Issue Date April 6, 2011	
Audit Report Number: 2011-CH-1007	

TO: Vicki B. Bott, Deputy Assistant Secretary for Single Family Housing, HU

FROM: Kelly Anderson

Kelly Anderson, Acting Regional Inspector General for Audit, 5AGA

SUBJECT PNC Mortgage Complied With HUD's Requirements for Loss Mitigation

HIGHLIGHTS

What We Audited and Why

We audited PNC Mortgage (PNC), a Federal Housing Administration (FHA)-approved nonsupervised lender and servicer. We selected PNC for audit based on a citizen's complaint regarding National City Mortgage Corporation (National City).[1] Our objective was to determine whether PNC actively and properly implemented the U.S. Department of Housing and Urban Development's (HUD) Loss Mitigation Program (program) for FHA-insured mortgages; specifically, whether it (1) prevented eligible borrowers from participating in the program and (2) inappropriately received loss mitigation incentive payments from HUD. The audit was part of the activities in our fiscal year 2010 annual audit plan.

What We Found

PNC complied with HUD's requirements for loss mitigation. It appropriately determined borrowers' eligibility and received loss mitigation incentive payments from HUD for only the borrowers that participated in the program. Therefore, the complainant's allegations that National City prevented eligible borrowers from participating in the program and received incentive payments from HUD for loss mitigation services that it did not provide were unsubstantiated.

[1] PNC acquired National City in December 2008. Therefore, the report will be addressed to the current entity.

What We Recommend

Since we did not identify any instances of noncompliance, this audit report contains no recommendations.

Auditee Response

We provided our discussion draft audit report to PNC's management on March 9, 2011. PNC did not request an exit conference.

We asked PNC to provide comments on our discussion draft audit report by March 24, 2011. PNC provided written comments, on March 24, 2011, that agreed with our conclusion in the report. The complete text of the auditee's response is provided in appendix A of this report.

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BACKGROUND AND OBJECTIVE

The U.S. Department of Housing and Urban Development (HUD) initiated the Loss Mitigation Program (program) in 1996 in an effort to provide maximum opportunities for Federal Housing Administration (FHA)-insured borrowers to retain home ownership. The program allows families to retain home ownership and significantly reduces the financial impact of foreclosure claims against the FHA insurance fund.

The program returns responsibility for managing loan defaults to the servicing lenders and provides financial incentives to recognize them for their efforts. The program includes five strategies used by lenders, as deemed appropriate, based on the borrowers' financial circumstances. Three of the program options promote retention of borrowers' homes (reinstatement options), while the remaining two options (disposition options) assist in the disposition of their homes.

The three reinstatement options are special forbearance, loan modification, and partial claim. Special forbearance is a written repayment agreement between a lender and borrower, which contains a plan to reinstate the mortgage loan that has been delinquent for at least 90 days. Loan modification is a permanent change in one or more of the terms of a borrower's loan, which if made, allows the loan to be reinstated and results in a payment the borrower can afford. A servicing lender can receive an incentive up to $200 for a completed special forbearance. The request for payment must be submitted within 60 days of the date of execution of the special forbearance agreement. Modifications may include a change in the interest rate; capitalization of delinquent principal, interest, or escrow items; extension of the time available to repay the loan; and/or reamortization of the balance due.

Partial claim is when a borrower's lender advances funds on the borrower's behalf in an amount necessary to reinstate the delinquent loan (not to exceed the equivalent of 12 months of the borrower's principal, interest, tax, and insurance payments). The borrower, upon acceptance of the advance, executes a promissory note and subordinate mortgage payable to HUD.

The FHA-Home Affordable Modification Program (HAMP) introduced a fourth FHA Loss Mitigation option from the Helping Families Save their Homes Act of 2009. The new loss mitigation reinstatement option effective August 15, 2009; allows the use of a partial claim of up to 30 percent of the unpaid principal balance as of the date of default combined with a loan modification. A three month trial period of revised payments completed by the borrowers is required to qualify for the FHA HAMP program. The servicer can receive an incentive of up to $1,250; $500 for the partial claim and $750 for the completed modification.

The two disposition options are preforeclosure sale and deed in lieu of foreclosure. A preforeclosure sale allows the borrower in default to sell the home and use the sales proceeds to satisfy the mortgage debt even if the proceeds are less than the amount owed. A servicing lender can receive a $1,000 incentive for a completed preforeclosure sale. Deed in lieu of foreclosure is another disposition option in which a borrower voluntarily deeds the home to HUD in exchange for a release from all obligations under the mortgage.

PNC Mortgage (PNC) is an FHA nonsupervised direct endorsement lender and mortgage servicer located in Miamisburg, OH. On December 31, 2008, PNC purchased National City Mortgage Corporation (National City). PNC participates in HUD's program, as did the former National City.

Our objective was to determine whether PNC actively and properly implemented HUD's program for FHA-insured mortgages; specifically, whether it (1) prevented eligible homeowners from participating in its program and (2) inappropriately received loss mitigation incentive payments from HUD. The audit was derived from a complainant's allegations that National City prevented eligible borrowers from participating in the program and received incentive payments from HUD for loss mitigation services that it did not provide.

