



Issue Date January 20, 2005
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Audit Case Number 2005-PH-1005
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TO: John C. Weicher, Assistant Secretary for Housing - Federal Housing  
Commissioner, H

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

SUBJECT: Fleet National Bank, Philadelphia, PA - Mortgagee Review. Fleet National  
Bank Issued and Submitted for Endorsement Loans With an Increased Risk of  
Defaults and Claims

## **HIGHLIGHTS**

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

We audited the Philadelphia branch of Fleet National Bank (Fleet), a supervised direct endorsement lender approved to originate Federal Housing Administration (FHA) single family mortgage loans. We selected Fleet for audit because it had a high default rate. Our objectives were to determine whether Fleet complied with the U.S. Department of Housing and Urban Development's (HUD) regulations, procedures, and instructions in the origination of Federal Housing Administration loans and whether Fleet's quality control plan, as implemented, met HUD requirements.

### **What We Found**

Fleet's Philadelphia branch office did not originate all Federal Housing Administration loans in accordance with HUD's loan origination requirements. Of the 20 loans we selected for review,<sup>1</sup> the branch office violated HUD requirements

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<sup>1</sup> Originally valued at \$930,520.

for 5 of the loans valued at \$224,245. Fleet did not exercise due diligence in the review of assets and income, did not verify rental history, and approved loans with excessive debt to income ratios. These deficiencies contributed to an increased risk to the Federal Housing Administration Insurance Fund.

Fleet also submitted loans for late endorsement when the payment histories of the buyer were not current. Of the 27 endorsements the branch office submitted from January 1, 2002, through December 31, 2003, 7 loans totaling \$434,804 were from borrowers who had delinquent mortgage payments. The deficiencies stem from Fleet's lack of supervision over its branch office.

Fleet's Philadelphia branch office was not operating in conformance with HUD requirements. It did not provide an accessible business environment for its clients during normal business hours, nor did it employ a branch manager to supervise operations.

HUD requires its mortgagees to develop and implement a quality control plan to ensure loans are originated according to HUD requirements. The quality control plan provided by Fleet does not meet the requirements of HUD regulations and, therefore, we cannot be assured that loans are originated according to HUD requirements.

### **What We Recommend**

We recommend that the Assistant Secretary for Housing – Federal Housing Commissioner require Fleet to take immediate action to determine whether deficiencies in Fleet's loan origination process warrant administrative action and if appropriate, request that the Mortgagee Review Board impose civil monetary penalties for Fleet's failure to provide an adequate quality control plan. We also recommend that HUD request indemnification from Fleet on Federal Housing Administration loans valued at \$619,614, which it issued contrary to HUD's loan origination procedures, and repayment of \$39,435 on one loan that went into default, causing HUD to pay a claim. Further, since we have been informed by Fleet that the Philadelphia branch office has been closed, we recommend HUD ensure the branch is removed from its systems as an approved direct endorsement lender.

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 provided Fleet a discussion draft on November 19, 2004, and held an exit conference with Fleet on December 16, 2004. We received written comments and additional documentation from Fleet on December 15, 2004. In addition, we discussed the issues with HUD's Quality Assurance Division. The discussions and additional documentation addressed and resolved many of the issues noted in the draft report. Consequently, we extensively revised the report including removing resolved issues. The complete text of the auditee's response, along with our evaluation of that response, can be found in Appendix B of this report.

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## BACKGROUND AND OBJECTIVES

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The U.S. Department of Housing and Urban Development's (HUD) Strategic Plan states that part of its mission is to increase homeownership, support community development, and increase access to affordable housing free from discrimination.

The National Housing Act, as amended, established the Federal Housing Administration, an organizational unit within HUD. The Federal Housing Administration provides insurance for mortgagees against loss on single-family home mortgages.

Beginning in 1983, HUD implemented the Direct Endorsement Program, which authorized approved mortgagees to underwrite loans without HUD's prior review and approval. HUD can place them on credit watch status or terminate their approval if their rate of defaults and claims exceeds the normal rate for the area. Many sanctions are available for taking actions against mortgagees or others who abuse the program.

The main office of Fleet National Bank (Fleet) is located in Providence, RI. The Philadelphia, PA, branch is one of its 30 active branches with direct endorsement approval. HUD approved the Philadelphia branch office on September 25, 2000. Fleet issued 4,193 Federal Housing Administration loans worth \$555,655,265 between January 1, 2002, and December 31, 2003, 137 of which were issued by the Philadelphia branch at a value of \$7,612,809. Of the 137 loans, we reviewed 20 loans worth \$930,520 that were in default status less than 2 years after closing.

During the period under review (January 1, 2002, to December 31, 2003), Fleet sold its loans and outsourced its underwriting process. The loans were sold and serviced by another company between January and December 2002. Between January 2003 and April 2004, Fleet outsourced its underwriting and processing function to a different company, which then purchased and serviced the loans.

In April 2004, Fleet began the process of merging with Bank of America. Currently, accounting and personnel files are being merged. Eventually, each branch office will become part of Bank of America, with the Philadelphia branch expected to complete its merger by the later part of 2004. As part of the merger, employees were laid off and offices were closed.

