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Issue #2 of Lender Insight / Training Opportunities

Issue #2 of *LENDER INSIGHT*

The Office of Lender Activities and Program Compliance (OLAPC) is excited to publish the second edition of our newsletter, *Lender Insight*. This issue contains updates to the Loan Review Findings Report for the quarter ending March 31, 2013, including details on lenders' mitigation efforts and changes to findings rankings. This issue also contains information on properly coding borrowers' source of funds, the upcoming consolidation of Title I and Title II ID numbers, tips on how to get ready for recertification early, and more.

The goal of *Lender Insight* is to offer insight to FHA lenders about what we see behind the scenes in lender approval, recertification, monitoring and compliance, and enforcement actions. Each issue contains core information designed to help our lenders better understand the trends we are seeing. The newsletter is distributed to readers via FHA's Single Family Housing Industry Email List. If you would like to receive the newsletter, but are not on the list, please visit http://bit.ly/FHARCPage to subscribe. **Issue #2 begins on the following page.**

Issue #2 is provided below:

In this issue >>>

Information from FHA's Office of Lender Activities and Program Compliance

Lender Insight

Issue No. 2
September 2013

What's Trending

Improper Data Entry for Loans with Gift Funds and/or Secondary Financing

Lenders are not always making sure that the source of borrowers' gift funds or secondary financing is properly entered in FHA Connection at loan endorsement.

These data inaccuracies may adversely impact FHA's Credit Watch Termination analysis. Prior to issuing a proposed Credit Watch Termination notice, the Office of Lender Activities analyzes a lender's portfolio to determine, among other things, if a lender's poor performance may be due to the type of loans originated or underwritten. For example, higher compare ratios may be explained by a lender's participation in bond programs (e.g., to serve first-time homebuyers).

Subsequent to issuing a proposed Credit Watch Termination notice, we independently validate information presented by the lender. If a lender fails to properly code a borrower's source of funds, we may be unable to verify what the lender asserts is negatively impacting its compare ratio.

Lenders must reflect the proper amount and source of the gift fund and/or secondary financing when completing the FHA Connection Insurance Application Screen at loan endorsement. Multiple entries are available. For secondary financing, the purpose must be entered. For certain sources the EIN and Name must also be reflected. Lenders can use the "Help Links" in FHA Connection to assist in understanding each data entry field on the Insurance Application Screen. The codes available on the Insurance Application Screen for source and purpose are listed to the right.

Gift Letter Source Field Options
N/A
Relative
Nonprofit/Religious/Community - Seller Funded
Nonprofit/Religious/Community - Non-Seller Funded
Government Assistance
Employer

Secondary Financing Source Field Options
N/A
Government & Nonprofit Instrumentality of Government
Nonprofit (not Instrumentality of Government)
Private Organizations / Eligible Individuals
Lender
Section 115 Entities

Secondary Financing Purpose Field Options
N/A
Borrower's Closing Costs
Required Minimum Cash Investment
Tax Abatement
Other

Updated Aug. 31, 2013

Refreshed Loan Review Findings

Mitigated Findings for Quarter ending March 31, 2013

FHA Lenders Mitigated Almost 50% of Unacceptable Loan Review Findings From March 31 Reporting Period

The initial loan review ratings for the quarter ending March 31, 2013 were shared in the June 2013 edition of *Lender Insight*. The updated report below reflects the revised results as of a data refresh on August 31, 2013. The updated report contains the following changes:

- A column reflecting an updated percentage of total findings by category based on lender mitigation and additional analysis;
- A column reflecting the percentage of initial unacceptable findings that were mitigated (%M);
- A column reflecting the percentage of findings that remain unacceptable as of August 31, 2013;
- A column reflecting the percentage change from an initial unacceptable rating through August 31, 2013; and
- An updated Top 5 Findings by Category list as a result of additional analysis and the data refresh. New findings are highlighted in light blue (e.g., Closing/Legal Document Deficiencies is shown in blue and now appears fourth on the Operational Deficiencies category listing).

On average, lenders mitigated approximately 49% of the findings initially rated as unacceptable. Lenders are typically able to mitigate unacceptable findings by providing documents that were missing or incomplete in the original endorsement binder, and/or providing additional documentation to support approval and endorsement of a loan in accordance with FHA requirements. Lenders should use the results of loan reviews to enhance their binder documentation process to ensure a complete binder is submitted to FHA.

