U.S. Department of Housing and Urban Development, Office of Single Family Housing

Voluntary Termination of Single-Family Insurance

Office of Audit, Region 7
Kansas City, KS

Audit Report Number: 2017-KC-0003
May 22, 2017

To: Robert Mulderig, Acting Deputy Assistant Secretary for Single Family Housing, HU

//**signed**//

From: Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

Subject: HUD Did Not Ensure That Lenders Properly Processed Voluntary Terminations of Insurance Coverage on FHA Loans and Disclosed All Implications of the Terminations to the Borrowers

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 Federal Housing Administration (FHA) single-family voluntary insurance termination requirements.

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 website. 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 913-551-5870.

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HUD Did Not Ensure That Lenders Properly Processed Voluntary Terminations of Insurance Coverage on FHA Loans and Disclosed All Implications of the Terminations to the Borrowers

Highlights

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development (HUD) to determine whether it ensured that lenders properly processed voluntary terminations of insurance coverage on single-family Federal Housing Administration (FHA) loans and disclosed all implications of the terminations to the borrowers. We initiated this audit because of our concern that borrowers might not be aware of the rights they give up when their insurance coverage is terminated.

What We Found

HUD did not always ensure that lenders properly processed voluntary terminations of FHA insurance for single-family loans and did not ensure that lenders disclosed all implications of voluntary termination of mortgage insurance to the borrowers. As a result, borrowers lost the protection of their FHA insurance coverage, overpaid FHA premiums, and were not fully informed of the financial impact of the voluntary terminations, and HUD's records were inaccurate.

What We Recommend

We recommend that HUD's Acting Deputy Assistant Secretary for Single Family Housing (1) investigate the 14 loans with unpaid mortgage amounts totaling more than $3 million, and require the lenders to obtain the borrowers consent, reinstate the insurance coverage, or take other action as appropriate given the facts of each particular loan; (2) remind lenders that voluntary termination is not the correct termination type to record third-party sales and borrower consent is required to terminate insurance, even if the loans are indemnified; (3) improve its procedures to detect and sanction improper voluntary terminations; and (4) update HUD Handbook 4000.1 to require the consent form to include an explanation that voluntary termination differs from mortgage insurance premium cancellation and the disclosure of any outstanding partial claims when lenders attempt to voluntarily terminate insurance.

Table of Contents

Background and Objective

The Federal Housing Administration (FHA) provides mortgage insurance for loans made by FHA-approved lenders throughout the United States and its territories. FHA mortgage insurance protects lenders against losses from homeowners' defaulting on their mortgage loans. The lenders bear less risk because FHA will pay a claim to the lender if a homeowner defaults on his or her loan. Loans must meet certain requirements established by FHA to qualify for insurance coverage.

One benefit of FHA mortgage insurance is that qualified borrowers have access to loss mitigation programs, which can provide protection against losing their homes. Loss mitigation is critical to FHA because it helps borrowers in default keep their homes while reducing the economic impact on the insurance fund. Borrowers are assisted through multiple types of FHA loss mitigation, including loan modifications and partial claims. Partial claims help borrowers keep their homes by advancing funds on their behalf to reinstate delinquent FHA-insured mortgages. The borrowers execute promissory notes and mortgages payable to the U.S. Department of Housing and Urban Development (HUD) when they accept the advances. Partial claim notes do not accrue interest and are not due and payable until their related FHA-insured mortgages are terminated. HUD's Financial Operations Center takes collection action against borrowers, including referring the delinquent debts to the U.S. Department of the Treasury. The U.S. Department of the Treasury can use methods, such as wage garnishment and tax return offsets, to recover unpaid partial claims.

FHA allows borrowers and lenders to cancel the mortgage insurance contract on a loan by mutual agreement. Once the mortgage insurance is voluntarily terminated by both parties, the mortgage is no longer governed by the FHA insurance program's rules and regulations as well as loss mitigation requirements. FHA requires lenders to document that they have obtained the borrowers' informed consent to terminate the insurance. Specifically, FHA requires lenders to inform borrowers in writing that electing to terminate the mortgage insurance means that the mortgage will no longer be governed by FHA insurance program rules, regulations, and loss mitigation requirements. Lenders must obtain signed consent from each borrower on the mortgage to voluntarily terminate the FHA mortgage insurance. The lenders must process the termination in the FHA Connection system within 15 days of receiving the signed consent. FHA Connection is a web-based system by which lenders access FHA systems and data.

