
AUDIT REPORT



FIRST COMMUNITY RESOURCES, INC.
ST. LOUIS, MO

SECTION 203(b) HOME MORTGAGE INSURANCE
PROGRAM

2001-KC-1005

SEPTEMBER 28, 2001

OFFICE OF AUDIT, GREAT PLAINS
KANSAS CITY, KANSAS



Issue Date	September 28, 2001
Audit Case Number	2001-KC-1005

TO: Ronald C. Bailey, Director, Denver Single Family Homeownership Center, 8AHH

Roger E. Niesen

FROM: Roger E. Niesen, District Inspector General for Audit, 7AGA

SUBJECT: First Community Resources, Inc.
Section 203(b) Home Mortgage Insurance Program
St. Louis, MO

We have completed an audit of First Community Resources, Inc, a loan correspondent approved by HUD on August 3, 1995. We selected First Community for audit because of the high default rate experienced in St. Louis, MO. Our audit objective was to determine whether First Community originated its HUD/Federal Housing Administration (FHA) insured loans in accordance with HUD's requirements.

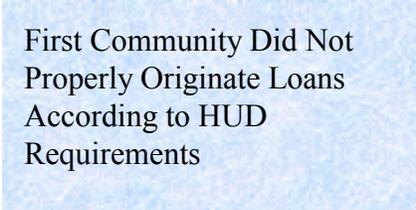
We reviewed five HUD/FHA insured defaulted loans that were originated by First Community. The loans were originated under HUD's section 203(b) program. We concluded that First Community did not originate four of the five loans in accordance with HUD's requirements. We did not find any problems with the other loan. This report contains one finding with four recommendations requiring action by your office.

Within 60 days please give us, for each recommendation in this report, a status report on: (1) the corrective action taken; (2) the proposed corrective action and the date to be completed; or (3) why action is considered unnecessary. Also, please furnish us copies of any correspondence or directives issued because of the audit.

Should you or your staff have any questions, please contact me at (913) 551-5870.

Executive Summary

We have completed an audit of First Community Resources, Inc., a loan correspondent since August 3, 1995. We selected First Community for audit because of their high default rate experienced in St. Louis. The audit objective was to determine whether First Community originated its HUD/Federal Housing Administration (FHA) insured loans according to HUD's requirements.



First Community Did Not Properly Originate Loans According to HUD Requirements

First Community Resources, Inc. improperly originated four of the five HUD/FHA insured loans we reviewed. The four loans were originated under HUD's section 203(b) program. First Community did not ensure a gift letter was included in a loan file, verify a co-borrower's employment history, verify borrowers had sufficient funds to close their loans, and adequately disclose the source of a down payment. Additionally, First Community does not have an adequate Quality Control plan. These problems exist because First Community does not have adequate management controls (i.e. enforced written policies and procedures) to ensure the proper origination of HUD/FHA insured mortgages.

Because HUD relied on First Community's loan origination process, HUD assumed abnormally high risks when it insured the four loans for \$293,081. One of the HUD/FHA loans foreclosed with a loss to HUD of \$23,564.

We recommend that the Director of the Denver Homeownership Center take appropriate action based upon the information contained in the Finding.

We presented our draft finding and narrative case presentations to First Community Resources during the audit. We held an exit conference with First Community on June 13, 2001. First Community Resources provided written comments to our finding and narrative case presentations on September 17, 2001. We included excerpts from the comments with our finding and narrative case presentations. Appendix C contains the complete text of First Community's written comments.

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Introduction

HUD approved First Community Resources, Inc. as a loan correspondent on August 3, 1995. First Community originates HUD/Federal Housing Administration (FHA) insured loans, Veterans Administration loans and conventional loans. The total number of loans originated and closed by First Community under FHA Programs was 86 in 1998; 61 in 1999 and 30 for the period January 01, 2000 through October 30, 2000.

First Community Resources, Inc. has offices in St. Louis, Missouri and Lincolnwood, Illinois. The St. Louis Office employs seven people. For the period January 1, 1998 through December 31, 1999 there were eleven mortgages originated by the St. Louis Office that defaulted. The HUD/FHA loans are underwritten by investors and sold to the investors for servicing. Our audit was limited to First Community's St. Louis Office Section 203(b) program activities.

