Issue Date March 15, 2006	
Audit Report Number: 2006-CH-1007	

TO: Brian D. Montgomery, Assistant Secretary for Housing-Federal Housing Commissioner, H
John W. Herold, Associate General Counsel for Program Enforcement, CE

FROM: Heath Wolfe, Regional Inspector General for Audit, 5AGA

SUBJECT: Huntington National Bank, Supervised Lender; Columbus, Ohio; Generally Complied with Requirements Regarding Submission of Late Requests for Endorsement and Underwriting of Loans

HIGHLIGHTS

What We Audited and Why

We audited Huntington National Bank (Huntington), a supervised lender approved to originate, underwrite, and submit insurance endorsement requests under the U.S. Department of Housing and Urban Development's (HUD) single family direct endorsement program. The audit was part of the activities in our fiscal year 2005 annual audit plan. We selected Huntington for audit because of its high late endorsement rate. Our objectives were to determine whether Huntington complied with HUD's regulations, procedures, and instructions in the submission of insurance endorsement requests and underwriting of Federal Housing Administration loans.

What We Found

Huntington generally complied with HUD's requirements on late requests for insurance endorsement; however, it improperly submitted 20 late requests for endorsement out of 761 loans tested. The loans were either delinquent or otherwise did not meet HUD's requirements of six monthly consecutive timely payments after delinquency but before submission to HUD. Huntington also incorrectly certified that all payments due were made by the borrowers before or within the month due for 12 loans and the escrow account for taxes, hazard insurance, and mortgage insurance premiums was current for one loan when it was not.

Further, Huntington generally complied with HUD's underwriting requirements. However, it underwrote two Federal Housing Administration loans that later defaulted by overstating income, understating liabilities, and providing no valid compensating factors to approve the two loans. Huntington also charged excessive and/or unallowable fees on five loans and incorrectly certified that due diligence was used in underwriting 5 of the 32 loans reviewed when it was not.

These improperly submitted and underwritten loans increased the risk to HUD's Federal Housing Administration insurance fund.

What We Recommend

We recommend that HUD's assistant secretary for housing-federal housing commissioner require Huntington to indemnify HUD for any future losses on 14 loans improperly submitted for endorsement with a total mortgage value of more than $1.4 million and take appropriate action against Huntington for violating the requirements in effect at the time when it submitted two loans with a mortgage value of nearly $178,000 without the proper six month payment histories. We also recommend that HUD's assistant secretary for housing-federal housing commissioner require Huntington to indemnify HUD for any future losses on two defaulted loans with a total mortgage value of more than $228,000 that were inappropriately underwritten, require Huntington to reimburse the borrowers or HUD as appropriate more than $1,300 in excessive and/or unallowable fees charged on five loans, and implement adequate procedures and controls to address the deficiencies cited in this report.

In addition, we recommend that HUD's associate general counsel for program enforcement determine legal sufficiency and if legally sufficient, pursue remedies under the Program Fraud Civil Remedies Act against Huntington and/or its principals for incorrectly certifying that all payments due were made by the borrowers before or within the month due for 12 loans, the escrow account for taxes, hazard insurance, and mortgage insurance premiums was current for one loan submitted for Federal Housing Administration insurance endorsement when the escrow account was not current, and due diligence was used in underwriting five loans when it was not.

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

During the audit, we provided the results of our late endorsement and underwriting reviews to Huntington's management. We also provided our discussion draft audit report to Huntington's mortgage group director, assistant vice president-quality control manager, and HUD's staff during the audit. We conducted an exit conference with Huntington's management on February 2, 2006.

We asked Huntington's mortgage group director to provide comments on our discussion draft audit report by March 1, 2006. The mortgage group director provided written comments dated February 27, 2006, that generally agreed with our findings, but disagreed with our recommendations for indemnification and penalties under the Program Fraud Civil Remedies Act. The complete text of the written comments, along with our evaluation of that response, can be found in appendix B of this report except for 130 pages of documentation that was not necessary for understanding Huntington's comments. A complete copy of Huntington's comments plus the documentation was provided to the director of HUD's Quality Assurance Division.

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BACKGROUND AND OBJECTIVES

W. Huntington & Company opened for business in 1866. In 1905, the company was incorporated as The Huntington National Bank of Columbus. In 1979, 15 banks including The Huntington National Bank of Columbus merged into one bank named the Huntington National Bank (Huntington).

As of March 2006, Huntington is part of a $32 billion bank headquartered in Columbus, Ohio. It provides retail and commercial financial products and services through more than 300 regional banking offices in Indiana, Kentucky, Michigan, Ohio, and West Virginia. Selected financial service activities are also conducted in other states including dealer sales offices in Florida, Georgia, Tennessee, Pennsylvania, and Arizona; private financial group offices in Florida; and mortgage banking offices in Florida, Maryland, and New Jersey. International banking services are made available through the headquarters office in Columbus and offices located in the Cayman Islands and Hong Kong. Huntington has seven individuals sitting on its board of directors and 17 executives, including seven regional presidents.

In August 1987, the U.S. Department of Housing and Urban Development (HUD) approved Huntington as a supervised direct endorsement lender. As a direct endorsement lender, Huntington determines that a proposed mortgage loan is eligible for insurance under the applicable programs' regulations and submits the required documents to HUD without its prior review of the origination and closing of the loan. Huntington is responsible for complying with all applicable HUD regulations and handbook instructions.

As of March 2006, Huntington is the sponsor of 91 active loan correspondents and authorized agent for six principals originating or processing Federal Housing Administration loans. From January 1, 2003, through December 31, 2004, Huntington originated and/or sponsored 2,346 Federal Housing Administration loans totaling more than $264 million. Huntington is approved to originate Federal Housing Administration insured loans in the following HUD offices' jurisdictions: Baltimore, Charleston, Cincinnati, Cleveland, Columbus, Coral Gables, Detroit, Flint, Grand Rapids, Indianapolis, Louisville, and Newark.

We audited Huntington as part of the activities in our fiscal year 2005 annual audit plan. We selected Huntington for audit because of its high late endorsement rate of 35 percent during the period of January 1, 2003, through December 31, 2004.

Our objectives were to determine whether Huntington complied with HUD's regulations, procedures, and instructions in the submission of insurance endorsement requests and underwriting of Federal Housing Administration loans.

RESULTS OF AUDIT

Finding 1: Huntington Generally Complied with HUD's Requirements Regarding Late Endorsement Loans

From January 2003 to December 2004, Huntington generally met HUD's requirements regarding late requests for endorsement. However, it submitted 20 loans totaling more than $2.2 million as late requests for insurance endorsement when the borrowers did not make six monthly consecutive timely payments after delinquency but before submission to HUD. For 29 loans' certifications reviewed, Huntington also incorrectly certified that all payments due were made by the borrowers before or within the month due for 12 loans and the escrow account for taxes, hazard insurance, and mortgage insurance premiums was current for one loan submitted for Federal Housing Administration insurance endorsement when the escrow account was not current. These deficiencies occurred because Huntington lacked adequate procedures and controls over its late endorsement process and its staff was not adequately trained on HUD's late endorsement requirements. These improperly submitted loans increased the risk to the Federal Housing Administration insurance fund.

Huntington Improperly Submitted Late Requests for Endorsement

Our analysis of the mortgage payment histories provided by Huntington and endorsement data from HUD's systems showed that for the 761 loans we tested, Huntington generally complied with HUD's requirements regarding late requests for endorsement. However, Huntington submitted 20 loans for endorsement when the borrowers did not make six monthly consecutive timely payments after delinquency but before submission to HUD.

After endorsement, 4 of the 20 loans were paid in full and no longer represent a risk to HUD's Federal Housing Administration insurance fund. Because these loans were no longer insured, we did not conduct further research or compliance testing. The remaining 16 loans still hold active Federal Housing Administration insurance with $1,654,877 in total original mortgage amounts and pose a risk to the insurance fund as of March 2, 2006.

Huntington signed certification letters for 13 of the 16 loans improperly submitted for late requests for endorsement and certified that all payments due were made by the borrowers before or within the month due for 12 loans and the escrow account for one loan was current. However, Huntington submitted the loans to HUD for late endorsement even though it had not received all payments due before or within the month due, and the escrow account was not current at the time of submission.

Appendix C of this report provides details of the federal requirements regarding late request for insurance endorsement as well as a citation for the Program Fraud Civil Remedies Act.

Huntington's assistant vice president provided us a letter dated August 17, 2005, regarding our late endorsement review results. The assistant vice president generally agreed with our findings, but disagreed with the number of loans recommended for indemnification and the number of loans subject to the Program Fraud Civil Remedies Act.

Huntington Took Corrective Action, but Additional Action Is Needed

During our audit period of January 1, 2003, through December 31, 2004, Huntington's insuring department was responsible for submitting loans to HUD for late requests for endorsement. When processing loans, Huntington's employees used an insuring procedures manual. The manual did not provide adequate guidance since it did not require the employees to ensure that borrowers' mortgage payments met HUD's requirements regarding late requests for endorsement before they submitted the loans to HUD.

Instead, the manual contained instructions on how to track and receive a loan and fund upfront mortgage insurance premiums, Federal Housing Administration connection instructions, and a checklist that required the employees to ensure the completeness of loan documents contained in Huntington's loan files. Huntington lacked adequate procedures and controls to ensure that its employees properly determined whether loans were subject to HUD's late requests for endorsement requirements. In addition, Huntington's quality control plan did not include a review of loans to determine whether they met HUD's late endorsement requirements.

After we provided our preliminary audit results in August 2005, Huntington's post-closing manager retrained all applicable staff and placed the two individuals responsible for the incorrect loan submissions on performance improvement plans. On May 18, 2005, Huntington's assistant vice president trained the quality control staff to review loans for HUD's late loan endorsement requirements when reviewing a closed loan through the Second Look software program. They were trained on how to properly read borrowers' payment histories and HUD's requirements regarding late requests for endorsement. Again, after we provided our preliminary audit results, Huntington's Second Look program was updated on September 12, 2005, to query the quality control reviewer if the mortgage insurance certificate was in the file and received within 60 days. This was put in place for the quality control reviewer to make sure the loan was endorsed in 60 days and if not determine whether the payments were current when the loan was submitted for endorsement. If the reviewer finds that the loan was not endorsed in accordance with HUD's late loan endorsement requirements, an exception is noted and it is brought to the attention of Huntington's assistant vice president and post closing manager.

According to HUD's Neighborhood Watch, Huntington submitted 7 out of 60 loans for late endorsement from June 1 through September 30, 2005, which represents nearly a 12 percent late endorsement rate. During this same period in 2004, Huntington submitted 58 of 183 loans late for endorsement for more than a 31 percent late endorsement rate. We did not determine whether the seven loans met HUD's requirements; we only used the information to determine whether Huntington's late endorsement rate increased or decreased.

Huntington should implement adequate procedures and controls to ensure that it follows HUD's requirements for late endorsements. Using the 13 loans improperly submitted for late endorsement with incorrect certifications from the 761 we tested with mortgage amounts totaling more than $88.9 million, the estimated total risk to the Federal Housing Administration is at least $759,447 for the next year if Huntington does not improve its late endorsement procedures and controls (13 divided by 761 times $88,913,679 in mortgages for two years).

Recommendations

We recommend that HUD's assistant secretary for housing-federal housing commissioner require Huntington to

1A. Indemnify HUD for any future losses on 14 loans (1 defaulted and 13 active with certifications that violated the Program Fraud Civil Remedies Act) with a total mortgage value of $1,477,215 and take other appropriate actions.

1B. Follow through on its Second Look software program that was started during this audit. Compliance with this program should ensure that $759,447 in funds will be put to better use over the next year.

We also recommend that HUD's assistant secretary for housing-federal housing commissioner

1C. Take appropriate action against Huntington for violating the requirements in effect at the time when it submitted two loans with a total mortgage value of $177,662 without the proper six month payment histories.

We recommend that HUD's associate general counsel for program enforcement

1D. Determine legal sufficiency and if legally sufficient, pursue remedies under the Program Fraud Civil Remedies Act against Huntington and/or its principals for incorrectly certifying that all payments due were made by the borrowers before or within the month due for 12 loans and the escrow account for one loan was current when submitted for Federal Housing Administration insurance endorsement when the escrow account was not current.

Finding 2: Huntington Generally Complied with HUD's Underwriting Requirements

Huntington generally complied with HUD's underwriting requirements for 32 loans reviewed. However, Huntington inappropriately underwrote Federal Housing Administration loans when it funded two loans that subsequently went to a claim or default status. The underwritten loans also included excessive and/or unallowable fees charged to borrowers on five loans totaling $1,325. In addition, Huntington incorrectly certified that due diligence was exercised during the underwriting of 5 of the 32 loans reviewed when it was not. The underwriting deficiencies occurred because Huntington's underwriters did not adequately evaluate information presented to them for compliance with HUD's requirements before approving the loans. As a result, HUD's Federal Housing Administration insurance fund was put at risk due to the inappropriately underwritten loans and excessive and/or unallowable fees charged.

Improper Underwriting of Federal Housing Administration Loans

Huntington sponsored 2,346 Federal Housing Administration loans between January 1, 2003, and December 31, 2004. Of the 2,346 loans, 24 loans defaulted and HUD paid a partial or full claim on eight as of February 27, 2006. We reviewed all 32 loans (24 defaults and 8 claims) for compliance with HUD's underwriting requirements. Based on our review, Huntington generally complied with HUD's underwriting requirements. However, it underwrote and approved two loans based on overstated income, understated liabilities, and no valid compensating factors.

