U.S. Department of Housing and Urban Development, Washington, DC

Home Equity Conversion Mortgage Program

Office of Audit, Region 3
Philadelphia, PA

Audit Report Number: 2015-PH-0004
August 21, 2015

To:	Kathleen A. Zadareky, Deputy Assistant Secretary for Single Family Housing, HU
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From:	David E. Kasperowicz, Regional Inspector General for Audit, Philadelphia Region, 3AGA
Subject:	HUD Policies Did Not Always Ensure That HECM Borrowers Complied With Residency Requirements

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of HUD's oversight of the Home Equity Conversion Mortgage (HECM) program.

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 215-430-6730.

Audit Report Number: 2015-PH-0004
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HUD Policies Did Not Always Ensure That HECM Borrowers Complied With Residency Requirements

Highlights

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD) oversight of its Home Equity Conversion Mortgage (HECM) program based on our strategic objective to protect the integrity of housing insurance and guarantee programs and because of residency issues identified in prior audits of the HECM program. Our objective was to determine whether HUD's Office of Single Family Housing had effective controls to ensure that HECM loan borrowers complied with residency requirements when concurrently receiving rental assistance from its multifamily programs.

What We Found

HUD policies did not always ensure that HECM borrowers complied with residency requirements. Of the 68 loans statistically selected for review, the borrowers for as many as 67 loans did not live in the properties associated with their loans because they received rental assistance from HUD's multifamily programs at a different address at the same time. This condition occurred because HUD's Office of Single Family Housing did not have controls to prevent or reduce the problem. Of the 67 loans, 18 were independently terminated by the servicing lenders during the audit. The remaining 49 insured loans had current balances totaling more than $7.1 million and maximum claim amounts totaling more than $8.4 million. As a result, 49 insured loans should be declared in default and due and payable to reduce the risk of loss to HUD's insurance fund of up to $1.3 million. Further, the borrowers for an additional 642 insured loans also may have violated the residency requirements. If HUD cannot confirm that these borrowers are complying with the residency requirements, these loans should also be declared in default and due and payable to reduce the risk of loss to HUD's insurance fund of up to $14.4 million.

What We Recommend

We recommend that HUD direct the applicable servicing lenders to verify borrowers' compliance with the residency requirements or for each noncompliant borrower, declare the loan in default due and payable, thereby putting up to $15.7 million to better use. Further, we recommend that HUD implement controls to prevent or reduce instances of borrowers violating residency requirements by concurrently participating in multifamily programs.

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Background and Objective

The U.S. Department of Housing and Urban Development (HUD) provides reverse mortgage insurance through the Home Equity Conversion Mortgage (HECM) program. The HECM program enables elderly homeowners to obtain income by accessing the equity in their homes. To be eligible for a loan, homeowners must be 62 years of age or older, have significant equity in their home, occupy the property as a principal residence, not be delinquent on any Federal debt, and participate in HUD-approved reverse mortgage counseling.

Borrowers are not required to repay the loan as long as they continue to occupy the home as a principal residence, maintain the property, and pay the property taxes and the mortgage insurance premiums. The loan agreement defines "principal residence" as the dwelling where borrowers maintain their permanent place of abode and typically spend the majority of the calendar year. A person may have only one principal residence at any one time. The borrower must certify to principal residency initially at closing and annually thereafter.

Servicing lenders are responsible for ensuring that borrowers meet the HECM program requirements, including the annual certification of principal residency. The mortgage note contains a clause stating that the lender may require immediate payment in full of all outstanding principal and accrued interest, upon approval of an authorized representative of the HUD Secretary, if the property ceases to be the principal residence of the borrower for reasons other than death and the property is not the principal residence of at least one other borrower.

HUD's Office of Multifamily Housing Programs provides project-based rental assistance to help families afford decent, safe, and sanitary housing. Under its programs, Federal funds are paid to multifamily project owners on behalf of tenants to keep the amount that tenants pay for rent affordable. The assistance is tied to the property, which means that the rental subsidy does not follow tenants if they move to another property. One of the key eligibility requirements for the multifamily rental assistance programs is that the rental unit for which a family applies must be the family's only residence. Further, project owners may establish rules stating when tenants may be terminated from the HUD programs due to extended absence or abandonment of the unit.

