U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

audit report

OFFICE OF INSPECTOR GENERAL

Issue Date
September 17, 1997
Audit Case Number
97-CH-221-1010

TO: Nicholas P. Retsinas, Assistant Secretary for Housing-Federal Housing Commissioner, and Chairman, Mortgagee Review Board

FROM: Dale L. Chouteau, District Inspector General for Audit, Midwest

SUBJECT: Major Mortgage Corporation
Section 203(k) Rehabilitation Home Mortgage Insurance Program
Livonia, Michigan

We completed an audit of the books and records of Major Mortgage Corporation, a direct endorsement mortgagee. We selected Major Mortgage for audit because half of the 203(k) loans it originated were to investors and non-profit agencies. A February 6, 1997 OIG audit of the 203(k) program determined that the program was highly vulnerable to waste, fraud, and abuse by investors and non-profit borrowers. The audit objective was to determine whether Major Mortgage originated the loans according to HUD's requirements and recommendations.

Our review concluded that for 20 of the 25 Section 203(k) loans we reviewed, Major Mortgage Corporation did not exercise due care when it underwrote the loans. In computing the maximum allowable mortgage amounts, Major Mortgage used the wrong loan to value ratio for 20 loans and, in addition, did not properly determine the property values for 8 of the 20 loans. As a result, HUD insured the loans for excessive amounts and assumed an unnecessary risk of $174,698.

If you have any questions, please contact me at (312) 353-7832.

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Executive Summary

We completed an audit of the books and records of Major Mortgage Corporation, a direct endorsement mortgagee. We selected Major Mortgage for audit because half of the 203(k) loans it originated were to investors and non-profit agencies. A February 6, 1997 OIG audit of the 203(k) program determined that the program was highly vulnerable to waste, fraud, and abuse by investors and non-profit borrowers. In doing our review, the Detroit HUD Office asked us to look at all loans from a particular non profit. The HUD Office was aware the nonprofit had identity of interests with some of the entities the non profit did business with and was concerned whether required procedures were followed. The audit objective was to determine whether Major Mortgage originated the loans according to HUD's requirements and recommendations.

We concluded that for 20 of the 25 Section 203(k) loans we reviewed, Major Mortgage Corporation did not exercise due care when it underwrote the loans. In computing the maximum allowable mortgage amounts, Major Mortgage used the wrong loan to value ratio for 20 loans and, in addition , did not properly determine the property values for 8 of the 20 loans.

Maximum Mortgages Were Not Properly Determined

Major Mortgage did not properly determine the property values and used the wrong loan to value ratio to compute the maximum allowable mortgage amounts for 20 of 25 loans we reviewed. All 20 deficient loans were made to the same non-profit organization. Contrary to HUD’s requirements, Major Mortgage used a sales price between identity-of-interest parties as the property value and did not obtain or require an appraisal. For three of the properties, a sale had occurred within the last year, but Major Mortgage did not use that sales amount to calculate the 203(k) mortgage. Major Mortgage also used a loan to value ratio of 97 percent instead of the 85 percent HUD requires when an identity of interest exists. As a result, HUD insured the loans for excessive amounts and assumed an increased risk which we estimated to total $174,698 for 15 loans. There was no impact for five of the deficient loans in which the wrong loan to value ratio was used, since the loans were no longer insured by HUD.

We recommend that the Mortgagee Review Board take appropriate action to reduce HUD's liability based on the information contained in the finding.

We presented our draft finding and narrative case presentations to Major Mortgage Corporation during the audit. We held an exit conference with Major Mortgage on August 7, 1997. Major Mortgage Corporation provided written comments to our finding and case presentations. We included excerpts from the comments with the finding. Appendix B contains the complete text of the auditee's comments.

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Introduction

Major Mortgage Corporation, a non-supervised direct endorsement mortgagee, originates and processes HUD/FHA and conventional loans in the Detroit area. Major Mortgage originates loans under the Section 203(b) and 203(k) programs. Our audit was limited to Major Mortgage's 203(k) program activities.

The Section 203(k) Program allows borrowers to combine, in a single mortgage package, the money needed to purchase a home and make home improvements. The program allows a borrower to finance both the acquisition and rehabilitation of a property with one loan. During the audit period, owner-occupants, investors and non-profit borrowers participated in the program. HUD declared a moratorium on loans to investors on October 29, 1996 because of abuses and increased risks of default.

Major Mortgage Corporation's books and records are located at 35200 Schoolcraft Road, Livonia, Michigan. The president and chief underwriter of the company is Marika Gonzalez.

Audit Objective

Our audit objective was to determine whether Major Mortgage Corporation originated Section 203(k) loans according to HUD's requirements and recommendations.

Audit Scope and Methodology

We judgmentally selected 25 loans for review from the two non-profits with which Major Mortgage did business. The Detroit HUD Office was concerned whether required procedures were followed when Major Mortgage originated the loans for a particular non-profit. The HUD Office was aware the non-profit had identity of interests with some of the entities with which the non-profit did business. As a result, we reviewed all twenty loans made to that non-profit. We selected two loans from the other non-profit. We also selected one loan from each of three of the four investors Major Mortgage made loans to.

We interviewed HUD staff and Major Mortgage employees to evaluate Major Mortgage's procedures for loan origination. We reviewed HUD's and Major Mortgage's FHA case files to ensure the files were consistent and contained required information. In the case files, we reviewed the sales and purchase agreements, property titles, and loan closing documents to ensure mortgage amounts were properly calculated. We also conducted a title search for eight properties at the office of the Wayne County Register of Deeds, to determine the last recorded sales values.

Our audit covered the period May 1995 through December 1996. We conducted the audit at Major Mortgage Corporation between March and July, 1997.

The audit was conducted in accordance with generally accepted government auditing standards. We provided a copy of this report to the president of Major Mortgage Corporation.

Major Mortgage Did Not Properly Determine Property Values And Used The Wrong Loan To Value Ratio

Major Mortgage Corporation did not always exercise due care when it underwrote Section 203(k) loans. In computing the maximum allowable mortgage amounts, Major Mortgage used the wrong loan to value ratio for 20 loans and, did not properly determine the property values for 8 of the 20 loans. As a result, HUD insured the loans for excessive amounts and assumed an unnecessary risk of $174,698.

HUD's Requirements

HUD regulation 24 CFR, 203.5(c) says a mortgagee should exercise due diligence when underwriting mortgages. The mortgagee should exercise the same level of care that it would exercise in obtaining and verifying information for a loan in which the mortgagee would be entirely dependent on the property as security to protect its investment.

HUD Handbook 4240.4 REV-2, 203(k) Rehabilitation Home Mortgage Insurance, Section 2-2 requires the mortgagee to establish two values for a property, an "As-is" value and a value after rehabilitation, in order to determine the maximum mortgage amount.

Mortgagee Letter 94-11 dated March 17, 1994 revised the above requirements and states a lender must establish an "As-is" value, but the lender may determine that an "As-is" appraisal is not feasible or necessary. The lender may use the contract sales price (on a purchase transaction) as the "As-is" value when it is clear to the lender that this amount does not exceed a reasonable estimate of value.

Mortgagee Letter 95-40 dated September 13, 1995 says the lender must obtain evidence of prior ownership if a property was sold in the last year. Prior ownership must be reviewed for identity of interest transactions. The 203(k) mortgage must be based on the lowest sales price in the last year.

Letter 95-40 also says if there is an identity of interest between the buyer and the seller of the property, the loan to value ratio will be limited to 85 percent and an "As-is" appraisal will be required.

Mortgage Values Were Not Properly Determined

For eight of the twenty five loans we reviewed, Major Mortgage did not properly determine the property value and used a loan to value ratio of 97 percent instead of 85 percent to compute the maximum mortgage amount. Additionally, Major Mortgage used the wrong loan to value ratio for another 12 loans. All 20 deficient loans were made to the same non-profit organization. Contrary to HUD's requirements, Major Mortgage accepted a sales price between identity-of-interest parties as the "As-is" value for the properties and did not obtain or require an appraisal. According to HUD's requirements, when transactions are between related parties, the maximum mortgage amount should be based on an "As-is" appraisal or the lowest arms length sales price within the last year plus estimated rehabilitation and allowable closing costs. Additionally, the loan to value ratio should be 85 percent when there are identity of interests. In each of the 20 loans, the final seller and the borrower, a non-profit organization, were the same; and, the seller did not own the property when the seller signed the purchase agreement.

