



Issue Date	October 25, 2006
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Audit Report Number	2007-KC-1002
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TO: Brian D. Montgomery, Assistant Secretary for Housing – Federal Housing Commissioner and Chairman, Mortgage Review Board, H

//signed//

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

SUBJECT: Manufactured Home Lending by Wells Fargo Home Mortgage,  
West Des Moines, Iowa

## **HIGHLIGHTS**

### **What We Audited and Why**

We audited Wells Fargo Home Mortgage (Wells Fargo) because it is the largest Title II manufactured housing lender in the U.S. Department of Housing and Urban Development's (HUD) Region VII and the second largest in the nation. We focused on Title II manufactured housing loans due to the high risk that the properties had mortgages insured by the Federal Housing Administration without meeting insurance requirements.

Our objectives were to determine whether Wells Fargo originated, sponsored, or purchased manufactured housing loans that were underwritten in accordance with HUD requirements and whether insured loans met HUD permanent foundation requirements specific to Title II manufactured housing loans.

### **What We Found**

Wells Fargo did not comply with HUD regulations, procedures, and instructions when underwriting 1 of 11 Federal Housing Administration-insured loans reviewed. The property for the loan was not eligible for insurance because its foundation did not meet HUD requirements, and Wells Fargo did not provide

HUD with all required certifications when submitting the loan for insurance. As a result, HUD insured one loan that unnecessarily placed the insurance fund at risk, causing HUD to incur a loss of \$64,612.

### **What We Recommend**

We recommend that the assistant secretary for housing – federal housing commissioner require Wells Fargo to reimburse HUD for one loan on which HUD incurred a loss of \$64,612 (see appendix C).

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**

Wells Fargo agreed with our conclusions. We provided the draft report to Wells Fargo on October 19, 2006, and requested a response by October 23, 2006. Wells Fargo provided written comments on October 23, 2006.

The complete text of the auditee's response can be found in appendix B of this report.

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## **BACKGROUND AND OBJECTIVES**

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Wells Fargo Home Mortgage (Wells Fargo) is a wholly owned subsidiary of Wells Fargo and Company and maintains its headquarters in West Des Moines, Iowa. The U.S. Department of Housing and Urban Development (HUD) approved Wells Fargo as a supervised direct endorsement lender on December 16, 1985. The Federal Housing Administration provides mortgage insurance on (endorses) loans made by approved lenders. The mortgage insurance protects lenders such as Wells Fargo against losses when homeowners default on their mortgage loan.

According to HUD's Single Family Data Warehouse system, Wells Fargo originated or sponsored 3,847 Title II manufactured housing loans that closed between July 1, 2004, and December 31, 2005. HUD's system also showed that Wells Fargo purchased 9,339 Title II manufactured housing loans after endorsement that closed during the same period.

HUD has established requirements that lenders must follow when underwriting a loan for it to qualify for Federal Housing Administration insurance. HUD also has specific requirements that manufactured housing permanent foundations must meet for the property to be eligible for insurance.

When submitting a manufactured housing loan for Federal Housing Administration insurance, the lender is responsible for ensuring that it

- Obtains an engineer's certification confirming that the permanent foundation complies with HUD requirements,
- Obtains a property appraisal from an appraiser that it must hire from HUD's approved Federal Housing Administration appraiser roster,
- Provides the engineer's certification to the appraiser before the property appraisal is conducted,
- Monitors the work of the appraiser as part of its quality control plan, and
- Obtains a compliance inspection for all new and proposed construction. The lender may use its own staff inspector or a fee inspector assigned by HUD.

Our objectives were to determine whether Wells Fargo originated, sponsored, or purchased manufactured housing loans that were underwritten in accordance with HUD requirements and whether insured loans met HUD permanent foundation requirements specific to Title II manufactured housing loans.

## RESULTS OF AUDIT

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### Finding 1: Wells Fargo Underwrote One Title II Manufactured Housing Loan for a Property with an Ineligible Foundation

Wells Fargo insured one Title II manufactured housing loan on a property with a foundation that did not meet HUD requirements. The property failed four of five structural areas inspected. As a result, HUD insured a loan that did not meet HUD requirements, causing an unnecessary loss of \$64,612 to the Federal Housing Administration insurance fund.