Under the section 203(b) Program, the required downpayment for a loan can be reduced to 3 percent and the borrowers can finance approximately 97 percent of the value of their home purchase through their mortgage. In addition, closing costs can be financed. Under this program, the borrower may finance many of the closing costs, which in turn reduces the borrower's up-front cost of buying a house. The current limit range for a loan is \$81,548 to \$160,950 depending on factors such as cost of living and if the mortgage is for a multi dwelling property.

First Community's books and records are located at 7245 Delmar Boulevard, St. Louis, MO 63130. The president of the company is Kenneth Goffstein and the vice-president is Millard Goffstein.

Audit Objective

The overall audit objective was to determine if First Community Resources, Inc. originated HUD-insured section 203(b) loans in accordance with HUD's requirements.

Audit Scope and Methodology

Our audit included tests of compliance with HUD's requirements for the origination of HUD/FHA 203(b) loans. We performed in-depth reviews on five of the eleven loans that were in default status as of December 31, 1999. We selected loans to review where: the mortgagors had filed for bankruptcy, or defaults occurred before six payments had been made, or the seller was a real estate agent.

We interviewed HUD staff and First Community's management to evaluate First Community's management controls and procedures as they relate to the five defaulted loans we reviewed. We interviewed one borrower but were unable to contact the other four borrowers. We reviewed the adequacy of First Community's loan origination and quality control procedures. We reviewed HUD's and First Community's FHA mortgage files to determine if they contained all required documents.

Our audit covered the period January 1, 1998 through December 31, 1999. We conducted on-site audit work at First Community Resources, Inc. from February 2001 through June 2001.

The audit was conducted in accordance with generally accepted government auditing standards. We provided a copy of this report to the President of First Community Resources, Inc.

FIRST COMMUNITY RESOURCES, INC. DOES NOT ORIGINATE LOANS IN ACCORDANCE WITH HUD'S REQUIREMENTS

First Community Resources, a loan correspondent, does not always originate loans in accordance with HUD's requirements. First Community does not have adequate management controls (i.e., written policies and procedures) to ensure the proper origination of HUD/Federal Housing Administration (FHA) insured mortgages. Furthermore, where policies do exist they are not complete or they contain ineffective procedures. As a result, First Community has experienced a high default rate (8.09 percent), has not been able to take appropriate actions to identify the cause(s) for the high default rate, and has increased the risk to HUD's insurance fund

HUD Requirements

The following are some of HUD's requirements that lenders should follow when processing loans:

HUD Handbook 4060.1 Rev-1, Mortgagee Approval Handbook, Chapter 6 - Quality Control Plan requires mortgagee's:

- To establish a adequate written Quality Control Plan that provides for an independent review by the mortgagee's management/supervisory personnel who are knowledgeable of required procedures and do not have direct loan processing, underwriting or servicing responsibilities.
- To analyze loans that go into default within six months after closing.
- To retain for a period of one year the results of quality control reviews, whether by the mortgagee or an outside firm.
- To report violations of law or regulation to the HUD regional office.
- To include in their Quality Control Plan a provision for written reverification of a mortgagor's

employment, deposits, gift letter or other source of funds.

HUD Handbook 4155.1, Mortgage Credit Analysis for Mortgage Insurance on One to Four Family Properties, requires:

- Lenders to properly establish a borrower's capacity to repay the mortgage debt by appropriately verifying employment and income. Income that is not stable or will not continue should not be used. The borrower must explain gaps in employment of one month or more.
- When applicable, the mortgage file to properly document the amount of and other appropriate details regarding a gift.
- Satisfactory evidence to show that funds borrowed for the required downpayment are fully secured by existing marketable assets such as, stocks, bonds, automobiles, or real estate (other than the property being purchased).
- For each loan, a verification of deposit and most recent bank statements be included in the mortgage file.

Loans Were Not Properly Originated.

Our review consisted of five Section 203(b) Program loans that defaulted during the period January 1, 1998 through December 31, 1999. In four out of the five loans, First Community did not originate the loans in accordance with HUD's requirements. Specifically, First Community did not ensure a gift letter was included in a loan file, verify a co-borrower's employment history, verify borrowers had sufficient funds to close their mortgages, and adequately disclose the source of a down payment.