Our audit objective was to determine whether HUD's Office of Single Family Housing had effective controls to ensure that HECM loan borrowers complied with residency requirements when concurrently receiving rental assistance from its multifamily programs.

Results of Audit

Finding: HUD Policies Did Not Always Ensure That HECM Borrowers Complied With Residency Requirements

HECM borrowers did not always comply with residency requirements. Contrary to requirements, the borrowers for as many as 67 of the 68 loans reviewed did not live in the properties associated with their loans because they received rental assistance under multifamily programs for a different address at the same time. This condition occurred because HUD's Office of Single Family Housing did not have controls to prevent or reduce the problem. Of the 67 loans, 18 were independently terminated by the servicing lenders during the audit. The remaining 49 insured loans had current balances totaling more than $7.1 million and maximum claim amounts totaling more than $8.4 million. As a result, 49 insured loans were potentially ineligible and should be declared in default and due and payable to reduce the risk of loss to the Federal Housing Administration (FHA) insurance fund of up to $1.3 million. Further, the borrowers for an additional 642 insured loans also may have violated the residency requirements. If HUD cannot confirm that these borrowers are complying with the residency requirements, these loans should also be declared in default and due and payable to reduce the risk of loss to its insurance fund of up to $14.4 million.

Borrowers Violated HECM Program Residency Requirements

Contrary to requirements, the borrowers for as many as 67 loans did not live in the properties for which they obtained HECM loans. According to regulations at 24 CFR (Code of Federal Regulations) 206.39, the property associated with the loan must be the principal residence of each borrower at closing. Also, regulations at 24 CFR 206.211 require servicing lenders to at least annually determine whether the property associated with a loan is the principal residence of at least one borrower and require borrowers to certify that the property associated with the loan is their principal residence. Further, regulations at 24 CFR 206.27 state that the mortgage balance will be due and payable in full if the property ceases to be the principal residence of a borrower for reasons other than death and the property is not the principal residence of at least one other borrower.

We analyzed data in HUD's Single Family Data Warehouse[1] and its Tenant Rental Assistance Certification System[2] and identified 946 loans for which borrowers may have violated HECM program residency requirements by concurrently participating in multifamily programs. We statistically selected 68 of the loans for review. Based on reviews of documents obtained from

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[1] HUD's Single Family Data Warehouse system contains case-level information covering all the processes in the mortgage insurance life cycle of FHA-insured loans.
[2] HUD uses its Tenant Rental Assistance Certification System database to manage its multifamily rental assistance programs.

servicing lenders and multifamily projects, there was substantial evidence indicating that the borrowers for as many as 67 loans did not live in the properties associated with their loans because they received rental assistance under multifamily programs for a different address at the same time. The documented overlap of the loan and the borrower's participation in multifamily programs ranged from 4 to 36 months.[3] The borrowers for 65 of the 67 loans were listed as heads of household in multifamily programs. The remaining two loans each had two borrowers who were listed as heads of household, co-heads of household, or spouses in multifamily programs.

Of the 67 loans for which borrowers may have violated HECM program residency requirements,

- The borrowers for 18 loans certified that they occupied the properties associated with their loans as their principal residence during the overlap of participation in multifamily programs,

- The borrowers for 36 loans did not provide occupancy certifications during the overlap[4] of participation in multifamily programs, and

- The borrowers for 13 loans certified that they did not occupy the properties associated with their loans.

While they had a HECM loan, the borrowers for these 67 loans received rental assistance for a different address through various multifamily programs. Specifically, the borrowers for 53 loans participated in the Section 8 project-based assistance program, and the borrowers for 11 loans participated in the Section 202 Supportive Housing for the Elderly program. The borrowers for the remaining three loans participated in the Section 811, Section 236, and Rent Supplement programs.

