AUDIT REPORT

MORTGAGE AMERICA BANKERS, LLC,

A NON-SUPERVISED LOAN CORRESPONDENT

KENSINGTON, MD

2004-PH-1012

September 10, 2004

OFFICE OF AUDIT, MID-ATLANTIC
PHILADELPHIA, PA

Issue Date
September 10, 2004
Audit Case Number
2004-PH-1012

TO: John C. Weicher, Assistant Secretary for Housing-Federal Housing Commissioner, H

FROM: Daniel G. Temme, Regional Inspector General for Audit, Mid-Atlantic, 3AGA

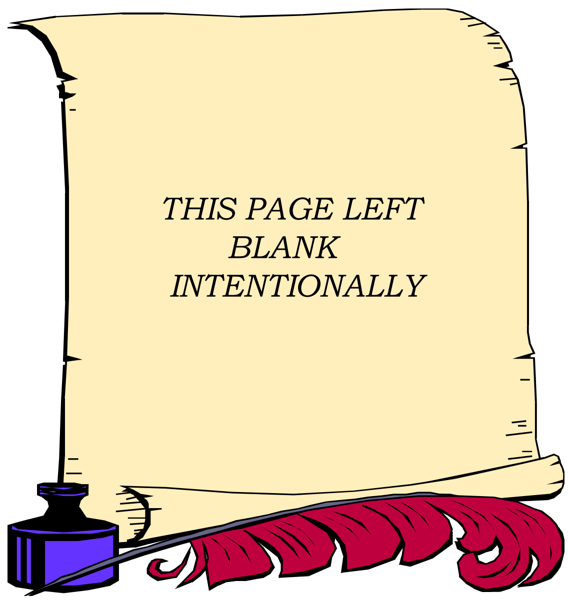
SUBJECT: Mortgage America Bankers, LLC, a Non-Supervised Loan Correspondent
Kensington, Maryland

We completed an audit of Mortgage America Bankers, limited liability company (LLC). We selected Mortgage America Bankers, LLC for review because of its high default rates. The objectives of our review were to determine whether Mortgage America Bankers, LLC, complied with HUD mortgagee approval requirements; complied with HUD regulations, procedures, and instructions in originating Federal Housing Administration (FHA)-insured loans selected for review; and Mortgage America Bankers, LLC's quality control plan is implemented according to U.S. Department of Housing and Urban Development (HUD) regulations. This report contains three findings and applicable recommendations requiring action by your office.

In accordance with HUD Handbook 2000.06, REV-3, within 60 days, please provide us for each recommendation without a management decision, 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. Additional status reports are required at 90 days and 110 days after the report is issued for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the audit.

We appreciate the courtesies and assistance extended by the management and staff of Mortgage America Bankers, LLC, and the HUD Philadelphia Homeownership Center.

Should you or your staff have any questions, please contact Ms. Christine Begola, Assistant Regional Inspector General for Audit, at (410) 962-2520.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Executive Summary

We completed a review of Mortgage America Bankers, LLC (Mortgage America), an FHA-approved non-supervised loan correspondent whose main office is located in Kensington, Maryland. The objectives of our audit were to determine whether Mortgage America complied with HUD mortgagee approval requirements; complied with HUD regulations, procedures, and instructions in originating FHA-insured loans selected for review; and Mortgage America's quality control plan was developed and implemented according to HUD regulations.

We found that Mortgage America's office operations did not comply with HUD/FHA mortgagee approval requirements, failed to justify loan overages and premium rate mortgages, and did not adequately develop and implement a quality control plan that meets HUD requirements. As a result, Mortgage America received $61,138 in ineligible fees and $27,718 in unsupported fees. In addition, it originated $2,983,501 in questioned loans. The results of our review are summarized below and detailed in the finding sections of this report.

Mortgage America Did Not Comply With HUD's Mortgagee Approval Requirements

Mortgage America did not administer its mortgagee office operations in conformity with HUD/FHA approval requirements as discussed in HUD Handbook 4060.1, REV-1. It originated loans from unauthorized offices and by non-Mortgage America employees, did not require exclusivity of its employees, and did not exercise control and supervision over its employees. In addition, it did not pay all of its employees' operating expenses. In our opinion, these deficiencies are a result of either Mortgage America's disregard for or lack of knowledge of HUD/FHA mortgagee approval requirements. Due to these compliance weaknesses, Mortgage America's eligibility as a HUD/FHA-approved mortgagee is questionable.

Mortgage America Could Not Justify Loan Discount Fees And Premium Rate Mortgages Charged To Borrowers

Mortgage America did not comply with HUD/FHA's loan origination regulations. It failed to justify loan overages (loan discount fees) charged to 13 borrowers; provided premium rate mortgages without reducing the borrower's closing costs (yield spread premiums) in 14 loans; and charged a real estate commission fee to one borrower when a financial interest existed between the real estate agent and Mortgage America. In our opinion, these deficiencies are a result of Mortgage America's disregard for or lack of understanding of HUD/FHA loan origination requirements. In addition, Mortgage America did not adequately supervise its branches and employees. Consequently, FHA loans originated by Mortgage America had unnecessarily higher mortgage payments, resulting in an increased risk to the FHA insurance fund.

Mortgage America's Quality Control Process Was Not Adequate

Mortgage America did not adequately develop and implement a quality control plan that fully meets HUD requirements as outlined in HUD Handbook 4060.1, REV-1, chapter 6. It failed to conduct the required quality control reviews or maintain its loan origination case files for the required 2-year period. The deficiencies associated with Mortgage America's quality control plan and procedures stem from either its disregard for or lack of knowledge of HUD's and its own quality control requirements. Therefore, Mortgage America is unable to guarantee the accuracy, validity, and completeness of its loan origination operations.

Recommendations

We recommend that HUD require Mortgage America to take immediate action to correct its ongoing operational deficiencies that do not comply with HUD/FHA mortgagee approval requirements. We also recommend that HUD require Mortgage America to establish policies and procedures to ensure that loans originated by its main and branch offices comply with HUD/FHA loan origination requirements. Further, we recommend that HUD take appropriate steps to ensure that Mortgage America takes immediate action to implement a quality control plan that meets all HUD requirements and consider taking appropriate administrative action against Mortgage America for its continual failure to comply with HUD requirements.

Auditee Comments

We provided our initial draft of this report to Mortgage America on June 25, 2004. We discussed the findings and recommendations with Mortgage America at an exit conference on July 8, 2004. Mortgage America provided written comments to the draft on July 22, 2004. Mortgage America's response consisted of a six-page letter and three attachments. The complete text of the letter is included in Appendix G. We did not include the attachments because they contained clients' personal loan information not available for public distribution.

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Introduction

The U.S. Department of Housing and Urban Development (HUD) insures mortgages made by private lending institutions under Section 203 of the National Housing Act. HUD designates these institutions as supervised mortgagees, non-supervised mortgagees, loan correspondents, investing mortgagees, and government institutions. Depending upon their designation, the institutions have the authority to originate, purchase, hold, service, or sell FHA-insured mortgages. A loan correspondent can only originate loans for an approved sponsor.

Mortgage America Bankers, LLC (Mortgage America) formed a limited liability company on May 6, 1996 under the laws of the state of Maryland. On December 4, 1998, HUD authorized Mortgage America as a non-supervised loan correspondent mortgagee. Mortgage America's main office is located at 3930 Knowles Avenue, Suite 305, Kensington, MD 20895.

As a non-supervised loan correspondent, Mortgage America's principal activity is the origination of mortgages for sale or transfer to an approved FHA sponsor under the HUD Single Family Direct Endorsement Program. The sponsor is responsible to HUD for the actions of its loan correspondent in originating insured mortgages. The sponsor underwrites the loans originated by the loan correspondent and is required to supervise and perform quality control reviews of its loan correspondents. The sponsor must be an approved mortgagee that is also authorized to participate in the HUD Single Family Direct Endorsement Program.

From September 1, 2001, through August 31, 2003, Mortgage America originated 146 FHA-insured loans totaling approximately $20 million. As of October 3, 2003, 14 of these loans (10 percent) have gone into default status at least once (see Appendix B). As of March 31, 2004, foreclosure action had been initiated on 8 of the 14 defaulting loans at least once during the life of the loan. Four of the eight loans have been conveyed to HUD with claims paid totaling $531,906 (see Appendix C). As of March 31, 2004, none of these four properties had been re-sold.