For one of the five loans we reviewed, First Community did not verify that there was a gift letter in the mortgage file. This gift was the source of funds necessary to close the mortgage for FHA Case Number 292-3509133. The amount needed from the borrower to close the loan was \$633. The \$633 was paid in money orders and signed by the borrower's daughter. The loan application stated the borrower's

daughter would provide the source of the down payment as a gift. However, the gift letter was not included in either HUD's or First Community's mortgage file. Since we were unable to contact the borrower's daughter we could not confirm whether or not the down payment was actually a gift. HUD regulations require the mortgage file to include a gift letter signed by the donor, specifying the dollar amount with a statement that the borrower does not need to repay the donor.

For the same loan, First Community did not adequately verify the co-borrower's employment history. First Community properly processed information related to the borrower; however, they did not for the co-borrower. For this loan the co-borrower's financial information was used to determine credit worthiness. The dates on the co-borrower's application differ from the dates on the verification of employment received from the employer. The application showed the co-borrower was employed for the period January 1997 through August 1997, while the verification of employment showed the period was April 1997 through August 1997. First Community did not obtain an explanation from the co-borrower for the difference in the reported information. HUD regulations state that borrowers must explain any gaps in employment of a month or more.

In addition, First Community did not properly determine the co-borrower's capacity to pay the mortgage debt. The co-borrower had three jobs within one year. According to the loan application, the co-borrower worked at the Holiday Inn from January 1997 through August 1997; at Hardees from August 1997 through October 1997; and at the Henry VIII Hotel starting in October 1997. The loan application is dated November 10, 1997. Since the changes in jobs were not promotions or for increased earnings, they indicate that the co-borrower may not have had a stable source of income. HUD regulations require a lender to only use stable income when establishing the borrower's capacity to repay the mortgage debt. Proper verification of a co-borrower's income helps protect HUD and the mortgage insurance fund against default. In this case the loan defaulted and HUD lost \$23,564.

In two of the five files we reviewed, First Community did not properly verify that borrowers had sufficient funds to close

their mortgages. For FHA Case Number 292-3559855, the HUD-1 closing statement showed that the borrower needed \$4,088 to close the loan. However, the mortgage files did not contain a verification of deposit or copies of the most recent bank statement to show that the borrower had sufficient funds to close the loan. The verification of deposit and copies of the most recent bank statements were also missing from the mortgage files for FHA Case Number 292-3673161. The HUD-1 closing statement showed the borrower needed \$449 to close the loan. HUD regulations state the lender must obtain a verification of deposit and the most recent bank statements or original bank statements covering the most recent three months.

For one of the five loans we reviewed, the borrower's application included an inaccurate description of the source of the down payment. First Community did not properly disclose on the application that the source of the down payment was a loan and not a gift. For FHA Case Number 292-3578102, the application showed the source of the down payment was a gift from a relative, when in fact it was a loan from a cousin's father-in-law. The borrower told us First Community knew the source of the down payment was a loan. The mortgage files contained information that showed the down payment was a loan even though the application showed it was a gift. The application was checked "no" where it asks if the down payment was borrowed and the Vice President of First Community signed the application. HUD regulations say funds can be borrowed for a required down payment as long as satisfactory evidence is provided that they are fully secured by existing marketable assets such as, stocks, bonds, automobiles, or real estate (other than the property being purchased). However, in this case the loan was from a private individual and First Community did not have any evidence that showed the loan was backed by marketable assets.

Management Controls Are
Not Adequate

The deficiencies noted above occurred because First Community does not follow adequate management controls. Specifically, First Community's policies and procedures do not require the use of their checklist, the duties of the loan officer and loan processor are not segregated, mortgage files are not secured before and after a loan is closed, and their Quality Control Plan is not adequate.

First Community did not include a requirement in their written policies and procedures that loan officers must use a checklist on all originated mortgage loans. First Community has a checklist that documents all the information a loan officer needs to obtain and maintain to close a loan. However, this checklist was missing from 3 of the 5 mortgage files we reviewed. In addition, the loan officer only used the checklist in 1 of the 2 files where it was included. Use of the checklist helps ensure that loans are processed and supported in accordance with requirements.

First Community does not adequately segregate the duties between the loan officer and loan processor. First Community's written policies and procedures allow loan officers to process loans they originate. Separating the responsibilities to authorize, process, record and review loan processing helps to reduce the risk of errors and the opportunity to commit fraud.

