COVID-19 Loss Mitigation

Office of Single Family Housing| 2023-KC-0005

June 13, 2023

Office of Audit | Office of Inspector General
U.S. Department of Housing and Urban Development

Date: June 13, 2023

To: Julie A. Shaffer
Acting Deputy Assistant Secretary for Single Family Housing, HU

From: Kilah S. White
Assistant Inspector General for Audit, GA

Subject: Servicers Generally Did Not Meet HUD Requirements When Providing Loss Mitigation Assistance to Borrowers With Delinquent FHA-Insured Loans

Attached are the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our audit of the Office of Single Family Housing's loss mitigation for Federal Housing Administration (FHA) loan servicing. HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act of 1978, as amended, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at https://www.hudoig.gov. If you have any questions or comments about this report, please do not hesitate to call Patrick Anthony, Audit Director, at (716) 646-7056.

Highlights

Servicers Generally Did Not Meet HUD Requirements When Providing Loss Mitigation Assistance to Borrowers With Delinquent FHA-Insured Loans | 2023-KC-0005

What We Audited and Why

We performed an audit of loan servicers' compliance with the Federal Housing Administration's (FHA) requirements for providing loss mitigation assistance to borrowers after their COVID-19 forbearance ended. We initiated the audit based on the large number of borrowers exiting forbearance, because the loss mitigation programs available to these borrowers were new and created a risk for both borrowers and the FHA insurance fund when servicers do not properly provide loss mitigation. Our audit objective was to determine whether servicers provided borrowers of FHA-insured loans proper loss mitigation assistance after the COVID-19 forbearance ended.[1]

What We Found

Servicers did not provide proper loss mitigation assistance to approximately two-thirds of delinquent borrowers after their COVID-19 forbearance ended. Based on a statistical sample drawn from 231,362 FHA-insured forward loans totaling $41 billion, servicers did not meet HUD requirements for providing loss mitigation assistance to borrowers of 155,297 FHA-insured loans. Nearly half of the borrowers did not receive the correct loss mitigation assistance. These borrowers did not receive the loss mitigation option for which they were eligible, had their loss mitigation option not calculated properly, or received a loss mitigation option that did not reinstate arrearages, which refers to any amount needed to bring the borrower current. Approximately one-quarter of the borrowers received the correct loss mitigation option, but servicers did not follow COVID-19 loss mitigation guidance to help borrowers with payments that were missed during forbearance.

What We Recommend

We recommend that HUD (1) review the sampled loans for which borrowers did not receive appropriate loss mitigation options to ensure that the borrowers are remedied by the servicers, (2) engage with the servicers in our sample to determine reasons for noncompliance and develop a plan to mitigate it going forward, (3) provide additional guidance and training to servicers to address common loss mitigation issues found during this audit, (4) update FHA frequently asked questions to clarify current loss mitigation requirements, (5) develop a process to update the "Save Your Home – Tips to Avoid Foreclosure" brochure and require servicers to distribute it, and (6) design and implement a data-driven methodology to determine the appropriate mix of origination and servicing lender monitoring and desk reviews.

[1] We concurrently conducted an audit of Nationstar Mortgage's compliance with FHA requirements for providing loss mitigation assistance to borrowers after their COVID-19 forbearance ended (HUD OIG report 2023-KC-1001). The audits complement each other by providing a comprehensive assessment of how servicers provided loss mitigation to borrowers exiting COVID-19 forbearance, as well as looking specifically at a large servicer's performance.

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Background and Objective

The Federal Housing Administration (FHA), part of the U.S. Department of Housing and Urban Development (HUD), provides mortgage insurance on loans made by FHA-approved lenders. Since its inception in 1934, FHA has insured nearly 50 million mortgages to protect lenders against loss from borrower default. The combined unpaid principal balance in FHA's insurance portfolio is nearly $1.3 trillion as of October 2022.

HUD's Office of Single Family Housing administers FHA programs and encourages lenders to provide mortgage financing to eligible home buyers, including first-time and low- to moderate-income home buyers. The Office of Single Family Housing's National Servicing Center is responsible for providing guidance and training to lenders so they can better assist homeowners. The Quality Assurance Division is responsible for monitoring origination and servicing activities, and the Office of Housing Counseling provides support and oversight to HUD-approved housing counseling agencies nationwide.