HUD's Quality Assurance Division performed a Title II monitoring review of Mortgage America in November 2001. The findings letter, prepared by the Quality Assurance Division, disclosed that Mortgage America's quality control plan failed to contain all elements required by HUD, and Mortgage America failed to implement its quality control plan in accordance with HUD guidelines and standards. It was not able to provide HUD with any quality control reports.

Audit Objectives

Our audit objectives were to determine whether Mortgage America complied with HUD mortgagee approval requirements; complied with HUD regulations, procedures, and instructions in originating FHA-insured loans selected for review; and to determine whether Mortgage America's quality control plan was developed and implemented according to HUD regulations.

Audit Scope And Methodology

To accomplish the audit objectives, we:

- Reviewed 100 percent of the FHA-insured loans (14 case files) originated by Mortgage America that had gone into early default at least once as of October 3, 2003. The 14 loans reviewed were from the universe of 146 loans originated by Mortgage America with beginning amortization dates for the 2-year period from September 1, 2001, to August 31, 2003. The results of the detailed testing apply only to the 14 FHA-insured loans selected and cannot be projected to the universe of 146 FHA-insured loans.

- Selected and reviewed an additional eight FHA-insured loans originated by Mortgage America with closing dates between July 1, 2003, to September 30, 2003 due to Mortgage America's current non-compliance with HUD/FHA guidelines (see Appendix B).

- Examined records and related documents of Mortgage America.

- Reviewed applicable HUD records relating to Mortgage America's non-supervised loan correspondent activities.

- Conducted interviews with officials and employees of Mortgage America and the HUD Quality Assurance Division.

In addition, we relied, in part, on data maintained by HUD in the Single Family Data Warehouse and Neighborhood Watch. We did not perform a detailed analysis of the reliability of HUD's Single Family Data Warehouse or Neighborhood Watch data.

Our audit generally covered the period of September 1, 2001, through August 31, 2003. Where applicable, the audit period was expanded to include current data through March 31, 2004. We conducted our fieldwork from October 2003 through May 2004.

Our review was conducted in accordance with Generally Accepted Government Auditing Standards.

Mortgage America Did Not Comply With HUD's Mortgagee Approval Requirements

Mortgage America did not administer its mortgagee office operations in conformity with HUD/FHA approval requirements as discussed in HUD Handbook 4060.1, REV-1. It originated loans from unauthorized offices and by non-Mortgage America employees, did not require exclusivity of its employees, and did not exercise control and supervision over its employees. In addition, Mortgage America did not pay all of its employees' operating expenses. These deficiencies and others noted below are a result of either Mortgage America's disregard for or lack of knowledge of HUD/FHA mortgagee approval requirements. Due to these compliance weaknesses, Mortgage America's eligibility as a HUD/FHA-approved mortgagee is questionable.

Mortgage America Originated HUD/FHA-Insured Mortgages From Offices Not Approved By HUD

Contrary to HUD requirements, we found Mortgage America was originating, processing and submitting FHA loans for endorsement from three locations that had not been approved by HUD. These locations included:

1. 3930 Knowles Avenue, Suite 305, Kensington, MD (Main Office)

2. 3006 St. Clair Drive, Marlow Heights, MD (Marlow Heights/Camp Springs)[1]

3. 1738 Elton Road, Silver Spring, MD

HUD Handbook 4060.1, REV-1, paragraph 1-2, General, states a mortgagee must be approved by HUD to originate, purchase, hold, or sell HUD/FHA-insured mortgages. In addition, subparagraph A states that for each branch office from which the mortgagee will submit mortgages for insurance, a Branch Office Notification Form and application fee must be submitted to the HUD field office in the jurisdiction in which the branch office is located. Further, according to Mortgagee Letter 2000-15, the origination of insured mortgages by lenders that have not received HUD/FHA approval increases the risk to the FHA

[1] The Marlow Heights office was formed in July or August 2002 after a previous branch located at 5625 Allentown Road, Camp Springs, MD, was closed. Two of the Camp Springs loan officers remained employed with Mortgage America and formed the Marlow Heights office. For purposes of this audit, we have grouped these branch offices together (Marlow Heights/Camp Springs).

insurance funds and to the public. Mortgagees found to be in violation may be subject to the full range of HUD sanctions.

HUD records show the only Mortgage America office approved by HUD to originate FHA mortgages is an office located at 8555 16th Street, Suite 205, Silver Spring, MD. However, our review found this location no longer functions as a Mortgage America office; instead, it is operated as a net branch of 1st Metropolitan Mortgage. Mortgage America moved its main office from the Silver Spring location to Kensington, MD in June or July 2003.

Of the 22 loans reviewed, Mortgage America originated 17 loans (77 percent) from unauthorized locations. Of these 17 loans, 15 loans were originated from the Marlow Heights/Camp Springs offices. The remaining two loans were originated from Mortgage America's branch office on Elton Road in Silver Spring.

Mortgage America's loan origination from unauthorized offices is a serious violation of HUD/FHA rules and regulations. Mortgage America's failure to register its main and branch offices with HUD has increased the risk to the FHA insurance fund and to the public. Four of the 17 loans originated from unauthorized offices have since been conveyed to HUD. The claims paid by HUD on these loans total $531,906 and should be paid back by Mortgage America. The other 13 loans originated from unauthorized offices have original mortgage amounts totaling $1,878,205 (see Appendix C). Due to the failure by Mortgage America to properly register its offices, we are seeking indemnification on these loans.

Mortgage America Did Not Originate And Close All HUD/FHA Loans In Their Own Name

Contrary to HUD loan origination requirements, Mortgage America did not originate and close all mortgages for HUD/FHA insurance endorsement in their own name. Of the 22 loans we reviewed, 4 loans totaling $573,390 were originated and closed by 1st Metropolitan Mortgage employees. Two of the four loans were originated and closed in the name of 1st Metropolitan Mortgage; however, Mortgage America's lender identification number was used to both originate and close these loans. In the other two loans, employees of 1st Metropolitan Mortgage originated and closed the loans in Mortgage America's name (see Appendix D). By allowing these four loans to be originated by non-Mortgage America employees, Mortgage America's former General Manager violated HUD/FHA requirements.

HUD Handbook 4060.1, REV-1, paragraph 2-25, Loan Origination Requirement, requires that mortgagees originate, close, fund, and submit mortgages for HUD/FHA insurance endorsement in their own name. Paragraph 2-14, Conducting Mortgagee Business, requires all employees, except the receptionist, whether full-time or part-time, to be employed exclusively by the mortgagee at all times.

Mortgage America's former General Manager did not comply with HUD's loan origination requirements that all loans originate and close in their own name. During the transition of Mortgage America's main office from Silver Spring to Kensington, its General Manager stopped functioning as the General Manager/Loan Officer for Mortgage America. Instead, he, along with some former Mortgage America loan officers, remained at the Silver Spring office to operate as a net branch of 1st Metropolitan Mortgage.

Senior Management Did Not Adequately Control And Supervise Its Employees

HUD Handbook 4060.1, REV-1, paragraph 2-13, Control and Supervision of Staff, requires a mortgagee to exercise control and responsible management supervision over its employees. The requirement regarding control and supervision must include, at a minimum, regular and ongoing reviews of employee performance and of work performed.

Mortgage America's management did not exercise control and supervision over its employees and did not actively participate in the loan origination process performed by its loan officers and loan processors. The only review of the loan officer's and processor's work that takes place is the completion of a standard checklist to ensure that all the necessary documents are present, signed, and dated. This review does not verify the quality or validity of the information provided in the loan file. Also, Mortgage America was unable to provide any written reviews regarding the loan officer's performance or improvements needed.

Mortgage America's failure to exercise control and responsible management over its employees prevents it from ensuring that the origination operations of its employees are in accordance with HUD/FHA practices.

Not All Employees Were Employed Exclusively By Mortgage America At All Times

HUD Handbook 4060.1, REV-1, paragraph 2-14, Conducting Mortgagee Business, requires all employees except the receptionist, whether full-time or part-time, to be employed exclusively by the mortgagee at all times.

Mortgage America did not enforce and require exclusivity of its employees as required by HUD. Review of the loan origination files documented that the branch manager of the Marlow Heights office was also an agent for Murrell, Incorporated, Realtors. Murrell, Incorporated, Realtors is located next door to the Marlow Heights branch office. Of the 22 loans we selected for review, 15 (68 percent) were originated from the Marlow Heights/Camp Springs offices. Murrell, Incorporated, Realtors was listed as the real estate agent in 6 of these 15 loans. The Marlow Heights branch manager acted as the real estate agent on two of these six loans, while the other Marlow Heights loan officer originated the loans (see Appendix E).

