

CHAPTER 6. QUALITY CONTROL PLAN

6-1 GENERAL REQUIREMENT. As a condition of HUD Title I approval, all lenders, including Loan Correspondents, shall prepare and implement a Quality Control Plan (QCP) The Department considers a QCP to be an important part of a lender's origination and servicing operations in order to ensure that the lender maintains compliance with HUD requirements and its own policies and procedures. The QCP must be sufficient in scope to enable the lender to evaluate the accuracy, validity and completeness of its loan origination and servicing operations.

- A. POLICY AND OBJECTIVES. All Nonsupervised and Supervised Lenders and Loan Correspondents shall prepare and implement a QCP which utilizes an independent program of internal or external audit performed by personnel who are knowledgeable and have no direct loan processing, underwriting or servicing responsibilities. The quality control function may be performed by either company personnel or an outside firm. The QCP shall provide for periodic reports to be provided to senior management. The reports will identify for senior management any areas of the loan origination or servicing functions that are deficient.
- B. SCOPE. The QCP must provide for a monthly review of not less than ten percent of all Title I loans originated by the lender on a monthly basis, including its branches and Loan Correspondents. For loan servicing, lenders must perform a quarterly review of a representative sample of loans that is sufficient in number to provide reasonable evidence that HUD loan servicing policies and requirements have been met. For each branch office that originates or services HUD insured Title I loans, an on-site branch office review must take place at least once every year. The QCP must also provide for a review of the lender's files and records to determine compliance with HUD's Fair Housing Act as amended in 1988.
- C. LOAN CORRESPONDENTS. While it is important for Sponsors to include each of their Loan Correspondents in their review samples, each Loan Correspondent must have its own QCP. It is not acceptable for a Sponsor to perform its routine review of Loan Correspondents

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and use this as a replacement for the Loan Correspondent's own review, unless a full 10 percent sample is reviewed.

As discussed below, Loan Correspondents may choose to use an outside source to perform their quality control reviews. However, if a Sponsor is used, the review must cover the full 10 percent sample.

- D. QUALITY CONTROL REVIEWS MUST INCLUDE:

1. A selection of loans on a random basis including loans from all branch offices, loan correspondents and servicing agents.
 2. Assurance that all loan officers, underwriters and servicers will have loans subjected to reviews.
 3. Analysis of all loans which go into default within six payments after closing.
 4. Procedures for expanding the scope of the review where a pattern of deficiencies or fraudulent activity is disclosed.
- E. CONTRACTING OUT. Lenders are permitted to use an outside source to perform their quality control reviews. This procedure may be useful for smaller lenders who do not have sufficient staff to devote to quality control, for example. The outside source is expected to use the lender's QCP or develop one that meets the Department's requirements. Lenders are still required to take appropriate actions in response to findings, as discussed in this Chapter.
- F. INITIATE CORRECTIVE ACTION. The QCP must require written notification to the lender's senior management, at least quarterly, of deficiencies cited as a result of the reviews. Senior management must promptly initiate action to correct all deficiencies. The actions taken by management must be formally documented by citing each deficiency, identifying the cause of the deficiency, and providing management's response or actions taken. Employees are to be provided with the results of the quality control review.

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- G. NOTIFICATION TO HUD OF SIGNIFICANT DISCREPANCIES. Approved lenders are required to report to HUD any violation of law or regulation, false statements or program abuses by a borrower, dealer, the lender, its Loan Correspondents, employees or any other party to the transaction (refer to 24 CFR Section 201.40(a)). These reports should be forwarded to the Monitoring Division in Washington, D.C. or the Office of Inspector General at the nearest HUD field office.

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GENERAL REQUIRED ELEMENTS OF THE QUALITY CONTROL PLAN. The quality control plan shall:

- A. Assure that each office of the lender including, if applicable, its approved Loan Correspondent(s) and branches maintain copies of all HUD issuances, including regulations, handbooks, and Title I letters, etc., which are relevant to the lender's Title I origination and servicing activities. These documents must be accessible to all employees, and new directives must be reviewed with appropriate staff.
- B. Assure that all loans reported by the lender to HUD/FHA for insurance are processed only by employees of the lender.

- C. Assure that the lender does not employ or conduct Title I business with any individual who is debarred, suspended or subject to a Limited Denial of Participation (LDP).
- D. Assure that a check was made through the Department's Credit Alert Interactive Voice Response System (CAIVRS) or some other means to determine whether an applicant is in default or a claim has been paid in connection with any loan obligation owed to or insured or guaranteed by the Federal government'.
- E. Assure that the originating lender is retaining a copy of the entire case file pertaining to all loan originations, either in hard copy or microfilm form, for at least two years from date of loan disbursement.
- F. Assure that Home Mortgage Disclosure Act (HMDA) reporting is being done accurately, timely and is properly documented.

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- G. Assure that the lender does not require, as a condition of providing an insured loan, that the principal amount of the loan exceed a minimum amount established by the lender.
- H. Assure that quality control reviews are performed within 90 days of loan disbursement. For loan servicing, reviews must be done at least quarterly.
- I. Assure that post-disbursement inspections are conducted to determine that improvements were completed or a manufactured home was properly installed.
- J. Assure that the lender keeps records of the results of quality control reviews, including findings and actions taken, for a period of one year.

6-3 REQUIREMENTS FOR LOAN ORIGINATION.

