

UNITED STATES OF AMERICA
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
BOARD OF CONTRACT APPEALS

Washington, D. C.

In the Matter of: :
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 GARY SNYDER, : HUDBCA No. 87-2407-D21
 : Docket No. 87-1114-DB (TDP)
 Respondent :
 :
 :

Mr. Gary Snyder

Respondent, Pro se

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Department of Housing and
Urban Development
Washington, D. C. 20410

For the Government

DETERMINATION ON REMAND

Statement of the Case

On November 24, 1986, a Temporary Denial of Participation ("TDP") was imposed against Gary Snyder by the Manager of the Tucson office of the U.S. Department of Housing and Urban Development ("HUD"). The TDP was affirmed on January 28, 1987, after an informal hearing. Snyder then requested a full hearing on the TDP pursuant to 24 C.F.R. §§24.18(a)(5)(iv) and 24.7(b). The TDP hearing was scheduled for June 6-7, 1987 in Tucson. On June 17, 1987, the Government issued a Notice of Suspension against Snyder, citing the same grounds as for the TDP, and moved that the TDP and suspension actions be consolidated for hearing. The motion for consolidation was granted.

The grounds for both actions were that Snyder, as a HUD-approved underwriter in the Direct Endorsement program, had certified sixteen loan applications for approval in a negligent, false or fraudulent manner. Specifically, Snyder was charged with three types of underwriting irregularities: 1) liabilities were not properly taken into account for underwriting purposes and were not properly shown on documents submitted to HUD, 2) tax returns and financial statements were improperly analyzed for underwriting purposes, and 3) real estate property holdings,

sales, and pending applications were not properly revealed on schedule of property submitted to HUD. The sixteen questioned loan applications involved one borrower, ██████████ Kaphing, a real estate investor.

At the conclusion of the hearing, oral findings of fact and conclusions of law were issued pursuant to 24 C.F.R. §26.24(d). In summary, it was found that any irregularities that occurred were either corrected, were minor in nature or there were mitigating circumstances which explained the apparent irregularities. It was concluded that Snyder was presently a responsible contractor and for that reason, neither sanction was warranted. A summary written determination was issued on July 10, 1987 incorporating the oral findings and conclusions. On July 24, 1987, the Government filed a request for Secretarial Review of the determination and order. That request was granted. On October 22, 1987, the case was remanded to the undersigned for further proceedings not inconsistent with the determination of the Secretarial Designee that the appropriate evidentiary standard of proof in cases involving TDPs and suspensions is "adequate evidence."

No further hearing is needed because a full evidentiary record was made by the parties at the hearing in July, 1987. This Determination on Remand is made in accordance with the October 22, 1987 determination of the Secretarial Designee.

Findings of Fact

1. The HUD Direct Endorsement program is designed to facilitate rapid and reliable processing of FHA single-family mortgages. After a mortgage company has been approved as an FHA mortgagee in general, it may obtain a higher FHA approval as a Direct Endorsement lender by meeting higher standards. Participation in the Direct Endorsement program means that the mortgage company can originate mortgages and effectively secure FHA insurance on the loans without prior loan-by-loan approval by HUD. After a loan is closed, the documents are forwarded to HUD for FHA insurance endorsement, which is granted automatically if the required documents are submitted.

The Direct Endorsement program relies heavily on the underwriter, an employee of the approved lender who must individually be approved by HUD as a Direct Endorsement underwriter. Each Direct Endorsement loan package submitted to HUD must contain a Form HUD-54113, Underwriter Certification. The Certification, signed by the underwriter under penalty of perjury, assures HUD that the loan has been processed and underwritten in a proper manner in compliance with HUD rules, regulations, and instructions. (Stipulation.)

2. Gary Snyder was, from 1982 to 1985, the manager of the Tucson, Arizona branch office of Colonial Mortgage Associates,

Inc. ("Colonial"). Colonial was a mortgage lender approved by HUD to participate in the Direct Endorsement program. General Motors Acceptance Corporation (GMAC) acquired Colonial in 1985, retaining Snyder as manager of the Tucson Office. Snyder's employment with GMAC terminated in May of 1986.

