Issue Date May 12, 2008
Audit Report Number 2008-NY-1005

TO: Brian D. Montgomery, Assistant Secretary for Housing – Federal Housing Commissioner, H

Edgar Moore

FROM: Edgar Moore, Regional Inspector General for Audit, 2AGA

SUBJECT: Mortgage Access Corporation, Morris Plains, New Jersey, Did Not Always Comply with HUD/FHA Loan Origination Requirements

HIGHLIGHTS

What We Audited and Why

We audited Mortgage Access Corporation, doing business as Weichert Financial Services, a nonsupervised lender located in Morris Plains, New Jersey. Mortgage Access Corporation was selected for review because its default rate of 10.74 percent for loans with beginning amortization dates between May 1, 2005, and April 30, 2007, was higher than the state of New Jersey's default rate of 5.49 percent.

The audit objectives were to determine whether Mortgage Access Corporation (1) approved insured loans in accordance with U.S. Department of Housing and Urban Development (HUD)/Federal Housing Administration (FHA) requirements, which include following prudent lending practices, and (2) developed and implemented a quality control plan that complied with HUD/FHA requirements.

What We Found

Mortgage Access Corporation did not always comply with HUD regulations in underwriting FHA-insured loans. Seven loans exhibited significant underwriting deficiencies such as inadequate credit analysis, inadequate verification of funds to close, minimum cash investment not met, and inadequate verification of income/employment. As a result, loans were approved for potentially ineligible borrowers, which caused HUD/FHA to incur an unnecessary insurance risk. In addition, one of these seven loans was approved for a property that was not eligible for FHA insurance. These deficiencies occurred because Mortgage Access Corporation lacked adequate controls to ensure that loans were processed in accordance with HUD requirements.

Mortgage Access Corporation failed to ensure that its quality control plan was implemented in accordance with HUD's requirements. Specifically for early defaulted loans, Mortgage Access Corporation did not ensure that (1) quality control reviews were conducted for all loans that defaulted within six months of closing, (2) reviews of early defaulted loans were performed in a timely manner, (3) adequate reverifications of loan documents were performed, and (4) management addressed the material deficiencies identified in quality control findings. Consequently, the effectiveness of its quality control plan, which was designed to ensure accuracy, validity, and completeness in its loan underwriting process, was lessened.

What We Recommend

We recommend that the Assistant Secretary for Housing – Federal Housing Commissioner require Mortgage Access Corporation to (1) reimburse HUD for one ineligible loan, (2) indemnify HUD against future losses on the remaining six loans with significant underwriting deficiencies, (3) establish procedures to ensure that HUD underwriting requirements are properly implemented and documented, and (4) implement procedures to ensure compliance with HUD's and its own quality control requirements. We also recommend that HUD's Homeownership Center's Quality Assurance Division follow up with Mortgage Access Corporation within one year to ensure that quality control reviews have been properly implemented.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided a draft report to Mortgage Access Corporation officials on March 26, 2008 and requested their responses by April 11, 2008. We discussed the results of our review during the audit and at an exit conference on April 11, 2008. Mortgage Access Corporation officials provided written comments at the exit conference, and generally agreed with the draft report findings. The complete text of Mortgage Access Corporation's response, along with our evaluation of that response, can be found in appendix B of this report. The auditee's response also contained attachments, which are available upon request.

TABLE OF CONTENTS

BACKGROUND AND OBJECTIVES

Mortgage Access Corporation became an approved U.S. Department of Housing and Urban Development (HUD) non-supervised lender in 1983. The company originates loans, which it then sells to investors, banks, and other mortgage bankers.

The main office of Mortgage Access Corporation is located in Morris Plains, New Jersey, and it has branches in Shrewsbury, New Jersey; Bethesda, Maryland; Norwell, Massachusetts; Spring Hill, Florida; and Johnson City, Tennessee.

Between May 1, 2005, and April 30, 2007, Mortgage Access Corporation underwrote 698 Federal Housing Administration (FHA)-insured mortgages in New Jersey and experienced a default rate of 10.74 percent, which was significantly higher than the New Jersey state average default rate of 5.49 percent.

On March 13, 2007, HUD notified Mortgage Access Corporation of its intent to terminate the lender's origination approval agreement based upon its default and claim rate of 9.44 percent during the 24-month period ending December 31, 2006. The Morris Plains branch's default and claim rate of 9.44 percent for all loans in the Camden, New Jersey, HUD office jurisdiction exceeded the HUD Camden office's default and claim rate of 2.96 percent and the national rate of 3.30 percent On June 15, 2007, HUD notified Mortgage Access Corporation that the explanation provided in its written responses and during the informal conference held with HUD officials did not mitigate the proposed termination action, and, therefore, HUD terminated Mortgage Access Corporation's authority to originate HUD/FHA-insured single-family mortgage loans in HUD's Camden jurisdiction.

The objectives of this audit were to determine whether Mortgage Access Corporation (1) approved insured loans in accordance with HUD/FHA requirements, which include following prudent lending practices, and (2) developed and implemented a quality control plan that complied with HUD/FHA requirements.

RESULTS OF AUDIT

Finding 1: Mortgage Access Corporation Did Not Always Comply with HUD's Underwriting Requirements

Mortgage Access Corporation did not follow prudent lending practices and HUD regulations in the origination and underwriting of the seven loans we reviewed. As a result, loans were approved for potentially ineligible borrowers, and these deficiencies contributed to an unnecessary insurance risk to HUD/FHA. The seven loans contained significant underwriting deficiencies such as inadequate credit analysis, inadequate verification of funds to close, minimum cash investment not met, and inadequate verification of income/employment. In addition to significant underwriting deficiencies, one loan was approved for a property that was not eligible for FHA insurance. These deficiencies occurred because Mortgage Access Corporation did not have adequate controls to ensure that loans were processed in accordance with HUD/FHA requirements.

Significant Underwriting Deficiencies

Our review of seven loans with amortization dates between May 1, 2005, and April 30, 2007, disclosed significant underwriting deficiencies in all seven loans, and one of the loans was approved for a property that was not eligible for FHA insurance. These deficiencies occurred because Mortgage Access Corporation did not follow prudent lending practices and regulations prescribed by HUD in its origination and underwriting of the seven loans.

HUD Handbook 4155.1, REV-5, entitled "Mortgage Credit Analysis for Mortgage Insurance," prescribes basic underwriting requirements for FHA-insured single-family mortgage loans. The lender must ensure that the borrower has the ability and willingness to repay the mortgage debt. This assessment must be based on sound underwriting principles in accordance with the guidelines, rules, and regulations described in this handbook and be supported by sufficient documentation. In addition, chapter 3-1 of the handbook requires that the application package contain sufficient documentation to support a lender's decision to approve a mortgage. While this decision involves some subjectivity, our examination of seven loans approved by Mortgage Access Corporation disclosed significant underwriting deficiencies in the approval of these seven loans. Mortgage Access Corporation did not always (1) sufficiently analyze borrowers' credit, (2) adequately verify the source of funds to close, (3) ensure that the minimum cash investment requirement was met, and (4) properly verify the borrowers' employment and/or income. In addition to significant underwriting deficiencies, one loan was approved for an individual unit in a non-

FHA-approved condominium. If the unit is located in a non-FHA-approved condominium project, it can qualify for spot-loan financing. However, the condominium project did not meet the 51 percent owner occupancy requirements for the unit to qualify for spot-loan financing.

Significant deficiencies are noted in the chart below and in appendix C. The deficiencies noted are not independent of one another, as one loan may have contained more than one deficiency.

Areas of deficiencies	***Number of loans***
Inadequate credit analysis	6 of 7 loans
Inadequate verification of funds to close	7 loans
Minimum cash investment not met	7 loans
Inadequate verification of employment and/or income	4 of 7 loans

Specific examples of these significant underwriting deficiencies follow:

- For FHA case #351-4737353, the lender did not conduct an adequate analysis of the borrower's credit history. The borrower's credit report reflected various major derogatory accounts including judgments and collection actions and late payment instances on a prior FHA mortgage loan and other accounts. However, the lender did not obtain a written explanation from the borrower about major derogatory accounts and failed to analyze the borrower's payment history of housing obligations and document its analysis as to whether the late payments were based on a disregard for financial obligations, an inability to manage debt, or factors beyond borrower's control. The lender also did not verify the borrower's funds for the investment in the property. The mortgage credit analysis worksheet indicated that the borrower's only source of funds was proceeds from a pending real estate sale; however, the lender did not document the actual sale. In addition, the borrower's employment income was overstated, which resulted in the lender's calculating incorrect debt-to-income ratios of 38.78 and 48.16 percent. After adjusting the borrower's income, these ratios would increase to 41.85 and 51.97 percent. Further, the lender did not describe compensating factors to justify the mortgage approval.