For seven of the eight cases where the property value was not properly determined, Major Mortgage used the contract sales price on the undated Buy and Sell Agreements to calculate the maximum mortgage amount. For the eighth case, the underwriter computed the mortgage amount by deducting the rehabilitation costs from the expected market value of the property after the proposed repairs and improvements. For three of the eight cases a sale had occurred within the past year, but Major Mortgage did not use the sale amount to calculate the mortgage. Major Mortgage did not request its title search company to look for sales within the past year. Therefore, the search only showed that the current owner had a clear title and did not reflect the past sales, since the sales did not impact on the titles. Major Mortgage did not have any evidence to show the contract sales prices it used were a reasonable estimate of the current value of the properties.

Major Mortgage should have used the sales amount within the last year for the 3 properties that sold within the last year, obtained an "As-is" appraisal for the other 5 properties and used a loan to value ratio of 85 percent for all 20 properties since there were identities of interests between the buyers and sellers. Mortgage Corporation of America, who had an identity of interest relationship with both the seller and the borrower, was the owner of record for 18 of the properties and had a land contract on the other 2 properties. A letter in Major Mortgage's files showed Mortgage Corporation of America was affiliated with Detroit Revitalization Inc, the borrower for the 20 properties.

The title search information that Major Mortgage received should have alerted it that there were identity of interests between the buyer and seller. According to the title search, the seller was not the owner of the properties when the sales agreements were signed. Major Mortgage knew that the deeds needed to be transferred before the seller listed on the Buy and Sell Agreement could become the legal owner and convey the deed to the borrower. In all 20 cases, the deeds were transferred at the time of the 203(k) loan closing at least once. The President of Major Mortgage said she knew there was an affiliation between Mortgage Corporation of America and the two organizations through which the interim transfers were made, Retail Realty and MRP-108 Limited Partnership.

We believe the undated Buy and Sell Agreements, the title searches which showed sellers did not have title to the property when the sales agreements were signed, the known identity-of-interest relationships between the owners and the borrowers, and the deed transfers at the time of the 203(k) loan closing should have been sufficient warning to Major Mortgage that the contract sales prices may not have been reasonable values to use in computing the mortgages. Major Mortgage should have required an “As-is” appraisal or used the latest recorded sales price between unrelated parties within the past year as the basis to compute the mortgages.

Major Mortgage also should have used a loan to value ratio of 85 percent instead of 97 percent because of the known identity of interests. Because of the oversights, HUD assumed an increased risk that we estimated to total $174,698 for 15 loans. Five of the deficient loans that had a wrong loan to value ratio had no impact since they were no longer insured by HUD.

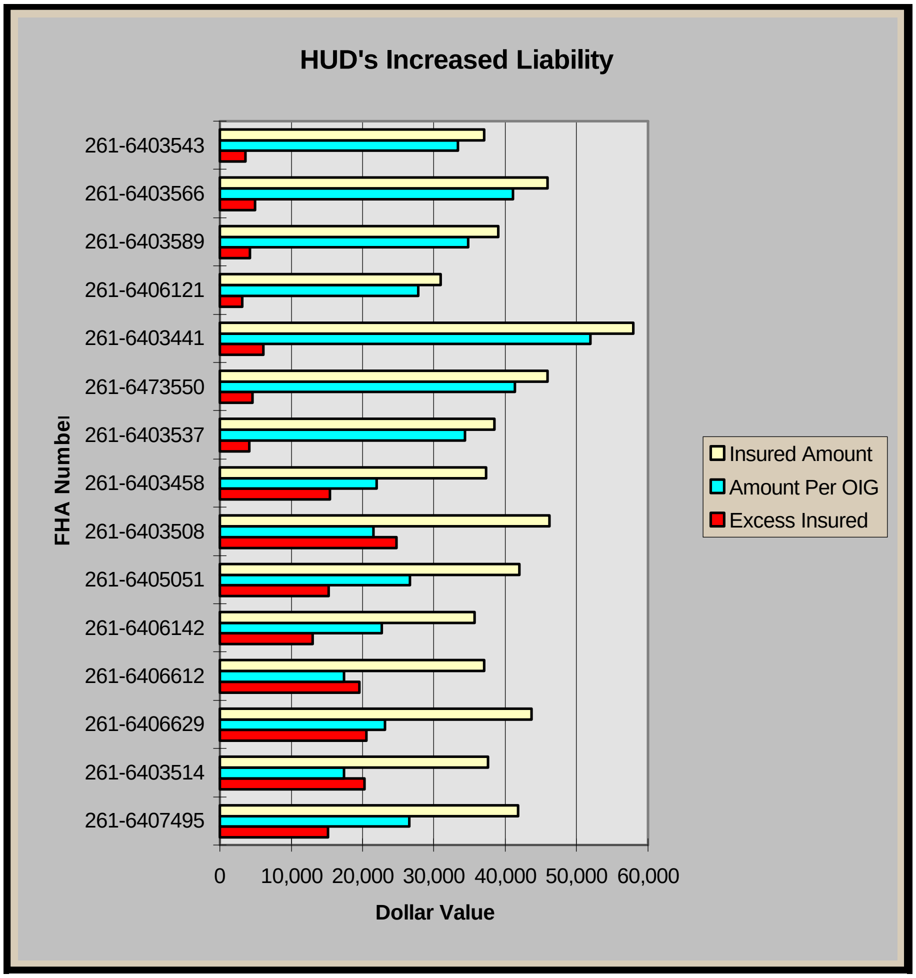
For example, in FHA Case No. 261-6407495, Major Mortgage Corporation used the contract sales price of $23,000 shown on the Buy and Sell Agreement as the value of the property to calculate the maximum mortgage amount. The Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) was undated. Based on the title search information received by Major Mortgage, it should have been aware that Retail Realty was not the owner of the property prior to closing.

The title search showed the owners of the property were Stanley and Harriet Van Reken. On January 26, 1996, the date of the 203(k) loan closing, the property was conveyed by Stanley and Harriet Van Reken to Mortgage Corporation of America for $10,870. Mortgage Corporation then conveyed the property to MRP-108 Limited Partnership who conveyed it to Retail Realty, the seller, through a quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization, the borrower, for $23,000. Mortgage Corporation of America, MRP-108 Limited Partnership, Retail Realty, and Detroit Revitalization were all related entities. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America. However, this does not explain the transfer to MRP-108 or the $12,130 increase in price.

Major Mortgage should have known that there was an identity of interest between the buyer and the seller. A letter in Major Mortgage's files showed Mortgage Corporation of American was affiliated with Detroit Revitalization. Also, the President of Major Mortgage said she knew Mortgage Corporation of America was affiliated with MRP-108 and Retail Realty Limited Partnership.

Because of the identity of interest relationships, Major Mortgage should have used $10,870, the amount Mortgage Corporation of America paid to acquire the property from the original seller within the last year as the value to compute the mortgage. HUD insured the loan for $41,800; however, if the $10,870 value and a 85 percent loan to value ratio had been used, the insured loan would only have been $26,600.

The following chart shows the excessive risk to HUD for the 15 properties. The amount per OIG was reconstructed using the last non-identity of interest sale and increasing the value at a rate of 6 percent per year as applicable. The Consumer Price Index for Shelter shows that the housing costs in Detroit have increased an average of 5.5 percent a year since 1984.



Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

It was suggested in the finding that our company did not always exercise due diligence when underwriting the 203(k) loans. I believe the processing and underwriting of our loans were based on HUD guidelines and our ongoing discussions and recommendations with our local HUD office. Please note that all our loans have been insured and we have had a zero fall out from foreclosure or delinquency.

Mortgagee Letter 94-11 states the lender may use the contract sales price (on a purchase transaction) as the "As-is" value when it is clear to the lender that this amount does not exceed a reasonable estimate of value. I would like to note that the appraiser always pulled comparables for "As-is" values". On each and every case, I personally made sure that the "As-is" value on the 203(k) work sheet reflected the range within the reasonable value of the property in "As-is" condition.

