



**Weststar Mortgage Corporation  
Albuquerque, NM**

**Did Not Comply With HUD FHA Single Family  
Requirements for 10 Loans Reviewed**



Issue Date: August 2, 2012

Audit Report Number: 2012-FW-1012

TO: Charles S. Coulter  
Deputy Assistant Secretary for Single Family Housing, HU

//signed//

FROM: Gerald R. Kirkland  
Regional Inspector General for Audit, Fort Worth Region, 6AGA

SUBJECT: Weststar Mortgage Corporation, Albuquerque, NM, Did Not Comply With HUD  
FHA Single Family Requirements for 10 Loans Reviewed

Attached is the U. S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our review of Weststar Mortgage, LLP.

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 8L, 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.



August 2, 2012

Weststar Mortgage Corporation, Albuquerque, NM, Did Not Comply With HUD FHA Single Family Requirements for 10 Loans Reviewed

# Highlights

Audit Report 2012-FW-1012

## What We Audited and Why

We audited Weststar Mortgage Corporation, a Federal Housing Administration (FHA) nonsupervised direct endorsement lender located in Albuquerque, NM. We selected Weststar for review based on a risk assessment of lenders in New Mexico. Our objective was to determine whether Weststar complied with U. S. Department of Housing and Urban Development (HUD) and FHA loan origination requirements for loans on which the borrowers defaulted and FHA paid claims between 2009 and 2011.

## What We Recommend

We recommend that the Deputy Assistant Secretary for Housing require Weststar to (1) reimburse the FHA insurance fund \$554,130 for losses incurred on six loans that were ineligible for FHA insurance; (2) correct the data in Neighborhood Watch for two loans; (3) implement procedures to ensure that it enters correct information into Neighborhood Watch; and (4) discontinue the practice of allowing employees to sign documents for underwriters and loan officers.

## What We Found

Weststar violated HUD FHA underwriting requirements for 10 loan originations reviewed. Six of the loans had significant violations and did not qualify for FHA insurance. Further, Weststar entered erroneous data into HUD's Neighborhood Watch system.<sup>1</sup> This noncompliance occurred because Weststar misunderstood some requirements and ignored other requirements. As a result, HUD FHA incurred losses of \$554,130 for six loans that were ineligible for FHA insurance, and the Neighborhood Watch system contained erroneous data. Further, Weststar allowed employees to sign documents for an underwriter and a loan officer. Weststar had updated its policies and procedures as of May 2010. If followed, the updated policies and procedures should address the underwriting deficiencies identified in our review.

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<sup>1</sup> Neighborhood Watch is Web-based software that displays loan performance data for FHA insured single family loans. The system is designed to highlight exceptions so that potential problems are readily identifiable.

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## BACKGROUND AND OBJECTIVE

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Weststar Mortgage Corporation is a nonsupervised direct endorsement lender with in-house underwriting that does business as Weststar Loan Company in 10 states. Weststar primarily originates conforming, conventional, Federal Housing Administration (FHA), U. S. Department of Veterans Affairs, and U. S. Department of Agriculture mortgage loans. As of October 15, 2011, it had \$90 million in total production with 70 percent being FHA loans.

The direct endorsement program simplified 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. Weststar was responsible for complying with all applicable HUD FHA regulations and was required to evaluate the borrower's ability and willingness to repay the mortgage debt. Weststar was protected against default by FHA's Mutual Mortgage Insurance Fund, which is sustained by borrower premiums. 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 that might not be able to meet conventional underwriting requirements by protecting the lender against default.

Between January 1, 2009, and June 30, 2011, borrowers defaulted<sup>2</sup> on 58 Weststar-originated FHA mortgages with original mortgage values<sup>3</sup> totaling more than \$6.7 million. HUD FHA incurred losses<sup>4</sup> totaling more than \$2.4 million upon resale of the properties.

HUD's Quality Assurance Division reviewed Weststar's performance in 2007 and found 11 types of violations of HUD FHA requirements. Some of the violations included failing to comply with the provisions of the Real Estate Settlement Procedures Act, failing to properly calculate income, and allowing documents to pass through the hands of interested third parties. In 2011, the Quality Assurance Division performed another review and found only two types of violations of HUD FHA requirements. The violations included seller or dealer contributions exceeding limits and missing documentation.

Our objective was to determine whether Weststar complied with HUD and FHA loan origination requirements for loans on which the borrowers defaulted and FHA paid claims between 2009 and 2011.

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<sup>2</sup> HUD defines default as the borrower's failing to make any payment or perform any other obligation under the mortgage and such failure continues for a period of 30 days.

<sup>3</sup> Original mortgage value is the actual insured amount of the mortgage as determined by statutory limitations, minimum requirements, loan-to-value ratio limitations, and the original requested amount plus any unpaid portions of mortgage insurance premiums if applicable.

<sup>4</sup> The profit or loss amount is the calculated amount of profit or loss resulting from the sale of a HUD property.

## RESULTS OF AUDIT

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### Finding: Weststar Did Not Follow HUD FHA Requirements for 10 Loans Reviewed

Weststar did not follow HUD FHA requirements for 10 loans reviewed. While all 10 loans contained underwriting deficiencies, six contained significant deficiencies and did not qualify for FHA insurance. Weststar originated the deficient loans because it misunderstood some requirements and ignored other requirements. As a result, HUD FHA incurred losses of \$554,130.

**Weststar Did Not Follow HUD FHA Requirements for Originating and Documenting Loans**

Each of the 10 Weststar loans reviewed had underwriting deficiencies as shown in table 1. Appendix C contains case narratives describing the underwriting deficiencies for the six loans with significant deficiencies. The six loans were originated during 2007 and 2008.

Table 1: Summary of loan deficiencies

FHA case #	Types of deficiencies				Indemnification amount
	Income	Credit	Documentation	Miscellaneous	
491-9062802	x	x	x	x	\$72,887
492-8020459	x	x	x	x	\$80,472
491-9194756	x		x		\$145,626
491-8985420		x	x	x	\$103,752
492-7865955			x	x	
491-8959489			x		\$61,272
494-3385769			x		
492-7767217			x		\$90,121
361-3081450		x	x		
491-9122005			x	x	
<b>Total</b>					<u>\$554,130</u>

### **Three Loans Had Income Deficiencies**

Three of the 10 loans had income deficiencies. Two loans improperly included overtime in the income calculation. One loan had unsupported income because documents were incomplete.

For FHA loans 491-9062802 and 491-9194756, Weststar incorrectly calculated income using unsupported overtime. It did not obtain support for 2 years worth of overtime and develop an average of overtime for the past 2 years as required. Further, it did not document its reason for using overtime in the income calculation. HUD Handbook 4155.1, REV-5, paragraph 2.6, requires the lender to verify the borrower's employment for the most recent 2 full years. Paragraph 2.7.A of the Handbook allows both overtime and bonus income to be used to qualify if the borrower has received such income for the past 2 years and it is likely to continue. There was no such evidence in the file.

For FHA loan 492-8020459, the underwriter relied on incomplete income documents, including check stubs without the employer's information or check numbers. The underwriter should have resolved these discrepancies. Paragraph 3 of the Handbook requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial situation, source of funds for the transaction, and the intended use of the property. It further requires all information to be verified and documented.

### **Four Loans Had Credit and Processing Deficiencies**

Four loans had credit and processing deficiencies. Two loans were not downgraded to manual underwriting, and two loans with credit discrepancies were not properly justified, documented, or explained.

For FHA loans 491-9062802 and 491-8985420, Weststar should have processed the loans manually based on derogatory and delinquent credit items found on the credit reports, such as delinquent property taxes, a repossession, and four of five disputed consumer accounts on the credit report within a 2-year period of the loan's approval. Technology Open to Approved Lenders (TOTAL) Scorecard guidelines require an underwriter to conduct a manual review when a borrower's credit report reveals that the borrower disputed credit accounts or public records. The underwriter did not downgrade the loans, and there was no indication in the files that the underwriter reviewed the disputed collection accounts as required.

For FHA loan 492-8020459, the underwriter did not adequately analyze the borrower's overall pattern of credit behavior. The borrower had two unexplained

collection accounts on the credit report within a 2-year period of the loan's approval. Paragraph 2.3.C of the Handbook requires court-ordered judgments to be paid off before the mortgage loan is eligible for FHA insurance endorsement. It further requires the borrower to explain in writing all collections and judgments.

For FHA loan 361-3081450, the credit report in the file was not the same credit report used to qualify the borrower. The credit identification number on the credit report in the HUD file did not match the credit identification number listed on the Federal National Mortgage Association's underwriting findings. This discrepancy may not have made the loan ineligible, but it demonstrated an inconsistency in file documentation. Paragraph 3.1 of the Handbook requires the application package to contain all documentation supporting the lender's decision to approve the mortgage loan. When standard documentation does not provide enough information to support this decision, the lender must provide additional explanatory statements, consistent with other information in the application, to clarify or supplement the documentation submitted by the borrower.

### **Ten Loans Had Documentation Deficiencies**

All ten loans had various document deficiencies including lack of documentation for (1) gift wire transfers, (2) documents handled by the builder and transmitted through the builder's fax machine, and (3) a sales contract dated after the appraisal. Further, documents in the lender's files did not match documents submitted to HUD in all 10 files, and other Weststar employees signed documents for the underwriter and loan officer in six files. Some of the 10 loans had multiple document deficiencies.

For FHA loan 492-7767217, the gift letter was missing from both HUD's and the lender's files. Paragraph 2.10.C of the Handbook requires the lender to document gift funds by obtaining a gift letter, signed by the donor and borrower, that specifies the dollar amount of the gift; states that no repayment is required; shows the donor's name, address, and telephone number; and states the nature of the donor's relationship to the borrower. Further, the Weststar file contained an inconsistency in the amount of the gift funds. The HUD-1 settlement statement showed a gift of \$9,257, and the mortgage credit analysis worksheet showed the gift as \$10,235.