- For FHA case #352-5447285, the lender did not obtain a credible explanation for the borrower's source of funds to close. The HUD-1 settlement statement showed an earnest money deposit of $25,000, which exceeded 2 percent of the $312,000 sale price. However, the file did not contain certification from the deposit holder acknowledging the receipt of the funds or a copy of the cancelled check. It appeared that the source of the earnest money was the borrower's funds in an investment account, but the lender did not verify the actual receipt of funds as required by HUD regulations. HUD Handbook 4155.1, REV-5, section 2-10 A, states that if the amount of the earnest money deposit exceeds 2 percent of the sales price or appears excessive based on the borrower's history of accumulating savings, the lender must verify with documentation the deposit amount and the source of funds. Section 2-10 L of the handbook also states that the actual receipt of funds must be verified and documented. The file contained a statement from the financial institution covering the period August 1 through September 30, 2005. In addition, the debt-to-income ratios were calculated incorrectly because liabilities were understated and employment income was overstated. After adjusting the borrower's income and liabilities, the ratios would increase to 54.17 and 65.11 percent.

- For FHA case #352-5499451, the lender approved a loan for an individual unit in a non-FHA-approved condominium. If a condominium is not FHA approved, it is possible that the individual unit may qualify for spot-loan financing if the building meets the 51 percent owner occupancy requirement. Based on detailed information obtained from HUD's Web site on condominiums, the building did not meet the 51 percent owner occupancy requirement. Also, there was a discrepancy between the number of units reported on the appraiser's report and by the condominium's management company. The lender did not ensure the accuracy of the information it relied upon and failed to perform a sufficient investigation and analysis to certify that the condominium project satisfied the eligibility criteria. In addition, the lender failed to conduct an adequate analysis of the borrower's credit history. The borrower's credit report reflected collection accounts and late payment instances within two years of the FHA loan closing; however, the lender did not obtain an explanations from the borrower. The lender did not obtain (1) original pay stubs showing the year-to-date earnings of at least one month, (2) adequate bank documents, and (3) gift fund transfer documents.

Conclusions

Mortgage Access Corporation did not always follow HUD regulations in the approval of loans. As a result, HUD remains at risk for more than $1.3 million, the value of the seven loans we reviewed, which had significant underwriting deficiencies.[1] The final loss that HUD incurs will depend upon what HUD realizes when it disposes of the property. HUD's most recent data disclosed that its loss rate is 39 percent. Net sales proceeds after considering carrying and sales expenses may mitigate the amount of the claim paid. Loans for which HUD remains at risk can be mitigated by requesting that the lender indemnify HUD. In this case, the lender reimburses HUD for any insurance claim, taxes, interest, and other expenses connected with the disposition of the property, reduced by any amount recouped by HUD via sale or other disposition.

[1] A reimbursement of $93,500 is recommended for the loan that was approved for a property not eligible for FHA insurance. The amount of cost savings or funds to be put to better use on the loans for which indemnification is recommended is estimated at $480,897 based on HUD's 39 percent default loss experience for the remaining six loans ($1,326,569 - $93,500 x 39 percent).

Appendix C of this report provides a summary of the underwriting deficiencies noted in the seven cases. Appendix D of this report provides a more detailed description of the deficiencies by case number.

Recommendations

We recommend that the Assistant Secretary for Housing – Federal Housing Commissioner require Mortgage Access Corporation to

1A. Reimburse HUD for the $93,500 loan that was approved for a property that was not eligible for FHA insurance.

1B. Indemnify HUD against future losses estimated to be $480,897 on six loans with significant underwriting deficiencies.

1C. Establish procedures to ensure that all HUD underwriting requirements are properly implemented and documented.

Finding 2: Mortgage Access Corporation Had Weaknesses in the Implementation of Its Quality Control Plan

Mortgage Access Corporation had weaknesses in the implementation of its quality control plan. It did not always comply with both HUD's and its own quality control requirements to ensure that (1) all HUD-insured loans that defaulted within the first six payments were reviewed, (2) reviews for early defaulted loans were conducted in a timely manner, (3) adequate reverification of loan documents was performed, and (4) management addressed the material deficiencies identified in quality control findings. These noncompliances occurred because Mortgage Access Corporation did not establish procedures to ensure that its quality control plan was properly implemented. Consequently, the effectiveness of Mortgage Access Corporation's quality control plan, which was designed to ensure accuracy, validity, and completeness in its loan underwriting process, was lessened.

Loans Defaulting within the First Six Payments Were Not Reviewed

Loans that defaulted within the first six payments (early payment defaults) were not reviewed as required by HUD regulations and by the lender's own quality control plan. HUD Handbook 4060.1, REV-2, section 7-6 D, requires the lender to review all loans going into default within the first six payments. Quality control reviews were not performed on 17 of the 41 early defaulted loans. Quality control reviews of the early defaulted loans can provide valuable information about the causes of default that may indicate inadequate underwriting. A Mortgage Access Corporation official stated that the focus for early defaulted reviews was to identify patterns and common factors among participants in the origination process; therefore, the lender could select for review loans in which six or more payments had been made. However, HUD regulations do not relieve the lender from its responsibility to review all early payment defaulted loans. Mortgage Access Corporation officials acknowledged that weaknesses existed in their early payment default quality control reviews, and they agreed to implement the HUD-required procedures.

Quality Control Reviews of Early Defaulted Loans Were Not Conducted in a Timely Manner

Quality control reviews for another 17 of 41 loans were significantly delayed. These loans were not reviewed within three to four months from the date that the loans were first reported as in default. Generally, early payment defaulted loans have a high incidence of problems; therefore, it is important to conduct quality control reviews in a timely manner so that lenders can identify patterns of deficiencies or problems that can be used as a training aid to eliminate problems in underwriting HUD/FHA loans. Mortgage Access Corporation officials acknowledged weaknesses in the timeliness of conducting early payment defaulted quality control reviews, and they agreed to correct their controls.

Documentation of Reverifications Was Inadequate

Our review of two randomly selected early payment default quality control reports found that contrary to HUD regulations, loan documents were not reverified. HUD Handbook 4060.1, REV-2, paragraph 7-6 E, states that documents contained in the loan file should be checked for sufficiency and subjected to written reverification. Items that must be reverified include but are not limited to the borrower's employment or other income, deposits, gift letters, and other sources of funds. If the written reverification is not returned, a documented attempt must be made to conduct a telephone reverification. If the original information was obtained electronically or involved alternative documents, a written reverification must still be attempted. Without detailed quality control reviews, problems in the loan origination and underwriting will not be identified and corrected. As a result, Mortgage Access Corporation's quality control reviews did not serve as a tool for identifying and correcting problems in origination and underwriting procedures.

Management Did Not Address Quality Control Review Findings

Our review of two randomly selected early payment default quality control reports found that although quality control reports identified deficiencies that needed to be addressed, management did not provide written responses to the findings nor document what corrective action was taken or would be taken to address the material findings noted. Paragraph 7-3I of HUD Handbook 4060.1, REV-2, requires that management take prompt action to deal appropriately with any material findings. The final report or an addendum must identify actions being taken, the timetable for their completion, and any planned followup activities. Mortgage Access Corporation officials mentioned that upon completion of reviews, regular meetings were held with operations managers to discuss findings and the corrective action plan verbally. However, they did not document their actions. Officials stated that they would implement the procedures, and in addition to regular meetings, a written response would be required from management.

Conclusions

Mortgage Access Corporation had weakensses in the implementation of its quality control plan because it did not review all early payment defaulted loans, ensure that quality control reviews were conducted in a timely manner, reverify appropriate loan documents, address quality control findings, or document that corrective action was taken or would be taken. As a result, the effectiveness of its quality control plan was lessened. Thus, Mortgage Access Corporation's inadequate quality control reviews of early payment defaulted loans could have contributed to origination and underwriting deficiencies/problems going undetected.

Recommendations

We recommend that the Assistant Secretary for Housing – Federal Housing Commissioner require

2A. Mortgage Access Corporation to establish procedures to ensure that (1) all HUD-insured loans that default within the first six payments are properly reviewed, (2) quality control reviews are performed in a timely manner, (3) the appropriate loan documents are reverified, and (4) adequate management follow-up is provided for any material findings resulting from quality control reviews.

2B. HUD's Homeownership Center's Quality Assurance Division to follow up with Mortgage Access Corporation within one year to ensure that the lender has implemented early payment default quality control reviews as required.

SCOPE AND METHODOLOGY

To achieve our objectives, we reviewed applicable laws, regulations, HUD handbooks, mortgagee letters, and reports from HUD's Quality Assurance Division. We reviewed independent audit reports issued by Mortgage Access Corporation's independent auditor and interviewed Mortgage Access Corporation's quality control officials to obtain an understanding of its internal controls.

We selected 20 defaulted loans from the Neighborhood Watch System that were underwritten by Mortgage Access Corporation with beginning amortization dates between May 1, 2005, and April 30, 2007. Loan selection was based on the following factors: loans that (1) defaulted within 12 or fewer payments, (2) were not indemnified by HUD, (3) were not reviewed by the Homeownership Center in Philadelphia, and (4) were not streamline refinanced. After review of the Homeownership Center files, we selected seven loans which appeared to have material underwriting deficiencies for on-site verification with Mortgage Access Corporation's files. The results of our detailed testing only apply to the seven loans tested and cannot be projected.