Our objective was to determine whether HUD ensured that lenders properly processed voluntary terminations of insurance coverage on single-family FHA loans and that they disclosed all implications of the terminations to the borrowers.

Results of Audit

Finding 1: HUD Did Not Always Ensure That Lenders Properly Processed Voluntary Terminations

HUD did not always ensure that lenders properly processed voluntary terminations of FHA insurance for single-family loans. This condition occurred because HUD did not have policies and procedures to detect and deter lender errors while processing voluntary terminations. As a result, borrowers lost the protection of their FHA insurance coverage and overpaid FHA premiums, and HUD's records were inaccurate.

Improperly Processed Voluntary Terminations of FHA Insurance

HUD did not always ensure that lenders properly processed voluntary terminations of FHA insurance for single-family loans. We reviewed a statistical sample of 115 of the 3,690 loans that were voluntarily terminated during fiscal years 2015 and 2016. For 64 of these loans, lenders did not always obtain borrower consent, process the termination in a timely manner, or correctly process the termination as a voluntary termination.

<u>Signed Borrower's Consent Form</u>

In 14 of 115 cases reviewed, lenders did not obtain signed consent forms from all borrowers on a mortgage before voluntarily terminating the insurance. HUD Handbook 4000.1 states that the lender must obtain a signed borrower's consent to voluntary terminate FHA mortgage insurance from each borrower on the mortgage before it can process a voluntary termination of insurance. (See appendix C.) In one example, the lender mistakenly believed it did not need to get the signed borrower's consent because the loan was indemnified, which means the lender was not allowed to file an insurance claim on this loan. In several other cases, the lender failed to get the signature of the second person on the mortgage to properly execute the voluntary termination.

<u>Untimely Processing</u>

In 38 of 115 cases reviewed, lenders did not process voluntary terminations within 15 days of receiving the borrowers' written consent. HUD Handbook 4000.1 states that lenders must submit requests for voluntary termination of mortgage insurance via the FHA Connection system within 15 days of receiving the executed borrower's consent form. While lenders processed most of the consent forms within a month of receipt, a few processed them more than 3 months after receipt.

<u>Nonconveyance Foreclosure Sales</u>

In 12 of 115 cases reviewed, lenders improperly processed insurance terminations as voluntary terminations when they should have been processed as nonconveyance foreclosure sales. During a nonconveyance foreclosure sale, a lender or third party purchases the property at a foreclosure sale. The FHA Connection Guide requires lenders to process voluntary terminations of insurance transactions using a particular code (termination type 21) and process nonconveyance foreclosure transactions using a different code (termination type 13). The lenders should have used the code for nonconveyance foreclosures to process the transaction for these 12 loans.

Lender Errors Not Detected or Deterred by Policies and Procedures

HUD did not have policies and procedures to detect and deter lender errors while processing voluntary terminations.

HUD did not require the review of voluntarily terminated loans when conducting monitoring reviews. HUD published specific requirements for voluntary terminations in Mortgagee Letter 2014-13 but did not develop procedures to monitor for lender compliance, either as part of lender monitoring reviews or any other type of review.

In addition, HUD did not have a policy of penalizing lenders falsely certifying that they had the borrowers' written consent to terminate their FHA insurance. HUD Handbook 4000.1 requires lenders to certify that all borrowers on the mortgage have signed the consent form and the FHA Connection system displays a popup dialog box when each lender is about to submit a voluntary termination of insurance request. The popup dialog box states, "The servicer must have signed copies of the Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance from each of the borrowers on the mortgage before executing a voluntary termination pursuant to 24 CFR [Code of Federal Regulations] 203.295. Click OK to certify that the each of the borrowers on the mortgage has signed and provided to the servicer the Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance."

HUD did not have policies and procedures for reviewing voluntary terminations to determine whether they were done properly and then assess penalties against lenders that improperly terminated insurance.

Borrowers Harmed and HUD Records Inaccurate

Borrowers lost the protection of their FHA insurance coverage and overpaid FHA premiums, and HUD's records were inaccurate.