On March 13, 2020, the President declared a national emergency concerning the COVID-19 pandemic. On March 27, 2020, the President also signed the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136) into law. The CARES Act provided a mortgage payment forbearance option for borrowers who, either directly or indirectly, suffered a financial hardship due to the COVID-19 national emergency. A forbearance allowed for reduced or suspended payments without specific terms of repayment. Before the forbearance ended, lenders servicing the loans (servicers) needed to evaluate borrowers for loss mitigation options to assist with repayment of missed amounts. HUD loss mitigation is designed to assist borrowers in default or imminent default in retaining their homes and reduce losses to the FHA insurance fund that result from mortgage foreclosures. Servicers use several loss mitigation options that lead to home retention, including a partial claim or a loan modification.

- Partial claim. Make a no-interest loan to the borrower in an amount sufficient to reinstate the mortgage.
- Loan modification. Update the interest rate, extend the term of the loan, and add missed payments to the loan balance to make payments more affordable.

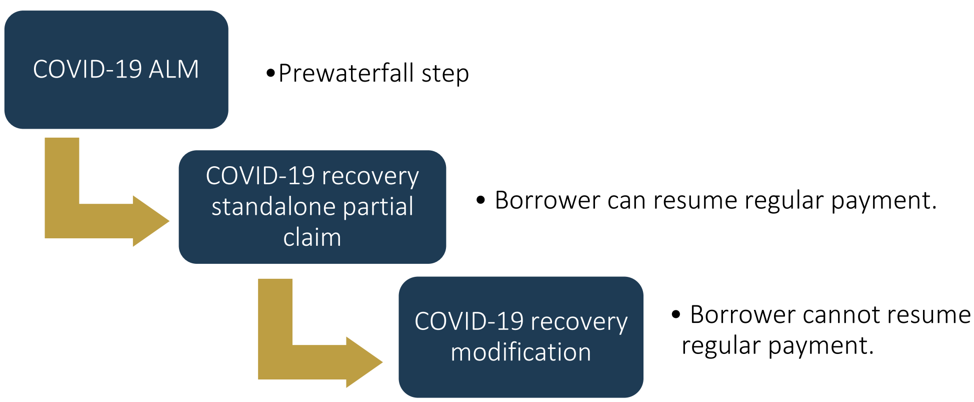
HUD changed its loss mitigation program in response to the COVID-19 national emergency.

- On April 1, 2020, HUD introduced the COVID-19 national emergency standalone partial claim in anticipation of COVID-19's financial impacts on many borrowers.
- On July 8, 2020, HUD introduced a full suite of COVID-19 loss mitigation options to build upon the previously introduced options.
- On February 16, 2021, to support broad economic recovery goals following the pandemic, HUD expanded COVID-19 loss mitigation options to address the impacts many Americans were experiencing in recovering financially from the long-lasting effects of the pandemic.
- On June 25, 2021, HUD released guidance on a new loss mitigation option, the COVID-19 advance loan modification (ALM). A COVID-19 ALM is a permanent change in one or more terms of a borrower's mortgage that achieves a minimum 25 percent reduction to the borrower's monthly principal and interest payment. ALM gave significant relief to eligible homeowners without the need for borrowers to contact their servicers.
- On July 23, 2021, HUD released new guidance after it further decided that broader payment relief might be needed to aid a sustained and equitable recovery and protect FHA's Mutual Mortgage

Insurance Fund. As a result, HUD streamlined COVID-19 loss mitigation options and introduced the COVID-19 recovery options, which included ALM, a COVID-19 recovery standalone partial claim, and a COVID-19 recovery modification—like the previously described options but expanded to qualify more borrowers for the streamlined options.

The pandemic caused a lengthy period of instability that deeply impacted FHA homeowners. HUD intended the options, described above, to provide borrowers impacted by the pandemic a path to significant and sustained recovery and, whenever possible, the ability to remain in their homes. HUD refers to its loss mitigation options as a waterfall, with decision point questions dictating which option servicers must offer and with ALM being a prewaterfall step. The new COVID-19 recovery home retention waterfall streamlined HUD's previous options for struggling homeowners, reduced required documentation, and allowed mortgage servicers to provide greater payment reduction for eligible homeowners. HUD issued two waivers allowing servicers additional time to transition to the new options. Based on the waivers, servicers had to offer ALM to qualifying borrowers who had not already been mailed documents for another option before August 24, 2021, and the recovery options needed to be offered to borrowers who had not been mailed documents for another option before October 21, 2021. Servicers were to follow the steps shown in figure 1 when determining borrowers' eligibility for each loss mitigation option.

Figure 1. HUD's COVID-19 loss mitigation options waterfall (home retention)



Further, HUD required that servicers of FHA-insured loans inform borrowers exiting forbearance about additional assistance available through the Homeowner Assistance Fund (HAF) if it was available in their jurisdiction. This program is a nearly $10 billion Federal program, administered by the U.S. Department of the Treasury, intended to prevent mortgage delinquencies leading to defaults and foreclosures. Further, borrowers could use HAF relief in conjunction with HUD's loss mitigation options. (See appendix B for more information on the COVID-19 loss mitigation requirements.)