We performed detailed testing and review of Mortgage Access Corporation's underwriting procedures and reviewed documentation from both HUD's Homeownership Center endorsement files and loan files provided by Mortgage Access Corporation officials. Our detailed testing and review involved (1) analysis of borrowers' income, assets, and liabilities; (2) review of the borrowers' savings ability and credit history; (3) verification of selected data on the underwriting worksheet and settlement statements; and (4) confirmation of employment and gifts. We discussed compliance issues with HUD and Mortgage Access Corporation officials.

We also reviewed Mortgage Access Corporation's quality control plan as well as its quality control reports, logs, and checklist. We tested the sufficiency and timeliness of quality control reviews for closed, rejected, and early payment defaulted loans. We selected a sample of 14 quality control reports, which included quality control reviews of nine closed loans, three rejected loans, and two early payment default loans, to test the adequacy of quality control review procedures and to determine compliance with HUD requirements.

We performed the audit fieldwork from November 2007 through January 2008. We conducted our audit in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Program operations – Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

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

- Safeguarding resources – Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

- Validity and reliability of data – Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

Based on our review, we believe the following items are significant weaknesses:

- Mortgage Access Corporation did not ensure that certain loans were processed in accordance with all applicable HUD underwriting requirements (see finding 1).

- Mortgage Access Corporation did not adequately implement its quality control plan to ensure compliance with HUD's and its own quality control requirements (see finding 2).

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1A	93,500	
1B		480,897

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

2/ Recommendation that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. This includes reduction in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings which are specifically identified. In this instance, if HUD implements our recommendations to indemnify loans that were not originated in accordance with FHA requirements, it will reduce FHA's risk of loss to the insurance fund. The amount above reflects HUD's statistics reflecting that FHA has an average loss experience of 39 percent of the claim amount when it sells a foreclosed property.

Appendix B

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation **Auditee Comments**

Weichert Financial Services

Executive Offices
225 Littleton Road
P.O. Box 510
Morris Plains, NJ 07950-0510
1-800-829-CASH

April 9, 2008

Mr. Edgar Moore
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General
26 Federal Plaza, Room 3430
New York, NY 10278 0068

RE: Mortgage Access Corporation d/b/a Weichert Financial Services
Audit Report Number 2008-NY-10XX

Dear Mr. Moore,

Mortgage Access Corporation d/b/a Weichert Financial Services ("MAC/WFS") is in receipt of HUD's Office of Inspector General ("OIG") Notice dated March 25, 2008. In which OIG provided a Draft Audit Report that contained two tentative findings that were found during an audit for loans with beginning amortization dates between May 1, 2005 and April 30, 2007.

After receiving the Notice, MAC/WFS conducted a thorough review of the findings and the loan files referenced therein. While MAC/WFS complied with FHA guidelines in some cases, we recognize that the Notice identifies certain deficiencies. In those cases we have acknowledged the deficiency. At all times MAC/WFS endeavored to provide dependable and professional service to both loan applicants and HUD, we are committed to educate and train our employees on issues regarding FHA compliance. This response and supporting documentation demonstrates any deficiencies that existed in connection with the findings in the Notice were addressed and substantial changes were made to ensure that such deficiencies do not recur. We appreciate this opportunity to respond to the matters raised in the Notice.

BACKGROUND/OVERVIEW

MAC/WFS received approval to participate in the Departments FHA mortgage insurance program as a non-supervised lender in 1983. The company has always maintained a strong commitment to its applicants and its relationship with HUD. The Company was a strong participant in HUD/FHA programs and produced high quality loans and is committed to ethical lending practices. We recognize and acknowledge that the default and claim rate exceeded the state's requirement of originated HUD/FHA loans for the period from 2005 through 2006.

Ask About Weichert's
One-Stop Shopping Services

Ref to OIG Evaluation **Auditee Comments**

Edgar Moore
April 9, 2008
Page 2

The majority of the loans in default and cited in the Notice were approved by one underwriter. We have taken disciplinary action against this employee, and terminated her position with MAC/WFS, which occurred well before the Department's audit.

We have made additional changes to our policies and procedures to ensure compliance with FHA requirements. Among the actions taken: (1) we terminated an underwriter responsible for a majority of the problem loans; (2) we made an underwriting manager change; (3) we have adjusted the number of FHA underwriters in an effort to better train and manage the loan approval process; (4) we have had several training sessions addressing fraud, income, assets and compensating factors, in addition, the DE designated underwriters have successfully completed two test cases; (5) every third FHA loan underwritten is being randomly audited and immediate feedback is provided to the respective underwriter; (6) we have revised and redistributed our FHA Underwriting Review Checklist as well as the Closing Checklist; (7) we are conducting a Quality Control audit prior to each loan closing; (8) we have tightened controls around the HUD-1 approval process to ensure that every HUD-1 is reviewed and approved by a DE underwriter prior to loan closing with a checklist being utilized for each review; (9) our Quality Control Plan was revised specifically to ensure that: quality control reviews are conducted for all loans that default within six months of closing, reviews of defaulted loans are reviewed in a timely manner, adequate re-verifications of loan documents are performed and management will address the material deficiencies identified in quality control findings. MAC/WFS have always taken its responsibilities as an FHA approved lender seriously and values its reputation with the Department.

RESPONSE TO FIDNINGS

In finding 1, the Notice states that MAC/WFS did not always adhere to HUD/FHA regulations in underwriting FHA insured loans. Specifically seven loans exhibited significant underwriting deficiencies. MAC/WFS did not always (1) sufficiently analyze borrowers' credit, (2) adequately verify the source of funds to close, (3) ensure that the minimum cash investment requirement was met, and (4) properly verify the borrowers' employment and/or income. In addition to significant underwriting deficiencies, one loan was approved for an individual unit in a non-FHA approved condominium, which did not meet the 51 percent owner occupancy requirements for the unit to qualify for spot-loan financing.

In finding 2, the Notice states that MAC/WFS did not always comply with both HUD's and its own quality control requirements to ensure that (1) all HUD-insured loans that defaulted within the first six payments were reviewed, (2) reviews for early payment defaulted loans were conducted in a timely manner, (3) adequate re-verification of loan

Ref to OIG Evaluation	**Auditee Comments**

Edgar Moore
April 9, 2008
Page 3

documents was performed, and (4) management addressed the material deficiencies identified in the quality control findings.

Finding 1 – Underwriting Deficiencies

Case number: **351-4737353**

Deficiencies Noted:
- **Income Overstated**
- **Incorrect Debt-to-Income Ratios**
- **Excessive Debt-to-Income Ratios without Compensating Factors**
- **Inadequate Credit Analysis**
- **Funds to Close Not Verified**
- **Negative Cash Reserve on HUD-1**
- **Incomplete Sales Contract**

The Notice states that borrower's monthly income of $3,602 shown on the mortgage credit analysis worksheet was overstated by $264. Borrower's income was averaged over a period of 17.33 months, and appeared that income used to calculate included either overtime or bonus income. As of June 16, 2005 borrower's current year-to-date income should have been $18,360 (5.5 months) and based on the $40,058 annual salary the pay stub dated as of June 16, 2005 showed total compensation of $23, 731. HUD Handbook 4155.1, REV-5, section 2-7 A, provides that overtime and bonus income may be used as qualifying income if such income has been received for approximately the past two years and is likely to continue. The mortgage credit analysis worksheet did not list any compensating factors for ratios in excess of 31 and 43 percent, as stated in Mortgagee Letter 2005-16. The loan file did not contain a written explanation from the borrower regarding major derogatory accounts and various credit inquiries. The mortgage credit analysis worksheet indicated that the borrower's source of funds was $50,000 available from a pending real estate sale. The file did not contain a fully executed HUD-1 settlement statement (buyers and sellers signatures were missing), as a result borrower did not have sufficient funds to close the loan. There were pages from the sales contract that were missing.

Comment 1

With regard to the income that was used to qualify the borrower and listed on the mortgage credit analysis worksheet we acknowledge that the income was higher than what was reflected on the borrower's paystub. We respectfully disagree to the issue raised for borrower's income being averaged over a period of 17.33 months, this approach is conservative and an acceptable common practice.

Ref to OIG Evaluation	Auditee Comments

Edgar Moore
April 9, 2008
Page 4

Comment 2

With regards to no compensating factors listed on the mortgage credit analysis worksheet the loan was approved through FNMA Automated Underwriting System Desktop Underwriter (DU) with the higher ratios. The DU feedback did not require compensating factors to be listed, however, our company policy requires the underwriter to list compensating factors for all loans underwritten outside of HUD's parameters regardless of DU documentation level. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Comment 3

Regarding the unexplained derogatory accounts and recent inquiries, in this case we acknowledge that a written credit explanation letter should have been obtained. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Comment 4

Regarding funds to close not verified and negative cash reserve we respectfully disagree. The proceeds from sale of borrower's previous home was the source of funds for the down payment and closing costs. The file contained the HUD-1 settlement statement which evidenced $71,000 in net proceeds and the borrower required $38,593.11 to complete the transaction. While we recognize that the HUD-1 settlement statement was not fully executed the HUD-1 was received prior to loan closing, the borrower needed the funds to close the loan and the settlement agent would not have closed the loan had the borrower not received these funds. Having said that, we acknowledge that the HUD-1 settlement statement was not fully executed. Please note the omission of the signed HUD-1 settlement statement does not reflect Company policy or practice.