First Community does not adequately secure its mortgage files while loans are being processed or after they are closed, cancelled, or rejected. During our review we noted that open files were left on desks or in unsecured file cabinets. Closed mortgage files were kept unsecured down in the basement. Properly secured files help protect against lost information and misuse of sensitive information.

First Community's Quality Control Plan does not comply with HUD's requirements. Specifically, First Community's Quality Control Plan does not include the following:

- A requirement to review loans that go into default within six months.
- Procedures for expanding the scope of a review when a pattern of deficiencies or fraudulent activity is disclosed.
- Standards for retaining mortgage files.
- Procedures to notify HUD of significant discrepancies.
- Procedures to reverify gift letters.
- Procedures to review loans that have been rejected.
- Procedures that cover who performs a review of the mortgage loans (Management/supervisory personnel who are knowledgeable and have no direct loan

processing, underwriting or servicing responsibilities should accomplish the reviews).

HUD's Increased Risk

An adequate Quality Control Plan helps to identify and correct deficiencies in the loan origination process, and prevent repeat occurrences of problems.

The problems we identified all contributed to First Community's high default rate. First Community has experienced an 8.09 percent default rate while the average for other mortgagee's in St. Louis is 1.76 percent. First Community's lack of management controls increases the risk to the HUD insurance fund and to date has resulted in the loss of \$23,564.

Auditee Comments

Excerpts from the Auditee's comments on our draft finding follow. Appendix C contains the complete text of the comments.

First Community has always had a procedures manual and Quality Control Plan in place. Files were turned in to the office manager who logged them in and checked them for completeness, compliance and over-all acceptability. When we discovered that there were inaccuracies in files generated by one loan officer in particular, she was immediately dismissed.

Effective as of the date of your report, our company policy was amended to clearly state that First Community Resources does not allow loan officers to process their own files. We have also reminded everyone about the use of the checklist by not only keeping the form with the processors, but including it in the loan application packets made up for the loan officers. We have revised our quality control plan to include all of your recommended changes.

I would also like to point out that for the last two years, since the dismissal of this particular loan officer, our company has attained an excellent record as to a low delinquency and default rate.

As I mentioned earlier, the loan officer responsible for three of the five files reviewed was discharged from our

employment in November 1998. Prior to her discharge, she was questioned by one of our processors as to the reason for the lack of gift letters and supporting documentation. She stated that she was told by the investor's underwriter that, in lieu of a gift letter, the name, address, phone number and relationship of the donor could be put under "assets" on the Uniform Residential Loan Application.

We have recently hired a new sales/office manager to assist in the daily operations of the company. He has in excess of 20 years experience in the mortgage banking field in St. Louis with an in depth knowledge of the production, processing, and closing of FHA/HUD loans. His responsibilities include the following:

- 1. Review all loan applications for accuracy pre-qualifying prior to processing.*
- 2. Review all completed applications with required documentation prior to submission for underwriting.*
- 3. Review all approved applications for conditions required prior to closing.*
- 4. Review all rejected applications to determine the accuracy of the underwriter's decision.*
- 5. Meet periodically with all loan officers and processors to review current FHA/HUD processing and underwriting procedures, paying special attention to any recent changes.*

In addition, we have refined our processing department to develop Quality Control Manager who will have the ultimate responsibility for reviewing all pre-closed and closed files. This person will work directly with all departments to monitor the quality of all files in our office.

With the relocation of our office we will have the capability of properly securing all files when not use.

The proposed penalties are extremely excessive and do not reflect fairly on how First Community operates its business.

OIG Evaluation of
Auditee Comments

HUD Handbook 4155.1 requires the mortgage file to contain a gift letter specifying the dollar amount of the gift, signed by the donor and the borrower and stating no repayment is required. The Handbook does not state that in lieu of a gift letter, the name, address, phone number and relationship of the donor can be put under “asset” on the Uniform Residential Loan Application. If proper management controls were in effect, this error should have been caught.

The actions the auditee has taken and planned should correct the problems found in this review if the actions are followed and enforced.

We changed Recommendation 1D to recommend the Single Family Homeownership Center take appropriate administrative penalties rather than recommending specific courses of action.

