



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

Date: January 11, 2017

**To: All FHA Approved Mortgagees
All Direct Endorsement Underwriters
All FHA Roster Appraisers
All FHA Roster Inspectors
All FHA Approved 203(k) Consultants
All HUD Approved Housing Counselors
All HUD Approved Nonprofit Organizations
All Government Entity Participants
All Real Estate Brokers
All Closing Agents**

Mortgagee Letter 2017-03

Subject	Federal Housing Administration (FHA) Loan Review System – Implementation and Process Changes
Purpose	The purpose of this Mortgagee Letter (ML) is to notify Mortgagees of FHA’s plan to implement a new Loan Review System, which will be used to manage Title II Single Family Loan Reviews, Title II Single Family Mortgagee Monitoring Reviews, and Mortgagee self-reporting of fraud, misrepresentation and other material findings. The ML also updates related process guidance in Handbook 4000.1.
Effective Date	As system development is ongoing, the effective date will be confirmed in a subsequent Mortgagee Letter but will be no earlier than March 1, 2017.
Affected Programs	This guidance applies to all Mortgagees approved for FHA Title II Single Family programs.
Affected Topics	This guidance will affect Handbook 4000.1 sections I.A.5.a.iii(A)(3)(a)(ii), <i>Test Case Phase/Case Binder Submission/Post-closing Submission</i> , I.A.5.a.iii(A)(3)(b), <i>Test Case Phase/Test Case Underwriting Report</i> , I.A.6.b, <i>Post-Approval Operations/Providing Information to FHA</i> , V.A.2.d.iv(F), <i>Fraud, Misrepresentation and Other Findings/External Reporting to FHA/Method of Reporting</i> , V.C.2.b, <i>Title II Mortgagee Monitoring Reviews</i> , V.C.3.b, <i>Title II Loan Reviews</i> .

Background FHA is in the process of implementing a new Loan Review System to manage FHA's Title II Single Family quality control processes. The Loan Review System builds on recent efforts by FHA to align the documentation of loan review results across various divisions, and it incorporates the Single Family Housing Loan Quality Assessment Methodology (Defect Taxonomy), which was posted to hud.gov on June 18, 2015.

The Loan Review System will be used to process the review of Test Cases submitted by Mortgagees applying for unconditional Direct Endorsement (DE) approval, as well as various post-endorsement Title II Loan Reviews, Title II Mortgagee Monitoring Reviews, and other reviews currently conducted by FHA's Processing & Underwriting and Quality Assurance Divisions.

The Loan Review System will not be used to manage any aspect of FHA's standard (non-test case) loan origination or endorsement processes.

Following a transition, the Loan Review System will replace the Underwriter Review Functions and eFindings functions in FHA Connection, which currently reflect loan reviews conducted by FHA's Processing & Underwriting Divisions. The Loan Review System will replace emails and other manual processes currently used by FHA's Quality Assurance Divisions. Mortgagees will also use the Loan Review System to report fraud, misrepresentation and other material findings to FHA, replacing the current Lender Reporting feature in FHA's Single Family Neighborhood Watch Early Warning System.

The Loan Review System will include automated requests and reminders for Mortgagees to respond to findings and submit required documentation. Various reports and downloadable data will provide Mortgagees with summary statistics and loan-level review results.

Summary of Changes

Changes to HUD Handbook 4000.1 affected topics are as follows:

- *Test Case Phase/Case Binder Submission/Post-closing Submission* (Section I.A.5.a.iii(A)(3)(a)(ii)) states that Test Case review results will be documented in accordance with the *Title II Loan Reviews* section, and that Mortgagees must respond through the Loan Review System.

- *Test Case Phase/Test Case Underwriting Report* (Section I.A.5.a.iii(A)(3)(b)) includes separate instructions for certain Mortgagees to review Test Case results in the Loan Review System based on the Mortgagee's Test Case approval letter date.
- *Post-Approval Operations/Providing Information to FHA* (Section I.A.6.b) includes a new subsection for Loan Review System authorizations.
- *Fraud, Misrepresentation and Other Findings/External Reporting to FHA/Method of Reporting* (Section V.A.2.d.iv(F)) identifies the Loan Review System as the new method of reporting to FHA.
- *Title II Mortgagee Monitoring Reviews/Notice* (Section V.C.2.b.i) states that FHA may deliver notice via email, and that the Mortgagee may access the Loan Review System for additional details.
- *Title II Mortgagee Monitoring Reviews/Findings* (Section V.C.2.b.iv) states that monitoring review Findings will be documented in the Loan Review System and includes a new reference to the *Title II Loan Reviews* section.
- *Title II Loan Reviews/Notice* (Section V.C.3.b.i) states that Mortgagees without Lender Insurance authority can view loan selections in the Loan Review System or on the Insurance Application screen in FHA Connection.
- *Title II Loan Reviews/Findings* (Section V.C.3.b.iv) states that loan review results will be documented in the Loan Review System, that FHA's Defect Taxonomy will be used to capture information about Findings, and that Mortgagees must respond to Material Findings electronically.