Paragraph 2-7 of HUD Handbook 4155.1, REV-5, states for most cases, borrower income will be limited to salaries and wages. However, several other types of income may be treated as effective income. To include other types of income as effective income, the lender must obtain additional documentation to support its determination that these other sources of income can be expected to continue for the first three years of the loan. For example, for overtime income to be included as effective income, an earnings trend needed to be established. To do so, the lender must document the income for the past two years and determine the income can reasonably be expected to continue.

Huntington overstated the borrower's income on Federal Housing Administration loan number 151-7669678. In this case, Huntington included overtime income in its calculation without verifying such income for the previous two years and/or justifying the likelihood of continuance.

Paragraph 2-11 of HUD Handbook 4155.1, REV-4, requires a lender to consider all recurring obligations, contingent liabilities, and projected obligations that meet

HUD's specific guidelines when evaluating a loan application. In computing debt-to-income ratios, the lender must include all borrower liabilities extending 10 months or more. Debts lasting less than 10 months must be counted if the amount of the debt affects the borrower's ability to pay immediately after loan closing.

Huntington did not consider all outstanding liabilities when approving Federal Housing Administration loan number 413-4129633. It did not include four revolving credit accounts and one installment loan with a combined total of $126 worth of recurring liabilities and a total balance of $2,864.

Paragraphs 2-12 and 2-13 of HUD Handbook 4155.1, REV-4 and REV-5, specify that the ratio of mortgage payments to effective income (front ratio) generally may not exceed 29 percent and the ratio of total fixed payments to effective income (back ratio) may not exceed 41 percent unless significant compensating factors are presented. The handbook allows greater latitude in considering compensating factors for the front ratio than the back ratio.

In both loans (151-7669678 and 413-4129633) previously mentioned, the borrowers' debt-to-income ratios calculated by Huntington exceeded the handbook's requirements, yet it approved the loans and submitted them for insurance endorsement without presenting valid compensating factors. In addition, after adjusting for the overstated income and understated liabilities as previously discussed, the borrowers' debt-to-income ratios continued to exceed HUD's requirements for both loans.

HUD Handbook 4000.2, REV-2, provides guidance as to what customary and reasonable closing costs and fees can be collected by the lender from the borrower. Chapter 2-15 of the HUD Homeownership Center Reference Guide provides a more detailed description of closing costs and fees. Whenever actual costs are permitted, it is expected that they will not exceed reasonable and customary costs for the area.

An unallowable fee is one that the local HUD office identified as not being a necessary/normal part of the loan origination process. An unearned fee is a closing cost that has no service or thing of value attached to it. An excessive fee is a closing cost charged to the borrower beyond the amount allowed by HUD.

For five loans we reviewed, Huntington failed to ensure that the borrowers were not charged excessive and/or unallowable fees. The fees were not accompanied by supporting documentation or justification for any of the five loans. As a result, Huntington allowed a total of $1,325 in excessive and/or unallowable fees (ranging from $235 to $385 per loan) to be charged to the borrowers.

Further, Huntington's underwriters incorrectly certified that due diligence was exercised in the underwriting of 5 (includes loans discussed previously) of the 32 loans reviewed when it was not. When underwriting a loan, HUD requires underwriters to certify the integrity of data, a review of the appraisals (if applicable), and the loans eligibility to be a Federal Housing Administration approved automated underwriting system loan. After underwriting a Federal Housing Administration loan, HUD requires the direct endorsement underwriters certify that they reviewed all associated documents and used due diligence in underwriting the mortgages.

Appendix D of this report provides a summary of all loans for which Huntington's underwriters incorrectly certified that due diligence was exercised in underwriting the loans. Appendix E provides a summary of all loans for which we are recommending a repayment of an excessive and/or unallowable fee. Appendix F provides a detailed description of all loans with underwriting deficiencies noted in this finding for which we are recommending indemnification.

Huntington Needs to Implement Adequate Procedures and Controls for Underwriting of Loans

Huntington needs to ensure that its underwriters fully understand HUD's requirements regarding allowable closing cost and prudent lending practices when underwriting Federal Housing Administration loans. It needs to implement adequate procedures and controls to provide reasonable assurance that its underwriters follow HUD's underwriting requirements, thereby ensuring that HUD endorses only Federal Housing Administration loans that have allowable or eligible amounts for insurance and protecting the Federal Housing Administration fund from future risks. Using the total original mortgage amount for 24 loans and/or the claims HUD paid on eight loans, the estimated total risk to the Federal Housing Administration is $237,484 per year if Huntington does not improve its underwriting procedures and controls (5 divided by 32 times $3,039,797 in claims and original mortgage amounts paid for two years).

Recommendations

We recommend that HUD's assistant secretary for housing-federal housing commissioner require Huntington to

2A. Indemnify HUD against potential future losses on two loans (151-7669678 and 413-4129633) totaling $228,470 that were inappropriately underwritten cited in this finding.

2B. Reimburse the borrowers or HUD as appropriate $1,325 in excessive and/or unallowable fees that violated HUD's requirements for the five loans cited in this finding.

2C. Implement procedures and controls to ensure its underwriters follow HUD's underwriting requirements. Such procedures and controls must include but are not limited to providing adequate training to the underwriters regarding HUD's underwriting requirements for Federal Housing Administration loans, adequately monitoring the underwriting of Federal Housing Administration loans to ensure full compliance with HUD's requirements, and ensuring the accuracy of its underwriting certifications submitted to HUD. These procedures and controls should help reduce risks to the Federal Housing Administration fund by $237,484 next year.

We recommend that HUD's associate general counsel for program enforcement

2D. Determine legal sufficiency and if legally sufficient, pursue remedies under the Program Fraud Civil Remedies Act against Huntington and/or its principals for incorrectly certifying that due diligence was exercised during the underwriting of five loans when it was not.

SCOPE AND METHODOLOGY

We conducted the audit at HUD's Columbus Field Office and Huntington's headquarters office. We performed our audit work between April and November 2005.

To achieve our objectives, we relied on computer-processed and hard copy data from Huntington, and data contained in HUD's Single Family Data Warehouse. We relied on the loan payment histories provided by Huntington, the certifications and loan payment histories in the case binders that Huntington submitted to HUD, and the various dates in Huntington's and HUD's data systems, including loan-closing dates, notice of rejection dates, submission dates, resubmission dates, and endorsement dates. We also relied on the documents in Huntington's case files and Federal Housing Administration files from HUD's Homeownership Centers.

In addition, we interviewed HUD's and Huntington's management and staff involved in processing late requests for endorsement, mortgage payments, and underwriting of Federal Housing Administration loans. Further, we reviewed HUD's rules, regulations, and guidance for proper submission and underwriting of Federal Housing Administration loans and Huntington's policies and procedures.

Using HUD's data system, we identified that Huntington sponsored 2,346 Federal Housing Administration loans with closing dates between January 1, 2003, and December 31, 2004. The total mortgage value of these loans was more than $264 million. In addition, we identified 32 loans that Huntington underwrote that went into default or claim. We selected and reviewed the 32 loans with a total mortgage amount of $3,225,330 to determine whether Huntington complied with HUD's underwriting requirements. We also reviewed the accuracy of Huntington's underwriting certifications for the loans improperly submitted for late endorsement and the loans inappropriately underwritten.

The following table depicts the adjustments made to the initial universe of 2,346 loans identified for late endorsement testing. A narrative explanation follows the chart.

Description of loans	Number of loans	Original mortgage amounts
Originated and/or sponsored by Huntington from January 1, 2003, through December 31, 2004	2,346	$264,366,252
Submitted within 66 days after closing *(before April 12, 2004)*	1,452	160,843,155
New construction	17	2,046,764
Submitted before the first payment was due	53	5,968,531
Transferred before submission	24	2,155,689
Closed after April 12, 2004	39	4,438,434
Loans tested	**761**	**$88,913,679**

For our late endorsement testing of the 2,346 loans in the initial universe, we removed 1,452 loans from our universe to limit it only to those loans received by HUD more than 66 days after the loans closed (before April 12, 2004).

We then removed 17 new construction loans and 53 loans that were submitted before the first payment due date because these loans were not subject to the 60-day pre-April 2004 submission requirements. We then identified 24 loans Huntington transferred the loan servicing to other lenders/servicers before submission for endorsement; therefore, we also removed these loans from our testing universe. We further removed 39 loans closed after April 12, 2004, not subject to the 90-day requirement.

While HUD requires lenders to submit loans for endorsement within 60 days of the loan closing and after April 12, 2004, an additional 30 days after closing, we allowed six additional days to ensure that we conservatively selected loans for further testing. We allowed six extra days because HUD's mailroom and endorsement contractor have three business days to process each loan and because any submission may be delayed in the mail for up to three days over a weekend.

The audit covered the period of January 1, 2003, through December 31, 2004. This period was adjusted as necessary. We conducted the audit in accordance with generally accepted government auditing standards.

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,
- Compliance with applicable laws and regulations, and
- Safeguarding resources.

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.

Relevant Internal Controls

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

- Program operations - Policies and procedures that management has implemented to reasonably ensure that a program meets its objectives.

- Validity and reliability of data - Policies and procedures that management has implemented to reasonably ensure that valid and reliable data are obtained, maintained, and fairly disclosed in reports.

- Compliance with laws and regulations - Policies and procedures that management has implemented to reasonably ensure that resource use is consistent with laws and regulations.

- afeguarding resources - Policies and procedures that management has implemented to reasonably ensure that resources are safeguarded against waste, loss, and misuse.

We assessed the relevant controls identified above.

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.

Significant Weakness

Based on our audit, we believe the following item is a significant weakness:

- Huntington lacked adequate procedures and controls over its late requests for insurance endorsement and underwriting of Federal Housing Administration loans (see findings 1 and 2).

FOLLOWUP ON PRIOR AUDITS

This was the first audit of Huntington's late requests for endorsement and underwriting of Federal Housing Administration-insured loans by HUD's Office of Inspector General (OIG).

The last two independent auditor's reports for Huntington covered the years ending December 31, 2003, and December 31, 2004. Both reports resulted in no findings.

In November 2003 and 2004, HUD's Quality Assurance Division performed two quality assurance reviews of Huntington. Both reviews resulted in findings that included nonconformance with HUD's requirements for a quality control plan and noncompliance with HUD's loan origination requirements by approving a loan with a temporary interest rate buy down without supporting documentation in the file to show the borrower's potential for increased income. Both of the findings were resolved and closed as of May 2004.

APPENDIXES

Appendix A

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

Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1A		$1,477,215
1B		759,447
2A		228,470
2B	$1,325	
2C		237,484
Totals	$1,325	$2,702,616

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or federal, state, or local policies or regulations.

2/ "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 later 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

Ref to OIG Evaluation **Auditee Comments**

Huntington
Mortgage Group

February 27, 2006

VIA FEDERAL EXPRESS

Mr. Ronald Farrell
Assistant Regional Inspector
General for Audit
U.S. Department of Housing
and Urban Development
Office of the Inspector General
Region V
200 North High Street, Room 334
Columbus, Ohio 43215

RE: Huntington National Bank
HUD OIG Draft Audit Report

Dear Mr. Farrell:

Huntington National Bank ("Huntington") is in receipt of the Draft Audit Report ("Report"), dated February XX, 2006, from the U.S. Department of Housing and Urban Development ("HUD" or "Department") Office of the Inspector General ("OIG"). The Report is based on a review of Huntington's procedures and practices in the submission of loans to the Department for Federal Housing Administration ("FHA") insurance endorsement and the underwriting of FHA-insured loans. The review was conducted between April and November of 2005, and covered loans with closing dates between January 1, 2003 and December 31, 2004.

The Report contains two findings, which state that Huntington generally complied with HUD requirements regarding late requests for insurance endorsement, as well as with HUD's underwriting requirements. Although the OIG has determined that Huntington substantially adhered to HUD guidelines regarding its case binder submission and underwriting practices, the Report alleges that, in a small number of cases, Huntington: (1) submitted late requests for FHA insurance endorsement to the Department; (2) omitted compensating factors during the underwriting process; (3) charged unallowable fees; and/or (4) made incorrect certifications in connection with the late endorsement requests and underwriting of certain loans. Based on these findings, the Report recommends that HUD require Huntington to: (1) indemnify the Department for any future losses in connection with 16 loans; (2) reimburse the borrowers or HUD approximately $1,500 in unallowable fees charged; (3) implement adequate procedures

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Ref to OIG Evaluation **Auditee Comments**

and controls to address deficiencies cited in the Report, including implementing underwriting controls and continuing to employ a software system designed to improve compliance with HUD's late endorsement requirements; and (4) in connection with certain loans involving incorrect late endorsement or underwriting certifications, determine the legal sufficiency and, if legally sufficient, pursue remedies under the Program Fraud Civil Remedies Act, 31 U.S.C. §§ 3801 et seq. ("PFCRA").

The OIG provided Huntington with an opportunity to submit written comments for inclusion in the final report. This response summarizes Huntington's history and operations, including several improvements Huntington has implemented in its case binder submission procedures, and addresses the individual findings in the Report. We appreciate the additional time afforded to Huntington to reply to the Report, as well as this opportunity to comment on the OIG's findings and recommendations.

I. BACKGROUND

The Huntington National Bank is a subsidiary of Huntington Bancshares, Inc., a $32 billion regional bank holding company headquartered in Columbus, Ohio. Huntington operates primarily in a five-state region that includes Ohio, Indiana, Michigan, West Virginia, and Kentucky. It also conducts select financial service activities in other states, including mortgage offices in New Jersey, Maryland, and Florida.

