



**Cornerstone Home Lending
Houston, TX**

**Single-Family Housing Mortgage Insurance
Program**



Issue Date: September 26, 2014

Audit Report Number: 2014-FW-1006

TO: Kathleen Zadareky,
Deputy Assistant Secretary for Single Family Housing, HU

Craig Clemmensen, Director, Departmental Enforcement Center, CACB

//signed//
FROM: Gerald R. Kirkland
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SUBJECT: Cornerstone Home Lending, Houston, TX, Did Not Adequately Underwrite 16
Loans, Violated the Real Estate Settlement Procedures Act, and Did Not
Implement an Adequate Quality Control Plan During Our Review Period

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Cornerstone Home Lending.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 817-978-9309.



September 26, 2014

Cornerstone Home Lending, Houston TX, Did Not Adequately Underwrite 16 Loans, Violated the Real Estate Settlement Procedures Act, and Did Not Implement an Adequate Quality Control Plan During Our Review Period

Highlights

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What We Audited and Why

We audited Cornerstone Home Lending, formerly known as Cornerstone Mortgage Company. We selected Cornerstone based upon a high default rate at Cornerstone's Branch 87 in 2007 through 2009. Our audit objectives were to determine whether Cornerstone (1) complied with HUD and Federal Housing Administration (FHA) regulations when originating and underwriting FHA-insured mortgages and (2) implemented a quality control plan that met requirements.

What We Recommend

We recommend that the U.S. Department of Housing and Urban Development (HUD) require Cornerstone to (1) reimburse HUD for 13 loans for which HUD has sold the properties and incurred losses totaling \$981,574 and (2) indemnify HUD for 3 actively insured loans which would cause additional losses of \$153,856 if they are foreclosed upon and resold. We also recommend that HUD pursue administrative actions against the owners and management of Cornerstone for the violations cited in the report.

What We Found

During the review period, Cornerstone (1) did not comply with HUD and FHA requirements when underwriting 16 of 34 loans, (2) violated RESPA when it paid marketing fees in exchange for the referral of FHA mortgage business, and (3) failed to properly implement a quality control plan. As a result, HUD paid claims for 13 of the loans, incurring losses of more than \$981,000 upon sale of the properties. Further, Cornerstone placed the FHA insurance fund at an increased risk of loss of almost \$154,000 if the three remaining loans are foreclosed upon and the properties are sold. In addition, Cornerstone could not ensure that its customers were able to shop for other lenders with better mortgage rates or that referral fees did not unnecessarily increase the costs of mortgage services. Lastly, Cornerstone was unable to ensure the accuracy, validity, and completeness of its loan origination operations, resulting in an increased risk to the FHA insurance fund. The findings in this report reflect Cornerstone's performance during 2007 through 2009, and may not reflect current performance.

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BACKGROUND AND OBJECTIVES

Cornerstone Home Lending's chairman and chief executive officer founded Cornerstone in 1988. It received Federal Housing Administration (FHA) approval on March 31, 1988, as a nonsupervised direct endorsement lender. Headquartered at 1177 West Loop South, Suite 200, Houston, TX, Cornerstone was a full-service mortgage banker and FHA-approved lender with 99 branch offices in 18 States¹ at the time of the audit. Cornerstone had 900 employees, and its loan officers could make loans in 44 States and the District of Columbia. According to Cornerstone, it closed 33 of its branch offices, and had 70 branch offices registered with HUD/FHA as of March 31, 2014.

Cornerstone acts as principal (processes, underwrites, or submits insurance endorsements) for nine authorized agents. In addition, it is the authorized agent for one principal. During fiscal year 2007, Cornerstone originated 1,104 FHA loans totaling \$129 million. In fiscal years 2008 and 2009, it originated 3,398 FHA loans totaling \$481 million and 6,255 FHA loans totaling \$936 million, respectively. In 2009, it had more than \$2.5 billion in home purchase and refinance loans.

Cornerstone Branch 87, located at 14515 Briarhills Parkway, Suite 202, Houston, TX,² was approved by FHA on April 28, 2004. Branch 87 originated 831 FHA loans totaling \$86.5 million from October 1, 2007, through September 30, 2009. During this same period, 92 of the loans (11.07 percent) were at least 90 days delinquent. The national average default rate was 4.94 percent, and the rate for the State of Texas was 4.88 percent. According to HUD's Neighborhood Watch Early Warning System,³ Branch 87's default rates continued to be higher than the National and State rates for 2010 and 2011. Cornerstone terminated Branch 87 in March 2012.

FHA's mortgage insurance programs help low- and moderate-income families become homeowners by lowering some of the costs of their mortgage loans. FHA mortgage insurance also encourages lenders to approve mortgages for otherwise creditworthy borrowers and projects that might not be able to meet conventional underwriting requirements by protecting the lender against default. The direct endorsement program simplifies the process for obtaining FHA mortgage insurance by allowing lenders to underwrite and close the mortgage loan without prior U.S. Department of Housing and Urban Development (HUD) review or approval. Lenders are responsible for complying with all applicable HUD regulations and are required to evaluate the borrower's ability and willingness to repay the mortgage debt. Lenders are protected against default by FHA's Mutual Mortgage Insurance Fund, which is sustained by borrower premiums.

As an FHA-approved lender, Cornerstone is required to follow 12 U.S.C. (United States Code) Chapter 27, Sections 2601-2617, and 24 CFR (Code of Federal Regulations) Part 3500, more

¹ Alabama, Arizona, California, Colorado, Florida, Georgia, Kansas, Minnesota, Mississippi, Missouri, Nevada, New Mexico, Oklahoma, Tennessee, Texas, Utah, Virginia, and Washington.

² Before its termination in March 2012, Branch 87 had relocated to 389 Cedar Street South, Matagorda, TX.

³ Neighborhood Watch refers to a Web-based software application that displays loan performance data for lenders and appraisers using FHA-insured single-family loan information. The system is designed to highlight exceptions so that potential problems are readily identifiable.

commonly known as the Real Estate Settlement Procedures Act (RESPA). RESPA applies to transactions involving a federally related mortgage loan. RESPA is a consumer protection statute initially passed in 1974. Its purposes are to help consumers become better shoppers for real estate settlement services and to eliminate kickbacks and referral fees that unnecessarily increase the costs of certain settlement services.⁴

Our audit objectives were to determine whether Cornerstone (1) complied with HUD and FHA regulations when originating and underwriting FHA-insured mortgages and (2) implemented a quality control plan that met requirements.

⁴ HUD's Office of RESPA and Interstate Land Sales was responsible for enforcing RESPA during the audit period. The Dodd-Frank Act transferred responsibility for enforcing RESPA to the Bureau of Consumer Financial Protection in 2010.

RESULTS OF AUDIT

Finding 1: Cornerstone Did Not Comply With HUD and FHA Requirements in Underwriting 16 FHA Loans

During 2007 through 2009, Cornerstone did not comply with HUD and FHA requirements when underwriting 16 of 34 (47 percent) FHA-insured loans reviewed (see case narratives in appendix C).⁵ Specifically, underwriters (1) violated restrictions on resales occurring 90 days or less after acquisition, (2) failed to review appraisal reports to ensure that properties' values were reasonable, and (3) did not adequately verify borrower assets or income. This noncompliance occurred because the underwriters failed to exercise due diligence in underwriting the loans. As a result, HUD paid claims for 13 of the 16 loans and incurred losses of more than \$981,000 upon sale of the properties (see appendix D). Further, Cornerstone placed the FHA insurance fund at an increased risk for three ineligible loans with unpaid principal balances of more than \$295,000 and estimated losses of almost \$154,000 if the loans are foreclosed upon and the properties are sold (see appendix E).

**Cornerstone Violated
Restrictions on Resales
Occurring Within 90 Days of
Seller Acquisition**

HUD prohibited originating FHA mortgages for homes resold within 90 days after seller acquisition, commonly referred to as “flipping” properties.⁶ However, Cornerstone’s underwriters ignored HUD regulations when they approved eight FHA loans for properties that had been flipped.⁷ The underwriters approved the eight loans, although the homes sold between 18 and 75 days, with an average of 53 days, following the seller’s acquisition (see table 1). As a result, FHA insured eight loans totaling \$754,402 that were not eligible for insurance and paid \$624,949 in claims on seven of them, including a partial claim for \$4,771.

⁵ All of the loans were originated by Branch 87.

⁶ HUD Handbook 4155.2, paragraph 4-7(e), Restrictions on Re-Sales Occurring 90 Days or Less After Acquisition. FHA defines the seller’s date of acquisition as the date of settlement on the seller’s purchase of that property, while the resale date is the date of execution of the sales contract by a buyer intending to finance the property with an FHA-insured loan.

⁷ HUD implemented the 90-day flipping rule to prevent FHA home purchasers from becoming victims of predatory flipping activity. Federal Register, May 1, 2003 (Volume 68, Number 84). HUD’s Assistant Secretary for Housing-Federal Housing Commissioner waived the anti-flipping rule, effective February 1, 2010, which was after our audit period. Thus, the waiver was not applicable to the loans in our sample.

Table 1: Properties ineligible for FHA insurance due to property flipping

Case number (493-)	Mortgage amount	Prior sale date per file	Contract execution date per file	Difference (days)	Effective date per contract	Price increase since seller acquisition	Percent increase
8959876	\$ 84,550	11/18/2008	01/20/2009	63	2/20/2009	\$32,410	60
8547028	80,612	12/20/2007	02/04/2008	46	3/27/2008	56,250	225
8693472	119,058	03/18/2008	05/25/2008	68	7/25/2008	59,999	100
8753582	79,373	05/21/2008	07/22/2008	62	8/22/2008	45,000	129
9141680	86,317	01/16/2008	02/12/2008	27	4/17/2008	50,000	138
8724586	88,301	05/09/2008	07/10/2008	62	No date	51,000	134
8721328	107,153	04/16/2008	06/30/2008	75	7/25/2008	43,254	67
8544391	109,038	01/04/2008	01/22/2008	18	No date	45,600	71
Total	\$754,402		Average days	53		Average increase	116

Cornerstone’s underwriters avoided the 90-day flipping rule by relying on the “effective date” in the purchase contract instead of determining the resell date by evaluating the loan documents. The “effective date” on the purchase contracts is supposed to be the date on which the contract becomes effective (all of the parties show their intent to be bound by the contract). In reality, the “effective date” on the flipped property contracts was an artificial date that would mislead HUD and FHA into believing that more than 90 days had passed between the seller’s date of acquisition and the resell. Cornerstone’s underwriters used the “effective date” to make the loans appear to be eligible and not violate the ant flipping rule. In some files, the “effective date” was meaningless. For example, in one unrelated loan file, the “effective date” was after the closing date, while in two flipped loan files above, the “effective date” was blank.

Evidence in the eight loan files showed that all of the contract terms had been agreed upon and the parties intended to be bound by the contract within less than 90 days after the sellers obtained the properties. Evidence included dates and signatures on contract addenda, loan applications, loan processing, earnest money deposits, appraisals, title insurance, and verifications of employment and deposit completed before the “effective date” of the contract and within 90 days following the seller’s acquisition.

Cornerstone Failed To Review Appraisal Reports

Cornerstone’s underwriters violated HUD requirements and Cornerstone’s quality control plan when they underwrote nine loans totaling \$866,705 without reviewing the appraisal reports (see table 2). HUD required the underwriters to review the appraisal reports,⁸ and Cornerstone’s quality control plan required

⁸ HUD Handbook 4155.2, paragraph 4-1(e)

them to verify the existence of the property appraisals.⁹ However, appraisal reports in nine loan files were dated after the loans closed. Therefore, the underwriters could not have reviewed the appraisal reports as required. Without acceptable appraisals, Cornerstone could not ensure that the loans met loan-to-value requirements.

In their direct endorsements,¹⁰ the underwriters certified to HUD that they had personally reviewed appraisal reports, credit reports, and all associated documentation in underwriting FHA-insured mortgages. However, the certifications were erroneous because the reports were dated an average of 16 days after loan closing and two reports were issued more than 30 days after closing.

Table 2: Loans originated without an appraisal report

Case number	Mortgage amount	Closing date	Appraisal report date	Difference (days)
493-8447975	\$ 81,357	10/30/2007	11/14/2007	15
493-8567176	109,137	07/08/2008	08/11/2008	34
493-8692510	71,931	07/28/2008	08/06/2008	9
493-8693472	119,058	07/31/2008	08/07/2008	7
491-9483914	80,416	05/01/2009	05/25/2009	24
493-8753582	79,373	08/25/2008	08/28/2008	3
493-8925706	94,261	03/06/2009	03/12/2009	6
493-8480034	142,871	12/21/2007	02/04/2008	45
493-8724586	88,301	08/16/2008	08/20/2008	4
Total	\$ 866,705		Average	16

Cornerstone Did Not Adequately Review Appraisal Reports

Cornerstone’s underwriters did not adequately review six appraisal reports to ensure that appraised values were reasonable. Its appraisers did not comply with HUD’s appraisal requirements,¹¹ and its underwriters did not verify the accuracy and compliance of the property appraisals as required in its quality control plan.¹²

⁹ Cornerstone Mortgage Company Quality Control Program for Single Family Originations, page 2

¹⁰ Direct Endorsement Approval for a HUD/FHA-Insured Mortgage (form HUD-92900-A).

¹¹ HUD Handbook 4150.2, Appendix D, Valuation Protocol, provides specific instructions that the appraiser must follow to establish the value of the property for mortgage insurance purposes.

¹² Cornerstone Mortgage Company Quality Control Program for Single Family Originations, page 2

As a result, HUD over insured six properties with original mortgage amounts totaling \$589,984 (see table 3).

Table 3: Loans originated without adequate appraisal review

Case number	Inadequate appraisal	Overstated values	Mortgage amount
493-8547028	Yes	Yes	\$ 80,612
493-8692510	Yes	Yes	71,931
493-8693472	Yes	Yes	119,058
493-8532052	Yes	Yes	96,239
493-8558066	Yes	Yes	79,273
493-8480034	Yes	Yes	142,871
Total			\$589,984

Cornerstone’s appraisal reports contained a number of omissions, errors, and contradictory statements, which its underwriters failed to detect. Specifically, the appraisers

- Inflated gross living areas, which caused the value of the subject properties to be increased, and
- Used comparable properties that were not truly comparable to the subject properties because they
 - Used only higher value properties for comparison,
 - Failed to make adjustments for dissimilarities (such as seller concessions, size, garage, age, etc.), and
 - Failed to properly disclose the physical condition of the subject properties and make appropriate adjustments.

As a result of the erroneous appraisals, subject properties were valued above the neighborhood’s predominant value. In one example, the predominant value was \$50,000, but Cornerstone’s appraiser valued the subject property at \$80,000. In a second example, the appraiser valued the subject property at \$148,000 when an unused comparable with equal location and condition sold for \$75,000.

Verifications of Assets and Income Were Inadequate

Cornerstone’s underwriters approved four FHA-insured mortgages totaling \$417,915 without adequately verifying or calculating borrowers’ income and source of funds (see table 4).

Table 4: Inadequate verification or calculation of assets and income

Case number	Mortgage amount	Inadequate support for income	Inadequate verification of assets
493-8447975	\$ 81,357	Yes	
493-8567176	109,137	Yes	
493-8959876	84,550		Yes
493-8480034	142871	Yes	
Total	\$417,915		

Unsupported Income:

Cornerstone’s underwriters used an unsupported income amount for one loan and miscalculated income for two other loans. HUD prohibits lenders from using income in evaluating the borrower’s loan if they cannot verify the income or if the income will not continue.¹³ Using unverifiable or unstable income would generate inaccurate debt-to-income ratios.¹⁴ In one loan, the borrower was no longer employed. The income calculations for two other loans were based on 40 hours per week when the borrowers’ pay stubs showed that they worked less than 40 hours per week. If based on year-to-date income, the borrowers’ mortgage payment-to-income ratio (front)¹⁵ and the total fixed payment-to-income ratio (back)¹⁶ would be 32.4 and 43.7 percent and 52.1 and 43.7 percent, respectively, exceeding HUD’s limits of 31 and 43 percent.

Unsupported Assets:

Cornerstone’s underwriters did not sufficiently verify borrower assets in FHA case number 493-8959876.¹⁷ The borrower had a bank account with a large unexplained increase of \$4,000. HUD requires the lender to obtain an explanation and evidence of source of funds for any large increases in bank accounts or recently opened accounts.¹⁸

¹³ HUD Handbook 4155.1, paragraph 4-D(1)(a)

¹⁴ HUD uses ratios to determine whether the borrower can reasonably be expected to meet the expenses involved in home ownership and otherwise provide for the family. There are two debt-to-income ratios. The mortgage payment expense-to-effective income, or front, ratio compares the borrower’s total mortgage expenses for the home to the borrower’s income. The total fixed payment-to-effective income, or back, ratio compares the borrower’s debt, including the mortgage, to the borrower’s income.

¹⁵ The front ratio is the total mortgage payment, including principal, interest, escrow deposits for taxes and insurance, mortgage insurance premium, homeowners’ association dues, ground rent, special assessments, and payments for secondary financing, compared to the borrower’s effective income. On April 13, 2005, HUD set the current front ratio limit at 31 percent in Mortgagee Letter 2005-16.

¹⁶ The back ratio is the total fixed payment (or total monthly debt payments) to income compared to the borrower’s effective income. On April 13, 2005, HUD set the current back ratio limit at 43 percent in Mortgagee Letter 2005-16.

¹⁷ This loan was for a flipped property.

¹⁸ HUD Handbook 4155.1, paragraph 5-B(2)(b)

Conclusion

Cornerstone did not comply with HUD and FHA regulations when underwriting 16 FHA-insured loans. Specifically, the underwriters violated restrictions on resales occurring 90 days or less after acquisition, failed to review or to adequately review appraisal reports to ensure that the properties' appraised values were reasonable, and did not adequately verify borrower assets and income. As a result, HUD paid claims for 13 of the 16 loans and incurred losses of more than \$981,000 upon sale of the properties (see appendix D). Further, Cornerstone placed the FHA insurance fund at an increased risk for three ineligible loans with unpaid principal balances of more than \$295,000, with estimated losses of almost \$154,000 if the loans are foreclosed upon and the properties are sold (see appendix E).

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing require Cornerstone Mortgage to

- 1A. Reimburse HUD for 13 loans for which HUD has sold the properties and incurred losses totaling \$981,574 (see appendix D).
- 1B. Indemnify HUD for three actively insured ineligible loans with unpaid principal balances of \$295,877. The projected loss of \$153,856 is based on the FHA insurance fund average loss rate of 52 percent¹⁹ of the unpaid principal balances (see appendix E).
- 1C. Ensure that it has adequately trained its managers and underwriters regarding HUD underwriting requirements, including reviewing appraisals and verifying assets and income.
- 1D. Review the FHA-insured mortgages originated by Branch 87 listed in appendix G, determine which mortgages were originated based on inflated appraisals, and reimburse or indemnify HUD for actual or potential losses on those loans.
- 1E. Review the FHA-insured mortgages originated by Branch 87 listed in appendix G, determine which mortgages were originated without an appraisal report on the closing date, and reimburse or indemnify HUD for actual or potential losses on those loans.

¹⁹ The Single Family Acquired Asset Management System's case management profit and loss by acquisition as of December 2013

- 1F. Establish procedures designed to ensure that it complies with all HUD and FHA underwriting requirements.

We also recommend that the Deputy Assistant Secretary for Single Family Housing

- 1G. Refer Cornerstone to HUD's Mortgagee Review Board for review and appropriate actions for violating HUD and FHA underwriting requirements.

We further recommend that the Director, Departmental Enforcement Center,

- 1H. Take appropriate administrative action, including possible debarment, against the appraiser responsible for the actions identified in this report.
- 1I. Take appropriate administrative action, including possible debarment, against the owners and management of Cornerstone for the violations cited in this report.

Finding 2: Cornerstone Violated RESPA When It Paid Marketing Fees in Exchange for the Referral of FHA Mortgage Business

In violation of RESPA requirements, Cornerstone paid realtors improper marketing fees in exchange for exclusive promotion of Cornerstone's mortgage products and programs as set forth in marketing agreements with the realtors. These violations occurred because Cornerstone ignored RESPA requirements. The \$382,500 in marketing fees, paid from December 31, 2007, to December 1, 2009, were in connection with Cornerstone's origination and processing of 31 defaulted FHA-insured mortgages totaling more than \$3 million (see appendix F).²⁰ As a result, Cornerstone could not ensure that its customers were able to shop for other lenders with better mortgage rates or that the referral fees did not unnecessarily increase the costs of mortgage services.