Mortgage America Does Not Pay All Its Own Operating Expenses

HUD Handbook 4060.1, REV-1, paragraph 2-17, Operating Expenses, specifies the mortgagee is responsible for paying all of its operating expenses. The operating expenses that must be paid by the mortgagee include but are not limited to equipment, furniture, office rent, overhead, and other similar expenses incurred in operating a mortgage lending business. Also, Mortgagee Letter 2000-15 states that if "the expenses are paid by the branch manager from a personal or non-mortgagee account (or by some third party), the arrangement is prohibited and a true branch does not exist."

Mortgage America does not pay all of its employees' operating expenses. When the Marlow Heights office was opened in 2002, the employees furnished the office. These employees personally paid for computers, telephones, a copy machine, and other office supplies. Mortgage America did not reimburse the employees for the set up of the office.

Also, the employees continue to pay general expenses such as office supplies, maintenance of the copier and computers, and the office's phone bill. When questioned about the payment of office expenses, Mortgage America stated that it pays the bills for the branch offices when it receives the bills from the loan officers. However, Mortgage America declared it is difficult to pay expenses when the officers in the respective branch offices do not submit bills to be paid. Mortgage America holds the staff responsible for submitting bills to be paid.

In addition, Mortgage America was unable to provide evidence of who was paying the lease for the Marlow Heights office space. We requested a copy of the lease agreement for the Marlow Heights office, but; Mortgage America was not able to provide us with one. Therefore, we question whether Mortgage America is paying for and/or leasing the office space for the Marlow Heights office.

Mortgage America's failure to pay all of its employees' operating expenses is a direct violation of HUD/FHA regulations. Not paying all the operating expenses creates a prohibited arrangement, and a true net branch does not exist.

Mortgage America Did Not Notify HUD Of Business Changes

HUD Handbook 4060.1, REV-1, paragraph 2-16, Office Facilities, states a mortgagee's main office must be its designated facility to which HUD directs all communications about the management affairs of the mortgagee and from which the public obtains information on the activities of the mortgagee. In addition, paragraph 2-21 specifies that mortgagees be required to notify HUD within 10 days of all corporate changes.

As discussed above, Mortgage America moved its main office from the Silver Spring location to 3930 Knowles Avenue, Suite 305, Kensington, MD, sometime in June or July 2003. However, Mortgage America failed to notify HUD of this change. By not notifying HUD of its new office location, Mortgage America's main branch in Kensington, MD is not an FHA-approved office. In addition, with no knowledge of its new office location, HUD is still directing all correspondence to an address at which Mortgage America no longer operates. Therefore, HUD is not able to accurately monitor the office activities of Mortgage America.

HUD Handbook 4060.1, REV-1, paragraph 2-16, Office Facilities, stipulates offices must be clearly labeled so that they are properly identified to the public. Mortgage America's branch office in Marlow Heights is located in a residential neighborhood. The office is located inside a detached house. The exterior of this building has no business signs to inform the public that it is either acting as a business or operating as a branch office of Mortgage America.

Mortgage America Claimed A Lack Of Knowledge Of HUD Requirements

In our opinion, the deficiencies addressed above and in Findings 2 and 3 stem from Mortgage America's disregard for or lack of knowledge of HUD requirements. Mortgage America admittedly failed to obtain the necessary understanding of HUD/FHA rules and regulations. This led to its inability to ensure the accuracy, validity, and completeness of its loan origination operations. This disregard or lack of knowledge has greatly increased the risk to the FHA insurance fund.

Auditee Comments

Except for Mortgage America's disagreement with our finding that a loan officer cannot simultaneously be employed as a real estate agent, Mortgage America generally agreed with our findings. In its response to the audit, it documented the actions it has taken to date to correct the deficiencies noted during the review. In December 2003, the General Manager was replaced. Under the new General Manager a systematic review of Mortgage America's operations and procedures was completed. A CPA was hired to assist in establishing the financial records and accounting system for the upcoming year. New contracts were issued to all loan officers and branch managers, requiring exclusivity. Leases were obtained for all offices, and bills are being collected and paid by the main Mortgage America office. In addition, all branch locations have been reported to HUD and are properly identified to the public.

Mortgage America states that there are many realtors who also are employed as loan officers in the industry. Mortgage America believes that because the loan officer/realtor did not receive a commission from Mortgage America on any loan for which they serve as the realtor, there is no violation of HUD/FHA's exclusivity rules.

OIG Evaluation of Auditee Comments

We are encouraged by the changes Mortgage America stated it has started to implement in response to the issues noted in this report. However, HUD will need to determine whether the proposed actions have been completed and are acceptable to correct the problems. Regarding the exclusivity of employees, we maintain our stance that the loan officer/realtor relationship is a violation of HUD/FHA regulations.

Recommendations

We recommend that the Assistant Secretary for Housing-Federal Housing Commissioner:

1A. Require Mortgage America to take immediate action to correct the operational deficiencies that are not in compliance with HUD/FHA loan correspondent approval requirements.

1B. Seek indemnification from Mortgage America against future losses to HUD/FHA on 13 of the 17 loans (original mortgage amounts totaling $1,878,205) originated from unauthorized offices in Marlow Heights/Camp Springs and Silver Spring.

1C. Seek reimbursement from Mortgage America to HUD/FHA for the net loss incurred by HUD (claims totaling $531,906) on the four remaining loans originated from the unauthorized offices which have already been conveyed to HUD.

1D. Seek indemnification against future losses to HUD/FHA on the four loans (original mortgage amounts totaling $573,390) originated in Mortgage America's name and/or using Mortgage America's origination identification by non-Mortgage America employees.

1E. Take administrative actions against the former General Manager of Mortgage America for continued non-compliance with HUD/FHA rules and regulations.

1F. Determine whether Mortgage America's deficiencies in its mortgagee approval requirements warrant administrative actions and/or its removal from participation in HUD's Single Family Mortgage Insurance Programs.

1G. If HUD determines Mortgage America can maintain its approval as a non-supervised loan correspondent, take appropriate monitoring measures to ensure that Mortgage America discontinues the practice of submitting loans that are originated by non-Mortgage America employees or unauthorized branches.

Mortgage America Could Not Justify Loan Discount Fees and Premium Rate Mortgages Charged to Borrowers

Mortgage America did not comply with HUD/FHA loan origination regulations. It failed to justify loan overages (loan discount fees) charged to 13 borrowers; provided premium rate mortgages without reducing the borrower's closing costs (yield spread premiums) in 14 loans; and charged a real estate commission fee to one borrower when a financial interest existed between the real estate agent and Mortgage America. In our opinion, these deficiencies are a result of Mortgage America's disregard for or lack of understanding of HUD/FHA loan origination requirements. In addition, Mortgage America did not adequately supervise its branches and employees. Consequently, FHA loans originated by Mortgage America had unnecessarily higher mortgage payments, resulting in an increased risk to the FHA insurance fund.

Mortgage America Could Not Justify Discount Fees It Charged Borrowers

The Tiered Pricing Rule, as described in 24 Code of Federal Regulations (CFR) 202.12 and HUD Mortgagee Letters 94-16 and 94-43, allows the lender to charge overages (discount fees) and retain them; however, a lender's customary lending practices may not provide for a variation in "mortgage charge rates" (discount point, origination fee and other such fees) exceeding two percentage points on its FHA-insured single family mortgages within a geographical area. Any variation within two percentage points must be based on actual variations in fees or costs to the lender to make a loan. Whenever a lender makes a variation in pricing within the two percent, the lender must provide a justification. A record of the justification must be maintained for a period of at least two years and must be made available to the Secretary of Housing and Urban Development upon demand.

Mortgage America charged borrowers overages in the form of loan discount fees in 16 of the 22 cases we reviewed. The loan discount fees were between 0.5 and 3.0 percent of the loan amount. However, we found in 13 of the 16 loans no justification was provided showing the reasons for the variations. When we asked the Operations Manager about the loan discounts, we were told that the loan discount is a way for Mortgage America to get a second origination fee. The loan discount fees in the 13 loans totaled $23,841 (see Appendix F, Chart 1).

In addition, the borrower in one case (249-4274668) was charged $3,877 or 3.75 percent of the loan amount for “services rendered.” The HUD-1 closing statement indicates this amount was “paid outside of closing” by the borrower to Mortgage America. However, we found no documentation to justify what services were “rendered” by Mortgage America for the additional fees or costs incurred in originating this loan.

These overages charged by Mortgage America totaling $27,718 were not properly supported; therefore, we consider them to be a violation of HUD/FHA regulations.

