



Issue Date November 22, 2004
Audit Case Number 2005-LA-1803

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

Joan S. Hobbs

FROM: Joan S. Hobbs, Regional Inspector General for Audit, 9DGA

SUBJECT: Wachovia Mortgage Corporation
Direct Endorsement Mortgagee
4343 North Scottsdale Rd.
Scottsdale, AZ 85251

We completed a limited review of Wachovia Mortgage Corporation (Wachovia), a Direct Endorsement mortgagee. The review was performed on one of the mortgagee's branch offices in Scottsdale, Arizona. We selected this branch office for review based on the results of a previous OIG audit that identified the use of false credit and employment documents by Keystone Mortgage, a loan correspondent of Wachovia. The review objective was to determine whether there were fraud indicators in the 27 Keystone Mortgage loan files underwritten by Wachovia, and if so, whether these indicators were identified and resolved during Wachovia's underwriting process. We conducted the review in accordance with generally accepted government auditing standards.

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 120 days after report issuance for any recommendation without a management decision. Also, please furnish us copies of any correspondence or directives issued because of the review.

If you have any questions, please contact me at (213) 894-8016, or Charles Johnson, Assistant Regional Inspector General for Audit, at (602) 379-7243.

SUMMARY

We reviewed a sample of 27 FHA loans and found Wachovia failed to identify and/or follow up on indicators of false credit and/or employment documents during the underwriting process for all 27 cases. As a result, loans were approved based on false information, causing FHA/HUD to assume unnecessary insurance risks. This report recommends that Wachovia indemnify HUD for any past or future losses on 25 of these 27 loans.

We discussed the findings with Wachovia officials during the audit and at an exit conference held on October 28, 2004. We also provided Wachovia with a copy of the final draft audit report for comments on October 29, 2004. We received their written response on November 15, 2004. Their response and our evaluation are discussed in the finding, and the full text of their response is included as Appendix D.

BACKGROUND

Wachovia is a HUD-approved, non-supervised Direct Endorsement lender. According to information in HUD's Neighborhood Watch system, Wachovia has 27 active branch offices throughout the country, and is an approved sponsor for 1,671 loan correspondents. Our review focused on one of Wachovia's branch offices located at 4343 North Scottsdale Road, Scottsdale, AZ 85251. For the two-year period including July 2002 through June 2004, this office originated 408 loans for mortgage amounts totaling approximately \$50 million. According to Wachovia, this branch office is a wholesale lender, and therefore does not originate loans, but acts as the underwriter for loans originated by its loan correspondents.

During a previous HUD-OIG audit of Keystone Mortgage, a loan correspondent of Wachovia, we identified the use of false credit and employment documents within 48 FHA loan files, including falsified credit reports, false credit history letters from utility companies, and/or falsified employment documents, such as pay stubs, W-2s, and verification of employment (VOE) forms. Wachovia performed the underwriting on 27 of these 48 loans as the sponsoring Direct Endorsement mortgagee. We analyzed the underwriting of these 27 loans during our review of Wachovia.

We performed our review during the period July 2004 through August 2004. The objective of our review was to determine whether there were fraud indicators in the 27 Keystone Mortgage loan files underwritten by Wachovia, and if so, whether these indicators were identified and resolved during Wachovia's underwriting process.

To accomplish our review objectives, we:

- Reviewed 27 FHA insured loans underwritten by Wachovia during the period January 2002 through August 2003. This included review of both the available FHA official case files and Wachovia's related loan processing files; and
- Interviewed Wachovia managers.

FINDING

WACHOVIA FAILED TO IDENTIFY AND/OR RESOLVE INDICATORS OF FALSE CREDIT AND EMPLOYMENT DOCUMENTS WHEN UNDERWRITING FHA LOANS

All 27 of the loans reviewed, totaling approximately \$2.9 million, contained indicators of false credit and/or employment documents that were not appropriately identified and/or resolved by Wachovia during the underwriting process. This occurred because Wachovia failed to exercise due diligence when underwriting the loans, i.e., Wachovia did not identify and follow up on indicators of irregularities that were present in the files. As a result, loans were approved based on false information, causing FHA/HUD to assume unnecessary insurance risks. Three of these 27 loans have resulted in mortgage insurance claims to HUD/FHA totaling \$341,479. The 24 other loans, totaling \$2,549,250 remain insured and represent a continuing insurance risk to FHA.

