
AUDIT REPORT



HUD's Controls Over Single-family Insurance Claims Allow Ineligible Interest Payments and Delays in Resolving Post-claim Findings

2005-DE-0001

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Office of Audit, Region 8
1670 Broadway, 24th Floor
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TO: Frank L. Davis, General Deputy Assistant Secretary for Housing, H

//signed//

FROM: Ronald J. Hosking, Regional Inspector General for Audit, 8AGA

SUBJECT: HUD's controls over single-family mortgage insurance claims allow ineligible interest payments and unnecessary delays in resolving post-claim findings.

HIGHLIGHTS

What We Audited and Why

We audited the process the U.S. Department of Housing and Urban Development (HUD) uses to pay Federal Housing Administration Single-Family insurance claims. The audit was part of our fiscal year 2004 Annual Audit Plan. We scheduled the audit because the annual dollar disbursements of Federal Housing Administration insurance claims represents a significant disbursement activity of the Department. HUD paid out almost \$6.5 billion in fiscal year 2003 to settle claims for principal and interest on about 73,750 foreclosed properties.

We wanted to determine whether HUD management and system controls over claims disbursements were functioning as designed and adequate to prevent payments for ineligible or unsupported costs.

What We Found

For most Federal Housing Administration Single-Family insurance claims, HUD management and system controls are adequate and effective in ensuring that only eligible and adequately supported costs are accepted and paid.

However, these controls are not sufficient to prevent the payment of interest that is disallowed for lenders' noncompliance with Federal Housing Administration foreclosure timeframes and reporting rules. We estimate that HUD paid approximately \$28.2 million in disallowed interest accruals not identified by HUD's systems on claims paid from October 1, 2000 to September 30, 2003. HUD primarily relies on lenders to comply with Federal Housing Administration foreclosure timeframes and reporting requirements, report violations, and appropriately adjust accrued interest curtailment dates, when submitting insurance claims. Payments of disallowed interest occurred because some lenders did not adjust their claims to comply with Federal Housing Administration requirements.

HUD uses interest curtailment as a means to encourage lenders to meet HUD's requirements. However, without establishing goals and methods of measuring performance, HUD has no way of determining whether the current level of interest curtailment and postclaim reviews are bringing the level of compliance to a level desired by HUD. If HUD sets measurable goals for lenders to meet then it would be in a better position to identify the best methods to bring about a desirable level of performance.

HUD also needs to resolve postclaim monetary findings in a timely manner and improve debt collection procedures. As part of HUD's quality assurance control over insurance claim disbursements, an independent contractor performs postclaim reviews to identify unsupported and disallowed costs claimed by lenders. HUD has neither settled nor collected an outstanding balance of \$2.3 million in monetary findings from 44 postclaim reviews that were done in fiscal years 1996, 1997, 1998, 2001, 2002 and 2003.

During our audit fieldwork, HUD took steps to address our concerns by consolidating claim collections under the Albany Financial Operations Center. HUD developed and implemented procedures to finalize disputed findings from postclaim reviews in a timely manner.

What We Recommend

We recommend that HUD:

- Establish and implement performance goals for the default monitoring requirements that HUD expects lenders to meet, utilizing existing data to the extent possible; and create a plan to obtain additional information necessary for HUD to establish performance goals and accurately measure lender performance for the foreclosure completion timeframe or in the absence of additional information, alternative methods for measuring lender performance.
- Create and implement a plan of action that HUD should follow to ensure lenders meet performance goals.

- Finalize disputed monetary findings in a timely manner and collect delinquent debts in accordance with the Debt Collection Act.

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.

Auditee's Response

We submitted the draft report to HUD on December 6, 2004. We requested that the Department provide written comments to the draft report by January 7, 2005. We approved HUD's request for an extension and received the written comments on the draft report on March 18, 2005. HUD generally concurred with the findings and the recommendations. We considered HUD's written comments to the draft report, and made the appropriate changes to the final report. The complete text of the Assistant Secretary for Housing's response can be found in Appendix B of this report. We excluded the attachments to the response because they contained internal policies, procedures and confidential information.

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BACKGROUND AND OBJECTIVES

The Federal Housing Administration provides mortgage insurance on single-family home loans made by Federal Housing Administration-approved lenders throughout the United States and its territories. Federal Housing Administration mortgage insurance provides lenders with protection against losses as the result of homeowners defaulting on their mortgage loans. When a mortgagor defaults and the lender is unable to bring the loan current through loss mitigation, the lender can submit a claim for single-family mortgage insurance benefits to the U.S. Department of Housing and Urban Development (HUD). There are many types of single-family claims, but conveyance claims are the most common. All claims must be submitted on HUD form HUD-27011, Single Family Application for Insurance Benefits. HUD encourages lenders to send all claim forms (parts A and B) to HUD electronically through the Electronic Data Interchange or the FHA Connection¹.

During a conveyance claim, the lender obtains the property through foreclosure and deeds the property to HUD. Either the holder² or the servicer³ of the mortgage may submit the claim. In either case, the disbursement will be remitted to the holder of the mortgage. The lender official signing a hardcopy of the form HUD-27011, which is submitted to HUD, is certifying that all information and statements contained in the claim are true and correct.

HUD processes the electronic claims information by computer at HUD Headquarters. The data are pre-screened before processing to determine whether certain essential data are missing or incomplete. If the information is complete, it passes through system edits and control checks. If there are not any hard errors,⁴ the system will compute and generate an electronic payment to the holder. If there is a fatal error,⁵ the lender must submit a corrected claim to resolve the fatal error before further processing can occur. The system edits are designed to permit prompt payment of most claims by accepting costs encountered in routine claims. If unusually high disbursements are reported, the claim payment will be reduced, and the holder may file a supplemental claim for the part of the claim disallowed, with documentation to support the amount of and the need for the higher payment. The advice of payment with the initial claim reimbursement will identify amounts and reasons for a reduced claim payment.

Although a claim may be processed and paid by the computer, HUD may upon a postclaim review or a property inspection, require reimbursement of any amounts that are found to be excessive or not supported by appropriate documentation or work done to the property.

¹ Home Equity Conversion Mortgage, supplemental, and reconveyance claims cannot be submitted electronically and need to be submitted on paper. Loss mitigation claims can be submitted electronically, via FHA Connection or on paper. Conveyance and preforeclosure sale claims can be submitted on paper, however they are subject to a \$100 processing fee.

² *Holder* – lenders who are holders of the credit instruments issued under a trust indenture, mortgage or deed of trust pursuant to which such holders act by and through a trustee therein named.

³ *Servicer* - a HUD approved lender who services HUD-insured mortgages.

⁴ *Hard error* - indicates that the field contains an error that must be corrected before further processing can occur.

⁵ Fatal errors cannot be pay-authorized (overridden) by the Claims Branch.

Our overall objective was to assess HUD's controls over the conveyance claim payment process to determine whether current controls were functioning as designed and adequate, to prevent the payment of ineligible or unsupported costs. Based on our survey work, we narrowed the overall objective to two specific objectives:

- 1) To analyze the data lenders submit to HUD to determine the amount of interest that could have been curtailed, as disallowed interest, for non-compliance with HUD's foreclosure timeframe and reporting requirements.
- 2) To review HUD's processes and procedures for resolving disputed postclaim review findings and ensure that outstanding receivables are processed in accordance with the Debt Collection Act.