The mitigation efforts since the June 2013 issue reduced the loans considered unacceptable by 77%; from 2,712 to 574 loans. Of the 574 loans with a rating of unacceptable, lenders executed indemnifications on 133 loans. The remaining 441 loans are under review by FHA staff or by lenders. FHA-approved lenders are reminded that a refusal to execute an indemnification agreement on a loan with unacceptable violations that cannot be cured will result in a referral to HUD's Mortgagee Review Board for administrative action.

Finding Category	% of Total	% Initial U	% M	% U as of	% Change
Program Eligibility	12%	77%	54%	21%	-73%
Credit/Underwriting	20%	79%	54%	24%	-69%
Collateral/Asset Valuation	7%	63%	45%	17%	-73%
Operational Deficiencies	7%	71%	48%	21%	-70%
File Documentation	54%	61%	45%	14%	-76%
Totals	100%				

Total Loans Reviewed:	6,251
Conforming:	19%
Deficient:	38%
Initial Unacceptable (U):	44%
Mitigated (M):	34%
Unacceptable (U) as of 8/31/13:	9%

Top 5 Findings Ranked by Category

Program Eligibility	% of Total	% Initial U	% M	% U as of 8/31/13	% Change
1. Purchase contract, Real Estate Certificate and/or amendatory clause missing, illegible or incorrect.	29%	64%	46%	15%	-76%
2. Mortgage amount incorrect, loan-to-value limit and/or statutory limit exceeded.	15%	96%	67%	28%	-71%
3. Issues related to National Mortgage Licensing System registration requirements.	13%	61%	47%	13%	-80%
4. Streamline refinance eligibility criteria not met.	11%	79%	62%	13%	-84%
5. Newly constructed home does not meet requirements.	6%	88%	64%	21%	-76%
6. All other	27%	85%	53%	30%	-64%
	100%				

Updated Aug. 31, 2013

Top 5 Findings Ranked by Category (Continued)

Credit and Underwriting	% of Total	% Initial U	% M	% U as of 8/31/13	% Change
1. Unacceptable, unsupported or insufficient source of funds.	22%	81%	53%	27%	-67%
2. Income improperly documented.	15%	76%	54%	21%	-73%
3. Obligations of borrower(s) (non-purchasing spouses included) omitted, inaccurate, not supported, not disclosed, and/or illegible.	14%	80%	54%	25%	-69%
4. Concerns related to assets derived from gift(s).	10%	81%	57%	24%	-71%
5. Income improperly calculated or from unacceptable source.	10%	77%	48%	28%	-63%
6. All other	29%	79%	54%	23%	-71%
	100%				

Collateral/Asset Valuation	% of Total	% Initial U	% M	% U as of 8/31/13	% Change
1. Concerns related to the Neighborhood, Site, and/or Improvements section of the appraisal report.	43%	60%	43%	15%	-75%
2. Concerns related to Sales Comparison Approach section of the appraisal report.	40%	58%	39%	19%	-68%
3. Repairs not acceptably addressed.	8%	86%	71%	14%	-84%
4. Property does not meet Minimum Property Requirements or Standards.	4%	96%	65%	31%	-68%
5. Concerns related to the Cost Approach of the appraisal report.	3%	63%	53%	9%	-86%
6. All other	3%	84%	65%	20%	-76%
	100%				

Operational Deficiencies	% of Total	% Initial U	% M	% U as of 8/31/13	% Change
1. Data integrity deficiencies: File documentation does not support Accept/Approve decision in AUS.	48%	69%	46%	22%	-69%
2. Unallowable, excessive costs/credits to borrower or other HUD-1 and/or Good Faith Estimate inaccuracies.	27%	78%	55%	21%	-73%
3. Lender Insured data integrity concerns: Insured loan data entered in FHA Connection is not supported by file documents.	18%	60%	38%	20%	-67%
4. Closing/Legal document deficiencies.	2%	94%	63%	11%	-88%
5. Sales contract dated less than 91 days from acquisition date by seller.	2%	74%	50%	42%	-43%
6. All other	2%	84%	55%	24%	-71%
	100%				