Mortgage America Provided Premium Rate Mortgages To Borrowers Without Reducing Closing Costs

Mortgagee Letter 94-7, states that premium rate mortgages (yield spread premiums), also known as “rebate pricing” mortgages, permit the borrower to pay a slightly higher interest rate in exchange for the lender paying the borrower’s closing costs. For mortgages to be insured by HUD, the funds derived from a premium interest rate must be disclosed on the “good faith estimate” and the HUD-1 settlement statement. The good faith estimate and HUD-1 settlement statement must provide an itemized statement indicating which items are being paid on the borrower’s behalf; disclosing only a lump sum is not acceptable.

We found Mortgage America provided 14 borrowers with premium rate mortgages without reducing the borrower’s closing costs. Mortgage America provided no evidence that the borrower received an up-front reduction in closing costs nor did the itemized closing statements indicate any items were paid on the borrower’s behalf. In total 19 of the 22 loans we reviewed contained yield spread premiums. In 14 of the 19 loans, the 1.0 percent loan origination fee plus an additional loan discount fee were charged in addition to the yield spread premiums. The yield spread premiums in these 14 cases totaled $52,888 and ranged from $1,031 to $6,093. The total of the loan origination fee plus the loan discount fee in these cases ranged from $1,842 to $6,007 (see Appendix F, Chart 2).

For example, in one loan for $187,468 (249-4493039), the borrower paid a loan origination fee of $1,847 and a loan discount fee of $3,749. In addition to these fees, the loan contained one yield spread premium of $6,093 and a second yield spread premium of $3,241. The total of all these fees is $14,930 or 8.0 percent of the loan amount.

Mortgage America did not provide any evidence to demonstrate the borrower actually received an up-front reduction in closing costs nor did the itemized closing statements indicate any items were paid on the borrower's behalf. Instead, it appears that the broker simply delivered a loan with a higher interest rate with no benefit being provided to the borrower. Therefore, we consider the yield spread premiums in these 14 cases, totaling $52,888, to be a violation of HUD/FHA regulations.

Borrower Paid A Prohibited Real Estate Broker's Fee

HUD Handbook 4000.2, REV-2, paragraph 5-3, subpart L, Real Estate Broker's Fees, explains that real estate broker's fees are allowable only if the broker is engaged independently by the mortgagor. It also states that these fees are prohibited if there is any financial interest between the broker and the mortgagee.

As discussed in Finding 1, the branch manager/loan officer of Mortgage America's Marlow Heights office is also employed as an agent of Murrell, Incorporated, Realtors. In one loan (249-4781170) the borrower paid a real estate commission to Murrell, Incorporated, Realtors in the amount of $8,250. This loan was originated from Mortgage America's Marlow Heights office. However, the branch manager/loan officer of this branch office acted as the agent for Murrell, Incorporated, Realtors on this loan. Due to the financial interest between the broker and the mortgagee, we consider this fee to be unallowable.

Auditee Comments

Mortgage America disagrees with our finding. In its response to the audit, it explains that charging yield spread premiums and broker discount fees on both FHA and conventional loans has been common practice for at least 20 years throughout the lending industry. Mortgage America states that the sponsoring lenders monitor each loan to ensure compliance with HUD/FHA regulations. Never has a sponsoring lender questioned Mortgage America on this practice.

OIG Evaluation of Auditee Comments

We do not dispute that charging variations (discount fees) and yield spread premiums are allowed practices. However, we maintain our stance that Mortgage America failed to provide (1) justification for the discount fees they charged and (2) reductions in the up front cash owed by the borrower or an itemized statement on either the HUD-1 settlement statement or good faith estimate showing which items were paid on the borrower's behalf in cases in which a yield spread premium was charged. We agree that the sponsoring lenders are responsible for reviewing each loan for compliance with HUD/FHA regulations; however, this does not absolve Mortgage America of its duties to comply with those regulations.

Recommendations

We recommend that the Assistant Secretary for Housing-Federal Housing Commissioner:

2A. Require Mortgage America to establish policies and procedures to ensure loans originated by its main and branch offices are in compliance with HUD/FHA loan origination regulations pertaining to tiered pricing and premium rate mortgages.

2B. Determine the eligibility of the $27,718 in overages charged by Mortgage America, which lacked adequate pricing documentation to justify such fees. If it is determined these fees are ineligible, require Mortgage America to reimburse the fees charged totaling $27,718 as follows:

- i. If the loan is current, a refund must be made to the borrowers.
- ii. If the loan is delinquent, a refund must be applied to the delinquency.
- iii. If a claim has been paid, a refund must be paid to HUD and sent to HUD Single Family Claims.

2C. Require Mortgage America to reimburse the ineligible $52,888 in yield spread premiums as follows:

- i. If the loan is current, a refund must be made to the borrowers.
- ii. If the loan is delinquent, a refund must be applied

to the delinquency.

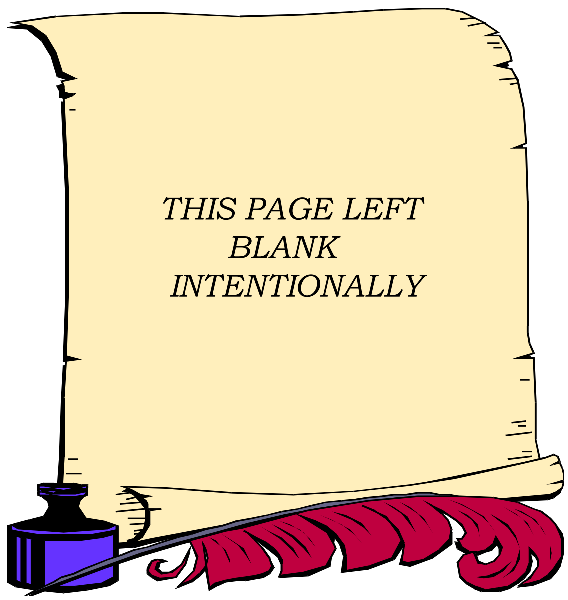
iii. If a claim has been paid, a refund must be paid to HUD and sent to HUD Single Family Claims.

2D. Require Mortgage America to reimburse the ineligible $8,250 real estate commission as follows:

i. If the loan is current, a refund must be made to the borrowers.

ii. If the loan is delinquent, a refund must be applied to the delinquency.

iii. If a claim has been paid, a refund must be paid to HUD and sent to HUD Single Family Claims.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Mortgage America's Quality Control Process Continues to Be Inadequate

Mortgage America did not adequately develop and implement a quality control plan that fully meets HUD requirements as outlined in HUD Handbook 4060.1, REV-1, chapter 6. It failed to conduct the required quality control reviews or maintain its loan origination case files for the required 2-year period. The deficiencies associated with Mortgage America's quality control plan and procedures stem from either its disregard for or lack of knowledge of HUD's and its own quality control requirements. Therefore, Mortgage America is unable to guarantee the accuracy, validity, and completeness of its loan origination operations.

Mortgage America's Quality Control Plan Does Not Meet HUD Requirements

As a condition of the HUD/FHA approval process, loan correspondents must have and maintain a quality control plan for the origination and servicing of insured mortgages. HUD Handbook 4060.1, REV-1, chapter 6, provides the general requirements along with mortgagee type specific requirements, for quality control plans. The primary objective of a quality control plan is to assure compliance with HUD/FHA requirements.

During a review conducted by the Philadelphia Homeownership Center in 2001, Mortgage America was informed that its quality control plan did not contain all of the specific elements as outlined in HUD Handbook 4060.1, REV-1, chapter 6. HUD instructed Mortgage America to update its plan to include all the required elements that pertain to loan correspondents. Mortgage America completed some of the necessary changes but not all. Thus, its quality control plan continues not to meet HUD requirements. Mortgage America's quality control plan did not include procedures to:

- Identify and review all loans that go into default within 6 months of closing,
- Require on-site branch office reviews at least once a year,
- Identify the cause of deficiencies and initiate prompt action to notify employees to correct the deficiencies, or

- Require notification to HUD of significant discrepancies.

The lack of an adequate quality control plan prevented Mortgage America from evaluating the accuracy, validity, and completeness of its loan origination operations. Therefore, potential deficiencies in the loan origination process were not identified and corrected.

Past Quality Control Reviews Were Not Adequate

In the Philadelphia Homeownership Center 2001 monitoring review, Mortgage America was unable to provide any evidence it completed quality control reviews. However, during our review Mortgage America did provide us with copies of past quality control reviews for loans it originated from January 1, 1999, through October 31, 2001. All three reviews were performed by an independent agency. Further, each of the audit summation letters that was provided to Mortgage America's management stated, "All files were given a cursory review for set-up and calculation accuracy. The information in the files was not re-verified." As such these three reviews are insufficient and do not meet the requirements of a quality control review.