RESULTS OF AUDIT

Finding 1: Measurable Performance Goals Are Needed To Ensure a Desirable Level of Lender Compliance Is Achieved

HUD systems were not designed to automatically determine whether a lender met the reasonable diligence timeframes or the default monitoring reporting requirements. HUD relies on lenders to determine how much interest should be deducted from their claims for noncompliance with these requirements. However, lenders do not always self-curtail interest when they fail to meet the requirements. We estimated that in a 3-year period, HUD paid disallowed interest of approximately \$28.2 million to lenders because the lenders did not self-report violations. HUD needs to maximize the conveyance of properties in the shortest amount of time possible to get the properties on the market sooner, which will help preserve the property value. HUD also needs to maximize full timely reporting to better determine the potential cost of future insurance claims. HUD uses interest curtailment as a means to encourage lenders to meet HUD's requirements. However, without establishing goals and methods of measuring performance, HUD has no way of determining whether the current level of interest curtailment and postclaim reviews are bringing the level of compliance to a level desired by HUD. HUD has sufficient information to evaluate lender performance in meeting HUD's requirement to report to the default monitoring system. However, HUD has insufficient information to measure a lender's ability to meet the foreclosure completion timeframes. In this case, HUD should establish a plan to obtain additional information necessary for HUD to accurately measure lender performance or in the absence of additional information, alternative methods for measuring lender performance. Once HUD has established measurable goals, it should create a plan to evaluate different methods or approaches that can be used to best achieve a desirable level of lender compliance with the requirements.

Disallowed Interest for Untimely Completion of Foreclosure

**Lenders Failed To Self-Curtail
Disallowed Interest of
Approximately \$7.6 Million in a
3-Year Period**

Based on our analysis of the data in HUD's systems we estimated that in a 3-year period, HUD paid out at least \$7.6 million in claim payments to which lenders were not entitled. HUD pays lenders the monthly interest accrued on the mortgage from the date the borrower defaults on the loan to the date HUD pays the claim. If lenders do not complete foreclosure within the prescribed timeframes they forfeit most of the interest accrued after the missed deadline. Without these timeframe requirements, there is little incentive for lenders to complete foreclosure and convey the property to HUD in a timely manner.

Based on 176⁶ postclaim reviews in fiscal year 2003, HUD disallowed interest payments of more than \$200,000 for claims with untimely completion of foreclosure. This was the third largest finding during the annual reviews.⁶ As the postclaim reviews showed, lenders are failing to self-report disallowed interest when they do not have a valid reason for exceeding the reasonable diligence requirements.

We performed additional analyses to estimate the disallowed interest that lenders did not self-report in a 3-year period for exceeding the reasonable diligence timeframes without a valid reason. Due to the limitations of data collected by HUD, we compared a non-statistical sample of more than 1,700 postclaim reviews with our analysis to identify an error rate that we could apply to our analysis to estimate the disallowed interest that lenders collected. We estimate that HUD paid out at least \$7.6 million in claim payments to which lenders were not entitled.

HUD Currently Does Not Collect Enough Information To Automate the Process

HUD does not collect enough information from lenders to automatically verify whether the lender has met the reasonable diligence requirements. In most circumstances, HUD's automated system can measure the time between two dates entered on the claim form, determine if time requirements have been met and calculate the date to which interest should be paid. However, if lenders exceed the reasonable diligence timeframe without a valid reason, HUD requires the lenders to calculate the last date it was eligible to receive interest payments. This is called the curtailment date. HUD will then reduce the claim amount based on the curtailment date provided by the lender.

Missing information needed by HUD's claim payment system to enforce the reasonable diligence requirement includes:

- 1) Type of foreclosure (judicial or non-judicial);
- 2) Foreclosure completion date;
- 3) Valid reasons for foreclosure delays and the length of the delays.

Lenders are not required to report the type of foreclosure. When the lender institutes foreclosure on a property, it must complete foreclosure within State specific timeframes⁷ prescribed by HUD. The reasonable diligence timeframes in some states vary depending on whether the foreclosure is judicial or nonjudicial.

⁶ All closed reviews as of March 2004.

⁷ Specified in appendix 7 of Handbook 4330.4, REV-1 for cases in which the first legal action to foreclose occurred before October 1, 2001, and in Mortgagee Letter 2001-19 for cases with the first legal action occurring after October 1, 2001. The Department is currently revising the reasonable diligence foreclosure timeframes for several jurisdictions.

HUD does not require lenders to always report the foreclosure date to HUD on the claims form. Lenders do report the date that they gained possession and acquired marketable title, which is the later of the acquisition of marketable title date or the vacancy date. If the acquisition of marketable title date is reported, HUD has the completion of foreclosure date; however, if the vacancy date is reported it does not.

Valid reasonable diligence delays that HUD permits are not fully reported by lenders. For example, a circumstance outside the lenders control such as a bankruptcy or court delay is considered a valid reason. HUD currently does not require lenders to get pre-approved extensions for reasonable diligence delays because it would be burdensome or unfeasible for lenders and HUD field offices.

**Measurable Performance Goals
and Results Needed to Assess
the Effectiveness of Interest
Curtaiment on Compliance**

Interest curtailment is a means to maximize the timely completion of foreclosure. However, HUD has no way to truly measure the effectiveness of interest curtailment on lender compliance because it has limited data that can be used to determine how many foreclosures exceed the timeframe or identify valid delays. HUD should establish a goal that results in the conveyance of properties to HUD in the shortest amount of time as possible. All future policy and system changes need to further HUD's ability to achieve this goal. Regardless of whether the process is automated, HUD needs to obtain sufficient information to ensure that HUD requirements are achieving desired results. Measurable requirements will enable HUD to compare actual results with performance goals. HUD is currently in the process of modifying the default monitoring system to accept the reporting of the foreclosure sale and eviction dates. This will bring HUD one-step closer to being able to measure lenders compliance with the current timeframe requirements. HUD would be able to measure the current requirement if it also obtains the type of foreclosure and the amount of time that the foreclosure was delayed due to a valid exception. If HUD sets measurable goals for lenders to meet then it would be in a better position to identify the best methods to bring about a desirable level of performance.

HUD is in the process of studying the feasibility of the Accelerated Claim Disposition Demonstration Program. Lenders participating in the program receive a fee instead of accrued interest to service eligible defaulted mortgages. Claims that are accelerated under the program will not be subject to the completion of foreclosure timeframe requirements. HUD should consider the potential impact of this program when considering the best approach to maximize the timely completion of foreclosure.

Additional Actions May to Be Necessary to Attain a Desirable Level of Performance

Automating interest curtailment would increase the lenders cost for failing to meet HUD's foreclosure timeframe requirements and may increase performance. Automating this requirement in its present form, including all of the valid exceptions, would require substantial changes to the system and the data collected, which could be a costly and time-consuming process. However, we believe that HUD can modify its policies and requirements to simplify the process and reduce the cost of system modifications. HUD could consider combining the reasonable diligence and conveyance timeframe requirements, which could utilize data already collected and would require minimal modifications to the system. The modified timeframe would combine the completion of foreclosure within the reasonable diligence State timeframes, and the conveyance of the property to HUD within 30 days after obtaining possession and marketable title.