Snyder had been in the mortgage business about five years when HUD instituted the Direct Endorsement program in 1983. At that time, Snyder had worked for about three and a half years as a loan officer. In December, 1982, he was promoted to Branch Manager by Colonial. His job was primarily that of a salesman calling on realtors to solicit mortgage business. He also took initial applications for mortgages from loan applicants and did an initial check to see whether these applicants would qualify for loans, including loans by HUD-FHA. (Tr. II, 64-66; Stipulation.)

3. When Snyder applied to participate as the underwriter for Colonial in HUD's new Direct Endorsement program, he was enrolled by HUD in a two-day training program, a half-day of which involved mortgage credit training. As a prerequisite to participation in the Direct Endorsement program, HUD required submission of a minimum of 15 cases under a pre-endorsement program in which HUD would sign a commitment for insurance based on cases worked up and submitted for approval by the underwriter candidate. In May 1984, Snyder was approved by HUD as Colonial's underwriter for the Direct Endorsement program. That approval continued when Colonial was acquired by GMAC. (Tr. II 62-63.)

4. Loan specialists in the Housing Development Division of the HUD Tucson office are primarily responsible for conducting Post-Endorsement Reviews of Direct Endorsement loans, especially with respect to reviewing the mortgage credit analysis involved in such loans. Upon conclusions of each such review, they complete the bottom portion of a Form HUD-54118, Underwriter Rating, and thus gives a rating of either "good," "fair," or "poor," to the mortgage company's underwriter. This rating is placed in the FHA loan file for the loan, along with all documents submitted by the mortgage company with respect to the loan. The form also contains space to indicate specific omissions or problems with the underwriting of a given loan application. These forms are referred to as "report cards." The primary purpose of the report card is to show a rating and review of the underwriter's work on each file. It is also the way that HUD communicates with an underwriter about whether his work is or is not satisfactory. (Stipulation; Govt. Exhs. 1, 3; Tr. I 44-45, 52, 166; Tr. II 4.)

5. Snyder performed his underwriting duties by comparing information entered on HUD Form 9-2900 to the initial application he had taken from the mortgage applicant to make sure that the information was complete and accurate. The loan processors at Colonial would have sent for all of the required verifications of

deposit and employment, appraisal, and credit report, and transferred that information onto the Form 9-2900 before it was given to Snyder for underwriting review. Snyder relied on instructions from the HUD office, HUD handbooks and seminars in making underwriting decisions. He particularly relied on the report cards prepared by the HUD loan specialists. (Tr. II 66-72, 95-96.)

6. Gerald Kaphing was a real estate investor in Tucson. Snyder had met Kaphing in the course of his employment and was not a personal friend. He knew Kaphing for about two and a half years before he underwrote the first loan for Kaphing under the Direct Endorsement program. He subsequently underwrote many loans for Kaphing ("Kaphing loans") under the Direct Endorsement program, including the following sixteen loans FHA Case Numbers

[REDACTED], and
[REDACTED]. (Govt. Exh. 3(a)-(p); Tr. II 74, 80-81.)

7. The report cards for the Kaphing loans were prepared by HUD loan specialists Ruben Betancourt and Sharon Atwell. Betancourt, now a HUD GS-11 senior loan specialist, was a GS-5 loan specialist trainee in January 1983 who had no previous experience with mortgage credit analysis. He reviewed twelve of the Kaphing loans. Betancourt received no actual training in mortgage credit analysis, and there were no supervisors who could help him evaluate loans made under the program. Although Betancourt was familiar with loan application files for owner-occupants, he was unfamiliar with the more complex financial data submitted by an investor, such as Kaphing. The loan processors who prepared the files at Colonial for Snyder to underwriter called Betancourt to ask questions about the proper way to show financial information for Kaphing, particularly how they should show Kaphing's monthly income. Betancourt apparently approved the formula used by Colonial's loan processors to calculate Kaphing's monthly income. Betancourt performed seven "detailed" reviews for the report cards on the Kaphing loans that he reviewed, and the remainder were " cursory" reviews. Betancourt would list any omissions or problems with a file on the report card. A serious problem would be discussed with the then manager of the HUD Office, Adele Kauth. He listed no problems with the Kaphing loan files that he reviewed and gave Snyder good report cards on all of them. (Tr. II, 3-13; Govt. Exh. 3.)