Recommendations

We recommend that the Director, Denver Single Family Homeownership Center:

- 1A. Requires First Community Resources to implement policies and procedures that ensure loan officers: retain gift letters in mortgage files, properly verify and explain discrepancies in employment histories, verify borrowers have sufficient funds to close loans, and correctly disclose sources of downpayments.
- 1B. Requires First Community to develop and implement management controls that enforce the use of a checklist to process loans, prevent loan officers from processing loans they originate, and adequately secure mortgage files when not in use.
- 1C. Requires First Community to develop and implement a Quality Control Plan that complies with HUD’s requirements.
- 1D. Conducts a Quality Assurance review of First Community within the next six months.

- 1E. Takes appropriate administrative action against First Community Resources.

Management Controls

In planning and performing our audit, we considered the management controls in relation to First Community Resources, Inc.'s HUD/Federal Housing Administration (FHA) loan origination process to determine our auditing procedures and not to provide assurance on their management controls. Management controls include the plan of organization, methods and procedures adopted by management to ensure that resource use is consistent with laws, regulations, and policies; that resources are safeguarded against waste, loss, and misuse; and that reliable data are obtained, maintained and fairly disclosed in reports.

Relevant Management Controls

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

- Controls to ensure that HUD insured loans are originated in accordance with HUD requirements.

We assessed the relevant controls identified above.

It is a significant weakness if management controls do not provide reasonable assurance that resource use is consistent with laws, regulations and policies; that resources are safeguarded against waste, loss and misuse; and that reliable data is obtained, maintained and fairly disclosed in reports.

Significant Weaknesses

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

- First Community's policies and procedures do not require the use of their loan checklist, the duties of the loan officer and loan processor are not segregated, and mortgage files are not secured before and after a loan is closed. In addition, their Quality Control Plan is not adequate (see Finding 1).

Follow Up On Prior Audits

This is the first OIG audit of First Community Resources, Inc.

Schedule of Mortgages Reviewed

MORTGAGES REVIEWED

Appendix	FHA Case # 292-	Original Mortgage Amount	Endorsement Date	Status as of 12/31/99	Number of Payments	Deficiency
B	3509133	\$ 35,590	01/12/98	Default	2	A, B
B	3559855	100,099	04/03/98	Default	7	C
B	3578102	52,137	06/17/98	Default	3	D
B	3586158	50,853	06/22/98	Default	9	None
B	3673161	105,255	11/13/98	Default	8	C

DEFICIENCIES IDENTIFIED

<i>Deficiency</i>	<i>Explanation of Deficiencies</i>	<i>Number of Deficiencies</i>
A	Gift Letter not Verified	1
B	Employment History not Verified	1
C	Inadequate Verification on Funds to Close on Loan(s)	2
D	Inaccurate Description of the Source of Downpayment	1

Narrative Case Presentations

FHA Case Number: 292-3509133

Property Address: 2024 Bella Clare, St. Louis, MO 63136

Insured Amount: \$35,590

Borrowers: Madeline and Joice Woods.

Section of Housing Act: 203(b)

Date of Loan Closing: 1/12/98

Current Status: Foreclosed, default status after 2 payments, sold by HUD at a loss of \$23,564

Summary: First Community Resources mortgage file did not contain a gift letter. This gift was the source of funds needed to close the loan. The application stated the gift was from the borrower's daughter. However, we were unable to contact the borrower's daughter and could not verify whether the funds provided were actually a gift. Since the source of a borrower's funds can have a direct impact on his/her ability to repay a loan, it is important that a mortgagee properly establish and support that a source of funds is a gift. In addition, First Community Resources did not explain the gaps in employment that were evident when the initial application prepared by the co-borrower was compared to documentation received from the employer. Further, First Community did not adequately assess the co-borrower's ability to repay the debt. The co-borrower showed she worked at one job three months longer than the employer reported, creating an employment gap that should have been explained. The co-borrower also had three jobs within one year. Since the jobs did not represent increases in responsibility or earnings they may have reflected that the co-borrower did not have a stable source of income. First Community's files did not contain documentation to show how they determined the co-borrower's income was stable and could be expected to continue. HUD lost \$23,564 due to the foreclosure and resale of this property

Violations:

- A Gift Letter Was Not Included in the Mortgage File. HUD Handbook 4155.1, section 3, pg.'s 2-21 and 2-22, requires that the mortgage file contain a gift letter specifying the dollar amount of the gift. The letter must be signed by the donor and the borrower and contain a statement that no repayment is required. The gift letter must show the donors name, address, telephone number and relationship to the borrower.
- No Explanation of Gaps in Employment in the Mortgage File. HUD Handbook, chapter 2, pg.'s 2-9 through 2-10 requires that the borrower explain any gaps in employment of a month or more.