Weststar accepted employment and income documents that were handled by the builder and transmitted through the builder's fax machine for FHA loan 491-8959489, Paragraph 3.1 of the Handbook prohibits lenders from accepting or using documents relating to the credit, employment, or income of borrowers when those documents are handled by or transmitted from or through interested third

parties (for example, real estate agents, builders, sellers) or by using their equipment.

The underwriter did not ensure that both borrower's and coborrower's final applications for FHA loan 491-8959489 were submitted to HUD and copies were kept in the lender's files. Paragraph 3 of the Handbook requires the lender to ask sufficient questions to elicit a complete picture of the borrower's financial situation, source of funds for the transaction, and the intended use of the property and to verify and document the information. It further requires the lender to verify and document the identity of the loan applicant(s). The loan file did not contain the borrower's final application, and the lender did not provide a complete picture of the borrower's financial position.

For FHA loans 491-8985420 and 492-7865955, Weststar did not document the transfer of gift funds from the donor to the borrower and keep the documentation in its mortgage loan application binder as required by paragraph 2.10.C of the Handbook.

The sales contract for FHA loan 361-3081450 was dated after the appraisal. Weststar's staff stated that the sales contract was misdated.

For FHA loans 491-8959489, 492-7865955, 494-3385769, 492-7767217, 361-3081450, and 491-9122005, the underwriter's and loan officer's signatures were written by other persons. Weststar acknowledged obvious differences and said that other Weststar employees were allowed to sign the underwriter's or loan officer's names when they were in a hurry. This practice represented a serious internal control weakness.

For all 10 loans, there were differences between the documents in the HUD files and the documents in Weststar's files. HUD Handbook 4000.2, REV-3, paragraph 5.4, requires lenders to prepare and submit a uniform case binder to HUD. The case binder must be purchased from private sources, meet FHA specifications, and contain documents arranged as prescribed by FHA.

### **Five Loans Had Miscellaneous Deficiencies**

Three loans had TOTAL Scorecard deficiencies, including excessive submissions and erroneous database entries.

Weststar submitted FHA loan 491-9062802 to TOTAL Scorecard 37 times and used the 20<sup>th</sup> submission for approval. TOTAL Scorecard flagged the loan for the excessive submissions and recommended that the underwriter review the application for accuracy. For FHA loans 492-7865955 and 491-9122005, Weststar incorrectly entered two TOTAL Scorecard-approved FHA loans into

HUD's Neighborhood Watch system as manually underwritten. Weststar said the errors were due to a technical problem when submitting the file.

Three of the 10 loans, including loan 491-9062802 that was submitted 37 times, contained other miscellaneous errors.

For FHA loan 492-8020459, Weststar did not properly document the source of funds or confirm the borrower's bank account when the borrower stopped direct deposits. Paragraph 2.10.B of the Handbook requires a verification of deposit and allows the verification, along with the most recent bank statement, to be used to verify savings and checking accounts. If there is a large increase in an account or the account was opened recently, the lender must obtain a credible explanation of the source of those funds. For this loan, Weststar did not confirm, resolve, or document several items including

- The borrower did not have a bank account, but his payroll records showed that his checks were being direct deposited. He opened a checking account on the advice of the lender, and his direct deposits stopped. There was no indication of where the payroll payments were going or the source of the funds used to open the account.
- Housing obligation information was inconsistent. The borrower stated that he had been living in a travel trailer on family property for the past 4 years, but his loan application showed that he had been renting an apartment for the past 3 years. Paragraph 2.3.A of the Handbook requires the lender to determine the borrower's payment history of housing obligations through either the credit report, verification of rent directly from the landlord (with no identity of interest with the borrower) or verification of mortgage directly from the mortgage servicer, or canceled checks covering the most recent 12-month period.
- The borrower's downpayment of \$500 in earnest money, which was paid before the loan closing, was not included on the settlement statement as required by the Real Estate Settlement Procedures Act. The Real Estate Settlement Procedures Act requires the settlement statement to reflect any amounts paid against the sales price before settlement.<sup>5</sup>
- There were significant differences between the lender case file and the file that the lender submitted to HUD. For example, the HUD file had a copy of the gift letter, which was signed and dated, while the lender's copy was neither signed nor dated. In another example, the HUD file contained several key documents that the lender file did not contain. The HUD file contained a nonendorsement notice, which showed that the mortgage amount exceeded the maximum allowed and a reduction of principal was required before HUD's

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<sup>5</sup> 24 CFR (Code of Federal Regulations) Part 3500, appendix A, instructions for line 201 state that the line is to be used for "...any amount paid against the sales price prior to settlement."

endorsement. Further, verification documents, such as copies of the borrower's driver's license and Social Security card, were in the HUD file but not in the lender file. Also, regulatory documents, such as the limited denial of participation, excluded parties list system, and Credit Alert Interactive Voice Response System reports, were in the HUD file but not the lender file.

For FHA loan 491-9062802, the underwriter did not document an explanation for a verification of employment that had obviously been changed using whiteout. Also, for FHA loan 491-8985420, the borrower's bank statements obtained by the lender were not included in the assets information listed on the loan application or the TOTAL Scorecard report. Paragraph 3 of the Handbook states that the lender is responsible for asking sufficient questions to elicit a complete picture of the borrower's financial situation, source of funds for the transaction, and the intended use of the property. All information must be verified and documented. The lender must also verify and document the identity of the loan applicant(s).

### **Weststar Appeared to Have Improved Its Performance**

Following a HUD review in 2007, the Mortgagee Review Board sent Weststar a notice of violation listing 11 types of findings that violated HUD FHA requirements. In May 2011, HUD's Quality Assurance Division conducted a quality control review of Weststar to ensure that it complied with requirements. In its review, HUD questioned 4 of 41 loans reviewed. Weststar provided adequate evidence for two of the loans and submitted a signed indemnification agreement for the other two loans.

Based on a comparison of HUD's 2007 and 2011 reviews of Weststar's FHA mortgage origination activities, practices, and procedures, the lender had improved its loan origination performance. We reviewed and confirmed that Weststar had updated its policies and procedures as of May 2010. If followed, the updated policies and procedures should address the underwriting deficiencies identified.

### **Conclusion**

Weststar did not follow HUD FHA requirements for the 10 loans reviewed. Some of the loans contained multiple underwriting deficiencies. This noncompliance occurred because Weststar either misunderstood or ignored FHA guidance and allowed unqualified persons to sign for the underwriter and loan officer certifying that the loans were accurate and properly underwritten. As a result, HUD FHA incurred losses of \$554,130 in claims on six loans that were ineligible for FHA insurance.

## Recommendations

We recommend that the Deputy Assistant Secretary of Single Family Housing require Weststar to

- 1A. Reimburse FHA \$554,130 for losses incurred on six loans that were ineligible for FHA insurance.<sup>6</sup>
- 1B. Correct the data in Neighborhood Watch for FHA loans 492-7865955 and 491-9122005.
- 1C. Implement procedures to ensure that it enters correct information into Neighborhood Watch.
- 1D. Discontinue the practice of allowing employees to sign documents for underwriters and loan officers.

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<sup>6</sup> FHA case numbers 491-9062802, 492-8020459, 491-9194756, 491-8985420, 491-8959489, and 492-7767217

## SCOPE AND METHODOLOGY

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We performed our fieldwork between October 18, 2011, and March 6, 2012, at Weststar's corporate office in Albuquerque, NM, and our offices in Albuquerque, NM.

To accomplish our objective, we

- Reviewed applicable HUD FHA regulations, requirements, and mortgagee letters;
- Reviewed FHA's 2007 and 2011 Quality Assurance Division reviews and the Mortgagee Review Board notice of violation and settlement agreement in November 2007 and August 2008, respectively;
- Reviewed a random sample of 10 of the 30 FHA loans that Weststar originated during 2007 and 2008 that were foreclosed upon and resold between 2007 and 2010;
- Reviewed Weststar's files, quality control plan, and policies and procedures;
- Conducted interviews with applicable Weststar staff; and
- Reviewed profit and loss data from HUD's Single Family Data Warehouse system.

We obtained a download of Weststar-originated loans, which had defaulted and on which HUD FHA had paid claims between January 1, 2009, and June 30, 2011. This download resulted in 58 loans with original loan values totaling more than \$6.7 million. HUD's Quality Assurance Division had conducted a review of Weststar in 2011, so we compared the 58 loans to the FHA loans reviewed in 2011 and determined that no duplicate files were selected. We selected a random sample of 30 loans on which HUD had incurred losses.<sup>7</sup> We narrowed the sample to 10 loans: the 5 loans that were listed as manually underwritten<sup>8</sup> and 5 randomly picked loans that had defaulted before the first payment.

We did not evaluate the reliability of HUD's Neighborhood Watch system because we were not auditing the system and used it only to select an auditee and identify which loans to review.

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. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

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<sup>7</sup> HUD paid claims, took possession of the properties, and incurred losses upon selling the properties.

<sup>8</sup> The loans were not processed through an automated underwriting system.

# INTERNAL CONTROLS

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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.

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## Relevant Internal Controls

We determined that the following internal control was relevant to our audit objective:

- Safeguarding FHA insured mortgages from high-risk exposure.

We assessed the relevant control identified above.

## Significant Deficiency

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

- Weststar allowed employees to sign documents for an underwriter and a loan officer (finding).

## APPENDIXES

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### Appendix A

#### SCHEDULE OF QUESTIONED COSTS

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Recommendation number	Ineligible <sup>1/</sup>
1A	\$554,130

<sup>1/</sup> 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.