The lender currently submits the institution of foreclosure and conveyance dates to HUD on the claim form. For this example, it would only require the additional reporting of whether the foreclosure was judicial or non-judicial. HUD already allows lenders to take this approach when the lender does a direct conveyance. HUD could continue to keep the timeframes separate but HUD would also need to obtain the completion of foreclosure date from the lender. The extension to convey date could then be used to account for valid delays.

HUD does not require lenders to get pre-approved extensions for valid reasonable diligence delays due to the time necessary to review and approve them. If the process was automated, HUD could decrease the burden of approving extensions by allowing lenders to obtain automatic extensions. By doing so, the lender would attest that there was a valid reason outside of the lenders control, such as a bankruptcy, causing the delay. HUD currently relies on lenders to self-curtail interest so why not trust lenders to request an automatic extension. It would be a better control since it is easier to omit a date than create a fictitious reason for a delay. HUD would need to publish clear guidance on what constitutes a valid delay and how to compute the extension.

Lenders could describe the reason for the delay in the comments field. If HUD provided lenders with key words to use for describing the delays, HUD could then pull the information out of the Single Family Data Warehouse to quantify the types of delays by lender and State, enabling HUD to identify lenders who have unusually high occurrences of delays for monitoring purposes. These suggestions would facilitate the measurement of lender performance and automation of the process.

Targeted Monitoring Reviews May Increase Compliance with Timeframe Requirement

Until HUD can measure results or achieve automation, it could enhance the recovery of funds after the claim payment by performing targeted postclaim reviews. The process would be enhanced because lenders would clearly understand the full scope of the problem, which could help them identify issues that are preventing the timely completion of the foreclosure process. When HUD performs a postclaim review, it selects a sample of claims to review. If the review identifies claims where the lender failed to curtail interest for not meeting the completion of foreclosure timeframes then the amount is extrapolated to the population that the sample was selected. It's unclear how effective this strategy is at improving lenders compliance with the timeframe requirement, since it appears that the level of noncompliance has not changed much in the last three years.

Once lenders start reporting the foreclosure sale date on a consistent basis to the default monitoring system, HUD can run exception reports to identify cases that were not completed within established timeframe requirements⁸. HUD could target lenders based on these exception reports and target the cases to be reviewed in a limited postclaim review. The files for these cases can be reviewed to determine whether the lender had a valid reason for not meeting the requirement. The lender can then have the interest curtailed for all cases in the period where it failed to meet the requirement. Lenders would then have a realistic assessment of its ability to meet HUD's foreclosure timeframes and may be more likely to improve its processes and systems. However, without measurable goals, HUD will not be able to evaluate the level of lender compliance.

The Use of Incentives for Lenders That Improve Performance or Penalties and Sanctions for Lenders That Fail to Improve May Be Necessary

Although, we are suggesting that HUD maximize interest curtailment through automation and targeted postclaim reviews, the true goal is to maximize the timely completion of foreclosure. Interest curtailment is a means to attain this goal. However, it may not be enough to bring about consistent compliance of the foreclosure completion timeframes. If lenders would rather pay the interest curtailment than invest the resources in its systems and processes to ensure the requirement is met, then HUD may lose out in the end because the delays may

⁸ Except for the four States who have different timeframes for judicial and nonjudicial foreclosures.

lead to a greater reduction of the net recovery amount from the sale of the property. If increasing the level of interest curtailment does not bring the level of compliance to an acceptable level HUD should consider other actions, such as the use of incentives for lenders who improve performance, or penalties and sanctions for lenders who fail to improve.

Disallowed Interest for the Untimely Reporting of the Institution of Foreclosure

Lenders Failed To Self-Curtail Penalties of Approximately \$20.6 Million in a 3-Year Period

Based on our analysis of the data in HUD's systems we estimated that in a 3-year period, HUD paid out \$20.6 million in claim payments to which lenders were not entitled because lenders failed to report the institution of foreclosure to HUD's Single Family Default Monitoring System in a timely manner. HUD imposed this requirement to improve the accuracy of reporting, in order to enhance HUD's ability to forecast the cost of future insurance claims by analyzing loans undergoing foreclosure.

Our analysis provides a conservative estimate since we gave the lenders credit if they reported a foreclosure in progress⁹ or foreclosure completed¹⁰ status in lieu of the institution of foreclosure¹¹ status code.

Based on 176¹² postclaim reviews in fiscal year 2003, HUD disallowed interest payments of more than \$639,000 for claims with untimely reporting of foreclosure institution. This was the largest finding encountered during the fiscal year 2003 postclaim reviews.¹²

We performed additional analyses to estimate disallowed interest claimed by lenders in a 3-year period when they failed to report the institution of foreclosure in a timely manner. We compared a non-statistical sample of more than 2,100 cases analyzed during the postclaim reviews with our analysis to identify an error rate that we could use to estimate the amount of disallowed interest lenders collected. We estimate that HUD paid out at least \$20.6 million in claim payments to which lenders were not entitled.

Our analysis showed an improvement over the last 3 years, as shown in the chart on the next page. This improvement occurred primarily because lenders are doing a better job of self-curtailing interest for the noncompliance with the reporting

⁹ Status code 45.

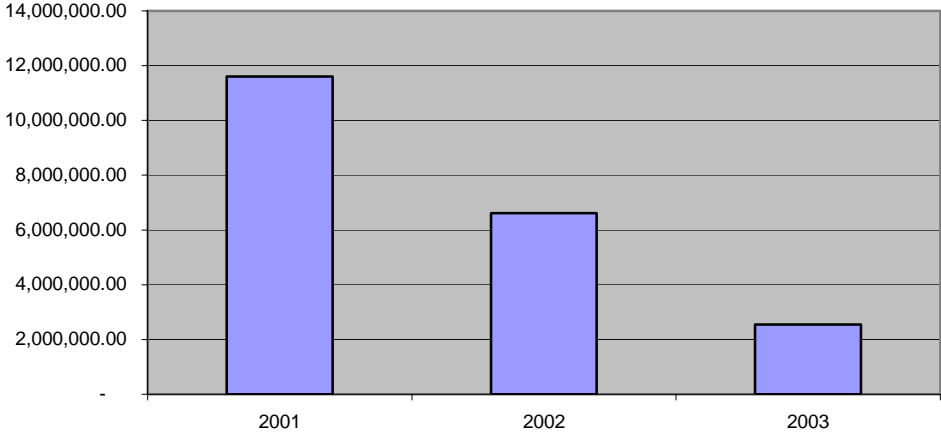
¹⁰ Status code 46.

¹¹ Status code 68.

¹² All closed reviews as of March 2004.

requirement. There has been a modest improvement in meeting the reporting requirement over the last three years, with the percentage of claims with untimely reporting dropping from 10 percent of the total claims in 2001 to 8 percent in 2003. Although HUD receives the information necessary to enforce the reporting requirement HUD cannot automatically enforce it because the claims payment system is not integrated with the default monitoring system.

