



**U.S. Department of Housing and Urban Development**  
**Office of Inspector General**  
Region VII Office of Audit, 7AGA  
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MEMORANDUM NO:  
2007-KC-0801

September 24, 2007

**MEMORANDUM FOR:** Brian D. Montgomery, Assistant Secretary for Housing – Federal Housing Commissioner and Chairman, H

*//signed//*

**FROM:** Ronald J. Hosking, Regional Inspector General for Audit, 7AGA

**SUBJECT:** Lenders Submitted Title II Manufactured Housing Loans for Endorsement without the Required Foundation Certifications

### **INTRODUCTION**

We audited the U.S. Department of Housing and Urban Development's (HUD) Title II manufactured housing loan program. We initiated this review because of the high insurance risk to the Federal Housing Administration (FHA) fund that manufactured homes have historically represented, and prior audit observations of foundation deficiencies with FHA-insured homes. Our objective was to determine whether, and to what extent, FHA insured Title II manufactured housing loans on properties with foundations that did not meet its requirements (see OIG Report #2007-KC-0004, issued September 24, 2007).

As part of this audit, we reviewed 205 FHA loan files for the required engineer's certification of the property foundation. FHA rules require lenders to provide the certification confirming that the foundation complies with FHA requirements. We found that lenders submitted 21 loans for endorsement without submitting the engineer's certification. We recommend that HUD seek indemnifications and recovery of losses incurred from the responsible lenders, unless the lenders can provide the required certifications. This memorandum provides our results specific to these certifications.

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

## **METHODOLOGY AND SCOPE**

To accomplish our objective, we evaluated Title II manufactured housing loans insured by FHA that closed between January 1, 2003, and December 31, 2005. We reviewed FHA loan files, HUD handbooks, and its guidebook for permanent foundation requirements. We also reviewed previous HUD Office of Inspector General (OIG) reports related to Title II manufactured housing. We interviewed HUD headquarters staff and homeownership center staff as well.

We identified the universe of all Title II manufactured housing loans that closed between January 1, 2003, and December 31, 2005, using data from HUD's Single Family Data Warehouse computer system. The universe consisted of 102,195 loans with original mortgage amounts totaling more than \$10.5 billion. The 102,195 loans included 84,491 loans that were actively insured or in claims status as of August 2006 with original mortgage amounts totaling more than \$8.7 billion. Using the universe of 84,491 loans, we employed an unrestricted attribute sampling plan to statistically select 68 loans and 32 replacement loans for review. We reviewed the FHA loan files for 98 of the loans in this sample. HUD was unable to provide the remaining two loan files for our review.

We also identified the universe of all Title II manufactured housing loans closing between January 1, 2000, and December 31, 2005, that became HUD real estate owned properties, using data from HUD's Single Family Acquired Asset Management System. The universe consisted of 7,573 loans with original mortgage amounts totaling almost \$700 million. From this universe, we selected a sample of 114 loans for review. We selected the 57 loans with the highest acquisition cost to FHA and the 57 loans with the highest loss amounts. We reviewed the FHA loan files for 107 of the loans in our sample. HUD was unable to provide the remaining seven loan files for our review.

We relied on computer-processed data contained in HUD's Single Family Data Warehouse and Neighborhood Watch systems. We assessed the reliability of the data, performed sufficient tests of the data, and found the data adequate to meet our audit objective. We also relied on data from HUD's Single Family Acquired Asset Management System to identify a sample of loans to review for evidence of the required engineer's certification on the foundation of the manufactured home. We did not use the electronic data to reach audit conclusions; therefore, we did not assess the reliability of the data.

In assigning a value to the potential savings to the FHA insurance fund if HUD implements our recommendations on previously insured loans for which it has not yet incurred a loss, we applied FHA's average loss experience for fiscal year 2005 provided by HUD. We calculated the savings value at \$223,164 for the seven properties currently actively insured, which is 29 percent of the original mortgage amounts of \$769,532.

We performed our audit work from August 2006 through April 2007.

## BACKGROUND

HUD manages the FHA insurance program. FHA provides mortgage insurance on loans made by approved lenders. It insures mortgages on single-family and multifamily homes, including manufactured (mobile) homes. FHA is the largest insurer of mortgages in the world, insuring more than 34 million properties since its inception in 1934. FHA mortgage insurance provides lenders with protection against losses as a result of homeowners' defaulting on their mortgage loans. The lenders bear less risk because FHA will pay a claim to the lender in the event of a homeowner's default. Loans must meet FHA requirements established by FHA to qualify for insurance.

Under its Title II program, FHA has provided loan insurance on manufactured homes since 1983. Manufactured homes with loans insured under the Title II program must be placed on a permanent foundation meeting FHA requirements contained in HUD Handbook 4930.3G, Permanent Foundations Guide for Manufactured Housing, revised in September 1996. According to HUD's Single Family Data Warehouse, FHA has insured more than 280,000 Title II manufactured housing loans within the last 10 years with original mortgage amounts of more than \$28.6 billion.