Cornerstone Executed an Improper Marketing Agreement

Section 8(a) of RESPA prohibits paying marketing fees to realtors in exchange for exclusive rights. Specifically, RESPA regulations state, "No person shall give and no person shall accept any fee, kickback or other thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or part of a settlement service involving a federally related mortgage loan (FHA-insured) shall be referred to any person."²¹

Cornerstone violated RESPA requirements in August 2007 and May 2008 when it executed \$382,500 in marketing agreements with realtors. The agreements required the realtors to exclusively market Cornerstone's loan products and programs in exchange for monthly payments of \$11,000 and \$2,083, respectively.²² As part of the agreements, the realtors were required to exclusively distribute and display various Cornerstone promotional and marketing materials at their sales offices, including business cards, flyers, and brochures describing various Cornerstone loan products and services.

One realtor was also required to provide Cornerstone employees with the exclusive privilege of working in the realtor's sales office. Cornerstone loan officers and loan processors were on site at the realtor's office. When borrowers came into the realtor's office, they were directed to Cornerstone employees, who provided such services as credit approval, mortgage financing, consulting, and expertise, effectively restricting borrowers' ability to shop for other lenders.

²⁰ Of the 831 loans underwritten by Branch 87, 145 (nearly 18 percent) were referred, while 31 of 74 (nearly 42 percent) defaulted loans with 6 or fewer payments were referrals.

²¹ 24 CFR 3500.14(b)

²² During our review period, Cornerstone paid \$37,500 in marketing fees to a national real estate franchise operator for FHA mortgage referrals.

The agreement restricted the realtor from entering into similar agreements with other lenders. The agreement stated, “During the terms of the agreement [realtor] agreed not to offer promotional opportunities similar to the one in the contract or rent office space to any other residential mortgage lender other than Cornerstone.”²³ In exchange, Cornerstone would pay the realtor \$11,000²⁴ per month. However, Cornerstone’s general ledger showed that it paid the realtor \$345,000 from December 2007 to December 2009. Cornerstone made an initial payment of \$46,000 in December 2007 and a second \$46,000 payment in January 2008 and paid \$11,000 per month from February 2008 through December 2009.

Other Payments to the Realtor:

Cornerstone made additional payments totaling \$44,058 from September 2007 through December 2009 to another entity owned by the realtor. There were no contractual agreements between Cornerstone and this entity, but the general ledger described them as rental, advertisement, telephone, and utility payments. Cornerstone’s executive vice president stated that these payments should have been labeled as marketing expenses but did not provide a marketing agreement with this entity.

Cornerstone Violated Conflict-of-Interest Statutes

In addition to violating RESPA, the marketing agreement violated conflict-of-interest statutes²⁵ because one of Cornerstone’s branch managers was a principal in a realty company. Local and Internet advertisements, in which the principal claimed to “run” and own a Cornerstone branch, indicated that the principal owned both the realty company and a branch of Cornerstone.

At the time of our review, on his Web site, the principal stated, he “... is also active in interim lending to other Real Estate Investors through his Houston Hard

²³ While Cornerstone employees were on site at the realtor’s office, Cornerstone denied paying rent during that time.

²⁴ The agreement called for Cornerstone to pay EGDG, LLC, \$11,000 per month for marketing and advertising services and if applicable, desk rental as outlined. (The agreement did not outline anything regarding desk rental. The amount of the fee attributed to rent was \$0, and the square footage space was left blank.)

²⁵ 24 CFR 202.5(l), “Conflict of interest: A mortgagee may not pay anything of value, directly or indirectly, in connection with any insured mortgage transaction or transactions to any person or entity if such person or entity has received any other consideration from the mortgagor, seller, builder, or any other person for services related to such transactions or related to the purchase or sale of the mortgaged property, except that consideration approved by the [HUD] Secretary may be paid for services actually performed. The mortgagee shall not pay a referral fee to any person or organization.”

Money²⁶ Lending Company, Jet Investor Lending, LLC, as well as offering home mortgage loans through his mortgage company, Cornerstone Mortgage Partners.”

In a March 2009 online trade magazine, an article referred to the principal as running Cornerstone. It stated, he “... does over 100 complete rehab transactions a year (buy, fix and sell). Plus, he runs a large hard money company, Jet Lending, and a traditional mortgage banking business through Cornerstone Mortgage.”

Further, Cornerstone quality control reports used the principal’s name to describe a branch.²⁷ According to Cornerstone’s executive vice president, the reference was used to describe the cost center and nothing else. The executive vice president stated that the principal had never been employed by Cornerstone.

Finally, Cornerstone originated loans from two locations during the audit period. The two locations were 14515 Briarhills and 15729 I-45 North Freeway. According to Neighborhood Watch, Branch 87’s address is 14515 Briarhills. The office at 15729 I-45 North Freeway housed Branch 87 staff, but it also housed businesses owned by the principal and a separate business owned by a Branch 87 loan officer.

Cornerstone originated 141 mortgages from its office collocated with the realtor. FHA insured the mortgages for more than \$13.7 million.

Cornerstone submitted erroneous certifications to HUD that effectively hid the RESPA violations and the conflict of interest. In its direct endorsements²⁸ for loans involving the realtor, Cornerstone certified that it and its owners, officers, employees, and directors did not have financial interests in or relationships, by affiliation or ownership, with sellers involved in the loan transactions. Further, Cornerstone certified to HUD that it did not pay any fee or consideration of any type, directly or indirectly, to any party in connection with the loan transactions.

According to one of Cornerstone’s managers as of March 6, 2014, Cornerstone continued to use marketing agreements.

Conclusion

Cornerstone violated RESPA’s restriction on referral fees by making improper payments to a realtor that referred FHA mortgage business to it and violated conflict-of-interest statutes by contracting with a branch manager, who was also a franchise owner as well as a realtor, lender, and investment company executive.

²⁶ According to Wikipedia, one definition of “Hard Money” is an asset-based loan financing secured by the value of a parcel of real estate.

²⁷ Branch P&L, Gant, LLC, West Houston (115)

²⁸ Form HUD-92900-A

Cornerstone submitted erroneous certifications to HUD, which effectively hid the relationships from HUD.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing

- 2A. Require Cornerstone to adequately train its managers and staff regarding RESPA requirements.
- 2B. Review Cornerstone's current marketing agreements and its payments to realtors under those agreements to determine whether they are improper referrals for FHA mortgage business.

We recommend that the Director, Departmental Enforcement Center,

- 2C. Take appropriate administrative action, including possible debarment, against the realtor for the RESPA violations.

Finding 3: Cornerstone Failed To Properly Implement a Quality Control Plan

From 2007 through 2009, Cornerstone did not always comply with HUD’s quality control requirements. Specifically, it did not (1) conduct timely quality control reviews, (2) review all early payment default and rejected loans or review them in a timely manner, (3) conduct timely onsite reviews or include all review items required by HUD, or (4) follow required reverification processes for loans it reviewed. Further, Cornerstone could not support that it took corrective actions in a timely manner. These conditions occurred because Cornerstone’s quality control plan conflicted with HUD regulations and its review process was inadequate. As a result, it was unable to ensure the accuracy, validity, and completeness of its loan origination operations, resulting in an increased risk to the FHA insurance fund.

Cornerstone Did Not Conduct Timely Quality Control Reviews

While Cornerstone performed quality control reviews on 10 percent of loans closed monthly, it did not complete those reviews in a timely manner—within 90 days of loan closing—as required by HUD regulations.²⁹ For example, Cornerstone did not complete quality control reviews for loans closed between December 2008 and April 2009 until 4 to 7 months after the loans closed. This condition occurred because Cornerstone’s quality control plan conflicted with HUD regulations. Cornerstone’s quality control plan required that quality control reviews be *conducted* within 90 days of loan closing. HUD regulations require that quality control reviews be *completed* within 90 days of loan closing.

Cornerstone Did Not Conduct Early Payment Default and Rejected Loan Reviews as Required

Cornerstone did not review or did not review in a timely manner 36 loans that defaulted within the first 6 payments³⁰ (early payment default loans) as required by HUD regulations³¹ and its quality control plan.³² It did not review 11 loans and did not review the other 25 loans in a timely manner. For example, in several

²⁹ HUD Handbook 4060.1, REV-2, paragraph 7-3(D), requires quality control reviews to be completed within 90 days of closing.

³⁰ The loans closed between April 2008 and December 2009.

³¹ HUD Handbook 4060.1, REV-2, paragraph 7-6(D), requires lenders to review all early payment default loans, including loans that become 60 days or more delinquent, within the first six payments.

³² Cornerstone’s quality control plan, page 8, required reviews to be performed on all loans going into default within the first six payments.

cases, the borrower made no payments, and Cornerstone did not conduct quality control reviews until as many as 8 months later.

Further, Cornerstone did not perform required quality control reviews on any of the 51 loans that Branch 87 rejected between July 1, 2007, and September 30, 2009.³³

Cornerstone Did Not Conduct Annual Onsite Reviews of Branch 87

Due to high default rates, new key employees (loan officers and a branch manager), and past problems, Cornerstone was required to conduct annual reviews of Branch 87.³⁴ From 2007 through 2009, Neighborhood Watch showed that Branch 87 ranked first among Cornerstone branches in the Houston area with a high percentage of defaulted loans in the first year. During that period, Branch 87 originated 831 loans and had 79 defaults and 13 claims. Branch 87's percentage of claims and defaults was 11.07 percent compared with 4.94 percent for the country. Despite the high default rates, new key employees, and past problems, Cornerstone did not conduct annual reviews of Branch 87. For example, Cornerstone conducted an onsite review during March 2008 but did not conduct another review until 21 months later in December 2009.

Further, Cornerstone's reviews did not address all of the items required by HUD. Cornerstone's reviews did not confirm whether Branch 87 revised procedures to reflect changes in HUD requirements and inform personnel of the changes. Further, the reviews did not ensure that Branch 87 personnel were all Cornerstone employees or contract employees performing functions that FHA allowed to be outsourced.

Cornerstone Did Not Follow Reverification Requirements

Cornerstone did not follow required reverification processes for loans that it reviewed under its quality control program. HUD requires quality control programs to include procedures for reviewing and confirming specific information on all loans selected for review.³⁵ HUD further requires that certain documents contained in the loan file be checked for sufficiency and subjected to written reverification. Specifically, HUD requires lenders to reverify the

³³ HUD Handbook 4060.1, REV-2, paragraph 7-8(A)(1), requires that of the total loans rejected, a minimum of 10 percent or a statistical random sampling that provides a 95 percent confidence level with 2 percent precision must be reviewed.

³⁴ HUD Handbook 4060.1, paragraph 7-3(G)

³⁵ HUD Handbook 4060.1, REV-2, paragraph 7-6(E)(2)

borrower's employment, other income, deposits, gift letters, alternate credit sources, acceptable sources of funds, and mortgage or rent payments. If the written reverification is not returned to the lender, the lender is required to make a documented attempt to conduct a telephone reverification, even if the original information provided during the loan origination process was obtained electronically or involved alternative documents. Cornerstone's case files did not contain documentation showing that it reverified unreturned verifications of employment for 105 Branch 87 loans.

HUD also requires lenders to obtain new credit reports for loans when performing quality control reviews, except for streamline refinance loans or loans processed using an FHA-approved automated underwriting system.³⁶ However, Cornerstone ordered new credit reports for only 18 of the FHA loans it reviewed during the audit period.

In one example (FHA case number 493-8447975), Cornerstone originated a loan for a borrower without verifying current employment. The employment verification in the file showed that the borrower was not employed when the loan closed. It showed previous employment, not current employment. When Cornerstone conducted a quality control review in December 2007, it again did not verify employment.

Cornerstone Could Not Support That It Took Timely Corrective Actions

Cornerstone could not provide support to show that it complied with HUD regulations requiring it to

- Report review findings to senior management within 1 month of completion of the initial report;
- Take prompt action to deal appropriately with any material findings; and
- Identify actions being taken, the timetable for completion, and any planned follow-up activities in the report.³⁷

The monthly quality control reports appeared to show that management responded to each of the required corrective action requests, but the reports were not dated except to say that they were for a specific month, and there were no follow-up dates given in any of the reports. As a result, it was not clear when or whether Cornerstone's management followed through with specific actions.

³⁶ HUD Handbook 4060.1, REV-2, paragraph 7-6(E)(1)

³⁷ HUD Handbook 4060.1, REV-2, paragraph 7-3(I)

Conclusion

Cornerstone did not always comply with HUD's quality control requirements during the review period. Specifically, it did not (1) conduct timely quality control reviews, (2) review all early payment defaulted and rejected loans or review them in a timely manner, (3) conduct timely onsite reviews or include all review items required by HUD, or (4) follow required reverification processes for loans it reviewed. Further, Cornerstone could not support that it took corrective actions in a timely manner. As a result, it was unable to ensure the accuracy, validity, and completeness of its loan origination operations, resulting in an increased risk to the FHA insurance fund.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing

- 3A. Verify that Cornerstone has implemented a HUD-approved quality control plan that fully complies with HUD and FHA requirements.

SCOPE AND METHODOLOGY

To accomplish our review objectives, we

- Reviewed applicable regulations, requirements, mortgagee letters, and HUD Quality Assurance Division reports;
- Reviewed reports and information in HUD's Neighborhood Watch system and Single Family Data Warehouse;³⁸
- Reviewed Cornerstone's files, ledgers, policies, procedures, and independent audit reports for the years ending December 31, 2007, and 2008;
- Reviewed 13 escrow files from 4 different title companies;
- Conducted interviews with Cornerstone staff and borrowers; and
- Performed appraisal reviews for 7 properties.

We obtained a data download of Branch 87 loans originated from October 1, 2007, through September 30, 2009, from Neighborhood Watch. The download showed that Branch 87 originated 831 FHA-insured loans valued at more than \$86.5 million. Three hundred of the loans were at least 30 days delinquent, and 74 of the loans with original loan amounts totaling \$7.4 million defaulted within the first 6 payments. We used the data to select a sample of loans for review, and did not rely on the data as a basis for our conclusions. Therefore, we did not assess the reliability of the data.

We selected a sample of 34 loans from the 74 defaulted loans. We did not review all 74 defaulted loans because we did not plan to project the results on the population of loans. The 34 sample loans reviewed were currently in default, were not refinanced, and had six or fewer payments before the first reported default. The original loan amounts for the 34 loans totaled nearly \$3.5 million. The results of our detailed testing apply to only the 34 loans selected and cannot be projected. The remaining 40 defaulted loans that we did not test are listed in appendix G with the loan status as of January 2014.

We performed detailed testing and reviewed the underwriting procedures for the 34 loans. We reviewed documentation from the HUD Homeownership Center³⁹ loan endorsement files and loan files provided by Branch 87. Our testing and review included (1) analysis of borrowers' income, assets, and liabilities; (2) review of borrowers' savings ability and credit history; (3) verification of selected data on the underwriting worksheet and settlement statements; and (4) confirmation of employment and gifts. In addition, we conducted site visits to 10 of the 34 properties to ensure they existed.

³⁸ Single Family Data Warehouse is a large and extensive collection of database tables organized and dedicated to support the analysis, verification, and publication of single-family housing data. It consists of database tables structured to provide HUD users easy and efficient access to Office of Single Family Housing case-level data on properties and associated loans, insurance, claims, defaults, and demographics.

³⁹ Homeownership Centers are offices where HUD has set up mortgage insurance operations to serve and monitor mortgagees, lenders, and home buyers. They are located in Philadelphia, PA, Atlanta, GA, Denver, CO, and Santa Ana, CA.

We obtained Cornerstone's quality control plan and all 105 of the quality control review reports and supporting documentation for loan reviews that it and its quality control contractor conducted during the 12-month period September 2008 through August 2009.⁴⁰ We reviewed the quality control plan, reports, and supporting documentation to determine the sufficiency and timeliness of the quality control reviews on closed loans. In addition, we reviewed the previously selected 74 loans that had defaulted within 6 months for evidence of early payment default reviews. Finally, we selected a random sample of 10 of 51 rejected loans from the period July 1, 2007, to September 30, 2009, to determine the adequacy of quality control reviews conducted for the rejected loans. We selected a random sample instead of reviewing all 51 rejected loans because we were determining the adequacy of the reviews instead of the number of errors in the population.

We selected a sample of 7 properties from the 74 defaulted loans. We selected properties with current sales prices and appraisal values exceeding the prior sales prices, list prices, and tax values. The results of this testing apply only to the 7 properties selected and cannot be projected to the remaining 67 properties. A HUD Office of Inspector General (OIG) appraiser performed appraisal reviews of the seven properties. OIG conducted physical inspections, researched neighborhoods, and verified comparable sales for the seven properties.

For the 13 ineligible loans that were foreclosed and the properties sold, we obtained profit and loss data from HUD's Single Family Acquired Asset Management System. We also calculated the estimated loss for the three ineligible loans that were in default using FHA's loss rate of 52 percent as of December 2013.

We performed our fieldwork between December 2009 and May 2010 on loans that Branch 87 originated between October 1, 2007, and September 30, 2009. We expanded our scope as necessary to include a RESPA violation and Cornerstone's quality control procedures. We performed our audit work at Cornerstone's headquarters and Branch 87 offices and at our office in Houston, TX.

We conducted the review in accordance with generally accepted government auditing standards, except as noted below. Those standards require that we plan and perform the review to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our review objectives.

We did not comply with the auditing standard for early communication of control deficiencies resulting in noncompliance with provisions of laws, regulations, contracts or grant agreements, or abuse because we suspended our audit from August 2010 until July 2013 at the request of the U.S. Department of Justice. We then updated our review work to incorporate changes in Cornerstone's operations for background purposes and to update the status of our sample loans.

⁴⁰ From October 1, 2007, to March 15, 2009, Cornerstone conducted quality control reviews internally. From March 15 to September 30, 2009, Cornerstone conducted some reviews internally but also used a contractor to perform external quality control reviews.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objectives:

- Policies and procedures intended to ensure that FHA-insured loans are properly originated, underwritten, and closed.
- Safeguarding FHA-insured mortgages from high-risk exposure.
- Policies and procedures intended to ensure that the quality control program is an effective tool in reducing underwriting errors and noncompliance.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiencies

Based on our review, we believe that the following items were significant deficiencies in 2007 through 2009:

- Cornerstone did not have effective controls in place to ensure that FHA-insured loans were originated, underwritten, and closed in accordance with HUD requirements, exposing HUD to unnecessary insurance risks (finding 1).

- Cornerstone ignored RESPA regulations by paying a realtor marketing fees in exchange for referrals for FHA mortgage business (finding 2).
- Cornerstone did not implement an effective quality control plan (finding 3).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1A	\$981,574	
1B		\$153,856

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified.

Implementation of our recommendation to require Cornerstone to indemnify HUD for the three loans that were not originated in accordance with FHA requirements will reduce FHA's risk of loss to the FHA insurance fund. The amount above reflects that upon the sale of the mortgaged property, FHA's average loss experience is about 52 percent of the unpaid principal balance as of December 12, 2013.⁴¹

⁴¹ According to the Single Family Acquired Asset Management System's case management profit and loss by acquisition as December 2013

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



March 31, 2014

Via Federal Express

Mr. Gerald R. Kirkland
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General
Office of Audit (Region 6)
819 Taylor Street, Suite 13A09
Fort Worth, Texas 76102

**Re: Cornerstone Home Lending, Inc.
HUD-OIG Draft Audit Report 2014-FW-100X**

Dear Mr. Kirkland:

Cornerstone Home Lending, Inc. ("Cornerstone" or "CHL" or the "Company") is in receipt of the letter, dated February 28, 2013, from the U.S. Department of Housing and Urban Development ("HUD" or the "Department") Office of Inspector General ("OIG") enclosing a draft audit report (the "Draft Report" or "Report"). The Draft Report stems from a review of a former CHL branch office (i.e., Branch 87) in 2009. It identifies potential concerns: in 16 Federal Housing Administration ("FHA") insured loans that former Branch 87 originated approximately 5 to 7 years ago; with 2 of Branch 87's marketing agreements that were terminated over 4 years ago; and, with a Quality Control Plan that is no longer in effect.

The Draft Report states that the OIG's audit objectives were to determine whether Cornerstone complied with HUD/FHA regulations when originating and underwriting FHA-insured loans and implemented a compliant Quality Control Plan. Based on the OIG's preliminary findings, the Draft Report recommends that HUD require Cornerstone to indemnify HUD in connection with the 16 loans referenced in Finding 1, as well as pursue administrative action against the Company in connection with all of the findings.

Cornerstone is disappointed in the manner with which this audit has been conducted. Cornerstone takes exception to all three findings in the Draft Report, as discussed in greater detail below. The Draft Report misstates both facts and law throughout the findings. It makes statements about the Company's operations that simply are not true, and it bases allegations on requirements that do not exist. What's more, the OIG conducted its review 5 years ago and based its findings on

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Comment 1
Comment 2

Comment 2

loans more than 6 years old, policies and procedures that have not been in effect for many years, and a branch office that the Company closed for business reasons 2 years ago. The significant passage of time and over 4-year delay by the OIG in issuing the Draft Report have placed Cornerstone at a severe disadvantage in responding to the preliminary findings. Under the circumstances, we question whether a final report should even be issued.