Additional Interest Curtailed for Untimely Reporting



Performance Goals Should Be Established and Existing Data Could Be Used to Measure Performance

Interest curtailment is a means to maximize the reporting of the institution of foreclosure. Lenders have significantly improved the self-curtailment of interest for not meeting the reporting requirement. However, there has only been a slight improvement in meeting the reporting requirement. Unlike the completion of foreclosure timeframe requirement, HUD has sufficient data in its systems to measure lenders compliance with the reporting requirement. HUD should establish performance goals for lenders to meet and measure the results. If HUD establishes goals for lenders to meet and uses existing data to measure performance, then it would be in a better position to identify the best methods to attain a desirable level of performance.

Additional Actions May Be Necessary To Ensure HUD Goals Are Met

Automating the process would increase interest curtailment, which may help maximize the reporting of the institution of foreclosure. HUD can consistently apply the curtailment of disallowed interest for the untimely reporting of the institution of foreclosure date by integrating the claim payment system with the default monitoring system. HUD will not be able to fully automate the process because in some States the property is conveyed to HUD before the expiration of the reporting requirement. Although we believe this would be an infrequent occurrence, HUD could mitigate the problem by making the claim payment if the reporting requirement has not yet expired. These cases could be flagged for a post payment review. HUD could determine later whether the lender reported in accordance with the requirements and bill the lender for the overpayments if necessary. This process could also be automated.

Without automating the process, HUD can take additional steps to increase interest curtailment in an effort to improve lender compliance by using available information to target lenders who failed to meet the default monitoring reporting requirement. HUD could run a report, using existing data, to match claims and default monitoring data from the Single Family Data Warehouse to identify cases where the lender failed to both report on time and self-curtail interest. HUD could send a monthly exception report to the lender with a notification that the lender failed to self-curtail interest for the cases and owed HUD a refund. The lender could file a supplemental claim to return the funds.

Another alternative would be for HUD to perform targeted postclaim reviews of lenders based on exception reports. The postclaim review contractor currently selects a statistical sample of claims during a lender review. Errors found in the sample are usually projected to the population. However, HUD's current policy is not to project errors caused by the failure to report to the default monitoring system. Therefore, lenders are only held accountable for the lack of interest curtailed from claims picked in the sample. By performing targeted reviews, the postclaim review could then hold the lender accountable for all instances in the period where the lender failed to curtail interest for the failure to report. Once lenders realize that HUD is holding them accountable for the reporting requirement, the quality of lender reporting may improve.

HUD imposes the curtailment of interest because it wants lenders to report the institution of foreclosure to the default monitoring system. Increasing the level of curtailment for not meeting the requirement may lead to improvements that bring the level of noncompliance to an acceptable level. However, if these steps do not bring the level of compliance to an acceptable level and lenders would rather pay

the interest curtailment than invest resources to improve its systems and processes, then HUD should also consider the use of incentives for lenders who improve performance or penalties and sanctions for lenders who fail to improve. The accurate reporting of the institution of foreclosure will enable HUD to accurately determine the potential cost of future insurance claims.

Conclusion

HUD systems were not designed to automatically determine whether a lender met the reasonable diligence timeframes or the default monitoring reporting requirements. HUD relies on lenders to determine how much interest should be curtailed from their claims for noncompliance with HUD requirements. However, lenders do not always self-curtail interest when they fail to complete foreclosure within HUD-prescribed timeframes or fail to timely report the institution of foreclosure to HUD. HUD currently does not measure lender performance in meeting these requirements and does not have enough information to accurately measure lender performance for meeting the completion of foreclosure timeframes.

HUD uses interest curtailment as a means to encourage lenders to meet HUD's requirements. However, without establishing goals and methods of measuring performance, HUD has no way of knowing whether interest curtailment is bringing the level of compliance to a level desired by HUD. Based on our estimates, it appears that in a three-year period, lenders are doing a better job of curtailing interest but there has only been modest improvement in compliance with the requirements.

If HUD sets measurable goals for lenders to meet then it would be in a better position to identify the best methods to bring about a desirable level of performance. By improving lender performance, lenders will convey properties to HUD more quickly, enabling HUD to get the properties on the market sooner, which can help preserve the property value; and lenders will report on time more often, enabling HUD to enhance its ability to forecast the cost of future insurance claims by analyzing loans undergoing foreclosure.

Recommendations

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

- 1A. Establish and implement performance goals for the default monitoring requirements that HUD expects lenders to meet, utilizing existing data to the extent possible.
- 1B. Create and implement a plan to obtain additional information necessary for HUD to establish performance goals and accurately measure lender performance for the foreclosure completion timeframe requirements, or in the absence of additional information, alternative methods for measuring lender performance.
- 1C. Create and implement a plan of the additional actions that HUD will take to encourage lenders to meet performance goals, that may include:
 - Automating the curtailment of interest;
 - Using exception reports to bill lenders for interest that was not self-curtailed;
 - Using exception reports to perform targeted postclaim reviews; and/or
 - Taking other actions, such as the use of incentives for lenders who improve performance or penalties and sanctions for lenders who fail to improve.

RESULTS OF AUDIT

Finding #2: HUD's Procedures for Resolving Disputed Monetary Findings and Debt Collection Are Inadequate

At the conclusion of our review, HUD had 44 postclaim reviews, performed in fiscal years 2003 and earlier, with an outstanding balance of \$2.3 million that had not been settled or collected. HUD lacked adequate procedures to resolve disputed monetary findings identified during postclaim reviews in a timely manner, thus affecting the collection of debts arising from the reviews. The Claims Branch sometimes permitted lenders an unlimited number of opportunities to submit additional supporting documentation not available during the postclaim review. In addition, the Asset Management Division did not always review in a timely manner appeals by lenders of decisions made by the Claims Branch. Further, when HUD made a final decision to conclude the finding amounts, it had not implemented a process to actively collect outstanding receivables, refer receivables more than 180 days old to the Department of Treasury, or report outstanding receivables on the Treasury Report on Receivables in keeping with the Department of the Treasury's debt collection requirements. We identified several outstanding debts that had been delinquent for more than 5 years. We recommend that HUD finalize disputed monetary findings in a timely manner and collect delinquent debts in accordance with the Debt Collection Act.

Untimely Collection of Debts Identified by Postclaim Reviews

HUD relies on postclaim reviews to ensure lenders submitted true, accurate, and supported Federal Housing Administration insurance claims¹³ for foreclosed properties insured by HUD¹⁴. A statistical sample of paid claims submitted by a lender is reviewed. A HUD contractor typically conducts the postclaim reviews. In fiscal year 2003, the postclaim review contractor performed 207 reviews, as of March 2004, of which 176 were closed and HUD collected \$3 million. HUD's Single Family Claims Branch works closely with the postclaim review contractor.

During the review, there were a total of 67 open postclaim reviews totaling \$6.8 million from reviews that occurred in fiscal years 1996, 1997, 1998, 2001, 2002 and 2003 that had not been settled or collected. Eight of the 67 cases, totaling \$3.9 million were under appeal by the lender and being reviewed by the Asset Management Division. Some of the receivables had been unresolved for more than 8 years. We reviewed HUD's processes and procedures to determine whether the Department was resolving disputed postclaim review findings within

¹³ Reported on Form HUD-27011.

