
CHAPTER 5. PROGRAM MANAGEMENT

5-1 PURPOSE. The authority to participate in the Direct Endorsement program is a privilege. This is evidenced by HUD's reliance on the mortgagee's certification for the purpose of endorsing the mortgage. The mortgagee maintains this privilege by recommending for endorsement only mortgages which comply with HUD requirements. Because the substantive review occurs after the mortgage is endorsed, it is imperative that mortgagee performance be continually monitored and that remedial action, when necessary, be taken by the Field Office as soon as underwriting deficiencies are identified. The objective of the remedial action is to either improve mortgagee performance or to remove noncomplying mortgagees from the program. This chapter sets forth the actions which can be taken against noncomplying mortgagees and mortgage employees.

5-2 FIELD OFFICE MONITORING. HUD Field Offices monitor the performance of mortgagees, underwriters, and mortgagees' technical staff by reviewing cases during post-endorsement technical reviews, analyzing quality control reports, following upon construction complaints or consumer complaints, and sharing information with other field offices, HUD's monitoring division, the Mortgagee Review Board, and the Housing Civil Penalties Panel.

- A. Post-Endorsement Technical Review. Chapter 4 discusses problems which may be detected during a review and gives examples of problems which should yield fair and poor ratings.

The Underwriting Report, Form HUD-54118 is the basic method of notifying the mortgagee that underwriting is unsatisfactory. The Underwriting Report, which accompanies the case binder through the post-endorsement technical review, is sent to the mortgagee, the fee appraiser and the fee inspector, as appropriate, after completion of the technical review to inform the underwriter, appraiser, inspector and closing supervisor of any deficiencies. If significant errors were found, the original report is placed in the Field Office's file on that Direct Endorsement mortgagee. If requested by the mortgagee, HUD will send the Underwriting Report to the mortgagee's main office or to the company's quality control department. However, the mortgagee must provide the HUD Field Office with mailing labels if the reports are to be sent to any address other than the branch office which originated the case.

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B. Quality Control Reports. Early default and claim reports and a variety of CHUMS reports are available to assist Field Offices with their management responsibilities. Analysis of these reports will alert the Field Office to continuing problems and trends.

- 1) Early Default and Claim Report. This report is produced quarterly using data extracted from the Single Family Insurance in Force File, A43, and the Single Family Default Monitoring System, R17.

It shows, for each mortgagee, the number and percentage of recently originated loans that are in default or have gone to claim. This is the key quality control report as poor underwriting practices would probably result in higher default and claim rates.

- 2) Analysis of Technical Reviews, F17JYCA. This CHUMS report is produced monthly, quarterly, and fiscal-year-to-date. It shows, for each mortgagee, the number of mortgages insured, technical reviews completed, and ratings given by the technical branches.
- 3) Underwriter Performance Report, F17GBCA. This CHUMS report is produced monthly, quarterly, and fiscal-year-to-date and shows ratings given to the underwriter by the technical branches.
- 4) Appraiser Performance Report, F17GCCA. This CHUMS report is produced monthly, quarterly, and fiscal-year-to-date and shows ratings given to the appraiser during the technical review cycle based on a desk review of the appraisal.
- 5) Field Review Report, F17FOCA. This CHUMS report is produced monthly (showing quarter-to-date data) and quarterly (showing fiscal-year-to-date data). It provides information on appraisals performed by fee panel members and mortgagee staff appraisers for both HUD-processed and Direct Endorsement cases. The report shows the ratings given to the appraiser during the field review of the appraisal.

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C. Manual Records. The only manual records kept for Direct

Endorsement relate to the mortgagee's approval and performance. Copies of Underwriting Reports which have significant findings are filed in the mortgagee's file. The Director of Housing Development, Field Office manager, or Field Office Chief should review these files on a regular basis to ensure that mortgagees are performing acceptably and that technical review ratings are consistent with findings noted on the Underwriting Reports.

5-3 TYPES OF DEFICIENCIES. This paragraph offers parameters to consider the seriousness of noncompliance actions.

A. Level One Deficiencies.

- 1) Definition. A level one deficiency is generally any minor underwriting deficiency which does not change the eligibility determination of the property, the mortgagor, the mortgage amount or the term.
- 2) Examples of level one deficiencies are the following: improperly completed builder certifications; missing construction exhibits that do not preclude inspection; appraisal reports without a conventional sale; use of a comparable sale more than six months old; insufficient documentation of compensating factors; and use of an outdated credit report.