File Documentation	% of Total	% Initial U	% M	% U as of 8/31/13	% Change
1. Form HUD-92900-A not properly completed or missing.	24%	51%	37%	12%	-76%
2. Uniform Residential Loan Application not properly completed or missing.	16%	49%	37%	10%	-79%
3. Form HUD-92800.5B substantially incomplete, incorrect or missing.	12%	57%	41%	15%	-74%
4. HUD-1, HUD-1 Addendum if applicable, and/or Good Faith Estimate either missing, not the final copy, not complete or illegible.	7%	58%	41%	15%	-74%
5. HUD-92900-LT FHA Loan Underwriting and Transmittal Summary is missing, illegible or incorrect.	7%	60%	44%	14%	-77%
6. All other	34%	76%	58%	17%	-77%
	100%				

Business Transformation >>>

Title I & Title II Consolidation Process

As part of the FHA Transformation Initiative, we continue to implement a counterparty risk framework that enables a better and timelier means of identifying, mitigating, and managing risk in the Approval, Recertification, Monitoring, Enforcement, and Post-Endorsement Technical Review processes.

To support the effort, we will be consolidating the FHA Lender ID numbers for lenders that participate in both FHA Title I and Title II Programs, provided the lenders have the same Tax ID number. Instead of separate IDs, we will be instituting Title I and Title II "authorities." Authorities will denote the type of FHA loans (Title I or Title II) lenders are approved to originate, underwrite, and/or service.

Consolidation will improve counterparty risk management and deliver reporting and operational oversight efficiencies. The consolidation will streamline the recertification process; lenders will have to submit only one set of financial statements and will now pay a single recertification fee.

The consolidation process will be similar to a merger and will occur automatically. For lenders currently approved for both FHA Title I and Title II Programs, the current FHA Title II ID will remain as the active ID, while the Title I ID will be changed to merged status. The surviving ID will automatically inherit both authorities (Title I and Title II) previously held. All active loans and reserves will be transferred to the surviving ID.

Instructions regarding the effect on corporate officers, home, and branch offices will be forthcoming. For now, lenders should review and update all administrative information in FHA Connection (address, phone number, email, etc.), as well as the list of designated corporate officers, branches, branch managers, and regional managers.

Going forward, we will be disseminating detailed communications about this process to ensure that all lenders are informed of the upcoming changes and the potential impact of these changes. We are targeting consolidation for the first quarter of calendar year 2014. Please stay tuned.

Enforcement Actions >>>

During the period from April through June 2013, cases heard by the Mortgagee Review Board (MRB) involved infractions consisting of the following types of fact-based violations:

- Failure to implement and maintain a Quality Control Plan
- Failure to review early payment default loans
- Source of funds issues regarding the borrower's down payment (e.g., improperly documented gift letters, insufficient funds to close, use of unacceptable source of funds, and improperly documented source of funds)
- Questionable income, assets, and liabilities of the borrower (e.g., failure to document discrepancies between the credit report and the credit application)
- Excessive mortgage payment-to-income ratios and debt-to-income ratios

Total Civil Money Penalties (CMPs):	$1,996,500
Lenders Sanctioned:	30
Settlement Agreements:	15
Lenders Who Entered Indemnification Agreements:	7
Loans Covered by Indemnification Agreements:	166
Lenders Withdrawn:	11

**Statistics cover the period October 1, 2012 through June 30, 2013 and refer to actions taken by the Mortgagee Review Board only*

Process Transformation >>>

Office of Single Family Housing Works to Deliver Consistency

To ensure consistent application of the policies and procedures used by FHA to review loan files, the Office of Lender Activities has established an Escalation Review Committee.

Members are the senior managers from both the Processing & Underwriting and Quality Assurance Divisions in the four Homeownership Centers, as well as senior managers in the Headquarters Offices of Program Development and Lender Activities.

The monthly Escalation Review Committee meetings provide a forum to discuss and achieve consensus on the handling of specific loan-level issues and ensure standardized application of FHA policies in the loan review process.