Comment 3

We acknowledge that the file did not contain all the pages to the Sales Contract. Please note the deficiency in connection with this matter does not reflect Company policy or practice.

Case Number **351-4764552**

Deficiencies Noted:
- **Incomplete Gift Fund Transfer**
- **Verification of Deposit Not Obtained**
- **Inadequate Credit Analysis**
- **Negative Cash Reserve on HUD-1**
- **Excessive Debt-to-Income Ratios**
- **Compensating Factors Listed Unallowable**
- **Verification of Paid-Outside-Closing Costs Not Obtained**
- **Verification of Rent Expense Not Obtained**

Ref to OIG Evaluation	**Auditee Comments**

Edgar Moore
April 9, 2008
Page 5

The Notice states that gift funds in the amount of $5,100 were not documented in accordance with HUD Handbook 4155.1, REV-5, section 2-10C. The source of funds for non payroll deposits totaling $11,855 were not documented. The borrower's credit report showed four derogatory accounts, three of which were placed for collection, a written credit explanation letter was not obtained. Adequate funds to close were not verified. Cash due from the borrower on the HUD-1 settlement statement was $4,100. If the unsupported paid-outside-closing cost for appraisal fee of $400 was added to the $4,100 the borrower was required to pay $4,500. The borrower only had an asset of $817 according to the mortgage credit analysis worksheet and would have had a deficit of $3,683 at closing. The $400 appraisal fee paid-outside-of-closing was not verified. There were no compensating factors listed on the mortgage credit analysis worksheet for ratios in excess of 31 and 43 percent. Borrower's rental payment history of $600 was not verified.

Comment 5

With regards to the gift funds not documented in accordance with HUD guidelines and unexplained large deposits we have been unable to locate the documentation in the file. Nevertheless, we are confident that such documentation was included in the file at the time of loan approval and in the case binder at the time of submission for FHA insurance endorsement. Without such documentation, the underwriter would not have approved, the investor would not have purchased, and HUD would not have insured the loan. Without this documentation we can not respond meaningfully to the deficiency noted.

Comment 3

Regarding the inadequate credit analysis we acknowledge that a written credit explanation letter should have been obtained. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Comment 6

In reference to the negative cash reserve we respectfully disagree. The HUD-1 settlement statement showed that the cost of the appraisal fee was $400 which was paid-outside-of-closing and a copy of the invoice is attached supporting documentation (Exhibit 1).

Comment 3

With regards to the excessive ratios and no compensating factors we acknowledge that the underwriter should have listed compensating factors to justify approving the loan with ratios that exceeded FHA threshold of 31 and 43 percent. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Ref to OIG Evaluation | **Auditee Comments**

Edgar Moore
April 9, 2008
Page 6

Comment 3

We acknowledge that the file did not contain evidence that the rental history was obtained. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Case Number: **351-4776935**

Deficiencies Noted:
- **. Incomplete MCAW**
- **. Inadequate Support for Income**
- **. Unsupported Earnest Money Deposit**
- **. Unexplained Derogatory Accounts**
- **. Funds to Close not Verified**
- **. Inadequate Funds to Close**
- **. Unsupported POC**

The Notice states that the file was missing borrower' s original pay stub covering the most recent 30-day period as required per HUD Handbook 4155.1, REV, section 3-1 E. The earnest money deposit of $5,745 that exceeded 2 percent of the sales price was not documented in accordance with HUD regulations. The credit report in the file indicated that the borrower had numerous late payments incurred within less than two years of the loan closing and a written credit explanation from the borrower was not obtained. The mortgage credit analysis worksheet and loan application listed $14,417 and $25,000 as assets, which appeared to be the borrower's retirement savings and estimated net proceeds from the sale of real estate. The file did not contain evidence of redemption of the retirement savings funds. Copy of the HUD-1 settlement statement for the property owned at that time indicated closing for both properties took place on the same day, there was no evidence in the file verifying actual proceeds from sale of real estate. The HUD-1 settlement statement for the FHA loan indicated that the borrower was required to pay $6,733.78. Due to the unsupported earnest money deposit of $5,745 and unsupported paid-outside-closing costs of $79 the borrower would have been required to pay $12, 557.78, the borrower did not have sufficient funds to close. The file did not contain any supporting documentation for $79 paid-outside-of-closing pest inspection fee before closing. The ratios listed on the mortgage credit analysis were incorrect because the principal, interest, tax, and insurance calculation excluded $273 in taxes.

Comment 3

In this case, as indicated in the Notice we acknowledge that; the mortgage credit analysis was incomplete, employment was not documented in accordance with HUD regulations, earnest money deposit was not documented, derogatory accounts were not explained, and $79 pest inspection fee paid-outside-of-closing was not supported. While we recognize that the file was not documented in full compliance with HUD regulations, thus, any deficiencies in connection with this matter constituted harmless error and do not

Ref to OIG Evaluation	Auditee Comments

Edgar Moore
April 9, 2008
Page 7

reflect Company policy or practice. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Comment 7

With regards to inadequate funds to close we respectfully disagree. The file contained the HUD-1 settlement statement from the sale of real estate that evidenced net proceeds of $23,000 and the borrower was required to provide $14,417 at closing. Therefore, the loan file contained acceptable documentation at the time of loan origination.

Case Number: **351-4778778**

Deficiencies Noted:
. Inadequate Credit Analysis
. Inadequate Gift Fund Transfer Documents
. Gift Funds did not Meet HUD/FHA Requirements
. Earnest Money Deposit not Supported
. Incorrect Calculation of Maximum Mortgage Amount
. Ratios Exceeded without Compensating Factors
. Negative Cash Reserve on HUD-1
. Verification of Paid-Outside-Closing Cost not Obtained

The Notice states that the file did not contain a written explanation from the borrower documenting the events that led to bankruptcy and failed to analyze risk of possible mortgage default. The transfer of gift funds from donor to the borrower was not documented. The amount of gift was $3,800 and was used as earnest money deposit which was not supported. Since the gift funds did not meet HUD requirements a dollar for dollar reduction in the sale price was required, therefore, the maximum mortgage amount should have been reduced according to HUD Handbook 4155.1, REV-5, section 1-7 B. There were no compensating factors provided for excessive debt-to-income ratios. The borrower only had $2,093 in a bank account and was required to pay $4,419 at closing, therefore, borrower would have had a negative cash reserve of $2,325. The HUD-1 settlement statement in the file reported that the borrower paid $619 for first quarter taxes outside-of-closing, there was no documentation to show that this amount had been paid before closing.

Comment 3

Regarding the inadequate credit analysis we acknowledge that a written explanation should have been obtained. In addition, compensating factors should have been listed for ratios exceeding HUD's parameters. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Ref to OIG Evaluation	Auditee Comments

Edgar Moore
April 9, 2008
Page 8

Comment 8

With regards to assets not documented in accordance with HUD's requirements we respectfully disagree. The loan file contained sufficient documentation to evidence that the borrower obtained gift funds in this case. The file contained a cashier's check in the amount of $3,800 and the funds were deposited directly into the real estate selling agent's account. The file evidenced sufficient documentation to verify assets.

Case Number: **351-4791637**

Deficiencies Noted:
. Inadequate Documentation for Gift Fund Transfer
. Inadequate Credit Analysis
. Negative Cash Reserve on HUD-1
. Ratios Exceeded without Compensating Factors
. Verification of Paid-Outside-Closing Costs not Obtained

The Notice states that the file did not contain gift fund transfer documentation as required by HUD Handbook 4155.1, REV-5. A copy of the official check was illegible, therefore, it is considered to be an inadequate supporting document. The borrower had filed for chapter 13 bankruptcy on December 20, 2004. The file was not documented whether the one year payout period under bankruptcy had elapsed, if the borrower's payment performance had been satisfactory and failed to obtain a sufficient written explanation from the borrower. Cash due from the borrower on the HUD-1 settlement statement was $10,797. If the unsupported paid-outside-closing costs of $400 for the appraisal fee and the $278 for property taxes were included the borrower would need $11,475. According to the bank statement and mortgage credit analysis worksheet the borrower only had $423 in assets available, therefore, the borrower had a deficit of $11,054 at closing. There were no compensating factors listed for ratios in excess of HUD's parameters.

Comment 9

Regarding inadequate gift fund transfer we respectfully disagree. The file contained a copy of the cashier's check in the amount of $11,500 made payable to the borrower. Thus, the loan file was documented that gift funds were verified in compliance with HUD's regulations and that the borrower had sufficient funds to close.