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#### Wells Fargo Underwrote a Loan with an Ineligible Foundation

Wells Fargo did not ensure that the foundation of one Title II manufactured housing unit met HUD requirements before submitting the \$103,290 loan to HUD for endorsement. As a result, HUD insured the loan for a property with an ineligible foundation.

HUD Handbook 4145.1, chapter 3, paragraph 4, states that manufactured homes for Title II mortgage insurance must have, with or without a basement, a site-built permanent foundation that complies with HUD Handbook 4930.3G, Permanent Foundations Guide for Manufactured Housing. The guide contains specific requirements for designing and constructing a permanent foundation so that a property qualifies for Federal Housing Administration insurance.

We inspected the property for compliance with HUD requirements specific to five areas: skirting, perimeter, piers, footings, and anchor straps. The property failed four of the five structural areas inspected. The anchor straps were satisfactory. Appendix C provides a detailed explanation of inspection results and HUD requirements.

#### **Skirting**

HUD requires Title II manufactured homes to have skirting that is permanent or attached to a permanent foundation. The property did not have skirting that met HUD requirements. The following inspection photograph shows that the skirting was not permanent or attached to a permanent foundation.



### **Perimeter**

HUD requires Title II manufactured homes to have a permanent perimeter wall to exclude entry of water and vermin. The property did not have an adequate permanent perimeter wall. The wall was thin vinyl siding with holes throughout that would allow entry of water and vermin. There were no reinforcement rods permanently attaching the perimeter wall. The following inspection photographs show the failed perimeter wall.



### **Piers**

HUD requires Title II manufactured homes to have piers that have mortared bed and head joints (i.e., dry-stacked piers are not permitted). The property piers did not have mortared bed and head joints. The following inspection photograph shows that the piers were dry stacked.



### **Footings**

HUD requires Title II manufactured homes to have reinforced concrete footings under the piers and perimeter wall. The property did not have reinforced concrete footings under the perimeter wall, as the following photograph shows.



### **Required Certifications**

Wells Fargo did not provide HUD with all required certifications when submitting the loan for insurance. HUD requires a professional engineer's certification of the foundation for all Title II manufactured homes. The certification is to show that the foundation plans and specifications met HUD foundation requirements. Wells Fargo was also unable to provide the engineer's certification in response to our audit.

### **Conclusion**

Wells Fargo did not ensure that the foundation of one Title II manufactured housing unit met HUD requirements before endorsement. Therefore, HUD insured the \$103,290 loan for a property with an ineligible foundation. HUD incurred a loss of \$64,612 on the loan when the borrower defaulted and HUD sold the property.

## **Recommendation**

We recommend that the assistant secretary for housing – federal housing commissioner and chairman, Mortgagee Review Board,

- 1A. Require Wells Fargo to reimburse HUD for one loan on which HUD incurred a loss of \$64,612 when it sold the property (see appendix C).

## SCOPE AND METHODOLOGY

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In conducting our audit, we evaluated Title II manufactured housing loans originated, sponsored, or purchased after endorsement by Wells Fargo. Wells Fargo is the largest Federal Housing Administration manufactured housing lender in HUD's Region VII and the second largest lender of such loans in the nation. This report addresses our results specific to loans that Wells Fargo originated or sponsored because Wells Fargo is directly responsible for ensuring that these loans comply with HUD requirements. We will address our results specific to loans that Wells Fargo purchased after endorsement in a separate report because lenders other than Wells Fargo are responsible for these loans.

To address our objectives, we obtained and reviewed the HUD and Wells Fargo loan files. We reviewed HUD's underwriting requirements and its permanent foundation requirements for Title II manufactured housing loans. We reviewed previous HUD Office of Inspector General (OIG) reports related to Title II manufactured housing. We also reviewed Wells Fargo's internal reports on its manufactured housing portfolio.

We interviewed HUD headquarters and Denver Homeownership Center staff and Wells Fargo staff that oversee its underwriting functions, including a group designated to manufactured housing. We also performed on-site foundation inspections. To ensure that we conducted the inspections properly, we provided the results of our seven initial inspections (i.e., field notes and photographs), to a HUD Office of Manufactured Housing engineer. The engineer confirmed our inspection approach and agreed with our conclusions that the seven foundations failed to meet HUD requirements. We completed the remaining on-site inspections using the same approach confirmed by the engineer.