Section 203 (b) (1) of the National Housing Act, as amended, authorizes HUD to provide mortgage insurance for single-family homes. A mortgagee that originates, purchases, holds or sells FHA insured loans must be formally approved by HUD. Mortgagees must follow the requirements of the National Housing Act and HUD instructions, guidelines, and regulations when originating insured loans. Mortgagees that do not follow these requirements are subject to administrative sanctions.

As part of the loan origination process, mortgagees are required to obtain a credit report for each borrower. The credit report is used as a guide in the underwriting process to evaluate the borrower's attitude toward credit obligations. If the credit report shows the borrower has made payments on previous or current obligations in a timely manner, the underwriter will find the borrower represents a reduced risk. If the borrower has not yet established a credit history with traditional credit accounts, such as credit cards, car loans or mortgages, the mortgagee can develop an "alternative" credit history using utility payment records, rental payments, automobile insurance payments, or other similar non-traditional credit sources. The mortgagee itself may obtain this alternative credit information, or the mortgagee may elect to use a credit-reporting agency to develop and provide a non-traditional mortgage credit report (reference HUD Handbook 4155.1 REV-5, Mortgage Credit Analysis for Mortgage Insurance on One-to-Four Family Properties).

The mortgagee must also obtain documentation evidencing the borrower's history of employment and income. The anticipated amount of income and likelihood of its continuance must be established to determine the borrower's capacity to repay the mortgage debt.

The underwriter's evaluation of a borrower's credit and income history is used as a basis for determining if the borrower represents an acceptable credit risk under HUD guidelines, and accordingly, whether or not the loan should be approved.

HUD Handbook 4000.4, REV-1 (Single Family Direct Endorsement Program), requires mortgagees to develop HUD/FHA insured loans in accordance with accepted sound mortgage

lending practices, ethics and standards. This handbook states that mortgagees and their underwriters must maintain the ability to detect fraud and be aware of the warning signs that may indicate irregularities.

Wachovia did not adhere to these requirements when it failed to identify and/or appropriately resolve questionable credit and employment documents when underwriting FHA-insured loans.

We reviewed 27 FHA insured loans underwritten by Wachovia. These loans were found to contain falsified borrower credit (26 loans) and/or employment (20 loans) documents during a previous audit of Wachovia's loan correspondent Keystone Mortgage. False credit and employment documents included falsified credit reports, fabricated or altered IRS W-2 forms, borrower pay stubs, and verification of employment forms. In many of the loan files involving false employment, the borrower's income or length of employment was overstated. In other cases, the borrower never worked for the purported employer, or the borrower worked as a contract laborer rather than as a full time employee as claimed. Also, in many cases, the Social Security numbers used to obtain a credit report for the borrowers and process the loan were invalid or did not belong to the borrowers (17 loans). The falsified documents in Wachovia's files were apparently intended to enhance the appearance of the borrower's credit and employment history, and thereby unduly influence the loan underwriting process in order to obtain loan approval.

All of the 27 loan files we reviewed contained indications of false borrower credit (26 loans) and/or employment documents (20 loans), yet Wachovia did not follow up to ensure the documents were legitimate. For example, the following indicators of false borrower credit and employment documents were present in the loan files, but not identified and/or resolved by Wachovia.

- Borrower pay statements and IRS W-2 forms did not reflect the standard Social Security and Medicare withholding percentages (20 loans).
- Year-to-date pay and withholding amounts on borrowers' consecutive pay stubs were incorrectly calculated (11 loans).
- Employment documents appeared to have been "cut-and-pasted" together (10 loans).
- Borrower credit reports in nearly all of the loan files contained references to alternative credit sources such as electric, gas, and cable television companies, yet the reports did not show any contact information to identify the credit sources, such as a telephone number or address as is typically included on a credit report (26 loans).
- Credit reports did not indicate alternative credit accounts were actually verified by the credit reporting agency (23 Loans).
- Credit reports listed alternative credit accounts, yet the creditor names were not shown on the reports. For example, the credit reports in these cases listed only "cable bill" or "CXDSCLR" (9 Loans).