Due to the ongoing merger with Bank of America and the outsourcing and selling of loans, obtaining historical and background information on Fleet and its Philadelphia branch was difficult. We were not able to obtain information relating to Fleet's quality control plan, policies and procedures related to loan origination, Fleet's status as a main office, or audited financial statements. In addition, we were not able to interview loan processors, underwriters, or supervisors.

The objective of our review was to determine whether Fleet originated Federal Housing Administration-insured loans in accordance with prudent lending practices and HUD requirements. We reviewed case files from both the Homeownership Center and the mortgagee and reviewed the oversight of Fleet over its branches to determine whether there was evidence of lack of oversight, intentional wrongdoing, or lack of professional due care that led to the high

number of defaults and late endorsements from the Philadelphia branch.

## RESULTS OF AUDIT

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### Finding 1: Fleet Issued Loans That Increased Risk to HUD

Fleet did not always originate Federal Housing Administration-insured loans in accordance with HUD requirements. For 5 of the 20 loans we reviewed, originally valued at \$232,500, Fleet did not exercise due diligence in the review of assets and income, did not verify rental history, and approved loans with excessive debt to income ratios. The deficiencies stem from the lack of supervision over its branch office. These deficiencies contributed to an increased risk to the Federal Housing Administration Insurance Fund.

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#### **Fleet Did Not Verify the Rental History of All Borrowers**

HUD requires<sup>2</sup> the lender to determine the borrower's payment history of housing obligations covering the most recent 12-month period. For 4 of the 20 cases reviewed, Fleet did not properly verify the previous rental history of the mortgagor.

#### **Fleet Did Not Verify Borrowers' Income or Capacity to Repay the Mortgage**

HUD requires the lender to verify the borrower's employment for the most recent two full years<sup>3</sup> and establish the borrower's capacity to repay mortgage debt.<sup>4</sup> In addition, the income must be expected to continue through at least the first 3 years of the mortgage loan.<sup>5</sup>

For 1 of the 20 cases reviewed, Fleet did not adequately verify the income. For FHA case number 441-6872755, Fleet did not verify the borrower's employment for the past two full years. Documentation in the FHA case binder only showed 1 year of employment with more than a year lapse between jobs.

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<sup>2</sup> HUD Handbook 4155.1, Mortgage Credit Analysis for Mortgage Insurance, One to Four Family Properties, paragraph 2-3 A.

<sup>3</sup> HUD Handbook 4155.1, Mortgage Credit Analysis for Mortgage Insurance, One to Four Family Properties, paragraph 2-6.

<sup>4</sup> HUD Handbook 4155.1, Mortgage Credit Analysis for Mortgage Insurance, One to Four Family Properties, chapter 2, section 2.

<sup>5</sup> HUD Handbook 4155.1, Mortgage Credit Analysis for Mortgage Insurance, One to Four Family Properties, paragraph 2-7.

### **Fleet Did Not Verify Borrowers' Assets**

HUD requires the lender to verify savings and checking accounts. A verification of deposit, along with the most recent bank statement, may be used to accomplish this. If there is a large increase in an account or the account was opened recently, the lender must obtain a credible explanation of the source of those funds.

For 1 of the 20 cases reviewed, Fleet did not adequately verify the assets stated on the Uniform Residential Loan Application. For FHA case number 441-6941957, Fleet did not verify all funds for the borrower's investment. The FHA case binder did not contain bank statements to support funds listed in a bank account on the Uniform Residential Loan Application.

### **Fleet Issued Loans in Which the Debt to Income Ratios Exceeded HUD Requirements**

HUD requires debt to income ratios not to exceed 29 and 41 percent (mortgage to income and all fixed payment to income, respectively). Ratios exceeding the 29 and 41 percent may be acceptable only if significant compensating factors are present. HUD identifies 10 compensating factors including good rental history, large downpayment, and potential for increased earnings.

For 1 of the 20 cases reviewed, Fleet allowed excessive ratios with no valid compensating factors provided. For FHA case number 441-6988925 the fixed payment to income ratio was 50.78 percent with no compensating factors listed.

The above cases illustrate that HUD assumed unnecessarily high risk when insuring the loans originated by Fleet. The deficiencies associated with Fleet's loan origination activities stem from its lack of supervision over its branch employees.

### **Recommendations**

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

- 1A. Determine whether Fleet's deficiencies in the loan origination process warrant administrative action.
- 1B. Request indemnification from Fleet on four loans issued with current unpaid

balances of \$184,810, in which Fleet's loan origination procedures did not comply with HUD requirements, and request repayment for one loan issued, with a loss to HUD of \$39,435, that went into default and a claim was paid.

## Finding 2: Fleet Submitted Loans for Late Endorsement When the Payment Histories Were Not Current

Fleet submitted loans for late endorsement when the payment histories of the buyers were not current. We found seven loans, valued at \$434,804, that were submitted for late endorsement when payment histories were not current. The deficiencies stem from Fleet's lack of supervision over its branch office.

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### Late Endorsements Were Not Current

HUD requires late endorsement submissions (more than 60 days after closing) to include a payment ledger showing the payments received.<sup>6</sup> The mortgage payments must not be delinquent when submitted for endorsement. If a payment is made outside the calendar month due, the lender cannot submit the case for endorsement until six consecutive payments have been made.