The undated purchase agreements from Detroit Revitalization Inc. were sent over to us for expediting the process of the appraisal order and at a later date, we requested fully executed copies which should be in the HUD case binder sent to HUD along with the dated seller's disclosures for insuring purposes. I am taking proper corrective actions to correct instances of undated or missing documents in the future.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation. Based on documentation we received from the local HUD office, Detroit Revitalization was approved as a Non-Profit organization and HUD encouraged them to take part in the 203(k) program. HUD investigated their legality, documents and portfolio before HUD issued an approval to participate in the program and HUD continues to monitor their actions. As a lender, we are responsible to document the updated eligibility of the Non-Profit organization from HUD along with documents to determine the Non-Profit's financial capacity for repayment of the loan. If there is an identity of interest, I am sure the local HUD office would have notified me and warned me. The transfers of deeds were necessary as it is a title requirement. (MRP-108 was organized for rental purposes, while Retail Realty Limited was organized to sell properties).

The loans were underwritten based on conservative calculations of maximum mortgage amounts (97/95 percent). The "As-is" values were based within the current market value range, not necessarily the sales price. We never exceeded the 110 percent of "After Repair" values.

Our appraisals and title work did not indicate any sales within the past 12 months. Therefore, it was not necessary to establish a sales history prior to one year.

Whether the original sales price (prior to 12 months) was disclosed or not, properties were purchased by Mortgage

Corporation of America and refurbished to the point where they could be rented to tenants by MRP 108. Some of the difficulties to gain access to appraise the properties was when MRP 108's tenants' cooperation was needed. We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your finding you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

In reference to Appendix A-1 through A-8 all values were in the low to middle range of “As-is” comparables with the exception of Appendix A-1. For A-1, twelve months seasoning was in existence since the blanket purchase.

Enclosed is a letter form International Appraisal and Investments, Inc. We asked them to address their opinion of the “As-is” value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an “As-is” value to assure that our "As-is” value calculation was in line with the market.

OIG Evaluation of Auditee Comments

Major Mortgage's President is correct in saying that none of the loans cited in the finding have been foreclosed or are delinquent at this time. However, because of a lack of diligence in underwriting the 20 loans, HUD assumed a higher risk than it should have.

Mortgagee Letter 94-11 states the lender may use the contract sales price as the “As-is” value when it is clear to the lender that this amount does not exceed a reasonable estimate of value. However, Mortgagee Letter 95-40 says if there is an identity of interest between the buyer and the seller of the property, the loan to value ratio will be limited to 85 percent and an “As-is” appraisal of the property will be required.

We do not believe that in the interest of expediting transactions, incomplete documents should be processed. Our review showed that none of the original Buy and Sell Agreements used for loan origination were dated. In HUD’s case binders, we found one agreement was missing, two were undated, and five were dated.

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, MRP 108 and Retail Realty Limited Partnership. Additionally, Major Mortgage should have been aware of the identity of interest relationship with Detroit Revitalization Inc., since Major Mortgage's property files contained a letter from Detroit Revitalization that said Detroit Revitalization was affiliated with Mortgage Corporation of America.

The fact that the local HUD office approved Detroit Revitalization to participate in the 203(k) program does not relieve Major Mortgage of its responsibility to ensure the proper requirements are followed. The local HUD office is not responsible for monitoring the 203(k) program. Major Mortgage is a Direct Endorsement non-supervised lender.

We believe the “As-is” comparables that Major Mortgage provided in its comments can not be relied on since there is no assurance they are comparable or that they represented the “As-is” value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. As indicated in Major Mortgage's comments the purchases involved distressed properties foreclosures, and investments. Since the properties needed 203(k) loans for repairs, it appears the after repair value is what would be comparable to the information provided by Major Mortgage, not the before repair “As-is” value. There were no documents in Major Mortgage's files that showed “As-is” comparables had been considered or that the properties had been improved since the last arms length sale.

Whether or not the properties sold for more than 110 percent of “after repair values” is not the issue. The issue is that the seller and borrower, through an identity of interest relationship passed a paperwork increase in value on to HUD through the 203(k) mortgage.

According to Major Mortgage, its appraisals and title work did not indicate any sales within the last 12 months. When a property is sold within the last 12 months a review of prior ownership for undisclosed identity of interest relationships is required. Also the 203(k) mortgage must be based on the lowest sales price in the last year. Our review found three of the properties had been sold within the last 12 months. Specifically:

(1) According to a land contract in Major Mortgage's loan file, the property at 15309 Faircrest was bought by Mortgage Corporation of America in a bulk sale in January, 1995 for $10,870. In December 1995, Mortgage Corporation of America sold the property to Detroit Revitalization for $23,000; therefore, there was not twelve months seasoning as Major Mortgage’s comments indicate.

(2) For the property at 14756 Kilbourne, the title search in Major Mortgage's files did not indicate that a sale had occurred within the last year. Our title search showed Mortgage Corporation of America acquired the property on July 31, 1995 by bulk purchase for $17,672, six months before it sold the property to Detroit Revitalization for $28,000. Major Mortgage did not specifically request its title search company to look for sales within the past year; therefore, the search only showed that the current owner had a clear title and did not reflect the past sale since it had no impact on the title.

(3) For the property at 12590 Camden, the title search again did not indicate that a sale had occurred within the last year. Our title search showed Mortgage Corporation of America acquired the property on June 28, 1995 in an arms length transaction. Additionally, on the day of the sale to Detroit Revitalization, the property was conveyed to MRP-108 for $24,500 who in turn sold it to Detroit Revitalization for $28,000. As on the previous property, Major Mortgage did not request its title search company to look for sales within the past year.

Recommendation

We recommend that:

(A) The Mortgagee Review Board take appropriate action to reduce HUD's liability based on the information contained in the finding.

Internal Controls

In planning and performing our audit, we considered the internal controls relating to Major Mortgage Corporation's HUD/FHA loan origination process to determine our auditing procedures and not to provide assurance on internal controls. Internal controls consist of the plan of organization, methods, and procedures adopted by management to ensure that resource use is consistent with laws, regulations and policies; that resources are safeguarded against waste, loss and misuse; and that reliable data is obtained, maintained, and fairly disclosed in reports.

Relevant Internal Controls

We determined the following internal controls applied to our audit objectives:

- HUD Program Regulations, Handbooks and Directives.

- Administrative and Quality Assurance controls over loan origination and closing.

We assessed the relevant controls identified above.

Significant Weaknesses

It is a significant weakness if internal controls do not give reasonable assurance that resource use is consistent with laws, regulations and policies; that resources are safeguarded against waste, loss and misuse; and that reliable data is obtained, maintained and fairly disclosed in reports.

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

- <u>HUD/FHA Loan Origination</u>. Major Mortgage did not properly determine current property values and used the wrong loan to value ratio to compute the maximum mortgage amount allowed to borrowers (see Finding).

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Follow Up On Prior Audits

This is the first OIG audit of Major Mortgage Corporation. The last independent audit for the year ended September 30, 1996 did not contain any findings related to this audit.

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Introduction to Narrative Case Presentations

Appendices A-1 through A-15 represent fifteen case-by-case narrative discussions summarizing and detailing the deficiencies cited in the Finding, and showing the increased insurance risk assumed by HUD for each loan.

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Appendix A-1

FHA Case No: 261-6407495

Property Address: 15309 Faircrest, Detroit, Michigan

Insured Amount: $41,800

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: July 10, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $23,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the “As-is” value of the property and did not ensure it was a reasonable estimate of value. Detroit Revitalization, Inc. and Retail Realty Limited Partnership had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owners of the property were Stanley and Harriet Van Reken, not Retail Realty who was the seller of the property. On January 26, 1996, the date of the loan closing, the property was conveyed by Stanley and Harriet Van Reken to Mortgage Corporation of America for $10,870. Mortgage Corporation then conveyed the property to MRP-108 Limited Partnership who conveyed it to Retail Realty, the seller, through a quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization, the borrower, for $23,000. Mortgage Corporation of America, MRP-108 Limited Partnership, Retail Realty, and Detroit Revitalization had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America. However, this does not explain the transfer to MRP-108 or the $12,130 increase in price.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have used $10,870 , the amount Mortgage Corporation of America paid to acquire the property within the last year, to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. When a property is sold within the last year, HUD requires the lender to obtain evidence of prior ownership and determine if there are any undisclosed identity of interest transactions. The 203(k) mortgage must be based on the lowest sales price in the last year. HUD also requires that a loan to value ratio of 85 percent be used when there is an identity of interest between the seller and the buyer.