## RESULTS OF REVIEW

Lenders did not provide HUD with the required engineer's certification of the foundation when submitting the loans for insurance on 21 of the 205 manufactured housing loans reviewed. As a result, FHA insured 21 loans, representing more than \$1.75 million in potential and actual losses, on properties for which HUD had no assurance that the foundations met its requirements.

FHA rules require lenders to provide an engineer's certification confirming that the foundation complies with FHA requirements. HUD deems the lender responsible for underwriting the loan and determining that the property is acceptable for mortgage insurance. When insuring a loan, HUD relies on certifications by the lender and the lender's underwriter that the loan complies with FHA regulations and underwriting instructions.

Nine of the loans submitted to HUD without the required engineer's certification were from the nationwide statistical sample. The remaining 12 loans were from the sample of 107 defaulted manufactured housing loans that closed from January 2000 through December 2005. These loans had gone through HUD's claims process, and HUD had acquired the properties for resale.

As of September 6, 2007, HUD's systems showed the following insurance status on the 21 loans.

Status of loans	Number of loans	Losses incurred	Estimated future losses
Currently insured**	7		\$223,164
Claims paid - property sold	14	\$1,529,723	
<b>Totals</b>	<b>21</b>	<b>\$1,529,723</b>	<b>\$223,164</b>

\*\*Estimated future losses are based on FHA's average loss rate of 29 percent of claims paid from the FHA insurance fund for fiscal year 2005.

## **RECOMMENDATIONS**

We recommend that the assistant secretary for housing – federal housing commissioner

- 1A. Seek indemnification of seven actively insured loans with original mortgage amounts of \$769,532 if the lenders cannot provide the required engineer's certifications showing that the foundations met FHA requirements. The projected loss is \$223,164, based on FHA's insurance fund average loss rate of 29 percent for fiscal year 2005.
  
- 1B. Seek recovery of \$1,529,723 in FHA losses incurred on 14 loans if the lender cannot provide the required engineer's certifications showing that the foundations met FHA requirements.

## APPENDIXES

### Appendix A

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

Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1A		\$223,164
1B	\$1,529,723	

- 1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or federal, state, or local polices or regulations.
- 2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an OIG recommendation is implemented. This includes reductions in outlays, deobligation of funds, withdrawal of interest subsidy costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings which are specifically identified.

Implementation of our recommendations to indemnify manufactured housing loans for which the lender cannot provide the required engineer's certifications will reduce FHA's risk of loss to its insurance fund. The amount for recommendation 1A reflects that, upon sale of the mortgaged property, FHA's average loss experience is about 29 percent of the claim amount based upon statistics provided by HUD.

## Appendix B

### AUDITEE COMMENTS AND OIG'S EVALUATION

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HUD provided limited comments to this memorandum as part of its response to the related audit report, OIG Report # 2007-KC-0004, issued September 24, 2007. In its response, HUD requested that OIG identify whether any of the 21 loans in this memorandum are part of the 55 loans recommended for indemnification in the audit report. In the draft version of this memorandum, we explained that we identified 21 loan files that were missing the engineer's certification. We also explained that six of those loans were included in the audit report's recommendation for indemnification and the remaining 15 loans were included in this memorandum's recommendation for indemnification. We have subsequently removed the recommendation for indemnification from the audit report and included the six loans without engineer's certifications in this memorandum.

The complete text of the response and our evaluation of that response can be found in the aforementioned audit report.

## Appendix C

### FHA LOANS SUBMITTED WITHOUT REQUIRED ENGINEER'S CERTIFICATION

FHA case number	Original mortgage amount	Loan status	Losses incurred - property sold
091-3820218	\$74,805	A*	
381-6326090	\$87,746	C**	<b>\$153,474</b>
381-6911809	\$96,485	C	<b>\$57,875</b>
263-3628226	\$102,312	A	
413-4020338	\$107,300	A	
372-3468633	\$108,050	A	
105-1216836	\$111,943	A	
411-3101480	\$113,798	C	<b>\$132,549</b>
042-7604566	\$123,722	C	<b>\$137,069</b>
493-7555494	\$126,022	C	<b>\$64,163</b>
201-3233594	\$128,204	A	
495-6063961	\$133,939	C	<b>\$116,645</b>
491-7474716	\$134,842	C	<b>\$116,568</b>
311-1773702	\$136,918	A	
491-7347306	\$144,333	C	<b>\$118,916</b>
491-7617132	\$149,774	C	<b>\$110,919</b>
491-6988555	\$154,111	C	<b>\$140,482</b>
052-1154412	\$163,651	C	<b>\$65,886</b>
052-2798753	\$164,531	C	<b>\$89,836</b>
052-2863017	\$168,358	C	<b>\$136,825</b>
291-3270679	\$168,430	C	<b>\$88,516</b>
<b>Totals</b>	<b>\$2,699,274</b>		<b>\$1,529,723</b>

\* A = Active/currently insured

\*\* C = Claim paid on defaulted loan