We reviewed all 27 endorsement submissions from January 1, 2002, through December 31, 2003, that were submitted for endorsement more than 60 days after closing. Fleet improperly submitted seven loans, totaling \$434,804, for endorsement more than 60 days after closing when the borrowers had delinquent payments before submission.

Because HUD relied on Fleet's loan origination process, it assumed abnormally high risk when it insured the seven loans.

### Recommendations

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

- 2A. Take appropriate steps against Fleet for not following HUD's requirements for late endorsement requests, including requiring indemnification for seven loans, totaling \$434,804, that were improperly submitted for endorsement.

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<sup>6</sup>HUD Handbook 4165.1, Endorsement for Insurance for Home Mortgage Programs (Single Family), paragraph 3-1.

## Finding 3: Fleet Did Not Administer Its Philadelphia Branch Office in Conformance with HUD Requirements

The Philadelphia office of Fleet is not functioning as a true branch, providing an accessible business environment for its clients, and furnishing proper oversight and supervision to its staff. Fleet did not maintain an office with adequate personnel and regular business hours and did not provide onsite supervision to the branch employees. The deficiencies indicate a disregard of HUD branch operation requirements. Therefore, the Philadelphia branch office's eligibility as an approved branch in the origination of Federal Housing Administration-insured loans is questionable.

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### **The Philadelphia Branch Did Not Employ Adequate Staff or Maintain Regular Business Hours**

The Philadelphia office, contrary to HUD requirements,<sup>7</sup> only employs two commission-based account executives who do not maintain regular business hours. The employees often work out of their homes or at other locations in the city. The office itself maintains no scheduled hours. For several days, we attempted to contact the office via telephone but received only an answering machine message. When we visited the office during regular business hours, the door was locked, and no one answered the bell. The account executives stated that they only come to the office when they set up a meeting with a client. Thus, accessibility for clients is limited to being able to contact one of the two account executives.

### **Fleet National Bank Did Not Supervise Its Employees**

The Philadelphia office does not have a branch manager located onsite as required by HUD.<sup>8</sup> Without the onsite supervision of a branch manager, proper oversight of the account executives and the loan process is severely impaired. This absence of supervision reflects a disregard for HUD requirements and has resulted in loans that lack proper documentation and credit analysis being issued and endorsed. These loans contributed to an increased risk to the Federal Housing Administration Insurance Fund. See Findings 1 and 2 for more detail.

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<sup>7</sup> Form HUD-92001-B, Title II Branch Office Notification, states that the mortgagee agrees to maintain and staff a branch open to the public during normal business hours.

<sup>8</sup> Form HUD-92001-B, Title II Branch Office Notification, states that the mortgagee agrees to employ a branch manager at the branch office.

Due to the lack of records made available to us, we were not able to determine how long the Philadelphia office has been functioning contrary to HUD requirements. However, we determined that there has been no onsite branch manager since at least July 2002.

In its response (see Appendix B), the auditee informed us the branch had been closed earlier in the year.

## **Recommendations**

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

- 3A. Ensure that Fleet's Philadelphia branch is removed from HUD's systems as an approved direct endorsement lender.

## Finding 4: Fleet Did Not Demonstrate That It Developed and Implemented a Quality Control Plan Compliant With HUD Requirements

Fleet originally failed to provide a copy of its quality control plan. After the draft report was issued, Fleet provided a copy of the plan. We reviewed the plan and found that Fleet's Quality Control Plan does not identify HUD-specific requirements as part of their review.

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### **Fleet's Quality Control Plan Does Not Identify HUD-Specific Requirements**

As part of our audit, we asked Fleet to provide us with its quality control plan and any reports that it generated from the reviews under the plan for a 2 year period. After several requests, Fleet provided a number of reports marked "Quality Control." When questioned about the quality control plan, Fleet responded that the quality control function had been contracted out to a company, from which it would obtain a copy of the plan. However, Fleet initially did not provide us a copy of the plan. It was not until after the draft was issued that Fleet provided a copy of the plan.

We reviewed the plan and found that Fleet's quality control plan does not identify all HUD requirements as part of their review. We noted Fleet's Quality Control Plan covered most of the basic elements and requirements, however some were not included.<sup>9</sup> Specifically, the Quality Control Plan does not specify the review of branches and early defaults (less than six months). In addition, the sampling methodology is not outlined in the plan.

Also, we noted Fleet's Quality Control Plan did not include at least the following specific elements which are required:<sup>10</sup>

- Determine whether there are sufficient and documented compensating factors if the debt ratios exceed FHA limits.
- Determine whether the loan was submitted for insurance within 60 days of closing or included a payment history showing the loan was current when it was submitted for mortgage insurance.
- Determine whether the seller acquired the property at the time of or soon before closing, indicating a possible property "flip."

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<sup>9</sup> HUD Handbook 4060.1, Mortgagee Approval Handbook, paragraph 6-3 and 6-6.

<sup>10</sup> HUD Handbook 4060.1, Mortgagee Approval Handbook, paragraph 6-7.