## Appendix B

# AUDITEE COMMENTS AND OIG'S EVALUATION

### Ref to OIG Evaluation

### Auditee Comments



July 6, 2012

#### VIA FEDERAL EXPRESS

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

**RE: Weststar Mortgage Corporation  
HUD OIG Draft Audit Report**

Dear Mr. Kirkland:

Weststar Mortgage Corporation ("Weststar" or "Company") is in receipt of the letter dated June 12, 2012 from the U.S. Department of Housing and Urban Development's ("HUD" or "Department") Office of Inspector General ("OIG") enclosing a draft report ("Report") stemming from the survey of ten Federal Housing Administration ("FHA") insured loans originated by Weststar in 2007 and 2008, on which FHA paid claims between 2009 and 2011.

The Report states that its primary objective was to perform a risk assessment of FHA-approved lenders in New Mexico and determine whether Weststar complied with HUD and FHA loan origination requirements. The Report alleges that six loans contained underwriting deficiencies, that Neighborhood Watch data was incorrectly entered in two cases, and that certain employees signed documents for other employees. Based on these assertions, the Report recommends that HUD require the Company to: (1) indemnify it in connection with the six loans involving underwriting deficiencies; (2) correct data in HUD's Neighborhood Watch system for two loans and implement procedures to ensure that it enters correct information into Neighborhood Watch; and (3) discontinue the practice of allowing employees to sign documents for other employees.

The OIG provided Weststar with an opportunity to submit written comments for inclusion in the final report. This response summarizes the Company's history

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NMLS Company ID #93243





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and operations and addresses the individual findings in the Report. We appreciate this opportunity to comment on the OIG's 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 company is not provided an opportunity to respond to these additional comments. Often, these comments include substantive allegations or statements that were not a part of the draft audit report provided to the company. 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 picture of the issues is presented in the final report.

#### **I. BACKGROUND**

Weststar opened for business in 1984 as a direct lender specializing in financing and purchasing non-conventional loans and servicing real estate contracts in private transactions. The Company received approval to participate in the Department's FHA mortgage insurance programs as a non-supervised mortgagee in September of 1993. During the time period at issue, Weststar's operations included a small mortgage lending division, which concentrated on providing FHA-insured loans to customers in the Texas manufactured housing market. Throughout most of the relevant period, the Company sold FHA-insured loans that it originated into the secondary market on a servicing-released basis. Its primary investors included Chase, GMAC Mortgage, and Taylor Bean and Whitaker. During this period, however, many investors ceased purchasing FHA-insured loans secured by manufactured housing.

The Company acts as a principal for two authorized agents and is an authorized agent for six principals. The Company enjoys excellent relationships with both consumers and its investors, and Weststar's employees consistently strive to produce high quality loans in compliance with HUD/FHA standards. FHA lending constitutes approximately sixty percent (60%) of Weststar's current loan production. As FHA-insured loans comprise a significant portion of its loan origination business, the Company takes its relationship with the Department and its responsibilities under the FHA program seriously. We strive to comply with applicable rules and regulations and are committed to educating and training our employees on issues of FHA compliance.

#### **II. RESPONSE TO THE FINDINGS**

After receiving the draft Report, Weststar conducted a thorough review of the findings and loan files cited therein. It examined HUD/FHA guidelines, as well as the





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**Comment 1**

Company's internal policies and procedures, in an effort to provide pertinent information and documentation with this response. Based on this stringent review, the Company believes indemnification would be unwarranted for the six loans identified in the draft Report. In these cases, the findings in the Report are at variance with the facts, do not constitute violations of HUD/FHA requirements, or do not affect the underlying loans' insurability. Although Weststar recognizes that there is always room for improvement, at no time did the Company intentionally disregard HUD guidelines or knowingly misrepresent information to the Department. We believe, and we hope the Department will agree, that this response and accompanying exhibits demonstrate Weststar's general compliance with HUD/FHA requirements and adherence to prudent lending standards with respect to the remaining loans that comprise this matter. Below we reply to the individual matters raised in the draft Report.

**Comment 2**

As an initial matter, while the draft Report notes in the Scope and Methodology section that the loans at issue were originated more than five years ago in 2007 and 2008, the body of the Report and Recommendations sections include several references to the time period in which the loans defaulted and during which HUD paid FHA insurance claims, which give the readers the impression that any issues identified occurred much more recently than the time period during which the referenced origination conduct occurred. As acknowledged in the Report, in the five years since this handful of loans were originated, the Company has "improved its loan origination performance" which the Report acknowledges in the "Results of Audit" section. For these reasons, we request that the references to the time periods associated with these loans include references to the origination time period rather than the timeframe in which the loans defaulted to give the reader a clear picture of the time period during which the referenced origination activities occurred.

**A. WESTSTAR COMPLIED WITH HUD'S UNDERWRITING GUIDELINES**

The Report alleges that Weststar did not underwrite six of the ten loans reviewed in compliance with HUD requirements. Specifically, the Report asserts that these loans involved deficiencies in: (1) income documentation; (2) credit documentation; (3) documentation involving gifts and other underwriting criteria; and (4) miscellaneous areas.<sup>1</sup> We address the individual assertions made in the six cited loans in turn below.

<sup>1</sup> We note that the draft Report asserts that the remaining four loans reviewed contained less significant deficiencies involving gift documents and signatures that were not serious enough to





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**1. Income Documentation**

**Comment 3**

The Report contends that the Company did not properly assess or document the borrowers' income in three cases. Weststar respectfully disagrees with these assertions. It is Weststar's policy and practice to comply with income requirements in all FHA loans, and we maintain that the Company did so in the loans cited in the Report. Our individual responses to these cases are set for the below.

**a. FHA Case No. 491-9194756**

**Comment 3**

In this case, the Report asserts that overtime income was improperly included in the borrower's qualifying income. Weststar respectfully disagrees. With regard to overtime income, HUD guidelines generally permit the use of overtime income to qualify a borrower when these earnings can be documented for the past two years. See HUD Handbook 4155.1 REV-5, ¶ 2-7(A).<sup>2</sup> Here, the Company properly included the borrower's overtime income in the qualifying income, as the loan files documented that the borrower had been receiving overtime income for more than two years. The Verification of Employment ("VOE") documented that the borrower had been employed with Crossroads Transportation for almost six years and that his current base salary was \$700 per week (**Exhibit A-1**), or \$36,400 annually. The VOE also documented significant overtime earnings for 2008, the current year, as well as the fact that the borrower was working an overage of 5-15 hours of overtime per week and overtime earnings were likely to continue (**Exhibit A-1**). The borrower's 2008 overtime was confirmed on his paystub (**Exhibit A-2**). While the borrower's employer did not include information on the VOE regarding the prior years' base or overtime earnings, the borrower's 2006 and 2007 IRS W-2 forms showed earnings of \$44,302 and \$55,257, respectively (**Exhibits A-3 and A-4**), which demonstrated that the borrower had earned significant overtime pay above the borrower's base salary for more than two years prior to the loan closing. The borrower had also recently received a raise, and had a good probability of continued employment (**Exhibit A-1**). Because the loan file contained documentation reflecting significant overtime earnings for more than two years with the probability

negatively impact loan approval. As Weststar addressed these issues throughout the OIG's survey, and the auditors determined that these findings do not warrant further action by HUD, we have not provided individual responses to these cases herein.

<sup>2</sup> While the Department has issued a new online version of Mortgage Credit Analysis Handbook, 4155.1, the new Handbook became effective for loans originated on or after May 11, 2009, after the loans cited in the Report were originated and closed. We therefore rely on the prior Handbook, 4155.1 REV-5, and accompanying Mortgagee Letters throughout this response.





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that it would continue, the Company complied with all applicable HUD guidelines and properly included the overtime earnings in the borrower's qualifying income. Therefore, indemnification in this case would be inappropriate and we request that this loan be removed from the final report.

**b. FHA Case No. 491-9062802**

Here, the Report also alleges that overtime income was improperly considered in the borrower's qualifying income, as the loan file documented less than two years of overtime earnings. HUD guidelines permit lenders to consider overtime income earned for periods of less than two years, provided that the underwriter adequately justifies and documents his or her reason for using the income for qualifying purposes. See HUD Handbook 4155.1 REV-5, ¶ 2-7(A). In this case, the VOE and paystub documented 10 months of overtime income in 2007, indicated that the borrower worked an average of 15 hours of overtime per week, and evidenced that overtime was likely to continue (**Exhibits B-1 and B-2**). Although the employer did not provide income information for 2006, the borrower had just received a pay increase several days before the VOE was completed, which was not used for income calculation purposes (**Exhibit B-1**). Moreover, the underwriter used a conservative monthly average of overtime earnings, as the borrower's monthly income with overtime was \$3,411.06, but the underwriter used only \$2,811.26 in effective income (**Exhibit B-3**). Based on the clearly documented overtime earnings in 2007, the underwriter reasonably included this income on the Mortgage Credit Analysis Worksheet ("MCAW") in compliance with HUD guidelines. For these reasons, indemnification is unwarranted and we respectfully request that this assertion be removed from the final report.

**c. FHA Case No. 492-8020459**

In this case, the Report asserts that the income documents contained incomplete information, as one of the borrower's paystubs did not contain employer information or a check number. As you know, HUD guidelines require FHA-approved lenders to obtain a VOE and one paystub to verify the borrower's income and employment history. See HUD Handbook 4155.1 REV-5, ¶ 3-1. In this case, the loan file contained a written VOE (**Exhibit C-1**), two paystubs (**Exhibit C-2 and C-3**), a detailed check activity report (**Exhibit C-4**), and W-2 forms for 2006 and 2007 (**Exhibit C-5 and C-6**). Although one of the paystubs did not contain employer information or a check number, Weststar transmitted a copy of the check to the borrower's employer, Polk Mechanical Company, and received verification of the information from a representative of the employer, who signed the paystub copy,



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thus verifying the income information on that document (**Exhibit C-2**). Based on this verification and the extensive supporting income documentation, the Company maintains that it complied with applicable HUD guidelines to document the borrower's income in this case. As a result, indemnification is unwarranted and this case should be removed from the Report.