Based on the “As-is” Value of $10,870, and a loan to value of 85 percent the maximum mortgage should have been $26,000. HUD assumed an unnecessary risk of $15,200 ($41,800-26,600).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

According to our title work and documents in the file, Mortgage Corporation of America had a blanket purchase with Van Reken in January of 1995, from which one of the properties was our subject. Twelve months seasoning was in existence.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $23,000 was in the lowest range of "As-is" value.

OIG Evaluation of Auditee Comments

According to a land contract in Major Mortgage's loan file, the property at 15309 Faircrest was bought by Mortgage Corporation of America in a bulk sale in January, 1995 for $10,870. In December 1995, Mortgage Corporation of America sold the property to Detroit Revitalization for $23,000; therefore twelve months seasoning did not exist.

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America's purchases involved distressed properties, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-2

FHA Case No: 261-6403514

Property Address: 19260 Bloom, Detroit, Michigan

Insured Amount: $37,600

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 26, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $24,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the “As-is” value of the property and did not ensure it was a reasonable estimate of value. Detroit Revitalization, Inc. and Retail Realty Limited Partnership had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On February 6, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to Retail Realty by quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $24,000. Mortgage Corporation of America, Retail Realty, and Detroit Revitalization had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America.

Our title search at the Wayne County Register of Deeds Office showed the property sold for $3,500 when it was acquired in a non-identity of interest transaction by MMC Financial group Limited in December 1988. There was no record of the sale from MMC to Mortgage Corporation of America. The Consumer Price Index for Shelter shows that housing costs in Detroit have increased an average of 5.5 percent a year since 1984. Therefore, assuming a 50 percent increase in property value since 1988, the value of the property would have been $5,250 in 1995.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an “As-is” appraisal to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. HUD requires a lender to obtain an “As-is” appraisal if it is not clear the sales price on a purchase transaction is a reasonable estimate of value. Because of the identity of interest relationships, Major Mortgage had no assurance the sales price on the purchase transaction was a reasonable estimate of value. HUD also requires a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and the buyer.

Based on an "As-is" value of $5,250, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $17,342. HUD assumed an unnecessary risk of $20,258 ($37,600-17,342).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $24,000 was in the lowest range of "As-is" value.

OIG Evaluation of Auditee Comments

We believe using the Consumer Price Index for Shelter is a reasonable approach to establish the value of the property since the transactions were between identity of interest parties, and there was no documentation that showed the property had been improved or that it should have appreciated faster than the market since the last arms length transaction.

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage

Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-3

FHA Case No: 261-6406629

Property Address: 16173 Coyle, Detroit, Michigan

Insured Amount: $43,700

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: July 10, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $28,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the "As-is" value of the property and did not ensure that the $28,000 was a reasonable estimate of value. Detroit Revitalization Inc. and Retail Realty had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On January 26, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to Retail Realty by a quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $28,000. Mortgage Corporation of America, Retail Realty, and Detroit Revitalization had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America.

Our title search at the Wayne County Register of Deeds Office showed a warranty deed dated November 30, 1994 to Mortgage Corporation for $9,000. The Consumer Price Index for Shelter shows that housing costs in Detroit have increased an average of 5.5 percent a year since 1984. Therefore, assuming a six percent increase in property value since 1994, the value would have been $9,540 in 1995.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an "As-is" appraisal to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. HUD requires a lender to obtain an "As-is" appraisal if it is not clear the sales price on a purchase transaction is a reasonable estimate of value. Because of the identity of interest relationships, Major Mortgage had no assurance the sales price on the purchase transaction was a reasonable estimate of value. HUD also requires a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and the buyer.

Based on an “As-is” value of $9,540, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $23,188. HUD assumed an unnecessary risk of $20,512 ($43,700-23,188).

Auditee Comments

Excerpts from the comments of Major Mortgage’s President follow. The complete text of the comments are at Appendix B.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the “As-is” value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an “As-is” value to assure that our “As-is” value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $28,000 was in the middle range of “As-is” value.

OIG Evaluation of Auditee Comments

We believe using the Consumer Price Index for Shelter is a reasonable approach to establish the value of the property since the transactions were between identity of interest parties, and there was no documentation that showed the property had been improved or that it should have appreciated faster than the market since the last arms length transaction.

We believe the “As-is” comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the “As-is” value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage

Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-4

FHA Case No: 261-6406612

Property Address: 12590 Camden, Detroit, Michigan

Insured Amount: $37,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: July 10, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage Corporation used the contract sales price of $28,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the "As-is" value of the property and did not ensure that the $28,000 was a reasonable estimate of value. Mortgage Corporation of America, MRP-108, Retail Realty, and Detroit Revitalization had identity of interest relationships. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On February 19, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to MRP-108 for $24,500. MRP-108 then conveyed the property to Retail Realty through quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $28,000. Mortgage Corporation of America, MRP-108 Limited Partnership, Retail Realty, and Detroit Revitalization had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America. However, this does not explain the transfer to MRP-108 or the $3,500 increase in price.

Our title search at the Wayne county register of Deeds Office showed the property sold for $10,000 in 1995 when it was acquired in a non identity of interest transaction from Joy of Jesus, Inc.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an "As-is" appraisal or used $10,000 to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. When a property is sold within the last year, HUD requires the lender to obtain evidence of prior ownership and determine if there are any undisclosed identity of interest transactions. The 203(k) mortgage must be based on the lowest sales price in the last year. HUD also requires that a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and buyer.

Based on an “As-is” value of $10,000, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $17,399. HUD assumed an unnecessary risk of $19,601 ($37,000-17,399).

Auditee Comments

Excerpts from the comments of Major Mortgage’s President follow. The complete text of the comments are at Appendix B.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the “As-is” value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an “As-is” value to assure that our “As-is” value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $28,000 was in the middle range of “As-is” value.

OIG Evaluation of Auditee Comments

We believe the “As-is” comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the “As-is” value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America’s purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair “As-is” value. There was no documentation that showed “As-is” comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Additionally, Major Mortgage should have calculated the mortgage using the lowest sales price in the last year. Major Mortgage did not request its title search company to look for sales within the past year. Therefore, the search only showed that the current owner had a clear title and did not reflect the past sales, since the sales did not impact on the titles.

Appendix A-5

FHA Case No: 261-6406142

Property Address: 14756 Kilbourne, Detroit, Michigan

Insured Amount: $ 35,700

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: July 10, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $28,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the "As-is" value of the property and did not ensure that the $28,000 was a reasonable estimate of value. Detroit Revitalization, Inc. and Retail Realty Limited Partnership had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On January 26, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to Retail Realty through quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $28,000. Mortgage Corporation of America, Retail Realty, and Detroit Revitalization Inc. had an identity of interest with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America.

Our title search showed that Mortgage Corporation acquired the property on July 31, 1995 as part of a bulk sale from MMC Financial Group. The total cost was $282,750 for 16 properties for an average price of $17,672 per property.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an "As-is" appraisal or used $17,672 to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. When a property is sold within the last year, HUD requires the lender to obtain evidence of prior ownership and determine if there are any undisclosed identity of interest transactions. The 203(k) mortgage must be based on the lowest sales price in the last year. HUD also requires that a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and buyer.

Based on an "As-is" value of $17,672, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $22,700. HUD assumed an unnecessary risk of $13,000 ($35,700-22,700).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $28,000 was in the middle range of "As-is" value.

OIG Evaluation of Auditee Comments

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Additionally, Major Mortgage should have calculated the mortgage using the lowest sales price in the last year. Major Mortgage did not request its title search company to look for sales within the past year. Therefore, the search only showed that the current owner had a clear title and did not reflect the past sales, since the sales did not impact on the titles.

Appendix A-6

FHA Case No: 261-6405051

Property Address: 17892 Bradford, Detroit, Michigan

Insured Amount: $42,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: July 10, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $31,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the “As-is” value of the property and did not ensure that the $31,000 was a reasonable estimate of value. Detroit Revitalization, Inc. and Retail Realty Limited Partnership had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On February 6, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to MRP-108 Limited Partnership for $21,500 who quit claim deeded the property to Retail Realty at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $31,000. Mortgage Corporation of America, MRP-108 Limited Partnership, Retail Realty, and Detroit Revitalization had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America. However, this does not explain the transfer to MRP-108 or the $9,500 increase in price.