Comment 1

That being said, and while Cornerstone disagrees with the allegations in Finding 1, the prejudice to the Company resulting from the OIG's delay is most apparent in connection with Findings 2 and 3. Finding 2 alleges that 2 marketing agreements maintained by former Branch 87 violated the Real Estate Settlement Procedures Act ("RESPA"). First and foremost, this allegation is incorrect. It demonstrates a misunderstanding of how RESPA applies to marketing agreements and a disregard for HUD's public statements on the matter. In addition, while CHL explains below why these agreements in fact complied with RESPA, we note that the agreements were terminated in 2009 and 2010. Thus, the statute of limitations for any enforcement action has passed, and inclusion of the incorrect finding in a final report would give a misimpression that Cornerstone has arrangements contrary to RESPA in place when that is not the case and would be unduly prejudicial.

Comment 3

Comment 2

Similarly, Finding 3 alleges that Cornerstone did not implement a compliant Quality Control Plan. The audit, however, was performed in 2009, at a time when the Company's written plan may not have reflected all of the Quality Control steps implemented by the Company, and Finding 3 is based on an outdated plan. The Company now has a more detailed and enhanced written plan in place, and its records reflect timely and accurate completion of required Quality Control reviews and activities. Inclusion of a Quality Control finding in the final report, therefore, would serve only to give the public a false impression of the Company's current policies and procedures. During the exit conference on March 6, 2014, OIG representatives themselves acknowledged that it may be appropriate at least to add language to Finding 3 stating that the Company's current Quality Control Plan resolves any concerns the OIG had in 2009. OIG representatives went further to indicate their commitment to clarifying in the final report that the findings reflect conditions between 2007 and 2009, not current conditions at the Company. The Draft Report as written does not reflect fairly Cornerstone's business operations and causes undue prejudice to the Company. For these reasons, Cornerstone respectfully requests that the OIG remove Findings 2 and 3 from any final report it issues.

Comment 2

The OIG provided Cornerstone with an opportunity to submit written comments for inclusion in a final report. This response summarizes the Company's history and operations and addresses the individual findings in the Draft Report. We appreciate this opportunity to respond to the OIG's preliminary findings and recommendations. That being said, we understand that final audit reports routinely include auditors' comments about the audited lender's written response, but that the lender is not

provided an opportunity to respond to these additional comments. Often, these comments include substantive allegations or statements that were not part of the draft audit report provided to the lender. To the extent that the OIG makes such additional substantive comments in this instance, we respectfully request an opportunity to respond to these additional statements to ensure that a full and fair picture of the issues is presented in the final report.

I. BACKGROUND - CORNERSTONE HOME LENDING AND BRANCH 87

Cornerstone was incorporated in the State of Texas in 1986, and began operations in 1988. Headquartered in Houston, the Company currently has over 1,100 employees and operates nationwide. It received approval to participate in the Department's FHA mortgage insurance programs as a non-supervised mortgage company on March 31, 1988, unconditional Direct Endorsement authority in June 1988, and Lender Insurance Authority in January 2006. It currently maintains 70 branch offices registered with HUD/FHA. The Draft Report states that CHL had 99 branch offices at the time of the audit but "terminated" about one-third of them later. We note, however that CHL did not "terminate" these offices; rather, it closed them for business reasons, just as companies in all industries routinely open and close offices throughout their regular course of business. Cornerstone, which acts as an authorized agent for one principal and as a principal for 9 authorized agents, sells all of its loans on a servicing-released basis, and its primary investors are Chase and PennyMac. It also is an approved lender for the Department of Veterans Affairs, Fannie Mae, Freddie Mac, Ginnie Mae, and the U.S. Department of Agriculture.

Cornerstone takes its relationship with the Department and its responsibilities under FHA programs seriously. It enjoys excellent relationships with both consumers and investors, and CHL employees consistently strive to produce high quality loans in compliance with HUD/FHA standards. Since its inception, the Company has sought to provide dependable and professional service and repeatedly has demonstrated its commitment to borrowers and its allegiance to the various lending programs in which it participates. To this end: the *Houston Chronicle* named Cornerstone a top workplace company every year for the past 4 years; the Texas Department of Housing & Community Affairs named Cornerstone Lender of the Year in 2008 and every year for the past 4 years; and, the Texas State Affordable Housing Corporation named Cornerstone the #1 lender every year for the past 4 years.

FHA lending constitutes a substantial portion of Cornerstone's business. The Draft Report states that, in fiscal year 2009 when the audit was conducted, Cornerstone originated 6,255 FHA loans. Over the past 2 years, Cornerstone has underwritten and closed 10,225 FHA loans, averaging 5,113 FHA loans per year.

The Draft Report is based on a review of Cornerstone's former Branch 87 located at 14515 Briarhills Parkway in Houston, Texas. Branch 87 was opened and approved by HUD/FHA in April 2004, and Cornerstone closed the office in March

Comment 4

Comment 2

Comment 5

2012, because the Branch Manager accepted employment elsewhere. The Draft Report states that Branch 87 was selected for review based on its high default/claim rate in 2009. Significantly, HUD determined that the high default/claim rate for Branch 87 at that time was not due to any fault or negligence of Cornerstone. Specifically, HUD withdrew a notice of proposed termination of Branch 87 after considering the facts and circumstances underlying the office's defaulted loans and reviewing Cornerstone's origination and underwriting activities. The findings in the Draft Report, however, are based on the very same general time period that HUD previously reviewed. Moreover, again, for separate business reasons, Cornerstone closed Branch 87 in March 2012 - over 2 years ago - and none of its employees continue to work for the Company.

II. RESPONSE TO THE FINDINGS

The Draft Report contains three findings. First, it alleges that Branch 87 originated 16 FHA-insured loans that did not comport with HUD/FHA requirements and, therefore, warrant indemnification from Cornerstone. Second, it alleges that Branch 87 maintained 2 marketing agreements that were inconsistent with RESPA. Third, it alleges that Cornerstone did not maintain and implement a Quality Control Plan in compliance with FHA requirements.

After receiving the Draft Report, Cornerstone conducted a thorough review of the findings and loan files cited therein. It also examined HUD/FHA guidelines and the Company's internal policies and procedures, in an effort to provide pertinent information and documentation with this response. Based on its stringent review, Cornerstone takes strong exception to the findings in the Draft Report.

Comment 1

To summarize, in the cases cited in Finding 1, the Draft Report contains factual inaccuracies, as well as asserts facts that either do not violate HUD/FHA requirements or were immaterial to the loan's insurability. Cornerstone substantially complied with HUD/FHA requirements in these cases and all of the borrowers qualified for FHA financing. Thus, the recommendations to HUD are wholly inappropriate. As each borrower qualified for FHA financing, neither reimbursement nor indemnification is warranted in any case, and administrative action would be insupportable. Moreover, Cornerstone already has rigorous training in place for its managers and underwriters regarding HUD underwriting requirements, including for reviewing appraisals and verifying assets and income.

Comment 1

Comment 6

In addition, the allegation in Finding 2 that Cornerstone paid real estate brokers for referrals in violation of RESPA is both erroneous and offensive. The allegation improperly describes how RESPA applies to marketing arrangements and HUD's public statements on the matter. Branch 87's former marketing agreements with real estate brokers involved fixed payments for actual marketing and promotional services performed in compliance with RESPA and related administrative guidance at the time. At no time did Cornerstone pay real estate brokers or others for referrals of business. The allegations in the Report are unsupported by the facts and



Comment 3

inconsistent with the law governing the subject. Moreover, the suggestion that HUD should require Cornerstone to stop paying marketing fees to realtors, which in fact are permitted under RESPA, is moot because the marketing agreements at issue were terminated in October 2009 and March 2010, over 4 years ago. Plus, the statute of limitations has long since run. For these reasons, and as explained in greater detail below, we submit that the OIG should remove Finding 2 from any final report.

Comment 2

Furthermore, the allegation in Finding 3 that Cornerstone did not maintain and implement a compliant Quality Control Plan is stale and no longer applicable to the Company. The wording in Finding 3 gives the impression that Cornerstone does not engage in adequate Quality Control, but Finding 3 is based on a written plan that the Company used five years ago, not the Company's current Quality Control Plan or program. Nevertheless, we note that Cornerstone always has maintained and implemented a robust Quality Control program. While it is possible that certain delays may have occurred in a handful of instances in the past, such isolated occurrences in no way reflect Cornerstone's compliance objectives or success overall. Moreover, the Company's current Quality Control Plan complies with applicable HUD/FHA requirements. For these reasons, and as explained in greater detail below, we submit that the OIG should remove Finding 3 from its final report.

Comment 7

Below we reply in greater detail to the individual findings in the Draft Report. We believe, and we hope that HUD and the OIG will agree, that this response and accompanying exhibits demonstrate Cornerstone's compliance with HUD/FHA requirements and adherence to prudent lending standards with respect to the matters raised in the Draft Report. Initially, however, we note that the lengthy passage of time between the OIG review of Branch 87 in November 2009, and issuance of the Draft Report at the end of February 2014, has placed Cornerstone at a significant disadvantage in responding to the findings and dictates against the imposition of any penalties or administrative action.

A. DEPARTMENT CLAIMS ARE BARRED BY LACHES

Comment 2

When a claimant brings a case against a respondent, the claimant must do so in a timely manner because, if too much time passes, the respondent no longer has sufficient resources to defend itself meaningfully. Here, many years have passed since the OIG audit and the OIG's findings are stale. The office that was audited closed over 2 years ago, cited loans are generally five to 7 years old, referenced agreements were terminated years ago, and the Company's policies and procedures have changed. Specifically, among other things:

Comment 2

- the OIG performed the review underlying the Draft Report in November 2009, nearly 4 and a half years ago, and conducted its first exit conference with the Company in April 2010, nearly 4 years before issuing the Draft Report;

Comment 7

- the loan files cited in Finding 1 were originated between October 1, 2007 and September 30, 2009, 4.5 to 6.5 half years ago, and HUD/FHA guidelines require lenders to maintain origination files for only 2 years after selling them;

Comment 3

- the 2 marketing agreements referenced in Finding 2 were terminated in October 2009 and March 2010, over 4 years ago, HUD is no longer the regulating body for RESPA, and the statute of limitations has run under the statute for any RESPA claims;

Comment 2

- the Quality Control Plan referenced in Finding 3 was the Company's plan 5 years ago in 2009, and it is not the Company's current plan; and

Comment 2

- Cornerstone closed Branch 87 2 years ago in March 2012.

Comment 7

Given all of these facts, it has been extremely difficult, and impossible in some instances, to re-create any type of historical record containing precise details surrounding the matters raised in the Draft Report. The lengthy passage of time has disadvantaged Cornerstone in its ability to reconstruct the files and reach former employees, vendors, and borrowers, and the Company no longer maintains (nor is it required to maintain) all of the file documentation.

Comment 2

The Draft Report acknowledges the lengthy passage of time in this case, stating that the OIG suspended its audit from August 2010 until July 2013 at the request of the U.S. Department of Justice ("DOJ"), after which time it updated its background information about the Company and the payment status of its sample loans. While we understand and appreciate that the OIG could not issue its report before July 2013 because DOJ was reviewing the case, the OIG could have issued its findings in 2013 if it deemed them still valid after DOJ determined not to pursue any case against Cornerstone. The OIG, however, waited another 8 months to issue its Draft Report without updating any information in it besides basic background information or the payment status of the files, all of which information was readily available at any time. We understand that these types of delays are atypical, and they have placed Cornerstone at a significant disadvantage and prejudiced its ability to respond to the findings. For these reasons, we believe that any claims by HUD in this case would be barred by the doctrine of laches.¹

¹ We understand HUD takes the position that it is not subject to the defense of laches in enforcing its rights. See In the Matter of Isaac and Emma Wilson, HUDBCA No. 99-C-SE-Y80, available at http://portal.hud.gov/hudportal/HUD?src=/program_offices/hearings_appeals/bca/decisions/dot/wilson99csey80. The standard for laches, however, is a lack of due diligence by the plaintiff and prejudice to the defendant, see Costello v. United States, 365 U.S. 265 (1961), both of which exist in this case, and courts have noted that HUD may be barred by laches where it is guilty of unreasonable and inexcusable delay that has prejudiced the defendant. See United States v. Salvation Army, 1997 U.S. Dist. LEXIS 882 (S.D.N.Y. Jan. 30, 1997).



That being said, without waiving the foregoing position or conceding that any claims by the Department would not be barred by laches, Cornerstone responds to the substantive matters raised in the Draft Report below to the best of its ability given the lengthy passage of time.

B. FINDING 1 - UNDERWRITING

In Finding 1, the Draft Report alleges that Cornerstone did not underwrite 16 of the loans reviewed in compliance with HUD/FHA requirements. Specifically, the Draft Report asserts that, in these cases: (1) the Company violated restrictions on resales occurring within 90 days or less after acquisition; (2) the underwriters did not review appraisal reports, or did not review them adequately, to ensure the properties' values were reasonable; and (3) the files do not verify adequately the borrowers' assets or income. The Report contends that "noncompliance occurred because the underwriters failed to exercise due diligence in underwriting the loans" and it recommends that HUD require Cornerstone, among other things: to reimburse HUD for the losses it has sustained in connection with claims on 13 of the 16 loans; indemnify HUD for the remaining three loans; and to ensure adequate underwriting training for its underwriters and managers. The Report also recommends that HUD refer Cornerstone to the Mortgagee Review Board for appropriate administrative action.

Comment 7

The 16 loans cited in Finding 1 were originated 5 to 7 years ago. While the HUD Quality Assurance Divisions typically review files dating 2 years back, and while HUD only requires a lender to maintain files for 2 years after selling the loans, the OIG has issued a Draft Report 5 years after conducting its review, 5 to 7 years after the cited loans were originated and closed, and 2 years after the branch office that originated the loans was closed. Thus, as Cornerstone may no longer have complete records or access to all persons involved in the transactions due to the lengthy passage of time, the Company is at a severe disadvantage in responding to the findings.

Comment 1

Nevertheless, Cornerstone takes exception to the underwriting findings and recommendations in the Draft Report. Our review of the files revealed substantial compliance with HUD/FHA requirements and guidelines. The recommendations in the Report are at odds with the facts and circumstances surrounding these cases and with the FHA requirements and regulatory guidance that apply to them. Below we address the three categories of findings, including the assertions made in the individual loans within each category.

1. Resales Did Not Occur Within 90 Days and Properties Were Exempt from the 90-Day Resale Restriction

First, the Draft Report contends that Cornerstone ignored HUD regulations by approving 8 FHA loans for properties that had been resold within 90 days of acquisition and using the "effective date" in the purchase contracts instead of

determining the resell dates by evaluating the loan documents. The Report states that the effective dates were artificial dates used to mislead HUD into believing more than 90 days had passed, when evidence in the loan files (e.g., contract addenda, loan applications, loan processing, earnest money deposits, appraisals, title insurance, and verifications of deposit and employment) showed that all contract terms had been agreed upon and the parties intended to be bound by the contract within less than 90 days.

Comment 1

The Report alleges that Cornerstone endeavored to mislead HUD into believing that resales did not occur within 90 days by using the effective dates of the contracts to determine the resale dates. We take strong exception to this suggestion. Cornerstone neither ignored HUD regulations nor tried to mislead HUD at any time. Just the opposite - Cornerstone followed HUD directions in determining the resale date in each case and complied with applicable FHA requirements.

Comment 8

When the subject loans were originated and closed, FHA guidelines prohibited a resale within 90 days of the seller's acquisition of the property. HUD defines the acquisition date as the date of settlement for the seller's prior purchase of the property and the resale date as the date on which the sales contract is executed by the borrower. See 24 C.F.R. § 203.37a(b); HUD Handbook 4155.2 4.7.e; Mortgagee Letter 2006-14. Given HUD's definition of the resale date as the date of contract execution by the borrower, Cornerstone properly relied on the effective dates of the contracts (i.e., the dates the borrowers signed the contracts) to determine the resale dates. Nowhere do HUD/FHA regulations or guidelines direct a lender to review loan file documents to determine when the parties intended to be bound by their contracts. According to HUD rules, the relevant date in each case was the date the borrower executed the sales contract, and that is the date on which Cornerstone relied in each case.

Comment 8

To this end, in 6 of the 8 cases cited in Finding 1, the Draft Report notes that between 91 and 129 days elapsed between the acquisition date and the date of contract execution (i.e., the effective date per the contract).² While the buyer and seller may have been engaged in discussions prior to the noted effective dates, the only relevant date in each case is the date on which the borrower executed the contract. The fact that the parties may already have been engaged in discussions, or

² These six cases are FHA Case Numbers: 493-8959876; 493-8547028; 493-8693472; 493-8753582; 493-9141680; and 493-8721328.



Comment 8

even have waited intentionally for the 90-day time period to pass,³ does not change the actual resale dates that should be used to determine the timing under HUD/FHA rules. In the remaining 2 cases, while the Draft Report suggests the effective date was left blank, in fact, the files show the effective dates. For example, in one case - with **FHA Case Number 493-8544391** - Finding 1 indicates that there was no effective date on the contract and that the file shows the parties intended to be bound on January 22, 2008. In this case, however, Cornerstone advised the parties to the loan that the property would be ineligible for FHA financing until April 7, 2008. The parties, therefore, presented a contract on April 7, 2008, which the appraiser reflected as the effective date of the sales contract in the appraisal report (**Exhibit A**). It appears that the parties inadvertently omitted the effective date when executing the contract, but the January 22nd date noted in Finding 1 reflects the date the earnest money was provided, not the date of contract execution, which HUD officials have informed Cornerstone in the past is the relevant date for determining the resale date. Moreover, HUD expressly allows a lender to rely on information provided by the appraiser in determining the date of property acquisition, see Mortgagee Letter 2006-14, and again, the appraisal report in this case shows an effective contract date of April 7, 2008, which was 93 days after the acquisition date. In all of these cases, as directed by HUD, Cornerstone properly relied on the dates the borrowers executed the contracts to determine the resale dates, and thus complied with the 90-day resale restriction.

Comment 9

What's more, please note that 7 of the 8 properties at issue were located in a presidentially declared disaster area. When a property is located in a presidentially declared disaster area, the property is eligible for relief from certain FHA underwriting guidelines for up to one year after the President's declaration of the disaster. See 24 C.F.R. § 203.37a(c)(8); Mortgagee Letter 2005-31. This relief includes exemption from the time restrictions (e.g., the 90-day resale restriction) contained in the anti-flipping rule. See Mortgagee Letter 2006-14. Here, 7 of the 8 subject properties were located in Harris County, Texas, where the number of natural disasters far exceeds the national average and where there have been 17 Presidential declarations of disaster. Just surrounding the timeframe for the subject loans (i.e., October 1, 2007 through September 30, 2009), on October 2, 2007, President Bush declared Harris County a disaster area as a result of Tropical Storm Erin damage. In addition, during the 2008 hurricane season, three hurricanes and a major tropical storm ravaged the Texas coast within a 90-day period and all Texas coastal counties,

³ For example, in connection with **FHA Case Number 491-9141680**, the Draft Report states that the seller acquired the property on January 16, 2008, and sold it to the borrower on February 12, 2008, 27 days after acquisition. The OIG states that the lender used the effective date on the sales contract in its file, which was April 17, 2008, but the earnest money was received on February 11, 2008, an appraisal was conducted on March 19, 2008, and a second appraisal was conducted on April 2, 2008. In this case, however, although the borrower initially contacted Cornerstone in February 2008, and paid his earnest money at that time, Cornerstone explained the 90-day restriction to the borrower and the borrower elected to place his sales contract and loan application on hold. After the 90 days had passed, the borrower executed a new sales contract and the earnest money was transferred to the new contract.



Comment 9

including Harris County, were declared as presidential disaster areas. On September 13, 2008, President Bush declared Harris County a disaster area as a result of Texas Hurricane Ike. See http://www.city-data.com/county/Harris_County-TX.html/. In 7 of the 8 cases cited, the properties were located in Harris County and loan applications were submitted within a year of a Presidential declaration of disaster.⁴ Thus, they should have been exempt from the 90-day resale restriction. Regardless of the exemption, however, Cornerstone properly determined the acquisition and resale dates as discussed above, and all 8 properties were purchased more than 90 days after the seller had acquired them.

Comment 10

Additionally, we note that HUD defines property flipping as reselling a recently acquired property for considerable profit with an artificially inflated value. See HUD Handbook 3155.2 4.7.a. In the 8 cases cited in this category under Finding 1, although the purchase prices had increased over the prior sale amounts, there is no reason to believe or evidence to suggest that the values were artificially inflated. For example, in one case - with **FHA Case Number 493-8959876** - the sales price increased by over \$32,000. The prior sale, however, was a foreclosure sale and may have been underpriced or not reflective of the full market value of the property. A recent retroactive appraisal established an appraised value of \$84,000 in March 2009, when the original appraisal was completed (**Exhibit B**). Notably, the original appraisal in the file established the value at \$86,600 (**Exhibit C**), and, as stated in the Draft Report, the mortgage amount in this case was \$84,550. Thus, there is no reason to believe the property value was artificially inflated.