HUD Handbook 4060.1, REV-1, paragraph 6-1, General, states that the quality control plan must be a prescribed function of the mortgagee's operations and assure that the mortgagee maintains compliance with HUD/FHA requirements and its own policies and procedures. Mortgage America's own quality control plan requires a "thorough analysis of the information by the quality control reviewer, as opposed to a cursory check of the existence of the various documents."

No Quality Control Reviews Have Been Completed Since October 2001

We found that Mortgage America has not completed any quality control reviews for loans originated after October 31, 2001. The failure to implement quality control procedures prevents Mortgage America from evaluating the accuracy, validity, and completeness of its loan origination operations and increases the overall risk to the FHA insurance fund.

Case Files Were Not Retained For The Required Two-Year Period

HUD Handbook 4000.2, REV-2, paragraph 5-10, Retention of Files, states the originating mortgagee must retain the entire case file pertaining to loan origination, either in hard copy or microfilm form, for at least 2 years from the date of insurance endorsement for auditing purposes. We requested that Mortgage America provide us copies of the 22 loan files we selected for review. It provided us 5 of the 22 loan files we requested. It did not retain 17 of the 22 loan origination files for the required 2 years; therefore, it was unable to ensure the loan origination process was properly documented.

Auditee Comments

Mortgage America agreed with our findings. On March 1, 2004, it hired a manager to maintain a quality control department. As part of his duties, he will ensure that all loan files (past and present) are organized and complete and that the data maintained in the files meets Mortgage America's quality control plan. In addition, he will implement a verbal/written quality control audit of 10 percent of all loans originated from January 1, 2003, to July 20, 2004, and provide monthly updates of his progress in each area, bring deficiencies to management's attention, and implement remedies. Lastly, the quality control manager will add Neighborhood Watch status checks to the quality control plan starting in September 2004 and review all loans that go into default within 6 months to determine the cause and to correct deficiencies.

OIG Evaluation of Auditee Comments

We are encouraged by the changes Mortgage America stated it has started to implement in response to the issues noted in this report. However, HUD will need to determine whether the proposed actions have been completed and are acceptable to correct the problems.

Recommendations

We recommend that the Assistant Secretary for Housing-Federal Housing Commissioner:

3A. Take appropriate monitoring measures to ensure that Mortgage America makes changes to its existing quality control plan according to HUD requirements.

3B. Require Mortgage America's senior management to implement the quality control plan. The controls should ensure that deficiencies in the loan origination process are identified and corrected before the loan packages are submitted to the direct endorsement sponsor.

3C. Require Mortgage America to take immediate action to comply with HUD's loan retention requirements.

3D. Take appropriate administrative action(s) due to the continual deficiencies and noncompliance with HUD requirements.

Management Controls

In planning and performing our audit, we considered the management controls of Mortgage America Bankers, LLC to determine the audit procedures, not to provide assurance on its management controls. Management controls include the plan of organization, methods and procedures adopted by management to ensure that its goals are met; the processes for planning, organizing, directing, and controlling program operations; and the systems for measuring, reporting, and monitoring program performance.

Relevant Management Controls

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

- Loan Origination Process - Policies and procedures that management has in place to reasonably ensure that the loan origination process complies with the HUD/FHA program requirements.

- Quality Control Plan - Policies and procedures that management has in place to reasonably ensure implementation of HUD/FHA quality control requirements.

The following audit procedures were used to evaluate the management controls:

- Review of established procedures formulated by Mortgage America in originating FHA-insured loans,

- Interviews with officials and employees of Mortgage America,

- Examination of records and related documents for FHA-insured loans originated between September 1, 2001 and September 30, 2003,

- Review of records and files maintained by HUD's Quality Assurance Division in connection with the oversight of Mortgage America, and

- Interviews with applicable officials and employees of HUD's Quality Assurance Division relating to activities associated with Mortgage America.

Significant Weaknesses

A significant weakness exists if management controls do not give 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 are obtained, maintained, and fairly disclosed in reports.

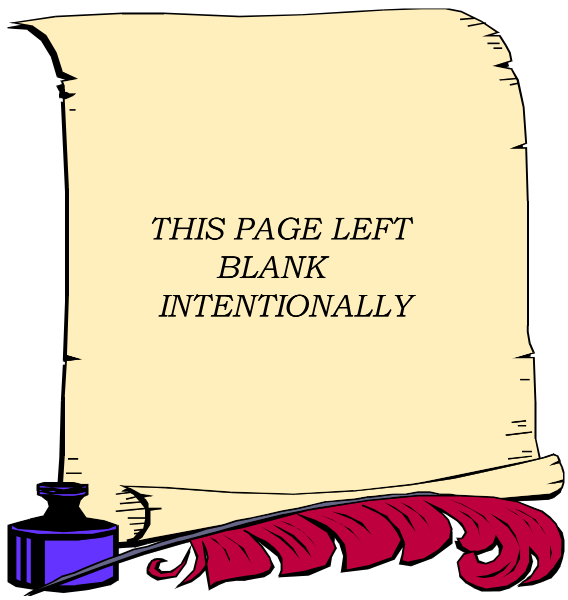
Our review of Mortgage America's management controls over its loan origination and quality control procedures for the origination of FHA-insured loans showed Mortgage America did not comply with HUD requirements. Our audit disclosed the following significant weaknesses with Mortgage America's Single Family loan program:

- Quality control process,
- Operating in accordance with HUD/FHA mortgagee approval requirements, and
- The loan origination process.

The deficiencies are discussed in detail in the findings in this report.

Follow Up On Prior Audits

This is the first audit of Mortgage America Bankers, LLC conducted by HUD's Office of the Inspector General. The mortgagee's last independent audit report for the year ending December 31, 2002, did not contain any findings.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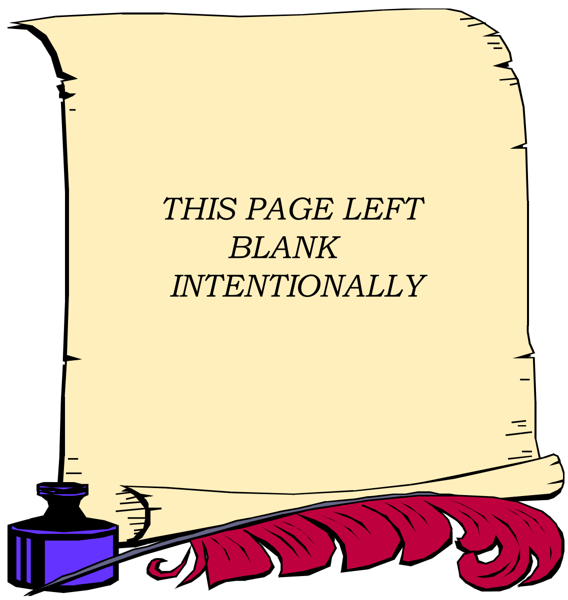
Schedule of Questioned Costs and Funds to Be Put to Better Use

Recommendation Number	Type of Questioned Cost		Funds Put to Better Use 3/
	Ineligible 1/	Unsupported 2/	
1B			$ 1,878,205
1C			$ 531,906
1D			$ 573,390
2B		$27,718	
2C	$52,888		
2D	$ 8,250		
Totals	**$61,138**	**$27,718**	**$ 2,983,501**

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 policies or regulations.

2/ Unsupported costs are costs charged to a HUD-financed or HUD-insured program or activity, and eligibility cannot be determined at the time of audit. The costs are not supported by adequate documentation or there is a need for a legal or administrative determination on the eligibility of the costs. Unsupported costs require a decision by HUD program officials. This decision, in addition to obtaining supporting documentation, might involve a legal interpretation or clarification of Departmental policies and procedures.

