Office of Lender Activities & Program Compliance

Loan Review System (LRS): Implementation and Process Changes

January 26, 2017

Presented by:
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Jack Higgins, Loan Review System Project Manager
Agenda

• Loan Review System (LRS) Overview

• Business Process Changes
  — Test Cases
  — Lender Monitoring Reviews
  — Lender Self-Reporting

• Defect Taxonomy

• Upcoming Activities
Loan Review System (LRS) Overview
Loan Review System

The Federal Housing Administration (FHA) manages the risks to Single Family insurance programs through various quality control processes.

FHA is committed to balancing risk management while meeting the needs of its target population.

A unified loan review process improves FHA quality control, making it more consistent & transparent.
Loan Review System (cont.)

- Enables a unified loan review process in a single system
- Implements Defect Taxonomy
Loan Review System (cont.)

- Test Cases & Post-Endorsement Loan Reviews
  - eFindings Letter & Notifications
  - Underwriter Review System

- Lender Monitoring Reviews of Underwriting, Servicing & Operations
  - Email Notifications/Requests
  - Manual Processes
  - Neighborhood Watch

- Self-Reporting of Fraud/Misrepresentation & Other Material Findings

- Responding to Findings
  - Mail/eMail to HOC

- Reports & Summary Data
  - Multiple Source Systems

All functions in ONE Loan Review System (LRS)
Access & User Roles

• LRS accessed via FHA Connection

• Lender’s Application Coordinator grants user access

• Three possible roles:
  1. Read Only
  2. Response Submission
  3. Indemnification Submission
Lender Dashboard

**RESPONSE REQUESTS (20)**

<table>
<thead>
<tr>
<th>Case Number</th>
<th>Property Address</th>
<th>Selection Reason</th>
<th>Review Level</th>
<th>Request Date</th>
<th>Response Date</th>
<th>Last Action By</th>
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<tbody>
<tr>
<td>351-3576367</td>
<td>97 Gonzales St.</td>
<td>Lender Monitoring</td>
<td>Mitigation 2</td>
<td>07/21/2016</td>
<td>08/01/2016</td>
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<td>351-4988773</td>
<td>8825 SW. Applegate Dr.</td>
<td>OIG Audit</td>
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<td>07/24/2016</td>
<td>08/04/2016</td>
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<td>351-1768306</td>
<td>712 Glenholme Dr.</td>
<td>Lender Self Report</td>
<td>HOC Escalation</td>
<td>07/24/2016</td>
<td>08/04/2016</td>
<td>Harkey, Evita</td>
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<td>351-5195201</td>
<td>72 Lakeview Dr.</td>
<td>Random Monthly</td>
<td>Mitigation 2</td>
<td>07/24/2016</td>
<td>08/04/2016</td>
<td>Jonas, Lendor</td>
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<td>351-1264427</td>
<td>7278 Saxton Dr.</td>
<td>Conditional</td>
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<td>351-9442796</td>
<td>9854 NW. Arlington Rd.</td>
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<td>08/04/2016</td>
<td>Domenico, Marline</td>
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<td>351-0151464</td>
<td>691 Edgemont Dr.</td>
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<td>Mitigation 2</td>
<td>08/01/2016</td>
<td>08/19/2016</td>
<td>Stickle, Pamiko</td>
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<td>351-3237642</td>
<td>944 Johnson St.</td>
<td>FHA Manual</td>
<td>Mitigation 1</td>
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<td>08/10/2016</td>
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<td>351-6025667</td>
<td>386 Westport St.</td>
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<td>HQ Escalation</td>
<td>08/01/2016</td>
<td>08/20/2016</td>
<td>Crowder, Odis</td>
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</table>