- If possible, determine whether the mortgagor transferred the property at the time of closing or soon after closing, indicating the possible use of a “strawbuyer” in the transaction.
- Determine that no one is employed for HUD origination, processing, underwriting or servicing who is debarred, suspended, subject to a Limited Denial of Participation or otherwise restricted from participation in HUD/FHA programs. HUD recommends a periodic check of the employee list, at least semi-annually.

### **On-Site Quality Control Review of the Philadelphia Branch Office Was Not Done**

Although branch reviews can be done electronically, annual visits are mandatory for offices meeting certain higher risk criteria such as high early default rates.<sup>11</sup> The Philadelphia branch had a default rate four times the national average. Therefore, an onsite quality control review should have been performed. However, we were not provided any documentation supporting a quality control review of the Philadelphia branch.

### **Fleet Personnel Were Not Aware of Key Monitoring Requirements**

To make quality control reviews more useful, mortgagees are encouraged to implement quality control throughout the loan origination process. Accordingly, HUD recommends mortgagees identify patterns of early defaults by location, program, and loan characteristic.<sup>12</sup> HUD’s Neighborhood Watch - Early Warning System (Neighborhood Watch) can be used to identify these patterns.

The Philadelphia branch has a default rate four times the national average. However, during an interview with Fleet staff, they questioned how they were supposed to track the defaults to know that the Philadelphia branch had such a high default rate. Fleet personnel were unaware of the monitoring requirements of the quality control plan and did not know how to use Neighborhood Watch to monitor its branches. In fact, they did not know that they had access to Neighborhood Watch.

Because Fleet could not demonstrate that it developed and implemented a quality control plan that was in compliance with HUD requirements, we have limited assurance that HUD was protected from unacceptable risk; guarded against errors, omissions, and fraud; and assured that swift and appropriate corrective action

<sup>11</sup> HUD Handbook 4060.1, Mortgagee Approval Handbook, paragraph 6-3 G.2.

<sup>12</sup> HUD Handbook 4060.1, Mortgagee Approval Handbook, paragraph 6-5 C.

would be taken when necessary in the origination and servicing of Federal Housing Administration loans.

## **Recommendations**

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

- 4A. Require Fleet to develop and implement a quality control plan in compliance with HUD requirements.
- 4B. Request the Mortgagee Review Board impose civil money penalties, for each of the two years in our audit period, for Fleet's failure to provide an acceptable quality control plan.

## SCOPE AND METHODOLOGY

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To accomplish our objectives we

- Reviewed 100 percent of the Federal Housing Administration-insured loans (20 cases) originated by Fleet's Philadelphia branch between January 1, 2002, and December 31, 2003, that had gone into default at least once. The 20 loans were part of a universe of 137 loans originated by the Philadelphia branch during that time. The results of the detailed testing apply to the 20 loans reviewed only and cannot be projected to the universe of Federal Housing Administration-insured loans.
- Examined records and related documents of Fleet.
- Reviewed applicable HUD handbooks and mortgagee letters.
- Conducted interviews with officials and employees of Fleet and Bank of America and the HUD Quality Assurance Division.

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

The audit generally covered the period from January 1, 2002, to December 31, 2003. This period was expanded to include the most current data while performing our audit. Therefore, when applicable, the audit period was expanded to include current data through September 30, 2004. We conducted our fieldwork from May through November 2004.

We performed our review in accordance with generally accepted government auditing standards.

# INTERNAL CONTROLS

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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. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

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## Relevant Internal Controls

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

- Loan Origination Process – Policies and procedures that management has in place to reasonably ensure that the loan origination process complies with HUD program requirements.
- Quality Control Plan – Policies and procedures that management has in place to reasonably ensure implementation of HUD quality control requirements.

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

## Significant Weaknesses

Based on our review, we believe the following items are significant weaknesses:

- Fleet did not operate in accordance with HUD requirements as they relate to loan issuance, late endorsements, and branch administration.
- Fleet provided a copy of the Quality Control Plan, however, the plan does not contain all HUD requirements.

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

## **FOLLOW-UP ON PRIOR AUDITS**

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This is the first audit of Fleet National Bank's Philadelphia branch office conducted by HUD's Office of the Inspector General (OIG).

## APPENDIXES

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### Appendix A

#### FUNDS TO BE PUT TO BETTER USE

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Recommendation Number	Funds To Be Put to Better Use 1/
1B	\$ 224,245
2A	\$ 434,804
<b>Total</b>	<b>\$ 659,049</b>

- 1/ “Funds to be put to better use” are quantifiable savings that are anticipated to occur if an 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.

## Appendix B

### AUDITEE COMMENTS AND OIG'S EVALUATION

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#### Ref to OIG Evaluation

#### Auditee Comments

**Comments 1  
through 14**

December 14, 2004

U.S. Department of Housing and Urban Development  
Wanamaker Building, Suite 1005  
100 Penn Square East  
Philadelphia, PA 19107-3380

Re: Audit of Fleet National Bank  
Philadelphia Branch of 8-9-2004

Dear Mr. Temme:

We have received your findings from the review of loans at the Fleet branch in Philadelphia, Pennsylvania conducted on August 9, 2004.

**Comment 15**

We have addressed your findings in the attached response. It was noted that there was a lack of supervision over this branch office. Please be aware that Carol Ramsey was acting as interim manager of this branch at the time of the audit. Also, this branch was closed earlier this year.