¹⁴ Per HUD Handbook 4330.4 REV-1.

a reasonable period and ensuring that outstanding receivables were processed in accordance with the Debt Collection Act.

HUD Provided Lenders Unlimited Opportunities To Submit Additional Documentation To Clear Findings

We found that HUD lacked adequate procedures to resolve disputed monetary findings in a timely manner or actively collect outstanding receivables resulting from postclaim reviews, thus affecting the outstanding time for the collection of debts arising from the reviews. HUD was unable to resolve monetary findings identified during postclaim reviews in a timely manner because: (1) the Claims Branch permitted lenders unlimited opportunities to submit additional documentation to clear findings and (2) the Asset Management Division took an unreasonable length of time to resolve appeals submitted by lenders.

During our audit, we reviewed 10 postclaim reviews performed in fiscal year 2003 to determine why the reviews had not been completed. We found that six lenders had submitted additional documentation in at least three separate responses to HUD's initial report. One of these lenders was up to its eighth response. This caused the resolution process to draw out for about a year in four cases.

When lenders disagree with the postclaim review contractor's findings, the Claims Branch will review the issue and may request additional supporting documentation to make a decision. The Claims Branch permitted lenders an unlimited number of opportunities to submit additional supporting documentation. However, during the audit the Claims Branch changed its resolution process based on our suggestions.

Starting in April 2004, the Claims Branch developed and implemented the following procedures to finalize disputed findings from postclaim reviews in a timely manner:

- Lenders will continue to have 45 days to submit a response to the initial report.
- Based upon the response and the documentation provided, the Claims Branch will issue a new report and revise the findings as appropriate.
- Lenders will then have 21 days to submit any additional response if they choose.
- After 21 days or upon review of the lender's "second response," HUD will send out a final report.

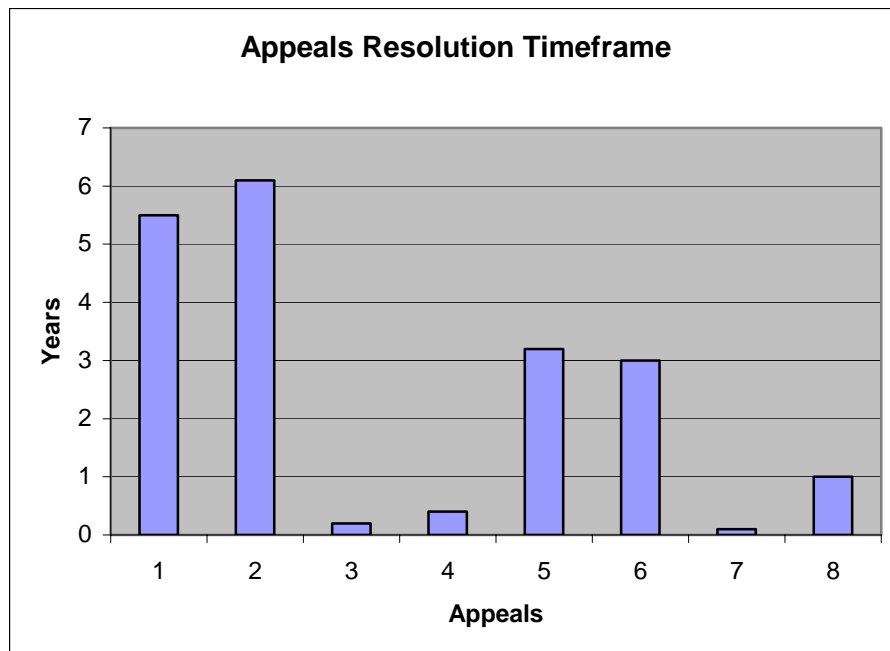
HUD's Appeal Resolution Process Needs Improvement

HUD was also unable to resolve disputed monetary findings from postclaim reviews because the Single Family Asset Management Division took an unreasonable length of time to resolve appeals submitted by lenders. When the lender disagrees with the decision made by the Claims Branch on the postclaim review, it is given the opportunity to take its dispute a step higher to a formal appeal process performed by the Asset Management Division. No collection efforts are made during the appeals process until the Asset Management Division makes a decision.

We selected a non-statistical sample of 15 postclaim reviews from fiscal year 2003 and earlier, with monetary findings totaling almost \$1 million, to determine why the debts were not resolved and collected in a timely manner. We found that 11 postclaim reviews had been under appeal, one of which had no active collection after the appeal was resolved. There were also no active collection efforts made by the Claims Branch on the remaining four cases. Since the lender did not pay the monetary findings and there were no active collection efforts by the Claims Branch for these five cases, they were outstanding for more than 180 days.

We reviewed the files maintained by the Asset Management Division for eight outstanding postclaim reviews¹⁵ that were in an active appeal status. The eight appeals totaled more than \$600,000. We found that six of the eight appeals were not resolved in a timely manner. The chart on the next page depicts the amount of time taken to resolve each appeal by the Asset Management Division. The period represents the time between when the appeal was first referred to the Asset Management Division by the Claims Branch and when the appeal decision was conveyed back to the Claims Branch or the date of our audit if the appeal process was still ongoing.

¹⁵ From the non-statistical sample of 15 postclaim reviews.



Six of the eight appeals totaling \$602,900 were not resolved in a timely manner and were under appeal from 5 months to more than 6 years. Two of these appeals totaling \$314,000 have been outstanding 3 or more years. Two appeals from the same lender, one of which was part of a congressional inquiry, were resolved in a timely manner. For many of these cases, we noticed a significant lack of action by the Asset Management Division. Once the appeal was referred to the Asset Management Division, it remained there until an appeal decision was made. The Claims Branch informed us that it sent numerous email follow-ups and prepared and resubmitted duplicate appeals packages to replace those misplaced by the Asset Management Division.

This lack of action contributed to appeals getting lost, ultimately causing the debt to be forgiven. For example, a decision made by the Claims Branch that was under appeal by the lender was upheld by the Asset Management Division. However, the debt of \$44,225 was forgiven because the appeal was pending for a long time and the Asset Management Division did not maintain documentation supporting the appeal decision. Further, the Claims Branch was not always aware that the lender requested an appeal because the appeal was sent directly to the Asset Management Division.

Asset Management Division staff told us that they try to complete the appeals within 30 days. However, a better system is needed to track, monitor the status of, and document all reviews under appeal. Asset Management Division staff asserted that postclaim appeals and the timeliness of appeal decisions are becoming a priority for them. The Claims Branch has been working with the Asset Management Division to resolve the old outstanding appeals.

HUD Needs To Implement a Process To Actively Collect Outstanding Debt

When HUD made a final decision to conclude the monetary findings, it had not implemented a process to actively collect outstanding receivables, refer receivables more than 180 days old to the Department of the Treasury, or report outstanding receivables on the Treasury Report on Receivables in keeping with the Department of the Treasury's debt collection requirements. We found that five of the fifteen cases in our sample were still outstanding after 180 days because there were no active collection efforts by the Claims Branch. These cases were not referred to the Department of the Treasury and were not reported on the Treasury Report on Receivables. Three of the cases were delinquent for more than 5 years.