3/ Funds Put to Better Use are costs that will not be expended in the future if our recommendations are implemented.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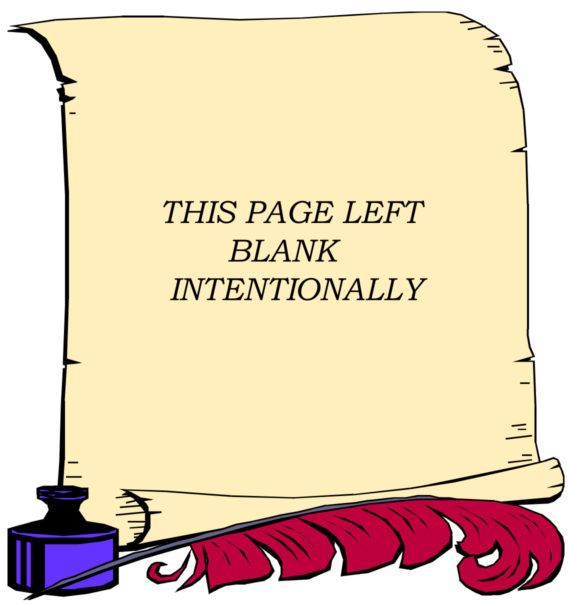
Twenty-Two FHA-Insured Loans Selected for Review

The following shows the 22 loans selected for review:

		Default Information		
Case Number	**Mortgage Amount**	**Current**	**Status Code as of 10/3/03**	**Sponsor Name**
081-0717369	$150,727.00		46	Wells Fargo
081-0724563	$144,732.00	Y	28	Wells Fargo
249-4244377	$126,308.00		20	Wells Fargo
249-4382189	$163,195.00	Y	42	Wells Fargo
249-4471936	$100,207.00	Y	68	International Mort. Corp
249-4493039	$187,468.00	Y	68	International Mort. Corp
249-4445170	$139,894.00		20	Fidelity Home Mortgage
249-4445187	$173,627.00		20	Fidelity Home Mortgage
249-4467153	$148,824.00		20	Fidelity Home Mortgage
249-4210423	$129,972.00	Y	45	Fidelity Home Mortgage
249-4274668	$103,377.00	Y	68	Fidelity Home Mortgage
081-0701658	$104,562.00		19	Fidelity Home Mortgage
081-0710298	$ 92,766.00	Y	28	Fidelity Home Mortgage
241-6581097	$124,019.00	Y	42	Fidelity Home Mortgage
249-4818445	$205,680.00	NR	NR	Wells Fargo
249-4648938	$166,320.00	NR	NR	Wells Fargo
249-4766144	$121,800.00	NR	NR	Wells Fargo
249-4781170	$103,603.00	NR	NR	Wells Fargo
249-4795770	$132,250.00	NR	NR	Wells Fargo
249-4803122	$148,824.00	NR	NR	First Mutual
249-4774857	$153,020.00	NR	NR	Wells Fargo
249-4779472	$148,824.00	NR	NR	First Mutual

Default Status	
Codes	**Descriptions**
19	Partial Reinstatement
20	Reinstated by Mortgagor
28	Modification
42	Delinquent 90 Days or More
45	Foreclosure Completed
46	Property Conveyed to Insurer
68	First Legal Action to Foreclose
NR	None Reported in Neighborhood Watch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Loan Originations at Unauthorized Offices

The following are the 4 loans originated by unauthorized offices and already conveyed to HUD:

			Default Status		Claims Paid by FHA	
Case Number	Originating Office	Loan Amount	Code	As of 3/31/04	Principal	Other
249-4471936	Camp Springs	$100,207.00	46	1/1/2004	$104,957.49	$ 8,448.16
081-0710298	Camp Springs	$ 92,766.00	46	1/1/2004	$ 96,854.02	-
249-4210423	Camp Springs	$129,972.00	46	10/1/2003	$139,057.06	$14,326.95
081-0717369	Elton Road - SS	$150,727.00	46	3/1/2003	$156,244.33	$12,018.33
	Total	**$473,672.00**		**Totals**	**$497,112.90**	**$34,793.44**

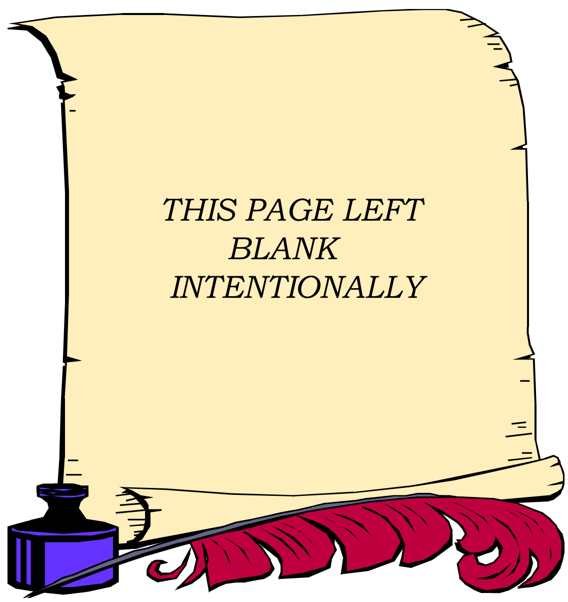
Default Status	
Codes	Description
46	Property Conveyed to Insurer

Total claims paid by FHA (rounded to the nearest dollar):

$ 497,113 - Principal
$ 34,793 - Other
$ 531,906 - Total Claims Paid by FHA

The following are the remaining 13 loans originated by unauthorized branches:

Case Number	Originating Office	Loan Amount
249-4445170	Camp Springs	$ 139,894.00
249-4274668	Camp Springs	$ 103,377.00
249-4244377	Camp Springs	$ 126,308.00
249-4382189	Camp Springs	$ 163,195.00
249-4493039	Camp Springs	$ 187,468.00
249-4445187	Camp Springs	$ 173,627.00
249-4467153	Camp Springs	$ 148,824.00
081-0701658	Camp Springs	$ 104,562.00
249-4781170	Marlow Heights	$ 103,603.00
249-4779472	Marlow Heights	$ 148,824.00
249-4818445	Marlow Heights	$ 205,680.00
249-4803122	Marlow Heights	$ 148,824.00
241-6581097	Elton Road - SS	$ 124,019.00
Total Original Loan Amounts		**$1,878,205.00**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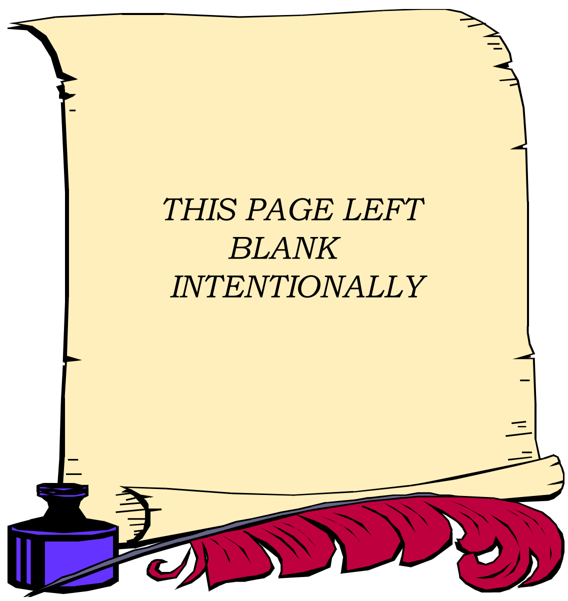
Loans Originated by Non-Mortgage America Employees

The following are the loans closed by non-Mortgage America employees:

Case Number	Originating Office	Loan Amount	Mortgagee Name Used to Close the Loan
249-4648938	1st Metropolitan	$166,320.00	1st Metropolitan Mortgage
249-4766144	1st Metropolitan	$121,800.00	1st Metropolitan Mortgage
249-4795770	1st Metropolitan	$132,250.00	Mortgage America Bankers
249-4774857	1st Metropolitan	$153,020.00	Mortgage America Bankers
	Total	**$573,390.00**	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Loans Originated at Marlow Heights/ Camp Springs Offices

The following are loans originated at Marlow Heights/Camp Springs Offices, some of which involve Murrell, Incorporated, Realtors:

Case Number	Originating Office	Loan Amount	
249-4471936	Camp Springs	$100,207.00	**M**
081-0710298	Camp Springs	$ 92,766.00	
249-4210423	Camp Springs	$129,972.00	
249-4445170	Camp Springs	$139,894.00	**M**
249-4274668	Camp Springs	$103,377.00	
249-4244377	Camp Springs	$126,308.00	
249-4382189	Camp Springs	$163,195.00	
249-4493039	Camp Springs	$187,468.00	
249-4445187	Camp Springs	$173,627.00	
249-4467153	Camp Springs	$148,824.00	**M**
081-0701658	Camp Springs	$104,562.00	
249-4781170	Marlow Heights	$103,603.00	**M,K**
249-4779472	Marlow Heights	$148,824.00	**M,K**
249-4818445	Marlow Heights	$205,680.00	
249-4803122	Marlow Heights	$148,824.00	**M**

M - Murrell, Incorporated, Realtors was the real estate broker on these loans.
K - The Marlow Heights branch manager served as the real estate broker on these loans.