**UNDER REVIEW BY FHA (103)**

<table>
<thead>
<tr>
<th>Case Number</th>
<th>Property Address</th>
<th>Selection Reason</th>
<th>Review Level</th>
<th>Request Date</th>
<th>Response Date</th>
<th>Last Action By</th>
</tr>
</thead>
<tbody>
<tr>
<td>347-1948267</td>
<td>9710 Brewery St.</td>
<td>Lender Monitoring</td>
<td>Mitigation 2</td>
<td>07/01/2016</td>
<td>07/11/2016</td>
<td>Hirsch, Sheryl</td>
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<tr>
<td>369-3197648</td>
<td>789 Creekside St.</td>
<td>FHA Manual</td>
<td>Mitigation 2</td>
<td>07/07/2016</td>
<td>07/19/2016</td>
<td>Magill, Lavia</td>
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<tr>
<td>355-6497135</td>
<td>86 Wall Ave.</td>
<td>Random</td>
<td>Mitigation 1</td>
<td>07/07/2016</td>
<td>07/19/2016</td>
<td>Pippin, Grace</td>
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<tr>
<td>346-6497220</td>
<td>7221 Valley Lane</td>
<td>Random</td>
<td>Mitigation 2</td>
<td>07/07/2016</td>
<td>07/19/2016</td>
<td>Neu, Flo</td>
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<tr>
<td>372-3480917</td>
<td>7990 Bedford Lane</td>
<td>Lender Monitoring</td>
<td>Mitigation 2</td>
<td>07/07/2016</td>
<td>07/16/2016</td>
<td>Kraushaar, Mahalia</td>
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<td>351-9457861</td>
<td>7729 Pearl Lane</td>
<td>FHA Manual</td>
<td>HOC Escalation</td>
<td>07/15/2016</td>
<td>08/01/2016</td>
<td>Gebhardt, Maudie</td>
</tr>
</tbody>
</table>
Responding to Findings

- Administrative Contact (registered in LEAP) notified by email when findings require a response
- All review details/history available in LRS
- Directly upload documentation and written responses
- May submit indemnification agreements electronically
Data & Reporting

• Reports available in LRS using MicroStrategy:
  – Loan Quality (material defect rates/details)
  – Request Processing/Timelines
  – Random Sample Outcomes

• Data from all review types in aggregate or in separate categories

• Download raw data to build your own reports
Business Process Changes
Test Cases

• Mortgagee Letter 2016-21

• New procedures for lenders approved on or after April 1, 2017

• Test cases will be reviewed post-closing

• Multiple opportunities to cure underwriting defects

• Acceptable rating results in Mortgage Insurance Certificate (MIC)

• Unacceptable Rating results in Notice of Return (NOR)
Lender Monitoring Reviews

• Email notification from LRS with list of selected loans

• On-site visit to focus on internal controls, operations, and QC Plan

• Most loans reviewed before the on-site visit

• Lender responses via LRS for operational and loan-level findings
Lender Self-Reporting

• Self-Report function replaces “Lender Reporting” in Neighborhood Watch

• Simplified data collection—from 36 to 6 critical data elements

• Report single or multiple loans with upload capability

• Automatically generates request for binder
Lender Self-Reporting (cont.)

1) Add Case(s) to Self-Report  2) Add Case Details: 2 Cases Selected

**DEFECT TYPE**
- [ ] Servicing
- [ ] Underwriting

**DEFECT AREAS**
- [ ] Borrower Income (BI)
- [ ] Borrower Credit (DC)
- [ ] Loan Amount (LA)
- [ ] Borrower Assets (BA)
- [ ] Property Eligibility (PE)

**FRAUD**
- [ ] Fraud has been detected for selected case(s)
  
  Types of Fraud
  
  - Appraisal Fraud, Credit, Employment, Equity Skimming

  Fraud Participants
  
  - Borrower, Appraiser

**FINDINGS AND CORRECTIVE ACTIONS**

Describe the Findings that led to this Self-Report:

This is a description. This is just placeholder text. Sample response to FHA from the lender about this finding/defect and an explanation. This is just placeholder text. Sample response to FHA from the lender.

Describe any Corrective Actions that have been taken:

- [ ] Loan Covered Under Settlement with HUD
Defect Taxonomy
Defect Taxonomy

FHA’s Single Family Housing Loan Quality Assessment Methodology
(Defect Taxonomy)
June 18, 2015
Defect Taxonomy

What is it?

- Method of identifying defects and their sources, causes, and severities
- Provides useful data and feedback through structured categorization of defects
- Balances risk management and business processes
Defect Taxonomy (cont.)