## **2. Credit/Processing Documentation**

In four loans, the Report takes issue with the analysis of the borrowers' credit histories. Weststar respects the importance of analyzing a borrower's credit performance and examining his or her attitude towards credit obligations. It is Weststar's policy and practice, with respect to every FHA applicant, to scrutinize the applicant's credit record and reasonably determine the potential borrower's creditworthiness. Given the potential risks not only to the Department, but also to the Company, of making a poor credit decision, the Company's management endeavors to monitor underwriting performance and provide ongoing training to employees on the issue of credit analysis. Weststar's employees take their underwriting responsibilities seriously and understand that they will face severe consequences for unsatisfactory analysis of borrower credit. The Company takes its underwriting responsibility seriously and would never knowingly approve a loan to an unqualified borrower.

In the cases cited in the Report, Weststar complied with FHA guidelines by examining the borrowers' overall pattern of credit behavior and reasonably determining that the borrowers qualified for FHA financing and documenting that decision pursuant to relevant guidelines. The Company properly considered each borrower's previous housing obligations, recent and/or undisclosed debts, collections, judgments, and bankruptcies, and Weststar underwriters reasonably determined that past derogatory items did not reflect a current disregard for financial obligations. The loan files contain required documentation and the Company prudently exercised the discretion granted to it by the FHA. As discussed below, the borrowers in these cases generally were hard-working individuals who took responsibility for their financial obligations. As a result, the Company adhered to FHA requirements by reasonably determining that the borrowers were creditworthy and qualified for FHA loans. Below, we address each of the cases cited in the Report.



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**a. Credit Analysis and Documentation**

**Comment 4**

In three cases, **FHA Case Nos. 491-9062802, 492-8020459, and 491-8985420**, the Report alleges that the loan file did not contain an adequate explanation of derogatory credit. As discussed above, HUD has delegated discretion to lenders to evaluate a borrower's creditworthiness. These three loans were all underwritten using Fannie Mae's Desktop Underwriter ("DU"). The user guide for DU dictates the credit-related documentation a lender must obtain in loans underwritten with this system. In connection with loans underwritten by automated underwriting systems, FHA guidelines state that the lender is accountable for documentation aspects not addressed in the user guides provided by the automated underwriting system's creator. See Mortgagee Letter 99-26. Verification messages are provided on the Fannie Mae Underwriting Findings Report specifying the specific credit documentation required in each case. Based on these directives, in loans underwritten by DU, Weststar obtained the documentation indicated in the verification messages provided in the Underwriting Findings Reports.

With regard to the three cited loans, the Report alleges that Weststar did not obtain an adequate explanation of derogatory credit items – specifically, collection accounts and delinquent property taxes. Two loans, **FHA Case Nos. 491-9062802 and 491-8985420**, received "Approve/Eligible" ratings from DU, indicating that the loans met both credit risk and eligibility requirements. Weststar complied with the approval conditions on the Underwriting Findings Reports with regard to credit documentation in these cases, which explicitly stated, "No further explanation for any adverse or other derogatory information is required" in paragraphs 18 and 23, respectively (**Exhibits D-1 and D-2**). Moreover, with regard to HUD's Technology Open Approved Lenders ("TOTAL") Scorecard requirements, while the draft Report correctly states that manual downgrades were required for disputed accounts, the TOTAL Scorecard requirements for collection accounts expressly state that "collection accounts for accept/approve risk classifications trigger neither an explanation requirement nor a hypothetical monthly payment to be used in qualifying the borrowers . . . [t]he presence of collection accounts in the borrower's credit history already result in lowering the credit bureau scores used in TOTAL and, this, no further information need be provided by the borrower." See Mortgagee Letter 05-15; FHA TOTAL Mortgage Scorecard User Guide, page 24. The collection accounts in the two loans at issue were included on the credit report considered by DU in the loan approval process, and the Underwritings Findings Report did not require Weststar to obtain an explanation regarding the collection accounts. Therefore, the loan files contained all necessary credit documentation in accordance with HUD requirements and manual downgrades were not warranted.





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The draft Report also alleges that the borrower's credit history was not fully analyzed in **FHA Case No. 491-9062802**, as delinquent property taxes were not on the credit report and were not considered by the automated underwriting system as derogatory credit. The Company disagrees with this assertion and maintains that this loan was processed in accordance with HUD guidelines. As evidenced by the tax certification (**Exhibit D-3**), the taxes on the property had been delinquent since 1999. Because the borrower did not take title to the property until 2004 (**Exhibit D-4**), the taxes were delinquent at the time the borrower acquired it. As a result, the delinquent property taxes were not "derogatory credit" with regard to the borrower, as the borrower had not created the delinquency and, as such, the item had no bearing on the borrower's attitude toward credit obligations. Thus, a manual downgrade was not required based on this tax debt, which the borrower satisfied at closing (**Exhibit D-5**).

In **FHA Case No. 492-8020459**, the loan received a "Refer/Eligible" rating from DU. Although the borrower's credit report showed several collection accounts, all three collection accounts were from 2004, more than four years prior to loan closing, and the borrower had successfully paid off one of the accounts (**Exhibit D-6**). In addition, the credit report evidenced that, over the past four years, the borrower had reestablished credit and was making timely payments on his current credit obligations, including paying off a high balance auto loan (**Exhibit D-6**). In sum, because the collection accounts were aged and the borrower had successfully reestablished credit, the underwriter reasonably determined that past credit problems did not pose a risk to the borrower's ability to make regular mortgage payments.

For the reasons discussed above, Weststar maintains that it complied with applicable HUD and guidelines in analyzing and documenting the borrowers' creditworthiness in these cases and, as a result, indemnification would be unwarranted. We respectfully request that these findings be removed from the final report.

#### **b. Disputed Accounts**

In **FHA Case No. 491-8985420**, the Report asserts that the borrower's credit report contains five accounts that had been disputed by the borrower and, therefore, the loan should have been manually underwritten. As discussed above, Weststar understands and appreciates that the TOTAL Scorecard User Guide requires a loan in which a borrower is disputing credit accounts to be referred to an underwriter for

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review. See FHA TOTAL Mortgage Scorecard User Guide, page 15; Mortgagee Letter 04-47. It was the Company's policy and practice to require manual underwriting review in such circumstances and we have reminded our employees of this requirement. Nevertheless, in this isolated instance, a manual underwriting review did not occur. That said, any oversight constituted, at worst, harmless error, as an underwriter could have reasonably approved the loan in spite of the disputed accounts. In this case, two of the referenced accounts were paid off by the borrower and had a zero balance (**Exhibit E-1**). The remaining two accounts had balances of less than \$500, and the last active dates on the accounts were more than 24 months prior to the loan application (**Exhibit E-1**). Based on these circumstances, an underwriter reasonably could have concluded that these past accounts had been resolved and/or did not reflect the borrower's current attitude toward credit obligations. In fact, in 2011, HUD's guidance was amended so that disputed accounts no longer need to be referred to an underwriter for review if any of the following circumstances apply: (1) the disputed account has a zero balance; (2) the disputed account is marked as "paid in full" or "resolved"; or (3) the disputed account is less than \$500 and more than 24 months old. See FHA TOTAL Mortgage Scorecard User Guide, page 15. All four accounts at issue in this case meet one of these exceptions, removing the need for a manual underwriter's review. For these reasons, indemnification in this case would be inappropriate and we respectfully request that this loan be removed from the final report.

### **3. Documentation**

In all ten loans reviewed, the Report asserts issues with various loan file documentation, including case binder documentation, document signatures, gift fund documents, and employment documents. We respond to a representative sample of these issues below.

#### **a. Loan File and Case Binder Documents**

In all ten cases at issue, the draft Report contends that documents in the Company's loan files did not correspond with documents provided to the Department during the FHA insuring process. As the OIG is aware, the Department requires FHA-approved lenders to retain all documents, including prior versions, in each FHA-insured loan, as well as compile a "case binder" of certain enumerated final documents on which the lender relied in originating the loan. HUD Handbook 4165.1 REV-2, ¶ 1-5. It is Weststar's policy and procedure to adhere to these requirements. In doing so, the Company's "loan file" will include additional documents and drafts of forms that are not required to be submitted to HUD in the





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**Comment 5**

case binder. Thus, in every instance, the case binder will not mirror the exact case binder submission. This does not constitute a violation of FHA requirements, but in fact is necessary to meet HUD's requirements of retaining all loan file documents and submitting a complete and accurate case binder in all cases.

Moreover, with regard to case binder submissions, in every case, Weststar endeavored to construct a case binder for submission to HUD that reflected the correct final loan documentation as required by HUD Handbook 4165.1 REV-2, ¶ 1-5 as well as retain a complete copy of the case binder documents submitted to HUD. At present, that process occurs through electronic imaging of file documentation. During the time period the loans reviewed in this survey were originated, however, Weststar's staff manually collected documents from our files to build the HUD case binder. Manual document collection and assembly is a process that inherently presents a risk of inadvertent mistakes, and it is possible that in some instances a non-final document was unintentionally included in the HUD case binder or a copy of the final document included in the case binder was not retained in the Company's loan file. We are confident that enhancements to the compilation and submission of case binders have resolved any concerns identified in the loan files reviewed and that any issues related to compiling case binders will not recur.