Huntington was approved by the Department as a supervised direct endorsement lender in August 1987. Huntington currently sponsors 91 active loan correspondents and acts as agent for six principals. Huntington is approved to originate FHA insured loans in the following HUD office jurisdictions: Baltimore, Charleston, Cincinnati, Cleveland, Columbus, Coral Gables, Detroit, Flint, Grand Rapids, Indianapolis, Louisville, and Newark.

During the relevant period from January 1, 2003 through December 31, 2004, Huntington originated or purchased 62,568 mortgages totaling $10.3 billion, including 2,346 FHA-insured loans totaling $264.4 million. While the number of loans submitted by Huntington to HUD is a small percentage of the total number of loans it originated during the audit period, Huntington takes its responsibilities in working with HUD to offer mortgage loans to deserving individuals seriously, values its good working relationship with HUD, and is committed to a standard of full compliance with HUD's requirements. Huntington is committed to working with HUD to extend credit to qualified borrowers and would never knowingly violate FHA requirements or endanger the reputation of Huntington or its employees. We continuously strive to adhere to applicable rules and

Ref to OIG Evaluation **Auditee Comments**

regulations, and are committed to educating and training employees on issues regarding FHA compliance.

II. RESPONSE TO THE FINDINGS

As previously noted, although the Report contains two findings in which the OIG determined that Huntington generally complied with FHA guidelines regarding underwriting and late requests for insurance endorsement, the Report alleges noncompliance with HUD requirements in a small number of cases and recommends action by HUD and the Departmental Enforcement Center regarding these assertions. Upon receipt of the draft Report, Huntington performed its own stringent analysis of the loans subject to the OIG's review. Based on Huntington's diligent examination, while Huntington acknowledges that deficiencies existed in certain late case endorsement submissions and underwriting documentation, Huntington disagrees with the number of instances of noncompliance and takes strong exception to certain of the recommendations made in the Report, including the suggestion that the Department consider pursuing remedies under PFCRA. Below we: (1) address each finding; (2) set forth our opposition to the OIG's recommendations regarding action under PFCRA in both findings; and (3) provide a brief discussion of the significant steps Huntington has taken to ensure compliance with FHA requirements.

A. FINDING 1 – HUNTINGTON GENERALLY COMPLIED WITH THE DEPARTMENT'S LATE CASE ENDORSEMENT REQUIREMENTS

In Finding 1, the Report asserts that, after reviewing 761 late case endorsement submissions made by Huntington, "Huntington generally met HUD's requirements regarding late requests for endorsement;" however, it alleges that 20 of the loans submitted did not conform to FHA guidelines. Specifically, while acknowledging that three of these loans have been paid in full, the Report alleges that the remaining 17 loans did not comply with HUD requirements regarding six monthly consecutive timely payments subsequent to delinquency but before submission to HUD. As a result, Finding 1 recommends that Huntington indemnify the Department in connection with 14 of these loans. In addition, in 13 of these 14 cases, the Report asserts that Huntington incorrectly certified that the mortgage and/or the escrow accounts were current and recommends that HUD's Associate General Counsel for Program Enforcement determine the legal sufficiency of and, if sufficient, pursue remedies under the PFCRA for the incorrect certifications in these cases. As discussed in detail below, Huntington takes exception to both the number of cases cited in the Report involving late submission and incorrect certifications, as well as with the unduly harsh and inappropriate recommendations to impose PFCRA penalties made in connection with this finding.

1. **Any Deficiency in Connection With the Cases Cited Was Contrary to Huntington Policy and Resulted From Increased Loan Volume**

As you know, HUD requires lenders to submit case binders involving a mortgage originated under the Direct Endorsement program for FHA insurance endorsement to the appropriate HUD Homeownership Center ("HOC") so that it is received within 60 days after closing. See 24 C.F.R. § 203.255(b); HUD Handbook 4165.1 REV-2, ¶ 2-2; HUD Handbook 4000.2 REV-3, ¶ 5-5(A). While, at the time, HUD required a mortgagee to submit a case binder for FHA insurance endorsement within 60 days of loan closing or funding, it permitted late requests for endorsement so long as certain requirements were met. Prior to April 12, 2004, HUD Handbook 4165.1 REV-1, ¶ 3-1 governed late case endorsement requirements. This guideline provided that, when submitting a late request for insurance endorsement, a lender was required to include: (1) an explanation for the delay; (2) a certification that the escrow accounts were current and intact; (3) a certification that the lender did not provide the funds to bring a loan current; and (4) a payment ledger reflecting that all payments received, including the payment due in the month in which the lender submitted the case binder, were made within the calendar month due. See HUD Handbook 4165.1 REV-1, ¶ 3-1(B). If a payment was made outside the calendar month due, HUD required lenders to ensure that the borrower made six consecutive payments within the calendar month due before the lender could submit the loan for FHA insurance endorsement. See id. These guidelines were amended by HUD Mortgagee Letter 2004-14, which was issued on April 12, 2004. This revised guidance required FHA-approved lenders to include with any late request for insurance endorsement a certification stating that all payments due were made by the mortgagor prior to or within the month due or, if any payments had been made after the month due, that six consecutive payments at the time of submission had been made prior to or within the calendar month due. See Mortgagee Letter 04-14.

Huntington understands and appreciates that, at the time it submitted the loans subject to the OIG's review for FHA insurance endorsement, Huntington was responsible for ensuring that late requests for endorsement complied with these provisions. It was and is Huntington's policy and procedure to strictly comply with HUD requirements and at the time the loans at issue were submitted to the Department, if a case binder was submitted more than 60 days after closing, Huntington required its

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employees to ensure that the loan was either current or the borrower had made six consecutive payments prior to submission and that the case binder contained all additional required documentation. Huntington acknowledges, however, that a small number of the 761 late case endorsement requests made during the audit period did not strictly conform to these requirements.

These deficiencies occurred as a result of human error during a period of unprecedented mortgage refinance activity experienced by the entire mortgage industry and did not result from any intentional effort to circumvent FHA rules and regulations. During the time Huntington originated the loans cited in the Report, interest rates were at historical lows and mortgage companies were experiencing extreme difficulty in maintaining the staffing levels required to address the increased origination volume. This expanded volume also increased Huntington's difficulty in obtaining all required loan documents within 60 days of loan closing, and resulted in a higher than normal percentage of late requests for endorsement. In an effort to keep pace with the overwhelming paperwork that accompanied this increase, while still attempting to submit case binders for insurance endorsement on a timely basis, Huntington hired additional staff in the Loan Insuring department and supplemented its staff with temporary employees and overtime. It appears that, in a handful of cases, these inexperienced employees with little to no previous experience related to late case endorsement requirements inadvertently submitted case binders to the Department that did not fully comply with FHA requirements for such submissions in place at that time.

As discussed in detail below, Huntington has since taken significant steps to ensure that all Loan Insuring department employees receive training regarding FHA requirements for late endorsement requests and Huntington closely monitors its operations to ensure compliance with FHA requirements. Moreover, following the audit period, Huntington has experienced a reduction in loan volume that has resulted in a decrease in Huntington's percentage of late case endorsement submissions. According to data obtained from HUD's Neighborhood Watch System, Huntington's late endorsement rate for loans closed from January 1, 2004 through December 31, 2004 was 27.06% **(Exhibit A-1)**, and Huntington's late endorsement rate for loans closed from January 1, 2005 through December 31, 2005 further declined to 16.76% **(Exhibit A-2)**.

2. <u>Huntington Disagrees With the Number of Case Binders Containing Inaccuracies Cited in the Report</u>

As discussed above, upon receipt of the Report, Huntington conducted a diligent review of the allegations and loans cited therein. While Huntington recognizes that

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errors occurred in certain cases cited in the Report, Huntington takes exception to the number of loans that the Report alleges were inaccurately submitted, as well as the number of inaccurate certifications cited in the Report.

a. Huntington Disagrees with the Number of Inaccurate Case Binder Submissions Cited in the Report

Of the 17 loans at issue in Finding 1, Huntington believes that all but one of these cases should be removed from consideration in this review. As discussed in detail below, 16 of these loans were either: (1) paid in full; (2) complied with HUD guidelines in effect at the time of case binder submission; or (3) would comply with current HUD guidelines. As fully discussed below, none of these 16 loans posed a risk to the FHA Insurance Fund and, therefore, should be removed from the final report.

i. Loans Paid in Full or in Compliance with HUD Guidelines at the Time of Submission Should be Removed from the Report

As stated above, Finding 1 alleges that Huntington improperly submitted 20 late case endorsement requests during the audit period, as these borrowers had not made six consecutive payments after a delinquency but prior to submission. The Report states that three of these loans have been subsequently paid in full and, as they no longer represent a risk to the FHA Insurance Fund, Finding 1 makes no recommendations regarding these loans. Of the 17 loans remaining, one additional loan, [redacted] – **FHA Case No. 411-3605152**, has also been paid in full **(Exhibit B-1)**. As this loan no longer represents a risk to the Department, indemnification is unwarranted and this loan should be removed from the final report. **Comment 1**

Moreover, in the [redacted] loan, **FHA Case No. 412-5204306**, contrary to the allegation in the Report, Huntington submitted this case binder in compliance with HUD guidelines in place at the time of submission. As discussed above, FHA requirements in effect when this loan was originated dictated that, for late case endorsement requests, a borrower must have made all loan payments due within the month due. See HUD Mortgagee Letter 04-14. In accordance with this requirement, Huntington ensured that the borrower had made all payments due prior to or within the month due before forwarding the case binder to the Department **(Exhibit B-2)**. The payment history in this loan evidences that the borrower made the first July 2004 payment on June 29, 2004, the August 2004 payment on July 27, 2004, and the September 2004 payment on August 23, 2004 **(Exhibit B-2)**. The loan was submitted for late case endorsement on October 12, 2004. While the borrower had not yet made the October 2004 payment at **Comment 2** the time of submission, the month was not over and, according to the requirement that all payments be made in the month due, this loan was considered current under HUD's late case endorsement requirements at the time of submission. As Huntington complied with HUD guidelines in submitting this loan to HUD, indemnification would be inappropriate and this loan should be removed from the final report.

Removing these two loans from consideration would reduce the number of loans cited in Finding 1 to 15 loans.

ii. Loans in Compliance with Current HUD Guidelines Should be Removed from the Report

Additionally, the Department recently amended its late case endorsement requirements. Under current guidelines, rather than require lenders to document a six-month consecutive pay history, HUD now expects lenders merely to certify that, at the time of late submission, no mortgage payment is currently unpaid more than 30 days. See HUD Handbook 4165.1 REV-2, ¶ 3-1; Mortgagee Letter 05-23. The Department expressly stated that its rationale for eliminating the six-month requirement was based on its assessment that the "risk at insurance endorsement is based by the status of the mortgage at the time of endorsement," rather than during any time prior to endorsement. See Mortgagee Letter 05-23.

Huntington's review of the remaining 15 loans identified that 13 of those loans were current at the time of submission, even though a six-month consecutive payment history may not have been present at that time. The following chart demonstrates that, as of the endorsement date in each of these 13 cases, the borrower had either made the most recent mortgage payment or was not more than 30 days behind on payments.[1]

FHA Case Number	Endorsement Date	Due Date at Endorsement	Exhibit
151-7221330	8/23/2004	9/1/2004	C-1
412-5170753	6/10/2004	7/1/2004	C-2
413-4318632	10/19/2004	10/1/2004	C-3

[1] We also note that [redacted], **FHA Case No. 411-3605152**, which has been paid in full and no longer represents a risk to the Department, would have complied with current FHA guidelines, as the loan was endorsed on October 17, 2003, and the next payment due date at that time was for October 1, 2003 **(Exhibit C-14)**.

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FHA Case Number	Endorsement Date	Due Date at Endorsement	Exhibit
413-4308171	11/29/2004	12/1/2004	C-4
413-4285744	10/13/2004	10/1/2004	C-5
261-8755989	1/20/2005	1/1/2005	C-6
413-4321030	2/4/2005	3/1/2005	C-7
413-4329901	1/14/2005	1/1/2005	C-8
412-5111971	2/10/2004	2/1/2004	C-9
411-3754098	2/16/2005	2/1/2005	C-10
413-4393519	2/17/2005	2/1/2005	C-11
412-4964010	4/20/2004	5/1/2004	C-12
413-4135429	11/12/2003	12/1/2003	C-13

Comment 3

As these 13 loans were current at the time of endorsement, and as the Department has since acknowledged that these loans therefore did not present a risk to the FHA Insurance Fund, we believe that indemnification likewise would be inappropriate in these loans. We note that the OIG has agreed with this conclusion in at least two recent Final Audit Reports involving Washington Mutual, Inc., see Audit Rpt. No. 2005-SE-1006 (July 5, 2005), and National City Mortgage Company, see Audit Rpt. No. 2005-CH-1015 (Aug. 23, 2005). In those reports, the OIG adjusted its recommendations to reflect HUD's recent change in late submission guidelines and removed loans that would comply with current guidelines from its indemnification recommendation. Based on these recent reports, these 13 loans should be removed from the loans under consideration in this matter. After removal of the 13 loans from the 15 remaining cases, only 2 cases should be the subject of this review.