Comment 3

We acknowledge that there were no compensating factors listed for ratios in excess of HUD's parameters and the file was not documented whether the one year of payout period under bankruptcy had elapsed. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Ref to OIG Evaluation	Auditee Comments

Edgar Moore
April 9, 2008
Page 9

Case Number: **352-5447285**

Deficiencies Noted:
- **Inaccurate Debt-to-Income Ratios**
- **Inadequate Compensating Factors**
- **Inadequate Disclosure of Liability**
- **Employment Income Overstated**
- **Inadequate Earnest Money Deposit Documentation**
- **Assets in Investment Account Not Verified**
- **Negative Cash Reserve on HUD-1**
- **Verification of Paid-Outside-Closing Costs not Obtained**

The Notice states that two of the three compensating factors listed on the mortgage credit analysis worksheet are not allowable according to HUD Handbook 4155.1, REV-5, section 2-13. A monthly installment payment of $226 was omitted from debt obligations. Monthly income on the mortgage credit analysis worksheet was listed as $4,592, however, our calculation of the monthly income was $3,432, income was overstated by $1,160. The file did not contain verification of earnest money deposit of $25,000. The mortgage credit analysis listed $57,549 as available assets, which appeared to be borrower's assets in an investment account. The file contained an account statement covering the period August 1 through September 30, 2005. Evidence of redemption and/or actual receipt of funds was not verified. The HUD-1 settlement statement reported that cash due from the borrower was $7,281 at closing. If adding the unsupported paid-outside-closing cost of $768 for hazard premium and the $25,000 unverified earnest money deposit the borrower would have been required to pay $33,049 at closing. The borrower only had $1,414 in assets in a bank account, therefore, the borrower would have had a deficit of $31,635 at closing.

Comment 3

In this case, as indicated in the Notice we acknowledge the deficiencies and recognize that the file was not documented in full compliance with HUD regulations. Please note the deficiencies in connection with this loan constitute error and do not reflect Company policy or practice. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Ref to OIG Evaluation **Auditee Comments**

Edgar Moore
April 9, 2008
Page 10

Case Number: **352-5499451**

Deficiencies Noted:
- **. Property Not Eligible for FHA Insurance**
- **. Inadequate Employment Documents**
- **. Inadequate Credit Analysis**
- **. Inadequate Bank Documents**
- **. Inadequate Gift Funds Transfer Document**
- **. Negative Cash Reserve on HUD-1**

The Notice states the property was located in a non-FHA approved condominium building. The property did not meet the 51 percent owner occupancy requirement for spot-loan financing. The file did not contain a recent pay stub from the borrower. The borrower's credit report showed that one collection account and two of five late payment instances were incurred within two years of loan closing and a written credit explanation from the borrower was not obtained. The file contained only one month bank statement and HUD Handbook 4155.1, REV-5, section 3-1 F requires verification of deposit and the most recent bank statement or the most recent three months bank statements. The transfer of gift funds was not documented in accordance with HUD regulations. The mortgage credit analysis worksheet reported a gift in the amount of $4,800 and the gift letter listed the gift as $2,850. The HUD-1 settlement statement shows cash due at closing from borrower was $2,024. If $1,000 earnest money deposit is added, which appeared to be from an incomplete transfer of gift funds, the borrower would have been required to pay $3,024 at closing. The borrower only had $2,348 in assets available according to the bank statement and loan application.

Comment 3

In this case, as indicated in the Notice we acknowledge the deficiencies and recognize that the file was not documented in full compliance with HUD regulations. Please note the deficiencies in connection with this loan constitute error and do not reflect Company policy or practice. Substantial changes were made to ensure such deficiencies do not recur, as outlined on page two in paragraph one.

Finding 1 – Quality Control Plan

The Notice states that there are weaknesses in the implementation of the quality control plan because all early payment defaulted loans were not reviewed, ensure that quality control reviews were conducted in a timely manner, re-verification of appropriate loan documents, address quality control findings, or document that corrective action was taken or would be taken.

Ref to OIG Evaluation **Auditee Comments**

Edgar Moore
April 9, 2008
Page 11

As a result, the effectiveness of its quality control plan was lessened. Thus, inadequate quality control reviews of early payment defaulted loans could have contributed to origination and underwriting deficiencies/problems going undetected.

With respect of the Department's rules and regulations concerning the quality control plan the Company diligently practices sound quality control measures and understands the importance of an effective quality control plan. Our focus for early payment default reviews has always been to identify patterns and common factors among participants in the mortgage origination process. As a result of previous early payment default reviews significant changes were made to our operations policies and procedures to ensure compliance with FHA requirements, prior to the Department's audit.

Comment 3

Having said that, we acknowledge that not all loans that defaulted within the first six payments were selected for review and/or conducted in a timely manner. We recognize that there is room for improvement and have made changes to our policy and procedures in order to comply with HUD's requirement. Among the changes: (1) all loans which go into default within the first six month will be selected for QC review, (2) checklist will be utilized to verify full review has been conducted as well as re-verification of documents (Exhibit 2), (3) detailed report will be generated and distributed to Operations Management (Exhibit 3), (4) Management will be required to provide a written response to deficiencies found and provide corrective action plan, when applicable.

Thank you for your kind consideration and the opportunity to respond to the Notice. If you have any questions regarding the content of this letter or any other concerns, please do not hesitate to contact me directly at (973) 490-8167 or via email at iwahl@weicherfinancial.com.

Sincerely,

Irene Wahl
Vice President, Quality Control

Enclosures

Cc: Stephen Adamo, President
Nancy Crocetto, SVP Operations

OIG Evaluation of Auditee Comments

Comment 1 The lender agreed that the income was higher than what was reflected on the borrower's pay stub. HUD-OIG did not imply that the averaging of the borrower's income is unacceptable. The income calculated by the auditee included either overtime or bonus income. Income to qualify may include overtime, bonus, and commission income, however, the lender will need to verify receipt over the past 2 years and the probability of its continuance as per HUD Handbook 4155.1, REV-5, section 2-7 A. The verbal verification of employment (VOE) did not list any overtime and/or bonus income, or the probability of its continuation. Therefore, we conclude that the borrower's monthly income was overstated.

In addition, during the course of our review, we also noted that the routine quality control review of this loan by the lender's quality control department also noted that "income was not properly documented and QC ratios were 41.12 percent and 51.25 percent". Thus, the ratios calculated by its quality control department are almost in line with HUD OIG calculated ratios of 41.85 and 51.97 percent.

Comment 2 Based on the document in the file, this loan had received a risk classification as 'refer,' therefore it required a manual underwriting review per the FHA Total Mortgage Scorecard User Guide. Accordingly, Mortgagee Letter 2005-16 states that for manually underwritten mortgages, the lender must describe the compensating factors used to justify mortgagee approval when the borrower's mortgage payment to effective income ratio (front) and total fixed payment to income ratios (back) exceeded 31 and 43 percent respectively.

Comment 3 The lender generally agrees with our determinations.

Comment 4 The lender concurs that HUD-1 settlement statement for the sale of a home was not fully executed. HUD Handbook 4155.1, REV-5, section 2-10 E provides that a fully executed HUD-1 settlement statement must be provided as satisfactory evidence of the cash proceeds accruing to the borrower. If the property has not been sold by the time of the underwriting, then loan approval must be conditioned upon verifying the actual proceeds received by the borrower. Since the borrower's only source of funds appeared to be from proceeds from the sale of a home, we conclude that the lender did not verify and document all funds for the borrower's investment in the property and the borrower did not have sufficient funds to close the FHA loan, as required by HUD Handbook 4155.1, REV-5, section 2-10.

Comment 5 The lender did not provide any comment because they were unable to locate the applicable documents in their file. Our exceptions were based on the review of the documents contain in the Homeownership Center's (HOC) file.

Comment 6 The lender provided a copy of an invoice for paid-outside-closing cost for the appraisal fee of $400. As such, we removed this deficiency and modified the negative cash reserve deficiency to reflect that the borrower still had a deficit (negative cash reserve) of $3,283 at closing because cash due from the borrower on the HUD-1 settlement statement was $4,100 whereas the borrower only had an asset of $817 as per the mortgage credit analysis worksheet. We excluded the gift of $5,100 listed on the mortgage credit analysis worksheet because the lender did not document the transfer of gift funds as required by HUD Handbook 4155.1, REV-5, section 2-10 C.

Comment 7 The HUD-1 settlement statement indicated that the borrower was required to pay $6,734 at closing. Due to the unsupported earnest money deposit of $5,745 and the unsupported paid-outside-closing cost of $79, the borrower would have been required to pay $12,558. The source of the funds to close the FHA loan appeared to be proceeds from the sale of a home. However, the HUD-1 settlement statement indicated that the closing for both properties took place on the same day. Therefore, there was no evidence as to which property was closed first. If the FHA loan was closed before the closing of the other property then the borrower would not have proceeds available to close the FHA loan.

Thus, the lender did not verify the actual proceeds received by the borrower because the file did not contain a copy of a check or verification of the transfer of funds from the buyer of the property to the borrower. HUD handbook 4155.1, REV-5, section 2-10 E provides that a fully executed HUD-1 settlement statement must be provided as satisfactory evidence of the cash proceeds accruing to the borrower. If the property has not been sold by the time of the underwriting, then loan approval must be conditioned upon verifying the actual proceeds received by the borrower. Section 2-10 of the Handbook also states that all funds for the borrower's investment in the property must be verified and documented; this was not done.