**Comment 6**

**b. Employee Signatures**

The draft Report asserts that in six cases, certain employees signed documents on behalf of other employees. During the course of the survey, HUD asked for explanations regarding different signatures on documents in two cases. In both cases, as previously explained, an employee was out of the office and provided express authorization for another employee to sign his or her name to a document on his or her behalf. In these limited instances, the authorizing employee possessed knowledge of the content of documents being signed and provided contemporaneous authorization to another employee to sign his or her name. With regard to the remaining loans referenced, the draft Report does not provide details regarding the signatures or documents at issue other than a general reference to one loan application and thus, the Company is not able to address the Report's concerns absent additional information. That said, contrary to the statement in the Report, at no time did the Company permit employees to sign another employee's name "When they were in a hurry," and we respectfully disagree that this issue represented a control weakness. Moreover, prior to the OIG's survey, the Company implemented procedures prohibiting employees from signing documents on behalf of other employees in any circumstances and requires each individual employee only sign his or her own name. We trust that this explanation resolves any outstanding





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concerns in connection with this issue and respectfully request that these assertions be removed from the final report.

**c. Gift Documentation**

In **FHA Case Nos. 492-7767217** and **491-8985420**, the Report asserts issues related to documentation to support gift funds received by borrowers that were used to close the loans. We respond to the individual assertions in turn below.

**Comment 7**

In **FHA Case No. 492-7767217**, the Report alleges that the Company did not retain the gift letter to document the gift funds used as a down payment. Weststar understands and appreciates that, to document gift funds in FHA loans, a lender must obtain a gift letter indicating that the funds are provided as a gift with no expectation of repayment, as well as evidence that the funds were actually provided by the donor to the borrower. See HUD Handbook 4155.1 REV-5, ¶ 2-10(C). The Company strictly adheres to these guidelines and requires that a gift letter is received and retained for all FHA loans. Contrary to the Report's assertions, a gift letter from the Home Downpayment Gift Foundation was retained in the loan file and evidenced a gift of \$10,235 (**Exhibit F-1**). Because the Company complied with HUD's guidelines by retaining a copy of the gift letter, indemnification is unwarranted in this case and we request that this loan be removed from the final Report.

**Comment 8**

The Report also asserts that the file did not contain documentation evidencing the transfer of gift funds in **FHA Case No. 491-8985420**. As noted above, the Company understands and appreciates that, to document gift funds in FHA-insured loans, a lender must obtain a gift letter indicating that the funds are provided as a gift with no expectation of repayment, as well as evidence that the funds were actually provided by the donor to the borrower. See HUD Handbook 4155.1 REV-5, ¶ 2-10(C); Mortgagee Letter 00-28. It is Weststar's policy and procedure to obtain and retain such documentation in each transaction in which the borrower utilizes gift funds to close the loan. In this instance, although Weststar is confident that it obtained evidence of the wire transfer of gift funds from the down payment assistance provider and the settlement agent, a copy of that documentation was inadvertently omitted from the Company's loan file in this isolated instance. Nevertheless, any oversight in this case constituted, at worst, harmless error, as the file contained the gift letter (**Exhibit F-2**) and the HUD-1, which properly denotes the gift funds and is signed by the buyer and the seller certifying to its validity (**Exhibit F-3**). As a result, indemnification in this case is unwarranted and we respectfully request that this assertion be removed from the final report.





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**d. Faxed Documentation**

**Comment 9**

In **FHA Case No. 491-8959489**, the Report asserts that certain of the borrower's income documents were transmitted through the builder's fax machine. Weststar understands and appreciates that verifications of employment and deposits must pass directly between the lender and the source. See HUD Handbook 4155.1 REV-5 ¶ 3-1. The documents at issue – W-2 forms, a tax return, and a Social Security benefits letter – are documents that are in a borrower's possession. As you know, borrowers often meet with loan officers outside of a lender's office in order to accommodate a borrower's work schedule, and borrowers often use fax machines made available by real estate agents or builder sales representatives, to which the borrowers would not otherwise have access, in order to deliver documents to the lender. To the best of our knowledge and recollection in this case, the borrower used the builder's sales representative's fax machine for this purpose. Whether the borrowers personally faxed the documents to the Company or handed the documents to an office assistant to fax, the borrowers themselves would have brought those documents to the corporate office for delivery to Weststar. That being said, the Company understands and appreciates that HUD requirements do not allow lenders to accept income documentation faxed through the equipment of an interested third party. See HUD Handbook 4155.1 REV-5 ¶ 3-1. Nevertheless, we believe that any oversight in this case constituted, at worst, harmless error. The W-2 forms, tax return, and Social Security benefits letter included in the loan files were computer-generated, and there is no evidence to suggest that these documents were altered or amended by any party (**Exhibit G-1**). As the loan file supported the income information used to qualify the borrower for FHA financing, we believe that indemnification would be inappropriate in this case.

**e. Verification of Employment**

**Comment 10**

The Report alleges that the VOE in one case, **FHA Case No. 491-9062802**, appeared to have been altered with whiteout and the underwriter did not resolve the discrepancy. With regard to employment documentation, Weststar understands and appreciates that a lender must verify a borrower's employment for the most recent two full years and obtain a verification of employment from the borrower's employer. See HUD Handbook 4155.1 REV-5, ¶ 2-6. It is the Company's policy and practice to comply with these requirements in all FHA loans, and we maintain that the Company did so in this case. Here, the VOE was received directly from the employer, Cassity Jones Lumber, and the total year-to-date income had no evidence of alteration by any party other than perhaps the employer (**Exhibit B-1**). Because the VOE was received directly from the employer and the figures matched the paystub submitted





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(Exhibit B-2), the Company had no reason to question the validity of the documentation. Weststar maintains that it followed all applicable HUD guidelines and indemnification in this case is unwarranted.

**f. Sales Contract Itemization**

In **FHA Case No. 491-9194756**, the Report asserts that the sales contract was not properly itemized to reflect delivery and installation costs. Weststar understands and appreciates that current HUD regulations require the costs of the unit and additional charges for delivery and installation to be itemized on an invoice if the manufactured home dealer is the general contractor for the installation. See Mortgagee Letter 09-16. However, this loan closed on May 23, 2008 and this requirement was not promulgated until 2009, through a Mortgagee Letter dated May 21, 2009. Weststar maintains that it complied with all applicable HUD guidelines in place at the time this loan was originated and requests that this allegation be removed from the final report.

**4. Miscellaneous Issues**

In five loans, the Report identified various miscellaneous issues with, among other items, entries into HUD's TOTAL Scorecard and Neighborhood Watch programs, documentation of the source of funds used to close, documentation of housing obligation history, and asset information. We address each of these issues in turn below.

**a. TOTAL Scorecard Information**

The Report asserts that one loan, **FHA Case No. 491-9062802**, was submitted to TOTAL Scorecard numerous times. As you are aware, in the origination of manufactured home loans, there are many variables that can change prior to underwriting and closing. Some of these factors that are subject to change involve property improvements, property location, floor plan, and construction upgrades. Because variables can change during the loan process, submissions to the automated underwriting system are necessary to determine the borrower's continued eligibility for mortgage financing in light of such changes. Additionally, the number of submissions to the automated underwriting system does not in and of itself evidence any violation of HUD guidelines. As such, indemnification is unwarranted in this case.

The Report also contends that Weststar incorrectly entered two loans, **FHA Case Nos. 492-7865955** and **491-9122005**, into HUD's Neighborhood Watch

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**Comment 13**

system as manually underwritten when in fact the loans had received approval through HUD's TOTAL Scorecard. In these two isolated cases, the Company experienced technical systems issues resulting in the entry of certain inaccurate loan data at the time information was conveyed to HUD through FHA Connection. Since then, Weststar has amended its procedures to ensure accurate reporting in FHA Connection and is confident that this issue will not recur. In addition, the Company contacted HUD about correcting the Neighborhood Watch data for the two referenced cases and made a formal request in writing to update the information (**Exhibit H-1**). We trust that these actions resolve the concerns raised in the Report and we respectfully request that this item be removed from the final report.

**b. Source of Funds**

**Comment 14**

In one loan, **FHA Case No. 492-8020459**, the Report contends that Weststar did not verify the source of the funds used by the borrower to open a checking account prior to closing. The Company understands and appreciates that, in FHA-insured loans, "[a]ll funds for the borrower's investment in the property must be verified and documented." HUD Handbook 4155.1 REV-5, ¶ 2-10. To verify assets held in a borrower's checking or savings account, HUD guidelines require lenders to obtain a verification of deposit ("VOD") or recent bank statements. See *id.* ¶¶ 2-10(B), 3-1. With regard to the deposits, HUD guidelines require that "[i]f there is a large increase in an account, or the account was opened recently, the lender must obtain a credible explanation of the source of those funds." See HUD Handbook 4155.1 REV-5, ¶ 2-10(B). Weststar maintains that it adhered to these requirements in connection with this loan. In this case, the borrower decided to open a checking account with \$2,000 from his retirement savings. The borrower provided the Company with account statements from his ING retirement account showing his balance before the withdrawal (**Exhibit I-1**) and the withdrawal confirmation for \$2,000 (**Exhibit I-2**). Because the borrower did not yet have a checking account, he withdrew \$2,000 from his retirement account and gave the check to his father for safekeeping (**Exhibit I-3**). After he opened a checking account with Wells Fargo, his father returned the money in cash, which the borrower deposited in increments of \$1,500 and \$500 (**Exhibit I-3**).