8. Sharon Atwell came to work at the HUD Tucson office in February 1985. She was previously employed by the Internal Revenue Service, and had substantial experience evaluating tax return data. However, she had no prior training in evaluating mortgage credit data when she was assigned to review four of the Kaphing loans underwritten by Snyder. Atwell never gave Snyder a

"poor" rating on any of the four report cards she prepared, but she did list certain deficiencies, including the manner in which Kaphing's monthly income was being reported. Snyder's processors both asked Atwell for guidance on how to properly reflect Kaphin's monthly income and Snyder talked with both Atwell and Adele Kauth about the problem when it was noted for the first time by Atwell on the report card. A statement of how Kaphing's monthly income was calculated has been included in each file underwritten by Snyder. No one at HUD had indicated any problem with that method until Atwell did so in 1985. Snyder corrected the method of calculating monthly income as soon as Atwell explained the problem to him. (Tr. I 118-119, 168-170, 179, 190-192.)

9. The method of calculating Kaphing's monthly income that was used at Colonial and approved for underwriting by Snyder was based on adjusted gross income as reflected on the investor's Federal income tax return. It is not in direct violation of any HUD regulations or handbooks. However, Atwell's specialized experience in evaluating income data gave her the training and insight to realize that such a method of calculation would give an unrealistically high estimate of monthly income for Kaphing because the \$79,000 he had to pay in interest on outstanding loans was not subtracted from his adjusted gross income to reflect the actual disposable income he would have to pay future loans. Also, the drop in Kaphing's income, as shown on the complex profit and loss statements submitted by Kaphing, should have alerted Snyder that Kaphing may have been overextended. (Tr. I 143, 154, 189-190.)

10. It is required that all liabilities of a purchaser be listed on the HUD Form 9-2900. It is the duty of the underwriter to check all of the supporting information in the purchaser's application file to make sure that all liabilities that appear on the credit report or bank verifications are reflected as liabilities on the 9-2900. Gerald Kaphing had personally guaranteed a construction loan given to Sun Country Development, Inc., a corporation which he solely owned. That loan for \$250,199.94 appeared on the credit report but it was not listed on the 9-2900 as a liability. There should have been a written explanation placed in the file by Snyder about why the loan was not listed as a liability when it appeared on the credit report. The loan was not required to be listed as a liability of Kaphing on the 9-2900, because it was really a liability of Sun Country, not Kaphing, but an explanation should have been included in the file. (Tr. I 135-136; Tr. II 79; Govt. Exh. 3.)

11. Sharon Atwell gave Snyder a "fair" report card on files that did not list the Sun Country loan on the 9-2900. Only a general notation was made on the report card about "open accounts on the credit report - no explanation." At their meeting with Snyder, Sharon Atwell and Adele Kauth did not specifically mention to Snyder the apparent failure to list or explain in

writing the Sun Country loan but Atwell believed that Snyder would have corrected the problem by putting in a written explanation, if it had been pointed out to him. Ruben Betancourt never noted this problem in any of the seven files for which he performed "detailed" reviews. (Govt. Ex. 3; Tr. I 186, 192.)

12. None of the Kaphing loan files underwritten by Snyder contained a schedule of real estate sales, purchases, or loans applied for by Kaphing through the Direct Endorsement program. Each loan application must contain a schedule of all other real estate holdings. None of Kaphing's purchases under the HUD program were listed on the schedule of real estate, although other mortgages were listed. None of the report cards noted the absence of the HUD loans on the schedule of real estate. In a detailed review, a loan processor should look for a schedule of real estate and if real estate holdings are missing, the deficiency must be noted. The Form 9-2900 itself does not require a list of all other loans applied for by an applicant, nor does HUD Handbook 4155, 3-17F require such a listing. Likewise, there is no specific requirement that a list of properties sold be included, although some forms have a box to be checked if a property has been sold. (Tr. I 128-129, 131, 146, 148, 152; Tr. II 57; Govt. Exhs. 2, 3.)