Comment 8 The lender stated that the loan file contained sufficient documentation to evidence that the borrower obtained gift funds because the file contained a cashier's check for $3,800 and the funds were deposited directly into the real estate selling agent's account. However, the copy of the cashier's check indicates that it was purchased by the borrower, not the donor. The borrower's bank statement had a handwritten notation of the word "gift," which indicated that gift funds were in the borrower's bank account. Therefore, we conclude that the transfer of gift funds was not adequately documented because the lender did not document the transfer from the donor and failed to determine whether the gift funds were provided from an acceptable source and were the donor's own funds as required by HUD handbook 4155.1, REV-5, section 2-10 C.

Comment 9 The lender disagreed that the transfer of gift funds was not adequately documented. As per the lender, the gift was verified because the file contains a copy of the cashier's check for $11,500 made payable to the borrower. However, the copy of the check is illegible and therefore we consider it as an inadequate supporting document. We conclude that the transfer of gift funds was not adequately documented because the lender did not document the transfer of gift funds and failed to determine that gift funds were provided from an acceptable source and were the donor's own funds as required by HUD handbook 4155.1, REV-5, section 2-10 C.

Appendix C
SUMMARY OF UNDERWRITING DEFICIENCIES

Apendix	D-1	D-2	D-3	D-4	D-5	D-6	D-7 *	
FHA Case #	351-4737353	351-4764552	351-4776935	351-4778778	351-4791637	352-5447285	352-5499451	Total Mortgage Amount
Sample #	1	3	6	7	8	18	20	
Mortgage Amount ($)	153,869	167,250	188,500	164,400	267,750	291,300	93,500	**1,326,569**
Areas of Deficiencies:								
Inadequate Credit Analysis								
Inadequate Credit Analysis	x	x	x	x	x		x	
Inadequate Evaluation of Savings Pattern								**6 loans**
Inadequate Verification of Funds To Close								
Verification Of Deposit Not Obtained		x						
Verification of Assets in Investment account not verified						x		
Verification of assets in retirement savings account not verified			x					
Verification of proceeds from real estate property sale not vericed	x		x					
Verification Of POC Cost Not Obtained			x	x	x	x		
Inadequate Bank Account Documentation							x	
Inadequate Earnest Money Deposit Documentation			x	x		x		**7 loans**
Minimum Cash Investment Not Met								
Negative Cash Reserve on HUD-1	x	x	x	x	x	x	x	
								7 loans
Inadequate Verification of Income/Employment								
Inadequate Support For Income Calculation	x					x		
Inadequate Support For Employment			x				x	**4 loans**
Qualifying Ratios and Compensating Factors								
Inaccurate Debt To Income Ratios	x		x			x		
Inadequate Compensating Factors	x	x	x	x	x	x		
Inadequate Disclosure Of Liabilities						x		**6 loans**
Property not eligible for FHA insurance							x	**1 loan**
Indemnification Recommended	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Yes**	**Repay**	**1,233,069 ****

* A repayment of $93,500 is recommnded because this property was not eligible for FHA insurance.

** The total mortgage amount for the remaining six loans is $1,233,069. Based upon HUD's current 39 percent defaulted loss experience, the amount of funds to be put to better use for which indemnification is recommended is estimated at $480,897.

Appendix D

CASE SUMMARY NARRATIVES

Appendix D-1
Page 1 of 3

Case number: 351-4737353
Loan amount: $153,869
Settlement date: July 22, 2005
Default status: Delinquent

Pertinent Details:

A. Income Overstated

The borrower's monthly income of $3,602 shown on the mortgage credit analysis worksheet was overstated. The borrower's recent pay stub in the file showed an annual salary of $40,058, which equals $3,338 in monthly income. Therefore, monthly income was overstated by $264. The lender averaged the borrower's income over a period of 17.33 months, and it appeared that income used to calculate the year-to-date amount as of June 16, 2005, included either overtime or bonus income because it reflected a higher income. The borrower's current year-to-date income as of June 16, 2005, should have been $18,360 (5.5 months) based on the $40,058 annual salary; however, the pay stub as of June 16, 2005, showed total compensation of $23,731. HUD Handbook 4155.1, REV-5, section 2-7 A, provides that overtime and bonus income may be used as qualifying income if the borrower has received such income for approximately the past two years and there are reasonable prospects of its continuance. The verbal verification of employment did not list any overtime and/or bonus income or the probability of its continuance. The verbal verification also did not list the borrower's earnings or employer's name and telephone number.

B. Incorrect Debt-to-Income Ratios

C. Excessive Debt-to-Income Ratios without Compensating Factors

The ratios calculated by the lender were incorrect because the borrower's monthly income was overstated. On the mortgage credit analysis worksheet, the lender listed a mortgage payment-to-effective income ratio (front) and total fixed payment-to-effective income ratio (back) as 38.78 and 48.16 percent, respectively. Based on monthly income of $3,338, we calculated ratios of 41.85 and 51.97 percent, respectively. Mortgagee Letter 2005-16 states that the lender must describe the compensating factors used to justify mortgage approval when the borrower's mortgage payment-to-effective income ratio (front) and total fixed payment-to-income ratio (back) exceeds 31 and 43 percent, respectively. The lender did not list compensating factors.

D. Inadequate Credit Analysis

The lender did not conduct an adequate analysis of the borrower's credit history. HUD Handbook 4155.1, REV-5, section 2-3, provides that major indications of derogatory credit require a sufficient written explanation from the borrower. The credit report in the file indicated (1) various major derogatory accounts including judgments and collection actions, (2) late payment instances on a prior FHA real estate mortgage loan and other accounts, and (3) credit inquiries in the past 90 days.

The lender did not (1) obtain a written explanation from the borrower about major derogatory accounts and various credit inquiries, (2) analyze the borrower's payment history for housing obligations, and (3) document its analysis as to whether the late payments were based on a disregard for financial obligations, an inability to manage debt, or factors beyond the borrower's control.

E. Funds to Close Not Verified

HUD Handbook 4155.1, REV-5, section 2-10, provides that all funds for the borrower's investment in the property must be verified and documented. The mortgage credit analysis worksheet indicated that the borrower's source of funds was the $50,000 assets available from a pending real estate sale. The file did not contain a fully executed HUD-1 settlement statement for the property (it did not contain signatures of the buyers and seller). Section 2-10 E of the handbook provides that a fully executed HUD-1 settlement statement must be provided as satisfactory evidence of the cash proceeds accruing to the borrower. If the property has not been sold by the time of the underwriting, then loan approval must be conditioned upon verifying the actual proceeds received by the borrower. The lender must document both the actual sale and the sufficiency of the net proceeds required for settlement. The file did not contain any such documents.

F. Negative Cash Reserve on HUD-1

The lender did not verify or document that the borrower had adequate funds to close. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. Cash due from the borrower on the HUD-1 settlement statement was $38,593. The borrower's only source of funds appeared to have been proceeds from a pending property sale. Since the proceeds from prior real estate transactions were not verified as explained in the paragraph above, the borrower did not have sufficient funds to close the loan.

G. Incomplete Sales Contract

Pages from the sales contract were missing from the Homeownership Center and lender's binders. HUD Handbook 4165.1, REV-2, section 1-5, provides that the lender has the responsibility to ensure that all documentation is appropriate and conforms to the requirements. The lender must assemble the processing and closing documents and place them in the case binder.

Case number: 351-4764552
Loan amount: $167,250
Settlement date: November 18, 2005
Default status: Servicing transferred

Pertinent Details

A. Incomplete Gift Fund Transfer

The mortgage credit analysis worksheet listed $5,100 in gift funds. The file contained a copy of a gift letter, dated November 8, 2005, and a letter from the donor, dated November 9, 2005. The borrower's bank statements covering the period October 5 through November 3, 2005, did not indicate whether the gift funds were deposited. HUD Handbook 4155.1, REV-5, section 2-10 C, requires the lender to document the transfer of gift funds from donor to borrower by obtaining a copy of a cancelled check or other withdrawal documents showing that the withdrawal is from the donor's personal accounts, along with the homebuyer's deposit slip and bank statement showing the deposit. Further, the lender must be able to determine that the gift funds ultimately were not provided from an unacceptable source and were indeed the donor's own funds. This information was not documented.

B. Verification of Deposit Not Obtained

The borrower's bank statement indicated that the bank account was new and there were several unexplained nonpayroll deposits totaling $11,855 from September 2 through November 3, 2005. HUD Handbook 4155.1, REV-5, section 2-10 B, states that if there is a large increase in a bank account or the bank account was opened recently, the lender must obtain a credible explanation of the source of those funds. The lender did not obtain a credible explanation of the source of funds.

C. Inadequate Credit Analysis

The lender did not conduct an adequate analysis of the borrower's credit history. HUD Handbook 4155.1, REV-5, section 2-3, provides that major indications of derogatory credit require a sufficient written explanation from the borrower. The borrower's credit report showed four derogatory accounts, three of which were placed for collection. However, the lender did not obtain a written explanation of the derogatory accounts from the borrower.