- The Lender Did Not Establish the Borrower's Capacity to Repay the Debt HUD Handbook, chapter 2, pgs 2-9 through 2-10 requires that the lender establish the borrower's capacity to repay the mortgage debt. Income from a source that can not be verified, is not stable or will not continue should not be used when calculating the borrower's income ratios.

Mortgagee Comments

The loan officer responsible for three out of the five files reviewed was discharged from our employment in November 1998. Prior to her discharge, she was questioned by one of our processors as to the reason for the lack of gift letters and supporting documentation. She stated that she was told by the investors underwriter that, in lieu of a gift letter, the name, address, phone number and relationship of the donor could be put under "assets" on the Uniform Residential Loan Application.

Evaluation of Mortgagee Comments

HUD Handbook 4155.1 requires the mortgage file to contain a gift letter specifying the dollar amount of the gift, signed by the donor and the borrower and stating no repayment is required. The handbook does not state that in lieu of a gift letter, the name, address, phone number and relationship of the donor could be put under "asset" on the Uniform Residential Loan Application. If the proper management controls were in place, such as the use of a checklist by the loan officers on all the loans originated, the loan processor should have caught this error. In addition, if the duties between the loan officer and loan processor had been segregated, the loan processor should have caught the error before the file went to the underwriter for final approval.

First Community Resources did not explain why they did not obtain an explanation on the gap in employment for the co-borrower.

FHA Case Number: 292-3559855

Property Address: 2 Wood Court, St. Louis, MO 63376

Insured Amount: \$100,099

Borrowers: Terry and Sherri Lewis

Section of Housing Act: 203(b)

Date of Loan Closing: 4/03/98

Current Status: Active; prior: default status after 7 payments

Summary: First Community Resources did not verify that the borrower had sufficient funds to close the loan. First Community did not obtain a verification of deposit from the borrower's financial institution nor did it have copies of the borrower's most recent bank statement to show that the borrowers had sufficient funds to close the loan. Verification of funds is an important step that helps ensure a borrower is financially able to meet the terms of a loan. Per the HUD-1, the amount needed from the borrowers to close the loan was \$4,088.

Violation:

- Verification of Deposit Not Included in the Mortgage File. HUD Handbook 4155.1, chapter 3, section 3.1, letter F requires a verification of deposit and most recent bank statements. If the lender does not use a verification of deposit, the lender must obtain from the borrower, original bank statement(s) covering the most recent three months (not more than 120 days old from when the loan has closed). The bank statement must show the previous month's balance

Mortgagee Comments

First Community Resources did not explain why they did not verify if the mortgagors had sufficient funds to close the loan.

Appendix B

FHA Case Number: 292-3578102

Property Address: 6435 Arthur, St. Louis, MO 63139

Insured Amount: \$52,137

Borrower: William E. Walls, Jr.

Section of Housing Act: 203(b)

Date of Loan Closing: 6/17/98

Current Status: Refinanced with another mortgage company; prior: default status after 3 payments

Summary: First Community Resources did not accurately describe the source of the down payment. The application showed the source of the down payment as a gift when in fact the source of the down payment was a loan from the borrower's cousin's father-in-law. The loan was obtained from a private individual and was not backed by existing marketable assets. The note included the terms for re-payment but was not included in the liability section of the application. The note was included on the assets side of the application as a gift. During our interview with the borrower, he said the mortgagee knew about the loan. We found a copy of the note in First Community's mortgage file and the Vice-President of First Community signed the application. It is important that the proper status of a borrower's funds be recorded in a loan file so that the borrower's ability to repay the loan is properly assessed.

Violation:

- Source of Down Payment was recorded as a gift but was actually a Loan. HUD Handbook 4155.1, chapter 2, D states that funds can be borrowed for a required down payment as long as there is satisfactory evidence provided that the funds are fully secured by existing marketable securities such as stocks, bonds, automobiles, and real estate (other than the property being purchased). In addition, certain types of loans such as signature loans, the cash value of life insurance policies, loans secured by a 401(k) do not require consideration of repayment for qualifying purposes.