- Alternative credit accounts for utilities at the borrower's prior residence showed dates that were clearly not consistent with the dates the borrower purportedly lived at the residence indicating these accounts were likely not valid (19 loans).
- Other miscellaneous discrepancies indicating credit and/or employment documents were potentially false (25 Loans) (see Appendix C for a discussion of these discrepancies).

The indicators of false borrower credit and employment documents found in the 27 loan files are summarized in Appendix B of this report. Each of the indicators noted represent significant discrepancies and taken as a whole within each of the loan files, the indicators presented a pattern of discrepancies that Wachovia should have identified and resolved. Because Wachovia failed to exercise due diligence and follow up on these indicators, loans were approved based on false information, causing FHA/HUD to assume unnecessary insurance risks on the 27 loans totaling approximately \$2.9 million.

AUDITEE COMMENTS

Wachovia provided a written response to the draft report dated November 12, 2004. Wachovia acknowledged it failed to identify fraud indicators in 25 of the 27 loans identified in Appendix B of the audit report and agreed to indemnification for these cases. For the remaining two loans (identified as #19 and #10 in Appendix B), Wachovia requested that OIG drop its recommendation for indemnification noting that these loans have never been in default and the cited deficiencies related to them were debatable. Wachovia also noted HUD guidelines at the time the 27 subject loans were originated did not require re-verification of borrowers alternative credit information and thus they relied on the accuracy and validity of the information provided by the credit reporting agency. Therefore, they felt that the three credit report related fraud indicators listed in the report should not be cited as indicators of false documents Wachovia failed to identify.

OIG EVALUATION OF AUDITEE COMMENTS

Since Wachovia agreed to indemnification for 25 of the 27 loans we concur this is an appropriate resolution to the audit report finding and have revised our recommendation accordingly.

Wachovia's response stated HUD guidelines at the time the subject loans were originated did not require re-verification of borrowers' alternative credit information. However, the audit report did not state mortgagees were required to re-verify alternative credit accounts in all cases, but rather that Wachovia should have identified and resolved the specific (credit related) fraud indicators noted in the audit report that were present in the loan files. This should have been done whether or not specific alternative credit re-verification requirements existed.

RECOMMENDATIONS

We recommend the Assistant Secretary for Housing require Wachovia to:

- 1A. Indemnify HUD/FHA for any losses already incurred, and future losses on the 25 loans identified in Appendix B.

FOLLOW-UP ON PRIOR AUDITS

This is the first Office of Inspector General review of the Wachovia branch office.

SCHEDULE OF QUESTIONED COSTS AND FUNDS PUT TO BETTER USE

<u>Recommendation Number</u>	<u>Type of Questioned Cost</u>		<u>Funds Put to Better Use 3/</u>
	<u>Ineligible 1/</u>	<u>Unsupported 2/</u>	
1A	\$38,172	\$112,092	\$2,331,795

- 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 future 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.