**Comment 16**

We have enclosed a copy of our Quality Control Plan for your review.

Respectfully,

  
Deborah Lewis  
Quality Assurance

Cc: Joyce Walsh  
SVP Retail Channel Risk Manager  
Allen H. Jones  
SVP Production Management Administrator

**Ref to OIG Evaluation**

**Auditee Comments**

**Comment 1**

Finding: [REDACTED] 441-6941957

Funds to close were not property verified or supported.

The borrower was not required to bring any funds to closing. However, there is a statement in the file from Hudson United Bank signed by [REDACTED] detailing the borrower's transactions in June and confirming the \$400.00 balance. The closing funds were covered by the borrower's Ameridream gift.

Payment history of housing obligations was not documented.

The rental payment history from July 2000 -- June 2002 was verified in file by a letter from the landlord dated June 11, 2002. The letter indicated that the rent had been paid in a timely manner.

**Comment 2**

Finding: [REDACTED] 441-7044758

Payment history of housing obligations was not documented.

The borrower claimed no housing expenses. None appears on the application or the MCAW. With no rental obligation, there would have been no payment history to document.

**Comment 3**

Finding: [REDACTED] 441-6765396

Payment history of housing obligations was not documented.

The borrower had no payment history to verify. He had been incarcerated for seven years (see borrower's letter), and since his release he had been living with his parents.

**Comment 4**

Finding: [REDACTED] 441-7041275

Income not properly supported.

The standard reduction of twenty-five percent to allow for vacancy and maintenance was applied to the \$500.00 rental. The payment of \$202.00 was deducted from this amount to arrive at the \$173.00 used for qualifying. The mortgage payment was obtained from the credit report, and the amount of rental was verified via a copy of the month-to-month lease.

The borrower's income from Social Security (\$473.00) and Supplemental Security Income (\$57.43) were documented by award letters in the file. The VA benefit was

Ref to OIG Evaluation

Auditee Comments

**Comment 5**

documented via bank statements showing receipt of \$62.00 on 8-30-02 and 8-1-02. These amounts were received every fourth Friday. The sum of these monies \$592.40 was then grossed up by a figure of 15% to acknowledge the non-taxable status of these payments.

Finding: [REDACTED] 441-6944670

Payment history of housing obligations was not documented

The borrower appears to have reported living with family at 3121 [REDACTED] Street in Philadelphia. There is evidence that Fleet acknowledged this from the screen prints from their processing system. Regrettably, this status was not appropriately transferred to the application.

**Comment 6**

Finding: [REDACTED] 441-6919715

Funds to close were not properly verified or supported.

The borrower required \$340.21 from her own funds to close the transaction. The borrower's savings account at Beneficial Savings Bank was not properly documented. This account held a balance of \$1,516.19 at the time of closing. If this amount, because of lack of complete identification, is to be ignored, then it is very reasonable that the borrower could have funded the closing from payroll monies. As you are aware, the borrower would have experienced a month without housing expense making it very possible for her to have sourced the \$340.21 from her regular salary.

Qualifying ratios not properly documented.

Although not specifically cited by the underwriter, the compensating factor justifying approval for this loan is the decrease in housing expense. The borrower had successfully managed a rental amount of \$615.00 for four years. The proposed payment with taxes and insurance was \$516.87 – nearly \$100.00 less than the housing expense she had demonstrated the ability to handle.

**Comment 7**

Finding: [REDACTED] 441-6893398

Qualifying ratios not properly documented

Although the borrower's mortgage payment to income exceeds the guideline of 29%, the fact that she had no other debt would be the compensating factor.

Payment history of housing obligations was not documented

Ref to OIG Evaluation

Auditee Comments

**Comment 8**

The borrower's rental payment history was verified in a letter dated December 1, 2001 from the property manager.

Finding: [REDACTED] 441-6942289

Payment history of housing obligations was not documented

Rental reference is not available. The borrower is a widow; other previous residence was a property owned by her deceased spouse. As can be seen from [REDACTED] credit report, she was not a party to any mortgage, if there indeed was a mortgage, on that property at [REDACTED] Philadelphia.

Funds to close were not properly verified or supported.

Borrower provided a bank statement dated 4-15-2002, evidencing an \$11,096.00 balance, sufficient to close the transaction. Based upon her husband's death (2-4-2002) it is not unusual that she would have received proceeds from the sale of property or other depository accounts held by the decedent. It's important to note that the \$960.00 figure has not been the borrower's income over a lengthy period of time. This borrower was recently widowed.

The Social Security income is non-taxable. Such income is often grossed-up to acknowledge the net benefit of the tax status. Using a 1.25% for grossing-up this income (without the income for [REDACTED]) would yield a total fixed payment to income ratio of 27.09%

Income not properly verified or supported.

One of the borrower's children was indeed thirty-three months away from the end of his Social Security benefits when the note was signed rather than the proscribed thirty-six months. If this income is excluded, the total fixed payment to income ratio is only 33.9% which is well below the guideline.

**Comment 9**

Finding: [REDACTED] 441-7024520

Income not properly verified or supported.