Mortgagee Comments

First Community Resources did not explain why they did not document the source of down payment as a loan instead of a gift.

FHA Case Number: 292-3673161

Property Address: 1 Harvest Meadow, St. Louis, MO 63376

Insured Amount: \$105,255

Borrowers: James and Rebecca Pennington

Section of Housing Act: 203(b)

Date of Loan Closing: 11/13/98

Current Status: Active; prior: default status after 8 payments

Summary: First Community Resources did not verify that the borrower had sufficient funds to close the loan. First Community did not obtain a verification of deposit from the borrower's financial institution nor did it have copies of the borrower's most recent bank statement to show that the borrowers had sufficient funds to close the loan. Verification of funds is an important step that helps ensure a borrower is financially able to meet the terms of a loan. Per the HUD-1, the amount needed from the borrowers to close the loan was \$449.

Violation:

- Verification of Deposit Not Included in the Mortgage File. HUD Handbook 4155.1, chapter 3, section 3.1, letter F requires a verification of deposit or most recent bank statements. If the lender does not use a verification of deposit, the lender must obtain from the borrower, original bank statement(s) covering the most recent three months (not more than 120 days old from the time the initial loan application is made). The bank statement must show the previous months balance.

Mortgagee Comments:

First Community Resources did not explain why they did not verify if the mortgagors had sufficient funds to close the loan.

Appendix B

FHA Case Number: 292-3586158

Property Address: 33 Westdell Drive

Insured Amount: \$50,853

Borrower: Gwendolyn Fleming

Section of Housing Act: 203(b)

Date of Loan Closing: 6/22/98

Current Status: Active; Prior default status: 9 payments

Summary: Our review did not identify any problems with the way this loan was processed.

Auditee Comments

SEP 17 2001

**FIRST COMMUNITY RESOURCES, INC.**

September 13, 2001

Mr. Roger E. Niesen
District Inspector General for Audit
U.S. Department of Housing & Urban Development
Great Plains District, 7AGA
Gateway Tower II – 5th Floor
Kansas City, Kansas 66101-2406

Dear Mr. Niesen:

This letter is to acknowledge receipt by our office of your draft audit finding dated August 10, 2001. As I indicated in my letter of August 22, 2001 to Michelle Scott requesting an extension for our response, we are in the process of relocating our office. The new address is 8220 Delmar Blvd., St. Louis, MO 63124. Our new phone number is (314) 993-9777, and our new fax number is 993-9776. We should be in full operation at the new address by October 1, 2001.

Regarding your recommendations in the findings, I would like to state that First Community Resources has always had a office procedures manual and Quality Control Plan in place. Files were turned in to the office manager who logged them in and checked them for completeness, compliance, and over-all acceptability. When we discovered that there were inaccuracies in files generated by one loan officer in particular, she was immediately dismissed. Since First Community Resources has been in business, several Loan Officers who generated FHA loans have resigned because they felt our processing policies were too restrictive.

Effective as of the date of your report, our company policy was amended to clearly state that First Community Resources does not allow loan officers to process their own files. We have also reminded everyone about the use of the checklist by not only keeping the form with the processors, but including it in the loan application packets made up for the loan officers. We have revised our quality control plan to include all of your recommended changes.

I would also like to point out that for the last two years, since the dismissal of this particular loan officer our, company has attained an excellent record as to a low delinquency and default rate. I am attaching a letter from Commonwealth United Mortgage, with whom we have placed in excess of 90% of the FHA/HUD loans we have originated in the past two years, which more accurately confirms who we are and how we operate our business.

7245 Delmar Boulevard • St. Louis, Missouri 63130 • (314) 863-7747 • FAX (314) 863-3620





This brings me to a very important fact that was never mentioned in any of the findings. First Community Resources, Inc. has been approved by the U.S. Department of Housing and Urban Development as a Correspondent Lender. All of our FHA/HUD loans must be underwritten and approved by either FHA/HUD or an Eagle Level approved lender prior to closing. We fully understand that this does not relieve us of the responsibility of properly processing the application, but our company does not make the final decision as to the approval or rejection of the application.