### **Underwriting Review**

According to HUD's Single Family Data Warehouse system, Wells Fargo originated or sponsored 3,832 Title II manufactured housing loans that closed between July 1, 2004, and December 31, 2005. According to Wells Fargo's data system, it had originated or sponsored only 2,327 Title II manufactured housing loans during the same period. We compared the two sets of loans and identified the following differences:

- 1,233 loans were in the HUD and Wells Fargo systems as manufactured housing,
- 2,599 loans were in the HUD system but not in the Wells Fargo data system, and
- 1,094 loans were in the Wells Fargo data system but not in HUD's system.

We initially reviewed 10 loans for compliance with HUD underwriting regulations, all of which were originated or sponsored by Wells Fargo. Of the 1,233 loans appearing in both systems as manufactured housing loans, two were in claims status. We selected these loans for our underwriting review because they had caused a loss to the insurance fund. Of the 1,094 loans in Wells Fargo's system but not in HUD's system, two were in claims status. We selected these loans for review due to the losses incurred by HUD. We also selected six actively insured loans from the group of 1,094 loans, using a representative, nonstatistical selection method. We did not select any loans from the group of 2,599 loans.

In addition, HUD's data system showed that Wells Fargo had purchased 8,646 loans after endorsement during the same 18-month period, but Wells Fargo's data showed that it had purchased 9,795 loans. We compared the two data systems and determined that there were 6,635 loans that both systems showed were purchased by Wells Fargo after endorsement.

We reviewed 18 additional loans for compliance with HUD underwriting regulations, all of which Wells Fargo purchased after endorsement. Of the loans that Wells Fargo purchased after endorsement, 44 were in claims status, and 428 were in default. We selected 10 loans from the group of 44 loans in claims status, selecting the 10 loans with the highest original mortgage amount because these loans represent the highest risk to HUD. From the group of 428 loans in default, we selected another eight loans for review, selecting the loans with the highest original mortgage amount.

### **Foundation Inspections**

According to HUD's Single Family Data Warehouse system, Wells Fargo originated, sponsored, or purchased after endorsement 12,478 Title II manufactured housing loans that closed between July 1, 2004, and December 31, 2005. According to Wells Fargo's data system, it had originated, sponsored, or purchased 12,122 such loans during the same period. We compared the two sets of loans and identified the following differences:

- 7,868 loans were in the HUD and Wells Fargo systems as manufactured housing,
- 4,610 loans were in the HUD system as manufactured housing but not in the Wells Fargo data system, and
- 4,252 loans were in the Wells Fargo data system as manufactured housing but not in HUD's data system as manufactured housing loans.

This resulted in identifying 16,730 loans that at least one of the data systems identified as Federal Housing Administration manufactured housing loans.

From the group of 16,730 loans, we identified 67 loans in claims status. Ten of these loans were originated or sponsored by Wells Fargo, and 57 were purchased by Wells Fargo after endorsement. Using the property locations from HUD's system data, we identified geographical clusters of the 67 properties. Based on these clusters, we selected 43 loans in Texas for foundation inspections.

We conducted on-site inspections of the permanent foundations of 33 of the 43 properties selected for review. Wells Fargo sponsored the loan for 1 of the 33 properties inspected. The additional 32 loans were originated or sponsored by 11 other lenders. We inspected the properties for compliance with HUD requirements specific to five areas: skirting, perimeter, piers, footings, and anchor straps. We did not inspect 10 properties because we could not gain adequate access to nine properties and one property was not a manufactured home.

We conducted tests of the Single Family Data Warehouse information and the Wells Fargo system data to establish the level of reliance that we could place on the two sets of data, including the identification of loans as manufactured housing loans. We found the Single Family Data Warehouse data adequate to meet our audit objectives but found the Wells Fargo system data unreliable. Therefore, we relied on HUD's data to reach our conclusions.

We did not assess Wells Fargo's underwriting controls because we identified only one improperly underwritten loan and one loan with an ineligible permanent foundation that were the responsibility of Wells Fargo. In addition, the majority of the loans reviewed and permanent foundations inspected were not the responsibility of Wells Fargo.