HUD Lacked Adequate Controls To Prevent or Reduce the Problem

HUD did not have control policies or procedures to prevent or reduce instances of borrowers violating HECM program residency requirements by concurrently participating in multifamily programs. However, in response to a prior audit, HUD was updating its guidance to detail the steps that servicing lenders should take for borrowers who fail to certify at least annually that the property associated with the loan is their principal residence.[5] Those borrowers include borrowers who do not provide a certification, those who do not provide the certification in a timely manner, and those who certify that they no longer occupy the property. While this measure would not prevent instances of borrowers violating residency requirements, it could reduce the problem by removing some noncompliant borrowers. Borrowers who continue to

[3] The audit covered the period November 2011 through October 2014.
[4] In 18 of the 67 cases, the documented overlap was less than 12 months. Therefore, occupancy certifications may not have been due during the overlap.
[5] See the Followup on Prior Audits section for additional information.

certify that they occupy the properties associated with their loans would not be impacted by the updated guidance. To further protect its FHA insurance fund, HUD needs to implement controls to identify instances of borrowers violating residency requirements by concurrently participating in multifamily programs.

Conclusion

HUD's Office of Single Family Housing needs to quickly work with the applicable servicing lenders to verify documentation of the borrowers' compliance with residency requirements for each of the cases identified or for each noncompliant borrower, declare the loan in default and due and payable. Of the 67 loans, 18 were independently terminated by the servicing lenders during the audit. The remaining 49 insured loans had current balances totaling more than \$7.1 million and maximum claim amounts totaling more than \$8.4 million. HUD risks loss to its FHA insurance fund for the current balances, which include loan advances and accrued interest, servicing fees, and mortgage insurance premiums. Further, HUD risks up to \$1.3 million in potential future claim liabilities[6] for undisbursed loan amounts and continued accrual of interest, servicing fees, and mortgage insurance premiums.

Further, because we identified issues in 67 of the 68 loans reviewed, we believe that the borrowers for the loans not selected as part of our statistical sample also may have violated the residency requirements. HUD needs to work with the applicable servicing lenders to verify documentation of the borrowers' compliance with the residency requirements for 642[7] additional loans or for each noncompliant borrower, declare the loan in default and due and payable to reduce the risk of loss of up to \$14.4 million to its insurance fund.[8] Doing so would reduce the risk of loss to the FHA insurance fund because HUD would be relieved of potential future claim liabilities related to the undisbursed loan amounts as well as continued accrual of interest, servicing fees, and mortgage insurance premiums.

The Office of Single Family Housing can prevent or reduce instances of borrowers violating residency requirements by concurrently participating in multifamily programs by periodically coordinating with the Office of Multifamily Housing Programs to compare data in their respective systems. This measure will allow HUD to identify potential violators of the residency requirements and work with applicable servicing lenders to take steps to verify borrowers' residency or otherwise declare loans in default and due and payable as appropriate.

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[6] The \$1.3 million risk for potential loss was calculated by deducting the \$7.1 million total current loan balances from the \$8.4 million total maximum claim amounts for the 49 loans. This difference accounts for undisbursed loan amounts as well as the potential for continued accrual of interest and fees on the outstanding loan balances.

[7] We statistically selected 68 loans for review from the 946 loans identified through data analysis. Of the 878 loans not selected for review, 236 were terminated during the audit. The remaining 642 loans represent an ongoing risk to HUD's insurance fund.

[8] The \$14.4 million risk for loss was calculated by deducting the \$83.7 million total current loan balances from the \$98.1 million total maximum claim amounts for the 642 loans. This difference accounts for undisbursed loan amounts as well as the potential for continued accrual of interest and fees on the outstanding loan balances.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing

1A. Direct the applicable servicing lenders to verify and provide documentation of the borrower's compliance with the residency requirements for each of the 49 cases identified during our review of statistically sampled loans or for each noncompliant borrower, declare the loan in default and due and payable, thereby putting up to $1,317,749 to better use.

1B. Direct the applicable servicing lenders to verify and provide documentation of the borrower's compliance with the residency requirements for each of the additional 642 loans identified as potentially out of compliance or for each noncompliant borrower, declare the loan in default and due and payable, thereby putting up to $14,431,528 to better use.

1C. Implement controls to prevent or reduce instances of borrowers violating HECM program residency requirements by concurrently participating in multifamily programs, including policies and procedures to at least annually coordinate with HUD's Office of Multifamily Housing Programs to match borrower data in the Single Family Data Warehouse to member data in the Tenant Rental Assistance Certification System.

Scope and Methodology

We conducted the audit from October 2014 to June 2015 at our office in Philadelphia, PA. The audit covered the period November 2011 through October 2014 but was expanded as necessary to accomplish our objective.