Because public assistance is an allowable source of income for FHA transactions, it is likely that the underwriter considered the borrower's transition from welfare to work as the two-year work history. The successful completion of six months employment at this modest wage position (\$7.50 per hour) would likely have been viewed as evidence of the borrower's success at bettering her financial perspective.

Ref to OIG Evaluation

Auditee Comments

**Comment 10**

HUD-1 settlement statement real estate agent signed for seller.

The sellers did fail to sign the HUD-1, however both sellers signed the HUD Termite Report Form 92053 on the day of closing evidencing their participation on that day. We agree that the settlement agent shouldn't have allowed the real estate agent to sign the HUD-1 on the seller's behalf, However the HUD-1 does not indicate any questionable charges so the lack of seller's signature appears to be a clerical oversight rather than an attempt to conceal charges or items from the sellers.

Finding: [REDACTED] 441-6887465

Income not properly verified or supported.

The documented income of \$545.00 monthly was grossed up as is allowable according to HUD guidelines. This is done to recognize the non-taxable status of this Supplemental Security Income received by the applicant from the Social Security Administration. The factor used to adjust the \$572.40 earnings (verified by letter from SSA on 2-28-2002) was 1.25 which was typical in 2002. The file also contains a letter from the borrower's doctor confirming that the SSI will continue for three years. Therefore, the qualifying ratios are 27.81/27.81 as originally stated.

**Comment 11**

Finding: [REDACTED] 441-6852489

Income not properly verified or supported.

The pay-stub in file does reflect a slightly lower income. The figure used was \$1,386.00 monthly. The pay-stub for pay period ending 3-6-2002 indicates a figure of \$1,355.38 per month (3.25 months divided by a YTD earning of \$4,405.72). This slight change affects the qualifying ratios by less than 1%. It is very important to remember that the total fixed payment to income ratio is well below the guideline for Total Debt-to-Income Ratio. The compensating factors listed on the MCAW signed on 4-30-02 are (1) similarity of proposed payment to previous rental payment and (2) a lack of other debt allowing the borrower to contribute a higher percentage to income to the housing payment.

**Comment 12**

Finding: [REDACTED] 441-6988925

Payment history of housing obligations was not documented.  
Qualifying ratios not properly documented.

Neither the application nor the MCAW indicate that the borrower has any current housing expense. We certainly acknowledge that this should have been explained along

Ref to OIG Evaluation

Auditee Comments

**Comment 13**

with the decision to approve the loan with a higher than normal total fixed payment to income ratio. However, without being able to consult the underwriter it is difficult to speculate. The borrower did have an excellent job and a FICO score of 658.

Finding: [REDACTED] 441-7070288

Mortgagee file was not available  
Qualifying ratios not properly documented

The information presented on the MCAW is, indeed, difficult to follow; however a review of origination file (located and now provided to you) clarifies some of the confusion. There are both rental verification form and a letter confirming payment experience from January 2000 through June of 2000. There are also rent receipts from January 2001 through September 2001 for the tenancy at 2083 [REDACTED] Street.

Payment history of housing obligations was not documented.

It is assumed that the underwriter's comment on the MCAW referencing the, "monthly housing payment remaining the same" refers to the satisfactory payment histories. Both rental amounts exceed the \$456.39 proposed payment amount. The borrower had also demonstrated good job stability. He'd been in the same type of job since 2000 and at his current company for two years at time of loan closing. He was receiving supplementary hourly pay as a work performance bonus.

**Comment 14**

Finding: [REDACTED] 441-6872755

Income was not properly verified or supported.

The borrower's employment history did cover a two-year period; however, during that period the borrower experienced some months of unemployment. The borrower did explain her gap in employment as is required in HUD Hand Book 4155.1, paragraph 2 - 6. Additionally, the borrower had been on her previous job for fifteen months, so it was not unreasonable to conclude that the likelihood of continuance at her then present job would be strong.

Payment history of housing obligations was not documented.

The borrower had no housing payment history to determine. The borrower's letter in the file dated April 11, 2002 explains that she'd been living rent free with her mother and sister.

Seller's signatures do not match on all documents.

**Ref to OIG Evaluation**

**Auditee Comments**

Although, the seller's signature does appear to be different, we are unaware of anything that would lead us to conclude definitively that the seller's signature had been forged.

## OIG Evaluation of Auditee Comments

### **Comment 1**

Fleet contends that the borrower was not required to bring any funds to closing because the closing funds were covered by the borrower's Ameridream gift. Fleet also states that a statement from Hudson United Bank confirms the balance of the bank account. However, Fleet did not provide any documentation to support this. Per a discussion with HUD's Quality Assurance Division, if the loan were manually underwritten, the down payment from Ameridream would be acceptable. However, since the loan was underwritten by an automated underwriting system, and the funds claimed by Hudson United Bank are part of the calculation used for the acceptance of the loan, the calculation is based on unsupported data.

Further, Fleet states that a landlord referral letter was in the file. However, the only letter we have was faxed from the selling agent. According to HUD Handbook 4155.1, the verification must come directly from the landlord, not from an interested third party.

The case will remain in the report.

### **Comment 2**

Fleet maintains the borrower had no previous housing expenses to document. However, according to the Uniform Residential Loan Application, the borrower is 38 years old with two children. Further, Fleet provided a copy of HUD-92900-A, Direct Endorsement Approval for a HUD/FHA-Insured Mortgage, stating that the borrower is a first-time homebuyer. There is no explanation as to the borrower's former housing situation.