Level one deficiencies also include more serious deficiencies which the mortgagee is able and willing to correct, such as obtaining flood insurance coverage for a dwelling located in a flood hazard area and increasing the amount of escrow when the mortgagee's assurance of completion escrow is insufficient as submitted with the endorsement request.

- 3) Response. Isolated incidents are brought to the attention of the underwriter via the Underwriting Report. Patterns or continual problems should result in probation or withdrawal of Direct Endorsement approval.

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B. Level Two Deficiencies.

- 1) Definition. A level two underwriting deficiency is one which, when corrected, results in a significant increase in mortgage risk, through either greater credit risk or a decrease in property security. It is also one which involves acceptance of a mortgagor or property not permitted

by HUD policy, such as a condominium unit in an ineligible project.

- 2) Examples of level two deficiencies include: gross miscalculation of income; acceptance of a property seriously deficient of the required standards; missing builder certifications; construction exhibits inadequate for inspection; construction changes that affect value without proper change orders; and utilization of the mortgagee's assurance of completion when the dwelling involved is not habitable, safe and essentially complete.
- 3) Response. Appropriate Field Office response to level two underwriting deficiencies requires careful consideration of the deficiency in terms of the previous Direct Endorsement performance of the mortgagee. A deficiency of this nature should result in probation or withdrawal.

C. Level Three Deficiencies.

- 1) Definition. A level three deficiency is one which involves an action by the mortgagee to misrepresent either the financial capacity of the applicant-mortgagor or the condition of the property offered as security for the mortgage.
- 2) Examples of level three deficiencies include: fraudulent information or documentation, such as falsified Verifications of Employment; false certifications, such as reporting a delinquent loan as being current; omitting conditions relating to the health and safety of the property; and construction exhibits that do not represent the property resulting in a significant change in the security of the mortgage.

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- 3) Response. Due to the severity of this type of deficiency, the appropriate response could include: (a) imposing a limited denial of participation, (b) withdrawal of Direct Endorsement approval, (c) referral to the Mortgagee Review Board to consider withdrawing the mortgagee's HUD approval, (d) referral to the Participation and Compliance Division in Headquarters to consider debarment proceedings, (e) referral to the Director of the Office of Lender Activities and Land Sales Registration for consideration of civil money penalties by the Housing Civil Penalties Panel or the Mortgagee Review Board, or (f) referral to the Regional

Office of the Inspector General.

- 5-4 APPLICATION OF SANCTIONS. The sanctions described in this Chapter have been designed to give Field Office staff the flexibility to respond appropriately to any noncompliance action of a mortgagee or an individual. Noncompliance actions vary significantly in their scope and effect. The more serious the scope and effect of the actions, the more serious would be the sanction applied by the Field Office.

In deciding what sanction is appropriate, consider the seriousness and extent of the violations, the degree of fault on the part of the individual or the mortgagee, and any mitigating factors.

Withdrawal actions should be taken particularly where there is a pattern or practice of actions demonstrating noncompliance with the Direct Endorsement program requirements or where any pre-closing review status period (whether initially imposed or imposed under terms of a probation) has failed to demonstrate that the mortgagee can perform satisfactorily.

- A. Probation or Withdrawal of Direct Endorsement Approval. The authority to apply the mortgagee sanctions (probation and withdrawal) rests with the same individual who has the authority to approve mortgagees for Direct Endorsement.
- B. Indemnification Agreement. The authority to enter into an indemnification agreement rests with the Office of Lender Approval and Land Sales Registration.

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- C. Limited Denial of Participation. The authority to impose a Limited Denial of Participation rests with the Field Office, and with the Deputy Assistant Secretary for Single Family Housing. Refer to HUD Handbook 1300.13 for further guidance.
- D. Withdrawal of HUD-approval and Administrative Sanctions against Mortgagees. The Mortgagee Review Board is the sole organization within HUD authorized to take administrative action against HUD-approved mortgagees. Refer to HUD Handbook 4060.2.
- E. Debarment and Suspension. Any Assistant Secretary of HUD, the General Counsel of HUD or the President of the Government National Mortgage Association (GNMA) may debar or suspend participants or contractors. Refer to HUD Handbook 1300.13 for further guidance.
- F. Civil Money Penalties. Field offices may refer program

participants for consideration of civil money penalties by the Housing Civil Penalties Panel (HCPP) or the Mortgage Review Board. The Office of Lender Activities & Land Sales Registration (OLA) serves as the staff to the HCPP and the Mortgagee Review Board.