The Report also alleges that the file contained inconsistent information regarding the borrower's past housing obligations. As you know, HUD guidelines require that the lender determine the borrower's housing obligation payment history and verify a borrower's housing history, See HUD Handbook 4155.1 REV-5, ¶ 3-1, and where file documentation suggests possible inconsistencies, lenders are required to resolve the inconsistency and document the resolution. Weststar did so





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in this case, and the file contains sufficient documentation and explanation of the borrower's previous housing history on the loan application and the borrower's statement regarding his housing. On the loan application, the borrower indicated that he was renting an apartment (**Exhibit I-4**). However, when the Company attempted to verify rent as required by HUD, the borrower submitted a letter of explanation clarifying that he owned a property that he was renting out to others, but he had been living in a trailer on his father-in-law's property rent-free (**Exhibits I-5 and I-6**). As to his current housing situation, the borrower purchased the apartment with another individual in the past, and began renting it out to others when his relationship with that individual ended and he began traveling for work, at which point he took up residence on his father-in-law's property (**Exhibit I-6**). The borrower's letter expressly clarified that he had been living on his father-in-law's property since June 2006, more than 16 months prior to closing, and that he had sold the property that he had referenced on the loan application as being rented in December 2006. The Company maintains that it complied with HUD requirements by requiring the borrower to provide an appropriate explanation for his housing history.

**Comment 15**

Finally, the Report alleges in this case that the borrower paid \$500 in earnest money to the seller before the closing, but that these funds were not disclosed on the HUD-1. Contrary to the assertion in the Report, the \$500 was not an earnest money deposit, but was a fee paid outside of closing to cover the cost of the appraisal. Nevertheless, we appreciate that the fee should have been noted as such, and we have counseled our employees on the importance of accurately disclosing all fees on the HUD-1. We are confident this issue has been resolved and will not recur.

For all of the reasons discussed above, the Company maintains that it substantially complied with HUD guidelines in this case and as such, indemnification would be inappropriate.

**c. Asset Information**

**Comment 16**

In one case, **FHA Case No. 491-8985420**, the Report alleges that Weststar did not include the borrower's banking information in the asset information listed on the loan application. In this case, Weststar maintains that it complied with applicable HUD guidelines by properly documenting the borrowers' assets on the final loan application. On the initial application, dated October 3, 2007 and taken over the telephone, the borrowers estimated their assets to be \$2,750.00 (**Exhibit J-1**). After Weststar requested and received bank statements and other asset information, the final application, dated October 22, 2007, showed an updated amount of \$2,405.08





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in assets and the corresponding bank account numbers (**Exhibit J-2**). In addition, the assets listed on the final application were used on the MCAW and to qualify the borrowers (**Exhibit J-3**). The Company complied with HUD guidelines and properly documented the borrower's banking information on the final application. Indemnification would therefore be inappropriate in this case and we request that this loan be removed from the final report.

**B. WESTSTAR DILIGENTLY ORIGINATED FHA LOANS**

Finally, the Report includes a conclusory allegation that the Company "either misunderstood or ignored FHA guidance." Weststar strongly objects to the inclusion of this allegation in the final report. This assertion made in the "Conclusion" section of the draft Report is unsupported by the other sections of the draft Report. As demonstrated above, the Company properly interpreted and strictly adhered to HUD guidelines in underwriting the loans at issue. For these reasons, these unnecessary allegations are unwarranted and should be removed from the final report.

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

As noted above, the Report merely recommends that the Department pursue indemnification in the cited cases. Upon receiving the final report, the Department will have an opportunity to independently examine the survey findings and make an independent determination of whether indemnification would be appropriate in these six cases. As discussed at length earlier in this response, Weststar disagrees that the Report's assertions warrant indemnification. HUD may also disagree with the Report's assertions and decide not to pursue indemnification in this instance.

In addition, while the survey 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 preliminary recommendations of the OIG before a final assessment as to their merit can be made by the Department. These entities often misinterpret the OIG's recommendations to be final actions by the Department. Under these circumstances, making these preliminary recommendations public and including allegations that HUD pursue indemnification in these loans 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 this review and its implications to the Company, the Report should include the following disclosure on the first page in bold, capitalized lettering:



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

### III. CONCLUSION

Weststar takes the matters raised in the Report seriously. Because FHA lending comprises a significant portion of the Company's overall business operations, Weststar is committed to educating and training its employees on issues regarding FHA compliance and to assuring their adherence to HUD's rules and regulations. We believe that, through this response and supporting documentation, we have demonstrated Weststar's compliance with HUD/FHA requirements and adherence to Handbook standards in connection with the findings in the OIG's Report. The Company appreciates this opportunity to respond to the matters raised in the Report. While we recognize that there is always room for improvement, we hope you will agree that the Company has satisfactorily resolved the issues identified in the draft Report.

We trust that this correspondence adequately addresses HUD's concerns, and we hope that you will consider this response and supporting documentation when reviewing the pending matter. Should you have any questions or need additional information, please call our Washington counsel, Phillip L. Schulman, at (202) 778-9027 or Krista Cooley, at (202) 778-9257.

Thank you for your kind consideration.

Sincerely,

A handwritten signature in black ink that reads "Kent Wiechert".

Kent Wiechert  
President





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Attachments

cc: Phil Schulman  
Krista Cooley



## OIG Evaluation of Auditee Comments

- Comment 1** Weststar disagreed with the findings and recommendations. We stand by the conclusions reached based on analysis of the loan files and HUD FHA requirements.
- Comment 2** Weststar was concerned that the report would lead readers to believe that the ineligible loans were recently originated. We reviewed the report and determined that the loan origination and default time periods were clearly stated. We did not change the report based on the comment.
- Comment 3** Weststar disagreed that it did not properly assess or document the borrowers' income for three loans. Weststar provided 13 exhibits in support of its position. We reviewed the documents and determined that we had considered them during the audit and that they did not refute the finding.
- Comment 4** Weststar contended that it complied with FHA guidelines when it analyzed and approved borrower credit in four loans questioned in the audit report. Weststar further contended that the loan files contained the required documentation and that it prudently exercised the discretion granted it by FHA. Weststar provided six exhibits in support of its position. We reviewed the documents and determined that they did not refute the finding. We did not change the report based on this comment.

Weststar stated that it complied with desktop underwriting requirements for three of the four questioned loans when it obtained the documentation indicated in the verification messages provided in the Underwriter Findings Reports. However, Weststar should not have processed the three loans using desktop underwriting. The loans were not qualified for desktop underwriting because they included a tax lien or consumer disputed items on credit reports that Weststar did not properly address.

- Comment 5** Weststar stated that it endeavored to construct a case binder for submission to HUD that reflected the correct final loan documentation that HUD required, as well as retain a complete copy of the case binder documents that it submitted to HUD. Weststar admitted that in some instances, a non-final document was unintentionally included in the HUD case binder or a copy of the final document included in the case binder was not retained in Weststar's loan file. However, Weststar asserted that it was confident that it had improved its compilation and submission process and had resolved any concerns identified in the loan files reviewed in the audit and that any issues related to compiling case binders would not recur.

The OIG found many differences between the documents in Weststar's case files and the documents that Weststar submitted to HUD. In some cases, the differences may have been material. Further, all the case binders that Weststar

submitted to HUD were incomplete because they did not contain the final loan documentation. We did not review any loans that Weststar originated after 2008 to confirm whether its revised procedures resulted in complete files, and we did not change the report based on this comment.

**Comment 6** Weststar agreed that in two cases employees were out of the office and the employees allowed other employees to sign documents on their behalf. Weststar denied that it allowed employees to sign for other employees when they were "in a hurry," and denied that the issue was a control weakness. As the report states, in 6 of the 10 files reviewed, employees signed documents for other employees. Further, when questioned about the practice, one employee admitted that Weststar was aware of it. Therefore, we do not believe that these were isolated instances or that Weststar did not at least implicitly allow employees to sign for other employees.

Further, Weststar stated that it had implemented procedures to prohibit employees from signing documents on behalf of other employees under any circumstance and require each individual employee to only sign his or her own name. We did not test any loans after the implementation; thus, we did not evaluate the implementation or the effectiveness of the procedures, and we did not change the report based on the comment.

**Comment 7** Weststar stated that it retained the required gift documentation for FHA Case Number 492-7767217 and provided a copy of the gift letter in its response. We reviewed the gift letter and determined that we had not seen it during the audit. It was not in the HUD file, and according to a Weststar representative during the audit, it was not in the lender's file. Further, there was a \$978 discrepancy between the gift fund amount on the HUD-1 settlement statement and the Mortgage Credit Analysis Worksheet. Therefore, we are uncertain of the authenticity of the gift letter and did not change the report based on the comment and the submitted document.

**Comment 8** Weststar admitted that it may have inadvertently omitted some of the gift letter documentation for FHA Case Number 491-8985420 but believed the oversight was a harmless error. We did not change the report based on the comment.

**Comment 9** Weststar admitted that the income documents may have been transmitted through the builder's fax machine but said that it was common for borrowers to use a builder's fax machine and believed that this was, at worst, a harmless error. We did not change the report based on the comment.

**Comment 10** Weststar did not dispute that a verification of the employment had been altered with whiteout but said it had no reason to question the validity of the document because it said it received the verification of the employment directly from the employer. We disagree because the underwriter should have required an

explanation and documented the results. We did not change the report based on the comment.

