrower's account, the lender must obtain a copy of the withdrawal document showing that the withdrawal is from the donor's account and the borrower's deposit slip and bank statement showing the deposit. Based on the documents in the file, there were discrepancies regarding the amount of gift funds provided to the borrower. The final loan application, FHA loan underwriting and transmittal summary, and FHA Loan Prospector showed a gift amount of \$4,000, while the initial loan application, HUD-1 settlement statement, and gift letter showed a gift amount of \$3,000. In addition, the file included the gift letter that indicated a gift of \$3,000.

However, the donor's wire transfer indicated a wire transfer of \$4,000 and showed the originator and beneficiary as the donor.

The lender took corrective actions by counseling the staff that worked on the file and reminded its underwriters to properly document gift funds. In addition, it added the policy for proper documentation of gift funds to its loan program matrix.