Comment 11

Lastly, as the Draft Report recognizes in Finding 1, the anti-flipping rule that prohibited resales within 90 days was no longer in effect by the time the OIG concluded its review of Cornerstone. The Department made a conscious decision 4 years ago to withdraw temporarily the 90-day resale restriction.

2. Appraisals Were Performed Timely and Scrutinized Adequately

In Finding 1, the Draft Report also alleges that Cornerstone did not review, or did not review adequately, the appraisal reports in 12 cases. It states that, in 9 of the 12 cases, the appraisals were dated after the loans closed. Specifically, the Draft Report asserts that the appraisals were dated between 3 and 45 days after closing and that Cornerstone's underwriters erroneously certified to HUD that they personally had reviewed the appraisal reports. The Draft Report further contends that, in 6 of the 12 cases, Cornerstone did not review the appraisals adequately to ensure reasonable value. It alleges that there were omissions, errors, and contradictions in the appraisal reports that Cornerstone did not detect.

Cornerstone understands and appreciates a lender's obligations with respect to appraisals. In every case requiring an appraisal, whether it is an FHA transaction

⁴ Only one of the 8 properties was located in a different county - with **FHA Case Number 491-9141680**.



or not, Cornerstone obtains an appraisal report and scrutinizes it prior to closing to verify the property value and other facts about the property. The Company would not be able to sustain its business if it failed to do so.

In the 9 cases where the OIG alleges that the appraisal reports were dated after closing, please note that the appraisals in fact were performed and reviewed prior to closing as required. The same appraiser [REDACTED] with the TriStar Group - performed 8 of the 9 appraisals at issue. In each of these cases, the Draft Report relies on the line titled "Date of Signature and report" for the date on which the appraisal was completed. The dates shown on this line, however, are not the dates the appraisals were completed and the reports issued. According to [REDACTED] and as our records show, whenever this appraiser makes a correction or update to an appraisal, his software automatically updates the "Date of Signature and report" date to reflect the date of the correction or update, despite the fact that the appraisal was performed and issued at an earlier date. Thus, if Cornerstone requests a correction to an appraisal report after funding (a common occurrence among lenders' insuring staff), the "Date of Signature and report" in the corrected report submitted to the Company will reflect the date on which the correction was made rather than the effective date of the appraisal. The date on the report and the invoice from the appraiser, however, both will show the actual date on which the appraisal was completed and the report issued to the Company. This situation was the same in 8 of the 9 cases identified in Finding 1. In the 9th case, all dates reflected on the appraisal report in fact were prior to closing. We address each file as follows:

- **FHA Case Number 493-8447975** - The Draft Report alleges that the loan closed on October 30, 2007, but the appraisal report was dated November 14, 2007. While the appraisal report reflects the date of signature as November 14, 2007, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including its front page and the effective date on page 6, and the invoice from TriStar Group (**Exhibit D**) are dated October 16, 2007, which was prior to the conditional commitment dated October 24, 2007 (**Exhibit E**), and prior to closing on October 30, 2007.
- **FHA Case Number 493-8567176** - The Draft Report alleges that the loan closed on July 8, 2008, but the appraisal report was dated August 11, 2008. Initially, please note that this loan actually closed on August 8, 2008, not July 8, 2008. The Settlement Date of July 8, 2008 reflected on the first page of the HUD-1 Settlement Statement ("HUD-1") is in error and likely was transposed from another document by accident. The executed certifications attached to the HUD-1 all reflect signatures on August 7th and 8th (**Exhibit F**), and the Execution and Notary dates on the Deed of Trust and Warranty Deed reflect a settlement on August 8th (**Exhibit G**). In addition, while the appraisal report reflects the date



Comment 12

Comment 12

Comment 12

of signature as August 11, 2008, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including its front page and the effective date on page 6, and the invoice from TriStar Group (**Exhibit H**) are dated July 16, 2008, which was prior to the conditional commitment dated August 5, 2008 (**Exhibit I**), and prior to closing on August 8, 2008.

Comment 12

- **FHA Case Number 493-8692510** - The Draft Report alleges that the loan closed on July 28, 2008, but the appraisal report was dated August 6, 2008. While the appraisal report reflects the date of signature as August 6, 2008, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including its front page and the effective date on page 6, and the invoice from TriStar Group (**Exhibit J**) are dated June 24, 2008, which was prior to the conditional commitment dated July 8, 2008 (**Exhibit K**), and prior to closing on July 28, 2008.

Comment 12

- **FHA Case Number 493-8693472** - The Draft Report alleges that the loan closed on July 31, 2008, but the appraisal report was dated August 7, 2008. While the appraisal report reflects the date of signature as August 7, 2008, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including its front page and the effective date on page 6, and the invoice from TriStar Group (**Exhibit L**) are dated June 30, 2008, which was prior to the conditional commitment dated July 28, 2008 (**Exhibit M**), and prior to closing on July 31, 2008.

Comment 12

- **FHA Case Number 491-9483914** - The Draft Report alleges that the loan closed on May 1, 2009, but the appraisal report was dated May 25, 2009. While the appraisal report reflects the date of signature as May 25, 2009, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including the front page and the effective date on page 6, and the invoice from TriStar Group (**Exhibit N**) are dated April 20, 2009, which was prior to the conditional commitment dated April 24, 2009 (**Exhibit O**), and prior to closing on May 1, 2009.

Comment 12

- **FHA Case Number 493-8753582** - The Draft Report alleges that the loan closed on August 25, 2008, but the original appraisal report and a second appraisal report were dated after the loan settlement, on August 28 and September 25, 2008, respectively. While the appraisal from TriStar Group reflects the date of signature as September 25, 2008, this date reflects a post-closing update. Both the appraisal report itself, including the front page and the effective date on page 6, and the



invoice from TriStar Group (**Exhibit P**) were dated August 13, 2008. This appraisal report was executed, effective, delivered, and reviewed prior to the conditional commitment, dated August 19, 2008 (**Exhibit Q**), and prior to closing on August 25, 2008. Note also that the second appraisal from Hill & Associates was dated August 14, 2008, and the invoice was dated August 11, 2008 (**Exhibit R**). Thus, this appraisal also was performed prior to closing.

Comment 12

- **FHA Case Number 493-8925706** - The Draft Report alleges that the loan closed on March 6, 2009, but the appraisal report was dated March 12, 2009. While the appraisal report reflects the date of signature as March 12, 2009, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. The appraisal report itself, including the front page and the effective date on page 6, was dated February 28, 2009, and the invoice from TriStar Group was dated February 23, 2009 (**Exhibit S**), both of which were prior to the conditional commitment dated March 2, 2009 (**Exhibit T**), and prior to closing on March 6, 2009.

Comment 12

- **FHA Case Number 493-8480034** - The Draft Report alleges that the loan closed on December 21, 2007, but the appraisal report was dated February 4, 2008. While the appraisal report reflects the date of signature as February 4, 2008, this date reflects a post-closing update. The actual report was executed, effective, delivered, and reviewed prior to closing. Both the appraisal report itself, including the front page and the effective date on page 6, and the invoice from TriStar Group were dated December 3, 2007 (**Exhibit U**), which was prior to the conditional commitment on December 18, 2007 (**Exhibit V**), and prior to closing on December 21, 2007.

Comment 12

- **FHA Case Number 493-8724586** - The Draft Report alleges that the loan closed on August 16, 2008, but the appraisal report was dated August 20, 2008. The appraisal report, however, was dated July 30, 2008, and executed on July 31, 2008 (**Exhibit W**), and the invoice from Market Elite, Inc. is dated July 31, 2008 (**Exhibit X**), which was prior to the conditional commitment dated August 13, 2008 (**Exhibit Y**), and prior to closing on August 16, 2008.

Comment 13

In the 6 cases where the Report alleges the appraisal reports contain deficiencies, we note the indication in the Report that the findings are based on review appraisals performed by an OIG appraiser who conducted physical inspections, researched neighborhoods, and verified comparable sales. Cornerstone, however, has not been privy to these review appraisals or the information underlying them. In each case cited, the underwriter was presented with an appraisal report at the time of loan origination that complied with HUD/FHA



requirements. Nothing on the face of the appraisals suggested erroneous information. While we understand that the OIG's review appraiser may have used different comparable sales or made different adjustments in these cases, that fact does not render the original appraisals invalid. Although an appraiser must follow certain rules in valuing a property, the process is largely subjective. Two different appraisers reviewing the same property may select different comparable sales or make different adjustments, with both appraisers complying with applicable FHA requirements. In the 6 cases cited in the Draft Report, the underwriters reviewed the appraisal reports prior to closing and reasonably determined they were acceptable based on the information available to him or her at the time. We address each of these 6 cases in turn below.

(1) FHA Case Number 493-8547028

Comment 13

In this case, the Draft Report alleges that the appraiser overstated the value of the subject property. This allegation, however, is unsupported. First, please note that Cornerstone obtained 2 appraisals of this property and both reports are contained in the file **(Exhibit Z)**. The Report, however, does not indicate to which of these reports the allegation applies. Moreover, the allegation that the appraiser overstated the value is based on 5 specific comments, none of which are accurate with respect to either appraisal in the file.

- First, the Report alleges that the appraiser did not use comparable property appraisals that were truly representative of the subject property and market conditions at the time of the appraisal. Both appraisers, however, used comparable properties from the immediate neighborhood, all of which closed within the most recent 6-month period and all of which were similar in style, design, size, and finish.
- Second, the Report alleges that the appraiser did not verify, document, and make adjustments for seller concessions for comparable property appraisals 1, 2, and 3. Both appraisers, however, made comments regarding their philosophies on sales concessions. One appraiser - [REDACTED] - adjusted for any concessions over the 3% she considered typical for the area. The other appraiser - [REDACTED] - adjusted for any concessions over the 6% he considered typical for the area.
- Third, the Report alleges that the appraiser included 2 comparable property appraisals that required excessive adjustments, which decreased the reliability of the comparable property appraisals. Notably, however, only one comparable property on either appraisal falls outside the preferred criteria - the property located at [REDACTED] [REDACTED], on which both appraisers relied. This property had a square footage adjustment over the preferred 10%, which brought the net and



gross adjustments over the preferred 15%/25%, but both appraisers addressed this issue in their reports.

- Fourth, the Report alleges that the appraiser did not disclose the correct number of bathrooms in the subject property, leading to incorrect adjustments to the comparable property appraisals. While [REDACTED] appraisal incorrectly noted only one bathroom in the subject property, the photographs attached to [REDACTED] appraisal show both bathrooms. The error in [REDACTED] appraisal, however, constituted at worst harmless error. All of the comparables used in that appraisal had one bathroom. Any adjustment for bathrooms, thus, would have required a positive adjustment to all of the comparable properties, thereby increasing the value of the subject property.
- Last, the Report alleges that the appraiser made site adjustments with no support or documentation. Both appraisers, however, commented on their site adjustments, and [REDACTED] noted that he adjusted based on site utility, lot costs, and market value.

Not only does the Report fail to identify with which appraisal report it is concerned in this case, but none of the contentions underlying its conclusion that the property was overvalued are supported. The appraisal reports in the file comply with HUD/FHA requirements and contain all required information. The underwriter properly scrutinized them prior to closing, and there is no reason to believe or evidence to support that the property was overvalued.

(2) FHA Case Number 493-8692510

In this case, the Draft Report alleges that the appraiser overstated the value of the subject property based on 4 comments. These comments, however, are unsupported.

First, the Report alleges that the appraiser did not measure and calculate properly the gross living area of the subject property. We are uncertain of the basis for this assertion. All information in the appraisal report (**Exhibit J**) indicates the square footage of 1,168 is correct. The sketch includes the calculations for the square footage and the math is calculated accurately.

Second, the Report alleges that the appraiser selected comparable properties that were not truly comparable to the subject property. The appraiser, however, used 6 comparables, all of which have minimum adjustments, are within close proximity, are recent sales, and are similar in age and amenities. The appraiser also certified that he had "completed a market study and chose the most representative available sales."



Comment 13

Third, the Report alleges that the appraiser did not analyze and disclose amenities of comparable property appraisals. The amenities, however, appear to be fully disclosed and analyzed in the appraisal report, and nothing in the report or elsewhere in the file supports the OIG's allegation.

Finally, the Report alleges that the appraiser did not make proper adjustments for dissimilarities between the subject property and the comparable properties. The only dissimilarity for which there is no adjustment is the site adjustment for comparable properties 2 through 5. In the appraisal report, however, the appraiser stated that "Lot size adjustments are based on market abstraction via matched paired analysis whenever possible and/or were applied at the rate of \$0.25 per sqft for differences greater than +/- 4000 sqft." Based on this information from the appraiser, comparable property 1 would not need any adjustment. Comparable properties 5 and 6 were listings pending sale. Thus, adjustments need not have been applied because they were not the focus of the value and were offered only in support. Comparable properties 2 through 4 should have received an adjustment barring any other influences. While comparable properties 3 and 4 were both located on the same street, the street was a thoroughfare with commercial influences and backed to a contributory to a bayou, thereby making the area a prime candidate for flooding. The site adjustments and their corresponding adjusted sales prices are as follows: (1) \$1,833 site adjustment to comparable property 2, yielding a final adjusted sales price of \$77,487; (2) \$9,097 site adjustment to comparable property 3, yielding a final adjusted sales price of \$63,403; and (3) \$8,916 site adjustment to comparable property 4, yielding a final adjusted sales price of \$84,401. These adjustments create a final adjusted sales price range between \$63,403 and \$84,401. As the value of the subject property was originally established at \$73,500, the appraised value was well within the acceptable range.

(3) FHA Case Number 493-8693472

Comment 13

In this case, the Draft Report alleges that a second appraisal should have been obtained and that the appraiser overstated the value of the subject property. These assertions are incorrect.

The Report suggests that Cornerstone should have obtained a second appraisal because the property was purchased for \$60,000 and resold for \$119,000. FHA guidelines, however, did not require as much. FHA guidelines state that a lender must obtain a second appraisal by a different appraiser if the resale price is 100% or more above the seller's acquisition price. See Mortgage Letters 2006-14 and 2009-48; HUD Handbook 4155.2 4.7.f. Here, while the resale price was only \$1 less than double the acquisition price, it was still less than 100% and a second appraisal was not required.

The Report also alleges that the appraiser overstated the value of the subject property because the appraiser did not accurately calculate the square footage, used inappropriate comparable properties, and did not make proper adjustments. It also



contends that the appraiser would have arrived at a different value conclusion more representative of the predominate value of properties in the neighborhood had the appraisal been performed properly. To this end, the Report states that the appraiser valued the property at \$120,500, but that the OIG's review appraisal showed the potential comparables ranged only from \$79,500 to \$99,000 and averaged about \$90,000. These assertions are unsupported.

Our review of the appraisal (**Exhibit L**) reflects accurate calculation of the square footage and selection of appropriate comparable properties with minimal adjustments needed and limited dissimilarities. The property condition is not in question given the information and pictures contained in the appraisal report and, while the value exceeds the predominant value in the neighborhood, the appraiser commented on this issue. Specifically, the appraiser noted that, while the estimated market value is above the predominant value for the market area, "it is well within the neighborhood's range. It is not considered an over improvement, but the result of being one of the larger homes and average/updated condition in the market area." Cornerstone scrutinized the appraisal report prior to closing and, for the reasons above, reasonably determined that the appraisal complied with FHA requirements and accurately reflected the property value. The fact that the OIG's review appraiser may disagree with the individual who originally appraised the property does not mean that the original appraisal was invalid. It complied with FHA requirements and Cornerstone properly reviewed and analyzed it.

(4) FHA Case Number - 493-8532052

In this case, the Draft Report alleges that the appraiser overstated the value of the subject property because the appraiser did not properly measure and calculate the gross living area of the subject property, used inappropriate comparable properties, and did not make proper adjustments for the foundation and electrical hazards that required further inspection, testing, and repairs. It also contends that the appraiser would have arrived at a different value conclusion had the appraisal been performed properly. To this end, the Report states that the appraiser valued the property at \$97,000, but that the OIG's review appraisal showed 6 comparable property appraisals ranging only from \$44,000 to \$78,500 and averaging about \$62,000. These assertions are unsupported.

Our review of the appraisal (**Exhibit AA**) reflects accurate calculation of the square footage and selection of appropriate comparable properties with typical adjustments that bracket the subject property in price. While the value exceeded the predominant value in the neighborhood, the upper range of value was only 15% above the predominant value, and the appraiser commented on this issue. Specifically, the appraiser stated that, although the estimated market value is above the predominant value for the market area, "it is well within the neighborhood's value range. It is not considered an over improvement, but the result of being one of the larger homes and in average/updated condition in the market area." There were no



Comment 13

indications of any foundation or electrical issues in the appraisal report or photographs, and Cornerstone had no reason to question the information presented in the appraisal report. Cornerstone scrutinized the appraisal report prior to closing and, for the reasons above, reasonably determined that the appraisal complied with FHA requirements and accurately reflected the property value. The fact that the OIG's review appraiser may disagree with the individual who originally appraised the property does not mean that the original appraisal was invalid. It complied with FHA requirements and Cornerstone properly reviewed and analyzed it.

(5) FHA Case Number - 493-8558066

Comment 13

In this case, the Draft Report alleges that the appraiser overstated the value of the subject property because the appraiser did not properly measure and calculate the gross living area of the subject property, used inappropriate comparable properties, and did not make proper adjustments for dissimilarities or for the foundation and problems that required further inspection, testing, and repairs. The Report states that its appraiser determined that the lender should have questioned several omissions between the photographs and adjustments made by the appraiser, and that the lender's appraiser valued the property at \$80,000 when the value should not have exceeded the predominant value of \$50,000 for the neighborhood.

Our review of the appraisal (**Exhibit BB**) in this case reflects accurate calculation of the square footage and selection of appropriate comparable properties. The comparables had exceptionally low adjustments, with square footage adjustments only for two of them and no adjustments exceeding 10%. The comparables also bracketed the subject property in price and square footage. While the value exceeded the predominant value for the neighborhood, the appraiser commented on this issue. Specifically, the appraiser stated that, although the estimated market value is outside the predominant value for the market area, "it is well within the neighborhood's range. It is not considered an over improvement, but he result of being one of the average homes and in average/updated condition in the market area." There were no indications of any foundation or other problematic issues in the appraisal report or photographs, and Cornerstone had no reason to question the information presented in the appraisal report. Cornerstone scrutinized the appraisal report prior to closing and, for the reasons above, reasonably determined that the appraisal complied with FHA requirements and accurately reflected the property value. The fact that the OIG's review appraiser may disagree with the individual who originally appraised the property does not mean that the original appraisal was invalid. It complied with FHA requirements and Cornerstone properly reviewed and analyzed it.

(6) FHA Case Number 493-8480034

Comment 13

In this case, the Draft Report alleges that the appraiser overstated the value of the subject property because the appraiser did not properly measure and calculate the gross living area of the subject property, used inappropriate comparable



properties, and did not make proper adjustments for dissimilarities or for the foundation, electrical conditions, termite damage, and other matters requiring further inspection, testing, and repairs. The Report states that its appraiser determined that the lender should have questioned several omissions between the photographs and adjustments made by the appraiser, and that the lender's appraiser would have arrived at a different value conclusion had the appraisal been performed properly. It states that the lender's appraiser valued the property at \$148,000, while the OIG's appraiser's comparables of equal condition and value sold for substantially less.

Our review of the appraisal (**Exhibit U**) in this case reflects accurate calculation of the square footage and selection of appropriate comparable properties. The comparables had exceptionally low adjustments, with the first 2 having no adjustments and comparables 3 through 6 having very minimal adjustments and all within the preferred guidelines. The comparables also bracketed the subject property in price and square footage. The OIG's suggestion that the appraiser chose comparables in the upper range is inconsistent with the fact that the appraised value of \$148,000 was below the predominant value in the neighborhood. Moreover, at the time of appraisal, there were no indications of foundation, termite, electrical, or other issues in either the appraisal report or the photographs attached to it. Cornerstone had no reason to question the information presented in the appraisal report. Cornerstone scrutinized the appraisal report prior to closing and, for the reasons above, reasonably determined that the appraisal complied with FHA requirements and accurately reflected the property value. The fact that the OIG's review appraiser may disagree with the individual who originally appraised the property does not mean that the original appraisal was invalid. It complied with FHA requirements and Cornerstone properly reviewed and analyzed it.

3. Assets and Income Were Verified

Lastly, Finding 1 contends that Cornerstone did not verify or calculate adequately the borrowers' income and source of funds in 4 cases. Specifically, it alleges that, the underwriter used unsupported income in one case, miscalculated income in 2 cases, and did not verify the source of a large deposit to the borrower's bank account in one case. Cornerstone respectfully disagrees with these assertions. The Company's underwriters understand and appreciate that a lender must verify 2 years of employment and the stability of borrower income. See HUD Handbook 4155.1, Chapter 4, Section D. It is Cornerstone's policy and practice to comply with income and asset requirements in all FHA loans, and we maintain that the Company did so in the 4 loans cited in Finding 1. Our individual responses to these cases are set forth below.