Our title search at the Wayne County Register of Deeds Office showed the property sold for $13,000 in 1994 when it was acquired in an non-identity of interest transaction from Pietrobono. The Consumer Price Index for Shelter shows that housing costs in Detroit have increased an average of 5.5 percent a year since 1984. Therefore, assuming a 6 percent increase in property value since 1994 the value of the property would have been $13,780 in 1995.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an “As-is” appraisal to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. HUD requires a lender to obtain an “As-is” appraisal if it is not clear the sales price on a purchase transaction is a reasonable estimate of value. Because of the identity of interest relationships, Major Mortgage had no assurance the sales price on the purchase transaction was a reasonable estimate of value. HUD also requires a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and the buyer.

Based on an "As-is" value of $13,780, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $26,700. HUD assumed an unnecessary risk of $15,300 ($42,000-26,700).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $31,000 was in the middle range of "As-is" value.

OIG Evaluation of Auditee Comments

We believe using the Consumer Price Index for Shelter is a reasonable approach to establish the value of the property since the transactions were between identity of interest parties, and there was no documentation that showed the property had been improved or that it should have appreciated faster than the market since the last arms length transaction.

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-7

FHA Case No: 261-6403508

Property Address: 10108 Nottingham, Detroit, Michigan

Insured Amount: $46,200

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 27, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. The Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) was undated and the lender was aware that Retail Realty was not the owner of the property. Detroit Revitalization and Retail Realty had an identity of interest relationship. The underwriter computed the “As-is” value of $25,000 by deducting the projected rehabilitation costs of $18,000 from $43,000, the appraised value of property after repairs and improvements.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On February 6, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to Retail Realty by quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $29,000. Mortgage Corporation of America, Retail Realty, and Detroit Revitalization, Inc. had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America. However, this does not explain why the sales price to Detroit Revitalization was $4,000 more than the computed “As-is” value.

Our title search showed that the last recorded value of the property was $5,300 in 1989. The Consumer Price Index for Shelter shows that housing costs in Detroit have increased an average of 5.5 percent a year since 1984. Therefore, assuming a 42 percent increase in property value, the value in 1995 would have been $7,526.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an “As-is” appraisal or used $7,526 to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. HUD requires a lender to obtain an “As-is” appraisal if it is not clear the sales price on a purchase transaction is a reasonable estimate of value. Because of the identity of interest relationships, Major Mortgage had no assurance the sales price on the purchase transaction was a reasonable estimate of value. HUD also requires a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and the buyer.

Based on an "As-is" value of $7,526, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $21,458. HUD assumed an unnecessary risk of $24,742 ($46,200-21,458).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $29,000 (Mortgage value computed on $25,000) was in the lower range of "As-is" value.

OIG Evaluation of Auditee Comments

We believe using the Consumer Price Index for Shelter is a reasonable approach to establish the value of the property since the transactions were between identity of interest parties, and there was no documentation that showed the property had been improved or that it should have appreciated faster than the market since the last arms length transaction.

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair “As-is” value. There was no documentation that showed “As-is” comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-8

FHA Case No: 261-6403458

Property Address: 14852 Cedargrove, Detroit, Michigan

Insured Amount: $37,400

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: May 21, 1996

Major Mortgage Corporation, did not properly determine the value used to compute the maximum mortgage amount. Major Mortgage used the contract sales price of $25,000 shown on the Buy and Sell Agreement between Detroit Revitalization, Inc. (borrower) and Retail Realty Limited Partnership (seller) as the "As-is" value of the property and did not ensure that the $25,000 was a reasonable estimate of value. Detroit Revitalization, Inc. and Retail Realty Limited Partnership had an identity of interest relationship. The Agreement was undated and the lender was aware that Retail Realty was not the owner of the property.

The title search obtained by the lender showed the owner of the property was Mortgage Corporation of America, not Retail Realty who was the seller of the property. On February 12, 1996, the date of the loan closing, the property was conveyed by Mortgage Corporation of America to Retail Realty through quit claim deed at no cost. Retail Realty then conveyed the property to Detroit Revitalization for $25,000. Mortgage Corporation of America, Retail Realty, and Detroit Revitalization Inc. had identity of interests with each other. We could not determine why the transfers were necessary and the property was not sold directly by Mortgage Corporation of America to Detroit Revitalization. The President of Detroit Revitalization said the property was transferred to Retail Realty because it was the selling arm of Mortgage Corporation of America.

Our title search showed that the last recorded value of the property was $8,000 in 1988. The Consumer Price Index for Shelter shows that housing costs in Detroit have increased an average of 5.5 percent a year since 1984; therefore, assuming a 50 percent increase in property value since 1988, the value of the property would have been $12,000 in 1995.

The title conveyance documents and a letter in Major Mortgage's file showed Mortgage Corporation of America had an identity of interest with all the parties to which the property was transferred. Therefore, Major Mortgage should have required an "As-is" appraisal or used $12,000 to establish the value of the property and should have used a loan to value ratio of 85 percent instead of 97 percent. HUD requires a lender to obtain an "As-is" appraisal if it is not clear the sales price on a purchase transaction is a reasonable estimate of value. Because of the identity of interest relationships, Major Mortgage had no assurance the sales price on the purchase transaction was a reasonable estimate of value. HUD also requires a loan to value ratio of 85 percent to be used when there is an identity of interest between the seller and the buyer.

Based on an "As-is" value of $12,000, and a loan to value ratio of 85 percent, the maximum mortgage amount should have been $22,000. HUD assumed an unnecessary risk of $15,400 ($37,400-22,000).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

Using the Consumer Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

Please find the enclosed letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific Multiple Listing Service information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market. International Appraisal and Investments, Inc. found the sales price of $25,000 was in the middle range of "As-is" value.

OIG Evaluation of Auditee Comments

We believe using the Consumer Price Index for Shelter is a reasonable approach to establish the value of the property since the transactions were between identity of interest parties, and there was no documentation that showed the property had been improved or that it should have appreciated faster than the market since the last arms length transaction.

We believe the "As-is" comparables Major Mortgage provided in its comments cannot be relied on since there is no assurance they are comparable or represent the "As-is" value. The comparables used by the appraiser represent sales of properties that had the required permits and met all codes. Mortgage Corporation of America's purchases involved distressed property, foreclosures, and investments. Since this property needed a 203(k) loan for repairs, it appears the after repair value is what would be a better comparable to the information provided by the appraiser, not the before repair "As-is" value. There was no documentation that showed "As-is" comparables, or appraisals were considered or obtained for this property or that the property had been improved since the last arms length sale.

Appendix A-9

FHA Case No: 261-6473550

Property Address: 14870 Ward, Detroit, Michigan

Insured Amount: $46,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: December 20, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to Retail Realty at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $41,421. HUD assumed an unnecessary risk of $4,579 ($46,000-41,421).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported the affiliation with Mortgage Corporation of America.

Appendix A-10

FHA Case No: 261-6403543

Property Address: 5203 Maryland, Detroit, Michigan

Insured Amount: $37,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 27, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to Retail Realty at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $33,418. HUD assumed an unnecessary risk of $3,582 ($37,000-33,418).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

Appendix A-11

FHA Case No: 261-6403537

Property Address: 17859 Bradford, Detroit, Michigan

Insured Amount: $38,500

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 27, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to Retail Realty at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $34,374. HUD assumed an unnecessary risk of $4,126 ($38,500-34,374).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

Appendix A-12

FHA Case No: 261-6403589

Property Address: 18901 Beland, Detroit, Michigan

Insured Amount: $39,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 27, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to Retail Realty at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $34,786. HUD assumed an unnecessary risk of $4,214 ($39,000-34,786).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

Appendix A-13

<u>FHA Case No</u>: 261-6403441

<u>Property Address</u>: 2475 Lamothe, Detroit, Michigan

<u>Insured Amount</u>: $58,000

<u>Borrower</u>: Detroit Revitalization, Inc.