5-5 PROBATION. When a mortgagee fails to comply with the Direct Endorsement program requirements, the Field Office may place the noncomplying office on probation.

A. Probation Elements. Probation consists of one or more of the following elements:

- 1) Training. The mortgagee's underwriter, or other technical staff, may be required to attend appropriate training sessions.
- 2) Pre-closing Review Status. The mortgagee may be placed back in pre-closing review status. Mortgagee submissions would then be subject to technical underwriting reviews and firm commitment processing prior to endorsement.

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The pre-closing review status continues until the mortgagee demonstrates, through satisfactory performance, that the underwriting shortcomings have been corrected, or until the mortgagee's Direct Endorsement approval is withdrawn.

- 3) Mortgage Audit. The Field Office may require the mortgagee to perform a procedural underwriting review and report the results to HUD.
 - 4) Quality Control Plan. The Field Office may require the mortgagee to make changes to its quality control plan.
- B. Notification Procedure. A written notice of the probation action is sent to the mortgagee. The notice explains which of the probation elements are being applied and describes the noncomplying action which precipitated the probation. The probation is effective upon receipt by the mortgagee of the notice. The format of the probation letter is in Appendix 12.

5-6 WITHDRAWAL OF DIRECT ENDORSEMENT STATUS. Depending upon the nature and extent of the noncompliance with the requirements of the Direct Endorsement program, the HUD Field Office may withdraw the approval of the noncomplying office to participate in the program.

- A. Notification Procedure. A written notice of the withdrawal action is sent to the mortgagee. The withdrawal is effective upon receipt by the mortgagee of the notice. The notice states the grounds for the action and provides the mortgagee the right to an informal conference before the decision maker. Such hearing, if requested, is to be arranged within 15 days of the mortgagee's request. The mortgagee may be represented by counsel.

A copy of the withdrawal letter is to be sent to the Office of Lender Activities and Land Sales Registration in Headquarters. Another copy is to be sent to the Single Family Development Division in Headquarters. The format of the withdrawal letter is in Appendix 13.

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- B. Hearing. The purpose of the hearing is to provide the mortgagee the opportunity to address the grounds for the action as stated in the notice, make documentary and oral presentations and advise the decision maker what, if any, corrective action may have been taken to address the problems identified.
- C. Hearing Follow-up. Following the hearing, the decision maker advises the mortgagee in writing whether the withdrawal is rescinded, modified or affirmed.

- 5-7 EFFECT OF DIRECT ENDORSEMENT SANCTIONS. The probation and withdrawal sanctions are applied to the mortgagee office (branch or main) which submitted the noncomplying cases. The action applies only to the one office of the mortgagee and only to the jurisdiction of the Field Office.

In those instances where an underwriter serves more than one office of a mortgagee in one or more HUD Field Office jurisdictions, the application of probation and/or withdrawal sanctions by one Field Office does not automatically affect the eligibility of the underwriter to serve other offices of the mortgagee in the same or other Field Office jurisdictions. The Field Office which applies mortgagee sanctions is to notify other offices. Other Field Offices would then act accordingly.

- 5-8 INDEMNIFICATION AGREEMENTS. Violations of HUD's requirements which significantly increase the Department's risk and were caused by fraud or serious negligence on the part of the mortgagee should be referred to the Monitoring Division of the Office of Lender Activities and Land Sales Registration. The Monitoring Division may schedule an on-site review of the mortgagee's origination practices. The Office of Lender

Activities and Land Sales Registration may request that the mortgagee enter into an Indemnification Agreement with the Department in lieu of referring the matter to the Mortgagee Review Board.

These agreements essentially guarantee that the Department will not suffer a loss on the loans. The mortgagee agrees to abstain from filing a claim or to reimburse the Department if a subsequent holder files a claim. The term of the agreement varies with the severity of the violation, typically they are effective for five years from the date of endorsement.

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5-9 WITHDRAWAL OF HUD APPROVAL. Serious noncompliance with the requirements of the Direct Endorsement program are to be referred to the Mortgagee Review Board and may result in withdrawal by the Board of the mortgagee's basic HUD approval. Withdrawal of HUD approval applies to the Mortgagee's main office and all branches. While HUD approval is withdrawn or suspended, the mortgagee may not originate or purchase any insured mortgages.

5-10 CIVIL MONEY PENALTIES. The Department may impose civil money penalties on program participants who knowingly and materially violate relevant program statutes, regulations and handbook requirements.