D. Negative Cash Reserve on HUD-1

The lender did not verify or document that the borrower had adequate funds to close. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. Cash due from the borrower on the HUD-1 settlement statement was $4,100. We excluded gift fund of $5,100 because the lender did not verify and document it as explained in section A. Thus, the borrower only had an asset of $817 according to the mortgage credit analysis worksheet; therefore, the borrower would have had a deficit of $3,283 at closing.

E. Excessive Debt-to-Income Ratios

F. Compensating Factors Listed Unallowable

The mortgage credit analysis worksheet listed mortgage payment-to-effective income ratio (front) as 38.56 percent and total fixed payment-to-effective income ratio (back) as 47.03 percent, which exceeded the HUD threshold. Mortgagee letter 2005-16 states that for manually underwritten mortgages in which the direct endorsement underwriter must make the credit decision, the qualifying ratios are raised to 31 and 43 percent, and if either or both ratios are exceeded on a manually underwritten mortgage, the lender must describe the compensating factors used to justify mortgage approval. Compensating factors listed on the mortgage credit analysis worksheet were not allowable according to HUD Handbook 4155.1, REV-5, section 2-13.

G. Verification of Rent Expense Not Obtained

The lender did not verify the borrower's rental payment history. The borrower's current housing expenses on the loan application were listed as $600 for rent. HUD Handbook 4155.1, REV-5, section 2-3 A, states that the payment history of the borrower's housing obligations holds significant importance in evaluating credit. The lender must determine the borrower's payment history of housing obligations through either the credit report or verification of rent directly from the landlord. Since the borrower's credit report did not reflect the rental payment history, the lender should have verified rent directly from the borrower's landlord.

Case number: 351-4776935
Loan amount: $188,500
Settlement date: January 27, 2006
Default status: Repayment

Pertinent Details

A. Insufficient Employment Documentation

The lender did not obtain the borrower's original pay stubs covering the most recent 30-day period. HUD Handbook 4155.1, REV-5, section 3-1 E, requires the lender to obtain a verification of employment and the most recent pay stub showing year-to-date earnings of at least one month.

B. Inadequate Earnest Money Deposit Documents

The HUD-1 settlement statement reported an earnest money deposit of $5,745 that exceeded 2 percent of the sale price. The lender did not obtain supporting documents as required by HUD regulations. HUD Handbook 4155.1, REV-5, section 2-10A, provides that if the amount of the earnest money deposit exceeds 2 percent of the sales price or appears excessive, based on the borrower's history of accumulating savings, the lender must verify the amount of the deposit and the source of funds.

C. Inadequate Credit Analysis

The credit report in the file indicated that the borrower had numerous late payments incurred within less than two years of the loan closing; however, the lender did not obtain a written explanation from the borrower. HUD Handbook 4155.1, REV-5, section 2-3, provides that major indications of derogatory credit require a sufficient written explanation from the borrower.

D. Funds to Close Not Verified

The mortgage credit analysis worksheet and loan application listed $14,417 and $25,000 as assets, which appeared to be respectively the borrower's retirement savings account funds and estimated net proceeds from the sale of real estate. The file did not contain evidence of redemption of the retirement savings funds. Also, the copy of the HUD-1 settlement statement for the property owned at that time indicated that closing for both properties took place on the same day. Therefore, there was no evidence that proceeds from the real estate property sale were available to close the FHA loan. The lender did not verify actual proceeds. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented.

E. Negative Cash Reserve on HUD-1

The HUD-1 settlement statement for the FHA loan indicated that the borrower was required to pay $6,734. Due to the unsupported earnest money deposit of $5,745 (explained in paragraph B) and the unsupported paid-outside-closing costs of $79 (explained in paragraph H), the borrower would have been required to pay $12,558. Since the funds to close were not verified as explained above, the borrower did not have sufficient funds to close the loan.

F. Incorrect Debt-to-Income Ratios

G. Incomplete Mortgage Credit Analysis Worksheet

The mortgage credit analysis worksheet listed mortgage payment-to-effective income (front) and total fixed payment-to-income (back) ratios as 23.40 percent and 39.0 percent, respectively. The ratios were incorrect because, the principal, interest, tax, and insurance calculation excluded $273 in taxes on the mortgage credit analysis worksheet. After adding the $273 into the principal, interest, tax, and insurance calculation, the front ratio would increase to 27.89 percent and the back ratio to 43.51 percent, which is slightly higher than the HUD threshold. The lender did not list the compensating factors as required. Mortgagee Letter 2005-16 states that the lender must describe the compensating factors used to justify mortgage approval when the borrower's mortgage payment-to-effective income ratio (front) and total fixed payment-to-income ratio (back) exceed 31 and 43 percent, respectively.

H. Verification of Paid-Outside-Closing Costs Not Obtained

HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. The HUD-1 settlement statement reported that the borrower paid $79 for pest inspection before closing. However, the file did not contain any supporting documents.

Case number: 351-4778778
Loan amount: $164,400
Settlement date: February 8, 2006
Default status: Servicing transferred or sold

Pertinent Details

A. Inadequate Credit Analysis

The credit report in the file reported that the borrower had filed for chapter 7 bankruptcy in the past. Contrary to HUD Handbook 4155.1, REV-5, section 2-3, the lender did not obtain a written explanation from the borrower and did not document that the borrower's current situation indicated that the events that led to bankruptcy were not likely to recur. Therefore, the lender failed to analyze how the previous failure did not represent a risk of possible mortgage default.

B. Inadequate Gift Fund Transfer Documents

C. Gift Funds Not Meeting HUD/FHA Requirements

The lender did not document the transfer of gift funds from donor to the borrower. The borrower's bank statement had a hand-written notation of "gift," which indicated that $3,800 in gift funds were in the borrower's bank account. HUD Handbook 4155.1, REV-5, section 2-10 C, states that if the gift fund is in the borrower's bank account, the lender is required to document the transfer of the gift funds from the donor to the homebuyer by obtaining a copy of the cancelled check or other withdrawal document showing that the withdrawal is from the donor's account. The homebuyer's deposit slip and a bank statement that shows the deposit is also required. The file only contained the borrower's bank statement.

A notarized letter signed by the donor, dated January 30, 2006, that was faxed from borrower's place of employment stated that the donor gave a cash gift. Cash on hand is not an acceptable source of donor's gift funds according to section 2-10 C of the HUD handbook. Further, regardless of when the gift funds are made available to the homebuyer, the lender must be able to determine that the gift funds ultimately were not provided from an unacceptable source and were indeed the donor's own funds. In addition, the gift letter did not include the required donor's address and phone number.

D. <u>Earnest Money Deposit Not Supported</u>

The earnest money deposit of $3,800 of the total $4,800 shown on the mortgage credit analysis worksheet and the HUD-1 appeared to be from an unverified and unacceptable source of gift funds as explained in the above paragraph; therefore, the $3,800 earnest money deposit is unsupported.

E. <u>Incorrect Calculation of Maximum Mortgage Amount</u>

Since the gift funds did not meet HUD requirements, as explained in the above paragraphs, a dollar-for-dollar reduction in the sale price was required. As a result, the maximum mortgage amount should have been reduced according to HUD Handbook 4155.1, REV-5, section 1-7 B.

F. <u>Ratios Exceeded without Compensating Factors</u>

The lender did not provide any compensating factors to justify the excessive debt-to-income ratios. Mortgagee Letter 2005-16 states that the lender must describe the compensating factors used to justify mortgage approval when the borrower's mortgage payment-to-effective income ratio (front) and total fixed payment-to-income ratio (back) exceed 31 and 43 percent, respectively. The borrower's ratios were 35.25 and 47.33 percent, respectively, according to the lender's calculation.

G. <u>Negative Cash Reserve on HUD-1</u>

HUD Handbook 4155.1, REV-5, section 2-10, provides that all of the funds for the borrower's investment in the property must be verified and documented. The borrower did not appear to have sufficient funds to close. If we add the $3,800 earnest money deposit, which appeared to have come from an unverified and unacceptable gift source, and the unsupported payment of $619 in paid-outside-closing funds toward the first quarter taxes (explained in paragraph H), the borrower would have been required to pay $4,419 at closing. The borrower only had $2,093 in a bank account; therefore, the borrower would have had a negative cash reserve of $2,325.

H. <u>Verification of Paid-Outside-Closing Costs Not Obtained</u>

The lender did not verify the payment for the paid-outside-closing costs. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. The HUD-1 settlement statement in the file reported that the borrower paid $619 for first quarter taxes outside the closing. However, there was no documentation to show that this amount had been paid before closing.

Case number: 351-4791637
Loan amount: $267,750
Settlement date: May 19, 2006
Default status: Repayment

Pertinent Details:

A. Inadequate Documentation for Gift Fund Transfer

The mortgage credit analysis worksheet and gift letter listed $11,500 as a gift. According to a Fannie Mae underwriting finding document, dated April 28, 2006, the lender was required to document and retain a copy of the transfer of gift funds and confirm that the gift came from an acceptable source. However, the file did not contain gift fund transfer documentation as required by HUD Handbook 4155.1, REV-5. According to the lender, the official check for $11,500 was made payable to the borrower. The copy of the official check was illegible; therefore, we consider it to be an inadequate supporting document. The borrower's bank statement covering the period December 29, 2005, through February 24, 2006, did not provide evidence that the gift funds were deposited into the account. HUD Handbook 4155.1, REV-5, section 2-10 C, requires the lender to document the transfer of funds from the donor to the borrower by obtaining a copy of the cancelled check or other withdrawal documents showing that the withdrawal was from the donor's account, along with the borrower's deposit slip and bank statement that shows the deposit. Further, the lender must be able to determine that the gift funds ultimately were not provided from an unacceptable source and were indeed the donor's own funds.