- Comment 11** Weststar asserted that a HUD requirement to itemize the sales contract to reflect delivery and installation costs was not effective until after Weststar originated the loan. We agreed and made appropriate changes to the report.
- Comment 12** Weststar asserted that there can be numerous submissions to TOTAL Scorecard because there are many variables that can change prior to underwriting and closing, such as property improvements, property location, floor plan, and construction upgrades. Weststar further asserted that the number of submissions to the automated underwriting system does not in and of itself evidence any violation of HUD guidelines. We noted that there was no explanation for the number of submissions in the file, and no reason to believe that property improvements, location, floor plan, and construction upgrades should have changed 37 times. The number of submissions was excessive and unexplained. We did not change the report based on the comment.
- Comment 13** Weststar admitted that it submitted inaccurate information to Neighborhood Watch for two cases. Weststar said that it has contacted HUD to correct the data and amended its procedures to ensure accurate reporting in FHA Connection and was confident that the issue will not recur. We did not review the corrected data or the amended procedures and do not have an opinion on whether the new procedures are effective. We did not change the report based on the comment.
- Comment 14** Weststar maintained that it adhered to HUD requirements to verify the borrower's source of funds to open a checking account for FHA Case Number 492-8020459. Weststar further maintained that it complied with HUD requirements to obtain a explanation for a discrepancy in the borrower's housing. Weststar provided six exhibits that it said proved its point. We reviewed the documents and determined that we had considered them during the audit and that they did not refute the finding.
- Comment 15** Weststar asserted that the borrower in FHA Case Number 492-8020459 paid \$500 outside closing to cover the cost of the appraisal but that the payment was erroneously recorded as earnest money. Weststar did not provide any evidence to support this assertion, and we did not change the report based on the comment.
- Comment 16** Weststar contended that it complied with HUD guidelines and properly documented the borrower's banking information and provided three exhibits that it said proved its point. We reviewed the documents and determined that we had considered them during the audit and that they did not refute the finding.
- Comment 17** Weststar objected to our conclusion that it either ignored or misunderstood the regulations and stated the conclusion was not supported by information in the other sections of the report. We stand by our conclusion based on the facts

presented in the report that show that 6 of the 10 loans reviewed were ineligible for FHA insurance due to various violations. We did not change our conclusion.

**Comment 18** Weststar stated that the allegations in the report were recommendations to HUD instead of a final action. Weststar suggested the OIG include a disclosure statement in the report indicating that the recommendations were not a final action. As part of the audit resolution process, we will work with HUD to reach agreement on the actions that it will take to resolve the recommendations, which may or may not include indemnification of loans. However, based on our assessment of the loans, the recommendations are appropriate; thus, we did not change them. Further, the suggested disclosure will not be included in the report because it is unnecessary.

## Appendix C

### CASE NARRATIVES

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#### Case Narrative – Loan Number 491-9062802

Mortgage amount: \$110,695

Date of loan closing: December 4, 2007

Status as of September 30, 2011: Claims paid<sup>9</sup> totaling \$119,670

Payments before first default: Four

HUD loss: \$72,887

Underwriting deficiencies:

- The lender did not process the loan correctly
- Borrower income was calculated incorrectly
- The verification of employment had evidence of alteration
- There was no explanation of derogatory credit items
- TOTAL Scorecard red flagged the number of loan submissions
- The HUD case binder was not identical to the lender file

**Summary:**

**The Lender Did Not Process the Loan Correctly**

The borrower had delinquent property taxes that did not appear on the credit report. FHA requires<sup>10</sup> the lender to downgrade the loan to a refer and manually underwrite it if derogatory or delinquent credit items are revealed during processing that are not reflected on the credit report. Weststar did not manually underwrite this loan as required by the TOTAL Scorecard manual. Weststar included payment of the delinquent property taxes in the borrower's closing costs; thus, Weststar was aware of the delinquency.

**Borrower Income Was Calculated Incorrectly**

Weststar erroneously included overtime from the current employer in the borrower's income calculation. According to HUD Handbook 4155.1, REV-5, paragraph 1.B.2.f, TOTAL Scorecard approval requires the lender use base pay only (no overtime or bonus pay) to qualify the borrower. Weststar calculated income based on 10 months of overtime. If Weststar had manually underwritten this loan as it should have, it would have had to document and explain compensating factors associated with exceeding HUD's underwriting ratios. Without the overtime included, the front end ratio was 43 percent and the back end ratio was 61 percent, both

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<sup>9</sup> The lender presents a claim to HUD for payment after the foreclosure sale.

<sup>10</sup> FHA's TOTAL Mortgage Scorecard User Guide, page 17

of which exceeded HUD's manual underwriting ratio standards of 31 and 43 percent,<sup>11</sup> respectively.

### **The Verification of Employment Had Evidence of Alteration**

The underwriter did not include evidence that he had resolved a questionable document. The verification of employment form had been altered with whiteout on the gross earnings and overtime and replaced with information that matched the paycheck stub submitted. According to Weststar, the underwriter had no reason to question the information reflected on the document as it was received directly from the employer.

### **There Was No Explanation of Derogatory Credit Items**

The borrower did not explain or provide documentation on 14 collection accounts found on the credit report. FHA regulations<sup>12</sup> state that the borrower must explain, in writing, all collections and judgments.

### **TOTAL Scorecard Red Flagged the Number of Loan Submissions**

The TOTAL Scorecard report noted a potential red flag as there was an unusually high number of loan submissions through the automated underwriting system. The loan was submitted through TOTAL Scorecard a total of 37 times with no documented explanation for the number of submissions. Weststar stated that often a TOTAL Scorecard report is run to determine eligibility based upon various financial scenarios that are of interest to the borrower, such as paying off credit cards or consolidating debt.

### **The HUD Case Binder Was Not Identical to the Lender File**

Weststar submitted to HUD several documents that differed from those in its own file. The documents included an automated underwriting report, mortgage credit analysis worksheet, and good faith estimate. Some of the documents contained significant differences in the amounts reported. FHA regulations<sup>13</sup> state that lenders must prepare and submit a uniform case binder to HUD. According to Weststar, it was possible that in some instances, a non-final document was unintentionally included in the HUD case binder.

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<sup>11</sup> HUD Handbook 4155.1, REV-5, paragraph 4.F.2.a

<sup>12</sup> HUD Handbook 4155.1, REV-5, paragraph 4.C.2.d

<sup>13</sup> HUD Handbook 4155.2, paragraph 8.B.1.d

## Case Narrative – Loan Number 492-8020459

Mortgage amount: \$102,464

Date of loan closing: August 14, 2008

Status as of September 30, 2011: Claims paid totaling \$109,452

Payments before first default: One

HUD loss: \$80,472

### Underwriting deficiencies:

- Earnest money was not on the settlement statement
- There was no explanation of derogatory credit items
- The lender did not document the source of funds
- Income documentation was not consistent
- The housing obligation requirement was not met
- The HUD case binder was not identical to the lender file

### Summary:

#### **Earnest Money Was Not on the Settlement Statement**

The loan file contained evidence that the borrower paid \$500 in earnest cash to the seller before the loan closing. The document was signed by the borrower and seller, but the settlement statement did not show the earnest money payment. The Real Estate Settlement Procedures Act<sup>14</sup> requires any money paid against the sales price before settlement to be included on the settlement statement. According to Weststar, the earnest money was paid by the borrower to the seller and was not considered as part of the loan transaction.

#### **There Was No Explanation of Derogatory Credit Items**

The borrower did not explain or provide documentation for collection accounts found on the credit report. FHA requires<sup>15</sup> that the borrower explain, in writing, all collections and judgments. Weststar obtained a credit explanation letter from the borrower for a previous mortgage but did not obtain an explanation for the collection accounts found on the credit report. One collection amount increased during the collection process.

#### **The Lender Did Not Document the Source of Funds**

Weststar did not obtain documentation to support where the borrower's payroll checks were direct deposited before the borrower opened a checking account. On the advice of Weststar, the borrower opened an account with funds noted as retirement money, but there was no documentation to support where the funds came from. FHA regulations<sup>16</sup> allow a verification of deposit, along with the borrower's most recent bank statement, to be used to verify savings and checking accounts, but if there is a large increase in an account or the account was recently

<sup>14</sup> 24 CFR Part 3500, appendix A, instructions for line 201

<sup>15</sup> HUD Handbook 4155.1, REV-5, paragraph 4.C.2.d

<sup>16</sup> HUD Handbook 4155.1, REV-5, paragraph 5.B.2.b

opened, the lender must obtain from the borrower a credible explanation and documentation of the source of funds.

### **Income Documentation Was Inconsistent**

The borrower submitted two paycheck stubs, one of which did not contain employer information or a check number. FHA requirements<sup>17</sup> state that income, employment, or asset documents sent to the lender by fax must clearly identify the name of the employer and the source of information. According to Weststar, one paycheck stub was copied and one was faxed, which may have accounted for the missing information; however, we found copies of both paycheck stubs, and the employer information was still missing on one.

### **The Housing Obligation Requirement Was Not Met**

According to the borrower, he had lived for the past 4 years in a manufactured home, the last 2 of which was on his father-in-law's property. According to his loan application, he had been renting an apartment for the past 3 years. FHA requirements<sup>18</sup> state that the lender must determine the borrower's housing obligation payment history through verification of rent received directly from the landlord or a review of canceled checks that cover the most recent 12-month period. The lender must verify and document the housing history even if the borrower states that he or she was living rent free. Weststar did not document or resolve the inconsistency between the loan application and the borrower statement regarding housing obligation.

### **The HUD Case Binder Was Not Identical to the Lender File**

Weststar submitted to HUD several documents that differed from those in its own file. The documents included a mortgage credit analysis worksheet, good faith estimate, and gift letter. The HUD case binder also contained verification documents, such as the limited denial of participation, excluded parties list system, and Credit Alert Interactive Voices Response System report, that were not in the lender file. FHA regulations<sup>19</sup> state that lenders must prepare and submit a uniform case binder to the appropriate Homeownership Center. According to Weststar, it was possible that in some instances, a non-final document was unintentionally included in the HUD case binder.