(1) FHA Case No. 493-8447975

In this case, Finding 1 alleges that the lender used unsupported income to qualify the borrower. Specifically, it alleges that the borrower was no longer

Comment 1



Comment 14

employed and that the income, therefore, was incorrect. It states that the lender obtained income documentation, including pay stubs and a Verification of Employment (“VOE”), but ignored the VOE, which stated that it was for prior employment and showed salary, the probability of continued employment, and the probability of bonus and overtime income all as zero.

Contrary to the suggestion in this case, the borrower’s employment was ongoing and the income stable in this case. As stated in the Draft Report, Cornerstone obtained a verbal VOE and pay stubs to verify the borrower’s employment prior to closing. The notation on the verbal VOE that the employment was “Previous” was a typographical error by the CHL production assistant who executed the form. This fact was clear at the time given that there was no ending date on the VOE for the employment noted (**Exhibit CC**) and that the most recent pay stub was dated October 5, 2007 (**Exhibit DD**), less than a week before the verbal VOE was obtained. In addition, the probability of continued employment, bonus, and overtime were not shown as “zero” as suggested by the OIG; rather, their line items reflect “Ø” as a means of indicating that the employer’s representative who verified the employment by telephone was unable to provide those specific pieces of information, which is commonly the case when lenders verify employment by telephone. The reflection of “Ø” in those fields by no means suggests that the borrower was not employed at the time and, again, the lack of an end date on the verbal VOE and the dates on the pay stubs confirmed current employment. What’s more, please note that Cornerstone has obtained a current verification from the employer confirming that the borrower in fact was still employed at the time of closing (**Exhibit EE**).

(2) FHA Case No. 493-8567176

Comment 15

In this case, Finding 1 alleges that the income calculation was based on an hourly rate of \$17 per hour for 40 hours per week when the pay stubs showed the borrower worked an average of only 35 hours per week. Finding 1 suggests that the borrower’s mortgage payment-to-income ratio, therefore, was 44%, which exceeded HUD’s 31% maximum, and there were no compensating factors to justify the excess.

Cornerstone recognizes that the underwriter inadvertently used a 40-hour work week instead of a 35-hour work week to calculate the borrower’s income. This mistake was unintentional, however, and does not reflect any effort to approve financing to an unqualified borrower. Moreover, the error was harmless and the borrower still qualified for the FHA loan. Using a 35-hour work week, and based on the borrower’s hourly rate of pay on his pay stubs, the borrower’s income would be \$2,578 per month (i.e., \$17 per hour x 35 hours per week x 52 weeks per year / 12 months) (**Exhibit FF**). Thus, the qualifying ratios would be 39.06% and 39.06% (**Exhibit GG**). Although the front-end ratio exceeded HUD’s benchmark guideline at the time, significant compensating factors justified loan approval. Specifically, the borrower had no monthly debts or obligations (**Exhibit GG**), and the non-purchasing



spouse received income from both employment and child support that was not used to qualify the borrower for the loan and that would assist greatly with their household expenses (**Exhibit HH**). The receipt of income not reflected in effective income was a compensating factor that HUD expressly permitted to justify ratios exceeding the benchmark guidelines, not to mention that HUD expressly permitted greater latitude on the front end ratio, see HUD Handbook 4155.1 4.F.3.b. and old HUD Handbook 4155.1 REV-5, 2-12, 2-13, and the borrower qualified for FHA financing in this case.

(3) FHA Case No. 493-8959876

Comment 16

In this case, Finding 1 alleges that there was a \$4,000 increase to the borrower's bank account for which the lender did not obtain a credible explanation. This assertion is incorrect.

In compliance with FHA requirements, it is Cornerstone's policy and practice to obtain an explanation of the source of funds for any large increase in a borrower's bank account. See old HUD Handbook 4155.1 REV-5, 2-10(B). In this case, the deposit funds were derived from a \$7,000 tax refund. The coborrower filed her 2008 tax return on January 27, 2009 and received a refund of over \$7,000 (**Exhibit II**). These funds were the source of the \$4,000 deposit a few days later on February 6, 2009. Cornerstone properly verified the source of the increase in the borrower's bank account.

(4) FHA Case Number 493-8480034

Comment 15

In this case, Finding 1 alleges that the lender miscalculated the borrower's income because it was based on 2 40-hour work weeks, while the most recent pay stubs showed that the borrower worked only 24 hours. It states that, based on year-to-date income, the borrower's ratios would be 32% and 52% without any compensating factors to justify loan approval with ratios exceeding HUD's benchmark guidelines. These allegations are incorrect.

The borrower in this case worked for Fisk Electric at the time of closing in December 2007; he had worked there previously from March 9, 2006, through March 14, 2007, left to work for Britton from March 15 through August 8, 2007, and then returned to Fisk on August 8, 2007, where he remained through the date on the VOE on December 5, 2007 (**Exhibit JJ**). Over the last 4 months that the borrower had worked for Fisk, he earned an average of \$4,553 per month, as reflected by his total earnings on the VOE between August 8 and December 5, 2007 (i.e., \$18,212.88 / four months). The year-to-date earnings on the borrower's pay stub dated December 9, 2007 is \$34,462 (**Exhibit KK**). This sum, however, covers all earnings from Fisk for the entire year. As the borrower had worked for Britton from March 15 through August 8, 2007, the \$34,462 covered only 6.54 months at Fisk (January 1 through March 14, 2007, and August 8 through December 9, 2007), thereby yielding an average of \$5,269 per month. Notably, and consistent with the information on the VOE, Cornerstone used a more conservative number of about \$4,500 when



Comment 15

approving the borrower for financing (**Exhibit LL**), rather than the higher average reflected on the borrower's pay stub. The lower income yielded qualifying ratios of 24% and 38%, which were below HUD's benchmark guidelines. Cornerstone did not miscalculate the borrower's income, the borrower's qualifying ratios were below HUD's benchmark guidelines, and the borrower qualified for FHA financing.

C. FINDING 2 - CORNERSTONE COMPLIED WITH RESPA

In Finding 2, the Draft Report alleges that 2 former marketing agreements violated RESPA. The allegations, however, are at variance with the legal requirements affecting marketing agreements in particular, and RESPA generally.

The Report alleges that Cornerstone ignored and violated RESPA requirements because it "executed \$382,500 in marketing agreements with realtors." It states that the agreements violated RESPA because they provided for the realtors' exclusive promotion of Cornerstone's mortgage products and programs through display and distribution of promotional and marketing materials at the realtors' sales offices and through an exclusive rental arrangement whereby Cornerstone was the only mortgage lender with a presence on site at the realtors' offices. The Report alleges that, when borrowers came into the realtor's office, they were directed to Cornerstone employees for mortgage services, which restricted their ability to shop for other lenders and may have increased the costs of settlement services. The Report also alleges that one of the marketing agreements resulted in a prohibited conflict of interest because one of Cornerstone's branch managers was a principal in the realty company.

Comment 6

All of the foregoing allegations are erroneous. They are unsupported by either the facts or the law, and they are offensive. The Draft Report gives the impression that Cornerstone paid real estate brokers for referrals and violated a consumer protection statute, but that is not the case. Under the two former marketing agreements at issue here, Cornerstone made reasonable monthly payments to two real estate brokers in return for actual promotional services performed. The payments were for services rendered, not for referrals, and the payment amounts remained the same regardless of the value or volume of business derived under the arrangements. Consumers were not required to use Cornerstone for mortgage financing, and consumer pricing was not affected in any way. After the 2 agreements at issue here were terminated, HUD issued specific guidance related to marketing agreements that changed the way the industry approaches marketing arrangements in some respects. The agreements in this case, however, were executed and terminated before HUD issued the guidance and they complied with RESPA requirements and regulatory guidance at the time. Moreover, there was no conflict of interest in connection with either agreement. Finally, both agreements were terminated 4 and 5 years ago, HUD is no longer responsible for RESPA implementation and enforcement, and the statute of limitations for any government enforcement action has run. Given these facts, as explained more fully below, the



recommendations to HUD in the Report are inappropriate, and we respectfully request that the OIG remove Finding 2 from its final report.

1. Marketing Agreements are Permissible Under RESPA and Cornerstone's Former Agreements Complied with Section 8

Comment 1

Contrary to the suggestion in the Draft Report, at no time did Cornerstone ignore or violate RESPA requirements or guidelines. Just the opposite - the Company worked hard to ensure its marketing arrangements complied with RESPA, and the agreements referenced in the Draft Report complied with statutory and regulatory requirements and HUD guidance at the time.

The Draft Report states that Cornerstone violated RESPA requirements in August 2007 and May 2008 when it executed marketing agreements with realtors. RESPA, however, does not prohibit marketing agreements, and regulators expressly have stated that they are permissible. While Section 8(a) prohibits giving or receiving anything of value in return for referrals of settlement service business, see 12 U.S.C. § 2607(a), Section 8(c)(2) provides that a reasonable payment in return for actual goods, facilities, or services is an exception to the Section 8(a) prohibition. See 12 U.S.C. § 2607(c)(2); 24 C.F.R. § 3500.14(g)(iv).⁵ This exception covers payments for marketing or advertising and serves as the basis for marketing agreements between settlement service providers. Regulators consistently have taken the position, that Section 8(c)(2) allows payments for marketing services in a manner that does not bear on the amount of business referred. See, e.g., HUD Informal Advisory Opinions, dated May 31, 1985 and December 11, 1986, by Grant E. Mitchell; HUD Informal Advisory Opinions, dated April 11 and 24, 1986, by John J. Knapp.⁶

Until June 2010, after the marketing agreements at issue here were terminated, HUD was fairly silent on the issue of marketing agreements and the foregoing guidance provided the benchmark for settlement service providers. Thus, the mere fact that Cornerstone had marketing agreements with realtors did not mean that it paid the realtors for referrals or violated RESPA, and according to HUD at the time, the marketing agreements were permissible if the realtors performed real work in return for reasonable compensation that was not tied to the number of referrals. Cornerstone's agreements satisfied these criteria.

⁵ At all times relevant to the OIG audit, HUD was still responsible for implementing and enforcing RESPA. Thus, although the Consumer Financial Protection Bureau ("CFPB") now has such responsibility, we refer throughout this response to HUD's citations and regulatory guidance in effect at the time the audit was conducted and which would be applicable to the marketing agreements at issue here.

⁶ Current HUD officials recognize that "Section 8(c) of RESPA and HUD's regulations allow payment of bona fide compensation for services actually performed" and "allow persons in a position to refer settlement service business to receive payments for providing additional compensable services as part of a transaction." 75 Fed. Reg. 36271, 36272 (June 25, 2010).



The Draft Report references two former marketing agreements, one between former Branch 87 and HomeVestors of America, Inc. ("HomeVestors"), and one between former Branch 87 and EGDG, LLC ("EGDG"). In both cases, as required by Section 8(c)(2) and, thus, as permitted under RESPA, the realtors performed actual, necessary, and distinct marketing services for Cornerstone in return for which Cornerstone paid reasonable fees consistent with the fair market value of the services rendered.

Under the HomeVestors agreement, which was executed in May 2008, HomeVestors agreed to: market and advertise Cornerstone to HomeVestors' franchisees; advertise Cornerstone's mortgage loan products and services in its monthly newsletter and on its Internet-based portal; invite Cornerstone to attend annual and mid-year conventions and summits; and allow Cornerstone to attend training programs and other appropriate functions. In return for these services, Cornerstone agreed to pay a one-time set-up fee and monthly fees. Similarly, under the EGDG agreement, which was executed in August 2007, EGDG agreed to: promote Cornerstone at its office locations and to its sales agents and customers; add a link to Cornerstone's website and additional advertising on EGDG's website; provide Cornerstone with access to customers and agents to explain its mortgage programs and products; invite Cornerstone to attend realtor-sponsored open houses and other functions and activities; allow Cornerstone to provide agent training; install promotional signage; include Cornerstone in its print advertisements; display Cornerstone related customer flyers and brochures; engage in co-marketing; and provide office space. In return for these services, Cornerstone agreed to pay a monthly fee.

Both the HomeVestors agreement and the EGDG agreement required the realtors to perform services that were actual, necessary and distinct from the work they otherwise would perform. The services were general marketing functions distinct from individual transactions for which compensation was due. The monthly payments by Cornerstone were in return for these services, not in return for referrals, and the payments were unrelated to the volume or value of business derived under the arrangements. Section 8(c)(2) of RESPA allows reasonable payments for actual services rendered, which is what occurred in this case, and Cornerstone's former marketing arrangements complied with the Act.

2. RESPA Does Not Prohibit Exclusivity Arrangements

The Draft Report alleges that Cornerstone's marketing agreements violated RESPA because they provided for the realtors' exclusive promotion of the Company and exclusive rental arrangements. The Report states that "Section 8(a) of RESPA prohibits paying marketing fees to realtors in exchange for exclusive rights." This assertion is untrue. Nowhere does Section 8(a) make any such statement. Section 8(a) provides:



No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.

12 U.S.C. § 2607(a). Section 8(a) does not mention marketing agreements, let alone the issue of exclusivity. Regulation X likewise is conspicuously silent on these matters. It was not until June 2010, after the Company's marketing agreements were terminated, that the Department issued an interpretive rule expressing a preference that marketing agreements do not contain exclusivity provisions. See <http://edocket.access.gpo.gov/2010/pdf/2010-15355.pdf>. HUD's preference, however, does not constitute a law or regulation, and the mere presence of an exclusivity provision in a marketing agreement does not render the agreement illegal. In fact, HUD itself did not even assert that exclusivity is prohibited by RESPA; rather, it stated that, in evaluating a payment by a home warranty company to a realtor, HUD "may" consider whether there is an exclusive arrangement and whether and how the arrangement impacts the pricing. See <http://edocket.access.gpo.gov/2010/pdf/2010-15355.pdf>. While HUD's statement of this preference has influenced how settlement service providers do business since June 2010, this preference was not espoused during the terms of the HomeVestors and EGDG agreements, and there is no prohibition against exclusivity.

Additionally, contrary to the suggestion in the Report that an exclusive rental arrangement violates RESPA, HUD made a public statement that exclusive rental arrangements are permissible under the Act. On June 7, 1996, HUD issued RESPA Statement of Policy 1996-3, in which HUD explained its interpretation of Section 8 of RESPA with regard to the rental of office space and lock-outs. HUD noted in the policy statement that RESPA permits a real estate broker to rent office space to a lender if the lender pays a general market value rent. HUD also noted that a lock-out situation, where a settlement service provider prevents other providers from marketing their services within a particular setting or rents space to one provider to the exclusion of other providers so that others are effectively "locked out" from access to the referrer of business and consumers, does not alone give rise to a RESPA violation. HUD went even further to state that RESPA does not give HUD authority to regulate access to the offices of settlement service providers. The interpretive rule discussed above does not address lock-outs or exclusive rental arrangements, and HUD's former guidance was never retracted.

Given all of the foregoing guidance, the mere fact that a marketing agreement provides for a realtor's exclusive promotion of a lender's products and programs does not suggest that the lender pays the realtor for referrals or is in violation of RESPA. Likewise, the fact that a lender has an exclusive rental arrangement with a realtor is not alone sufficient to trigger a RESPA violation. Nevertheless, we note that only one of the two former agreements in this case contained an exclusivity provision - the



EGDG agreement. The HomeVestors agreement did not contain an exclusivity provision and, instead, expressly stated that HomeVestors would be marketing other lenders and that the contract was executed on a “non-exclusive” basis. We further note that, at no time were customers required to use Cornerstone. Although Cornerstone maintained a presence in the realtors’ offices, customers were always free to select the mortgage provider of their choice. Moreover, customer costs were unaffected by the marketing arrangements. Every Cornerstone customer paid the same fees that he or she would have paid in connection with mortgage financing had there been no marketing agreements in place.

3. Cornerstone Did Not Pay Marketing Fees in Connection with Individual Loans, Although RESPA Does Not Prohibit Transaction-Based Compensation

The Draft Report states that Cornerstone paid marketing fees “in connection with Cornerstone’s origination and processing of 31 defaulted FHA-insured mortgages.” This statement is incorrect.

Comment 6

Cornerstone did not pay any marketing fees to any realtors in connection with its origination and processing of any mortgage loans. As explained above, the Company paid reasonable monthly fees in return for actual promotional services performed. The payments were not tied to individual transactions and the fees remained the same regardless of how many loans Cornerstone originated or how much business it derived from the arrangement.

That being said, we note that RESPA does not prohibit transaction-based compensation. Nothing in the statute or implementing regulation discusses compensation methods, and there is little regulatory guidance on the subject. Section 8(c)(2), however, allows payments of bona fide compensation for actual services performed and HUD expressly stated in its 2010 interpretive rule that, if a real estate broker or agent performs actual compensable services in a transaction, “transaction-based compensation of that broker or agent that is reasonable would not be an indicator of an unlawful referral arrangement and would be permissible.” See <http://edocket.access.gpo.gov/2010/pdf/2010-15355.pdf>. In this instance, however, as explained above, Cornerstone did not make any transaction-based payments. It paid only monthly fees in return for general services under both agreements.

4. The Marketing Agreements Were Terminated 4 and 5 Years Ago

Comment 3

Finally, please note that the HomeVestors and EGDG agreements were terminated four and five years ago in December 2009, and April 2010, respectively. The OIG has been aware of the agreements since April 2010, and the statute of limitations for any government enforcement action pursuant to Section 8 is three years from the date of the occurrence of the violation. See 12 U.S.C. § 2614. Thus,



no government enforcement action could or should be brought against Cornerstone in connection with these former agreements.

5. There Was No Conflict of Interest

Comment 6

Lastly, Finding 2 alleges that one of Cornerstone's marketing agreements violated FHA's conflict of interest provision because one of its branch managers was a principal in a realty company. Specifically, it alleges that this individual claimed to run and own both a Cornerstone branch and a hard money company. The Draft Report further asserts that Cornerstone's Quality Control reports used this individual's name to describe a branch office, although Cornerstone officers have denied the individual worked for the Company, and that Cornerstone originated loans from a location that housed businesses owned by this individual. The Report contends that this information demonstrates a violation of the FHA regulation that prohibits a lender from paying anything of value in connection with an FHA loan to an individual who receives other consideration from the mortgagor, seller, builder, or any other person for services related to the transaction or the purchase and sale of the property. See 24 C.F.R. § 202.5(l). The Report further suggests that Cornerstone submitted erroneous certifications to HUD effectively hiding the conflict of interest.

First, if in fact a branch manager at Cornerstone also owned a realty company, this dual role would not have violated FHA requirements. While FHA guidelines state that employees must be exclusively employed by the mortgagee in the mortgage lending and real estate fields, see HUD Handbook 4060.1 REV-2, ¶ 2-9(A), they specifically state that officers, including Branch Managers, may be owners, officers, partners, or members of other entities. See HUD Handbook 4060.1 REV-2, ¶ 2-9(B), (C). Thus, if a Cornerstone Branch Manager did own an interest in a hard money company, the dual ownership alone would not violate FHA requirements.

Comment 17

That being said, the factual assertions in the Report are incorrect. The referenced individual was never a Cornerstone employee. If he stated otherwise in advertisements or elsewhere, then he misrepresented his status. He was never a Company employee and Cornerstone never represented that he was.⁷ The OIG is aware of that fact and, thus, its language in the Draft Report is prejudicial and inflammatory. Furthermore, the suggestion that Cornerstone submitted erroneous certifications to HUD in an effort to hide a conflict of interest that the OIG knows did not exist is both provocative and untrue. Cornerstone did not condone the individual's misstatements and neither participated in nor had any control over how he advertised himself. Its certifications to the Department were forthright and accurate. Moreover, we have scoured our Quality Control files and have been unable to find any references to any offices that include the individual's name. One office, located at 14515 Briarhills Parkway, was referred to as the W. Houston office. The

⁷ At one time, Cornerstone contemplated entering into a joint venture arrangement to create a new business with the individual, but the arrangement was never consummated.



other office, located at 15735 North Freeway, was referred to as the Richey Road office. To our knowledge, there were no businesses at either location other than Cornerstone's mortgage loan business.

Finally, the conflict of interest provision cited in the Draft Report would not apply to the current situation even if the individual had been a Cornerstone employee. Section 202.5(l) prohibits a mortgagee from making payments to an individual in connection with an FHA-insured transaction if such individual will receive other compensation from an interested party in connection with the same transaction. Cornerstone takes care to comply with this requirement in all cases and prohibits its employees from maintaining employment in other real estate related fields. In this instance, however, the Report is suggesting that a marketing agreement somehow violated Section 202.5(l). Again, this provision refers to payments in connection with insured transactions. The marketing agreements, however, provided for monthly payments for services rendered regardless of whether or how many individual transactions were derived under the arrangement. Cornerstone did not pay any marketing fees in connection with individual transactions and Section 202.5(l) does not apply to the situation at hand. Nevertheless, again, the referenced individual was not an employee of Cornerstone.