<u>Section of Housing Act</u>: 203 (k)

<u>Date of Loan Endorsement</u>: July 15, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to Retail Realty at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $51,935. HUD assumed an unnecessary risk of $6,065 ($58,000-51,935).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

Appendix A-14

FHA Case No: 261-6406121

Property Address: 19385 Eureka, Detroit, Michigan

Insured Amount: $31,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: May 21, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to MRP-108 Limited Partnership and then Retail Realty in turn at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $27,821. HUD assumed an unnecessary risk of $3,179 ($31,000-27,821).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

Appendix A-15

FHA Case No: 261-6403566

Property Address: 11142 Charlemagne, Detroit, Michigan

Insured Amount: $46,000

Borrower: Detroit Revitalization, Inc.

Section of Housing Act: 203 (k)

Date of Loan Endorsement: June 27, 1996

Major Mortgage Corporation used the wrong loan to value ratio, 97 percent, to compute the maximum mortgage amount. HUD requires the loan to value ratio be limited to 85 percent when there is an identity of interest between the buyer and the seller of a property.

For this property, there was an identity of interest between Detroit Revitalization, Inc., (borrower) and Retail Realty Limited Partnership (seller). The title search obtained by the Major Mortgage showed the owner of the property was Mortgage Corporation of America who transferred the property to MRP-108 Limited Partnership and then Retail Realty in turn at the 203(k) closing. The title conveyance documents and a letter in Major Mortgage's files showed that Mortgage Corporation of America had an identity of interest with Detroit Revitalization and Retail Realty Limited Partnership.

Based on a loan to value ratio of 85 percent, the maximum mortgage amount should have been $41,060. HUD assumed an unnecessary risk of $4,940 ($46,000-41,060).

Auditee Comments

Excerpts from the comments of Major Mortgage's President follow. The complete text of the comments are at Appendix B.

An identity of interest between Mortgage Corporation of America and Detroit Revitalization Inc., an approved Federal Housing Administration Non-Profit Organization, is not apparent based on Detroit Revitalization's documentation.

We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America along with Retail Realty Limited Partnership which was the selling arm of Mortgage Corporation of America. As explained to us by the Partnerships and the fact that all deeds were signed by the same person, we did not see an identity of interest.

OIG Evaluation of Auditee Comments

Based on its own files and its comments to our draft report, Major Mortgage was aware of the identity of interest relationships between Mortgage Corporation of America, and Retail Realty Limited Partnership. Major Mortgage should have also been aware of the identity of interest with Detroit Revitalization Inc., since a letter in Major Mortgage's property files from Detroit Revitalization reported that Detroit Revitalization was affiliated with Mortgage Corporation of America.

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Auditee Comments

Major
Mortgage
Corporation

32080 SCHOOLCRAFT STE 100 LIVONIA, MICHIGAN 48150 , (313) 425-7800 FAX (313) 425-8767

August 5, 1997

U.S. Department of HUD
Office of the Inspector General
477 Michigan Avenue
Room 1790
Detroit, MI 48226-2592

Dear Mr. MuhammadAkhtar and Ms. PatMcNamee:

I have received your draft findings of July 21, 1997 of our company audit. Herein I would like to address my position and comments regarding the issues in the manner it was requested by you.

(1) It was suggested on the findings that our company did not always exercise due diligence when underwriting the 203(K) loans. Based on the following comments and findings I believe the processing and underwriting of our loans were based on HUD guidelines and our ongoing discussions and recommendations with our local HUD office. I feel as I will outline in the following pages, that we exercised due care when underwriting the cases. Please also note that all our loans have been insured and we have had a zero fall out from foreclosure or delinquency.

(2) HUD 4240.2, Revision 2 - Section 2-2 is not applicable in our cases.

Mortgagee Letter 94-11 states the lender may use the contract sales price (on a purchase transaction) as the “As-is” value when it is clear to the lender that this amount does not exceed a reasonable estimate of value. On all of the subject properties (8 loans) we used a reasonable “As-is” value amount for mortgage calculations.

(3) Either a comment from the appraiser shows the “As-is” value range or the sales price plus rehabilitation cost agree with the after value amount which is a conservative value on each and every appraisal on these cases with documentation attached by the appraiser on the current

market value. (In some instances, extra comparables and 3-8 current listings/sales are supporting the "After Repair" value. Also for "As-is" value determinations, please refer to the attached letter from International Appraisal and Investments, Inc., dated August 4, 1997). The management at our local HUD office also stated that on the DRI, and all other cases, the "As-is" value appraisal is not required because they are sales (purchases) and that would expedite the appraisal process. This can be verified by the appraiser who estimated the values on the subject cases. This is a commonly used procedure with any lender. In some instances where it was not clear, conservative values and common sense were used to lower the amount for mortgage calculations.

(4) Mortgagee Letter 95-40 states the lender must obtain evidence of prior ownership when a property was sold in the last year. None of the subject properties were sold in the past 12 months, the appraiser states on each and every appraisal the past 12 months sales history per MLS and/or tax rolls. Attached to all appraisals are the tax bill statements which show current ownership. Also our title work shows the same owners on all cases. If no prior ownership was evident for the last year, the identity of interest and lowest sales price issues are not applicable.

(5) For all 8 cases the value I used to compute the maximum mortgage amounts were determined through the appraisal process, "As-is" value ranges on each and every property compared to sale prices and rehabilitation amounts - please refer to comparables from IA & I attached to this letter. In each loan we looked at the current owner; Mortgage Corporation of America was the owner in all cases (per the tax bills, appraisal, title work). We understand MRP 108 was organized for the purpose of renting properties for Mortgage Corporation of America, along with Retail Realty Limited Partnership which is the selling arm of Mortgage Corporation of America. The purchase agreements were signed by Retail Realty - MRP 108 which agrees with our title work as interested parties. As explained to us by the Partnerships and the fact that all deeds were signed by the same person (Mortgage Corporation of America, MRP, Retail Realty), we did not see an identity of interest. For title work purposes, any interested parties would be required to execute and record deeds at closing unless it is a refinance transaction. To our understanding, Mortgage Corporation of America as a mortgage lender, has an inventory of real estate for sale and/or for rent and the Partnerships are executing that portion of it's business. They are limited partnerships formed by the executive board of Mortgage Corporation of America.

(6) Again, the Buy and Sell agreements either represented the "As-is" value or they were lowered by deducting the rehabilitation costs from the "After Repair" value to be conservative and still representing the "As-is" value range according to the appraisal and it's comments. Please refer to additional documentation from IA & I attached to this letter. I also would like to note that the appraiser on the subject cases always pulled comparables for "As-is" values (even though it was not necessary per guidelines) and ongoing conversations were between the appraiser, the local HUD office and myself regarding these issues. On each and every case I personally made sure that the "As-is" value on the 203(K) worksheet reflects the range within the reasonable value of the property in "As-is" condition. (See IA & I letter).

(7) In reference to your findings regarding the letter in our file showing Mortgage Corporation of America had an identity of interest with DRI - we are unaware of any letter; we have no knowledge of such findings. Mortgage Corporation of America is a lender and DRI is a Non-Profit Organization. Based on the documentation we received from the local HUD office, DRI was approved as a Non-Profit organization by the same office and HUD encouraged them to take part in the 203(K) program due to their goals. HUD investigated their legality, documents and portfolio before they issued an approval to participate in the 203(K) program and continues to monitor their actions. As a lender, we are responsible to document the updated eligibility of the Non-Profit organization from HUD along with documents to determine the Non-Profit's financial capacity for repayment of the loan. If there is an identity of interest legally, I am sure the local office would have notified me and warned me for MIC purposes. As I referred to the title process in paragraph 5, the deeds were necessary to execute and record as it is a title requirement. (MRP 108 was organized for rental purposes; Retail Realty Limited was organized to sell properties).

(8) The undated purchase agreements from DRI were sent over to us for expediting the process of the appraisal order and at a later date, we requested fully executed copies which should be in the HUD case binder sent to HUD along with the dated seller's disclosures for insuring purposes. If a copy was not kept or undated papers are in the files, it is our clerical error and I can assure you that I am taking proper corrective actions regarding this issue. I have immediately discussed it with management to have the employees' who are copying packages and putting together shipping packages to be aware of possible errors and not to do it in the future. The sellers, Mortgage Corporation of America/Retail Realty/MRP, were the property owners. Please refer to paragraph 5 and also paragraph 7 regarding your findings of identity of interest between owners and borrowers.