Since HUD books a receivable before the dispute resolution process begins, it is difficult to know, without reviewing the case history, at what point HUD created a valid debt. Therefore, we have not quantified the total amount of outstanding debts that were not submitted to the Department of the Treasury within 180 days.

We addressed this issue in our Nationwide Review of Indemnification for Claims on Single Family Insured Loans.¹⁶ We found at that time that HUD relied on administrative offset from a later claim to collect outstanding receivables. When we started this review the Claims Branch was completing our recommendations from the prior audit and had not yet considered whether the outstanding debts from postclaim reviews should be processed in the same manner as debts from indemnified loans.

Consequently, HUD was not following the Debt Collection and Improvement Act of 1996¹⁷ for outstanding debt derived from postclaim reviews. HUD's practice of waiting for an administrative offset did not facilitate active collection efforts, and putting outstanding postclaim review receivables in an administrative delay status prevented receivables outstanding for more than 180 days from being reported on the Treasury Report on Receivables as required.

After we raised the issue, the Claims Branch decided in April 2004 to forward delinquent debts to the Financial Operations Center in Albany, NY for active debt collection efforts, refer outstanding debts to the Department of the Treasury after 180 days, and assure that Department of the Treasury requirements are met. The Claims Branch transferred 38 debts totaling approximately \$1.7 million to the Financial Operations Center, including eight of the 15 outstanding postclaim debts in our sample.

¹⁶ Report Number 2004-DE-0001, issued December 15, 2003.

¹⁷ 31 U.S. Code 3701

As previously mentioned, there were 67 open postclaim reviews totaling \$6.8 million, from reviews that occurred in fiscal year 2003 or earlier, that had not been settled or collected. By the conclusion of our review, HUD had collected more than \$2 million and wrote-off \$2.4 million, most of which was forgiven after reviewing the lenders appeals. Therefore, at the conclusion of our review there were 44 open postclaim reviews totaling \$2.3 million, from reviews that occurred in fiscal year 2003 or earlier, that had not been settled or collected. Thirty-two cases with a balance of \$1.2 million have already been transferred to the Financial Operations Center, four totaling about \$661,000 are still under appeal and the remaining eight totaling about \$418,000 have just been finalized and have not been referred to the Financial Operations Center.

Conclusion

We found that HUD lacked adequate procedures to resolve disputed monetary findings identified during postclaim reviews in a timely manner or actively collect outstanding debts arising from postclaim reviews, thus affecting the outstanding time for the collection of postclaim receivables. As a result, 44 postclaim reviews, performed in fiscal years 2003 and earlier, with an outstanding balance of \$2.3 million had not been settled or collected. Further, HUD failed to collect and transfer to the Department of the Treasury outstanding postclaim receivables over 180 days old in a timely manner and did not properly report all outstanding debts on the Treasury Report on Receivables.

Improvements have been made since we started our review. The Claims Branch has developed and implemented procedures to finalize postclaim reviews in a timely manner. In addition, the Claims Branch began transferring the debt collection process resulting from the postclaim review to the Financial Operations Center to collect the debts in accordance with Treasury requirements. Further, the Asset Management Division started to prioritize postclaim appeals, and the Claims Branch has been working with the Asset Management Division to resolve old outstanding appeals.

Recommendations

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

- 2A. Require the Asset Management Division to develop and implement written procedures to track, monitor the status of, and document all reviews under appeal and ensure that current active appeals of about \$661,000¹⁸ are resolved as quickly as possible.

¹⁸ From fiscal years 2003 and earlier.

- 2B. Require that all debts arising from postclaim reviews are collected in accordance with the debt collection requirements and have the Claims Branch provide us with a timetable for the transition of the remaining outstanding debts of about \$418,000,¹⁶ that are being finalized, to the Financial Operations Center.

- 2C. Ensure that all outstanding postclaim review debts are properly reported on the next Treasury Report on Receivables and have the Claims Branch provide us a copy of the next report.

SCOPE AND METHODOLOGY

During our audit, we reviewed the controls for three claim types: conveyance, preforeclosure and supplemental. Our audit period was fiscal year 2003, and the total claim payments included in the population totaled more than \$7 billion. We analyzed the disbursements and found that the claim payments for principal and interest accounted for 93 percent of the total claims. We focused our audit work on claim disbursements for these two expenses.

The automated controls over principal disbursements include the recalculation of the unpaid principal balance based on the loan terms. Our testing showed that the control was properly working. This control only works for fixed-rate loans, which account for 89 percent of the population. While HUD is unable to automatically verify the unpaid principal balance for variable-rate loans since the Department does not require reporting of such data, lenders must submit supporting documents to the Review and Compliance Specialists in the Claims Branch, who then validate the amount. The postclaim reviews have not found any problems in this area so we did not perform additional work on this control.

The second largest claim expense is for interest, which was \$600 million in fiscal year 2003. HUD's automated system edits and controls curtailed \$70 million of debenture interest because lenders did not meet certain foreclosure processing timeframes. Further, lenders who did not meet HUD's requirements self-curtailed the debenture interest they claimed by \$90 million.

To identify disallowed and unsupported costs, HUD relies on a postclaim review process, through which a statistical sample of claims submitted by a lender is reviewed. We summarized the postclaim review monetary findings for 176 closed postclaim reviews performed in fiscal year 2003 and found that \$839,600 of the total \$1.9 million¹⁹ in findings were the result of lenders failure to (1) process foreclosures within HUD's timeframes and (2) self-curtailed accrued interest on the claims. We performed additional work in this area to estimate the amount of disallowed interest payments to determine the benefit HUD could realize if it improved its policies, procedures, and systems.

We performed additional analyses to estimate the total amount of disallowed interest paid by HUD in a 3-year period, October 1, 2000 through September 30, 2003, for lenders who exceeded the reasonable diligence timeframe without a valid reason or failed to report to HUD the institution of foreclosure in a timely manner. Due to the limitations of data collected by HUD, we compared a sample of postclaim reviews²⁰ with our analysis to identify an error rate that we could apply to our analysis to estimate the amount of disallowed interest not reported by lenders.

¹⁹ The amount is based on the original finding amounts and excludes the amount extrapolated to the population from which the sample was selected. HUD billed lenders more than \$3.1 million for the 176 postclaim reviews, as of March 31, 2004.

²⁰ We selected a non-statistical of sample of 2,100 conveyance claims reviewed by the postclaim review contractor in fiscal year 2003. The sample was reduced to 1,700 when analyzing the timely completion of foreclosure results because we dropped cases in which the bankruptcy release date occurred after the institution of foreclosure date.

If the borrower files bankruptcy that runs concurrently with the foreclosure, the number of days in bankruptcy is added to the reasonable diligence timeframe. Only the latest bankruptcy release date is reported on the claims form. In some cases borrowers, have filed numerous bankruptcies. We excluded from our analysis cases in which the bankruptcy release date occurred after the institution of foreclosure date, because cases with long bankruptcies would skew the results. This reduced the population by 20 percent.

Some States have different timeframes for judicial and non-judicial foreclosures. Lenders do not currently report to HUD the type of foreclosure. To be conservative, if a State had two different timeframes, we used the longest period for our analysis.