FRAUD INDICATORS NOT RESOLVED BY WACHOVIA

Loan #	Original Mortgage Amount	FHA Case Number	False Employment Documents ³	False Credit Documents ³	False Social Security Number ³	Employment Documents Did Not Reflect Standard Withholding Percentages	Year-to-Date Pay and/or Withholding Amounts Were Not Properly Computed	Employment Documents Appeared Questionable or "Cut-and-pasted"	Creditor Contact Information Was Not Shown on the Credit Report	Credit Report Did Not Indicate Alternative Credit Accounts Were Actually Verified	Creditor Name Was Not Shown on the Credit Report	Opening Date for Gas or Electric Accounts Did Not Agree to Dates Borrower Lived at the Address	Other Indicators of False Credit or Employment Documents ⁴
1	104,362	023-1212351	X	X	X	X			X	X			X
2	114,326	023-1135867		X	X				X	X	X	X	X
3	104,362	023-1158658	X	X		X	X		X	X			
4	102,393	023-1422221	X	X	X	X	X	X	X	X		X	X
5	88,609	023-1449511	X	X	X	X	X		X	X		X	X
6	86,640	023-1162407	X	X		X			X	X	X	X	X
7	97,470	023-1394193	X	X	X	X		X	X	X		X	X
8	105,346	023-0986059	X	X	X	X	X		X	X			X
9	105,346	023-1166018 ¹	X	X		X		X	X	X	X		X
10	99,113	023-1198339 ⁵		X	X				X	X	X	X	X
11	120,115	023-0846990	X	X		X	X	X	X	X		X	X
12	128,612	023-0925095	X	X	X	X	X		X	X	X	X	X
13	107,539	023-1244013	X	X		X		X	X	X		X	X
14	122,459	023-1189366	X	X	X	X			X	X	X	X	X
15	103,870	023-1262597 ²	X	X		X	X	X	X	X	X		X
16	97,470	023-1270801	X	X		X	X		X	X	X	X	X
17	87,132	023-1449382	X	X		X	X	X	X	X		X	X
18	106,915	023-1126416		X	X				X	X	X		X
19	118,342	023-1711787 ⁵		X					X			X	
20	120,115	023-1721472	X	X	X	X		X	X			X	X
21	100,424	023-1557814	X	X	X	X	X		X	X		X	X
22	112,140	023-1730711		X	X				X	X		X	X
23	114,527	023-1611235	X	X	X	X	X	X	X	X		X	X
24	99,439	023-1620555		X	X				X	X		X	X
25	93,335	023-1731609	X	X	X	X			X			X	X
26	118,065	023-0924984		X	X				X	X			X
27	113,739	023-0927038 ²	X			X		X					X
TOTAL:	2,872,205		20	26	17	20	11	10	26	23	9	19	25

- 1 Foreclosure claim totaling \$112,092 was paid by HUD. The property has not yet been resold.
- 2 Properties foreclosed, conveyed to HUD, and resold by HUD. Loss amounts for these 2 loans totaled \$38,172.
- 3 Indicates false employment, credit, or Social Security numbers were found during the previous HUD OIG audit of Wachovia's loan correspondent Keystone Mortgage.
- 4 Other indicators of false credit and employment documents are explained in Appendix C.
- 5 Loans excluded from the audit report recommendation for indemnification (two cases). Wachovia agreed to indemnify the remaining 25 loans.

SCHEDULE OF “OTHER” FRAUD INDICATORS**Loan Number 1**

Credit→ Credit reports in the loan file indicated the borrowers might own a retail business; however, this was not addressed in the loan file. This is an indication the borrowers' employment was false, or that the borrowers were inappropriately using Social Security numbers assigned to others (i.e., the business owner). A credit report in Wachovia's loan file for the co-borrower listed a landlord account; however, the credit reports found in the FHA loan file showed this account was removed from the co-borrower's credit report and added to the borrower's credit report without explanation. The credit reports indicated the borrowers Social Security numbers were issued between 1987 and 1989 and between 1991 and 1993, approximately 10 to 14 years prior to the loan. However, the borrowers apparently did not have any driver licenses or ID cards issued in the United States, because Mexican government identification cards were included in the loan file. Unexplained name variations for the borrowers were shown on the credit reports and on an identification card in the file from the Mexican government. The loan application indicated the co-borrower was 24 years old, yet a credit report shows a birth date in 1958, indicating that he would have been over 40 years old at the time of the loan application. The signature shown on the borrower's Social Security card does not even resemble the borrower's signature shown throughout the loan file. Also, the co-borrower's Social Security card was not signed.

Loan Number 2

Credit→ The credit report listed multiple last names for both the borrower and co-borrower, indicating possible use of false Social Security numbers, yet this was not explained in the loan file. Wachovia's loan file included an IRS form W-9 (taxpayer ID number request); however, the borrower's full signature was not included on the form.

Loan Number 4

Credit→ The borrower's credit report indicated the borrower might own a retail business. However, this was not addressed in the loan file. The borrower's credit report was run using an incorrect residence address for the borrower. Instead, the address of Keystone Mortgage (Wachovia's loan correspondent) was shown in place of the borrower's address. The credit report for the co-borrower indicated eleven inquiries were made related to his Social Security number. However, no inquiries were made related to his address, indicating the co-borrower may have inappropriately used a Social Security number belonging to an individual living at a different address. A separate credit report in Wachovia's loan file from a different credit reporting service contained a warning stating "INPUT SOCIAL SECURITY NUMBER NOT ISSUED AS OF 09/02" indicating the borrower was using a false Social Security number.