Quarterly Loan Review Findings

FHA's Quarterly Loan Review Summary for Quarter ending June 30, 2013

Introduction >>>

The FHA Quarterly Loan Review Findings include all Single Family Post-Endorsement Technical Loan Reviews (PETRs) conducted by FHA between April 1, 2013 and June 30, 2013. **This report reflects the initial rating of each file reviewed during the quarter**. A loan rated unacceptable may change if the lender provides mitigating documentation to FHA. Even if a rating is subsequently mitigated, an initial rating of unacceptable indicates the loan endorsement file exhibited a material defect at the time of endorsement. The loans reviewed are selected by a risk targeting methodology and are not representative of the overall FHA portfolio. For additional details on the Report, please see our June 2013 edition of *Lender Insight*.

Loan Sample Characteristics >>>

Total Loans Reviewed:	5,311	Purchase:	68%
Conforming:	18%	Rate & Term Refinance:	5%
Deficient:	37%	Streamline Refinance:	27%
Initial Unacceptable:	46%	HECM:	0%
		EPDs:	40%

Finding Category	% of Total	% Unacceptable (U)
Program Eligibility	11%	75%
Credit/Underwriting	21%	79%
Collateral/Asset Valuation	7%	65%
Operational Deficiencies	7%	74%
File Documentation	53%	63%
Totals	100%	

Top 5 Findings Ranked by Category

Program Eligibility	% of Total	% U
1. Purchase contract, Real Estate Certificate and/or amendatory clause missing, illegible or incorrect.	28%	59%
2. Mortgage amount incorrect, loan-to-value limit and/or statutory limit exceeded.	13%	97%
3. Issues related to National Mortgage Licensing System registration requirements.	13%	61%
4. Streamline refinance eligibility criteria not met.	12%	82%
5. Newly constructed home does not meet requirements.	6%	89%
6. All other	28%	81%
	100%	

Collateral/Asset Valuation	% of Total	% U
1. Concerns related to Sales Comparison Approach section of the appraisal report.	44%	59%
2. Concerns related to the Neighborhood, Site, and/or Improvements section of the appraisal report.	40%	63%
3. Repairs not acceptably addressed.	8%	91%
4. Property does not meet Minimum Property Requirements or Standards.	5%	92%
5. Appraisal is missing or expired.	2%	78%
6. All other	2%	64%
	100%	

Operational Deficiencies	% of Total	% U
1. Data integrity deficiencies: File documentation does not support Accept/Approve decision in AUS.	49%	69%
2. Unallowable, excessive costs/credits to borrower or other HUD-1 and/or Good Faith Estimate inaccuracies.	28%	86%
3. Lender Insured data integrity concerns: Insured loan data entered in FHA connection is not supported by file documents.	19%	65%
4. Sales contract dated less than 91 days from acquisition date by seller.	1%	100%
5. Requirements for properties sold within 91-180 days not documented	1%	91%
6. All other	1%	91%
	100%	

File Documentation	% of Total	% U
1. Form HUD-92900-A not properly completed or missing.	23%	54%
2. Uniform Residential Loan Application not properly completed or missing.	16%	50%
3. Form HUD-92800.5B substantially incomplete, incorrect or missing.	11%	60%
4. HUD-92900-LT FHA Loan Underwriting and Transmittal Summary is missing, illegible or incorrect.	9%	57%
5. HUD-1, HUD-1 Addendum if applicable, and/or Good Faith Estimate either missing, not the final	7%	62%
6. All other	35%	78%
	100%	

Top 5 Findings Ranked by Category (Continued)		
FOCUS Credit and Underwriting	% of Total	% U
1. Unacceptable, unsupported, or insufficient source of funds.	19%	82%
2. CAIVRS, LDP/GSA authorization, and/or delinquent federal debt issues not properly documented or satisfied.	14%	59%
3. Income improperly documented.	14%	78%
4. Concerns related to assets derived from gift(s).	12%	80%
5. Obligations of borrower(s) (non-purchasing spouses included) omitted, inaccurate, not supported, not disclosed, and/or illegible.	11%	85%
6. All other	29%	86%
	100%	

REMINDER: Restrictive Covenants are prohibited on FHA loans

FHA insurance requirements at 24 CFR § 203.41 state that a mortgage shall not be eligible for insurance if the mortgaged property is subject to legal restrictions on conveyance. FHA regulations permit exceptions for eligible government and non-profit programs.

Any legal restrictions that prevent free assumability or that restrict conveyance of an FHA-insured property are prohibited.