The case will remain in the report.

### **Comment 3**

Fleet provided an explanation to the lack of previous housing obligations. We discussed the issue with the Quality Assurance Division and they stated that it was a viable explanation.

The case was removed from the report.

### **Comment 4**

Fleet did not provide any additional information to support the rental income. However, Fleet was able to explain how it calculated the borrower's income. Based on the supported income provided by Fleet, we recalculated the total debt to income and housing costs to income ratios. The lack of support for the rental income did not adversely affect the ratios and thus would not have changed the borrower's ability to purchase the home.

The case was removed from the report.

### **Comment 5**

Fleet could provide no support for its statement that it was aware of the borrower's prior housing situation.

The case will remain in the report.

### **Comment 6**

Fleet is stating that even though the funds in the bank account do not specifically identify the borrower as the owner of the account, the borrower still could have come up with the closing costs from payroll and lack of housing expense for the first month of the mortgage. In addition, the seller paid most of the closing costs for the borrower. Per a discussion with HUD's Quality Assurance Division, since the loan was manually underwritten HUD would accept the seller as the main source of funds for the closing.

In addition, Fleet is now stating as a compensating factor for the high ratios, the mortgage payment is lower than the previous rental payment.

The case was removed from the report.

### **Comment 7**

Fleet was able to justify the high ratios (no other debt) and provide a letter of payment of previous housing obligations.

The case was removed from the report.

### **Comment 8**

Fleet provided a viable explanation for the lack of housing expenses and the bank account. Further, Fleet calculated the income and ratios using the grossing up of income based on its non-tax status which is allowable under HUD Handbook 4155.1.

The case was removed from the report.

### **Comment 9**

Fleet is stating that public assistance (welfare) is an acceptable form of income. Per HUD's Quality Assurance Division, welfare is acceptable income if it is expected to continue for at least 3 years. In this case, the welfare ended and the borrower was now working.

In addition, Fleet provided evidence that the sellers were at settlement on the day of closing.

The case was removed from the report.

### **Comment 10**

Fleet provided support that the income will continue for at least three years. In addition, Fleet is grossing up the income due to its non-tax status which is allowable under HUD Handbook 4155.1.

The case was removed from the report.

### **Comment 11**

Fleet agrees that the income stated on the Uniform Residential Loan Application is not supported by documents in the file. However, using only the income that is supportable does not drastically change the overall ratios and thus would not have changed the borrower's ability to purchase the house.

In addition, Fleet cites the mortgage payment as being close to the previous rental payment and the fact that there is no other debt as compensating factors.

The case was removed from the report.

### **Comment 12**

Fleet cannot provide any justification (without talking to the underwriter who is no longer employed by Fleet) why it approved the loan with no rental history and high ratios (50.78%).

The case will remain in the report.

### **Comment 13**

Fleet was able to provide support for the rental payments. The compensating factor concerning the rental payment being more than the mortgage is now supported.

The case was removed from the report.

### **Comment 14**

Fleet provided letters from the borrower explaining the gaps in employment and the lack of rental history (living with mother and sister). However, continuous employment for the borrower could only be supported for one of the two years required by HUD Handbook 4155.1.

The case will remain in the report.

### **Comment 15**

Fleet states that the Philadelphia branch office was closed. However, as of January 3, 2005, the branch was still listed in HUD's Neighborhood Watch - Early Warning System. Fleet needs to

notify HUD of the closing of the branch office so HUD can take the necessary steps to remove the office from its records.

**Comment 16**

Fleet provided a copy of its Quality Control Plan. However, as explained in the report, the plan does not contain language specific to the requirements of the FHA program as required by HUD Handbook 4060.1.

## Appendix C

### SCHEDULE OF CASE FILES

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<b>FHA Case #</b>	<b>Purchase Price</b>	<b>Unpaid Principal Balance**</b>	<b>Claim Paid</b>	<b>Inadequate Rental History</b>	<b>Unsupported Income</b>	<b>Unsupported Assets</b>	<b>High Ratios With No Supporting Factors</b>
441-6872755	\$ 44,000	\$ 42,339.58			X		
441-6941957	\$ 38,000	\$ 0.00	\$39,435.00	X		X	
441-6944670	\$ 43,500	\$ 41,944.45		X			
441-7044758	\$ 55,000	\$ 49,947.55		X			
441-6988925	\$ 52,000	\$ 50,578.59		X			X
	\$232,500	\$184,810.17					

\*\* Unpaid Principal Balance as calculated in HUD's Insurance in Force System.

## Appendix D

### NARRATIVE CASE PRESENTATIONS

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Case Number: 441-6872755

Mortgage Amount: \$43,320

Date of Loan Closing: April 26, 2002

Status: Default - First Legal Action to Commence Foreclosure

Payments Before First Default Reported: 0

Unpaid Principal Balance: \$42,340

Summary:

Fleet did not properly verify the borrower's income.

Pertinent Details:

**Income Was Not Properly Verified or Supported**

Fleet did not document two years of consecutive employment. The employment certification only shows one year of continuous employment with more than a year lapse between jobs (HUD Handbook 4155.1, paragraph 2-6).