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<sup>17</sup> HUD Handbook 4155.1, REV-5, paragraph 1.B.1.i

<sup>18</sup> HUD Handbook 4155.1, REV-5, paragraph 4.C.2.b

<sup>19</sup> HUD Handbook 4155.2, paragraph 8.B.1.d

## Case Narrative – Loan Number 491-9194756

Mortgage amount: \$145,626

Date of loan closing: May 23, 2008

Status as of September 30, 2011: Claims paid totaling \$150,067

Payments before first default: Three

HUD loss: \$145,626

### Underwriting deficiencies:

- Borrower income was calculated incorrectly
- The loan application was not completed correctly
- The HUD case binder was not identical to the lender file

### Summary:

#### **Borrower Income Was Calculated Incorrectly**

Weststar erroneously included overtime from the current employer in the income calculation. According to HUD Handbook 4155.1, REV-5, paragraph 1.B.2.f, TOTAL Scorecard approval requires that the lender use base pay only (no overtime or bonus pay) to qualify the borrower. Weststar used overtime the borrower received in 2008 in its calculation. If Weststar had manually underwritten this loan, it would have had to document and explain compensating factors associated with exceeding HUD's underwriting ratios. For this loan without the overtime included, the back end ratio totaled 60 percent, which exceeded HUD's manual underwriting ratio standard of 43 percent.<sup>20</sup>

#### **The Loan Application Was Not Completed Correctly**

The borrower listed source of downpayment on the loan application as equity in land; however, the sales contract showed the borrower purchasing the land from the manufactured home dealer. FHA regulations<sup>21</sup> state that the underwriter's responsibility includes certifying that the uniform residential loan application and addendum were personally reviewed and all application documents are in compliance. According to Weststar, the downpayment did not come from equity in the real property but was obtained through downpayment assistance. The loan application contained a certification signed by the underwriter, stating that to the best of the lender's knowledge, the statements in the application were true and correct.

#### **The HUD Case Binder Was Not Identical to the Lender File**

Weststar submitted to HUD two documents that differed from those in its own file. The documents included a different mortgage credit analysis worksheet and good faith estimate. Some of the documents contained significant differences in the amounts reported. In addition, the HUD case binder did not contain the gift letter documentation showing that downpayment

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<sup>20</sup> HUD Handbook 4155.1, REV-5, paragraph 4.F.2.a

<sup>21</sup> HUD Handbook 4155.2, paragraph 2.A.4.b

assistance was received. FHA regulations<sup>22</sup> state that lenders must prepare and submit a uniform case binder to the appropriate Homeownership Center. According to Weststar, it was possible that in some instances, a non-final document was unintentionally included in the HUD case binder.

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<sup>22</sup> HUD Handbook 4155.2, paragraph 8.B.1.d

## Case Narrative – Loan Number 491-8985420

Mortgage amount: \$121,677

Date of loan closing: October 22, 2007

Status as of September 30, 2011: Claims paid totaling \$130,101

Payments before first default: Four

HUD loss: \$103,752

### Underwriting deficiencies:

- The borrower's credit report contained disputed items
- There was no explanation of derogatory credit items
- The gift funds transfer was not documented by the lender
- Borrower financial information was not used
- The lender submitted an invalid loan application to HUD
- The HUD case binder was not identical to the lender file

### Summary:

#### **The Borrower's Credit Report Contained Disputed Items**

The borrower's revised credit report, dated October 19, 2007, contained five disputed items. FHA requirements, dated December 2004,<sup>23</sup> state that any credit report containing disputed items must be manually underwritten. According to Weststar, the loan was not referred for manual underwriting because the FHA requirements were not implemented until "this past year" (calendar year 2011) and the loan was underwritten in 2007. This statement showed that Weststar did not know the HUD FHA and TOTAL Scorecard regulations, and Weststar did not manually underwrite this loan as required by the TOTAL Scorecard manual.

#### **There Was No Explanation of Derogatory Credit Items**

The borrower did not explain or provide documentation for 12 derogatory items found on the credit report. FHA regulations<sup>24</sup> state that major indications of derogatory credit, such as judgments, collections, and other recent credit problems, require written explanation from the borrower. In addition, significant compensating factors are required if the borrower had recent financial difficulty and had not maintained a good payment record. This loan was processed through TOTAL Scorecard. If Weststar had manually underwritten this loan, it would have had to document borrower explanations and significant compensating factors.

#### **The Gift Funds Transfer Was Not Documented by the Lender**

The Weststar file did not contain the gift funds wire transfer documentation. FHA requirements<sup>25</sup> state that the lender must document the transfer of gift funds from the donor to

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<sup>23</sup> FHA's TOTAL Mortgage Scorecard User Guide, page 21

<sup>24</sup> HUD Handbook 4155.1, REV-5, paragraph 4.C.1.c

<sup>25</sup> HUD Handbook 4155.1, REV-5, paragraph 5.B.5.b

the borrower and the documentation is to be kept in the mortgage loan binder. Weststar did not document the transfer of the gift funds as required by FHA.

### **Borrower Financial Information Was Not Used**

Weststar did not use the borrower's banking information when qualifying the loan. FHA regulations<sup>26</sup> state that the lender must obtain and verify the borrower's information to get a complete picture of the borrower's financial position and source of funds for the mortgage transaction. The borrower's banking information was not included in the asset information listed on the loan application. The loan application contained a certification signed by the underwriter, stating that to the best of the lender's knowledge, the statements in the application were true and correct.

### **The Lender Submitted an Invalid Loan Application to HUD**

The final loan application submitted in HUD's case file contained a signature page that appeared to have been copied, and the details of transaction amounts appeared to have been changed. FHA requirements<sup>27</sup> state that the underwriter's responsibility includes certifying that the loan application and addendum are reviewed and all application documents are in compliance. According to Weststar, the signature page attached to the final application in its file reflected the correct and accurate information, and it was unable to determine why a second signature page was in the file. The loan application was certified by the underwriter as a representative of the lender that the data supplied were true and correct.

### **The HUD Case Binder Was Not Identical to the Lender File**

Weststar submitted to HUD several documents that differed from those in its own file. The documents included a good faith estimate, sales contract, and loan application. The sales contract submitted to HUD did not contain any signatures and was missing information related to seller-required repairs after closing. FHA regulations<sup>28</sup> state that lenders must prepare and submit a uniform case binder to the appropriate Homeownership Center. According to Weststar, it was possible that in some instances, a non-final document was unintentionally included in the HUD case binder.

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<sup>26</sup> HUD Handbook 4155.1, REV-5, paragraph 1.A.4.c

<sup>27</sup> HUD Handbook 4155.2, paragraph 2.A.4.b

<sup>28</sup> HUD Handbook 4155.2, paragraph 8.B.1.d

## Case Narrative – Loan Number 491-8959489

Mortgage amount: \$64,877

Date of loan closing: May 2, 2007

Status as of September 30, 2011: Claims paid totaling \$75,532

Payments before first default: One

HUD loss: \$61,272

### Underwriting deficiencies:

- Documents were handled by a third party.
- An unqualified person certified documents
- The HUD case binder was not identical to the lender file

### Summary:

#### **Documents Were Handled by a Third Party**

Weststar accepted and used documents relating to employment and income of the borrowers that were handled and transmitted through fax by interested third parties, such as the builder. FHA regulations state that lenders may not accept or use documents relating to the credit, employment, or income of borrowers that have been handled by or transmitted from or through the equipment of interested third parties, such as real estate agents, builders, or sellers.<sup>29</sup>

#### **An Unqualified Person Certified Documents**

The file contained obvious differences in signature styles on the initial and final uniform residential loan applications with no explanatory statements. FHA requirements state that the underwriter's signature on this form certifies that he or she has personally reviewed all application documents and finds compliance with the applicable documents and must be attuned to the warning signs that may indicate any irregularities.<sup>30</sup>

Weststar acknowledged the signature differences and said that it consented and instructed an employee of Weststar to sign certified documents when the underwriter and the loan officer were out of the office.

#### **The Borrower's Final Application Was Missing**

Both HUD's and lender's case binders were missing the borrower's final application. FHA requires the lender to provide a complete picture of the borrower's financial position and source of funds for the mortgage transaction.

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<sup>29</sup> HUD Handbook 4155.1, REV-5, paragraph 1.B.1.f

<sup>30</sup> HUD Handbook 4155.2, paragraph 2.A.4.b

## Case Narrative – Loan Number 492-7767217

Mortgage amount: \$119,892

Date of loan closing: March 30, 2007

Status as of September 30, 2011: Claims paid totaling \$127,159

Payments before first default: 12

HUD loss: \$90,121

### Underwriting deficiencies:

- An unqualified person certified documents
- The HUD case binder was not identical to the lender file
- A gift letter was missing

### Summary:

#### **An Unqualified Person Certified Documents**

The file contained obvious differences in signature styles on the initial and final uniform residential loan application with no explanatory statements. FHA requirements state that the underwriter's signature on this form certifies that he or she has personally reviewed all application documents and finds compliance with the applicable documents and must be attuned to the warning signs that may indicate any irregularities.<sup>31</sup>

Weststar acknowledged the signature differences and said that it consented and instructed an employee of Weststar to sign certified documents when the underwriter and the loan officer were out of the office.

#### **The HUD Case Binder Was Not Identical to the Lender File**

Weststar submitted to HUD two documents that differed from those in its own file. The documents included a mortgage credit analysis worksheet and good faith estimate. FHA regulations state that lenders must prepare and submit a uniform case binder to the appropriate Homeownership Center.<sup>32</sup> According to Weststar, it was possible that in some instances, a non-final document was unintentionally included in the HUD case binder.

#### **A Gift Letter Was Missing**

The Weststar file did not contain gift letter documentation. FHA requires the lender to document any gift funds through a gift letter, and the documentation is to be kept in the mortgage loan binder.<sup>33</sup>

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<sup>31</sup> HUD Handbook 4155.2, paragraph 2.A.4.b

<sup>32</sup> HUD Handbook 4155.2, paragraph 8.B.1.d

<sup>33</sup> HUD Handbook 4155.1, REV-5, paragraph 5.B.5.a