D. FINDING 3 - QUALITY CONTROL

In Finding 3, the Draft Report alleges that Cornerstone did not always comply with HUD's Quality Control requirements during the review period. Specifically, it alleges that, for a one-year period between September 2008 and August 2009, Cornerstone did not (1) conduct timely Quality Control reviews, (2) timely review all early payment default and rejected loans, (3) conduct timely onsite reviews or include all required review items, or (4) follow reverification requirements. The Draft Report further alleges that Cornerstone did not demonstrate that it took corrective actions in a timely manner. It contends that these conditions occurred because Cornerstone's Quality Control Plan conflicted with HUD regulations and its review process was inaccurate.

Comment 18

The OIG reviewed a Quality Control Plan that Cornerstone used 5 to 7 years ago, not the Quality Control Plan that it uses today. The language in the Draft Report gives the wrong impression to readers that Cornerstone does not have or abide by a compliant Quality Control Plan. By drafting findings based on an outdated plan that the Company has not used in over 5 years, and citing loans and activities from 6 and 7 years ago, the OIG unfairly prejudices the Company. In determining the reliability of an entity's compliance program and adequacy of Quality Control reviews, the relevant question is whether the entity is currently complying with current rules, or perhaps even whether it has been in compliance over the past couple of years. A review of an outdated plan and an entity's activities 6 and 7 years ago does not provide an accurate or useful view of the entity's compliance posture.



During the Company's exit conference with the OIG on March 6, 2014, OIG representatives recognized that they had reviewed an outdated plan that is no longer in effect and that does not reflect Cornerstone's current operations. Thus, OIG representatives agreed that it may be appropriate to remove this Finding 3 before issuing any final report. To this end, enclosed please find a copy of Cornerstone's current Quality Control Plan (**Exhibit MM**), which we believe includes all required items and accurately reflects the Company's current Quality Control processes and review procedures. For these reasons, and as explained in greater detail below, Cornerstone respectfully requests that the OIG remove Finding 3 before issuing any final report.

That said, please note that, contrary to the suggestion in the Draft Report that Cornerstone had an inadequate review process in place, the Company always has maintained a rigorous Quality Control and compliance program. Its Quality Control department has grown from 7 employees in 2008, and 16 employees in 2009, to 26 employees currently. These individuals have been removed from loan origination, processing, and underwriting functions and have been dedicated to Quality Control and compliance matters. While there may have been occasional delays in reviewing files due to increased workloads at different times, or a handful of documents that the Company could not locate by the time the OIG conducted its audit, the Draft Report gives a misimpression that Cornerstone shirked its Quality Control responsibilities when that simply is not the case. We address each issue raised in Finding 3 in turn below.

1. Timely Quality Control Reviews

The Draft Report alleges that, while Cornerstone performed reviews on 10% of loans that closed monthly (as it was supposed to do), it did not complete the reviews in a timely manner (within 90 days of closing). To this end, it states that Cornerstone did not complete reviews of loans that closed between December 2008 and April 2009 until 4 to 7 months after the loans closed.

Cornerstone understands and appreciates that Quality Control reviews are to be completed within 90 days of closing, see HUD Handbook 4060.1 REV-2, ¶ 7-3(D), and it always has been the Company's policy and practice to do so. The OIG references only a 4-month period in the Company's 26-year operational history when loan reviews were delayed. Notably, the reviews were delayed during these months because Cornerstone was in the process of shifting the Quality Control review function from an internal process to a third-party vendor. At that time, the Company ceased performing Quality Control reviews in-house and began to outsource the reviews to The StoneHill Group, Inc. ("StoneHill"). During this brief transition period, reviews were delayed by a couple of months. StoneHill, however, did review of all the files for which reviews were required.

Comment 19



2. Early Payment Defaults and Rejected Loans

The Draft Report also alleges that Cornerstone did not review 11 early payment default loans, did not review 25 early payment default loans timely, and did not review 51 loans that Branch 87 rejected.

First, with respect to early payment defaults, it always has been Cornerstone's policy and practice to review all loans that become 60 days or more delinquent within the first 6 months as required. See HUD Handbook 4060.1 REV-2, ¶ 7-6(D). Like other loan originators that sell their loans servicing-released, however, it can be difficult to identify such loans. To do so, Cornerstone relies on HUD's Neighborhood Watch. The Queries screen on the Neighborhood Watch home page has an option for Default Cases that allows a lender to view those loans reported as 60 days past due in the past 12 Single Family Default Monitoring system ("SFDMS") reporting cycles. After obtaining loan-level 60-day results, the lender can determine which cases became 60 days past due in the first 6 payments by using the "# of payments before first 90-day def reported" column. If the borrower made 5 or fewer payments before the first 90-day default, then that means there was a 60-day default in the first 6 payments. A lender also may click on individual case numbers on the 60-day report to review the recent default history reported by the servicer in the SFDMS. See <https://entp.hud.gov/sfnw/public/help-FAQ.cfm#18>. The accuracy and timeliness of the data supplied in Neighborhood Watch, however, is dependent on timely reporting by servicers to the SFDMS. If a servicer does not report the status of a loan timely, then the loan may not appear in the 90-day default report and the report being used by the loan originator to identify early payment defaults will not capture all of the early payment defaults the lender should review. When this occurs, the lender will be unable to identify and review all of the early payment defaults, or will be unable to review them timely. Thus, the fact that it took several months to review some of the early payment default files in no way suggests a lack of adequate Quality Control or care on Cornerstone's part.

With respect to rejected loans, FHA guidelines direct lenders to review a minimum of 10% (or a statistical random sampling that provides a 95% confidence level with 2% precision) of "the total loans rejected." See HUD Handbook 4060.1 REV-2, ¶ 7-8(A)(1). The review requirement applies to all of the Company's rejected loans, not just those loans rejected by a single branch office. Thus, the number of rejected loans from Branch 87 that Cornerstone reviewed is irrelevant. If the Company reviewed 10% of "the total loans rejected" by the Company, then it complied with FHA requirements. Significantly, Cornerstone did in fact perform Quality Control reviews on at least 10% of the loans that the Company rejected during the relevant time period. What's more, contrary to the suggestion in the Draft Report, Cornerstone did review some of Branch 87's rejected loans. Specifically, it reviewed three - or 5.9% - of the 51 loans.

Comment 20



3. Onsite Reviews

The Draft Report alleges that Cornerstone did not conduct annual onsite reviews of Branch 87, which it was required to do because of the branch's high default rate, new key employees, and past problems. It also states that the onsite reviews performed did not include all of the items required by HUD, such as confirmation that Branch 87 revised procedures to reflect changes in HUD requirements and inform personnel of the changes, and verification that all Branch 87 personnel were Cornerstone employees or contract employees.

Comment 5

FHA guidelines provide that a lender must conduct annual onsite visits for offices meeting certain higher risk criteria, such as high early default rates, new branches or new key personnel, sudden increases in volume, and past problems. See HUD Handbook 4060.1 REV-2, ¶ 7-3(G)(2). Cornerstone consistently adheres to this requirement. On March 13, 2008, it performed an onsite review of Branch 87. While certain action items were noted at the time, no significant unresolved issues were left outstanding. While the branch's default/claim rate remained high, HUD itself withdrew a Credit Watch proceeding initiated in March 2010, indicating its agreement that the high default/claim rate for the period January 1, 2008 through December 31, 2009 was not attributable to any wrongdoing or deficient loan origination or underwriting by Branch 87. During that time, Branch 87 was not considered to be a problem branch, there were no sudden increases in volume or new key personnel, and HUD agreed that its high default/claim rate was not due to any fault of the branch. Thus, FHA guidelines did not require another onsite review that year. Nevertheless, as stated in the Draft Report, Cornerstone did perform another onsite review on December 18, 2009, and it performed yet another onsite review on September 23, 2010. Cornerstone took care to monitor Branch 87's activities and FHA compliance, just as it always has done with all of its branch offices, and it performed onsite reviews of Branch 87 as required under the applicable FHA guidelines.

Comment 21

With respect to the specific items HUD requires to be included in the onsite reviews, Cornerstone's checklist for the site reviews at the time included all of the items listed in the applicable FHA guideline, see HUD Handbook 4060.1 REV-2, ¶ 7-3(G)(1), except the two referenced in the Draft Report. These two items, however, are better verified through a lender's corporate office where the information is housed. Specifically, the OIG notes that the checklist did not include confirmation that Branch 87 revised procedures to reflect changes in HUD requirements and inform personnel of the changes. When there is a change in Company procedures, however, such change may be dictated by the corporate office, not the Branch Manager, and any new policies or procedures may have been provided to the branch. Thus, verification of this information may not have been possible at the branch level. The OIG also notes that the checklist did not verify that all Branch 87 personnel were Cornerstone employees or contract employees. Again, this information may have been better verified at the corporate office where human resources information was



Comment 22

housed, not at the branch office level. Thus, while the checklists used while visiting the branch may not have included these two items, their absence from the checklist does not mean that Cornerstone did not verify and confirm these items during the onsite review process. Nevertheless, please note that the review checklist that the OIG reviewed was the form in place in 2008 and 2009, not the form in place today. Cornerstone's current branch audit checklist is significantly longer than the prior form and includes all of the items listed in the HUD handbook, including the two noted by the OIG, as well as numerous other items (**Exhibit NN**).

4. Reverification Requirements

Finding 3 alleges that Cornerstone did not follow required reverification processes for loans it reviewed under its Quality Control program. Specifically, it alleges that Cornerstone's case files did not contain documentation showing it reverified unreturned VOEs for 105 Branch 87 loans. It also alleges that Cornerstone ordered new credit reports for only 18 of the FHA loans it reviewed during the audit period. The Report cites one example, with **FHA Case Number 493-8447975**, where Cornerstone allegedly originated the loan without verifying current employment and performed a Quality Control review after closing without verifying employment. The OIG asserts that the VOE in the file showed that the borrower was not employed when the loan closed and showed only previous employment instead of current employment. Cornerstone takes exception to these findings.

Comment 7

First, with respect to the purportedly unreturned verifications, the Report does not indicate to which 105 loans it is referring. Cornerstone's recent internal review reflects only 45 cases without reverifications of employment in the file (not 105), 21 files with partial reverifications, and 28 files with acceptable reverifications. Unfortunately, given that many years have passed since the OIG conducted its review, and given that many years have passed since the Company's obligation to retain the files expired, Cornerstone cannot respond adequately to the OIG's assertions. It is very possible that reverifications were obtained in the 45 above-referenced cases and can no longer be located. The OIG's lengthy delay in issuing its findings has made a meaningful response impossible. Please note, however, that it has been and remains Cornerstone's policy and procedure to reverify employment in each and every case subject to a Quality Control review.

Second, with respect to credit reports, FHA guidelines require a lender to obtain a new credit report for each borrower whose loan is included in a Quality Control review, unless the loan was a streamline refinance or was processed using an automated underwriting system. See HUD Handbook 4060.1 REV-2, ¶ 7-6E(1). The Report does not indicate which 18 files the OIG reviewed, but Cornerstone's recent internal review did not identify 18 loans without required credit reports. Cornerstone reviewed 95 FHA files between October 2007 and December 2008. In 18 cases, the files contained new credit reports as required. In 65 cases, new credit reports were not required: one loan was a streamline refinance transaction, and 64



loans were automatically underwritten with Desktop Underwriter or Loan Prospector. In the remaining 12 cases, new credit reports were required but cannot be located in the files. Note, however, that in 9 of these cases, Company logs show that new credit reports in fact were pulled. The fact that we can no longer locate them in the files is not surprising given how many years have passed since the OIG conducted its audit and that Cornerstone is no longer required to maintain the files.

Comment 14

Lastly, in the Report's case file example, as explained above in Finding 1, the borrower's employment was ongoing. Cornerstone obtained a verbal VOE and pay stubs to verify the borrower's employment prior to closing. The notation on the verbal VOE that the employment was "Previous" was a typographical error by the CHL production assistant who executed the form. This fact was clear at the time given that there was no ending date on the VOE for the employment noted and that the most recent pay stub was dated less than a week before the verbal VOE was obtained. Cornerstone also has obtained a current verification from the employer confirming that the borrower in fact was still employed at the time of closing.

5. Corrective Actions

In Finding 3, the Report also contends that Cornerstone was unable to provide support to show that review findings are reported to senior management within a month of completion of the initial Quality Control report, that the Company takes prompt action to deal appropriately with any material findings, and that the Company identifies actions being taken, the timetable for completion, and any planned follow-up activities. Despite these assertions, the Report acknowledges that the monthly Quality Control reports show that management responded to each of the required corrective action requests, although the reports were not dated beyond the month and included no follow-up dates. The OIG, therefore, was unclear as to whether or when Cornerstone's management followed through with specific actions.

Comment 22

Although the Report alleges Cornerstone's inability to support that findings were reported to senior management and corrective actions were taken in a timely manner, it acknowledges that the monthly reports show management responses to all action requests. Contrary to the suggestion in the Report, senior management was notified of findings within a month of report completion and prompt corrective actions were taken as required. All Quality Control reports and all responses from the appropriate departments were uploaded to the Company's server, and each report and response contains a creation date in the system when it was saved. Thus, as the Report acknowledged, senior management was informed of findings and responded to action items, and, as Cornerstone's records evidence, management followed through with specific actions in response to the findings.



III. THE ALLEGATIONS CONSTITUTE A RECOMMENDATION TO HUD, RATHER THAN A FINAL ACTION BY THE DEPARTMENT

The Draft Report merely recommends that the Department pursue indemnifications and other administrative actions. Upon receiving a final report, the Department will have an opportunity to independently examine the audit findings and make an independent determination as to whether indemnification and/or other action would be appropriate in connection with any of the OIG's findings. As discussed at length earlier in this response, Cornerstone strongly disagrees with the findings in the Draft Report. HUD also may disagree with them and decide not to pursue indemnifications or other administrative action in this instance.

In addition, while the audit process is still ongoing at the time the OIG issues its "final" report, the report and the OIG's recommendations typically are made public on the OIG website. As a result, a lender's investors and peers are able to access the OIG's preliminary recommendations before the Department even has an opportunity to assess their merit. These entities, however, often assume the OIG's assertions are founded and/or misinterpret the OIG's recommendations to be final actions by the Department. Under these circumstances, the OIG's publication of its preliminary findings and recommendations that HUD pursue indemnification and other serious actions in this case will have a material, adverse effect on the Company's business.

If the OIG's goal is to present the reader with a full and accurate disclosure of its audit process and findings and their implications for the Company, the Report should include the following disclosure on the first page in bold, capitalized lettering:

THE REPORT FINDINGS REFLECT THE VIEWS OF THE OFFICE OF INSPECTOR GENERAL AND DO NOT CONSTITUTE A FINAL DETERMINATION OF THE MATTERS RAISED HEREIN BY THE U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT. THE FINAL DETERMINATION IN THIS MATTER WILL BE MADE BY THE REPORT'S ADDRESSEE, THE HUD ASSISTANT SECRETARY FOR HOUSING – FEDERAL HOUSING COMMISSIONER, WHO WILL ULTIMATELY DECIDE WHETHER TO ACCEPT THE REPORT'S RECOMMENDATIONS IN WHOLE OR IN PART OR REJECT THEM.

Such a disclosure would convey more accurately the status of the OIG's "final" report to the Company's investors, customers, and the public.

IV. CONCLUSION

For the reasons stated herein, Cornerstone believes firmly that a final audit report should not be issued in this case. The OIG conducted its review 4 and a half years ago, the loans that the OIG reviewed were originated on average 6 years ago, the branch office that the OIG reviewed was closed 2 years ago, the marketing



Mr. Gerald R. Kirkland
March 31, 2014
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agreements that the OIG reviewed were terminated over 4 years ago, and the Quality Control Plan that the OIG reviewed was used 5 years ago. The OIG's findings are stale and, as OIG representatives acknowledged during our exit conference, they do not reflect current conditions at the Company. For these reasons, and given the significant disadvantage that the Company faces as a result of the OIG's delay, a final report in this case would be unduly prejudicial.

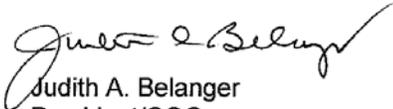
Moreover, the findings in the Draft Report are generally in error. This response demonstrates Cornerstone's substantial compliance with HUD/FHA requirements in the cases cited in Finding 1, the OIG's assertions conflict with the applicable law in Finding 2, and Finding 3 is based on a long-outdated Quality Control Plan that has not been in effect for many years.

Cornerstone appreciates this opportunity to respond to the matters raised in the Draft Report. After considering this response and supporting documentation, we hope the OIG will agree that a final report should not be issued or, at the very least, that Findings 2 and 3 should be removed.

If you have any questions or need additional information, please call our Washington counsel, Phillip L. Schulman, at (202) 778-9027, or Emily J. Booth, at (202) 778-9112.

Thank you for your kind consideration.

Sincerely,



Judith A. Belanger
President/COO
Cornerstone Home Lending, Inc.

cc: Phillip L. Schulman, Esq., K&L Gates LLP
Emily J. Booth, Esq., K&L Gates LLP

Enclosures



OIG Evaluation of Auditee Comments

Comment 1: Cornerstone disagreed with the findings and disputed the accuracy of the report and OIG's interpretation of rules. We reviewed Cornerstone's comments and the supporting documentation. We changed the report where appropriate.

Comment 2: Cornerstone noted that the information in the report was dated and therefore did not reflect current operations. Cornerstone also questioned whether a report should even be issued due to the lag time. Further, Cornerstone believed that the lengthy passage of time since the audit work prevented the OIG and HUD from taking action against it for the findings in the report. Cornerstone further stated that it had closed Branch 87 more than 2 years ago when the branch manager accepted employment elsewhere. Cornerstone noted that OIG agreed at the exit conference to clarify that the findings were based on dated information.

The conditions in the report were the conditions at the time of the audit. The lag time in audit work and report issuance was due to pending Department of Justice work and does not reflect upon the standards in which our audit work was conducted. Further, even though much time has passed, HUD OIG has a right to report what it found. However, we made changes where appropriate in the report to clarify that the information was dated and may not reflect current operations.

Comment 3: Cornerstone noted that the marketing agreements terminated in 2009 and 2010, but was inconsistent on the termination dates, twice reporting them as October 2009 and March 2010, and once reporting them as December 2009 and April 2010.

Even though the marketing agreements mentioned in the report had terminated, one of the managers told OIG at the exit conference that Cornerstone has continued to use marketing agreements. Based on this response, we added a recommendation that HUD review both the new agreements and Cornerstone's payments under those agreements to determine whether Cornerstone is currently violating RESPA.

Comment 4: Cornerstone provided updated background data. We used the data to update the Background and Objectives section of the report.

Comment 5: Cornerstone stated that HUD withdrew a Credit Watch proceeding initiated in March 2010, and interpreted this to mean that HUD did not attribute Branch 87's high default and claim rate to any wrongdoing or deficient loan origination or underwriting by Branch 87.

Cornerstone did not provide a copy of any HUD documentation regarding a withdrawal of a Credit Watch proceeding. Further, according to Cornerstone,

HUD initiated the Credit Watch proceeding in March 2010, which was well after the audit period and withdrew the proceeding at some later date which Cornerstone also did not provide. Since the proceeding and withdrawal were after the audit period, they cannot reasonably be expected to absolve Cornerstone from its obligation to have reviewed Branch 87 annually during the audit period. We did not change the report based on this comment.

Comment 6: Regarding RESPA violations, Cornerstone stated that (1) its marketing agreements did not violate RESPA and involved fixed payments for marketing and promotional services to realtors for services rendered instead of payment for referrals, and that such payments are expressly allowed by HUD's 2010 interpretive rule (2) there was no conflict of interest in connection with the agreements, (3) there was no conflict of interest with personnel because HUD Handbook 4060.1 REV-2, paragraph 2-9(B) and (C) specifically allowed officers to be owners, officers, partners, or members of other entities, (4) HUD is no longer responsible for RESPA and the statute of limitations has expired, and (5) OIG misinterpreted Section 8(a) of RESPA, and that it does not prohibit paying marketing fees to realtors in exchange for exclusive rights.

We disagree with Cornerstone on all 5 RESPA issues that it raised. Cornerstone did not explain why it was necessary for the agreements to be exclusive, why its employees worked in a realtor's office, why payments were more than the agreed upon \$11,000 per month, and why it made additional payments to another entity owned by the same realtor without a marketing agreement. Further, Cornerstone's denial of a conflict of interest relationship did not address the second part of HUD Handbook 4060.1 REV-2, paragraph 2-9 (C), which requires a clear and effective separation between the two entities. The shared management and ownership, exclusive agreement, co-location of employees, and payment structures all demonstrate that Cornerstone violated the requirement to clearly separate itself from the realty company.

Also, while HUD may no longer be responsible for investigating RESPA violations, and while the statute of limitations for some actions may have expired, HUD may have the right to take administrative actions. Further, OIG has a right to report its findings and to refer them to other agencies, especially since Cornerstone is still using marketing agreements.