A. Background. The HUD Reform Act of 1989 was signed into law on December 15, 1989. Section 107 of the Reform Act authorizes the Department to impose civil money penalties on program participants. The Reform Act and the implementing regulations (24 CFR Part 30) provide for increased program enforcement efforts on the part of the Department. A civil money penalty may be imposed in addition to other administrative sanctions or any other civil or criminal penalty.

B. Housing Civil Penalties Panel (HCPP) and Mortgagee Review Board. The HCPP, which is within the Federal Housing Administration, is responsible for reviewing recommendations for civil money penalties and proposing the imposition of civil money penalties against program participants. The HCPP is composed of the following members, or their designees: Assistant Secretary for Housing-Federal Housing Commissioner, Chairman; Deputy Assistant Secretary for Operations; Deputy Assistant Secretary for Multifamily Housing Programs and the Deputy Assistant Secretary for Single Family Housing. The HCPP also includes the Assistant Secretary for Fair Housing and Equal Opportunity, or designee (in cases involving violations of the Department's nondiscrimination requirements). A designee of the Office of General Counsel serves in a non-voting advisory capacity to the HCPP.

The Department's Mortgagee Review Board is also authorized to impose civil money penalties against mortgagees. This authority is in addition to the Board's other functions.

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- C. Office of Lender Activities & Land Sales Registration. The Office of Lender Activities & Land Sales Registration (OLA) serves as the staff to the HCPP and the Mortgagee Review Board. The OLA coordinates all referrals and is the designated contact point for all civil money penalty cases involving Housing's programs. The OLA notifies program participants of the Department's intention to seek civil money penalties, presents cases to the HCPP and Mortgagee Review Board for action, negotiates Settlement Agreements and notifies program participants of all HCPP and Mortgagee Review Board decisions.
- D. Field Office Referrals of Civil Money Penalty Cases. Field Offices may refer program participants for consideration of civil money penalties by the HCPP or the Mortgagee Review Board. A referral must be based upon adequate documentation that a program participant has knowingly and materially engaged in violations of the Department's rules or requirements. Generally, the term "materially" means that the violations have a financial impact on the Department or may have influenced a Departmental decision, i.e. whether to endorse a mortgage for insurance. The term "knowingly" means that the program participant had actual knowledge of the violations or was acting with deliberate ignorance or reckless disregard of the Department's requirements.

All referrals are to be sent to the Director, OLA. The referral must contain a report which includes a full factual background of the violations, citation(s) of the Department's regulations or requirements that have been violated, and all available supporting documentation that evidences the violations and all information that the program participant has previously submitted to the field office. The Director of the OLA will coordinate the referral and, if appropriate, submit the case to the HCPP or the Mortgagee Review Board for action.

- E. Examples of Violations for Which Civil Money Penalties May Be Imposed on Mortgagees. A civil money penalty may be imposed by the Department against a mortgagee for knowing and material program violations that include:
 - 1) Transfer of an insured mortgage to a mortgagee not approved by the Department.

- 2) Use of escrow funds for any purpose other than that for which they were received.

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- 3) Falsely certifying to the Department or submitting to the Department a false certification by another person.
- 4) Failure to comply with mortgage servicing requirements.
- 5) Submitting false information to the Department in connection with any insured mortgage transaction.
- 6) Hiring or employing an individual such as an officer, director, principal or employee whose duties involve programs administered by the Department, while that individual is under suspension or debarment by the Department.
- 7) Failing to comply with any agreement, certification or condition set forth, or applicable to, the application of a mortgagee for approval by the Department.
- 8) Failure by a mortgagee to segregate escrow funds received from mortgagors and to deposit such funds in a special account with a federally insured depository institution.
- 9) Hiring or retaining an agent whose duties involve programs administered by the Department while such agent is under suspension or debarment by the Department.
- 10) Failure to remit, or timely remit, mortgage insurance premiums, loan insurance charges, or late charges or interest penalties.
- 11) Failure to timely submit documents that are complete and accurate in connection with a conveyance of property or a claim for insurance benefits.
- 12) Failure to comply with the provisions of the Real Estate Settlement Procedures Act (RESPA).

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- 5-11 EFFECT OF SANCTIONS ON CASES IN PROCESS. The application of Direct Endorsement sanctions against a mortgagee does not affect the eligibility of the mortgagee to participate in HUD's single family programs through the conditional/firm commitment process.

Arrangements will be made for those mortgage loan applications undergoing the mortgagee's Direct Endorsement origination process. Mortgages closed on or before the date the mortgagee receives the notification will be accepted for Direct Endorsement processing. All other applications in process are to be submitted to HUD for prior approval processing prior to closing.