Borrowers in 14 of 115 cases with mortgages totaling an unpaid balance of more than $3 million lost their rights to FHA loss mitigation protections without consenting. By projecting these results to the universe, we estimate that 272 borrowers with unpaid mortgage balances of $35.8 million lost their FHA loss mitigation protections.

In addition, 38 borrowers in our sample paid a total of $2,000 more in mortgage insurance premiums than necessary when lenders failed to process the mortgage cancellation request within 15 days. However, the borrowers still had access to loss mitigation assistance during the delay, so they did obtain some benefit from the extra payments. By projecting these results to the universe, we estimate that 1,140 borrowers continued to pay premiums for insurance that remained in force after they requested termination.

Finally, FHA lacked reliable data on the volume and characteristics of voluntary terminations as well as nonconveyance foreclosures. These data inaccuracies could hamper its ability to analyze its past mortgage insurance activities, to perform future planning activities, and to generate reports showing insurance activity by lender.

Conclusion

HUD was not aware that lenders improperly processed voluntary terminations of insurance because it did not review these transactions. It also did not sanction lenders for terminating insurance without obtaining the required consent. We project that over a 2-year period, lenders improperly processed voluntary terminations for 1,910 FHA loans. HUD should develop procedures to review a sample of voluntary terminations, either as part of its regular monitoring reviews or using some type of a scorecard.

Recommendations

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

1A. Investigate the 14 loans with unpaid mortgage amounts totaling $3,035,819, and require the lenders to obtain the borrowers consent, reinstate the insurance coverage, or take other action as appropriate given the facts of each particular loan.

1B. Remind lenders that voluntary termination is not the correct termination type to record third-party sales and that borrower consent is required to terminate insurance, even if the loans are indemnified.

1C. Improve its procedures for detecting and sanctioning improper voluntary terminations.

Finding 2: HUD Did Not Ensure That Lenders Disclosed All Implications of Voluntary Termination

HUD did not ensure that lenders disclosed all implications of voluntary termination of mortgage insurance to the borrowers. This condition occurred because HUD did not have comprehensive disclosure requirements. As a result, borrowers were not fully informed of the financial impact of their voluntary termination decisions.

Implications of Voluntary Termination of Mortgage Insurance Not Disclosed

HUD did not ensure that lenders disclosed all implications of voluntary termination of mortgage insurance to the borrowers. Mortgagee Letter 2014-13 states that lenders are required to document that they have obtained the borrowers' informed consent to terminate their insurance coverage. We reviewed a statistical sample of 115 of the 3,690 loans that were voluntarily terminated during fiscal years 2015 and 2016. For 23 of these loans, although the lenders obtained the borrowers' signed consent, the borrowers were not fully informed as the lenders did not explain that partial claims would become due and payable or that monthly mortgage insurance premium cancellation differed from voluntary termination of insurance.

Partial Claims Become Due and Payable

When lenders received the borrowers' written consent to terminate their mortgage insurance, they did not disclose that partial claims associated with their loans would become due and payable in 22 of the cases in our sample. One lender stated that it did not provide disclosure or counseling or otherwise have contact with the borrowers about the acceleration of the partial claim notes because it was not required by HUD. These 22 loans are in contrast to 7 other loans in our sample for which another lender, realizing the potential financial harm to the borrowers, paid off the partial claims to HUD and informed the borrowers that their partial claim amounts would become due to the lender when the first mortgage was satisfied.

Mortgage Insurance Premium Cancellation Differs From Voluntary Termination of Insurance

In 1 of 115 cases reviewed, the lenders did not explain to the borrower the difference between monthly mortgage insurance premium cancellation and voluntary insurance termination. When the borrower requested the cancellation of her monthly mortgage insurance premium, the lender had her sign the consent for voluntary termination without explaining that voluntary termination would result in loss of FHA's loss mitigation protections, while premium cancellation would have retained those protections. Further, lenders' responses for other cases in our sample showed that the lenders themselves did not understand this distinction. In three cases, lenders processed voluntary terminations of insurance without signed consent forms rather than monthly mortgage insurance premium cancellations. When lenders process monthly mortgage insurance premium cancellations, the loans remain actively insured, and the borrowers are eligible for FHA loss mitigation protections. In the FHA Connection Guide, HUD notes that for eligible cases with a closing date after December 31, 2000, and a case number assignment date before June 3, 2013, the lender should not terminate insurance on the case if the borrower prepays the mortgage and reaches the required loan to value ahead of schedule. Instead, the lender should process a monthly mortgage insurance premium cancellation.