Comment 4

In one of these remaining cases [redacted] – **FHA Case No. 412-5226064**, the loan was current on January 25, 2005, when Huntington initially shipped the case binder to HUD for insurance endorsement. By the time the Department received the case binder on February 2, 2005, however, the loan was no longer current, as the borrower had not made the January 2005 payment by February 1, 2005. Thus, Huntington acknowledges that, at the time HUD issued the Mortgage Insurance Certificate on February 3, 2005, the loan would not have complied with current FHA guidelines. Nevertheless, the payment history in this case demonstrates that the borrower made the January 2005 payment on February 14, 2005, and the February 2005 payment on February 28, 2005 **(Exhibit D)**. Based on these payments, under the current HUD requirements for late endorsement, this loan would have been eligible for submission in

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March 2005. This documentation evidences that, under current HUD guidelines, this loan became current within a few days after insurance endorsement and, as a result, ultimately did not present a risk to the FHA Insurance Fund. Accordingly, we respectfully submit that indemnification would not be appropriate and request that this loan be removed from the final report.

Comment 5

Finally, it is important to note that, in 5 of the 13 cases in which the case binders would have complied with current HUD requirements, the borrowers made six consecutive payments subsequent to initial submission and, had the case binders been submitted at a later date, the loans would have been eligible for FHA financing even under former FHA requirements. These loans are as follows: (1) **FHA Case No. 151-7221330**; (2) **FHA Case No. 412-5170753**; (3) **FHA Case No. 413-4318632**; (4) **FHA Case No. 413-4308171**; and (5) **FHA Case No. 413-4285744 (Exhibits E-1 through E-5)**. While Huntington understands and appreciates that inaccuracies may have occurred at the time of submission, these loans have since performed and no longer pose a risk to HUD. Therefore, Huntington maintains that indemnification is not an appropriate remedy in these five loans.

Comment 6

In summary, evidence provided by Huntington demonstrates that, in 2 of the 17 loans at issue in the Report, either the loan has been paid in full or Huntington in fact complied with HUD requirements at the time it submitted the case binder to the Department. As these loans do not represent a risk to the FHA Insurance Fund, indemnification is unwarranted and the Department's figures should be reduced to 15 loans. Furthermore, of the remaining loans, as 13 loans would have complied with current FHA guidelines for late endorsement requests, and one additional loan complied with such requirements within a few days of endorsement, none of these 14 loans represented a risk to the Department. Based on HUD's recent statements regarding the absence of risk presented to the Department by these cases, as well as the OIG's recent adjustment to similar recommendations as a result of HUD's guidance, indemnification is not warranted in these cases, which reduces the loans under consideration to only one case, which is discussed below. Therefore, Huntington maintains that, at most, only one case should be under consideration in connection with Finding 1 of this review.

b. Huntington Disagrees with the Number of Inaccurate Late Case Endorsement Certifications Cited in the Report

In addition to the above allegations, Finding 1 asserts that, in 12 of the 17 loans discussed above, the case binder contained a certification that incorrectly indicated that

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all payments due were made by the borrowers before or within the month due, and that, for one additional loan, the escrow account was current. After reviewing these allegations, Huntington respectfully disagrees that these certifications were inaccurate in two of the loans at issue.

First, as discussed above, in th[redacted]oan, **FHA Case No. 412-5204306**, contrary to the allegation in the Report, Huntington submitted this case binder in compliance with HUD guidelines in place at the time of submission. In accordance with Mortgagee Letter 04-14, Huntington ensured that the borrower had made all payments due prior to or in the month due before forwarding this case binder to the Department for insurance endorsement. The payment history evidences this fact **(Exhibit B-2)**. Therefore, the certification contained in the case binder **(Exhibit F)**, which indicated that all payments due had been made prior to or within the month due, was accurate and fully adhered to HUD requirements in place at that time. See Mortgage Letter 04-14. As Huntington complied with HUD's certification requirements in this case, the Report's allegation and recommendation regarding this certification is unwarranted and should be removed from the final report.

Comment 7

Moreover, in t[redacted]oan, **FHA Case No. 201-3271960**, while Huntington acknowledges that this loan was incorrectly submitted for FHA insurance endorsement, Huntington takes exception to the allegation that the escrow certification in this case was not accurate. This loan closed on August 8, 2003 and was submitted for late endorsement on October 31, 2003. The borrower's first payment was due on October 1, 2003 **(Exhibit G-1)**. While the loan was not current at the time of submission, the month in which the first payment was due had not yet elapsed. As a result, when Huntington submitted the loan to the Department on October 31, 2003, the borrower had not yet been required to make any payments to the escrow account in this case, aside from the escrow funds prepaid at closing. Therefore, at the time of submission, the escrow account was still current and the certification in this case stating that the escrow accounts were current and intact was accurate **(Exhibit G-2)**. As the statements contained in this certification were correct, the Report's allegation and recommendation regarding the certification is inappropriate and should be removed from the final report.

3. Huntington Takes Strong Exception to the Recommendation that PFCRA Penalties Are Appropriate in this Case

Comment 8

As noted above, in Finding 1, the Report alleges that Huntington incorrectly certified that the mortgage and/or the escrow accounts for 13 loans cited in the Report were current and recommends that HUD's Associate General Counsel for Program

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Enforcement determine the legal sufficiency of and, if sufficient, pursue remedies under PFCRA for the incorrect certifications in these cases. As discussed in detail above, Huntington takes exception to the inclusion of 2 cases in this allegation. Importantly, however, Huntington believes that two of these certifications were in fact accurate and should be removed from consideration. In the remaining cases, Huntington takes strong exception to this recommendation. As you know, HUD is authorized to impose civil penalties under PFCRA against persons who "make, submit, or present, or cause to be made, submitted, or presented, false, fictitious, or fraudulent claims or written statements to Federal authorities or to their agents." 24 C.F.R. § 28.1. For the reasons that follow, Huntington strongly disagrees with the inclusion of such an inflammatory recommendation in this instance.

a. Huntington Did Not Intend to Submit Incorrect Certifications in the Cited Loans

First and foremost, Huntington believes that this recommendation is unduly harsh given that the Report does not allege, and there is no evidence to suggest, that Huntington or its employees intended to circumvent HUD late case endorsement requirements. The certifications in these cases were not executed in an attempt to mislead the Department regarding the status of the loans at issue. Rather, any incorrect certifications resulted from inadvertent errors caused by Huntington's retention of new and inexperienced staff and its efforts to timely submit case binders for FHA insurance in the midst of the mortgage industry's largest refinance boom. In fact, the Report acknowledges that Huntington generally complied with HUD's late case endorsement requirements and that any improper certifications resulted from an incomplete employee manual rather than intent on the part of Huntington to evade HUD requirements or knowingly misrepresent facts to the Department. Furthermore, incorrect certifications were present in less than 2.0% of the 761 FHA loans Huntington submitted for late case endorsement during the audit period. Such a low error rate does not evidence a pattern or practice of deficiency, but rather indicates inadvertent oversights in the manual case binder preparation process.

Importantly, the Report does not allege that Huntington or its employees knowingly misrepresented facts to the Department or intentionally provided false information in the cases at issue. Before imposing penalties on FHA-approved lenders, HUD weighs a number of factors, including whether the deficiency was intentional or resulted from errors on the lender's part, whether there was any injury to the public, and the mortgagee's history of prior offenses. While intentional violations or a disregard for HUD requirements can lead to severe sanction, such as PFCRA penalties, HUD usually

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imposes less severe consequences, such as indemnification, for deficiencies caused by unintentional error. The Report recommends such lighter sanctions in these cases, but takes its recommendations one step further by including the PFCRA recommendation in Finding 1. By adding this recommendation, the OIG effectively alleges that Huntington engaged in fraud while at the same time acknowledging that the inaccuracies in these cases resulted from human error. This allegation would have an extremely detrimental effect on Huntington's reputation and could create a chilling effect on other mortgage lenders who want to participate in the FHA Program. Enforcement actions are meant to reinforce HUD's rules and regulations, rather than discourage broad participation in FHA lending or needlessly punish FHA lenders. In the interests of all parties, therefore, we believe the OIG should reconsider its PFCRA recommendation in this case and reserve such assertions for other cases involving fraudulent actions against the Department.

We also note that, in each of the cases cited in Finding 1, the review practices of HUD's staff were also deficient. As you know, the Department conducts a pre-endorsement review on 100% of the case binders submitted for endorsement. When those case binders contain late requests for endorsement, HUD staff members review the binders to determine whether all additional documentation is included, and to ensure that the loan is current, before endorsing the loan. In each of the cases cited in Finding 1, a HUD employee reviewed the case binder documents, determined that all information was accurate and complete, and issued an FHA insurance policy. We suspect that the oversights that occurred in the Department's pre-endorsement reviews resulted from having to hire inexperienced staff to timely review the increased volume of loans being submitted for insurance endorsement during the high volume of the refinance boom. Had these individuals diligently reviewed the case binders and identified the incorrect certifications at that time, the Department could have significantly mitigated its risk in connection with these cases. While Huntington acknowledges that it is ultimately the lender's responsibility to ensure that all case binder documentation is accurate and complete, we believe that this discussion demonstrates that human error occurred at both Huntington and the Department in connection with the loans cited in Finding 1. Huntington maintains that alleging violations under PFCRA in this matter is unduly harsh.

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b. Recent Amendments to Late Case Endorsement Requirements Make the PFCRA Recommendation Unnecessary

Comment 9

In addition, as stated above, the Department's current guidelines require lenders merely to certify that, at the time of late submission, no mortgage payment is currently unpaid more than 30 days, rather than to document a six-month consecutive pay history. See HUD Handbook 4165.1 REV-2, ¶ 3-1; Mortgagee Letter 05-23. HUD eliminated the six-month history requirement based on evaluation of the risk to the Department in late case requests and its determination that the "risk at insurance endorsement is based by the status of the mortgage at the time of endorsement," rather than during any time prior to endorsement. See Mortgagee Letter 05-23. As indicated above, Huntington's review identified 14 loans that would have met the Department's current late case endorsement requirements, had those provisions been in place when Huntington submitted the case binders to HUD. While Huntington appreciates that it was required to comply with HUD guidelines in place at the time of submission, Huntington believes that it is both unnecessary and inappropriate to recommend penalties under a statute designed to combat fraud against the government in connection with loans that, if submitted today, would fully comply with HUD requirements. Thus, at the very least, the Report should remove those loans that would comply with current HUD requirements from any recommendation regarding the imposition of PFCRA penalties.

c. The Recommendation Constitutes Selective Enforcement

Comment 10

Finally, Huntington believes that it is being audited under different standards than other national lenders that the OIG determined were not in compliance with HUD's late case endorsement requirements. For instance, in recent years, the OIG has issued reports alleging that three national lenders submitted inaccurate information regarding the content of case binder documentation. See Audit Rpt. No. 2004-KC-1003 (July 16, 2004); Audit Rpt. No. 2003-KC-1004 (Jan. 17, 2003); Audit Rpt. No. 2003-KC-1001 (Oct. 2, 2002). Not one of these reports, however, recommended that the Department consider PFCRA penalties. Furthermore, in a recent audit report issued on July 5, 2005, the OIG took issue with another national lender's late case request practices, but refrained from including a recommendation that HUD consider PFCRA penalties. See Audit Rpt. No. 2005-SE-1006. Huntington believes that the OIG should examine and make recommendations for national lenders based on a similar set of standards to ensure that lenders are not audited differently by different OIG offices or disadvantaged

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by their geographical location in one OIG jurisdiction versus another. Here, Huntington believes that it is being held to a different standard than other national lenders that have had late case endorsement concerns raised by the OIG. We therefore respectfully request that the OIG use its discretion in making recommendations to ensure that national lenders receive consistent treatment from the agency.

4. Corrective Actions Taken by Huntington

Finally, while the Report alleges that Huntington lacked adequate procedures and controls to ensure that it followed HUD requirements regarding late requests for insurance endorsement during the audit period, the Report acknowledges that Huntington has taken significant steps to ensure that future case binder submissions made 60 days or more after loan closing fully comply with all applicable HUD guidelines and documentation requirements.

For example, as acknowledged in the Report, Huntington retrained all personnel responsible for submitting loans for FHA loan insurance to ensure their complete understanding of the applicable HUD requirements and placed two individuals responsible for the incorrect loan submissions on performance improvement plans. Huntington has also trained its Quality Control staff to review loans submitted for late case endorsement to ensure compliance with HUD guidelines. This training included reviewing closed loans through Huntington's Second Look software program as well as guidance on accurately interpreting payment histories. Moreover, Huntington will ensure that any new associates receive training on interpretation of loan payment histories in addition to HUD requirements. Finally, Huntington has revised its written policies and procedures manual to require that a department supervisor review any loan that was previously suspended due to delinquency and determine adherence to FHA guidelines prior to submission.

Huntington will continue to monitor the Loan Insuring department to ensure compliance with Huntington policy and FHA guidelines. As discussed above, these improvements, along with an overall decrease in loan volume, have resulted in a substantial reduction in Huntington's late case submission rates.

B. FINDING 2 – HUNTINGTON GENERALLY COMPLIED WITH THE DEPARTMENT'S UNDERWRITING GUIDELINES

In Finding 2, the Report acknowledges that, after reviewing 32 loans originated by Huntington during the relevant period that had gone into default, "Huntington generally complied with HUD's underwriting requirements." Notwithstanding this

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finding, the Report alleges that Huntington: (1) improperly underwrote two FHA loans by overstating income or understating liabilities; (2) incorrectly certified that due diligence was used in underwriting five of the 32 loans reviewed; and (3) charged excessive or unallowable fees in six cases. Based on these allegations, the Report recommends that HUD require Huntington to indemnify the Department in two cases and refund the cited fees. In the five cases involving allegedly incorrect certifications, Finding 2 recommends that HUD's Associate General Counsel for Program Enforcement determine the legal sufficiency of and, if sufficient, pursue remedies under the PFCRA. As discussed in detail below, Huntington takes exception to both the number of cases cited in the Report involving underwriting issues, as well as with the unduly harsh recommendation to impose PFCRA penalties made in connection with this finding.