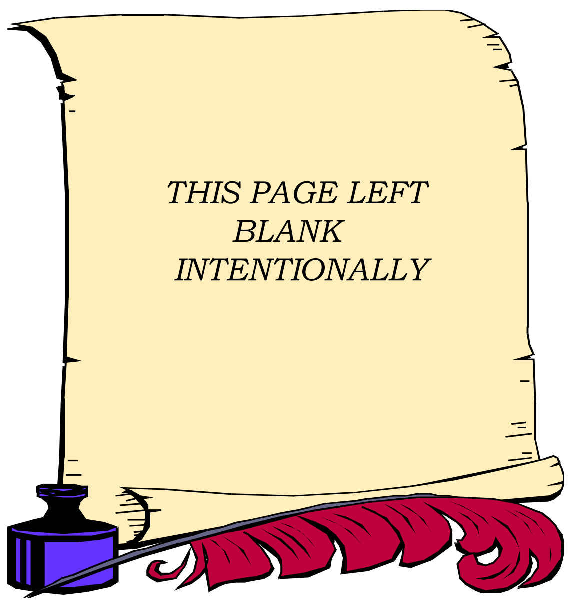
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Chart of Unearned and Unallowable Fees

Chart 1 - shows the 13 loans for which unearned discount fees were charged:

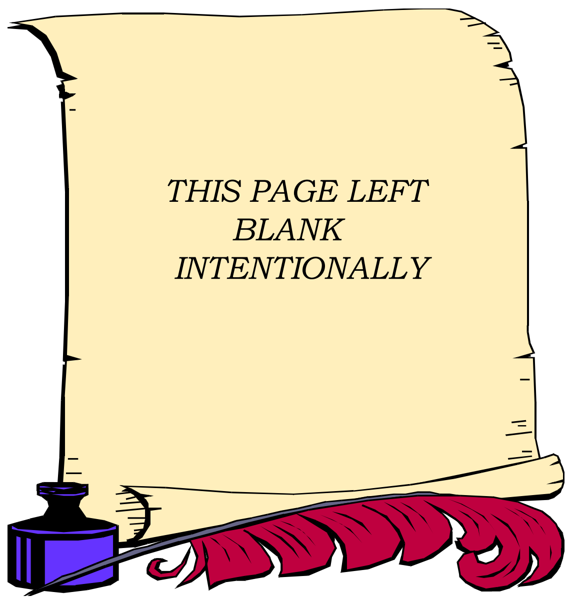
FHA Case Number	Loan Amount	Origination	Discount	% of Loan Amount
249-4471936	$100,207.00	$ 987.27	$1,252.59	1.25%
249-4445170	$139,894.00	$1,378.27	$1,049.20	0.75%
249-4274668	$103,377.00	$1,018.50	$2,067.54	2.00%
081-0710298	$ 92,766.00	$ 913.96	$ 927.66	1.00%
081-0717369	$150,727.00	$1,485.00	$4,521.81	3.00%
249-4244377	$126,308.00	$1,263.08	$2,084.08	1.65%
249-4382189	$163,195.00	$1,631.95	$1,327.79	0.81%
249-4210423	$129,972.00	$1,280.52	$2,599.44	2.00%
081-0701658	$104,562.00	$1,030.17	$2,091.24	2.00%
249-4803122	$148,824.00	$1,466.25	$ 744.12	0.50%
241-6581097	$124,019.00	$1,221.87	$1,240.19	1.00%
249-4648938	$166,320.00	$1,638.63	$2,494.80	1.50%
249-4766144	$121,800.00	$1,200.00	$1,440.89	1.18%
		Total Unearned Discount Fees	**$23,841.35**	

Chart 2 - shows the 14 loans with unearned yield spread premiums (YSP):

		Fees Charged				
FHA Case Number	**Loan Amount**	**Origination (A)**	**Discount (B)**	**Total of A+B**	**1st YSP**	**2nd YSP**
249-4471936	$ 100,207.00	$ 987.27	$ 1,252.59	$ 2,239.86	$ 2,254.66	
249-4445170	$ 139,894.00	$ 1,378.27	$ 1,049.20	$ 2,427.47	$ 1,031.02	
081-0710298	$ 92,766.00	$ 913.96	$ 927.66	$ 1,841.62	$ 2,736.60	
081-0717369	$ 150,727.00	$ 1,485.00	$ 4,521.81	$ 6,006.81	$ 1,101.81	
249-4244377	$ 126,308.00	$ 1,263.08	$ 2,084.08	$ 3,347.16	$ 3,631.36	
249-4382189	$ 163,195.00	$ 1,631.95	$ 1,327.79	$ 2,959.74	$ 5,457.24	
249-4493039	$ 187,468.00	$ 1,846.98	$ 3,749.36	$ 5,596.34	$ 6,092.71	$3,241.32
249-4210423	$ 129,972.00	$ 1,280.52	$ 2,599.44	$ 3,879.96	$ 3,545.64	
081-0701658	$ 104,562.00	$ 1,030.17	$ 2,091.24	$ 3,121.41	$ 3,245.60	
249-4803122	$ 148,824.00	$ 1,466.25	$ 744.12	$ 2,210.37	$ 5,580.40	
249-4648938	$ 166,320.00	$ 1,638.63	$ 2,494.80	$ 4,133.43	$ 3,953.43	
249-4766144	$ 121,800.00	$ 1,200.00	$ 1,440.89	$ 2,640.89	$ 2,805.05	
249-4774857	$ 153,020.00	$ 1,530.20	$ 1,147.65	$ 2,677.85	$ 3,352.67	
081-0724563	$ 144,732.00	$ 1,425.94	$ 519.59	$ 1,945.53	$ 4,858.65	
Totals	**$1,929,795.00**	**$19,078.22**	**$25,950.22**	**$45,028.44**	**$49,646.84**	**$3,241.32**

Total Unearned Yield Spread Premiums (rounded to the nearest dollar):

$ 49,647 - 1st unearned yield spread premium
$ 3,241 - 2nd unearned yield spread premium
$ 52,888 - Total unearned yield spread premiums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Auditee Comments

MORTGAGE AMERICA BANKERS, LLC
3930 KNOWLES AVENUE, #305
KENSINGTON, MD 20895

July 21, 2004

U.S. Department of HUD
Wanamaker Building, Suite 1005
100 Penn Square East
Philadelphia, PA 19107-3380

ATTN: Daniel G. Temme
Regional Inspector General for Audit

REF: Draft Audit Report of 6/25/04

At the time of the entrance conference the week of October 20, 2003, Mortgage America Bankers, LLC (MAB) was under the full operating control, per its Operating Agreement, of its general manager, Robert D. Koontz. Mr. Robert D. Koontz is the father of MAB's two member-owners, Kaptain D. Koontz (91% member-owner) and Khristopher D. Koontz (9% member-owner).

Robert D. Koontz has been the General Manager of MAB since its inception in May of 1996, and has had sole authority to sign checks on MAB's account at Suntrust Bank's Silver Spring branch since its inception. Kaptain and Khristopher Koontz became member-owners in early 1998.

After multiple meetings with the Inspector General's (IG) auditors, it became apparent Robert Koontz had operated MAB in a manner seriously out of compliance with HUD-FHA requirements as prescribed in the Mortgage Approval Handbook 4060.1 Rev-1; particularly in the areas of approved office locations, supervision of branches and employees, quality control and recordkeeping.

Based on these meetings, Kaptain D. Koontz on December 20, 2003, removed Robert D. Koontz as general manager and took control of MAB's bank accounts and the day-to-day management of MAB as General Manager. (see attached letter)

Beginning in January 2004, Kaptain Koontz began a systematic review of all MAB's operations and procedures, along with a systematic effort to collect all records from all branches, including hiring a moving van.

A CPA was hired in early January 2004 to supervise the establishment of MAB's financial records and accounting systems for the coming year.

New contracts were issued for all branch managers and all loan officers with an exclusivity requirement along with MAB's employee handbook for their signature. All other employees were issued the employee handbook for their signature.

All leases were obtained and all offices were found to be properly leased to MAB. All bills for all branches are now collected by and paid by MAB at its main office (3930 Knowles Avenue, #305) from its new Suntrust Bank account opened in early January 2004 as part of the financial system instituted with the CPA's advice, and in conformity with HUD guidelines for a true net branch system.