Inadequate Disclosure

HUD did not have adequate disclosure requirements for voluntary terminations. HUD's sample consent form did not include language informing borrowers that any outstanding partial claims become due upon mortgage insurance termination. In addition, HUD's sample consent form did not explain the difference between voluntary termination and mortgage insurance premium cancellation. When HUD introduced Mortgagee Letter 2014-13 in July 2014, it provided lenders with the sample consent form to document that they had received the borrowers' informed consent. This mortgagee letter was superseded on June 24, 2015, when its requirements were published in HUD Handbook 4000.1, FHA Single Family Housing Policy Handbook. HUD Handbook 4000.1 did not require lenders to disclose partial claim amounts to the borrowers when voluntarily terminating insurance. It also did not require lenders to disclose to the borrowers that voluntary terminations differ from mortgage insurance premium cancellation.

Financial Impact on Borrowers

Borrowers were not fully informed of the financial impact of their voluntary termination decisions.

Borrowers for 22 sample items had partial claims totaling $570,429 that became due without notice and for which HUD is about to start the collection process. If the borrowers do not repay these amounts, they will have their tax refunds or other income garnished. Two borrowers that we were able to speak with stated that they were unaware that their partial claims were now due and payable and were unable to satisfy them.

One borrower, who requested mortgage insurance premium cancellations and instead had her insurance terminated, would not receive the benefit of FHA loss mitigation if needed in the future. This borrower, with an unpaid mortgages balance of $195,941, lost her rights to future FHA loss mitigation protections. However, the lender proactively reinstated the FHA insurance on the loan after the audit started.

Conclusion

HUD's sample consent form did not ensure that borrowers gave their informed consent because it did not disclose to them that partial claims became due and payable upon insurance cancellation. In addition, the consent form language did not explain that voluntary termination differed from mortgage insurance premium cancellation. Over our 2-year audit period, borrowers had $570,429 in partial claims that became due and payable without being informed of such. If HUD updates its disclosure form, over the next year it will put half of that amount, or $285,215, to better use by ensuring that borrowers give informed consent before terminating their insurance coverage.

Recommendations

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

2A. Update Handbook 4000.1 to require the voluntary termination of insurance consent form to include an explanation that voluntary termination differs from mortgage insurance premium cancellation and the disclosure of any outstanding partial claims to put $285,215 to better use.

Scope and Methodology

To accomplish our objective, we

- interviewed HUD staff;
- reviewed Federal regulations, HUD handbooks, and mortgagee letters;
- reviewed HUD's Quality Assurance Division Desk Guide and FHA Connection Guide;
- selected and reviewed a statistical sample of loans for which insurance coverage was voluntarily terminated in HUD's Single Family Data Warehouse;
- reviewed sample documentation from lenders; and
- interviewed some of the borrowers associated with the sample loans.

We performed our audit between October 2016 and March 2017. Our audit generally covered October 1, 2014, through September 30, 2016. We conducted onsite work at HUD headquarters, 451 7th Street SW, Washington, DC.

The 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. Using this system, we identified 3,759 loans with insurance voluntarily terminated during fiscal years 2015 and 2016. We excluded 69 loans, which reduced our sampling universe to 3,690. We reviewed a sample of 115 of those loans with an unpaid mortgage balance of $19,123,286. See appendix D for a detailed explanation of our sample selection and results projection.

For each loan in our statistical sample, we requested from the lenders documentation of the borrowers' initial request to cancel the FHA insurance, the borrowers' written consent, the date of receipt of the consent, and any counseling or explanations given to the borrowers. We also requested information regarding the lenders' policies for voluntary terminations of loans with outstanding partial claims and any contact with the sampled borrowers regarding their partial claims. We also requested any further documentation relevant to explaining or supporting the voluntary termination of the FHA insurance on the sampled loans. We reviewed this information to determine whether each sampled loan had the required written consent, was terminated within 15 days of receiving consent, and was a voluntary termination rather than a nonconveyance foreclosure.