13. At some undetermined date, Snyder's office provided a computerized print-out of all of Kaphing's real estate holdings, including all of the Direct Endorsement Program loans, to Adele Kauth. The Tucson office did not keep a separate listing of HUD loans and holdings of all mortgagors until February 1986, although HUD Handbook 4000.4 ¶3-16 requires that such a listing be maintained. (Tr. II 43, 50, 60, 94; Govt. Exh. 1.)

14. Ruben Betancourt and Adele Kauth were both aware that a large number of Direct Endorsement loans were being made to Kaphing in a relatively short period of time. Betancourt called that fact to Kauth's attention. He does not remember if he was specifically aware that the Direct Endorsement loans were not listed on Kaphing's schedule of real estate but he did talk with Adele Kauth about the Kaphing loans and files. Kauth assured Betancourt that she had met with Kaphing and Snyder, and the loans to Kaphing were low risk and there was no problem with the application files. (Tr. II 33-34, 52.)

15. Snyder denied that he was ever directed by Kaphing to omit Kaphing's Direct Endorsement loans on the schedule of real estate. Snyder did not direct the loan processors who prepared the files to omit that information from the real estate schedule. Snyder was not sure how this omission occurred, and was able to offer no reasonable explanation for the absence of the properties on Kaphing's real estate holding schedule. He admitted that he should have noticed their absence from the schedule. (Tr. II 77-79, 81-82, 85-88.)

16. The first time Snyder was given less than a "good" report card on a Kaphing loan was by Sharon Atwell, who gave a "fair rating" on three loan files. Two of the report cards on those files were dated May 17, 1985, and one was dated May 6, 1985. Each contained the same notations of problems, which included a question about the method for calculating Kaphing's 1984 income, use of financial statements prepared on Kaphing's computer rather than by a CPA, no explanation for open accounts on the credit report, missing lease agreements for rental property, and a statement that "schedule of real estate should be dated and filled out completely." (Govt. Exh. 3(c), (m) and (o).)

17. Snyder was very concerned that he was given less than a good rating on a report card and decided to fight the rating. A meeting was immediately held between Snyder, Adele Kauth and Sharon Atwell. Snyder was most worried about having to tell Kaphing that he could not use his computer-generated financial statements in future applications. The actual meeting focused on the method of calculating Kaphing's income. The unspecified deficiencies on the schedule of real estate and unexplained open accounts on the credit reports were not discussed to the best recollection of Snyder and Atwell. It was Atwell's opinion, based on that meeting with Snyder, that he was cooperative, wanted to do a good underwriting job, and was willing to correct mistakes pointed out to him. (Tr. I 168-169, 179, 186, 192; Tr. II 92-93, 96.)

18. Adele Kauth moved to the HUD Phoenix office and was replaced by Dean Miller in early 1986. Miller issued the TDP against Snyder as a culmination of a series of events involving the Kaphing loans. When Miller came on the job as manager of the HUD Tucson office, he found that about 20 Kaphing loans were about to go into default. He met with Kaphing and Snyder to work out a way for Kaphing to bring the loans current. A few months later, a number of Kaphing loans were again in default, with approximately 70 loans about to go into default. GMAC had acquired the loans and notified HUD that it would foreclose on all of them a few at a time. Miller again met with Kaphing and Snyder to try to protect the HUD insurance funds that covered the loans. Kaphing was unable to keep up with the payments due and the insurance fund had to pay about \$3,000,000 in losses after liquidation of the properties.