Defect Areas

1. Borrower Income (BI)
2. Borrower Credit (BC)
3. Loan to Value/Maximum Loan Amount (LM)
4. Borrower Assets (BA)
5. Property Eligibility (PE)
6. Property Appraisal (PA)
7. Borrower Eligibility (BE)
8. Mortgage Eligibility (ME)
9. Lender Operations (LO)
Defect Taxonomy (cont.)

- Each Defect Area has a set of possible sources and causes
- Sources are numbered 1, 2, 3...
- Causes are lettered A, B, C...
- Each finding in LRS will be coded by distinct Defect Area/Source/Cause
## Defect Taxonomy (cont.)  
**Sample – Property Eligibility (PE)**

<table>
<thead>
<tr>
<th>Sources</th>
<th>Causes</th>
</tr>
</thead>
<tbody>
<tr>
<td>MPR and General Acceptability Criteria</td>
<td>Determinations are not supported by documents provided</td>
</tr>
<tr>
<td>Property zoning does not meet policy</td>
<td></td>
</tr>
<tr>
<td>Property flood requirements not met</td>
<td></td>
</tr>
<tr>
<td>Manufactured home ineligible</td>
<td></td>
</tr>
<tr>
<td>New Construction ineligible</td>
<td></td>
</tr>
<tr>
<td>Property fails to adhere to flipping guidelines</td>
<td></td>
</tr>
<tr>
<td>Condo project not approved or withdrawn</td>
<td></td>
</tr>
<tr>
<td>Condo – loan level issues</td>
<td></td>
</tr>
<tr>
<td>Repairs not completed or repair escrow account not established</td>
<td></td>
</tr>
<tr>
<td>Required compliance inspections not completed</td>
<td></td>
</tr>
<tr>
<td>Property not acceptable</td>
<td></td>
</tr>
<tr>
<td>Non-MPR repair issues/escrow account not established</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td></td>
</tr>
</tbody>
</table>
Defect Taxonomy (cont.)

Severity Assessment

• Four possible severity tiers
• Severity is driven by the impact on insurability
• Measured by nature of the deviation from FHA’s requirements
• Finding notification will include the tier of each defect

Tier 1
Tier 2
Tier 3
Tier 4
Defect Taxonomy (cont.)

**Tier 1**
- Fraud/Misrepresentation
- Violations of statutory requirements
- Significant eligibility or insurability issues
- Inability to determine/support loan approval

**Tier 2**
- Material errors that impact loan approval
- Failure to comply with FHA policy
Defect Taxonomy (cont.)

**Tier 3**
- Minor errors or issues impacting approval
- Failure to comply with guidelines by small degree

**Tier 4**
- Errors that impact calculations or data integrity
- Loan would have been approvable despite errors
Upcoming Activities
Upcoming Activities

• Mortgagee Letter to confirm LRS go-live date
• Additional webinars before and after system implementation
• User documentation posted prior to go-live
• FHA INFO notices
References

• Mortgagee Letters 2016-21 (Test Cases) and 2017-03 (LRS Implementation)
  https://portal.hud.gov/hudportal/HUD?src=/program_offices/administration/hudclips/letters/mortgagee

• Defect Taxonomy

• Lender Insight
  http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/lender/SFH_Lender_Insight

• FHA INFO provides the lending industry updates on new Mortgagee Letters, Handbooks, and other notices, as well as a FHA Housing Industry Training. Lenders may subscribe to this e-mail distribution through the “subscribe to FHA INFO” link on the HUD Resources section of the main FHA lender web page at  www.hud.gov/lenders
The FHA Resource Center

• Origination through Endorsement FAQs on SF Handbook Information page:
  • Commonly asked questions/detailed answers.
  • Uploaded to the online Knowledge Base.

• [www.hudanswers.gov](http://www.hudanswers.gov): 1900+ Qs and As addressing 90 percent of our phone calls and announcements of policy changes and training opportunities.

• Email: answers@hud.gov
• Phone: (800) CALL-FHA or (800) 225-5342
• TTY: 1-800-877-8339
• Monday through Friday 8:00am – 8:00pm Eastern
Thank You!