We also obtained the current status of the partial claims in our audit universe from HUD's National Servicing Center. The National Servicing Center contracts the servicing, collecting, and managing of partial claims to its national loan servicing contractor. We used this information to determine the stage in the collection process for each partial claim in our sample.

We relied in part on data maintained by HUD in its Single Family Data Warehouse database. Specifically, we relied on the data to identify loans with insurance coverage voluntarily terminated during our audit period. Although we did not perform a detailed assessment of the reliability of the data, we verified the fields used to determine our sample universe against documentary evidence supplied by the lenders for our 115 sample loans. Based on the work performed, we determined that the computer-processed data were sufficiently reliable for the purposes of this report.

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 controls were relevant to our audit objective:

- Controls to ensure that lenders complied with the requirements for voluntarily terminating FHA insurance coverage on single-family loans.

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 are significant deficiencies:

- HUD did not have policies and procedures to detect and deter lender errors while processing voluntary terminations of insurance (see finding 1).
- HUD did not have adequate disclosure requirements for voluntary terminations of insurance (see finding 2).

Appendixes

Appendix A

Schedule of Questioned Costs and Funds To Be Put to Better Use

Recommendation number	Unsupported 1/	Funds to be put to better use 2/
1A	$3,035,819	
2A		$285,215
Totals	3,035,819	285,215

1/ Unsupported costs are those costs charged to a HUD-financed or HUD-insured program or activity when we cannot determine eligibility at the time of the audit. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of departmental policies and procedures.

2/ 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 case, if HUD implements our recommendation, it will ensure that borrowers acknowledge their responsibility for the accelerated repayment of their outstanding partial claims when terminating their insurance. We believe this will provide greater assurance that FHA will recover those partial claims. Our estimate reflects only the initial year of this benefit. These amounts do not include potential offsetting costs incurred by HUD to implement our recommendations to strengthen controls.

Appendix B

Auditee Comments

The Acting Deputy Assistant Secretary for Single Family Housing informed us that HUD did not wish to provide written comments to include in the final report.

Appendix C

Criteria

HUD Handbook 4000.1(III)(A)(1)(l)(ii)(B)

Voluntary Termination of Mortgage Insurance

(1) Definition

A Voluntary Termination of Mortgage Insurance is a mutual agreement between the Borrower and the Mortgagee [lender] to terminate FHA mortgage insurance.

(2) Standard

The Borrower and the Mortgagee may agree to voluntarily terminate FHA mortgage insurance at any time.

(a) Borrower's Consent to Voluntary Termination

The Mortgagee must obtain a signed Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance from each Borrower on the Mortgage.

(b) Request for Voluntary Termination

To request voluntary termination, the Mortgagee must:

- submit the request for voluntary termination of mortgage insurance via FHAC [FHA Connection] within 15 Days of receiving the executed Borrower's Consent form; and
- certify in FHAC that all Borrowers on the Mortgage have signed the consent form.

Mortgagee Letter 2014-13 (July 3, 2014)

Subject: Voluntary Termination of FHA Mortgage Insurance

Background: Pursuant to 24 CFR 203.295, at the request of the borrower and mortgagee, FHA may terminate a mortgage insurance contract. Upon the voluntary termination of FHA insurance, the borrower and mortgagee are only entitled to those rights or benefits available if the insurance contract was terminated as a result of the insured mortgage being paid in full. Also, upon the termination of FHA insurance for any other reason, the mortgage is no longer governed by the FHA insurance program's rules and regulations, including FHA's Loss Mitigation requirements.

Mortgagees will now be required to document that they have obtained the borrowers' informed consent to terminate.

Voluntary Termination Documentation

In order to ensure that voluntary terminations of mortgage insurance are processed in accordance with the National Housing Act and HUD regulations, HUD now requires mortgagees requesting such termination to inform borrowers in writing that electing to terminate the mortgage insurance means that the mortgage will no longer be governed by FHA insurance program rules and regulations, including FHA's loss mitigation requirement.

Mortgagees must obtain a signed Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance. The form must be on the mortgagee's letterhead and must include the language in the sample form in Attachment 1. Each borrower on the mortgage must sign the consent form in order for request for voluntary termination to be considered valid by FHA.

Mortgagees must retain copies of the consent form(s) in the servicing file in accordance with HUD's record retention policies.