To accomplish our objective, we reviewed

- Relevant background information on the loans and applicable regulations,
- HECM program requirements,
- Information in HUD's Single Family Data Warehouse,
- Information in HUD's Office of Multifamily Housing Programs' Tenant Rental Assistance Certification System,
- Accurint[9] information on the borrowers and the properties associated with the loans as needed,
- Loan documentation provided by the servicing lenders, and
- Multifamily programs documentation provided by multifamily projects.

We interviewed staff from HUD's Office of Single Family Housing.

For this audit, we compared Social Security numbers of borrowers for 899,402 endorsed HECM loans to more than 2.7 million participant Social Security numbers in the subsidized multifamily housing program data found in HUD's Tenant Rental Assistance Certification System. This comparison identified 1,027 potential matches. We performed additional data analysis on these matches and identified 972 unique matches in which we believe (1) the borrower was the same person as the household member shown in the multifamily housing program data, (2) the borrower was not listed as a live-in attendant in the multifamily housing program data, (3) the address for the HECM property did not match the rental property address for the multifamily program, and (4) there was an overlap in which the borrower had an active HECM loan while receiving rental assistance during the period November 2011 through October 2014. These 972 matches represent 946 HECM loans. We statistically selected 68 of the 946 loans for review. We reviewed documentation from the relevant lenders and multifamily projects for each of the loans selected.

We reviewed the documents outlined above to determine whether borrowers potentially violated HECM program residency requirements by concurrently participating in multifamily programs. Specifically, we reviewed loan applications, counseling letters, appraisals, loan agreements, settlement statements, deeds of trust, and annual recertification documents for each loan. For the

[9] Accurint is a public records search tool that includes more than 45 billion public and proprietary records.

multifamily programs, we reviewed the forms HUD-50059 and HUD-50059a[10] covering the audit period, along with inspection and lease information. Based on this review, the borrowers for as many as 67 loans did not live in the properties associated with their loans because they received rental assistance under multifamily programs for a different address at the same time. The remaining loan was found to comply with the residency requirements.

For the 67 loans that were potentially out of compliance with HECM program requirements, we obtained updated loan information from HUD's Single Family Data Warehouse. Since the beginning of our audit, 18 of the 67 loans cited had been terminated by the servicing lenders. As of May 31, 2015, the remaining 49 loans had current balances totaling more than $7.1 million and maximum claim amounts totaling more than $8.4 million. HUD risks loss to its FHA insurance fund for the current balances, which include loan advances and accrued interest, servicing fees, and mortgage insurance premiums. Further, HUD risks up to $1.3 million in potential future claim liabilities for undisbursed loan amounts and continued accrual of interest on the outstanding balances, servicing fees, and mortgage insurance premiums. The $1.3 million risk for loss was calculated by deducting the $7.1 million total current loan balances from the $8.4 million total maximum claim amounts for the 49 loans. While some of the 49 loans were in default, these loans represent an ongoing risk to HUD because interest, servicing fees, and mortgage insurance premiums continue to accrue until the loans are terminated. Also, because it is possible that the defaults on these loans could be cured, the borrowers could have access to additional undisbursed funds unless HUD ensures that the servicing lenders continue to pursue the defaults.

Because we identified issues in 67 of the 68 loans reviewed, we believe that the borrowers for the remaining 878 loans not selected as part of our statistical sample also may have violated the residency requirements. Of the 878 loans, 236 had been terminated since the beginning of our audit. As of May 31, 2015, the remaining 642 insured loans had current balances totaling more than $83.7 million and maximum claim amounts totaling more than $98.1 million. HUD risks loss to its FHA insurance fund for the current balances, which include loan advances and accrued interest, servicing fees, and mortgage insurance premiums. Further, HUD risks up to $14.4 million in potential future claim liabilities for undisbursed loan amounts and continued accrual of interest on the outstanding balance, servicing fees, and mortgage insurance premiums. The $14.4 million risk for potential loss was calculated by deducting the $83.7 million total current loan balances from the $98.1 million total maximum claim amounts for the 642 loans. While some of the 642 loans were in default, these loans represent an ongoing risk to HUD because interest, servicing fees, and mortgage insurance premiums continue to accrue until the loans are terminated. Also, because it is possible that the defaults on these loans could be cured, the borrowers could have access to additional undisbursed funds unless HUD ensures that the servicing lenders continue to pursue the defaults.