Starting in early March, MAB instituted regular monthly meetings with all branch managers to explain their contracts and MAB's policies and procedures for originating, processing, and quality control. The General Manager and the Operations Manager visited both branches during March and April of this year.

On March 1, 2004, MAB hired Khristopher Koontz (9% owner-member) to establish and manage a quality control department. His responsibilities are to:

1) Organize all loan files obtained from MAB's branches both past and present;

2) Review all files for both their completeness and quality of documentation as outlined in MAB's quality control program;

3) Provide a list of docs required in order to review all files, incomplete files to be documented and forwarded to management;

4) Obtain all loan computer data files and create a database of all loans originated from January 2003 to present with the following information fields:

- Borrower name and address with phone numbers
- LTV/loan amount and type of loan
- Lender name and loan officer/branch
- Processor name and QC status (including pre and post settlement file review, as well as verbal and/or written QC audit)
- Dates of application and closing/denial.

5) Implementation of a verbal/written QC audit of 10 percent of all loans originated from 1/1//03 to 7/30/04 with additional audits if any manager or loan officer did not have one of their loans audited;

6) Provide monthly updates of progress in each area above with all deficient files brought to management attention. Review progress reports and deficiencies at monthly meetings of branch managers with management to address all areas of deficiency and implement remedies;

7) Add to the QC plan: neighborhood watch as a monthly status check on all MAB originations, semi-annual branch office reviews starting September 2004, review all loans that go into default within six months of closing, identify cause of and prompt notice of employees to correct deficiencies and notify HUD of significant discrepancies.

In April 2004, an auditor was hired for the annual FHA audit and the 2003 tax returns. This late start was due to delays in obtaining all 2003 banking and other records along with the 2003 Quickbooks accounting program from the former general manager.

The relocation of MAB's main office to the Kensington, Md. address was reported to FHA in our annual FHA Recertification along with our fee. The Silver Spring and Marlow Heights offices were told not to originate any FHA loans from their branch offices. The Marlow Heights office now has a sign.

The four loans originated by non-MAB employees occurred in the previous 16th Street office during July and August of 2003 when this office was run by Robert D. Koontz as a First Metropolitan net branch, and he is responsible for the misuse of MAB's FHA ID number. MAB relocated to its present office at 3930 Knowles Avenue on July 1, 2003, and had no information about these loans until advised of them by the IG's auditors. Robert D. Koontz continued as General Manager with sole signature authority on MAB's business account until the attached letter of December 20, 2003. Robert D. Koontz continued to demand all branches to provide him with all their closed loan files until January 2004.

MAB requires all branch loan files to be submitted to MAB at its main office when first submitted for underwriting to allow for pre-closing review and random verbal audits; a copy of all loan conditions with closed loan HUD-1 or denial, and the computer data file for all loans.

In reference to Finding 2: MAB's failure to justify loan overages and premium rate mortgages:

Mortgage brokers charging loan origination fees along with discount and/or yield spread premiums has been common practice for at least 20 years on both conventional and FHA loans.

All of MAB's correspondent lenders/sponsors have required preliminary HUD-1s showing these fees, required MAB to submit a final fee sheet again showing all fees after locking in the rate with or without a yield spread premium. Never has an underwriter or closer with any correspondent lender/sponsor questioned this practice. The same lenders have continually monitored all of our loans for compliance with HUD/FHA regulations. This monitoring has been accompanied by periodic notices of changes in the regulations and laws governing how loans must be processed for submission and what is not acceptable.

No correspondent lender/sponsor has ever requested a justification of loan discount fees or that a yield spread premium was to provide a benefit to the borrower by reducing the borrower's closing costs.

A November 21, 2003, NEWSFLASH from Wells Fargo Wholesale Lending (attached) states, "Brokers may charge a discount on government loans closed in their or WFHM's name…" and concludes in bold letters, "If a broker charges a discount on an FHA or VA loan, it must be clearly labeled as 'broker discount' or 'discount points to broker' on the HUD-1." The only mention of lowering the rate is when Wells Fargo charges the discount point, and Wells Fargo is explicitly acknowledging broker discounts as not lowering the rate but as part of the total broker compensation cap computation.

This is the first notice MAB has received from any of its correspondent lenders/sponsors in reference to FHA discount points, and the notice clearly contradicts Finding 2. and it does not even mention above par = yield spread premiums except to state they are counted in the price and broker compensation cap – nothing about reducing borrower's closing costs.

In fact, the NEWSFLASH explicitly counts all loan origination, discount and yield spread premiums as components of the broker's fee income and nothing more or less, as it has always been treated.

Attached is MAB's broker fee sheet with Arlington Capital in which MAB charged a 2.5% origination with a 1.5% yield spread. Arlington Capital put a portion of the origination as discount on the 6/30/04 HUD-1. (attached)

Therefore, MAB respectfully disagrees with the auditor's conclusion MAB should return any discount or yield spread premium fees.

Case #249-4274668 – Services Rendered

Auditor states borrower was charged $3877 / 3.75% and that the HUD-1 indicates this amount was paid outside of closing (POC) by the borrower to MAB.

A careful examination of the HUD-1 reveals line 905- Services Rendered transposes MAB's name into America Mortgage B. This fee is the yield spread premium, not a fee paid by the borrower. Some title companies use this term for yield spread premium. Mr. Lewis M. Smith, Jr., purchased this property with seller paid closing, a charitable gift, and a broker credit of $789.69 from MAB. Mr. Smith did not personally pay MAB any direct fee POC.

Case #249-4493039

Auditor states borrower paid a loan origination and discount fee along with two (2) yield spread premiums (YSP). The second YSP was received by International Mortgage Corporation, not MAB. Again, this is a common practice for a wholesale lender/sponsor to pay a portion of the total market yield spread premium to the broker while keeping the balance of the YSP as their income. The second YSP was not on the HUD-1, but in the notes of the lender/sponsor's file. Here again, the lender/sponsor knew all of MAB's fees and never raised any questions.

Case #249-4781170 - Unallowed Fee

The auditor states a real estate commission paid to Murrell, Inc., in the amount of $8250, should be refunded by MAB when MAB did not receive the real estate commission because MAB's branch manager, who is also a licensed real estate agent, acted as the real estate agent in this transaction, and referred the loan to his co-branch manager.

The branch manager disclosed in writing his position with MAB as part of the real estate contract. MAB's loan officer was paid a commission for the loan and the branch manager functioning as a realtor was paid a real estate commission by Murrell, Inc. Realtors. MAB did not pay the branch manager for the loan, only the loan officer.

On Wednesday July 21, 2004 MAB's Operations Manager, Stuart S. Feinberg, spoke with two (2) underwriters in reference to the auditors' understanding the real estate commission was un-allowable. Both, Helen Glass- FHA underwriter with Wells Fargo Home Mortgage / Mclean, Va branch and Eileen Gernet- Head Underwriter and Director of Wholesale for Arlington Capital in Cherry Hill, NJ both understood the regulations to require the Realtor / Loan Officer to disclose his relationships, and that he could perform and be paid for only one of the functions in any transaction. In the twenty (20) year experience of Mr. Feinberg this is what he has been told consistently by all lenders. There are many Realtor / Loan officers in the industry. The key has always been to wear only one hat at a time. In this case Murrell, Inc and MAB have no financial interest in each other except the normal one in a realtor – lender relationship: to get a property with its loan to the settlement table.

In an extended conversation between Mr. Feinberg and Ms. Gernet, it was the opinion of Ms. Gernet the auditors mis-interpreted the Mortgagee Letters 94-16 & 94-7, and she agreed with Wells Fargo's view of the discount points and that yield spread premiums were additional compensation to the broker as disclosed on the Good Faith Estimate (GFE). Chase Home Mortgage also makes the same stipulation to disclose the yield spread on the GFE, and says nothing more about the matter in its loan approval stipulation sheet.

In conclusion, since January 2004 MAB has made every possible effort to bring all aspects of its operations, procedures, record keeping, accounting, branch and employee supervision, processing and quality control into compliance with its HUD-FHA approval requirements. MAB has spent considerable time and effort in addition to over $20,000 in legal, accounting and audit fees in addition to hiring a QC manager and an assistant to the QC manager.

MAB does not believe it should be required to refund any fees it has collected, nor indemnify for loans originated under the previous General Manager, Robert D Koontz.

I hope this response to the draft audit report of June 25, 2004 is both complete and adequate for MAB to continue to originate FHA loans as an approved non-supervised loan correspondent.

Sincerely,

Kaptain D. Koontz,
President / 91% Member-Owner