Miller directed his staff to do an audit of the Kaphing loan files to try to pinpoint the problems and avoid a repeat in the future. Miller focused on Snyder because he was the underwriter for all of the loans and had accompanied Kaphing at the meetings with Miller. He decided to impose a TDP on Snyder because he concluded that his underwriting was inadequate and faulty, based upon the audit of the file by his staff. He did not attempt to discuss the matter with Snyder or to get mistakes corrected before he imposed the sanction. Miller decided that a TDP was

necessary because the files were "too pat" and he got the sense that Snyder had prepared them in a manner designed to deceive HUD and to aid Kaphing in getting insured loans for which he might otherwise have been rejected. (Tr. I 36-40, 106-107, 112.)

19. Not a single witness knew of an instance when a specific problem had been pointed out to Snyder and he had failed to correct it. (Tr. I 85, 192.)

Discussion

The purpose of all administrative sanctions, including temporary denials of participation, suspensions and debarments, is to assure the Government that it only does business with responsible contractors and grantees. 24 C.F.R. §24.0. None of the sanctions are to be used for punitive purposes. They may only be used for the purpose of protecting the public. 24 C.F.R. §24.5(a). The test for the need for any of the sanctions is present responsibility. Although a finding of lack of present responsibility may be based on past acts, Schlesinger v. Gates, 249 F. 2d 111 (D.C. Cir. 1957), all mitigating circumstances must be taken into consideration in deciding that a sanction is necessary. Gonzalez v. Freeman, 344 F. 2d 570 (D.C. Cir. 1964).

Causes for imposition of both the TDP and the suspension must be established by adequate evidence. 24 C.F.R. §§24.12 and 24.18. However, the immediate purposes of the two sanctions are different. The TDP is a local office sanction that is limited to the specific program in which the irregularity occurred for a twelve-month duration, unless the irregularity is corrected sooner or it is in the best interest of the Government to resume business with the contractor. 24 C.F.R. §24.18(a)(3). Snyder's TDP was based on alleged irregularities in his past performance in the Direct Endorsement Program. The scope of the TDP, as applied by Dean Miller, included all HUD 203 programs. That scope was overly broad. All of the irregularities cited by HUD were restricted to the Direct Endorsement Program. The TDP should have been limited to that program only. 24 C.F.R. §24.18(a)(3)(i).

The suspension sanction is a temporary protective measure that allows the Government to avoid doing business with a contractor or grantee that it suspects is not presently responsible, pending completion of an investigation and such administrative or legal proceedings as may ensue. While a TDP involves irregularities that actually have occurred and that have been established by adequate evidence, the regulation provides that a suspension may be taken when a contractor or grantee is suspected of having committed certain acts, based upon adequate evidence. 24 C.F.R. §24.13(a)(i) and (2).

In the instant case, Snyder was days away from his hearing on the TDP which when the Department proposed a suspension based

on the identical charges cited in the TDP. It would have not only been impossible, but a denial of due process, to make a determination that the suspension could be sustained on adequate evidence to support a suspicion that certain sanctionable events had occurred, so as to allow the Government time to investigate the suspected conduct, when the HUD local office had not only decided that that conduct had actually occurred but had already applied a TDP based on it. The Government was directed to submit adequate evidence that the alleged irregularities had actually occurred, not just adequate evidence to support a suspicion that they had occurred. There was an apparent misunderstanding on the part of the Government that the evidentiary standard of adequate evidence had not been applied because of oral references made to the debarment sanction. Adequate evidence is the mandated evidentiary test, and was applied.

The Government has charged Snyder with three types of "irregularities" in the performance of his underwriting duties. Snyder's failure to put in the file an explanation of why the Sun Country loan was not listed on the Form 9-2900 as Kaphing's personal liability was less than excellent underwriting. Such a note would indicate that the credit report and verifications from the banks had been carefully checked against the information on the 9-2900. The loan was not a personal liability of Gerald Kaphing that had to be listed on the 9-2900. I find this charge to be of minor importance, and certainly does not rise to the level of a performance irregularity that requires protection of the public fisc. Had anyone at HUD pointed out to Snyder that such an explanation should be placed on the file to show that the underwriter was aware of the "debt," I find that he would have done so. I do not find that Snyder neglected to write an explanation in order to mislead HUD or to approve Kaphing for an insured loan for which he did not actually qualify.