B. Inadequate Credit Analysis

The borrower had filed for chapter 13 bankruptcy on December 20, 2004. Contrary to HUD Handbook 4155.1, REV-5, section 2-3 E, the lender did not document whether the one-year payout period under bankruptcy had elapsed and whether the borrower's payment performance had been satisfactory. The lender also failed to obtain a sufficient written explanation from the borrower.

C. Negative Cash Reserve on HUD-1

The lender did not verify or document that the borrower had adequate funds to close. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. Cash due from the borrower on the HUD-1 settlement statement was $10,797. If the unsupported paid-outside-closing costs of $400 for the appraisal fee and the $278 for property taxes (explained in paragraph E) were added, then the borrower needed to pay $11,475 at closing. However, according to the bank statement and mortgage credit analysis worksheet, the borrower only had $423 in assets available. Therefore, the borrower would have had a deficit of $11,052 at closing.

D. Ratio Exceeded without Compensating Factors

The lender calculated the mortgage payment expense-to-income ratio (front) as 32.15 percent, which exceeded HUD’s threshold; however, no compensating factors were listed. Mortgagee Letter 2005-16 requires the lender to describe the compensating factors used to justify mortgage approval when the maximum ratios are exceeded.

E. Verification of Paid-Outside-Closing Costs Not Obtained

HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower’s investment in the property be verified and documented. The HUD-1 settlement statement reported that the borrower paid a $400 appraisal fee and $278.44 for property taxes outside of closing. However, there were no documents to show that these obligations had been paid before closing.

Case number: 352-5447285
Loan amount: $291,300
Settlement date: December 6, 2005
Default status: Modification started

Pertinent Details:

A. Inaccurate Debt-to-Income Ratios

B. Inadequate Compensating Factors

The mortgage credit analysis worksheet listed the mortgage payment-to-effective income ratio (front) and total fixed payment-to-income ratio (back) as 42.97 and 47.62 percent, respectively; however, these ratios were inaccurate because the lender understated liabilities and overstated income as explained in the paragraphs below. After adjusting income and liability, the debt-to-income ratios would increase to 54.17 and 65.11 percent. Two of the three compensating factors listed on the mortgage credit analysis worksheet are not allowable according to HUD Handbook 4155.1, REV-5, section 2-13. The third compensating factor stated that the borrower had an excellent reserve, which is allowable; however, the source of reserve appeared to be funds from an investment account, which was not verified and documented as explained below. Therefore, we concluded that debt-to-income ratios were exceeded without adequate compensating factors.

C. Inadequate Disclosure of Liability

The lender omitted a monthly $226 installment account payment. The account shown on the borrower's credit report had an outstanding balance of $2,943, and a monthly payment of $226 was required. If the borrower had continued to make a monthly payment of $226, it would have taken approximately 13 months to pay off the balance. HUD Handbook 4155.1, REV-5, section 2-11 A, requires the lender to include the monthly housing expense and all additional recurring charges extending 10 months or more, including payments on installment accounts.

D. Employment Income Overstated

Monthly employment income on the mortgage credit analysis worksheet was listed as $4,592; however, our calculation of the monthly employment income was $3,432. Therefore, income was overstated by $1,160.

E. Inadequate Earnest Money Deposit Documentation

The HUD-1 settlement statement reported an earnest money deposit of $25,000, which exceeded 2 percent of the sale price. The file did not contain a certification from the deposit holder acknowledging the receipt of the funds or a copy of a cancelled check as required by HUD Handbook 4155.1, REV-5, section 2-10 A.

F. Assets in Investment Account Not Verified

The mortgage credit analysis worksheet listed $57,549 as available assets, which appeared to be the borrower's assets in an investment account. The lender obtained an investment account statement covering the period August 1 through September 30, 2005. Evidence of redemption and/or actual receipt of funds was not verified and documented as required by HUD Handbook 4155.1, REV-5, sections 2-10 K and L.

G. Negative Cash Reserve on HUD-1

The lender did not verify or document that the borrower had adequate funds to close. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. The HUD-1 settlement statement reported that cash due from the borrower was $7,281 at closing. If we add the unsupported paid-outside-closing costs of $768 for hazard premium (explained in paragraph H) and the $25,000 unverified earnest money deposit (explained in paragraph E), the borrower would have been required to pay $33,049 at closing. However, the borrower only had $1,414 in assets in a bank account. Therefore, the borrower would have had a deficit of $31,635 at closing.

H. Verification of Paid-Outside-Closing Costs Not Obtained

HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. The HUD-1 settlement statement reported that $768 for hazard insurance premium was paid outside of closing; however, the file did not contain any supporting documents.

FHA number: 352-5499451
Loan amount: $93,500
Settlement date: June 23, 2006
Default status: Reinstated by borrower

Pertinent Details:

A. Property Not Eligible for FHA Insurance

The lender approved a loan for a property that was not eligible for FHA insurance. The property was located in a non-FHA-approved condominium building. If a condominium building is not FHA approved, it is possible that an individual unit may qualify for spot-loan financing. To qualify for spot-loan financing, the condominium also must meet the 51 percent owner occupancy requirements in addition to other requirements listed in Mortgagee Letter 96-41 and regulations at 24 CFR (*Code of Federal Regulations*) 234.26. Based on detailed information about condominiums obtained from HUD's Web site, the condominium did not meet the 51 percent owner occupancy requirements. In addition, the status of the condominium was shown as withdrawn as of April 27, 2001; therefore, the property did not meet the owner occupancy requirement for spot-loan financing. HUD's Single Family Housing, Homeownership Center Reference Guide, section 1-28, states that condominium projects that have been previously rejected or withdrawn by HUD are not eligible under the spot approval process.

We also noted a discrepancy between the number of units reported on the appraiser's report and by the condominium's management company. Mortgagee Letter 96-41 states that the lender must perform an underwriting analysis and certify that the project satisfies the eligibility criteria for spot-loan approval. It also states that the lender may use information provided by the appraiser, owners association, management company, and real estate brokers. However, it remains the lender's responsibility to ensure the accuracy of the information it relies upon and perform sufficient investigation and analysis to certify that the condominium project satisfies the eligibility criteria.

B. Inadequate Employment Documents

The lender did not obtain a recent pay stub from the borrower. HUD Handbook 4155.1, REV-5, section 3-1 E, requires the lender to obtain the most recent pay stub showing the year-to-date earnings of at least one month and the verification of employment. According to the verification of employment, dated June 6, 2006, the borrower had been working in New Jersey since January 1, 2004, whereas the credit report indicated that the borrower resided in North Carolina from August 26, 2003, to September 2004. This discrepancy was not explained.

C. Inadequate Credit Analysis

The lender did not conduct an adequate analysis of the borrower's credit history. HUD Handbook 4155.1, REV-5, section 2-3, provides that major indications of derogatory credit require a sufficient written explanation from the borrower. The borrower's credit report showed that one collection account and two of five late payment instances were incurred within two years of loan closing; however, the lender did not obtain an explanation from the borrower.

D. Inadequate Bank Documents

HUD Handbook 4155.1, REV-5, section 3-1 F, requires the lender to obtain a verification of deposit and the most recent bank statement. As an alternative to obtaining a verification of deposit, the lender may obtain from the borrower original bank statement(s) covering the most recent three-month period. Provided the bank statement shows the previous month's balance, this requirement is met by obtaining the two most recent, consecutive statements. The lender only obtained the bank statement for one month.

E. Inadequate Gift Funds Transfer Document

The lender reported $4,800 as a gift on the mortgage credit analysis worksheet, whereas the gift letter listed the gift as $2,850. The lender did not document the transfer of the gift funds. HUD Handbook 4155.1, REV-5, section 2-10 C, requires the lender to document the transfer of gift funds from the donor to the borrower by obtaining a copy of a cancelled check or other withdrawal documents showing that the withdrawal is from the donor's personal accounts, along with the homebuyer's deposit slip and bank statement showing the deposit. Further, regardless of when the gift funds are made available to the homebuyer, the lender must be able to determine that the gift funds ultimately were not provided from an unacceptable source and were indeed the donor's own funds.

F. Negative Cash Reserve on HUD-1

The lender did not verify or document that the borrower had adequate funds to close. HUD Handbook 4155.1, REV-5, section 2-10, requires that all funds for the borrower's investment in the property be verified and documented. Cash due from the borrower on the HUD-1 settlement statement was $2,024 at closing. If we add the $1,000 earnest money deposit, which appeared to be from an incomplete transfer of gift funds as explained in the paragraph above, the borrower would have been required to pay $3,024 at closing. However, the borrower only had $2,348 in assets available according to the bank statement and loan application.