Loan Number 5

Employment → The written verification of employment in the file was an extremely poor copy and information on the form was not legible. The sections on the verification of employment form for the borrower's current year-to-date and prior years earnings were blank. Although the verification of employment form was not clear, it appeared to show the borrower was paid monthly, yet the pay stubs indicate the borrower was paid on a weekly basis.

Credit → The "date reported" and "date of last activity" shown on the credit report for the alternative credit accounts was December 2002, yet this date is after the date the credit report was ordered and completed, October 17, 2002.

Loan Number 6

Employment → The "rate" and "hours" sections of the pay stubs showed inconsistent and apparently extraneous amounts that do not compute to the total pay amounts shown. The text on two of the three pay stubs in the file was significantly blurred and it appears some of the numbers on the stubs may have been altered using a pen or pencil.

Credit → The address shown for the borrower on the credit report does not match the address shown on the W-2 forms for the prior two years, or the address shown on the borrower's State of Arizona identification card.

Loan Number 7

Credit → The loan application indicated the borrower was 32 years old; however, the borrower's birth date shown on the credit report indicated the borrower was 28-29 years old. This is an indication the Social Security number used may not belong to the borrower.

Loan Number 8

Credit → The credit report indicated seven inquiries were made related to the borrower's Social Security number; however, zero inquiries were made related to the borrower's address, indicating the borrower may be inappropriately using the Social Security number of someone living at a different address. A Social Security card for the borrower in the loan file appeared questionable. The borrower's full name and Social Security number on the card were not legible.

Loan Number 9

Employment → The file contained several inconsistencies related to the employer's name. For example, a loan application in Wachovia's file, the loan application in the FHA file, and a verbal verification of employment form each showed a different company name for the borrower's employer. The written verification of employment did not list the employer's name but rather was addressed to "operations".

Credit → The borrower's address was not shown on the credit report. Instead, the address of Keystone Mortgage (Wachovia's loan correspondent) was shown in place of the borrower's address. The Social Security number shown on the credit report in the FHA loan file did not match the Social Security number shown on the loan application.

Loan Number 10

Credit → The loan application indicated the borrower had lived at his current address for the prior seven years. However, data from the three credit bureaus (Experian, TransUnion, and Equifax) shown on the report indicated a completely different address for the borrower. This is an indication the Social Security number used for the borrower may actually have belonged to someone living at a different address. A resident alien card in the loan file indicated the borrower's name was spelled differently than the name used throughout the loan file.

Loan Number 11

Credit → The credit report states "none" for inquiries and lists no credit trade lines open; however, the list of creditor contact information at the end of the report includes 44 creditor addresses. This is an indication information about prior inquiries or accounts may have been excluded from the report. Due to the large number of creditors listed, this should have been resolved and explained in the loan file.

Loan Number 12

Employment → A loan application in Wachovia's file dated May 17, 2001, only listed one employer for the borrower, yet a subsequent application dated January 23, 2002, in the FHA file showed a second current employer (start date April 16, 2000) and one prior employer. A year 2000 W-2 form and pay stubs for November 2001 listed the property being purchased as the borrower's address; however, the loan applications in Wachovia's file and the FHA file indicated the borrower had never lived at this address.

Credit → The credit report did not list the borrower's current address. Instead, it listed the property being purchased as the borrower's address.

Loan Number 13

Employment → The file did not contain a written verification of employment for the co-borrower's prior employer, and accordingly, a full 2 years of employment was not verified. The pay stubs did not show the co-borrower's name (or any name).

Credit → The address listed on the borrower's bank statement was different than the address listed on the final and preliminary loan application and credit report. The credit report contained an alert stating the borrower's address and surname did not match those on file.