Case Number: 441-6941957

Mortgage Amount: \$37,410

Date of Loan Closing: June 28, 2002

Status: Foreclosure Completed/Conveyance

Payments Before First Default Reported: 2

Unpaid Principal Balance: \$36,610

Claim Paid: \$39,435

Summary:

Fleet did not (1) properly verify the borrower's funds to close and (2) include in the loan origination file or case binder a proper determination of the borrower's payment history of housing obligations.

Pertinent Details:

Funds To Close Were Not Properly Verified or Supported

All funds for the borrower's investment in the property were not properly verified. There were no bank statements in the file to support funds in an account listed on the Uniform Residential Loan Application (HUD Handbook 4155.1, paragraph 2-10B). Since the loan was underwritten by an automated underwriting system, and the funds claimed by the borrower are part of the calculation used for the acceptance of the loan, the calculation is based on unsupported data.

Payment History of Housing Obligations Was Not Documented

Fleet did not include in its loan origination file or case binder a determination of the borrower's payment history of housing obligations through either the credit report, directly from the landlord-or mortgage servicer, or through canceled checks covering the most recent 12-month period (HUD Handbook 4155.1, paragraph 2-3A).

Loan Foreclosure Completed

The loan was foreclosed, and conveyance was complete September 21, 2004, for a loss to HUD of \$39,435.

Case Number: 441-6944670

Mortgage Amount: \$42,822

Date of Loan Closing: July 30, 2002

Status: Default - Foreclosure Started

Payments Before First Default Reported: 12

Unpaid Principal Balance: \$41,944

Summary:

Fleet did not include in the loan origination file or case binder a proper determination of the borrower's payment history of housing obligations.

Pertinent Details:

Payment History of Housing Obligations Was Not Documented

Fleet did not include in its loan origination file or case binder a determination of the borrower's payment history of housing obligations through either the credit report, directly from the landlord or mortgage servicer, or through canceled checks covering the most recent 12-month period (HUD Handbook 4155.1, paragraph 2-3A).

Case Number: 441-7044758

Mortgage Amount: \$51,156

Date of Loan Closing: October 31, 2002

Status: Default - First Legal Action To Commence Foreclosure

Payments Before First Default Reported: 10

Unpaid Principal Balance: \$49,948

Summary:

Fleet did not include in the loan origination file or case binder a proper determination of the borrower's payment history of housing obligations.

Pertinent Details:

Payment History of Housing Obligations Was Not Documented

Fleet did not include in its loan origination file or case binder a determination the borrower's payment history of housing obligations through either the credit report, directly from the landlord or mortgage servicer, or through canceled checks covering the most recent 12-month period (HUD Handbook 4155.1, paragraph 2-3A).

Case Number: 441-6988925

Mortgage Amount: \$51,592

Date of Loan Closing: September 30, 2002

Status: Default - Repayment

Payments Before First Default Reported: N/A

Unpaid Principal Balance: \$50,579

Summary:

Fleet did not (1) include in the loan origination file or case binder a proper determination of the borrower's payment history of the housing obligations and (2) properly document the borrower's qualifying ratios.

Pertinent Details:

Payment History of Housing Obligations Was Not Documented

Fleet did not include in its loan origination file or case binder a determination of the borrower's payment history of housing obligations through either the credit report, directly from the landlord or mortgage servicer, or through canceled checks covering the most recent 12-month period (HUD Handbook 4155.1, paragraph 2-3A).

Qualifying Ratios Not Properly Documented

Fleet did not identify any compensating factors to justify approval of a loan. For ratios exceeding the benchmark guidelines of 29 percent (mortgage payment to income) and 41 percent (total fixed payment to income), the underwriters must record the compensating factors in the "remarks" section of the Mortgage Credit Analysis Worksheet, and they must be supported by documentation. The fixed payment to income ratio is 50.78 percent with no compensating factors identified (HUD Handbook 4155.1, paragraphs 2-12 and 2-13).

In addition, the settlement agent signed the HUD-1 Settlement Statement for the trustees of the estate (sellers), but there was no documentation authorizing it.

## Appendix E

### SCHEDULE OF LATE ENDORSEMENTS

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<b>Case Number</b>	<b>Original Mortgage Amount</b>	<b>Unpaid Principal Balance</b>	<b>Closing Date</b>	<b>Endorsement Date</b>	<b>Late Payments</b>
441-7024202	\$ 46,512	\$ 45,532.33	10/29/2002	4/22/2003	Yes
441-7090378	\$ 57,855	\$ 56,618.85	12/27/2002	4/28/2003	Yes
441-7037258	\$ 38,884	\$ 37,965.60	10/31/2002	1/10/2003	Yes
441-6961642	\$ 54,150	\$ 53,087.96	8/7/2002	3/11/2003	Yes
441-6926053	\$ 73,742	\$ 72,202.32	6/24/2002	1/28/2003	Yes
441-6852522	\$134,436	\$131,393.32	4/19/2002	8/13/2002	Yes
441-6905240	\$ 38,870	\$ 38,004.09	5/10/2002	7/18/2002	Yes
	<b>\$444,449</b>	<b>\$434,804.47</b>			