As our responses to these individual allegations indicate, Huntington has a proven track record of strong underwriting decisions in FHA-insured loans. According to data obtained from HUD's Neighborhood Watch system on February 15, 2006, Huntington's December 31, 2005 default rate for active loans originated from January 1, 2004 through December 31, 2005, was 1.65%, or 47% of the average default rate for the United States of 3.57% **(Exhibit H-1)**. Huntington was able to maintain its low default rate relative to the national average in spite of the high default rate of its primary lending states. For example, Huntington's default rate for Ohio for the same performance period is 1.51%, or 37% of the state average of 4.09% **(Exhibit H-2)**. The performance of the loans closed by Huntington during the two-year period under audit performed similarly well with a default rate of 1.36% at the time of the OIG audit. Our responses to the assertions in the Report similarly demonstrate Huntington's diligence in underwriting loans in accordance with HUD guidelines. We address each of the allegations in Finding 2 in turn below.

1. Huntington Complied with HUD Guidelines in Underwriting the Cited Loans

First, Finding 2 asserts that, in two cases, Huntington underwrote and approved cases based on overstated income or understated liabilities that had invalid or no compensating factors. The Report recommends that HUD request indemnification in both loans. As discussed in detail below, we disagree with the allegations in both cases.

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a. [redacted] – FHA Case No. 151-7669678

Comment 11

In this case, Finding 2 alleges that the borrowers' effective monthly income of $4,172 was overstated, as the loan file lacked evidence to justify receipt of continuing overtime income of $610. The Report asserts that, without considering the overtime income, the borrowers' fixed payment-to-income ratio increases to 48.31% and the Mortgage Credit Analysis Worksheet ("MCAW") did not include valid compensating factors to support this higher ratio. The Report also asserts that the loan file did not contain a copy of the disclosure required by the Truth in Lending Act, 15 U.S.C. §§ 1601 et seq. ("TILA").

With regard to the TILA disclosure, while a hard copy of this document may have been absent from Huntington's paper loan file at the time of the review, Huntington provided the borrowers with this disclosure at the time of closing and retained a copy of the disclosure in its imaged file. A copy of that disclosure is attached as **Exhibit I-1**.

With regard to the borrowers' effective income, contrary to the allegations in the Report, the loan file contained sufficient evidence to justify receipt of continuing overtime income. To include overtime earnings in a borrower's effective income, a lender must document that the borrower received such income for a period of two years and that the income is likely to continue, as well as establish an earnings trend for such income. See HUD Handbook 4155.1 REV-5, ¶ 2-7(A). Huntington fully complied with these guidelines in including such earnings in the borrowers' effective income and used a conservative estimate of overtime earnings to qualify these individuals for FHA financing.

To document the borrower's effective income, Huntington obtained a Verification of Employment ("VOE") indicating that the borrower had been employed in his current position for three and a half years **(Exhibit I-2)**, as well as the borrower's most recent pay stub **(Exhibit I-3)** and W-2 forms for 2002 and 2003 **(Exhibit I-4)**. The borrower's pay stub indicated that he had earned $7,598 in overtime income as of June 24, 2004 **(Exhibit I-3)**. While the W-2 forms provided for the previous two years did not break out the borrower's overtime earnings from his regular earnings, based on the $36,816 base salary indicated on his VOE **(Exhibit I-2)**, it was clear from the W-2 forms, which indicated total earnings of $44,570 in 2002 and $40,528 in 2003 **(Exhibit I-4)**, that the borrower had consistently earned overtime income during his 3.5 year tenure with his current employer. As the loan file documented the borrower had received overtime earnings for more than two years, and as there was no evidence in the loan file to suggest that such overtime was unlikely to continue, Huntington properly included such income in the borrowers' effective earnings in this case.

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To establish an earnings trend, Huntington subtracted the borrower's base salary of $36,816 from the total earnings in 2002 and 2003,[2] and averaged the documented overtime earnings of $7,754 in 2002 ($44,570 - $36,816 = $7,754), $3,712 in 2003 ($40,528 - $36,816 = $3,712) **(Exhibit I-4)**, and $7,598 in 2004 year-to-date as reflected on the pay stub **(Exhibit I-3)**, to arrive at average overtime for that 30-month period of $635.50 ($7,754 + $3,712 + $7,598 = $19,064 / $635.50). As indicated in the Report, the underwriter used a more conservative estimate of $610 in monthly overtime to qualify the borrowers. The underwriter similarly used conservative estimates of the borrowers' base salaries to arrive at the $3,562 used to qualify these individuals for the FHA loan **(Exhibits I-3 through I-5)**.

As evidenced in the above discussion and attached documentation, Huntington complied with HUD guidelines calculating the borrowers' effective income of $4,172 in this case, as well as including in that amount a conservative estimate of $610 in overtime income based on the borrower's documented 3.5 years of receiving such income and the establishment of an earnings trend over a 30-month period. As a result, the 41.25% fixed payment-to-income ratio documented on the MCAW was accurate based on the borrowers' earnings and liabilities in this case **(Exhibit I-6)**. While the Report points out that this qualifying ratio was slightly over HUD's benchmark guideline of 41%, see HUD Handbook 4155.1 REV-5, ¶ 2-12, Huntington disagrees with the assertion that the loan file did not contain sufficient compensating factors to offset this very slightly higher percentage. For instance, HUD guidelines expressly state that the fact that a "borrower receives documented compensation or income not reflected in effective income, but directly affecting the ability to pay the mortgage" constitutes a compensating factor to offset higher-than-average qualifying ratios. HUD Handbook 4155.1, REV-5, ¶ 2-13(E). In this case, the borrower's pay stub indicated that he earned regular bonus income that was not included in the effective income **(Exhibit I-2)**, but would directly affect the borrowers' ability to meet their payment obligations in this case. Moreover, FHA requirements state that a minimal increase in the borrower's housing expense also compensates against higher qualifying ratios. In this case, the MCAW indicates that the borrowers experienced only a modest housing expense increase by obtaining this FHA loan **(Exhibit I-6)**. These factors more than compensated for the 41.25% back-end ratio in this case.

In summary, Huntington fully complied with HUD requirements in underwriting the [redacted]an. The loan file clearly documented the borrower's regular overtime

[2] Please note that these calculations are based on the conservative assumption that the borrower did not receive normal pay increases during this 30-month period.

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earnings for the past 30 months, and the underwriting established an earnings trend to support the overtime amount included in the borrowers' effective income. Moreover, while the fixed payment-to-income ratio in this case slightly exceeded HUD's benchmark guideline, compensating factors documented in the file more than offset this factor. Huntington adhered to HUD requirements and the underwriter reasonably determined that these borrowers qualified for FHA financing. Therefore, we believe that indemnification of this loan is unwarranted and that these allegations should be removed from the final report.

b. [redacted] – FHA Case No. 413-4129633

Comment 12

In th[redacted]oan, the Report asserts that the recurring liabilities referenced on the MCAW are understated by $126, as the underwriter did not include five credit accounts with a total balance of $2,864 and a combined monthly payment amount of $126. Finding 2 alleges that, when the $126 monthly payment is included, the borrower's fixed payment-to-income ratio increases to 44%; however, the MCAW did not include valid compensating factors to support this higher ratio.

Huntington understands and appreciates that, in computing debt-to-income ratios, a lender must include the monthly housing expense and all other additional recurring charges extending ten months or more. See HUD Handbook 4155.1 REV-4, CHG-1, ¶2-11(A); see also HUD Handbook 4155.1 REV-5, ¶ 2-11(A). It is Huntington's policy and practice to do so in every FHA transaction. In this instance, at the time this loan was underwritten, the underwriter had received verification that the liabilities in question were being paid at closing and, therefore, excluded these payments from the calculation of debt-to-income ratios on the MCAW **(Exhibit J-1)**. Contrary to the information used to underwrite the loan, however, the borrower did not satisfy the referenced liabilities as intended at closing. While Huntington appreciates that the MCAW should have been revised to include liabilities, any oversight in this case resulted in, at worst, harmless error. Although the inclusion of the liabilities would have increased the borrower's qualifying ratios, the loan file contained evidence of substantial compensating factors that would have offset this increase. For instance, this transaction was a FHA cash-out refinance of an existing FHA-insured loan **(Exhibit J-2)**. The loan-to-value ratio was 86% based upon a loan amount of $99,200 and an appraised value of $115,000 **(Exhibit J-1)**. Moreover, the borrower reduced her interest rate from 8% to 6% as a result of this transaction, which reduced the borrower's monthly housing obligation by $182.80 **(Exhibit J-1)**. As discussed above, FHA requirements state that a minimal increase in the borrower's housing expense also compensates against higher qualifying ratios. See HUD Handbook 4155.1 REV-4,

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CHG-1, ¶ 2-13. Here, the transaction actually provided housing payment relief to the borrower. In addition, the reduction of $182.80 in monthly housing expense exceeded the $126 of recurring liabilities not included in the borrower's ratios. Thus, the reduction in housing expense achieved through this transaction more than offset the inadvertent exclusion of the $126 in liabilities at issue.

In addition to these compensating factors, the loan file demonstrated that the borrower had a stable employment history, as she had been employed with her current employer for six years **(Exhibit J-3)**. Moreover, the borrower was a head-of-household single parent who received regular child support, as evidenced by a court-ordered child support statement and a history of the support being received contained in the file **(Exhibit J-4)**. As indicated on the MCAW, the underwriter used a more conservative figure for child support income than was documented in calculating the borrower's qualifying ratios **(Exhibit J-1)**. Thus, the loan file documented "compensation or income not reflected in effective income, but directly affecting the ability to pay the mortgage" which HUD has expressly stated should compensate for higher qualifying ratios. See HUD Handbook 4155.1 REV-4, CHG-1, ¶ 2-13. Finally, the borrower had originally acquired the property securing this FHA loan in December of 1999 and, at the time of underwriting, had demonstrated her ability consistently to make a monthly mortgage payment of $907 for three and one-half years **(Exhibit J-5)**. Importantly, HUD requirements in place at the time this loan closed stated that, "if the borrower over the past 12-24 months has met his or her housing obligation as well as other debts, there should be little reason to doubt the borrower's ability to continue to do so despite having ratios in excess of those prescribed." HUD Handbook 4155.1 REV-4, CHG-1, ¶ 2-13(A). Not only had the borrower been able to timely meet her housing obligation in this case, as discussed above, the FHA transaction at issue actually decreased the borrower's payments by $182.80 per month and resulted in cash at closing in the amount of $1,692 **(Exhibit J-1)**. These substantial compensating factors more than offset the higher qualifying ratios in this case.

In summary, although Huntington acknowledges that $126 in monthly obligations were not included in the calculations on the MCAW, any oversight in this case was harmless, as the loan file demonstrated significant compensating factors that would have more than offset the resulting higher qualifying ratios. The underwriter reasonably determined that this borrower qualified for FHA financing and, in fact, this refinance transaction benefited the borrower by reducing both her interest rate and monthly payment. Therefore, indemnification would be inappropriate and these allegations should be removed from the final report.

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2. **Huntington Exercised Due Diligence in Underwriting the Loans at Issue**

Secondly, Finding 2 asserts that, in five cases, the underwriter's certification on page 3 of the Addendum to the Uniform Residential Loan Application ("URLA"), Form HUD-92900-A ("Addendum") was incorrect, the underwriter certified to using due diligence in underwriting these cases but did not do so. Based on Appendix D, we understand that this allegation is predicated on the OIG's determination that these five cases, which include the two loans discussed above, contained underwriting deficiencies. The Report alleges that these underlying oversights demonstrate that the underwriter did not exercise due diligence in examining the loan file and, as a result, the certification on the Addendum in these cases was incorrectly signed. Finding 2 recommends in connection with these allegations that HUD's Associate General Counsel for Program Enforcement determine the legal sufficiency of and, if sufficient, pursue remedies under the PFCRA for the inaccurate certifications in these cases. As discussed in detail below, Huntington takes exception to the allegation that these loans contained underlying origination deficiencies, as well as the inflammatory recommendation to impose PFCRA penalties made in connection with this finding. We address both of these issues in turn.

a. **Huntington Complied with HUD Requirements in the Cited Loans**

As discussed above, in the five cases cited in connection with the underwriter certifications in Finding 2, Huntington respectfully disagrees with the underlying assumption that the loans contained underwriting deficiencies. As demonstrated by the below discussion and attached documentation, Huntington substantially complied with HUD requirements in each of these cases and the underwriter made a reasonable decision to approve the loan after exercising due diligence in examining each of the files at issue. Thus, the certifications in these five cases were correct, and the allegations and recommendations regarding these loans should be removed from the final report.

i. [redacted]FHA Case No. 151-7669678 and [redacted]HA Case No. 413-4129633

Comment 13

According to [redacted]ppendix D to the Report, two of the five cases underlying this recommendation ar[redacted] **– FHA Case No. 151-7669678** an[redacted]**FHA Case No. 413-4129633**, w[redacted]are discussed at length above in connection with the Report's indemnification recommendation. Here, the Appendix indicates that deficiencies in the underwriter's income analysis and/or debt-to-income ratio calculation resulted in an

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incorrect certification on the Addendum. Huntington strongly disagrees with these allegations. As previously demonstrated in this response, Huntington complied with HUD guidelines in calculating the borrowers' income and in examining the borrowers' debt-to-income ratios. The above discussion evidences that significant compensating factors were present in both cases and offset any higher-than-average qualifying ratios in either case. Our response and the attached documentation demonstrate that Huntington complied with HUD guidelines in these cases, the underwriters exercised due diligence to make sound underwriting decisions, and the borrowers qualified for FHA financing. As no underwriting deficiencies were present in these two cases, the underwriters' certifications were correct and any assertion to the contrary and resulting recommendation are unwarranted and should not be included in the final report.

ii. [redacted] FHA Case No. 412-5040490

Comment 14

In the [redacted] ase, Appendix D alleges that this loan contained underwriting deficiencies regarding violations of the Real Estate Settlement Procedures Act of 1974, 12 U.S.C. §§ 2601 et seq. ("RESPA") and income analysis. Huntington respectfully disagrees that such oversights occurred in this case.