Processing Voluntary Terminations in FHA Connection

Voluntary terminations for single-family forward mortgages must be requested via FHA Connection. Mortgagees are no longer to use Electronic Data Interchange (EDI), Business-to-Government (B2G), and bulk processes for voluntary terminations.

When completing the Insurance Termination (HUD Form 27050-A) actions in FHA Connection, mortgagees must certify that all borrowers on the mortgage have signed the Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance. The voluntary termination will not be processed unless the mortgagee provides this certification.

Attachment 1

Borrower's Consent to Voluntary Termination of FHA Mortgage Insurance
Mortgagee:____________________________________
FHA Case Number:____________________________
Borrower's Name:______________________________
Property Address:______________________________

I/We, _____________________, as borrower(s), and Mortgagee are electing to voluntarily terminate the FHA insurance contract associated with my/our mortgage in accordance with Section 229 of the National Housing Act (*12 USC [United States Code] 1715(t)*) (*Act*).

I/We understand that upon the termination of FHA insurance, I/we, as borrower(s), and Mortgagee will be entitled only to those rights or benefits available if the insurance contract had terminated as a result of payment in full of the insured loan or mortgage.
I/We further understand that upon execution of this request, the Mortgagee may submit the Insurance Termination form (HUD Form 27050-A) to HUD and as of the termination date set forth on the Insurance Termination form the mortgage will no longer be governed by FHA insurance program rules and regulations, including FHA's loss mitigation requirements set forth in 24 CFR 203.501, and will no longer be subject to the collection of mortgage insurance premiums.

I/We certify that I/we have read and understand the foregoing and hereby consent to terminate the FHA insurance contract associated my/our mortgage.

Borrower(s):

Printed Name:________________________ Date:________________

Signature:____________________________

Printed Name:________________________ Date:________________

Signature:____________________________

Printed Name:________________________ Date:________________

Signature:____________________________

Sample Partial Claim Note

FHA Case No. _____________
PROMISSORY NOTE
[Date]
[Property Address]
1. PARTIES
"Borrower" means each person signing at the end of this Note, and the person's successors and assigns. "Secretary" or "Lender" means the Secretary of Housing and Urban Development and its successors and assigns.
2. BORROWER'S PROMISE TO PAY
In return for a loan received from Lender, Borrower promises to pay the principal sum of ___ Dollars (U.S. $________), to the order of the Lender.
3. PROMISE TO PAY SECURED
Borrower's promise to pay is secured by a mortgage, deed of trust or similar security instrument that is dated the same date as this Note and called the "Security Instrument." The Security Instrument protects the Lender from losses, which might result if Borrower defaults under this Note.
4. MANNER OF PAYMENT
(A)Time
On , [insert maturity date of insured primary mortgage] or, if earlier, when the first of the following events occurs:
(i) Borrower has paid in full all amounts due under the primary Note and related mortgage, deed of trust or similar Security Instruments insured by the Secretary, or
(ii) The maturity date of the primary Note has been accelerated, or
(iii)The primary Note and related mortgage, deed of trust or similar Security Instrument are no longer insured by the Secretary.

Appendix D

Sampling and Projections

Our sampling universe consisted of 3,690 loans, which had insurance termination dates during fiscal years 2015 or 2016 as defined by the "term_prcs_dt" in the FHA Single Family Data Warehouse. Voluntary terminations were identified with a "term_typ_cd" of "21." These loans were recorded as having a total outstanding balance of more than $646 million. This number did not include 69 loans, which had loan values exceeding $450,000.

To control for variance, we stratified loans by (1) the size of the servicing bank, (2) whether their insurance was cancelled as part of a large group on the same day, and (3) whether there was a partial claim loan on the mortgage. Loans were sorted and ranked by dollar value within these groups and stratified into six subgroups according to percentile points along this continuum. (See the sample design table below.)

We validated the sample design using replicated sampling (computer simulations) across several audit scenarios. A sample size of 115 was found to be sufficient.

Based on the design, we selected a statistical sample using the surveyselect procedure in SAS®, a widely used statistical software package.