As I mentioned earlier, the loan officer responsible for three of the five files reviewed was discharged from our employment in November 1998. Prior to her discharge, she was questioned by one of our processors as to the reason for the lack of gift letters and supporting documentation. She stated that she was told by the investor's underwriter that, in lieu of a gift letter, the name, address, phone number and relationship of the donor could be put under "assets" on the Uniform Residential Loan Application.

We have recently hired a new sales/office manager to assist me in the daily operations of the company. He has in excess of 20 years experience in the mortgage banking field in St. Louis with an in depth knowledge of the production, processing, and closing of FHA/HUD loans. His responsibilities include the following:

1. Review all loan applications for accuracy pre-qualifying prior to processing
2. Review all completed applications with required documentation prior to submission for underwriting
3. Review all approved applications for conditions required prior to closing
4. Review all rejected applications to determine the accuracy of the underwriter's decision
5. Meet periodically with all loan officers and processors to review current FHA/HUD processing and underwriting procedures, paying special attention to any recent changes.

In addition, we have refined our processing department to develop a Quality Control Manager who will have the ultimate responsibility for reviewing all pre-closed and closed files. This person will work directly with all departments to monitor the quality of all files in our office.

With the relocation of our office we will have the capability of properly securing all files when not in use.

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Since we have been in business, First Community Resources has sent their employees to various training programs for FHA loan originators and processors, not only to increase their knowledge, but also to make everyone aware of regulations and changes in the industry.

In conclusion, I believe that the proposed penalties are extremely excessive and do not reflect fairly on how we operate our business. Again, we did not make the final decisions on any of these loans. If the files were incomplete or incorrect, the underwriter prior to closing should have advised us. I wish to refer again to our excellent reputation with Commonwealth for the last several years. I personally have been in the mortgage banking industry in St. Louis in excess of 47 years, and I am proud to say that I enjoy a very good reputation. I have been originating FHA loans during this entire period and have not had one complaint.

Based upon the above stated facts, we would appreciate your reconsideration of your original recommendations and the elimination of the suggested penalties to be imposed up us.

Sincerely,

Millard Goffstein
Vice President/Branch Manager



**Commonwealth
United Mortgage**

A Division of National City® Mortgage Co.

10800 Farley, Suite 300
Overland Park, KS 66210
Telephone: (913) 661-0055
Fax: (913) 661-0559

September 6, 2001

Millard Goffstein
% First Community Resources
7245 Delmar Blvd.
University City, MO 63130

Dear Millard:

As always, it is a pleasure sending correspondence to our quality originators regarding their volume and low delinquencies.

Our records show that First Community Resources is ranked in the top 10 percent in loan volume and in the bottom 5 percent for delinquencies for loans originated out of our office.

Year-to-date you have sold us 81 loans for \$12.2 million and for the past 24 months of closed originations, you have had no conventional loans delinquent and only one FHA loan that has been 60 or more day's delinquent.

You and your staff are to be commended and we thank you for your quality business.

Sincerely,



Farley Gilliam
Regional Vice President

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United States, Senate, Washington, DC 20510

Chairman, Committee on Governmental Affairs, 706 Hart Senate Office Building,
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Chairman, Committee on Government Reform, 2185 Rayburn Building, House of
Representatives, Washington, DC 20515

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House of Representatives, Washington DC 20515

Subcommittee on Oversight and Investigations, Room 212 O'Neil House Office Building
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Director, Housing and Telecommunications Issues, United States General Accounting
Office, 441 G Street NW, Room 2T23, Washington DC 20548

Senior Advisor, Subcommittee on Criminal Justice, Drug Policy & Human
Resources, B373 Rayburn House Office Building, Washington, DC 20515

Chief, Housing Branch, Office of Management & Budget, 725 17th Street, NW, Room 9226,
New Executive Office Building, Washington, DC 20503

Department of Veterans Affairs Office of Inspector General, 810 Vermont Ave., NW
Washington, DC 20420

Department of Veterans Affairs OIG Audit Operations Division, 1100 Main, RM 1330,
Kansas City, Missouri 64105-2112

House Committee on Financial Services, 2129 Rayburn House Office Building,
Washington, DC 20515

Director, Office of Federal Housing Enterprise Oversight, 1700 G Street, NW, Room 4011,
Washington, DC 20552