The above mentioned policy changes will be incorporated into Handbook 4000.1 as follows:

**HUD Single
Family
Housing
Policy
Handbook
4000.1**

Post-closing Submission (I.A.5.a.iii(A)(3)(a)(ii))

Mortgagees who receive a DE Program Test Case approval letter from HUD's Homeownership Center dated on or after April 1, 2017, must submit all Test Case binders for review post-closing. The HOC will perform a review for compliance with FHA underwriting and closing guidelines. Review results will be documented in accordance with the Title II Loan Reviews/Findings section of this *SF Handbook*, and Mortgagees must respond to requests using the functions provided in the [Loan Review System](#).

The HOC will issue either a Firm Commitment (approval) or Firm Reject (denial) via a Notice of Return (NOR). Once a Firm Commitment is issued, the HOC will process the case for endorsement. If a NOR is issued, the Mortgagee must make all necessary corrections and provide all required documentation to the HOC using the [Loan Review System](#) before the Mortgage can be endorsed.

Test Case Underwriting Report (I.A.5.a.iii(A)(3)(b))

For Mortgagees who receive a DE Program Test Case approval letter from HUD's Homeownership Center dated on or before March 31, 2017, the Mortgagee, or its underwriter, must review the Underwriting Report completed by the HOC available through FHA Connection (FHAC) on all Test Cases. For Test Cases with an Unacceptable rating, the Mortgagee may submit mitigating documentation to the HOC that processed the Test Case. The Mortgagee must include all relevant documentation to support its request.

Mortgagees who receive a DE Program Test Case approval letter from HUD's Homeownership Center dated on or after April 1, 2017, must review all Test Case results in the [Loan Review System](#).

**Post-Approval Operations/Providing Information to FHA (I.A.6.b)
viii. Loan Review System Authorizations**

The Mortgagee must grant the Loan Review System authorizations in [FHAC](#) to staff it deems qualified to perform the relevant function(s).

The Mortgagee must grant the Loan Review System Indemnification authorization to individuals authorized by the Mortgagee to sign indemnification agreements.

**HUD Single
Family
Housing
Policy
Handbook
4000.1
(continued)**

**Fraud, Misrepresentation and Other Findings/External Reporting to
FHA/Method of Reporting (V.A.2.d.iv(F))**

The Mortgagee must use the Self-Report feature in the [Loan Review System](#) to report Findings to FHA. FHA may request supporting documentation, including the endorsement case binder, the QC report, and any other documentation necessary for FHA to fully evaluate the Finding.

Title II Mortgagee Monitoring Reviews/Notice (V.C.2.b.i)

FHA provides Mortgagees with notice prior to FHA monitoring reviews. Such notice may be transmitted via email to the Mortgagee's administrative contact, which is described in the [Doing Business with FHA](#) section of this *SF Handbook*. The Mortgagee may access the [Loan Review System](#) for detailed information about such monitoring review.

Title II Mortgagee Monitoring Reviews/Findings (V.C.2.b.iv)

At the conclusion of a monitoring review, FHA will document any identified Findings in the [Loan Review System](#) and will specify the remedies and response that are required from the Mortgagee. For reviews of mortgages conducted as part of a monitoring review, results will be documented in accordance with the [Title II Loan Reviews/Findings](#) section of this *SF Handbook*.

Title II Loan Reviews/Notice (V.C.3.b.i)

FHA will notify Mortgagees with Lender Insurance (LI) authority daily via email of its intent to review the Mortgagee's LI case binders. Mortgagees that do not have LI authority can view loans selected for review in the [Loan Review System](#) or on the Insurance Application screen in [FHAC](#).

Title II Loan Reviews/Findings (V.C.3.b.iv)

FHA will document the results of each review in the [Loan Review System](#) and will use its [Single Family Housing Loan Quality Assessment Methodology \(Defect Taxonomy\)](#) to identify and capture detailed information about any Findings related to compliance with FHA underwriting requirements. FHA will specify the remedies and response that are required from the Mortgagee. The Mortgagee must respond to any Material Findings using the functions provided in the [Loan Review System](#).

Paperwork Reduction Act The information collection requirements contained in this document are approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB control numbers 2502-0005, 2502-0059 and 2502-0600. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to a collection of information unless the collection displays a currently valid OMB control number.

Questions For additional information on this ML, please visit www.hud.gov/answers or call FHA's Resource Center at 1-800-CALLFHA (1-800-225-5342). Persons with hearing or speech impairments may reach this number via TTY by calling the Federal Relay Service at 1-800-877-8339.

Signature Edward L. Golding
Principal Deputy Assistant Secretary for Housing