In summary, I present the following:

As noted previously, identity of interest between Mortgage Corporation of America and DRI, an FHA approved Non-Profit Organization, is not apparent based on DRI's documentation.

The loans were underwritten based on conservative calculations of maximum mortgage amounts (97/95% LTV). The "As-is" values were based within the current market value range, not necessarily the sales price. We never exceeded the 110% of "After Repair" values.

Our appraisals and title work did not indicate any sales within the past 12 months. Therefore, it was not necessary to establish a sales history prior to one year.

Whether the original sales price (prior to 12 months) was disclosed or not, properties were purchased by Mortgage Corporation of America and refurbished to the point where it could be rented to tenants by MRP 108. Some of the difficulties to gain access to appraise the properties was when MRP 108's tenants' cooperation was needed.

Using the Consumers Price Index for Shelter would be assuming that there has not been any update to the property. Being unaware of the condition, the market value or type of purchase (i.e. distressed, foreclosure, estate, investor, etc.) of the property, we feel the Index is not applicable. In your findings you suggest an excessive risk to HUD based on the type of reconstructed calculation of property values according to the Consumer Price Index for Shelter which is not used in the Mortgage Lending, Real Estate and Appraisal Industry. We do not feel there is an excessive risk to HUD.

In reference to Appendix A-1 through A-8 please refer to our letter and our reply below, with the exception of Appendix A-1, Paragraph 2 which is as follows: According to our title work and documents in the file, Mortgage Corporation of America had a blanket purchase with Van Reken in January of 1995, from which one of the properties was our subject. 12 months seasoning was in existence.

Please also find enclosed a letter from International Appraisal and Investments, Inc. We asked them to address their opinion of the "As-is" value to prove that excess insuring by HUD did not occur. The letter contains specific MLS information on each property to achieve an "As-is" value to assure that our "As-is" value calculation was in line with the market.

Appendix A-1 through A-8:

Appendix A-1: Sales Price $23,000 - lowest range of “As-is” value. See IA & I letter, page 5 (#6).

Appendix A-2:Renegotiated Sales Price $24,000 - lowest range of “As-is” value. See IA & I letter, page 4 (#2).

Appendix A-3: Sales Price $28,000 - middle range of “As-is” value. See IA & I letter, page 5 (#7).

Appendix A-4: Sales Price $28,000-middle range of “As-is” value. See IA& I letter, page 5 (#8).

Appendix A-5: Sales Price $28,000-middle range of “As-is” value. See IA& I letter, page 3 (#1).

Appendix A-6: Sales Price $31,000-middle range of “As-is” value. See IA & I letter, page 4(#3).

Appendix A-7: Sales Price $29,000-Mortgage Amount computed on “As-is” 'value of $25,000 - lower range of “As-is” value. See IA & I letter, page 4 (#4).

Appendix A-8: Sales Price $25,000 - middle range of “As-is” value. See IA & I letter, page 4 (#5).

We hope that this letter and documentation reflects our position of your findings. We feel that comments in regards to corrections or corrective actions are not necessary except where it has been noted in our letter (Paragraph 8). We feel that we did due diligence in underwriting the 203(K) cases according to HUD guidelines.

Respectfully,

Marika L. Gonzalez
President

Attachments
MLG/dn

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8/4/97

Major Mortgage Corporation
32080 Schoolcraft, Suite 100
Livonia, Mi. 48150

Attn.: Ms. Marika Gonzalez, President

Dear Ms. Gonzalez

In reference to the eight (8) appraisal reports detailed below, completed by Mr. Ronald Rice and/or myself, Ms. Patricia Brown, RM, GAA, no “as is” value estimate was provided because these properties were current sales and their sale price appeared to represent “as is” value. Per HUD's memorandum 94-11, dated 3/94, appraisers are not required to submit an “as is” appraisal if the sale price appears to reflect market value. In addition, at the time these reports were completed, the chief of production at the HUD Detroit Office requested that all 203K appraisal reports be expedited as fast as possible in order to increase the volume of 203K loans in their portfolio. Several factors must be considered when a 203K appraisal is completed. A few very pertinent considerations are as follows.

1 . Appraisers are required by the HUD 203K guidelines to accept "without question" the repairs, renovations, and costs outlined in the plan reviews. Although these reports are provided by **HUD approved** consultants and inspectors, their plans/specifications are frequently ambiguous and poorly narrated, at best. Therefore, the appraiser must often **ASSUME** that some hazardous repairs, which should normally be remedied under the 203B and 22ld2 programs, have been adequately addressed and included in the consultant's repair requirements. Conversely, it must also be **assumed** that the appraisers for reportedly closed sales of FHA 203B/22ld2 **comparables** have required necessary repairs of major hazardous conditions on those properties at the time of the appraisal. Therefore, many of the costs outlined in the 203K consultants report may or may' not contribute to the “after repair” value of the subject property, depending on the terms of the comparable sale being analyzed in the appraisal.

International Appraisal & Investments, Inc. - 689 N. Mill, Plymouth, Mi. 48170
Phone (313) 459-0420 Fax (313) 459-6064

2. “As is” market value frequently can be substantially higher and/or lower than a sale price, which is dependent upon the seller's objectives, the buyer's motivations to purchase the property, and both their reactions to completing required repairs. Further, the “type” of purchaser/seller and the terms /conditions of the sale must also be analyzed.

An arms-length purchaser (prospective owner/occupant) is typically less cognizant of the market, oblivious of some repair conditions, can be uninformed of their cost to cure, and usually must rely on independent contractors to negotiate a purchase price, as well as to discover/remedy deficiencies in a property. However, an investor (purchaser for future re-sale or tenancy), is typically more knowledgeable of “as is after repair” market values, as well as necessary repairs and their costs to cure. An owner-occupant seller may be willing to sell below market value for personal reasons and/or in order to avoid their obligation to complete specific repair conditions, while an investor owner is motivated to obtain the maximum return on the investment. Further, the definition of market value is based upon sale transactions, which represent an agreement between two presumably non-related, informed parties. However, specific terms, costs, conditions, and associations between buyer/seller are often-times **not disclosed** in the sale documents. Suffice it to say that in my 30+ years of appraising, I have rarely, if ever, seen a profit or non-profit investor purchase a property at a **higher than market value price.**

Several additional considerations must also be analyzed when completing an appraisal, regardless of the type of loan being processed. However, the objective of this letter is not to inundate you with a dissertation of an appraiser's extensive responsibilities and obligations required by the Uniform Standards of Professional Appraisal Practice (USPAP). Since the inception of the 203K loan program in the Detroit - HUD office, under the tutelage of Mr. Kiertanis, chief appraiser at HUD for several years, I was trained to process 203K appraisals by completing **detailed research** on the **neighborhoods,** the **subject property,** and the **comparable sales,** analyzing both the **“as is” and "after repair"** value scenarios, as well as the **plan reviews submitted.** A narrative “as is” appraisal report was always completed on refinance and non-arms-length transactions, estate sales, and/or if the sale price appeared to be **substantially different** from the **“as is”** value range found through my market research. To this date, I continue to practice this methodology, regardless of the extra time/effort involved.

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I have always been and am still acutely aware of the frailties, pitfalls, and the room for potential abuse of the 203K loan program, as well as its benefits to the community and neighborhood homeowners. As you know, I have actively and gratuitously contributed my time and expertise to HUD, Mr. Kiertanis, Mr. Pace, Mr. Fralick, and Mr. Niebieszczanski, as well as HUD's A & E Department, the Plan Reviewers/Consultants, and many lenders, in order to assist in the avoidance of the exact circumstances/abuses which are now occuring.

In reference to my appraisal reports and the borrower in question, I can only say that I **have personally and continually voiced my substantial concerns to Mr. Fralick, Mr. Niebieszczanski, and Mr. Kiertanis,** regarding the **appearance of a conflict of interest between the parties to these transactions, as well as several substantial discrepancies in the sale prices versus the estimated market values,** since I began appraising their properties. I can also say that my services were not utilized by that borrower for long, because I diligently scrutinized the properties being valued, as well as their plan reviews, with a thorough "as is" and "after repair" appraisal report being provided on most of their sale transactions.