When we verified the results from our analysis of the reasonable diligence requirements, the primary reasons for discrepancies between our analysis and the postclaim review were:

- 1) The vacancy occurred after the foreclosure was complete and the vacancy date was reported by lenders instead of marketable title date and
- 2) Lenders had a valid reason for the delay.

When we verified the results from our analysis of the reporting requirements, the primary reasons for discrepancies between our analysis and the postclaim review were:

- 1) Lenders were over penalized because the postclaim review contractor did not have the reporting history for the case and the lender did not have sufficient documentation to show it reported to HUD on an different date than the date identified in the review. Also, in some cases we picked up an earlier reporting date because we took a more conservative approach as described above.
- 2) The lender reported incorrect dates to HUD on the claim form.
- 3) The lender provided documentation to the postclaim reviewer showing that they reported to HUD; however, the default monitoring system did not have the report.
- 4) An incorrect reporting code was accepted by the postclaim reviewer.

While reviewing the postclaim reviews during the audit, we identified several cases in which the Claims Branch permitted the lender numerous opportunities to submit additional documentation to resolve a finding. We also found 45 reviews with an outstanding balance of almost \$1.8 million that were more than 180 days old, some of which were 8 years old. We selected a non-statistical sample of 15 postclaim reviews from a universe of 67 open postclaim reviews to identify causes for these delays. This sample included eight postclaim reviews that were currently under appeal. The review of these cases showed that HUD books a receivable before the dispute resolution process begins. Consequently, it is difficult to know, without reviewing the case history, at what point HUD created a valid debt. Therefore, we did not quantify the total amount of outstanding debts that were not submitted to the Department of the Treasury within 180 days.

To achieve our audit objectives, we examined HUD records at the Single Family Claims Branch and Asset Management Division at 451 7th Street SW, Washington DC 20410 and the Financial Operations Center, 52 Corporate Circle, Albany, NY 12203, relating to HUD's postclaim review

resolution and collection process. We also reviewed records maintained by the postclaim review contractor, Walker & Company, LLC, 4200 Wisconsin Avenue, NW, Suite 300, Washington, DC 20016. We conducted interviews with HUD officials, employees, and contractors.

To review the disbursement process we analyzed information from the Single Family Data Warehouse, which contained data relevant to our review from the Single Family Insurance System – Claims Subsystem and Single Family Default Monitoring System. In addition, to review the debt collection process, we analyzed data from the Accounts Receivable Subsystem. We assessed the reliability of the data from these systems to ensure the data were sufficiently reliable to base our audit conclusions.

Our audit generally covered the period of October 1, 2000 through September 30, 2003. However, when applicable, the audit period was expanded to include current data through September 2004. We conducted our fieldwork from March through August 2004.

We performed our review in accordance with generally accepted government auditing standards, which included tests of internal controls that we considered necessary to our audit objectives.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

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

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives; the processes and procedures for planning, organizing, directing and controlling program operations; and the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- HUD's automated system and edit checks for Federal Housing Administration-insured Single Family conveyance claim disbursements and the postclaim payment review of paid disbursements;
- The policies and procedures established by HUD to resolve disputed monetary findings resulting from postclaim reviews; and
- The policies and procedures established by HUD to collect outstanding postclaim review receivables, report all receivables to the Department of the Treasury as required, and transfer all receivables more than 180 days to the Department of the Treasury as required by the Debt Collection Act.

We assessed the relevant controls identified above.

Significant Weakness

A significant weakness exists if internal controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Based on our review, we believe significant weaknesses exist in three areas:

- Measurable performance goals are needed to ensure HUD is taking the appropriate actions to bring the level of compliance to a level desired by HUD. (finding 1),
- Postclaim review dispute resolution process (finding 2), and

- Compliance with the Debt Collection Act (finding 2).

The deficiencies are discussed in detail in the Results of Audit section of this report.

APPENDIXES

Appendix A

SCHEDULE OF FUNDS TO BE PUT TO BETTER USE

Finding Number	Funds To Be Put To Better Use 1/
1	\$28.2 Million
2	\$2.3 Million ²¹

1/ “Funds to be put to better use” are quantifiable savings that are anticipated to occur if an Office of Inspector General (OIG) recommendation is implemented, resulting in reduced expenditures at a later time for the activities in question. This includes costs not incurred, deobligation of funds, withdrawal of interest, reductions in outlays, avoidance of unnecessary expenditures, loans and guarantees not made, and other savings.

²¹ HUD took proactive measures during the audit to address our recommendations by transferring most of the finalized outstanding monetary findings and penalties from the postclaim reviews. Of the \$2.3 million that has not been settled or collected, \$1.2 million has been transferred to the Financial Operations Center, \$660,000 is still under appeal, and \$418,000 is being finalized and has not been transferred.

Appendix B

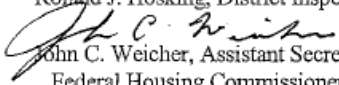
AUDITEE COMMENTS



ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

MAR 17 2005

MEMORANDUM FOR: Ronald J. Hosking, District Inspector General for Audit, SAGA
FROM:  John C. Weicher, Assistant Secretary for Housing-
Federal Housing Commissioner, H
SUBJECT: Response to Office of Inspector General (OIG) Internal Audit
of Federal Housing Administration Claim Payments

Thank you for the opportunity to review and comment on your draft audit report on Federal Housing Administration Claim Payments. Attached to this memorandum is HUD's response to the recommendations outlined in the report.

If you have any questions regarding this response, please contact Joseph McCloskey, Acting Deputy Assistant Secretary of Single Family Housing, at (202) 708-2733.

Attachment



HUD's Response to Findings and Recommendations

Finding 1: Measurable Performance Goals Are Needed To Ensure a Desirable Level of Lender Compliance Is Achieved

The Office of Inspector General (OIG) believes that this finding resulted in “Disallowed interest for Untimely Completion of Foreclosure.”

Recommendation 1A: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner establish and implement performance goals for the default monitoring requirements that HUD expects lenders to meet, by utilizing existing data to the extent possible.

HUD's Response: The Office of Single Family Asset Management agrees with this recommendation. HUD currently measures compliance with its default monitoring requirements at the case level and periodically revises its goals through issuance of mortgagee letters. A new mortgagee letter will be soon be issued to announce updated reporting requirements for HUD's Single Family Default Monitoring System (SFDMS). It will also include revised guidance related to the proper evaluation of the Notice of Foreclosure reporting requirement. Where mortgagees have failed to properly report the Notice of Foreclosure, they shall be reminded of the requirement to self-curtail the claim for insurance benefits. With respect to monitoring efforts, currently, a report generated using both claim and SFDMS data is used by the post claim reviewers to identify cases in the audit universe where it appears that initiation of foreclosure was not reported at all. This report will be updated to provide the post claim review staff a better tool to identify those cases where the notice of foreclosure was either not reported or was not reported timely.