- A. GENERAL. Lenders are expected to exercise prudence and diligence in determining whether the borrower is an acceptable credit risk, with a reasonable ability to make payments on the loan obligation. All documentation supporting the determination of creditworthiness must be retained in the loan file.
 - 1. The QCP must ensure that all loans comply with the applicable provisions of 24 CFR Part 201 and requirements contained in Title I letters.
 - 2. The QCP must provide for the reverification of the borrower's employment and deposit by telephone or in writing with the employer and depository. It must also provide for the reverification of gift letters or other sources of funds. All reverifications must be documented in the loan file.

3. A new in-file credit report must be obtained and compared to the original for discrepancies. Also, the credit report must be reconciled with the credit application to determine that all liabilities were listed or properly adjusted and documented.

B. SPECIFIC REQUIREMENTS: The QCP must provide for a review of the loan origination and underwriting functions in order to:

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1. Determine whether all income and employment data is supported by written verification or other documentation, especially for self-employed applicants and those with non-employment income. Determine whether the loan file contains a financial statement or Federal income tax return if the borrower is self-employed.
2. Determine whether a complete and current consumer credit report on the borrower and any co-maker or co-signer was obtained, and any credit inquiries reported within the previous 90 days were checked. If more than one credit report was obtained, determine whether all information was considered by the underwriter and any discrepancies were resolved.
3. Determine whether a written verification of the source of funds was obtained through verifications of deposit, bank statements, gift letters or other written documentation, when the principal balance of the loan exceeds \$5,000 and the initial payment exceeds five percent of the loan amount.
4. Determine whether the borrower's expense-to-income ratios are within the allowable ratios established by HUD/FHA, or that there are appropriate compensating factors that support approval of the loan.
5. Determine whether all conflicting information or discrepancies were reconciled and properly documented in writing.
6. Determine whether the lender completed a face-to-face or telephone interview with the applicant before making a final determination of creditworthiness in order to ensure the accuracy of information in the file. (Refer to 24 CFR 201.22(a) (9)).
7. Determine that proper procedures were used to determine borrower eligibility and evaluating whether the loan proceeds were intended to be used for eligible purposes. (Refer to 24 CFR 201.20 or 201.21 as appropriate.)

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8. Determine whether the property improvement loan files contain all required documents, including but not limited to, completion certificates and inspections of completed improvements.
9. Determine whether each manufactured home loan file contains all required documents, including but not limited to, a placement certificate and a site-of-placement inspection.
10. Where the lender approves dealer loans, determine that the lender supervises and monitors each dealer and visits the dealer periodically.
 - a. Determine that each dealer's approval is documented on a HUD-approved form signed and dated by both parties.
 - b. Determine that each dealer file contains the dealer's current financial statement, including a determination that the dealer meets the minimum net worth requirements of 24 CFR 201.27(a) (1), and credit reports on the dealership and its owners, principals and officers.
 - c. Determine that each file contains documentation of the lender's experience with the dealer's Title I loans, including information on borrower defaults and borrower complaints and their resolution.
 - d. Determine whether the lender reviews the dealer's advertising during the time of annual re-approval and during the semi-annual on-site visits to ensure it is not inaccurate or misleading regarding the Title I Program.

6-4 REQUIREMENTS FOR LOAN SERVICING

- A. GENERAL The lender shall service loans in accordance' with accepted practices of prudent lending institutions. It shall have adequate facilities for contacting the borrower in the event of default, and

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shall otherwise exercise diligence in collecting the amount due. The lender shall be responsible for proper collection efforts, even though actual loan servicing and collection may be performed by an agent of the lender. The lender shall have an organized means of identifying, on a periodic basis, the payment status of delinquent loans to enable collection personnel to initiate and follow-up on collection activities, and shall document its records to reflect its collection activities on delinquent loans.

- B. SPECIFIC REQUIREMENTS The QCP must provide for a review of the loan servicing function in order to:

1. Determine that loan servicing records are promptly established after loan closing or acquisition and that the servicing

records contain the information necessary to properly service the loan. Also, determine that the borrowers have been notified concerning the transfer of servicing.

2. Determine through a review of individual loan servicing records that the amount of fees and charges imposed on the borrower do not exceed those permitted by HUD regulations at 24 CFR 201.25.
3. Determine that inquiries from borrowers concerning their individual loan accounts are promptly responded to.
4. Determine that an analysis is performed on all loans that default early (less than 6 payments) to determine the cause of the default and confirm that the loans were underwritten properly.
5. Determine that borrowers are provided every reasonable opportunity to remedy a delinquency or default, including modification agreements or informal repayment plans.
6. Determine that adequate collection activities and accurate documentation of collection efforts are recorded.
7. Determine that a face-to-face meeting or telephone

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interview with the borrower is attempted before the lender takes any action to accelerate the maturity of the loan to discuss the reasons for lack of payment and to determine the necessary steps to bring the loan current.

8. Determine whether the notice of default and acceleration is in compliance with the regulations (24 CFR 201.50(b) and Title I Letter TI-408).
9. Determine whether there are sufficient controls to assure that all aspects of the claims for insurance benefits are prepared accurately and on a timely basis.
10. Determine whether the borrower's default is reported to a credit reporting agency following acceleration of the loan maturity.
11. Determine whether foreclosure or repossession proceedings are initiated and completed on a timely basis and in accordance with HUD requirements. Determine that valid and enforceable deficiency judgements are taken against the borrowers where required or appropriate to establish the validity of the obligation.

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