Loan Number 14

Credit → The borrower's address shown on the credit report did not match the address listed on the loan application. The credit report indicated six inquiries were made related to the borrower's Social Security number; however, only one inquiry was made related to the borrower's address, indicating the borrower may have been inappropriately using the Social Security number of someone living at a different address. The loan file indicated the borrower was living at his current address for the prior four years, and the credit report indicated the borrower's Social Security number was issued five to six years earlier. However, the only form of identification used for the borrower in the file was an ID card apparently issued by the Mexican government. Also, the report indicated the borrower used two other slightly different Social Security numbers. The ID card found in the file for the borrower was such a poor copy that most of it was not legible. The credit report indicated the borrower was associated with a retail business, yet this was not explained in the loan file.

Loan Number 15

Employment → The borrower's claimed employer appeared to be a local restaurant; however, the check numbers on the borrower's consecutive pay stubs dated November 27 and November 15 contain an unusually large gap of 57,101 checks. The loan application in Wachovia's files dated October 18, 2002, showed the borrower's monthly income as \$1,300, yet the loan application in the FHA file dated December 20, 2002, showed the borrower's monthly income as \$2,457.

Loan Number 16

Employment → The pay stub for the period ending September 14, 2002, noted the borrower's address had been changed, yet the same address was shown as on the previous stub.

Credit → The credit report showed a paid collection account for a "Southwest Gas" account opened in January 2001, yet it also listed a Southwest Gas alternative credit account opened in March 1999, running through September 2002, with no late payments reported.

Loan Number 17

Employment → The last pay stub for 2002 was a heavily blurred copy, while the subsequent paycheck in the following year was not. This appears to be intentional since the year-to-date amount shown on the last pay stub for 2002 did not match the amount shown on the 2002 W-2 from this same employer.

Loan Number 18

Credit → The credit report noted six inquiries were made related to the borrower's Social Security number, yet none were made for the borrower's address, indicating the borrower could have been using a Social Security number that belonged to someone living at a different address.

Loan Number 20

Credit → One credit report in the loan file dated April 9, 2003, with a print date of July 8, 2003, indicated alternative credit accounts were "verified" by the credit reporting agency. However, a second credit report with a later date of July 16, 2003, and a print date of July 16, 2003, showed the "verified" comment for the alternative credit accounts was removed from the report. The credit reports did not show the borrower's correct address, but rather listed the business address of Keystone Mortgage, the loan correspondent who originated the loan. Also, the borrower's name was misspelled on both credit reports in the file. The second credit report did not list three inquiries dated March – April 2003 that appeared on the earlier copy of the credit report.

Loan Number 21

Employment → The pay stubs contained multiple identical ink markings, indicating they may have been created using a template, and the stubs did not include the borrower's Social Security number.

Credit → The Social Security card in the file appeared questionable. The numbers on this card were significantly blurred and appeared to have possibly been altered using a pen or pencil.

Loan Number 22

Credit → The Social Security number used for the borrower's credit report did not match the number shown on the loan application and mortgage credit analysis worksheet in the FHA loan file. Several variations of the borrower's address were shown on the borrowers tax returns, loan application, HUD-1 and credit report.

Loan Number 23

Employment → The employer's address was not listed on the written verification of employment. The Social Security number listed on the loan application did not match the Social Security number listed on the verification of employment and pay stubs. A loan application found in Wachovia's file dated April 8, 2003, showed the borrower was employed only one year, while the loan application in the FHA file dated June 10, 2003, showed 2.3 years. Also, the loan application in Wachovia's file showed a different Social Security number for the borrower, and listed the borrower's current housing expense as \$350; yet the FHA loan file loan application and credit report showed \$670. Another updated

version of the loan application found in Wachovia's file listed the borrower's length of employment as 1.3 years and included a reference to a prior employer. The FHA file contained a verification of employment for the prior employer, yet this was not listed on the FHA loan application.

Credit → The Social security number listed on the loan application in the FHA file does not match the number shown on the credit report.

Loan Number 24

Credit → The borrower's last name was not spelled correctly on the credit report. Also, the credit report did not show the borrower's correct address, but rather listed the business address of Keystone Mortgage, the loan correspondent who originated the loan.

Loan Number 25

Employment → The 2001 W-2 form and pay stubs showed the borrower's last name spelled incorrectly. The borrower's first name shown on the 2001 W-2 was also inconsistent with other documents in the file.