The Department is currently undergoing rulemaking to require mortgagees to report earlier in the delinquency cycle, and is in the final decision phases for a new Task Order to update SFDMS to accommodate this increased reporting. The planned expansion of SFDMS will allow the Department to begin tracking delinquencies at the point where the loans are 30 days or more delinquent, rather than the current process where the delinquency reporting begins where the loans are 90 days or more delinquent. In addition, the planned SFDMS enhancements will allow mortgagees to begin advising the Department when the foreclosure sale is held, when the mortgagee has title and when the eviction is completed. This new information will enable the Department to develop realistic goals for compliance with reporting requirements and will improve the Department's ability to monitor compliance with those goals.

Past experience has shown that the industry complies with our rules when monetary sanctions are pending. We also agree to issue a mortgagee letter reminding the industry of the importance of accurate default reporting to the Department and will also alert the industry that, if our objectives for accurate reporting are not achieved within a specified time frame, we will implement more

stringent enforcement actions including changes in both the SFDMS reporting requirements as well as within the post claim review process.

Recommendation 1B: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner create and implement a plan to obtain additional information necessary for HUD to establish performance goals and accurately measure lender performance for the foreclosure completion timeframes, or in the absence of additional information, alternative methods for measuring lender performance.

HUD's Response: The Department agrees with this recommendation. HUD will soon issue a new mortgagee letter that will update the reasonable diligence time frames and provide new guidance to mortgagees regarding the requirement to self-curtail the claim for insurance benefits when HUD performance goals are not met. The Department will also develop a new report that will assist the post claim review staff in identifying those cases in the audit universe that are most at risk of having failed to meet HUD's reasonable diligence requirements.

Establishing overall compliance goals to measure lender performance in a given period is more difficult as there are many complicating factors beyond the mortgagee's control that may extend the time required to complete foreclosure yet the mortgagee would still be considered to be in compliance with HUD's requirements. Further, there are voluntary actions, such as utilization of loss mitigation, that automatically extend normal reasonable diligence time frames but which should be encouraged. As an alternative to fixed percentage goals for lender compliance, a plan will be developed that will utilize existing data in the SFDMS and Single Family Claims systems to create exception reports to target mortgagees whose overall performance against HUD's foreclosure timelines is outside of reasonable norms.

Recommendation 1C: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner create and implement a plan of additional actions that HUD will take to encourage lenders to meet performance goals that may include:

- Automating the curtailment of interest;
- Using exception reports to bill lenders for interest that was not self-curtailed;
- Using exception reports to perform targeted reviews; and/or
- Taking other actions, such as the use of incentives for lenders who improve performance or penalties or other sanctions for lenders who fail to improve.

HUD's Response: The Department agrees with the majority of these recommendations and will develop plans for the implementation of all items it believes are practical and appropriate.

- As stated previously, a plan will be developed that will identify the additional data that may be collected through the planned expansion of SFDMS reporting to provide the post claim review staff with new reports. These reports will be designed to assist in identifying those accounts where the mortgagee has apparently failed to self curtail for

either missing the reasonable diligence time frame or has apparently failed to report the notice of foreclosure. To some extent, these reports may be used to perform targeted post claim reviews.

- The Department has engaged contractor support to review and update its current Tier Ranking Scoring procedures that may become the basis for providing additional incentive payments to the top performing lenders. Other factions of the mortgage industry (e.g., Freddie Mac & Fannie Mae) currently include a component that incorporates compliance with default reporting in their overall lender scoring. Therefore, the Department will consider incorporating, default reporting compliance as a part of the scoring.
- The Single Family Post Insurance Division reviewed open and closed post claim reviews for fiscal year 2003 and confirmed that the post claim review process will recover at least the amount that it is estimated would be saved by automating this activity. This results from the broad coverage of post claim reviews, the statistical selection of the sampled cases, and the extrapolation of the sample results for this audit finding to the universe of paid claims.
- Finally, Housing recognizes that there would be clear advantages to an automated process rather than the current process of recovery via post claim review if the timeframes that were being measured were uniform, with little or no exceptions or variations. However, due to variations in state foreclosure laws, some foreclosures are completed and the properties conveyed before the actual expiration of the Notice of Foreclosure reporting requirement. This, along with the complications brought to individual cases due to bankruptcy filings, results in a very large volume of claims that will not process correctly and would require manual exception processing by HUD staff in the Claims Branch.

Additionally, automating compliance to the Notice of Foreclosure regulation will require, at a minimum, a real time interface with HUD's SFDMS, as well as complex programming. Therefore, given extremely limited human and programming resources, we cannot commit to implement this recommendation at this time. However, we will continue to explore all options, including increased automation, which will make these processes more efficient.

Finding 2: HUD's Procedures for Resolving disputed Monetary Findings and Debt Collections are Inadequate

Recommendation 2A: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner require the Asset Management Division to develop and implement written procedures to track, monitor the status of, and document all reviews under appeal and ensure that current active appeals of \$661,000 are resolved as quickly as possible.

HUD's Response: HUD agrees with this recommendation. As of December 15, 2004, there are only two cases under appeal with a value of \$283,490.48. The Office of Single Family Asset Management recently updated internal procedures to establish processing protocols and timeframes. The procedures have been completed and are attached.

Recommendation 2B: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner require that all debts arising from post claim reviews are collected in accordance with the debt collection requirements and have the Claims Branch provide us with a timetable for the transition of the remaining outstanding debts of \$418,000, that are being finalized, to the Financial Operations Center.

HUD's Response: HUD agrees with this recommendation. In early 2004, the Office of Financial Services (OFS) decided to transfer receivable processing for post claim review audits from the Single Family Post Insurance Division to the Albany Financial Operations Center (AFOC). This decision was made to address problems with post claim review receivables that were revealed as part of the HUD OIG's audit of indemnification agreement receivables. OFS' internal agreement provided that dates for this conversion would not be established until the transfer of the indemnification receivable processing to Albany was substantially completed.

A timetable for the transfer of post claim receivables was established in November 2004. Changes to existing receivable processes were necessary to incorporate new methods of processing post claim reviews. When the post claim review contract was re-awarded in September 2004, the requirements for reviews were changed to reduce the amount of time the reviews could remain open before issuance of the report and establishment of the final receivables.

Our current plans are that all post claim review receivables resulting from the new post claim contract will be initially billed and subsequently tracked and reported in Albany. HUD anticipates the first receivable from this process will be created in the January - February 2005 timeframe.

The open post claim receivables from past post claim review contracts will remain in the Single Family Claims System accounts receivable (A/R) sub-system until they are collected or reach 150 days old. At 150 days, any open receivables will be transferred to the AFOC. This will allow the AFOC 30 days to process the receivables into the Treasury collection process in order to meet the 180-day requirement. Given the age of existing receivables, this conversion will be completed not later than June 30, 2005.

Recommendation 2C: It is recommended that the Assistant Secretary for Housing-Federal Housing Commissioner ensure that all outstanding post claim review debts are properly reported on the next Treasury Report on Receivables and have the Claims Branch provide us a copy of the next report.

HUD's Response: Single Family Housing agrees with this recommendation. Subsequent to the transfer of this activity to the Albany Financial Operations Center (FOC), outstanding receivables for post claim reviews will only be reported on the Treasury Report of Receivables produced by the FOC. As of the reporting period ending on June 30, 2005, this reporting will be accurate and complete.