First, with regard to RESPA, the Report asserts that the Good Faith Estimate ("GFE") did not accurately disclose the yield-spread premium that was to be paid to the mortgage broker, which resulted in a violation of Section 5 of RESPA and Regulation X, its implementing regulation. Section 3500.7(c) of Regulation X indicates that "a good faith estimate consists of an estimate, as a dollar amount or range, of each charge which (1) will be listed in section L of the HUD-1 or HUD-1A." 24 C.F.R. § 3500.7(c)(1). Further, Section 3500.7(c)(2) indicates that "each such estimate must be made in good faith and bear a reasonable relationship to the charge a borrower is likely to be required to pay at settlement, and must be based upon experience in the locality of the mortgaged property." Id. § 3500.7(c)(2). In compliance with these requirements and contrary to the allegation in the Report, the GFE, which was signed by both borrowers, expressly discloses that the broker is to receive "Yield Spread Premium approx 0-4%" under the Compensation to Broker section of that form **(Exhibit K-1)**. In addition, the payment of a yield-spread premium of up to 5% was disclosed to the borrower through a Mortgage Loan Origination Disclosure Statement **(Exhibit K-2)**. Accordingly, Huntington properly disclosed the estimated range of the yield spread premium in compliance with RESPA requirements.

With regard to Huntington's documentation and calculation of the borrower's income, Huntington maintains that the underwriter conservatively estimated the income used to qualify the borrowers for FHA financing in this case. The year-to-date earnings

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on the borrower's pay stub reflected a base income of $1,733 per month **(Exhibit K-3)**. While the pay stub also indicated that the borrower earned regular overtime, as a two-year history with the current employer could not be documented, the underwriter properly excluded such earnings from the calculation of effective income. The co-borrower's pay stub reflected year-to-date income of $11,204.09 as of May 15, 2003 **(Exhibit K-4)**; however, prior years' earnings for 2002 and 2001 were $33,954.70 and $30,869.20, respectively **(Exhibit K-5)**. Due to the variation in the co-borrower's income, the underwriter used an average of the most recent 16.5 months of income to qualify the borrower for the loan, which resulted in income of $2,736 per month ($11,204 + $33,954/16.5 = $2,736) **(Exhibits K-4, K-5)**. The combined income for the borrower and co-borrower based on these figures is $4,469 per month ($1,733 + $2,736 = $4,469). The underwriter used a more conservative monthly income estimate of $4,434 to qualify the borrowers for FHA financing in this case **(Exhibit K-6)**. Use of this effective income amount resulted in qualifying ratios of 19%/37% **(Exhibit K-6)**, which were well below HUD's benchmark guidelines. See HUD Handbook 4155.1 REV-4, CHG-1, ¶ 2-12. This discussion and documentation evidences that Huntington properly calculated the borrower's income based on loan file documentation and the underwriter used a conservative earnings amount to determine that the borrowers qualified for the FHA loan.

In summary, Huntington complied with RESPA requirements and HUD guidelines in this case, and the underwriter exercised due diligence in examining all loan documents. As a result, the underwriter executed an accurate certification on the Addendum in this loan and, thus, the allegations and recommendation regarding this case should be removed from the final report.

iii. [redacted] FHA Case No. 413-4051601

Comment 15

Here, the Report asserts that the appraisal value in this case was overstated, and the underwriter's lack of diligence in examining this appraisal led to an incorrect underwriter certification. Specifically, Finding 2 takes issue with the comparables used to support the appraiser's valuation of the subject property. Huntington maintains that it fully complied with HUD guidelines in underwriting this loan.

As part of Huntington policy and practice, Huntington requires its underwriters to assume the responsibility of reviewing appraisal reports to ensure reasonable conclusions, sound reports and compliance with HUD requirements, as well as the decisions relating to the acceptability of appraisals. HUD Handbook 4000.4, REV-1, CHG-2, ¶ 2-4(C); Mortgagee Letter 97-45; see also HUD Handbook 4000.4 REV-1, CHG-2, ¶ 3-3. It is Huntington's policy and procedure to require that each underwriter

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review the appraisal in accordance with HUD valuation policy to determine whether the appraiser's conclusions are acceptable and, in the event that an appraisal report's findings are inconsistent or otherwise unacceptable, Huntington requires its underwriters to obtain additional information or explanation from the appraiser or return the case to the appraiser for reconsideration. See HUD Handbook 4000.2, REV-2, ¶ 2-15. When reviewing the appraisal, Huntington appreciates that HUD guidelines indicate that "comparable sales data should not be over six months old" and that "if a comparison is seven or eight months old, the reviewer should expect an explanation for its use." See HUD Handbook 4150.1 REV-1, ¶ 9-2 (as incorporated into HUD Handbook 4150.2); see also HUD Handbook 4150.2, CHG-1, ¶ 4-6(A2).

Huntington maintains that it and the underwriter complied with these requirements in th[redacted]an. Here, Huntington obtained an appraisal of the property securing the FHA loan at issue from an independent third party appraiser on June 10, 2003 **(Exhibit L-1)**. The appraiser used three comparables to arrive at the appraised value indicated in the Uniform Residential Appraisal Report ("URAR"). Although these comparables had sales dates more than six months prior to the appraisal, all were within one year of the URAR date according to page 2 of the appraisal **(Exhibit L-1)**. Moreover, the appraiser stated on the URAR comments section that "all comps are located in the same general vicinity as the subject property" **(Exhibit L-1)**. This language evidences that the appraiser adequately justified the use of these comparables to arrive at the stated value. It is also clear from the appraisal that the comparables were all located within the same condominium complex and that the appraiser used the comparables due to like amenities of the properties to the subject property. All comparables had minimal adjustments and were similar to the subject property **(Exhibit L-1)**. At the time of closing, the underwriter received the URAR, examined the appraisal, and determined that the comparables were reasonably chosen by the appraiser and supported the valuation analysis of the subject property. The underwriter exercised due diligence in examining the URAR and Huntington complied with HUD guidelines in this case.

Moreover, while the closing dates of the comparables were slightly outside of the recommended time frame for closed sales, an analysis of market conditions and sales activity in preparation of this response demonstrates that the comparables used were supportive of the market conditions and sales activity within the complex at the time of closing. Sales activity in the subject condominium complex during this one-year period is presented in the table below.

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Property Description	Property Address	Sale Date	Sales Price
Sheriff or HUD Sale	6056 Georges Park Dr. 4B	4/12/2002	$70,000
Comparable	6085 Georges Park Dr. 5A	04/25/2002	$93,000
Comparable	6143 Brice Park Dr. 10F	09/10/2002	$89,900
Comparable	6112 Georges Park Dr.	09/09/2002	$86,500
Sheriff or HUD Sale	6151 Brice Park Dr. 10D	10/31/2002	$72,000
	6045 Georges Park Dr.	04/18/2003	$92,500

As indicated in the above chart, Huntington's review revealed that there were six sales in the subject condominium complex from May of 2002 to May of 2003, including one Sheriff's sale and one HUD sale **(Exhibit L-2)**. The appraiser properly used three of the remaining four sales to analyze the subject property's value. These sales support the appraiser's value and further evidence the underwriter's diligence in reviewing the URAR and accepting the appraiser's comparable selection at the time of closing.

Moreover, the loan at issue was a refinance of an existing FHA loan. The borrowers purchased the property from the builder on February 24, 2000 for $81,700. The appraisal in question was completed for this refinance transaction in August of 2003 and indicated the value was $90,000 as of June 10, 2003 **(Exhibit L-1)**. Average appreciation in the Columbus, Ohio market area ranges from 3-6% per year. Appreciating the original purchase at 3% per year, the estimated value would have been approximately $89,275, further supporting the appraiser's value.

In summary, Huntington's underwriter reviewed the appraisal report in this case and was satisfied with the overall value conclusions of the appraiser based on the information provided. A lender does not physically visit the subject property or review the available comparables sales data when it contracts with an independent third party appraiser. Lenders like Huntington, therefore, must be able to rely on the appraiser's decisions regarding comparable sales and observations noted in the appraisal report. Here, as evidenced by loan file documentation and additional analysis of the market conditions in preparation of this response, the underwriter used due diligence in examining this appraisal and reasonably relied on the appraiser's observations and representation that the comparables were the best available sales data, even though some of the comparables had been sold over six months ago. These appraisal reports appeared to meet applicable HUD/FHA guidelines and appraisal standards. For these reasons, Huntington respectfully requests that the recommendations related to this loan be removed from the Report.

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iv. [redacted] FHA Case No. 413-4135429

Comment 16

Finally, in this loan, Finding 2 alleges that unresolved deficiencies concerning gift documentation evidenced the lack of due diligence that resulted in an incorrect underwriter certification.

With regard to gift funds obtained by a relative, as in this case, HUD guidelines in place when this loan closed required a lender to obtain the following documents: (1) a gift letter specifying, among other items, the dollar amount given, the donor's name, address, telephone number, and relationship to the borrower, and stating that no repayment is required; (2) a copy of the canceled check or other withdrawal document showing the withdrawal from the donor's personal account; and (3) the homebuyer's deposit slip or bank statement that shows the deposit of the gift funds. See HUD Handbook 4155.1, REV-4, CHG-1, ¶2-10 (C); Mortgagee Letter 00-28. In this case, to evidence the borrower's receipt of gift funds, Huntington obtained a gift letter in an amount of $3,100 from the borrower's spouse **(Exhibit M-1)**, and a cashier's check made payable to the settlement agent in an amount of $3,063 listing the donor as the remitter **(Exhibit M-2)**. While we recognize that documentation evidencing the withdrawal of the funds from the donor's bank account should have been obtained to evidence the gift, please note that the omission in this instance does not reflect Huntington policy or practice and was an anomaly. Huntington has advised its personnel of the findings in this case and reminded them of the documentation requirements for gifts set forth in HUD guidelines. We are confident that any oversight in connection with this matter has been resolved and will not recur.

Having said that, the donor did in fact provide the gift funds in this case. Both the gift letter and the cashier's check evidence that the borrower's spouse provided the funds in question. Furthermore, the Report offers no evidence to suggest that these funds came from an impermissible source and the settlement company would not have closed this loan absent receipt of such funds. Thus, any deficiency regarding documentation in this case constituted, at worst, harmless error. The donor provided the gift funds, which the borrower used to satisfy settlement costs, and the borrower qualified for FHA financing in this case. Although the gift documentation contained in the loan file did not strictly comply with HUD guidelines in place at the time the loan was originated, Huntington maintains that the underwriter in this case nevertheless used due diligence to determine that the borrower in fact received the gift funds and ultimately qualified for FHA financing. As a result, we believe that the certification in the Addendum was accurate and that this allegation and the recommendation regarding the certification should not be included in the Report.

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b. Huntington Takes Strong Exception to the Recommendation that PFCRA Penalties Are Appropriate in this Case

Comment 17

As previously discussed under Finding 1, HUD is authorized to impose civil penalties under PFCRA against persons who "make, submit, or present, or cause to be made, submitted, or presented, false, fictitious, or fraudulent claims or written statements to Federal authorities or to their agents." 24 C.F.R. § 28.1. The Report indicates that the "underwriting deficiencies occurred because Huntington's underwriters did not adequately evaluate information presented to them for compliance with HUD's requirements before approving the loans." As demonstrated in the above discussion, however, in the five cases cited in connection with the underwriter certifications in Finding 2, Huntington substantially complied with HUD requirements in each of these cases and the underwriter made a reasonable decision to approve the loan after exercising due diligence in examining each of the files at issue. Moreover, the Report itself acknowledges that Huntington generally complied with HUD's underwriting guidelines. For these reasons, Huntington disagrees with the recommendation of any penalty in connection with these loans, let alone the harsh sanction of PFCRA penalties recommended in the Report.

Additionally, the Report does not allege, and there is no evidence to suggest, that Huntington or its employees intended to circumvent HUD underwriting guidelines in these cases. Rather, the certifications in these five cases were executed by the underwriters after diligent review of the loan files in which these individuals made every effort to comply with FHA requirements. The certifications in these cases were executed in the belief that the borrowers qualified for FHA financing, which in fact they did in each case, rather than in an attempt to mislead the Department. As with the late case endorsement certifications discussed in Finding 1, the Report does not allege that Huntington or its underwriters knowingly misrepresented facts to the Department or intentionally provided false information in the cases at issue. Before imposing penalties on FHA-approved lenders, HUD weighs a number of factors. While intentional violations or a disregard for HUD requirements can lead to severe sanction, such as PFCRA penalties, HUD usually imposes less severe consequences for deficiencies caused by unintentional error. Additionally, Huntington maintains that the borrowers in all five cases qualified for FHA financing and, at most, Huntington inadvertently left certain documentation out of the final loan file. At worst, certain of these five loans contained minor errors that did not affect the insurability of the loans. As indicated above, Huntington believes that the final report should omit recommendation of any

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penalty in connection with these cases, making the recommendation of PFCRA penalties all the more severe under these circumstances.