Restrictive covenants most often noted are those associated with builder affiliated mortgage lenders and new home production; this is an unacceptable practice. FHA lenders may not allow sellers to place restrictions on conveyance subject to the consent of a third party

Lenders that allow restrictive covenants in violation of FHA eligibility requirements will be subject to administrative action by the Mortgagee Review Board.

Focus: CREDIT & UNDERWRITING >>>

Included below are common examples of credit and underwriting issues that may lead to unacceptable ratings. This list is not exhaustive and is meant as an informal resource only.

1. *Unacceptable, unsupported, or insufficient source of funds.*

- Unacceptable if the earnest money deposit, closing costs, fees, or reserve requirements imposed by the AUS or HUD requirements are not fully satisfied and the file indicates the borrower is unlikely to acquire the amount needed between verification of funds and closing. Also unacceptable if there are sufficient funds to close, but the source of the funds is unsupported or from a prohibited source and the borrower is unlikely to acquire the amount needed between verification of funds document date(s) and closing.

2. *CAIVRS, LDP/GSA authorization, and/or delinquent federal debt issues not properly documented or satisfied.*

- Unacceptable if the HUD-92900-LT reflects a CAIVRS hit that cannot be mitigated based on documentation in the file, or if the lender failed to check CAIVRS or LDP/GSA. There must be a reference code, as well as documentation provided in the file to demonstrate a CAIVRS check was completed. Remember that if the borrower, seller, listing or selling real estate agent or loan officer is found on HUD's LDP or the GSA list and an exception does not apply, the mortgage loan is not eligible for FHA mortgage insurance. Additionally, a finding in this category is considered unacceptable if federal debt is reflected and there is no evidence the debt has been satisfied or that there is an acceptable approved payment plan in place.

3. *Income improperly documented.*

- Unacceptable if required income documentation is either missing, incomplete, or illegible to the point the reviewer is unable to substantiate the minimum income necessary to support the approval of the loan.

4. *Concerns related to assets derived from gift(s).*

- Unacceptable if the file is missing significant documentation related to the gift, such that the reviewer cannot determine the funds were from an acceptable gift source or that it was received by the borrower. Many times, the gift letter is missing from the file. Unacceptable if the relationship between the donor and the borrower does not meet HUD requirements or the charitable organization or governmental agency does not meet HUD requirements for a gift donor. The gift letter must reflect the relationship between the donor and the borrower. Unacceptable if withdrawal documentation (e.g., withdrawal document, bank statement, cancelled check, wire transfer) from donor's account is missing. Unacceptable if documentation in the file leads to information that indicates the gift documentation is a loan from the gift donor.

5. *Obligations of borrower(s) (non-purchasing spouses included) omitted, inaccurate, not supported, not disclosed, and/or illegible.*

- Unacceptable if full disclosure of the borrower's obligations impacts the debt ratios or credit history to the point where the loan would not have been approved. Unacceptable if material recurring obligations (e.g., alimony/child support payments, real estate loans, revolving accounts) of the borrower were omitted without adequate supporting documentation, or if contingent liabilities were omitted without documentation that other parties bear sole and legal responsibility for the debt. Unacceptable if debts projected to last 10 months or less were omitted even though they will significantly affect the borrower's ability to pay the mortgage during the immediate months after loan closing, and the borrower does not have cash reserves after closing to meet the projected debts; or if obligations projected to require payments within the next 12 months were omitted without adequate supporting documentation (e.g., student loans subject to repayment within 12 months of closing).

Lender Recertification >>>

Anticipating Fiscal Year End: 5 Steps to Help Get Ready for Recertification Early

It may only be September, but before we know it many lenders will be preparing for the end of their fiscal year. This year, help prepare for recertification season early by following these quick tips and reminders:

1. **Update Your Administrative Information in FHA Connection**

Ensure that your contact information on file with FHA is up to date. This includes your business address, phone number, and email addresses. Also make sure to update your branch information. These changes can be made in FHA Connection. Updates to information on corporate officers must submitted to the Lender Approval Division.

2. **Keep the New Net Worth Requirements in Mind**

The final phase of FHA's revised net worth requirements went into effect on May 20, 2013. At that time, we notified lenders who were below or just slightly above the new threshold. Lenders who do not meet the revised requirements are subject to administrative action by the Mortgagee Review Board. If you do not meet the new requirements, or if you received a letter and have not yet responded with the appropriate documentation, please contact FHA immediately. For more information on the net worth requirements, please see Mortgagee Letter 2010-20.