We conducted audit work at Wells Fargo's offices, located in Des Moines, Iowa, and Minneapolis, Minnesota, and conducted on-site foundation inspections in multiple locations in Texas. We performed our audit work from January through July 2006. We conducted the audit in accordance with generally accepted government auditing standards, except as noted.

## APPENDIXES

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### Appendix A

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

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Recommendation number	Ineligible 1/
1A	\$64,612

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.

## Appendix B

### AUDITEE COMMENTS

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MAC X9903-022  
2650 Wells Fargo Way  
2nd Floor, West Building  
Minneapolis, MN 55467-0001

October 23, 2006

Ronald J. Hosking  
Regional Inspector General for Audit  
Office of Inspector General  
Gateway Tower II - 5<sup>th</sup> Floor  
400 State Avenue  
Kansas City, KS 66101-2406

Re: FHA File #: 492-7299317  
Wells Fargo # 0140533696  
[REDACTED]

Dear Mr. Hosking:

We have received your letter of October 6, 2006 regarding the above referenced loan that was closed as an FHA loan on October 19, 2004 and sponsored by Wells Fargo Bank. We have reviewed our loan origination files and the inspection photos and certifications on the disc enclosed in your letter.

Wells Fargo Home Mortgage proud of the fact that the quality of WFHM's FHA-insured originations exceeds the industry average and that HUD recognizes us as the largest servicer with a Tier 1 ranking. We are justifiably proud of our record of originating good-quality Federal Housing Administration (FHA) loans and of our efforts to comply with HUD's origination, underwriting and servicing standards.

While the loan cited in your recent letter failed to meet several HUD requirements, we are confident that it represents an isolated departure from these standards. As the leading originator of Government National Mortgage Association (GNMA) loans for the past several years, WFHM values its relationship with HUD and is committed to continuing to improve its origination, underwriting and servicing operations and processes. As a result, we take very seriously any individual case where we did not meet HUD requirements and look to ensure that we address any issues. The following outlines the failed ratings and WFHM response

**Skirting – Failed**

Skirting was not permanent or attached to a permanent foundation. Skirting was thin vinyl siding with several bulges, tears, and holes throughout. Skirting was missing in several places. Several holes underneath skirting that showed no footing.

**WFHM Response**

At the time the appraisal was completed on October 8, 2004, the appraiser required that skirting be repaired or replaced on the left and right side of the unit. Inspection Report shows that the skirting damage was repaired. It is likely the additional damage showing on the disc photo occurred over a period of time, after the loan closed and prior to the time the disc photos were taken.

October 23, 2006

Re: FHA Case number: 492-7299317 / WF # 0140533696

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**Perimeter - Failed**

No permanent perimeter wall. The perimeter wall was made of thin vinyl siding. No reinforcement rods were evident. The vinyl was sitting on top of the finished grade and had several gaps and holes throughout that would allow water and vermin entry into the crawl space. No foot under perimeter wall was evident.

**WFHM Response**

We agree that the photos indicate the perimeter does not meet the HUD requirements for reinforcement rods and shows the perimeter wall was sitting on the finished grade in some places.

**Piers – Failed**

Piers were constructed of concrete blocks that were dry stacked (not mortared) and installed under the chassis beams. Some piers were sitting on poured concrete footings and some were sitting on top of the finished grade with no visible footing. Wood shims were used to level piers under chassis.

**WFHM Response**

We agree that the piers do not appear to be constructed properly and some are not sitting on poured footings but rather placed on the finished grade. We agree that the wood shims shown are not acceptable.

**Footings – Failed**

No footing under perimeter wall. Wall was thin vinyl skirting sitting on top of finished grade. Some piers were sitting on poured concrete footings but we could not determine the depth. Some piers were sitting on finished grade with no visible footing.

**WFHM Response**

We agree that the footings do not meet the HUD requirements for manufactured homes and some were missing.

To summarize, we agree with all the deficiency findings except the skirting. While skirting damage was present at the initial inspection, appropriate repairs were ordered. The damage evident in the photos you provided appears to have occurred after loan closing and the skirting was not subsequently repaired by the homeowner.