Finally, regarding the applicability of Section 8(a) of RESPA, OIG contends that the exclusivity of the agreements appears to be an attempt to stifle competition, while the inconsistency of the payments under those agreements appears to be payments for referrals.

Therefore, we did not change the audit report or the recommendations based on Cornerstone's comments regarding RESPA.

Comment 7: Cornerstone noted that the loans were dated, and that it was not required to keep loan documentation after 2 years. Cornerstone also noted that OIG relied on other information which it can no longer locate. Cornerstone stated that since the information in the report was dated, it was at a significant disadvantage in responding to the finding.

At the exit conference, OIG extended its usual comment period by 2 weeks and offered to send the electronic files it used for its review to Cornerstone. Cornerstone did not request the files. Further, Cornerstone did not request the documents that we used to support our reverification analysis.

Comment 8: Cornerstone stated that the only relevant date was the date that the borrower executed the contract, that it had a right to rely on the sales dates in the sales contracts, and that when the date fields were blank, the dates could be found in other documents such as the date field in the appraisal.

Based on documentation in the files, the contracts were agreed too much earlier than reported by the sales contract in the file. The blank dates in the contracts show that Cornerstone used incomplete documents, and the sales date had to be a calculated number. Further, Cornerstone wants to use the dates in other documents such as the appraisal reports which the audit found to be questionable. We did not change the report based on Cornerstone's comments regarding sales contract dates.

Comment 9: Cornerstone stated that most of the properties were in a presidentially-declared disaster area, which should have exempted them from the anti-flipping rule. Cornerstone referred to Mortgagee Letter 2006-14.

Cornerstone's position is not valid. We could not find any indication of an exemption for counties in Texas during the affected period. Mortgagee Letter 2006-14 states that FHA will announce eligibility for exemptions to the restrictions of the property flipping rule in a Mortgagee Letter. Further, the Mortgagee Letter will specify how long the exemption will be in effect and the specific disaster area affected. Cornerstone did not provide evidence showing that Harris County had an exemption from the anti-flipping rule. We did not change the report based on this comment.

Comment 10: Cornerstone stated HUD's definition of property flipping was reselling recently acquired properties for considerable profit with artificially inflated values. Cornerstone further stated that there was no reason for it to believe property values were artificially inflated.

Many of the properties in the report had artificially inflated values as noted by the OIG reappraisals at Table 3. Also, had Cornerstone exercised due diligence in reviewing both the erroneous appraisals at Table 3 and the appraisal reports at Table 2, it should have noticed that many of the property values were artificially

inflated. Further, the 8 properties questioned for property flipping in the report increased in cost by an average of 116 percent from the prior sale to the current sale which should have been a red flag to Cornerstone. We did not change the report based on this comment.

Comment 11: Cornerstone noted that HUD's prohibition against property flipping was no longer in effect when OIG conducted the audit.

As stated in the report, the waiver occurred after Cornerstone originated the subject loans; thus, the waiver was not applicable to them.

Comment 12: Cornerstone stated that it received the questioned appraisals prior to the closing date. Cornerstone further stated that it had discussed the issue with the appraiser, and blamed any inconsistencies in dates on the appraiser's software which it stated updated automatically to reflect the current date each time the appraiser printed the report. Cornerstone addressed each case separately and provided copies of invoices to support appraisal dates.

Cornerstone did not provide a copy of a statement from the appraiser or any other source to support its position on automatic dates in the appraisal reports. Further, the invoices are not useful because they do not indicate whether the appraisal services could have been pre-paid. In any case, OIG reviewed the appraisals in the files and did not find multiple copies of appraisals with different signature dates. Therefore, if the dates were automatically updated, then Cornerstone's underwriters would have been relying on appraisals that had not been finalized before the closing. We did not change the finding based on this comment.

Comment 13: Cornerstone stated that it had not had access to the OIG's appraisals, and that it did not find anything on the face of its appraisals that suggested they were incorrect. Cornerstone defended each of the six appraisals separately.

Cornerstone did not request copies of the appraisals either at or after the exit conference and their response failed to mention numerous appraisal errors and inconsistencies that its underwriters either did not detect or did not question. Further, the report specifically mentioned two appraisals that were at the upper end of the value range for their locations. If Cornerstone's quality control program had been adequate at that time and had its underwriters exercised due diligence and professional skepticism, Cornerstone should have identified and investigated these anomalies, which should have determined that the appraisals were erroneous. Cornerstone was responsible for its appraisers, and it did not follow the HUD requirements outlined in HUD Handbook 4150.2.

We summarized the errors for each of the 6 appraisals in their case reviews at Appendix C. Each appraisal had similar errors. Thus, rather than rebut each of Cornerstone's arguments that the appraisals were accurate, we included the

appraisal errors for FHA Case Number 493-86934872 below as an example of the types of appraisal errors that we found.

Cornerstone's appraiser

1. Failed to properly measure and calculate the correct gross living area of the subject property.

The appraiser stated the gross living area was 1,601 square feet, while the Harris County Appraisal District stated the size to be 1,538 square feet. Our actual measurements provided a gross living area of 1,536 square feet. The Houston Area Realtor Multiple Listing System (MLS) also listed the property's gross living area as 1,538 square feet. The appraiser overstated the gross living area by 63 square feet. This overstatement under adjusted the larger home comparables and over adjusted the smaller comparables, and therefore favored the contract price of the subject property as compared to the comparables.

2. & 3. The appraiser selected comparable properties that were not truly comparable to the subject property and used comparable property appraisals that provided the value conclusion only in the upper value range. Further, the appraiser disregarded a number of comparable properties in the neighborhood that were more similar to the subject property.

The appraiser stated the value range of properties in the neighborhood was \$41,000 to \$180,000 with a predominant value of \$89,000. However, the subject property's value at \$120,500 was well above the predominant value with only a comment that the subject property was one of the larger homes and in average/updated condition in the market area. A review of neighborhood MLS listings and sold information, and Harris County Appraisal District data showed that the subject's gross living area was very comparable to other homes in the neighborhood and the subject was not one of the larger homes in the neighborhood. MLS at the time of the subject appraisal indicated several listings and sold properties ranging in size from +/-1,400 to +/-1,800 square feet. The appraiser misled the reader with his statement, and incorrectly justified a higher market value for the subject property.

Of the comparables used in the sales grid, it appeared that the comparables selected were all in the upper end of the price range and were in superior condition compared to the subject property. The appraiser noted the subject and all of the comparables as average/updated, which masked the condition of the subject. Information available indicated the subject's condition should have been rated fair and condition adjustments made for differences between subject and comparables. The appraiser made some positive

adjustments to comparables 1 and 3 and made no adjustments to comparables 2 and 4 for condition adjustments.

The appraiser made no distinction between the subject and comparables for age. However, in the narrative section, he discussed age adjustments as follows: "Age adjustments were applied at the rate of 0.5% of sales price, per year's difference between subjects and comparable's effective age." This statement is confusing since no age adjustments were made.

4. Failed to make proper adjustments for dissimilarities (seller concessions, fireplace, storage sheds) between the subject property and the comparable properties.

The appraiser analyzed a total of six properties using the sales grid approach, four of which were closed sales, one that was a current listing, and one that was a pending sale. Of the four sales, two were more than 6 months old with no comments. Appendix D: Protocol states - "If a sale of over six months is used, an explanation must be provided." The appraiser did not provide an explanation.

The HUD Handbook requires that the appraiser verify concessions with sources other than MLS. The appraiser provided no evidence in the report or in the work file that he obtained verification. Of the four closed comparable sales in the report, concessions were disclosed in MLS for two, but the appraiser noted them as conventional and no seller points. The appraiser's failure to disclose and make appropriate adjustments resulted in inflated adjusted values on comparables sales # 3 (\$6,720) and #4 (\$3,400).

The appraiser failed to note or make adjustments for upgrades on some comparables. Comparables 2 and 3 had storage sheds, and 3 also had an above ground pool. Lack of these adjustments favored the contract price of the subject property.

5. Failed to properly disclose the subject property's condition and make proper condition adjustments to the comparable property appraisals.

The offering and list price stated by the appraiser were very misleading. The appraiser stated "MLS Listing #3296054; listed 10/20/2007 for \$94,900; DOM (days on market) – 36." However, this was not the listing as of the date of the contract. The listing as of date of contract was for sale by owner.

The subject property was listed as MLS #3296054 on October 20, 2007, for \$89,900. The price changed several times, and ranged from \$82,900 to \$89,900. The MLS listing was terminated on November 25, 2007. This appears to have been a pre-foreclosure listing. The property was relisted on

December 31, 2007, as MLS #7575874 for \$69,900 with a pending sale on February 18, 2008, and a closing date of May 3, 2008, for \$60,000. Apparently the property was a “For Sale by Owner” at the time the current purchasers signed the contract on July 25, 2008. According to LexisNexis, the contract date was July 29, 2008, and the recording date of the deed was August 6, 2008. Attached to the contract was an FHA/VA amendment clause dated July 31, 2008, and a lead base paint disclosure signed on May 25, 2008. The appraiser was required to research, verify, analyze, and report on any current agreement for sale of the subject property, and any offering for sale within the 12 months prior to the effective date of the appraisal. The appraiser signed a certification affirming that he had researched and analyzed and reported all listing and offerings and had analyzed each. However, there was no evidence that he had done so, and no mention of any of the previous listings or the “For sale by Owner” in the subject portion of the appraisal report. The appraiser made no mention of the analysis of any of these listings as to whether they were market or below market and what repairs had been made since the May 3, 2008 purchase of the property.

The MLS indicated at the time of the subject appraisal that the neighborhood had several foreclosed properties and real estate owned properties being offered. MLS information showed that the Sterling Green community had a total of 178 properties that were sold between January 5, 2007, and June 30, 2008, ranging in price from \$44,900 to \$140,000. Of these properties, 63 (35 percent) real estate owned and distressed sale properties sold, ranging in value from \$44,900 to \$135,000. Typically, an area with relatively large numbers of real estate owned properties indicates a market area suffering a decline. Even though some data for the subject’s zip code indicates increasing values for the first two quarters of 2008, with a decline in the 3rd and 4th quarters, MLS data indicated possible distress in the immediate market of the subject property. The appraiser needed to address these issues and make a determination as to whether or not the area around the subject property was suffering a decline due to real estate owned and distressed properties. Instead, the appraiser stated the area was stable and in balance for housing trends.

The appraiser stated the year built as 1977 (actual age – 31 years) with an effective age of 15 years. Effective age is based on the entire structure including the foundation, framing, plumbing, wiring, etc. Based on our review, the effective age appeared to be understated. An average quality brick veneer home has a typical building life of 60 years. Using the appraiser’s effective age the remaining effective life would be 45 years rather than 60 years as the appraiser claimed.

The appraiser stated in the narrative portion of the report “The subject house has been updated with quality hard wood, tile and carpet flooring throughout the house, new paint (inside and outside), fixtures, wainscoting, bathrooms

and kitchen have been redone.” However, an inspection on April 12, 2009, and conversations with another appraiser who inspected the property on August 20, 2009, showed no hardwood flooring.

Handbook 4150.2 requires that the appraiser provide photos at an angle so that the front/side and rear/side can be seen. The appraiser provided straight on front and rear photos that did not provide a view of the sides. Further, the appraiser appears to have cut and pasted photos from the MLS listing information. Appendix D: Valuation Protocol (D-13) requires that the appraiser include the appraiser’s photographs. If MLS photos are included, they can be included as a reference to show the condition of property at the time of listing/closing. The appraiser did not mention that the photos were from the MLS; however it was very evident when comparing MLS photos with the ones in the report that they had been cut and pasted.

HUD Handbook 4150.2 does not require a cost approach on older dwellings. The appraiser developed the cost approach using “Average” quality construction and arriving at a cost of \$121,744 with a remaining effective life of 60 years. The cost approach value is inflated because the appraiser failed to calculate the correct gross living area, and underestimated the effective age. Using the cost approach resulted in a value that is inflated by about 26 percent.

6. The appraiser made other errors

The property was noted as “vacant” at time of the inspection. If a property is vacant at the time of the inspection, protocol requires the appraiser to comment in the “Improvement” section whether the utilities were on or off. If utilities are off, the appraiser should have conditioned the appraisal on a satisfactory re-inspection. The appraiser made no comment.

The appraiser made several non-applicable boiler-plate comments in the narrative section on the report. While these comments were not applicable to the subject appraisal, they would confuse the reader.

The building sketch did not show dimensions of the front porch and the patio and whether they were covered or not covered. The subject property had a covered front porch located at the front door and a small patio located at the rear of dwelling. After the purchase, the current owners expanded the patio and built a cover over it. HUD Handbook required the appraiser to include in the sketch the patio, decks, etc., and indicate whether they were covered or not covered.

The appraiser stated that the gross living area “adjustments were made at the rate of \$20 per square foot for differences greater than +/- 100 sq ft per Uniform Standards of Professional Appraisal Practice (USPAP) guidelines.” This was an erroneous statement because USPAP does not provide

guidelines or address adjustments to be made. USPAP requires the appraiser to research, analyze and report the market reactions for adjustments.

The appraiser described the location of the subject and comparables as average. HUD Handbook 4150.2; Appendix D: requires the appraiser to state subdivision name for the subject and each comparable, noting comparables as superior, equal, or inferior. Location adjustments should be made for superior and inferior location if the market indicates.

The appraiser described the view of the subject and comparables as residential. HUD Handbook 4150.2; Appendix D: requires the appraiser to state them as residential/good or residential/fair and make adjustments for differences, if needed.

As noted, the appraisal contained many errors. The other sample appraisals contain similar discrepancies. We did not change the report based on Cornerstone's comments regarding the appraisals.

Comment 14: Cornerstone stated that the marks on the documentation in the file did not mean that the borrower was unemployed at closing. Further, it stated that a recent income verification showed that the borrower was employed at the time of closing. Cornerstone provided some documentation, including a post-employment verification which it obtained on March 4, 2014.

OIG had already reviewed and considered all of the documentation provided. The post-employment verification showed the last pay date for the borrower as October 31, 2007, which was one day after closing. We did not change the report based on the comment.

Comment 15: Cornerstone stated that one of the loans had adequate compensating factors to justify exceeding the ratios, while income for the other loan was calculated correctly. Cornerstone provided various file documents to support its position.

We considered the documents provided by Cornerstone during the audit, and they did not refute our analysis. For FHA Case 493-8567176, the auditee accepted a note written by the loan processor to the underwriter which claimed that the non-purchasing spouse received child support and was employed. A note is not sufficient documentation. Further, the non-purchasing spouse's name did not appear on the HUD-1 and the underwriter did not document the compensating factor on the MCAW Form as required. For FHA Case 493-8480034, the verification of income was not legible, and we based our calculations on figures from the pay stub. We did not change the report based on the comment.

Comment 16: Cornerstone stated that it obtained a credible explanation for a large increase in the borrower's bank account.

Cornerstone provided a copy of a tax return showing that the borrower was due a large refund. However, OIG had already reviewed this document during the audit and determined that the increase in the borrower's bank account was unsupported because the documentation did not adequately support the \$4,000 bank deposit. The deposit was significantly less than the refund amount, was less than 1 week (6 days) after the return was filed, and there was no documentation for a refund loan or a letter of explanation from the borrowers as required by HUD. We did not change the finding based on the comment.

Comment 17: Cornerstone stated that the referenced individual was never a Cornerstone employee and that Cornerstone never represented him in that way. Also, Cornerstone stated that OIG is aware of this and that the language in the draft report is prejudicial and inflammatory.

The report laid out all the facts obtained regarding the referenced individual during the audit. Further, it noted the auditee's response regarding his employment. Despite Cornerstone's response, the totality of the facts, including (1) collocation of businesses, (2) payments to the individual, (3) the trade magazine article that referred to the individual as a Cornerstone owner, and (4) the auditee's quality control reports that utilized the individual's name to describe a branch argue that the individual was a Cornerstone employee.

Comment 18: Cornerstone noted that the quality control plan that OIG reviewed had been superseded by a new plan, and provided an undated copy of the new plan. Cornerstone stated that OIG admitted at the exit conference that it might be appropriate to delete the quality control finding from the report.

OIG evaluated Cornerstone's quality control system as it existed at the time of the audit. The system may have changed, and Cornerstone provided a quality control handbook as part of its response to the draft report, but the handbook was undated and we have not determined if or when Cornerstone implemented it. Further, Cornerstone's statement about OIG agreeing to remove the quality control finding was incorrect. OIG only agreed to reword the finding to show that the quality control information is dated, and the current quality control system has not been evaluated – not to remove it from the report. We added language to the report to clarify that the finding relates to Cornerstone's quality control system during the audit period, and that the audit period may not represent Cornerstone's current quality control performance.

Comment 19: Cornerstone admitted that it did not conduct all of its required quality control reviews timely during the audit period because it was in transition from an in-house review system to a contracted review system. However, Cornerstone

stated that its contractor reviewed all of the files for which reviews were required.

The contractor came aboard in March 2009. Our review of the quality control reports showed deficiencies as late as August 2009 which included the contractor's work. We did not change the report based on the comment.

Comment 20: Cornerstone stated that the requirement to review 10 percent or a statistical random sample of rejected loan applications applied to the company as a whole, and not to a specific branch. Further, Cornerstone stated that three of Branch 87's 51 rejected loans during the audit period had been reviewed.

The OIG requested denied and rejected loan reviews for Cornerstone - not solely for Branch 87. Cornerstone stated in multiple interviews that it reviewed all denied and rejected applications daily but failed to provide copies of the reviews and stated in its response that they were not retained. Cornerstone's policy specifically stated that the retention for denied and rejected records was 25 months and quality assurance records were retained for 2 years or 24 months.

Comment 21: Cornerstone noted that it has changed the checklist that it uses to review Branch offices since the audit, and provided a copy of the checklist.

We have not evaluated the checklist or determined whether Cornerstone actually implemented it.

Comment 22: Cornerstone stated that prompt corrective actions were taken as required to address quality control report findings.

Cornerstone did not provide any evidence to support its assertion. We did not change the report based on this comment.

Appendix C

NARRATIVE CASE SUMMARIES – UNDERWRITING DEFICIENCIES

FHA case number: **493-8447975**
Loan amount: \$81,357
Settlement date: October 30, 2007
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$73,880
Requesting reimbursement: Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not properly verify the property value before closing the loan.

The Lender Used Unsupported Income To Qualify the Borrower

HUD Handbook 4155.1, paragraph 4-D(1)(a), prohibits lenders from using income in evaluating the borrower's loan if the income cannot be verified, is unstable, or will not continue. The borrower was no longer employed; therefore, the income was incorrect. The lender obtained income documentation, including pay stubs and verification of employment, but ignored the verification, which stated that it was for previous employment and showed salary, the probability of continued employment, and the probability of bonus and overtime as zero.

Failure To Review Appraisal Report Before Settlement

The loan settlement was dated October 30, 2007, while the appraisal report was dated November 14, 2007. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that "lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion."

FHA case number: **493-8567176**
Loan amount: \$109,137
Settlement date: July 8, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$97,207
Requesting reimbursement: Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not properly verify the property value before closing the loan.

The Lender Miscalculated the Borrower's Income

The income calculation was based on an hourly rate of \$17 per hour x 40 hours per week when the pay stubs showed that the borrower worked an average of 35 hours per week. Therefore, based on year-to-date income, the borrower's mortgage payment-to-income ratio should have been 44 percent, which exceeded HUD's maximum of 31 percent. Further, there were no compensating factors in the loan file to justify exceeding the limit.

Failure To Review Appraisal Report Before Settlement

The loan settlement was July 8, 2008, while the appraisal report was dated August 11, 2008. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that "lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion."

<u>FHA case number:</u>	<u>493-8959876</u>
Loan amount:	\$84,550
Settlement date:	March 6, 2009
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$76,749
Requesting reimbursement:	Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not verify assets and the property did not qualify for FHA insurance.

Inadequate Verification of Assets

The lender did not sufficiently verify borrower assets. The borrower had a large increase of \$4,000 in a bank account. However, the lender did not obtain a credible explanation of the source of those funds as required. HUD Handbook 4155.1, paragraph 2-10(B), requires the lender to obtain an explanation and evidence of the source of funds for any large increases in bank accounts or recently opened accounts.

Flipping Sale

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), "if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA." The seller acquired the property on November 18, 2008, and sold it to the borrower on January 20, 2009, 63 days after acquisition. The sales price had increased by 60 percent. The lender ignored the flipping prohibition.

FHA case number: 493-8547028
Loan amount: \$80,612
Settlement date: April 14, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$74,449
Requesting reimbursement: Yes

We are seeking reimbursement of this loan because the property did not qualify for FHA insurance and because the lender did not adequately review the appraisal.

Flipping Sale

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), “if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA.” The seller acquired the property on December 20, 2007, and sold it to the borrower on February 4, 2008, 46 days after acquisition. The sales price had increased by 225 percent. The lender ignored the flipping prohibition.