Credit → The credit reports for all three credit bureaus (Equifax, Transunion, and Experian) reported the borrower as having a different first name than the name used for the loan. The borrower's Social Security number was changed slightly from the initial loan application to the final loan application. Credit reports were run under both Social Security numbers, and since both reports listed the borrower's alternative credit accounts, it appears the borrower was using multiple Social Security numbers, and multiple names, yet this was not resolved by Wachovia during the underwriting process. A credit report dated June 30, 2003, indicated eight inquiries were made related to the borrower's Social Security number, yet, zero inquiries were made related to the borrower's address, indicating the Social Security number used may have belonged to someone living at a different address.

Loan Number 26

Credit → One of two credit reports (dated January 7, 2002) in the FHA file contained a note stating the "INPUT SOCIAL SECURITY NUMBER NOT ISSUED AS OF 12/01", indicating that the co-borrower's Social Security number was false. However, another nearly identical (same "date ordered" and "report date") credit report found in the FHA file had this comment removed without any explanation. In addition, a CREDCO credit report dated a week later (January 15, 2002) found in Wachovia's loan file noted the same comment, "INPUT SOCIAL SECURITY NUMBER NOT ISSUED AS OF 12/01". The credit reports in the FHA file both noted the borrower's Social Security number was issued between 1953 and 1955, meaning the borrower was approximately 46-48 years old at the time of the credit report, dated January 7, 2002, yet the loan application indicated the borrower was only 28 years old.

Loan Number 27

Employment → The home address of the borrower listed on the 2002 pay stubs did not match the address shown on the borrower's W-2 from this same employer. The address on the pay stubs also did not match either the prior or current addresses shown on the loan application covering the prior four years. The credit report also showed the borrower was associated with a trade or business, yet this was not addressed in the file.

AUDITEE COMMENTS

Wachovia Mortgage Corporation
401 South Tryon Street, 22nd Floor
Charlotte, NC 28288



WACHOVIA

November 12, 2004

BY UPS

Ms. Joan S. Hobbs
Regional Inspector General for Audit
U.S. Department of Housing and Urban Development
Office of Inspector General
Pacific/Hawaii Region IX
611 West Sixth Street, Suite 1160
Los Angeles, CA 90017-3101

Re: Wachovia Mortgage Corporation
Discussion Draft Audit Report
Audit Case No. 2005-LA-XXXX

Dear Ms. Hobbs:

Wachovia Mortgage Corporation (“Wachovia” or the “Company”) is pleased to have this opportunity to respond to the Office of Inspector General’s discussion draft audit report, Audit Case Number 2005-LA-XXXX.

Wachovia takes the Office of Inspector General’s (“OIG”) draft findings very seriously. As a mortgagee that has enjoyed a positive relationship with HUD, Wachovia has always been committed to strict compliance with HUD-FHA requirements and demonstrating this commitment through our loan origination practices. The Company respectfully submits that it was as much a victim as was HUD with respect to the alleged violations regarding the 27 FHA loans cited in the Report.

The Report contains one finding. That is, Wachovia failed to resolve indicators of false credit and employment documents when underwriting FHA loans. It is significant to note that the 27 loans were originated by Keystone Mortgage and Investment, a former HUD-approved loan correspondent for Wachovia. The Company terminated its relationship with Keystone in July 2003.

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HUD OIG Response
November 12, 2004

Wachovia's Response

The 27 loans cited in the Report with "indicators" of fraud were underwritten by four staff underwriters in our Scottsdale, Arizona branch office. The transactions covered a period from January 2002 through July 2003. The report, cites 17 loans- for false social security numbers. While Wachovia does not agree or refute each of the individual "indicators" cited with respect to these loans, it is acknowledged that the social security information is not valid in 16 of the 17 loans. Accordingly, Wachovia will agree to indemnify HUD (Exhibit A) for these 16 loans with the exception of Loan# 10-Garduno. The Garduno loan is addressed in this response. Further, HUD's recent implementation of procedures for Social Security_number validation at the time of a case I.D. assignment, should result in reduction of the instances of Social Security number misrepresentation.