The Government also cites Snyder's failure to properly evaluate Kaphing's tax returns and financial statements as an "irregularity." First, those statements were highly complex, Second, Snyder was not in violation of any regulation, law or procedure mandated by HUD. A statement of the method used for calculating Kaphing's monthly income - which is what this alleged irregularity is really about - was included in each file. It had been accepted by everyone at HUD as a legitimate, reliable method for projecting monthly income. That method was not called into question until Sharon Atwell was assigned to do a post-endorsement review of four Kaphing loans. She had specialized experience in analyzing complex tax data. She educated not only Snyder but the HUD staff. Snyder changed the method to the one suggested by Atwell as soon as it was brought to his attention. With hindsight, the Government claims that the method Snyder approved was obviously unacceptable and clearly designed to artificially inflate Kaphing's available income. I find nothing in the record to support this accusation. The method of calculating Kaphing's monthly income that Snyder

approved for underwriting was not an "irregularity" that would necessitate a sanction. It was not an "irregularity" at all. It is true that the HUD underwriting programs have benefited from the expertise of Sharon Atwell because she made everyone aware of more sophisticated methods of evaluating financial data that would provide more reliable indexes of financial liquidity. Nonetheless, that does not mean that the previously accepted method was an "irregularity." This charge is entirely inappropriate to support either a TDP or a suspension in the absence of evidence that the method used was deliberately chosen to mislead or defraud. I find no such evidence.

The evidence does establish that Snyder certified for underwriting files that did not contain complete listings of Gerald Kaphing's real estate holdings. Such listings are required by procedure, but not by law or regulation. This failure to provide complete real estate listings concerned me. However, because such a list was provided to Adele Kauth, although not included in each file, I find the seriousness of this omission mitigated to a certain degree. Certainly, such information is necessary to make an informed underwriting decision. Also, HUD requires it to determine whether investors are violating the "seven unit" rule for HUD property holdings. Violation of the seven unit rule was not an issue before me in this case, and I cannot find that the failure to place the schedule in each file was so serious as to warrant either suspension or debarment, absent evidence of intent to mislead or defraud by such omission. I find it to be less than good underwriting, but I do not find evidence of fraud. Snyder is aware of the need for such a schedule. He should not have missed the fact that holdings were missing from the list that Kaphing had given him. This was an irregularity in past performance, but I find that the subsequent production of a complete list and Snyder's awareness of the problems created by an incomplete list mitigate that irregularity.

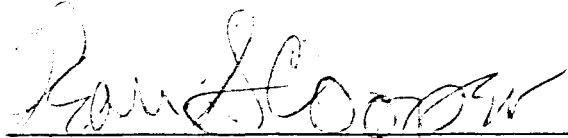
I find that Snyder is presently a responsible contractor, based on the record established before me. There was no evidence of fraud or collusion with Kaphing. I found Snyder to be a reliable, open and honest witness. He expressed genuine regret that he was not a better underwriter in 1984-1985. He is now fully familiar with the esoterica in the HUD handbooks that set out underwriting standards and techniques for evaluating financial data. Sharon Atwell testified that, although she did not find his underwriting to be as good as it should have been, Snyder was cooperative and made corrections as soon as the need for them was shown him. This is not the conduct of a contractor trying to mislead or defraud. It is responsible conduct.

No sanction is appropriate for a contractor who is presently responsible. 24 C.F.R. §24.0. Even if causes for a sanction are established, it is not mandatory that the sanction be applied. Based on the record before me considered as a whole, I find that

it is in the best interest of the Government to again do business with Gary Snyder as of the date of the hearing of this case because he is presently responsible. He cannot again be an approved underwriter for HUD without again making application and going through a screening. Any protection the public interest and HUD may need from Gary Snyder is more than served by that requirement. The TDP and suspension should be terminated because they are not presently warranted or necessary to protect the public interest.

CONCLUSION

For the foregoing reasons, the TDP and suspension imposed on Gary Snyder should be terminated.



Jean S. Cooper
Administrative Judge

Date: February 26, 1988