To address the “as is” values of the reports in question, the following data has been provided. Similar research was done at the time I completed the appraisal. However, a definitive narrative “as is” report was not submitted, per HUD's instructions, if the sale price appeared to be “somewhat” reasonable.

1. 14756 Kilboume, Detroit: Sale price - $28,000, Repairs - $6,073 + contingency, After repair value estimate - $33,500. "As is" comparables:

1. 5459 Faircrest: Sold $26,900, FHA, 11/22/95, MMLS #261993
2. 16221 Lappin: Sold $27,900, FHA, 11/20/95, MMLS #262272
3. 14745 Maddelein: Sold $28,500, C., 10/27/95, MMLS #253820
4. 14996 Liberal: Sold $31,000, FHA, 11/27/95, MMLS #257030
5. 12414 Landsdowne: Sold $25,500, $, 8/9/95, MMLS #204014
6. 15902 Fairmount: Sold $29,500, Assum, 7/26/95, MMLS #251879

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2. 19260 Bloom, Detroit: Sale price - $34,000, Repairs - $11,478 + contingency, After repair value estimate - $35,500. "As is" comparables:

1. 13646 Carlisle: Sold $25,000, FHA, 6/23/95, RC II #513327
2. 18664 Concord: Sold $24,900, C., 11/13/95, MMLS #258057
3. 19328 Dean: Sold $25,000, FHA, 11/15/95, MMLS #263922
4. 20230 Binder: Sold $27,000, FHA, 10/27/95, MMLS #257283
5. 20553 Westphalia: Sold $28,900, FHA, 8/3/95, MMLS #200663
6. 20297 Waltham: Sold $29,900, FHA, 7/24/95, MMLS #250367

3. 17892 Bradford, Detroit: Sale price - $31,000, Repairs - $9,165 + contingency, After repair value estimate - $38,500. "As is" comparables:

1 19580 Fairport: Sold $31,900, FHA, 8/18/95, MMLS #256289
2. 19500 Alcoy: Sold $28,000, FHA, 9/15/95, MMLS #259853
3. 15660 Eastwood: Sold $33,000, FHA, 11/6/95, MMLS #259815
4. 19511 Hickory: Sold $33,000, LC, 11/13/95, MMLS #262900
5. 19380 Westphalia: Sold $31,900, $, 11/15/95, MMLS #264539
6. 17215 Bradford: Sold $32,500, C., 8/25/95, RC II #504178

4. 10108 Nottingham, Detroit: Sale price - $34,000, Repairs - $18,574 + contingency, After repair value estimate - $43,000. "As is" comparables:

1. 4343 Three Mile Dr.: Sold $33,000, LC, 8/23/95, RC II #502832
2. 14453 Kilboume: Sold $19,500, LC, 12/27/95, RC II 535070
3. 4544 Radnor: $29,500, $, 12/26/95, MMLS #266872
4. 14750 Maddelein: $32,000, LC, 11/27/95, MMLS #254284
5. 17131 Cincinnati: $34,000, FHA, 12/18/95, MMLS #258380
6. 15758 Evanston: $25,900, VA, 8/25/95, MMLS #251986

5. 14852 Cedargrove, Detroit: Sale price - $25,000, Repairs - $10,322 + contingency, After repair value estimate - $35,000. "As is" comparables:

1. 15669 Novara: Sold $21,500, $, 11/l/95, MMLS #261121
2. 15872 Novara: Sold $21,500, Assm., 10/30/95, MMLS #262931
3. 15870 Manning: Sold $26,000, $, 9/5/95, MMLS #257220
4. 15859 Fairmount: Sold $26,900, FHA, 11/29/95, MMLS #256001
5. 16221 Lappin: Sold $27,900, FHA, 11/20/95, MMLS #262272
6. 15902 Fairmount: Sold $29,500, Assm., 7/26/95, MMLS #251879

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6. 15309 Faircrest, Detroit: Sale price - $23,000, Repairs - $15,444 + contingency, After repair value estimate - $38,500. “As is” comparables:

1. 16060 Liberal: Sold $31,500, C., 5/18/95, RC II #515995
2. 9400 Camley: Sold $22,000, $, 10/25/95, MMLS #259517
3. 19670 McCormick: Sold $25,000, C., MMLS #253771
4. 15902 Fairmount: Sold $29,500, Assm., 7/26/95, MMLS #251879
5. 13330 State Fair: Sold $28,000, C., 8/2/95, MMLS #252275

7. 16173 Coyle, Detroit: Sale price - $28,000, Repairs - $13,038 + contingency, After repair value estimate - $40,000. “As is” comparables:

4. 15033 Strathmoor: Sold $35,000, FHA, 10/10/95, RC II #535078
1. 15090 Whitcomb: Sold $25,000, LC, 9/11/95, RC II #539306
2. 15346 Prest: Sold $28,900, FHA, 4/14/95, RC II #450434
3. 15717 Strathmoor: Sold $33,000, C., 7/12/95, RC II #517703

8. 12590 Camden, Detroit: Sale price - $28,000, Repairs - $7,100 + contingency, After repair value estimate - $34,000. “As is” comparables:

1. 12724 Glenfield: Sold $29,900, LC, 11/l/95, MMLS #259976
2. 9238 Yorkshire: Sold $29,500, $, 8/16/95, MMLS #256775
3. 14421 Glenwood: Sold $28,900, FHA, 3/13/95, MMLS #189423
4. 4626 Nottingham: Sold $29,500, FHA, 3/31/95, MMLS #196702
5. 15311 Evanston: Sold $24,900, FHA, 12/20/95, MMLS #257495

Sales selected appear to be similar in construction, design, bedroom count, and overall amenity. However, please note that specific details relating to the above comparable sales, such as specific primary siding, age, square footage, amenities, and seller concessions have not been verified and it has been often found that the data provided by the Michigan Multiple Listing Service is frequently incorrect and/or it lacks specific descriptive data. However, these sales, coupled with my MLS research of active and pending sales, which was provided in my appraisal report, produce a reasonable bracket for the “as is” sale prices of the subject properties in most cases. Further, my “after repair” appraisal reports typically analyzed four to six comparable sales, if sufficient data was found, with all pertinent data being verified.

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Phone (313) 459-0420 Fax (313) 459-6064

It should be noted that at the time these appraisal reports were produced HUD directed that the upper value indicators could and frequently should be used to estimate “after repair” market value for 203K properties, because the program was designed to improve and extend the viability of a declining neighborhood. Further, HUD dictated that comparable sales could be used “anywhere in the state of Michigan” if it was necessary to support the loan being considered. However, I have usually selected a median indicator as being the most representative of my market value estimate, which was bracketed by the other comparables researched in the analysis. In addition, most of the comparables considered were selected from the immediate neighborhood and/or competitive areas of the same community. Both the Michigan Multiple Listing Service (MMLS) and the Realcomp II Multiple Listing Service (RC II) have been referenced in my research.

Cash sales, Land Contract sales, and Conventional sales are considered to best represent “as is” property values because they typically do not require that hazardous repair conditions be completed. However, because HUD's policy on repair requirements has been substantially relaxed and minimally enforced over the past two years, FHA sales can and frequently do reflect “as is” value, with the costs for major hazardous conditions being removed from the equation, such as foundation repairs, bad roofs, non-functional mechanical equipment, and excessive peeling of paint, etc..

As I have previously stated to you **AND TO HUD,** most of my reports completed for DRI/RIMCO did include an “as is” and an “after repair” appraisal, because I felt that the sale prices **DID NOT** represent “as is” values. However, the reasoning and motives for these deviance's are still unknown to me. At all times, a very thorough analysis was completed by myself and my staff for all 203K appraisals, which entailed substantially more work than would be required for a standard 203B/221d2 report.

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For the purpose of expediency, I am not forwarding a copy of the MLS sheets applicable to the above comparable sales. I have listed the MLS numbers for verification of specific data on each sale, if your underwriter has the respective MLS books available in office. If you require copies of the MLS sheets, please feel free to contact me and I will forward them to you. I hope that this letter and the data contained herein will clarify any questions you may have and be of assistance.

Sincerely,

Patricia Brown, GAA
President

International Appraisal & Investments, Inc. - 689 N. Mill, Plymouth, Mi. 48170

Phone (313) 459-0420

Fax (313) 459-6064

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