RESULTS OF AUDIT

PNC Complied With HUD's Requirements for Loss Mitigation

PNC complied with HUD's requirements for loss mitigation. It appropriately determined borrowers' eligibility and received loss mitigation incentive payments from HUD for only the borrowers that participated in the program. Therefore, the complainant's allegations were unsubstantiated.

PNC Adequately Determined Borrowers' Eligibility

Using HUD's data maintained in its Single Family Data Warehouse system[2], we identified 23,505 loans, the borrowers of which were 90 days or more delinquent with their mortgage payments during the period January 1, 2007, through December 31, 2009. Of the 23,505 loans, 9,664 borrowers (41 percent) participated in the program, and the remaining 13,841 borrowers (59 percent) did not. Of the 13,841 borrowers, PNC determined that 55 were ineligible to participate in the program, or the borrowers' homes were in foreclosure.

For the 55 borrowers, we determined that

- 15 borrowers failed to follow through with their agreements or submit all required documentation in a timely manner,
- 13 borrowers vacated their homes or were unresponsive to PNC's attempts to initiate contact,
- 11 borrowers desired to remain in their homes but did not qualify for the program's retention options due to inadequate income,
- 8 borrowers were reviewed by PNC for loss mitigation assistance but were still going through the foreclosure process as of December 31, 2009,[3]
- 4 borrowers did not opt for the type of loss mitigation actions available, and
- 4 borrowers' delinquent mortgages were resolved without loss mitigation.

[2] SFDW is a HUD data system of FHA-insured mortgages identified by individual case numbers providing mortgage details related to the underwriting, servicing, and claims for each mortgage.
[3] PNC reviewed these eight borrowers for loss mitigation actions during our audit period. The borrowers were later approved for loss mitigation actions.

Therefore, for the 55 borrowers that PNC determined were ineligible or were in foreclosure during our audit period, there was no indication that these borrowers were unjustly prevented from participating in the program.

PNC Did Not Inappropriately Receive Loss Mitigation Incentive Payments From HUD

For the 13,841 borrowers that did not participate in the program, PNC did not submit claims or receive loss mitigation incentive payments from HUD. It only received payments for the 9,664 borrowers that participated in the program.

Conclusion

Our review disclosed that the complainant's allegations were unsubstantiated.

SCOPE AND METHODOLOGY

To accomplish our objective, we researched and reviewed applicable HUD handbooks, regulations, mortgagee letters, and other reports and policies related to the program. We also conducted interviews with HUD's staff.

In performing our review of the loan loss mitigation program, we

- Reviewed PNC's loss mitigation policies, loss mitigation quality control policies, loss mitigation case files, and loss mitigation internal quality control reviews.

- Interviewed PNC's employees, which included former National City employees that worked in its collections, claims, and loss mitigation departments.

- Reviewed PNC's internal quality control reviews of loss mitigation files.

- Compared the mortgage data from PNC with data in HUD's Single Family Data Warehouse.

- Reviewed PNC's and HUD's data to determine loss mitigation incentives paid per loan loss mitigation actions completed, as applicable.

Additionally, using HUD's data maintained in its Single Family Data Warehouse system, we identified 23,505 loans, the borrowers of which were 90 days or more delinquent with their mortgage payments during the period January 1, 2007, through December 31, 2009. Of the 23,505 loans, 9,664 (41 percent) borrowers participated in National City's/PNC's program, while the remaining 13,841 borrowers (59 percent) did not participate in the program. Of the 13,841 borrowers, we determined that 55 were either determined to be ineligible for loss mitigation or in foreclosure. Therefore, we selected these 55 borrowers (100 percent testing) for review.

We assessed the reliability of PNC's and HUD's computerized data and determined the data to be sufficiently reliable for our purpose. Audit testing and results were limited to addressing the complainant's allegations. Therefore, PNC's overall compliance with HUD's program requirements was not assessed during this audit.

We performed our onsite audit work at PNC's Miamisburg, OH, office. We performed our audit work from August to December 2010. The audit covered the period January 1, 2007, through December 31, 2009, and was expanded as necessary.

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

INTERNAL CONTROLS

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

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

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

Relevant Internal Controls

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

- Effectiveness and efficiency of operations – Policies and procedures that the audited entity has implemented to provide reasonable assurance that a program meets its objectives, while considering cost effectiveness and efficiency.

- Reliability of financial reporting – Policies and procedures that management has implemented to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles.

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

We assessed the relevant controls identified above.

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

Significant Deficiency

We evaluated internal controls related to the audit objective(s) in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance on the effectiveness of the internal control structure as a whole. Accordingly, we do not express an opinion on the effectiveness of PNC's internal controls.

APPENDIX

Appendix A

AUDITEE COMMENTS

Ref to OIG Evaluation **Auditee Comments**

PNC

Travis Saunders
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Dear Mr. Saunders:

PNC Mortgage appreciates the opportunity to review and exhibit our loss mitigation practices with the U.S. Department of Housing and Urban Development's Office of the Inspector General. Based on the positive outcome of this audit, PNC Mortgage respectfully declines the opportunity to further review this in an exit conference. PNC Mortgage remains committed to the on-going-quality servicing of HUD insured loans.

Respectfully,

Dave Schlegel

Dave Schlegel
Vice President, Loss Mitigation
PNC Mortgage, a Division of PNC Bank, NA