Failure To Adequately Review Appraisal

The lender did not adequately review the appraisal report, which contained several noncompliance issues. According to HUD Handbook 4155.2, paragraph 4-1(e), “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

Our review of the lender’s property appraisal showed that the lender’s appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to use comparable property appraisals that were truly representative of the subject property and market conditions at the time of the appraisal;
- (2) Failed to verify, document, and make adjustments for seller concessions for comparable property appraisals 1, 2, and 3;
- (3) Included two comparable property appraisals that required excessive adjustments, which decreased the reliability of the comparable property appraisals;
- (4) Failed to properly disclose the correct number of bathrooms in the subject property, leading to incorrect adjustments to the comparable property appraisals; and
- (5) Made site adjustments with no support or documentation.

FHA case number: 493-8692510
Loan amount: \$71,931
Settlement date: July 28, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$49,868
Requesting reimbursement: Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not properly verify the property value before closing the loan. Further, when the lender received the appraisal report, it did not adequately review the report.

Failure To Review Appraisal Report Before Settlement and Adequately Review the Appraisal

The loan settlement was July 28, 2008, while the appraisal report was dated August 6, 2008. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. The lender also did not adequately review the appraisal report, which contained several noncompliance issues. These actions were in direct violation of HUD regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

Our review of the lender’s property appraisal showed that the lender’s appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to properly measure and calculate the correct gross living area of the subject property,
- (2) Selected comparable properties that were not truly comparable to the subject property,
- (3) Failed to analyze and disclose amenities of comparable property appraisals, and
- (4) Failed to make proper adjustments for dissimilarities between the subject property and the comparable properties.

FHA case number:	493-8693472
Loan amount:	\$119,058
Settlement date:	July 31, 2008
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$63,080
Requesting reimbursement:	Yes

We are seeking reimbursement for HUD losses on this loan because the lender initiated the loan for an ineligible property, did not properly verify the property value before closing the loan, and did not adequately review the appraisal report.

The lender approved the loan for a property purchased for \$60,000 but resold the property for \$119,999, \$1 less than double the acquisition price, which would have required a second appraisal. HUD Handbook 4155.2, paragraph 4-7(f), requires the lender to obtain a second appraisal by a different appraiser if the resale price is 100 percent or more above the seller’s acquisition price.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), “if a property is resold 90

days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA.” The seller acquired the property on March 18, 2008, and sold it to the borrower on May 25, 2008, 68 days after acquisition. The sales price had increased by 100 percent. The lender ignored the flipping prohibition.

Failure To Review Appraisal Report Before Settlement and Adequately Review the Appraisal

The loan settlement was July 31, 2008, while the appraisal report was dated August 7, 2008. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. The lender also did not adequately review the appraisal report, which contained several noncompliance issues. These actions were in direct violation of HUD regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

Our review of the lender’s property appraisal showed that the lender’s appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to properly measure and calculate the correct gross living area of the subject property,
- (2) Selected comparable properties that were not truly comparable to the subject property and used comparable property appraisals that provided the value conclusion only in the upper value range,
- (3) Disregarded a number of comparable properties in the neighborhood that were more similar to the subject property,
- (4) Failed to make proper adjustments for dissimilarities (seller concessions, fireplace, storage sheds) between the subject property and the comparable properties, and
- (5) Failed to properly disclose the subject property’s condition and make proper condition adjustments to the comparable property appraisals.

If the appraisal had been performed properly, the appraiser would have arrived at a different value conclusion that would have been more representative of the predominate value of properties in the neighborhood. The lender’s appraiser valued the subject property at \$120,500 (sold for \$119,999). Our review appraisal showed that potential comparables ranged from \$79,500 to \$99,900 and averaged about \$90,000.

FHA case number:	491-9483914
Loan amount:	\$80,416
Settlement date:	May 1, 2009
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$73,941
Requesting reimbursement:	Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not properly verify the property value before closing the loan.

Failure To Review Appraisal Report Before Settlement

The loan settlement was May 1, 2009, while the appraisal report was dated May 25, 2009. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

FHA case number:	493-8753582
Loan amount:	\$79,373
Settlement date:	August 25, 2008
Status:	Reinstated by borrower
Requesting indemnification:	Yes
Unpaid balance:	\$75,234

We are seeking indemnification of this loan because the property did not qualify for FHA insurance and because the lender did not properly verify the property value before closing the loan.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), “if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA.” The seller acquired the property on May 20, 2008, and sold it to the borrower on July 22, 2008, 62 days after acquisition.⁴² The lender used an effective date found on the sales contract in the lender’s file, which was August 22, 2008. However, the title company files did not show an effective date on the purchase agreement. Further, the purchase agreement was faxed to the title company on July 25, 2008, with a cover letter stating, “attachment: Landa⁴³ executed contract.pdf.” The title insurance commitment documents were dated July 29, 2008. The sales price had increased by 129 percent. The lender ignored the flipping prohibition.

Failure To Review Appraisal Report Before Settlement

The loan settlement was August 25, 2008, although both the original appraisal report and a second appraisal report were dated after the loan settlement. The property required a second appraisal report because the sales price was more than double the acquisition price. The appraisal reports were dated August 28, 2008, and September 25, 2008, respectively. Therefore, the lender could not have reviewed either appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which state that “lenders are responsible for properly reviewing appraisals and determining if the

⁴² July 22, 2008, was one of three dates on the purchase agreement. The other dates were July 17, 2008, and August 22, 2008. The loan application was dated July 22, 2008.

⁴³ “Landa” is the name of the street where the property is located.

appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

FHA case number: **493-8925706**
Loan amount: \$94,261
Settlement date: August 12, 2009
Status: Delinquent
Requesting indemnification: Yes
Unpaid balance: \$105,052

We are seeking indemnification for HUD losses on this loan because the lender did not properly verify the property value before closing the loan.

Failure To Review Appraisal Report Before Settlement

The loan settlement was March 6, 2009, while the appraisal report was dated March 12, 2009. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

FHA case number: **493-8532052**
Loan amount: \$96,239
Settlement date: February 29, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$97,578
Requesting reimbursement: Yes

We are seeking reimbursement for this loan because the lender did not adequately review the appraisal report.

Failure To Adequately Review Appraisals

The lender did not adequately review the appraisal report, which contained several noncompliance issues. According to HUD Handbook 4155.2, paragraph 4-1(e), “lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion.”

Our review of the lender’s appraisal showed that the lender’s appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to properly measure and calculate the correct gross living area of the subject property;

- (2) Selected comparable properties that were not truly comparable to the subject property and used comparable property appraisals that provided the value conclusion only in the upper value range;
- (3) Disregarded a number of comparable properties in the neighborhood that were more similar to the subject property;
- (4) Failed to make proper adjustments for dissimilarities (seller concessions, view, site, age, fireplace) between the subject and comparable properties; and
- (5) Failed to properly disclose the condition of the subject property and make appropriate adjustments for the foundation and a number of electrical hazards that required further inspection, testing, and repairs before FHA underwriting and adjustments for the remaining economic life of the subject property.

If the appraisal had been performed properly, the appraiser would have arrived at a substantially different value conclusion for the subject property. The lender's appraiser valued the subject property at \$97,000 (sold for \$97,000). Our review appraisal showed six potential comparable property appraisals that ranged from \$44,000 to \$78,500 and averaged about \$62,075.

<u>FHA case number:</u>	<u>493-8558066</u>
Loan amount:	\$79, 273
Settlement date:	August 12, 2009
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$83,159
Requesting reimbursement:	Yes

We are seeking reimbursement for this loan because the lender did not adequately review the appraisal report.

Failure To Adequately Review Appraisals

The lender did not adequately review the appraisal report, which contained several noncompliance issues. According to HUD Handbook 4155.2, paragraph 4-1(e), "lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion."

Our review of the lender's appraisal showed that the lender's appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to properly measure and calculate the correct gross living area of the subject property,
- (2) Selected comparable properties that were not truly comparable to the subject property and used comparable property appraisals that provided the value conclusion only in the upper value range,
- (3) Disregarded a number of comparable properties in the neighborhood that were more similar to the subject property,
- (4) Failed to make proper adjustments for dissimilarities between the subject property and comparable properties, and

- (5) Failed to properly disclose the condition of the subject property and make appropriate adjustments for foundation repairs and problems that required further inspection and testing to determine the extent of the foundation problems and adjustments for the remaining economic life of the subject property.

The OIG appraiser concluded that “The mortgage underwriter should have reviewed the (lender’s) appraisal and questioned several obvious omissions between the photographs and adjustments made by the (lender’s) appraiser, requesting the appraiser to properly address these issues prior to proceeding with the loan.”

The OIG appraiser further concluded that the true value “would have been within the predominant range of values in the subject neighborhood and not higher than the predominant value.” The predominant value was \$50,000. The lender’s appraiser valued the subject property at \$80,000 (sold for \$79,900), well above the predominant value for the neighborhood.

FHA case Number:	491-9141680
Loan amount:	\$86,317
Settlement date:	April 21, 2008
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$67,611
Requesting reimbursement:	Yes

We are seeking reimbursement for HUD losses on this loan, because the property did not qualify for FHA insurance.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), “if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA.” The seller acquired the property on January 16, 2008, and sold it to the borrower on February 12, 2008, 27 days after acquisition. The lender used an effective date found on the sales contract in the lender’s file, which was April 17, 2008. However, earnest money was received on February 11, 2008, and an appraisal was conducted on March 19, 2008. Further, a second appraisal was conducted on April 2, 2008, because the sales price more than doubled the acquisition price. The loan application was not dated at the time the lender took it. The sales price had increased by 138 percent. The lender ignored the flipping prohibition.

FHA case number:	493-8480034
Loan amount:	\$142,871
Settlement date:	December 21, 2007
Status:	Claim paid - property conveyed to HUD and resold
Loss to HUD:	\$97,812
Requesting reimbursement:	Yes

We are seeking reimbursement for HUD losses on this loan because the lender did not properly determine the borrower's capacity to repay the loan, verify the property value before closing the loan, or adequately review the appraisal report.

Income

The lender miscalculated the borrower's income. HUD Handbook 4155.1, paragraph 4-D(1)(a), prohibits lenders from using income in evaluating the borrower's loan if the income cannot be verified, is unstable, or will not continue. The lender's income calculation was based on two 40-hour work weeks, while the most recent pay stub showed that the borrower worked only 24 hours. Based on year-to-date income, the front and back ratios would be 32 and 52 percent, respectively. HUD limited the front and back ratios to 31 and 43 percent, respectively, in Mortgagee Letter 2005-16. There were no compensating factors in the loan file to justify exceeding the ratio limits.

Failure To Review Appraisal Report Before Settlement and Adequately Review the Appraisal

The loan settlement was December 21, 2007, while the appraisal report was dated February 4, 2008. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. The lender also did not adequately review the appraisal report, which contained several noncompliance issues. These actions were in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that "lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion."

Our review of the lender's appraisal showed that the lender's appraiser overstated the value of the subject property by failing to use due diligence in performing the appraisal. Specifically, the appraiser

- (1) Failed to properly measure and calculate the correct gross living area of the subject property;
- (2) Selected comparable properties that were not truly comparable to the subject property and used comparable property appraisals that provided the value conclusion only in the upper value range;
- (3) Disregarded a number of comparable properties in the neighborhood that were more similar to the subject property;
- (4) Failed to make proper adjustments for dissimilarities (seller concessions, size, garage, age) between the subject and comparable properties; and
- (5) Failed to properly disclose the condition of the subject property and make appropriate adjustments for foundation and termite damage, rotten beams, siding and decking, and a number of hazardous electrical conditions, requiring further inspection, testing, and repairs before FHA insurance and adjustments for the remaining economic life of the subject property.

The OIG appraiser concluded that "The mortgage underwriter should have reviewed the (lender's) appraisal and questioned several obvious omissions between the photographs and adjustments made by the (lender's) appraiser, requesting the appraiser to properly address these issues prior to proceeding with the loan."

The OIG appraiser further concluded that if the appraisal had been performed properly, the lender's appraiser would have arrived at a substantially different value conclusion for the subject property. The lender's appraiser valued the subject property at \$148,000 (sold for \$144,000), while an OIG appraiser's potential comparable with equal condition and equal location was sold for \$75,000. Other potential comparables with equal location and superior condition were sold for \$82,500, \$84,500, and \$87,000. Finally, a comparable with a slightly superior location and superior condition was sold for \$118,000, well below the lender's appraisal for the subject property.

FHA case number: 493-8724586
Loan amount: \$88,301
Settlement date: August 16, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$71,514
Requesting reimbursement: Yes

We are seeking reimbursement of this loan because the property did not qualify for FHA insurance and because the lender did not verify the property value before closing the loan.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), "if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA." The seller acquired the property on May 9, 2008, and sold it to the borrower on July 10, 2008, 62 days after acquisition. There was no "effective date" on the contract. The sales price had increased by 134 percent. The lender ignored the flipping prohibition.

Failure To Review Appraisal Report Before Settlement

The loan settlement was August 16, 2008, while the appraisal report was dated August 20, 2008. Therefore, the lender could not have reviewed the appraisal report before approving and closing the loan. This action was in direct violation of regulations in HUD Handbook 4155.2, paragraph 4-1(e), which states that "lenders are responsible for properly reviewing appraisals and determining if the appraised value used to determine the mortgage amount is accurate and adequately supports the value conclusion."

FHA case number: 493-8721328
Loan amount: \$107,153
Settlement date: August 8, 2008
Status: Foreclosure deed recorded - claim paid for \$4,771
Requesting indemnification: Yes
Unpaid balance: \$115,591⁴⁴

We are seeking indemnification for the remainder of the loan because the property did not qualify for FHA insurance.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), "if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA." The seller acquired the property on April 16, 2008, and sold it to the borrower on June 30, 2008, 75 days after acquisition. The purchase agreement had several dates: June 30, 2008, the date option fee received; July 25, 2008, the effective date; and August 7, 2008. However, the appraisal fee payment was dated June 12, 2008, and the appraisal was conducted on July 10, 2008. The credit report was dated June 12, 2008, and the loan application was dated August 5, 2008, 1 day before closing. The sales price had increased by 67 percent. The lender ignored the flipping prohibition.

FHA case number: 493-8544391
Loan amount: \$109,038
Settlement date: April 22, 2008
Status: Claim paid - property conveyed to HUD and resold
Loss to HUD: \$54,726
Requesting reimbursement: Yes

We are seeking reimbursement of this loan because the property did not qualify for FHA insurance.

Flipping Sales

The property did not qualify for FHA insurance because it was resold less than 90 days after acquisition. According to HUD Handbook 4155.2, paragraph 4-7(e), "if a property is resold 90 days or fewer following the date of acquisition by the seller, the property is not eligible for a mortgage insured by FHA." The seller acquired the property on January 4, 2008, and sold it to the borrower on January 22, 2008, 18 days after acquisition. The sales price had increased by 71 percent. The lender ignored the flipping prohibition.

⁴⁴ The loan balance increased after the loan was modified in December 2008 and again in January 2010.

Appendix D

SCHEDULE OF LOSSES UPON PROPERTY SALES

Case number	Claims paid (rounded)	Resale amount	HUD loss (rounded)
493-8447975	\$ 100,814	\$ 33,500	\$ 73,880
493-8567176	123,887	41,000	97,207
493-8959876	94,691	30,501	76,749
493-8547028	96,530	29,000	74,449
493-8692510	75,576	32,210	49,868
493-8693472	125,835	72,500	63,080
491-9483914	88,382	22,500	73,941
493-8532052	110,303	19,500	97,578
493-8558066	91,438	15,500	83,159
491-9141680	94,761	33,100	67,611
493-8480034	148,401	61,000	97,812
493-8724586	95,525	32,101	71,514
493-8544391	112,836	69,501	54,726
Totals	\$1,358,979	\$491,913	\$981,574

Appendix E

SUMMARY OF UNDERWRITING DEFICIENCIES

Case number	Mortgage amount	Unpaid balance ⁴⁵	Indemnification amount ⁴⁶	Flip sale	Appraisal report after closing	Inadequate appraisal review	Inadequate income support	Inadequate asset verification
493-8447975	\$81,357	Conveyed			X		X	
493-8567176	109,137	Conveyed			X		X	
493-8959876	84,550	Conveyed		X				X
493-8547028	80,612	Conveyed		X		X		
493-8692510	71,931	Conveyed			X	X		
493-8693472	119,058	Conveyed		X	X	X		
491-9483914	80,416	Conveyed			X			
493-8753582	79,373	\$ 75,234	\$ 39,122	X	X			
493-8925706	94,261	105,052	54,627		X			
493-8532052	96,239	Conveyed				X		
493-8558066	79,273	Conveyed				X		
491-9141680	86,317	Conveyed		X				
493-8480034	142,871	Conveyed			X	X	X	
493-8724586	88,301	Conveyed		X	X			
493-8721328	107,153	115,591	60,107	X				
493-8544391	109,038	Conveyed		X				
Totals	\$1,509,887	\$295,877	\$153,856	8	9	6	3	1

⁴⁵ Conveyed properties were foreclosed upon and resold. Losses to HUD are in appendix D.

⁴⁶ 52 percent of the unpaid balance

Appendix F:

SCHEDULE OF REFERRAL LOANS - RESPA VIOLATIONS

Count	Case number	Mortgage amount		Count	Case number	Mortgage amount
1	493-8447975	\$81,357		16	493-8544391	109,038
2	493-8699656	123,523		17	493-8796775	74,778
3	493-8427719	79,273		18	493-8917071	85,536
4	493-8959876	84,550		19	493-8971746	135,745
5	493-8724586	88,301		20	493-8972595	112,818
6	493-8693472	119,058		21	493-8977840	83,361
7	493-8753582	79,373		22	493-9020135	127,153
8	493-8532052	96,239		23	493-8542224	101,398
9	493-8558066	79,273		24	493-8678525	93,263
10	493-8769771	105,687		25	493-8949284	65,786
11	493-8707247	117,570		26	493-9022845	135,009
12	493-8925706	94,261		27	493-8967163	92,592
13	493-8480034	142,871		28	493-8809334	78,573
14	493-8418819	69,451		29	493-8608705	64,490
15	493-8845801	124,854		30	493-8915511	89,331
				31	493-8916111	74,594
					Total	\$3,009,106

Appendix G:

SAMPLE LOANS THAT WERE NOT REVIEWED BY OIG⁴⁷

Count	Case number	Original mortgage	Loan status ⁴⁸	Unpaid balance	Claims
1	493-9090011	\$107,025	Claim		\$127,559
2	493-9094319	151,304	Claim		161,403
3	493-9130235	110,953	Bankruptcy	\$111,552	750
4	493-8917071	85,536	Claim		92,211
5	493-8971746	135,745	Delinquent	135,527	14,491
6	493-8990961	126,663	Claim		137,689
7	493-8483394	39,099	Reinstated	39,006	
8	493-8915511	89,331	Delinquent	94,916	1,750
9	493-8972595	112,818	Delinquent	130,116	21,587
10	493-8608705	64,490	Reinstated	65,515	1,000
11	493-8743766	106,422	Claim	36,798	48,565
12	493-8924312	75,905	Reinstated	74,191	
13	493-8977840	83,361	Forebearance	69,182	
14	493-8992927	139,690	Claim		155,671
15	493-9002755	116,353	Delinquent	114,578	
16	493-9020135	127,153	Ineligible	135,878	1,700
17	493-8750297	79,070	Claim		88,934
18	493-8542224	101,398	Claim		122,028
19	493-8678525	93,263	Claim		100,693
20	493-8941058	78,341	Claim		95,692
21	493-8949284	65,786	Bankruptcy	63,485	750
22	493-9050120	115,862	Claim		129,912
23	492-8337332	83,264	Claim		85,473
24	493-8973767	95,243	Promise to pay	83,894	750
25	493-8986909	106,184	Delinquent	102,839	
26	493-8992904	68,732	Claim	39,871	41,354
27	493-9022845	135,009	Repayment	125,698	
28	493-8709152	93,600	FHA HAMP*	101,505	1,500
29	493-8908579	97,646	Claim		104,088
30	493-8592611	111,122	Delinquent	104,325	
31	493-8727229	147,682	Reinstated	141,606	
32	493-8926134	117,358	Delinquent	131,930	750
33	493-8952514	77,470	Delinquent	71,992	
34	493-8965661	61,927	Delinquent	57,948	
35	493-8967163	92,592	Reinstated	91,840	
36	493-8906339	115,232	Reinstated	107,644	
37	493-8744574	87,241	Reinstated **	94,214	750
38	493-8626159	46,842	Reinstated	43,791	
39	493-8809334	78,573	Delinquent	59,776	
40	493-8929431	81,557	Reinstated	75,730	
Totals		\$3,902,842		\$2,505,347	\$1,537,050

* Home Affordable Modification Program

⁴⁷ Loan status, unpaid balance, and claims information current as of January 14 through January 16, 2014

⁴⁸ Bankruptcy = bankruptcy plan confirmed: Reinstated = reinstated by mortgagor: Reinstated ** = reinstated after loss mitigation: Forebearance = type II special forbearance: Ineligible = ineligible for loss mitigation