We also note that, rather than cite new allegations, the PFCRA recommendation in Finding 2 appears to be an attempt to pile on the allegations made against Huntington's underwriting practices in this Report. Typically, OIG audit reports allege certain deficiencies in a company's FHA operations, and the company is given an opportunity to address the materiality and accuracy of the allegations. By also adding an incorrect certification allegation to these underwriting assertions, the Department has created a situation where every misunderstanding of FHA requirements or oversight of a detail or document in a FHA loan could give rise to allegations of a false certification claim. Considering that FHA financing recently has significantly decreased in volume, such actions will create a chilling effect on lenders who want to participate in the FHA Program and endanger the longevity of the FHA Program's future. As discussed above, enforcement actions are meant to reinforce HUD's rules and regulations, rather than discourage broad participation in FHA lending. For the sake of the Program, therefore, we believe the OIG should reconsider its approach to alleging false certifications and focus on the reinforcement of FHA rules and regulations.

Finally, as with the recommendation regarding late case endorsement certifications, Huntington believes that it is being audited under different standards than other national lenders that the OIG determined were not in compliance with HUD's underwriting requirements. For instance, in recent years, we are aware that the OIG has issued reports alleging underwriting deficiencies in loans originated by two national lenders. See, e.g., Audit Rpt. No. 2005-AT-1014 (Sept. 15, 2005); Audit Rpt. No. 2006-NY-1001 (Nov. 18, 2005). Not one of these reports, however, recommended that the Department consider PFCRA penalties. Huntington believes that the OIG should examine and make recommendations for national lenders based on a similar set of standards to ensure that lenders are not audited differently by different OIG offices or disadvantaged by their geographical location in one OIG jurisdiction versus another. Here, Huntington believes that it is being held to a different standard than other national lenders that had underwriting concerns raised by the OIG. We therefore again respectfully request that the OIG use its discretion in making recommendations to ensure that national lenders receive consistent treatment from the agency.

3. Huntington Generally Complied with HUD Requirements in Imposing Fees

Comment 18 Finally, Finding 2 of the Report asserts that, in six loans, Huntington did not ensure that borrowers were not charged excessive and/or unallowable fees. According

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to Appendix E of the Report, the fees at issue are a $200 processing fee in one case, $85 tax service charge fees in five cases and underwriting fees of either $100 or $150 in six cases, totaling $1,475. Finding 2 recommends that HUD require Huntington to refund these fees to the borrower or HUD, depending on the status of the loan.

Huntington's policy consistently has been to charge only those fees permitted by HUD requirements. See HUD Handbook 4000.2 REV-2, ¶ 5-2. Huntington understands and appreciates that, under HUD requirements in effect at the time these six loans were closed, FHA guidelines prohibited lenders from charging the fees listed in Appendix E to FHA borrowers. See id. We are not aware, however, of any HUD requirement prohibiting lenders from passing such fees along to parties to the sales transaction other than the borrower, i.e. the seller or mortgage broker. In each of the six cases cited, with the exception of one tax service fee listed, the HUD-1 Settlement Statements ("HUD-1") indicate that a party other than the borrower paid the listed fees. These HUD-1s are attached as **Exhibit N-1**. As indicated on these documents, the fees at issue were paid outside of closing by a party other than the borrower, either directly or through a broker credit to the borrower, or were paid as part of the seller's closing costs **(Exhibit N-1)**. Nevertheless, in one case [redacted] **FHA Case No. 412-5040490**, Huntington acknowledges that the tax service fee was inadvertently charged to the borrower. Therefore, Huntington has refunded the fee amount to the borrower in that case **(Exhibit N-2)**.

In summary, with one exception, contrary to the allegations in Finding 2, Huntington complied with HUD guidelines regarding borrower fees. In addition, we note that, under the recently issued Mortgagee Letter 2006-04, HUD now permits lenders to pass on reasonable and customary underwriting and processing fees, like those cited in the Report, to FHA borrowers, but indicates that lenders must continue to refrain from charging FHA borrowers a tax service fee. On February 10, 2006, Huntington communicated to all production associates the new HUD guidelines regarding allowable fees set forth in Mortgagee Letter 2006-04 and reemphasized that borrowers may not be charged a tax service fee. Huntington's Loan Insuring department currently reviews all FHA loans to ensure that unallowable fees were not collected. If an unallowable fee was inadvertently collected, Huntington refunds the fee to the borrower. On February 3, 2006, the Loan Insuring department manager reviewed Mortgagee Letter 2006-04 with that department and again reinforced the need to diligently review for unallowable or excessive fees. In addition, we note that all of the loans cited in the Report were originated by third parties, i.e. mortgage brokers or loan correspondents. As a result, Huntington is considering changes to its current process related to review of third-party originated loans to encompass a thorough review of fees on the HUD-1 prior to

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purchase of the loan. We are confident that these measures will ensure Huntington's full compliance regarding the charging of fees in connection with FHA loans.

III. **CONCLUSION**

In summary, Huntington takes the matters raised in the draft Report seriously. Huntington is committed to educating and training employees on issues regarding FHA compliance and to assuring their adherence to HUD's rules and regulations. As discussed above, Huntington generally complied with FHA underwriting requirements and made loans to qualified FHA borrowers. Huntington's thorough review of the findings set forth in the Report indicated that, while certain inaccuracies occurred in a handful of FHA loans submitted for late case insurance endorsement or underwritten by Huntington, any oversights were the product of human error and occurred as a result of high refinance volume and inexperienced staff. While Huntington agrees to work with the OIG and the Department to resolve the cases in which deficiencies took place, Huntington's review demonstrated that a significant number of the loans cited in the Report either complied with HUD requirements at the time of underwriting or submission for insurance endorsement, or do not represent an increased risk to the FHA Insurance Fund. Accordingly, we respectfully request that the OIG revise the number of allegations cited in the Report based on the information and documentation provided in this response.

Finally, Huntington believes that the recommendations involving PFCRA penalties are unwarranted, as they suggest an intent to circumvent HUD requirements when no such intention existed in these cases. Huntington values its relationship with the Department and did not, in any manner, seek to misrepresent any information to HUD. Huntington believes that the various remedies available to HUD, short of the severe sanctions under PFCRA, are commensurate to resolve any deficiency identified in the Report. We believe, and we hope the OIG will agree, that this response and accompanying exhibits demonstrate that including these recommendations in the Report is unnecessary, inappropriate, and will damage Huntington's reputation. We respectfully request that the OIG revise its recommendations to fit the facts of this case.

If you have any additional questions, or if you need additional information, please do not hesitate to contact our internal counsel, Deborah Freye, at (614) 480-5181, or our Washington counsel, Phillip L. Schulman, at (202) 778-9027.

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Thank you for your kind consideration.

Sincerely,

James R. Baron
Director
Huntington Mortgage Group, a division of
The Huntington National Bank

Attachments

cc: Deborah Freye, Esq.
Phillip L. Schulman, Esq.

OIG Evaluation of Auditee Comments

Comment 1 We adjusted Recommendation 1C to reflect the loan that was paid in full since the issuance of our discussion draft audit report to Huntington.

Comment 2 We agree that Huntington's lender certification for Federal Housing Administration loan 412-5204306 loan was dated October 12, 2004. However, Huntington's vice president of post closing provided an Excel computer program file from its DOCSMART system that showed the loan was submitted to HUD on October 18, 2004. HUD Handbook 4165.1, REV-1, "Endorsement for Insurance for Home Mortgage Programs (Single Family)," dated November 30, 1995, chapter 3, section 3-1(B) states that a loan request for endorsement from the lender must include a payment ledger that reflects the payments received, including the payment due for the month in which the case is submitted if the case is submitted after the 15th of the month. Additionally, Huntington's assistant vice president provided us a written response dated August 17, 2005, that showed full payment was received and applied on October 20, 2004 for this loan. Based upon the documentation provided by Huntington, no adjustments were made to this report.

Comment 3 We are recommending indemnification of the first 11 loans presented in Huntington's comments based upon the certifications provided to HUD and HUD's requirements in effect when these loans were submitted for endorsement.

Comment 4 The loan payment for the month before submission for endorsement, December 2004, was not applied to the mortgage until January 18, 2005. Based upon HUD's requirements at the time of submission, the payment was not made in the month due, the loan was not eligible for endorsement, and the certification provided to HUD was incorrect.

Comment 5 During our audit, we used the applicable HUD regulations, guidelines, and other requirements when reviewing Huntington's late requests for endorsement. According to 24 CFR [*Code of Federal Regulations*] 203.255, for applications for insurance involving mortgages originated under the direct endorsement program, the lender shall submit to the secretary of HUD, within 60 days after the date of closing of the loan or such additional time as permitted by the secretary, properly completed documentation and certifications as set forth in the applicable handbook. As required by HUD's regulation, we used HUD Handbook 4165.1, REV-1, and Mortgagee Letter 2004-14 because these were applicable for reviewing loans that Huntington sponsored and submitted to HUD from January 2003 through March 2005.

Comment 6 We adjusted Recommendation 1C to reflect the payment in full of Federal Housing Administration loan 411-3605152. As previously stated, Federal Housing Administration loan 412-5204306 and the other 13 loans were not submitted for endorsement in accordance with HUD's requirements. Huntington contends that the loans no longer pose a risk to the Federal Housing Administration insurance fund. We disagree because according to 24 CFR [*Code of Federal Regulations*] 203.255, by insuring the mortgage (or loan), the mortgagee (or lender) agrees to indemnify HUD under the conditions of section 256(c) of the National Housing Act (12 United States Code, section 1717z-21(c)). As authorized by HUD's regulations, indemnifying HUD begins when a mortgage is endorsed and not when a mortgage becomes in compliance with HUD's requirements after the endorsement date. We concluded that at endorsement loans begin to pose a risk to the Federal Housing Administration insurance fund.

Comment 7 Huntington agrees that the loan was not current at the time of submission for endorsement. Since the loan was not current for October 2003, the escrow account was also not current. Mortgagee Letter 95-20 states in part that the borrower shall include in each monthly payment, together with the principal and interest as set forth in the note and any late charges, a sum for (a) taxes and special assessments levied or to be levied against the property, (b) leasehold payments or ground rents on the property, and (c) premiums for insurance required.

Comment 8 Huntington objected to the inclusion of an "inflammatory recommendation" in our discussion draft audit report. Specifically, Huntington objected to it being referred for administrative penalties under the Program Fraud Civil Remedies Act, 31 United States Code, section 3801 *et seq.*, arguing that enforcement-related actions are intended to reinforce HUD's rules and regulations, rather than to discourage broad participation in HUD's Federal Housing Administration lending. Our administrative penalties recommendation is not inflammatory, nor was it intended as such. Rather, it is a reasonable and appropriate recommendation based upon the false certifications regarding the status of loans and currency of escrows that Huntington submitted to HUD for insurance endorsement.

Moreover, we disagree with Huntington's argument that holding mortgagees responsible for failing to abide by applicable late endorsement requirements and the falsely certifying as to the status of loans and the currency of loan escrows will "discourage broad participation in Federal Housing Administration lending". Rather, we believe that the overwhelming majority of lenders recognize the importance of Federal Housing Administration's requirements and compliance with the same, and this recommendation reinforces that understanding.

Further, Huntington concedes that it is fully responsible for its employees' actions, including those of its approved branch offices. Thus, we correctly conclude that Huntington is responsible for the 14 false certifications submitted by its employees. Generally, direct endorsement loans must be submitted to HUD within 60 days after closing. *See* 24 CFR [*Code of Federal Regulations*] 203.555 and HUD Handbook 4165.1, chapter 2, section 2-1. However, mortgagees may make a late request for endorsement. *See* HUD Handbook 4165.1, REV-1, chapter 3, section 3-1. HUD will evaluate the circumstances and make a determination to accept or reject such requests. A mortgage that is in default when submitted for endorsement cannot be endorsed for insurance. Thus, lenders must certify as part of the late endorsement request, among other things, that the escrow accounts for taxes, hazard insurance, and mortgage insurance premiums are current and intact except for disbursements which may have been made from the escrow accounts to cover payments for which the accounts were specifically established. Lenders seeking late endorsement were also required to submit a payment ledger that reflects the payments received, including the payment due date for the month in which the late endorsement is requested.

Huntington submitted 14 requests for late endorsement forms, which included the requisite certifications. Attached to each request document was a payment history ledger from Huntington. A review of the payment histories indicates that as to each of these loans either the loan was in default or at least one monthly payment had not been made or cured during the history of the mortgage. Accordingly, each of the loans was at least one payment in arrears at the time the late endorsement request was submitted by Huntington. Notwithstanding this fact, Huntington certified that the loans and/or the escrow accounts were current at the time of the requests for endorsement. The certification is a condition of eligibility for insurance endorsement, and, thus, is patently material. Further, actual knowledge of the status of the loans and escrows (for example, maintenance of the payment histories), in combination with the act of affirmatively certifying the status of the loan and escrows, demonstrates that the false certifications were intentional as opposed to inadvertent.

In addition, precedent establishes that, since the focus of a False Claim/Program Fraud Civil Remedies Act case is the conduct of the presenter/claimant, the fact that HUD may have had documentation with which it could have ascertained the falsity of the certifications made by Huntington is of no consequence with respect to the issue of whether it submitted false certifications.

Comment 9 Huntington contends that the 14 loans with incorrect certifications should be removed from this report and that our recommendation related to these incorrect certifications is unnecessary. Huntington's basis for its contention is the loans now comply with HUD's new guidelines in Mortgagee Letter 2005-23. We neither removed the loans with incorrect certifications nor the related recommendation because the certifications were false.