Wells Fargo Bank team members are aware of the requirement to obtain an engineer's certification to meet the HUD requirements for manufactured home foundations and we believe this was an isolated oversight. We communicate any deficiencies such as these noted to the appropriate underwriting and compliance staff in ongoing conference calls and monthly reports and establish action plans for those more egregious or repetitive findings. In addition, we will reiterate this requirement in an upcoming communication to our field site offices.

October 23, 2006

Re: FHA Case number: 492-7299317 / WF # 0140533696

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Sincerely,

A handwritten signature in black ink, appearing to read 'K Lofrano', written in a cursive style.

Kurt Lofrano  
Vice President Credit Risk Management

CC: Lew Raccio  
Michael Schimek

## Appendix C

### CASE STUDY OF IMPROPERLY UNDERWRITTEN LOAN

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Case number: 492-7299317

Section of Housing Act: 203(b)

Date of loan closing: October 19, 2004

Insured amount: \$103,290

Date of inspection: May 11, 2006

HUD costs incurred:

**\$64,612 loss on sale of property**

#### **Skirting - Failed**

Skirting was not permanent or attached to a permanent foundation. Skirting was thin vinyl siding with several bulges, tears, and holes throughout. Skirting was missing in several places. Several holes beneath skirting showed no footing.

#### **Perimeter - Failed**

There was no permanent perimeter wall. The perimeter wall was made of thin vinyl siding. No reinforcement rods were evident. The vinyl was sitting on top of the finished grade and had several gaps and holes throughout that would allow water and vermin entry into the crawl space. No footing under perimeter wall was evident.

#### **Piers - Failed**

Piers were constructed of concrete blocks that were dry stacked (not mortared) and installed under the chassis beams. Some piers were sitting on poured concrete footings, and some were sitting on top of the finished grade with no visible footing. Wood shims were used to level piers under chassis.

#### **Footings - Failed**

There was no footing under the perimeter wall. The wall was thin vinyl skirting sitting on top of finished grade. Some piers were sitting on poured concrete footings, but we could not determine the depth.

#### **HUD Requirements**

HUD Permanent Foundations Guide for Manufactured Housing, section 100-1-C-d, requires vertical stability, including that the foundation enclose a basement or crawl space with a continuous wall (whether bearing or nonbearing) that separates the basement or crawl space from the backfill and keeps out vermin and water.

HUD Handbook 4145.1, chapter 3-4, section 5, states that there must be a properly enclosed crawl space with a continuous permanent foundation-type construction (similar to a conventionally built foundation; i.e., concrete, masonry or treated wood). The perimeter enclosure, if separate from supporting the foundations, must be adequately secured to the

perimeter of the unit to exclude entry of vermin and water and allow proper ventilation of the crawl space.

HUD Permanent Foundations Guide for Manufactured Housing, sections 503-2B and 503-4, require that the minimum thickness for a pier be eight inches. All masonry piers and walls shall have mortared bed and head joints. In addition, sections 503-1B, 503-2, and 503-2B require that footings for pier foundations be reinforced concrete and placed below the frost penetration depth. The minimum reinforced concrete footing thickness will be six inches or 1.5 times the length of the footing projection from the foundation wall, whichever is greater. The minimum thickness for a pier footing is eight inches or 1.5 times the length of the footing projection from the pier, whichever is greater.

HUD Handbook 4145.1, chapter 3-4, section C, states that the foundation design information in HUD's Permanent Foundations Guide for Manufactured Housing may be used to verify the design of the existing system. The lender must provide a structural engineer's certification to verify compliance with the handbook guidelines and with the requirements set forth in section B of the handbook.

HUD Handbook 4150.2, chapter 8-1, states that the manufactured home must be erected on a permanent foundation in compliance with the Permanent Foundations Guide for Manufactured Housing. All proposed or newly constructed manufactured homes must meet the standards set forth in the guide. A licensed professional engineer's seal and signature (certification) is required to indicate compliance with the guide. The lender should furnish the appraiser with a design engineer's inspection of the foundation before the appraisal.

HUD Handbook 4060.1, chapter 6-3-E and F, states that the lender's quality control program must provide for the review of a representative sample of a lender's loans. This review must evaluate the accuracy and adequacy of the information and documentation used in reaching decisions in either the origination or servicing processes.

HUD Handbook 4060.1, chapter 6-7-B, states that the lender's quality control program must provide for a review of mortgage loan files to evaluate the loan origination and underwriting functions.