[10] Forms HUD-50059 and HUD-50059a are used by HUD's Office of Multifamily Housing Programs to collect data on the people who participate in multifamily programs.

We relied in part on computer-processed data in HUD's Single Family Data Warehouse and Tenant Rental Assistance Certification System. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing and found the data to be adequate for our purposes. The testing entailed matching information obtained from the Single Family Data Warehouse and the Tenant Rental Assistance Certification System to documents provided by servicing lenders and multifamily projects.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit 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 audit objective.

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 control was relevant to our audit objective:

- Compliance with laws and regulations – Policies and procedures that management has implemented to reasonably ensure that the use of resources is consistent with laws and regulations.

We assessed the relevant control 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 Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- HUD lacked adequate control policies or procedures to prevent or reduce instances of borrowers violating program residency requirements by concurrently participating in multifamily programs.

Followup on Prior Audits

U.S. Department of Housing and Urban Development, Washington, DC, Home Equity Conversion Mortgage Program; Audit Report 2014-PH-0001; Issued September 30, 2014

The following recommendation was still open at the time of this report: 1C. Update its guidance to detail the steps that servicing lenders should take for borrowers who fail to certify at least annually that the property associated with the loan is their principal residence. This includes borrowers who do not provide a certification, those who do not provide the certification in a timely manner, and those who certify that they no longer occupy the property. HUD agreed to update its guidance by issuing a mortgagee letter by August 30, 2015.

Appendixes

Appendix A

Schedule of Funds To Be Put to Better Use

Recommendation number	Funds to be put to better use 1/
1A	$ 1,317,749
1B	14,431,528
Total	**$15,749,277**

1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (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. In this instance, implementation of our recommendation to direct the applicable servicing lenders to verify and provide documentation of the borrowers' compliance with the residency requirements or for each noncompliant borrower, declare the loan in default and due and payable would reduce the risk of loss to the FHA insurance fund because HUD would be relieved of potential future claim liabilities related to undisbursed loan amounts and continued accrual of interest, servicing fees, and mortgage insurance premiums.

Appendix B

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation | **Auditee Comments**

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

OFFICE OF HOUSING

JUL 24 2015

MEMORANDUM FOR: David E. Kasperowicz, Regional Inspector General for Audit, Philadelphia Region, 3AGA

FROM: Kathleen A. Zadareky, Deputy Assistant Secretary for Single Family Housing, HU

SUBJECT: Auditee Response

HUD Policies Did Not Always Ensure that HECM Borrowers Complied with Residency Requirements
Audit Report Number: 2015-PH-XXXX

The Office of Inspector General (OIG) for Audit conducted an audit of HUD's oversight of the Home Equity Conversion Mortgage (HECM) Program. The objective was to determine whether HUD's Office of Single Family Housing had effective controls to ensure that HECM loan borrowers complied with residency requirements when concurrently receiving rental assistance from HUD's Office of Multifamily Housing Programs.

OIG's Finding:

HUD policies did not always ensure that HECM borrowers complied with residency requirements. Of the 68 loans statistically selected for review, borrowers for as many as 67 loans reviewed did not live in the properties associated with their loans because they received rental assistance under multifamily programs for a different address at the same time. This condition occurred because HUD's Office of Single Family Housing did not have controls to prevent or reduce the problem. Of the 67 loans, 18 were independently terminated by the servicing lenders during the audit. The remaining 49 loans should be declared due and payable to reduce the risk of loss to HUD's insurance fund of about $1.3 million. Further, the borrowers for an additional 642 insured loans also may have violated the residency requirements. If HUD cannot confirm that these borrowers are complying with the residency requirements, these loans should also be declared in default and due and payable to reduce the risk of loss to HUD's insurance fund of about $14.4 million.

Single Family Housing's Response:

The Office of Single Family Housing intends to address the audit recommendations as follows:

Comment 1

Upon receipt of the list of loans identified by the OIG, the Office of Single Family Asset Management (OSFAM) will instruct the servicers to obtain current occupancy certifications from the borrowers. Servicers will be further instructed to submit a due and payable request for any loans in which they are unable to provide an occupancy certification that is less than 12 months old.

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OIG Evaluation of Auditee Comments

Comment 1 HUD’s planned actions meet the intent of our audit recommendations 1A and 1B.