If HUD approval is withdrawn and the mortgagee does not intend to seek reinstatement, cases must be submitted to the HUD Field Office for prior approval processing within five days of receipt of the withdrawal letter. Loans covered by firm commitments may be closed and insured in the name of the mortgagee. Conditional commitments must be transferred or assigned to another HUD-approved mortgagee.

- 5-12 SANCTIONS AGAINST INDIVIDUALS. Where the situation warrants, take action against the individual as well as the mortgagee. See HUD Handbook 1300.13.

Under the Department's regulations (24 CFR Part 24) there are administrative sanctions which may be taken against persons who lack business responsibility. The sanctions discussed in this paragraph may be applied against mortgagee employees approved for Direct Endorsement participation, such as the underwriter, a staff appraiser, a staff mortgage credit examiner and a staff inspector.

Underwriters who falsify their credentials or experience should have their approval revoked. In addition, apply other administrative sanctions as appropriate.

Any criminal, fraudulent or other seriously improper conduct of an underwriter may be attributed to the organization with which the underwriter was connected when the impropriety was performed within the course of the underwriter's official duty, resulting in appropriate administrative sanctions against the mortgagee.

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- A. Limited Denial of Participation. A Regional Administrator or a Field Office Manager may impose a Limited Denial of Participation

(LDP) against any participant or contractor, except HUD-approved mortgagees. Officers and employees of mortgagees may also be sanctioned, unless that would be a de facto sanction against the mortgagee.

In each case, even if the offense or violation is of a criminal, fraudulent or other serious nature, the decision to order an LDP is discretionary and should be imposed only if in the best interests of the Government.

- 1) Causes for ordering a Limited Denial of Participation are listed in 24 CFR 24.705.

Included are: (a) approval of an applicant who is an unsatisfactory risk; (b) falsely certifying in connection with any HUD program; (c) failure to proceed in accordance with the Direct Endorsement underwriting requirements which include the Department's written regulatory and handbook requirements relating to all aspects of mortgage loan origination (architectural review, property analysis, mortgage credit analysis, underwriting procedures).

- 2) Period and Scope. A Limited Denial of Participation extends only to participation in the program under which the cause arose. In terms of an LDP, program means any or all of the functions within the jurisdiction of an Assistant Secretary. Where the LDP is based on an indictment, conviction, or suspension or debarment by another agency, it need not be based on offenses against HUD and it may apply to all programs of HUD.

The sanction may be imposed for a period not to exceed 12 months and is limited to the geographic jurisdiction of the office imposing it.

- 3) Written Notice. The individual is sent a written notice of the action, by mail, return receipt requested. The sanction is effective as of the date of the notice. When the sanction is taken against an individual employed by the mortgagee, a copy of the notice is sent to the mortgagee.

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The notice provides the grounds upon which the action is based and the potential effect of the sanction. The notice advises the individual of his right to request in writing, within 30 days of receipt of the notice, a conference on the sanction, and the right to have such conference held within

10 business days of receipt of the request by HUD.

- 4) Conference. Upon receipt of a written request for a conference, the decision maker in the HUD Field Office will arrange such a conference within 10 business days. The decision maker may designate another official to conduct the conference.

The sanctioned individual may be represented by counsel and may present all relevant materials to the official, or designee.

After consideration of the materials presented, the official will advise the individual, in writing, within 20 days after the conference and receipt of materials, of the decision to withdraw, modify or affirm the order, the individual may request an appeal.

Any individual desiring an appeal must file a written request for a hearing before an Administrative Law Judge authorized to conduct these proceedings by HUD's Secretary or his designee. The appeal request must be sent to the Debarment Docket Clerk, Department of HUD 451 Seventh Street, SW, Washington, DC 20410-8000.

- 5) Combined TDP/LDP List. Field Offices must notify HUD's Participation and Compliance Division when LDP actions are taken. That Division distributes a list of Temporary Denials of Participation (the precursor to LDP) and Limited Denials of Participation. Requests for this list would be directed to the Participation and Compliance Division, 451 Seventh Street, SW, Washington, DC 20410-8000.

- B. Suspension and Debarment. In addition to the actions described above, serious noncompliance is referred to HUD Headquarters and may result in suspension and debarment sanctions. These sanctions, taken by an Assistant Secretary, are effective nationwide and exclude the individual from participating in any HUD program. The sanctioned individual is entitled to appeal the action. Upon appeal, a hearing will be held before an Administrative Law Judge.