There were 26 loans cited in the report with findings related to non-traditional credit reports. The findings cited included the following; creditor contact information was not shown on the credit report, credit report did not indicate alternative credit accounts were verified, and creditor name was not shown on the credit report. In Wachovia's review of these findings, it appears that HUD's guidelines related to credit bureau reporting of non-traditional credit were updated in October of 2003 in HUD Handbook 4155.1 Rev-5. The loans cited in the audit report were originated prior to these new HUD guidelines. Accordingly, Wachovia in its underwriting of the loans was not required to perform any re-validation of the credit report, but relied on the accuracy and validity of the information provided by the credit reporting agency, Far West Credit Services, located at 1214 Wilmington Ave., #101, Salt Lake City, UT. Wachovia respectfully disagrees that these items should be cited as "indicators" of false documents that were not identified by Wachovia. If the credit report information was found to be invalid, it is anticipated that HUD will look to Far West Credit for an explanation regarding the information that was provided. The revised HUD guidelines as of October 2003, are set forth below:

HUD Handbook 4155.1 Rev-5: Section 2-3 As an alternative, the lender may elect to use a non-traditional mortgage credit report developed by a credit-reporting agency, provided that the credit-reporting agency has verified the existence of the credit providers and the lender verifies that the non-traditional credit was extended to the applicant. The lender must verify the credit using a published address or telephone number to make that verification.

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There are two loans cited in the Report that Wachovia is requesting the OIG to reconsider and dismiss its findings. These loans are addressed below:

Loan# 10, WMC Loan# 7381157 - Garduno

Audit findings cited the following: false credit documents, false social security number, opening date for gas and electric accounts did not agree to dates borrower lived at address, other indicators of false credit, as well as the credit report findings addressed above.

During Wachovia's review of this loan, the Company was unable to confirm that the Social Security number is misrepresented. It appears the number was issued in 1986-1988, when borrower was approximately 11 years of age. No other issues were noted with respect to the Social Security number. Accordingly, Wachovia respectfully submits that there is no conclusive information indicating misrepresentation. Regarding the findings of opening dates for gas and electric, information in the file shows that the borrower was in the property 4/95, utilities opened 5/95 and 6/95. Due to the minor variation in the dates, there is not sufficient information to determine if misrepresentation occurred. The borrower reasonably may have signed a lease in April, but not moved into the property until May. Due to the lack of conclusive information regarding any misrepresentation in the file, as well as the loan's current performance (no defaults since inception), Wachovia requests that HUD reconsider and withdraw its request for indemnification on this loan.

Loan# 19, WMC Loan# 748399 – Wilcox

Based on Appendix B, findings cited for this loan are false credit documents, as well as the credit report findings addressed above. No details are provided in the Report on falsified documentation. As stated previously, the revised guidelines for non-traditional credit reports were not implemented by HUD at the time that this loan was originated. The loan is current and has had no defaults since inception. Wachovia requests that HUD reconsider and withdraw its request for indemnification on this loan.

For the remaining loans shown in Exhibit B, that were not addressed in the response above, Wachovia acknowledges that there were fraud indicators which it failed to identify. The Company agrees to indemnification for these cases.

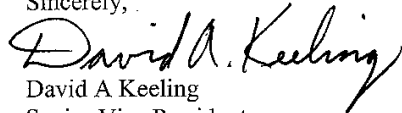
Wachovia takes fraud prevention and mitigation very seriously. Over the past several years we have implemented significant pre-funding processes and tools for the prevention of fraud. These include a Social Security number validation program, verbal verifications of employment prior to funding, automated valuation of property values, property flip identification program, validation of credit reporting on manually underwritten loans, and the validation of income through the IRS 4506 process. These tools and processes will be reinforced on an ongoing basis with our operations staff.

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Again, thank you for the opportunity to respond to the draft report. Wachovia has a comprehensive Quality Assurance Program in place and through this program it monitors continued compliance with HUD's guidelines. Wachovia, like HUD, was a victim in these transactions. We value our relationship with HUD and request that you carefully consider this response and the actions Wachovia has taken, and will take, in the future to strengthen our FHA loan origination processes as a result of the OIG Report.

Should you have any questions, please contact me at 704-383-2930.

Sincerely,



David A Keeling
Senior Vice President
Third Party Operations Leader

Cc: Mitch Kider
Carol Dubie
John A Miles
Ben Cowen
Dee Sossaman
Linda Davila
C.D. Davies