Percentages, counts, and average dollar amounts were estimated and projected to the universe as a whole. Because all randomly selected samples are subject to "the luck of the draw," we calculated a margin of error for each type of measure and made a final projection on that basis. This was done by computing the mean and standard error of the percentages and dollar amounts using the means estimating procedure (surveymeans) and counts estimating procedures (surveyfreq) in SAS®. Variances were calculated using a Taylor series. We used the traditional formulas (Cochran 1977, Wayne W. Daniel 1983) for estimating the lower bounds (LCL) of counts and dollar amounts as noted below:

$$Count_{LCL} = N\ (pct - t_{\alpha/2}\ SE_{\%})$$

$$Amount_{LCL} = N(\mu - t_{\alpha/2}\ SE_{\$})$$

We found that 14 of the 115 insurance cancellations were missing signed consent from all borrowers. We also found that 38 of the borrowers in our sample paid extra insurance premiums because the lender delayed processing the termination. Taking together failures to obtain consent, delayed terminations, and mishandling of how third-party sales were recorded, we found 64 improperly handled insurance terminations in our sample. Applied to the loans in our universe, we can say the following things with a one-sided confidence interval of 95 percent:

<u>Projection of Terminated Loans That Were Missing Consent</u>
Based on our sample, we can say that the lender failed to obtain consent from all borrowers for at least 272 loans. These represented $35.8 million in unpaid balances after deducting a margin of error.

Calculations below:
(10.99% - 1.6583 X 2.16%) x N = 7.4% x N ≈ 272 policies cancelled without borrower consent

$(23671.72 - 1.6617 \times 8401.83) \times N \approx 9709.79 \times N \approx$ $35,800,000 in loans without signed consent

Projection of Terminated Loans That Were Processed Late

Based on our sample, we can say that delays in processing the termination cost borrowers at least $55,800 in extra insurance premiums after deducting a margin of error. These problems affected at least 1,140 loans.

Calculations below:

$(37.2\% - 1.6583 \times 3.46\%) \times N = 31.5\% \times N \approx 1{,}140$ loans with overpaid MIP [mortgage insurance premium]

$(23.56 - 1.6617 \times 5.07) \times N = 15.13 \times N \approx$ $55,800 in overpaid MIP

Overall Projection of Improperly Processed Terminated Loans

Based on our sample we can say, after deducting a margin of error, that at least 1,910 loans had their insurance terminated improperly due to missing borrower's signed consent, late processing of the consent, or mislabeling a third-party sale as a voluntary termination.

Calculations below:

$(59.03\% - 1.6583 \times 3.49\%) \times N = 53.2\% \times N \approx 1{,}910$ loans with improperly terminated insurance

Sample design

Strata	Lower bound	Universe	Samples	Wts.
BgBank_ComDate_0-10pct	> 0	194	4	48.500
BgBank_ComDate_10-30pct	≥ 79,850	387	8	48.375
BgBank_ComDate_30-50pct	≥ 118,570	451	10	45.100
BgBank_ComDate_50-70pct	≥ 154,321	470	10	47.000
BgBank_ComDate_70-90pct	≥ 203,912	499	11	45.364
BgBank_ComDate_90-100pct	≥ 289,832	302	6	50.333
BgBank_RanDate_0-10pct	> 0	112	2	56.000
BgBank_RanDate_10-30pct	≥ 79,850	167	3	55.667
BgBank_RanDate_30-50pct	≥ 118,570	179	4	44.750
BgBank_RanDate_50-70pct	≥ 154,321	214	4	53.500
BgBank_RanDate_70-90pct	≥ 203,912	199	4	49.750
BgBank_RanDate_90-100pct	≥ 289,832	109	2	54.500
SmBank_RanDate_0-10pct	> 0	78	2	39.000
SmBank_RanDate_10-30pct	≥ 79,850	72	2	36.000
SmBank_RanDate_30-50pct	≥ 118,570	40	2	20.000
SmBank_RanDate_50-70pct	≥ 154,321	43	2	21.500
SmBank_RanDate_70-90pct	≥ 203,912	28	2	14.000
SmBank_RanDate_90-100pct	≥ 289,832	12	2	6.000
YES_0-10pct	> 0	28	7	4.000
YES_10-30pct	≥ 79,850	38	10	3.800
YES_30-50pct	≥ 118,570	27	7	3.857
YES_50-70pct	≥ 154,321	17	5	3.400
YES_70-90pct	≥ 203,912	15	4	3.750
YES_90-100pct	≥ 289,832	9	2	4.500
Totals		3,690	115	