Comment 10 Huntington claims that our recommendation constitutes selective enforcement in that it believes that Huntington is being audited under different standards than other national lenders we determined that did not comply with HUD's late endorsement requirements. Huntington respectfully requested that we use our discretion in making recommendations to ensure that national lenders receive consistent treatment. Huntington states that OIG's audit reports (audit report numbers 2004-KC-1003, 2003-KC-1004, 2003-KC-1001, and 2005-SE-1006) on other lenders cited the same late endorsement-related issues as cited in this report, but refrained from including a recommendation related to the Program Fraud Civil Remedies Act. We disagree with Huntington's claim. We are consistent in the treatment of Huntington and other lenders since we have discretion when making audit recommendations. Specifically, we either refer cases to HUD related to violations of the Program Fraud Civil Remedies Act outside of our audit reports or to cite such cases with the appropriate recommendations in our audit report. In this case, we cited such cases with the appropriate recommendation in this report.

Comment 11 We removed the reference to missing documentation for the truth in lending disclosure in appendix F for Federal Housing Administration loan 151-7669678. There is no documentation in the loan file to indicate that the borrower received overtime earnings for 2002 and 2003. Huntington used The Work Number for its verification of employment. The Work Number lists information current as of July 22, 2004, and shows the rate of pay as "$36,816 annual" and the average hours per pay period as "40." We disagree with Huntington's calculation to establish an earnings trend. There is no information in the loan's file to indicate whether the borrower earned overtime pay for 2002 and 2003. In fact, the W-2 information in the loan file indicates that the borrower's income decreased from 2002 to 2003 by $4,042. HUD Handbook 4155.1, REV-5, chapter 2-7(A), states in part that both overtime and bonus income may be used to qualify if the borrower has received such income for the past two years and it is likely to continue. The borrower's employer indicated to us that the company's policy is to never confirm or state that an employee's overtime earnings would be expected to continue. The borrower's employer also stated that the annual rate of pay on The Work Number is based upon the borrower's 2004 hourly rate of pay times 40 hours times 52 weeks, which is $36,816. The borrower's hourly rate of pay was available to Huntington when the borrower provided his pay stub. A conservative calculation of the borrower's income would have been to use the wage information from the 2002 and 2003 W-2 forms along with The Work Number information.

Comment 12 We disagree that the underwriter used a conservative figure for the child support income. The child support payment documentation for 12 months of payments in 2002 and 2003 shows that the borrower actually received an average monthly child support payment of $214. Huntington referred to the child support agreement that provides for monthly child support payments of $514. Huntington contends that the borrower's monthly housing expense was reduced by $183 after the refinancing to $724. This is not completely accurate. The borrower's previous monthly housing expense was $706 per month and a second mortgage of $211 per month for a total of $917 monthly housing expense. Huntington contends that the borrower demonstrated the ability to consistently make a monthly mortgage payment of $907 (actually $917 per our calculations) for more than three years. However, the borrower's credit report dated May 1, 2003, shows that the second mortgage was opened in March 2003 and there was no payment history.

Comment 13 As discussed in our evaluation of Huntington's comments to our discussion draft audit report under Comments 11 and 12 previously mentioned, we addressed the inconsequential compensating factors for Federal Housing Administration loans 151-7669678 and 413-4129633.

Comment 14 We removed the reference to missing documentation for the truth in lending disclosure in appendix D for Federal Housing Administration loan 412-5040490. We disagree with Huntington's calculation of income for the co-borrower. Huntington used the co-borrower's pay stub with year-to-date income of $11,204 as of May 15, 2003. This income amount included income items that were not received on a continuing basis and were not explained in the loan's file documentation. Such items were noted on the pay stub as FinSpec, Bravo, ExpCreditC, and ExpMerchnt. Any additional income should have been documented as to its expected continuance. A verification of employment to clarify the pay category and its expected continuance could have validated Huntington's income calculation.

Comment 15 HUD Handbook 4150.2, dated July 1, 1999, chapter 4-6, requires an appraiser to consider the amount of time elapsed between the sales date and the effective date of the appraisal. Sales data should not exceed six months between the date of the appraisal, the sales date of the comparable, and must not exceed 12 months. An explanation is required for sales dates in excess of six months. We agree that lenders must be able to rely on the appraiser's decisions regarding comparable sales and observations noted in the appraisal report. However, HUD Handbook 4000.4, REV-1, requires the underwriter to review the appraisal report to determine the acceptability of the conclusions reached by the appraiser. Huntington and its underwriter did not comply with HUD's requirements.

Comment 16 We commend Huntington for bringing this weakness to its employees' attention in an effort to prevent this oversight from occurring in the future.

Comment 17 Huntington objected to the inclusion of a recommendation that HUD's associate general counsel for program enforcement determine legal sufficiency and if legally sufficient, pursue remedies under the Program Fraud Civil Remedies Act against Huntington and/or its principals for incorrectly certifying that due diligence was exercised during the underwriting of five loans in our discussion draft audit report.

As stated in HUD Handbook 4000.4, REV-1, chapter 2-4.C., HUD looks to the underwriter as the focal point of the direct endorsement program. The underwriter <u>must</u> assume the following responsibilities: (1) compliance with HUD's instructions, the coordination of all phases of underwriting, and the quality of decisions made under the program, (2) the review of appraisal reports, compliance inspections, and credit analyses performed by fee and staff personnel to ensure reasonable conclusions, sound reports, and compliance with HUD's requirements, (3) the decisions relating to the acceptability of the appraisal, the inspections, the buyers capacity to repay the mortgage, and the overall acceptability of the mortgage loan for HUD insurance, (4) the monitoring and evaluation of the performance of fee and staff personnel used for the direct endorsement program, and (5) awareness of the warning signs that may indicate irregularities, and an ability to detect fraud, as well as the responsibility that underwriting decisions are performed with due diligence in a prudent manner.

Huntington respectfully requested that we use our discretion in making recommendations to ensure that national lenders receive consistent treatment. We disagree with Huntington's belief of inconsistent treatment. We are consistent in the treatment of Huntington and other lenders since we have discretion when making audit recommendations. Specifically, we either refer cases to HUD related to violations of the Program Fraud Civil Remedies Act outside of our audit reports or to cite such cases with the appropriate recommendations in our audit report. In this case, we cited such cases with the appropriate recommendations in this report.

Comment 18 We removed the underwriting fee for Federal Housing Administration loan 411-3691859 since the settlement statement indicated that an acceptable third party paid this cost outside of closing. We did not remove the underwriting fees for the remaining five loans because in one case, the borrower paid the fees, and no documentation was provided to show that the seller or an acceptable third party paid these costs outside of closing.

The documentation provided by Huntington for the tax service fee for Federal Housing Administration loan 412-5040490 was not sufficient to show that the borrower was refunded the fee. The exhibit shows a voided check. The documentation did not clearly show if the fee was indeed repaid to the borrower. Based upon HUD's requirements at the time of closing, the tax service fee was paid by the borrower in one case, and no documentation was provided to show that the seller or an acceptable third party paid these costs outside of closing.

Appendix C

FEDERAL REQUIREMENTS

According to 24 CFR [*Code of Federal Regulations*] Part 203.255(b), for applications for insurance involving mortgages originated under the direct endorsement program, the lender shall submit to the secretary of HUD, within 60 days after the date of closing of the loan or such additional time as permitted by the secretary, properly completed documentation and certifications.

HUD Handbook 4165.1, REV-1, "Endorsement for Insurance for Home Mortgage Programs (Single Family)," dated November 30, 1995, chapter 3, section 3-1(A), states late requests for endorsement procedures apply if

- The loan is closed after the firm commitment,
- The direct endorsement underwriter's approval expires, and/or
- The mortgage is submitted to HUD for endorsement more than 60 days after closing. Section 3-1(B) states that a loan request for endorsement from the lender must include

  (1) An explanation for the delay in submitting for endorsement and actions taken to prevent future delayed submissions.

  (2) A certification that the escrow account for taxes, hazard insurance, and mortgage insurance premiums is current and intact except for disbursements which may have been made from the escrow account to cover payments for which the account was specifically established.

  (3) A payment ledger that reflects the payments received, including the payment due for the month in which the case is submitted if the case is submitted after the 15th of the month. For example, if the case closed February 3 and the case is submitted April 16, the payment ledger must reflect receipt of the April payment even though the payment is not considered delinquent until May 1. Payments under the mortgage must not be delinquent when submitted for endorsement.

    (a) The lender must submit a payment ledger for the entire period from the first payment due date to the date of the submission for endorsement. Each payment must be made in the calendar month due.
    (b) 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 within the calendar month due.

  (4) A certification that the lender did not provide the funds to bring the loan current or to affect the appearance of an acceptable payment history.

Mortgagee Letter 2004-14, “Late Request for Endorsement Procedures,” clarifies procedures for mortgage lenders when submitting mortgage insurance case binders to the Federal Housing Administration for endorsement beyond the 60-day limit following closing. It replaces the instructions found in the section “Late Request for Endorsement,” contained in chapter 3 of HUD Handbook 4165.1, REV-3.

A request for insurance is considered “late” and triggers additional documentation whenever the binder is received by HUD more than 60 days after the mortgagee loan settlement or funds disbursement, whichever is later.

If HUD returns the case binder to the lender by issuing a notice of rejection (or a subsequent notice of rejection), HUD’s Homeownership Center must receive the reconsideration request for insurance endorsement within the original 60-day window or 30 days from the date of issuance of the original notice of rejection, whichever is greater.

When submitting a late request for endorsement, in addition to including a payment history or ledger, the mortgage lender is required to include a certification, signed by the representative of that lender on company letterhead, which includes the lender’s complete address and telephone number. This certification must be specific to the case being submitted (i.e., identify the Federal Housing Administration case number and the name(s) of the borrower(s)) and state that

1) All mortgage payments due have been made by the borrower before or within the month due. If any payments have been made after the month due, the loan is not eligible for endorsement until six consecutive payments have been made before and/or within the calendar month due.

2) All escrow accounts for taxes, hazard insurance, and mortgage insurance premiums are current and intact, except for disbursements that may have been made to cover payments for which the accounts were specifically established.

3) The mortgage lender did not provide the funds to bring and/or keep the loan current or to bring about the appearance of an acceptable payment history.

Title 31, *United States Code*, section 3801, “Program Fraud Civil Remedies Act of 1986,” provides federal agencies, which are the victims of false, fictitious, and fraudulent claims and statements, with an administrative remedy to recompense such agencies for losses resulting from such claims and statements; to permit administrative proceedings to be brought against persons who make, present, or submit such claims and statements; and to deter the making, presenting, and submitting of such claims and statements in the future.

Appendix D

SUMMARY OF LOANS WITH INCORRECT UNDERWRITING CERTIFICATIONS

Loan number	Original mortgage amount	Appraisal	Income analysis	Debt –to-income ratio	Improper fees	Documentation
151-7669678*	$129,270		X	X		
412-5040490	108,605		X		X	
413-4051601	80,000	X			X	
413-4129633*	99,200			X		
413-4135429	100,522				X	X
Totals	**$517,597**	1	2	2	3	1

* These loans have underwriting deficiencies that affected their insurability.

Appendix E

SUMMARY OF EXCESSIVE AND/OR UNALLOWABLE FEES CHARGED

Loan number	Excessive origination/ processing fee	Tax service fee	Underwriting fee	Total fees
151-7269327		$85	$150	$235
412-5040490		85	150	235
413-4051601		85	150	235
413-4128151		85	150	235
413-4135429	$200	85	100	385
Totals	**$200**	**$425**	**$700**	**$1,325**

Appendix F

NARRATIVE CASE PRESENTATIONS

Loan number: 151-7669678

Mortgage amount: $129,270

Section of Housing Act: 203 (b)

Date of loan closing: August 18, 2004

Status as of February 27, 2006: Loan no longer active

Prior status: Pre-foreclosure sale completed

Payments before first default reported: Not applicable

Claims paid: $35,542
Summary:

Income analysis

Huntington's underwriter (M958) overestimated the borrower's effective monthly income. Huntington's and HUD's loan files lacked evidence to justify the receipt of continuing overtime. Huntington reported the effective income as $4,172 per month, which included $610 per month for overtime. However, we calculated effective monthly income as $3,562 per month. Huntington overestimated the borrower's effective monthly income by $610 per month.

Inaccurate/excessive debt-to-income ratios

Huntington did not show the borrower as an acceptable credit risk. The underwriter (M958) calculated the fixed payment-to-income ratio as 41.25 percent. We recalculated the qualifying ratios using the correct monthly income as discussed above. The recalculated mortgage's fixed payment-to-income ratio of 48.31 percent exceeded HUD's requirement by 7.31 percent. The loan's mortgage credit analysis worksheet failed to include valid compensating factors.

Loan number: 413-4129633

Mortgage amount: $99,200

Section of Housing Act: 203 (b)

Date of loan closing: June 2, 2003

Status as of February 27, 2006: Default - delinquent

Prior status: Not applicable

Payments before first default reported: Eight

Unpaid principal balance: $96,352
Summary:

Understated liabilities

The borrower's recurring liabilities of $592 on the mortgage credit analysis worksheet were understated by $126. Huntington failed to include five credit accounts with a total balance of $2,864.

Inaccurate/excessive debt-to-income ratios

Huntington did not show the borrower as an acceptable credit risk. Huntington's underwriter (BA39) calculated the fixed payment-to-income ration as 44 percent. We recalculated the qualifying ratio using the omitted liabilities discussed above. The recalculated mortgage's fixed payment-to-income ratio of 48.67 percent exceeded HUD's requirement by 7.67 percent. The loan's mortgage credit analysis worksheet failed to include valid compensating factors.