3. **Make Sure a Corporate Officer Completes the Certification**

Only a designated corporate officer may complete the Certification. The corporate officer completing the certification must have the authority to legally bind the institution and must be registered as a corporate officer with FHA. FHA limits the number of officers that may complete the electronic annual certification to three.

4. **Remember to Report Business Changes within 10 Days**

All business changes must be reported to FHA within 10 business days. For more information on what qualifies as a business change, please see Mortgagee Letters 2011-34 and 2009-31. Remember that any sanctions, exclusions, fines, or penalties must be reported to FHA. This includes all settlement agreements and consent orders entered into with state or federal regulators.

5. **If You Believe You Will be Unable to Certify, Take Action**

Start your certification ahead of time. Give yourself plenty of time to navigate through any unforeseen issues. If you think you will be unable to certify based on events that took place during the fiscal year, you will click the "unable to certify" button. This will prompt you to submit an explanation and supporting documentation which will then be reviewed by the Office of Lender Activities. You will subsequently be informed as to whether you will be able to proceed with recertification. This process can take anywhere from a few days to a few weeks, depending on volume. To speed the process, please respond to all follow up requests for additional information and documentation as quickly as possible. Also, make sure to add UnableToCertify@hud.gov to your email list of trusted contacts. For more information on the unable to certify process, please see Mortgagee Letters 2010-38 and 2009-31.

Coming soon >>>

In the Next Issue...

Focus: Program Eligibility Findings

More Information on LEAP 3.0 and our Upcoming Electronic Recertification Procedures

...and more updates on OLAPC initiatives and policy changes. Stay tuned!

The FHA Resource Center is here to help! Contact us at:

Phone: **1-800-CALL-FHA (225-5342)**

TTY: **1-800-877-8339**

Email: **answers@hud.gov**

For more information, please visit our FHA Lender page at **www.hud.gov/lenders** and our online FAQ site at **www.hud.gov/answers**

Your Door to FHA HOMEOWNERSHIP

Training Opportunities

Course Title: FHA Loss Mitigation Training in Ft. Lauderdale, FL ***ON-SITE TRAINING***
Date/Time: Wednesday, September 25 from 8:30 am to 4:00 pm (Eastern Time)
Location: Hyatt Place – Ft. Lauderdale Airport and Cruise Port, 91 SW 18th Avenue, Dania Beach, FL 33004

Registration Link: http://www.hud.gov/emarc/index.cfm?fuseaction=emar.registerEvent&eventId=1883&update=N

Description: This is a chance for classroom training provided by HUD. The intended audience for this training is HUD-Approved Counseling Agencies, Servicing Lenders and Nonprofits. We will discuss the changes of the retention waterfall, Pre-foreclosure and Deed-In-Lieu. Please bring a calculator to class.

Special Instructions: The Hyatt hotel has offered special room rates of $85 plus tax. You must call the hotel (954) 922-0436, ask for the sales department, and mention the HUD meeting sleep rooms. You must complete the HUD Registration form to attend the training. Training is free and lunch is on your own. If you have any questions please email Virginia.vich@hud.gov.

Course Title: 203(K), 203(H) & EEM TRAINING
Date/Time: Friday, September 27, 2013, 1:00 pm-3:30 pm Central
Location: HUD, 500 Poydras Street, Basement Level Meeting Room, New Orleans, LA 70130

Registration Link: http://www.hud.gov/emarc/index.cfm?fuseaction=emar.registerEvent&eventId=1882&update=N

Description: This FREE half-day classroom training by FHA representatives from the Denver Homeownership Center will cover the 203K Program (for rehabilitation and repair), 203H loan (Disaster Victims Program), and the Energy Efficient Mortgage (EEM) program. In addition, the HUD staff will allow time for questions and answers. This training is intended for new mortgage lending professionals, or, a refresher course for seasoned professionals. Real estate sales professionals and loan originators are encouraged to attend.

Special Instructions: Class size is limited; first-come, first-served. On the day of the class, check-in begins at 12:30 pm. Class begins promptly at 1:00 pm Central. Registration is required.