Our audit objective was to determine whether servicers provided borrowers of FHA-insured loans proper loss mitigation assistance after the COVID-19 forbearance ended.

Results of Audit

Many Borrowers of Delinquent FHA-Insured Loans Did Not Receive Proper Loss Mitigation Assistance

Servicers did not provide proper loss mitigation assistance to approximately two-thirds of delinquent borrowers after their COVID-19 forbearance ended. The COVID-19 pandemic created a unique environment for mortgage servicing, which required FHA to make rapid changes to its requirements and many servicers were challenged in adapting their servicing operations and processes to keep pace with these changes. This environment placed significant stress on servicer's loss mitigation activities and servicers struggled to ensure compliance with HUD's new requirements. As a result, some delinquent borrowers previously on COVID-19 forbearance faced an additional hardship from improper loss mitigation. Furthermore, the FHA insurance fund could be at a higher risk of loss from approximately 100,910 loans totaling $20 billion that received an incorrect option, improperly calculated option, or option that did not reinstate the loan.

Approximately Two-Thirds of Borrowers Did Not Receive Proper Loss Mitigation Assistance

From a universe of 231,362 FHA-insured forward loans totaling $41 billion, borrowers of a projected 155,297 FHA-insured loans did not receive proper assistance after the COVID-19 forbearance ended. This projection is based on a statistical sample of 85 loans. (See appendix D). As shown in table 1, 67 of these borrowers did not receive proper assistance, either because they received incorrect loss mitigation or because servicers did not follow HUD's guidance.

Table 1. Sample loan count and statistical projection

Issue	Count of sample	Statistical projection count (percentage)
Borrowers received incorrect loss mitigation ▪ Improper loss mitigation option ▪ Proper loss mitigation option but incorrectly calculated or did not reinstate arrearages[2]	48	100,910 (43.6%)
Servicers did not follow HUD's guidance ▪ Improper HAF notification ▪ Significant delays ▪ Improper waterfall use ▪ Failure to review for ALM ▪ Unnecessary documentation ▪ Late mailing of the modification documents	31	65,580 (28.3%)
Total*	67	155,297 (67.1%)
*Some of the sampled loans had multiple issues. See appendix C for more information		

[2] The COVID-19 Recovery Options needed to reinstate arrearages, which included any amount needed to bring the borrower current. See Mortgagee Letter 2021-18 in appendix B for more specifics.

Borrowers Did Not Receive Correct Loss Mitigation

Based on the sample projection, nearly half (43.6 percent) of the borrowers did not receive correct loss mitigation. These borrowers did not receive the loss mitigation option for which they were eligible, had their option not calculated properly, or received an option that did not reinstate arrearages.

HUD's guidance required servicers to review all borrowers who were on a COVID-19 forbearance for the COVID-19 loss mitigation options and, later, for the COVID-19 recovery loss mitigation options to bring their mortgages current after the completion or expiration of the borrowers' forbearance. We found 22 instances in which borrowers did not receive the appropriate option for which they were eligible. For example, some servicers

- Denied borrowers the COVID-19 loss mitigation options.
- Evaluated borrowers for standard loss mitigation rather than streamlined COVID-19 loss mitigation options. (See illustration 1 describing one sampled loan.)
- Did not offer ALM to eligible borrowers.
- Denied borrowers another opportunity for a loss mitigation option when they were not able to return their signed documents by the deadline.
- Did not follow HUD's COVID-19 loss mitigation waterfall and allowed borrowers to choose a loss mitigation option for which they were not eligible.
- Continued processing previous COVID-19 loss mitigation options after new guidance became effective to start evaluating or reevaluating borrowers for the new COVID-19 recovery loss mitigation options.

Illustration 1. Incorrect loss mitigation option

A borrower was on a COVID-19 forbearance. The servicer evaluated the borrower for a standard loan modification without first reviewing him for the streamlined COVID-19 loss mitigation options. The servicer required the borrower to provide financial documents, which the borrower had to resubmit multiple times. In November 2021, the borrower was approved for a standard loan modification with partial claim, and he was required to complete a trial payment plan. The borrower was unable to complete his trial payment plan due to the servicer's error in processing the last payment, and the loan modification was denied. The borrower sold his home in May 2022. The financial documents and trial payment plan were not required for the COVID-19 loss mitigation options. The borrower could have had a much easier experience with loss mitigation had he been properly evaluated for the COVID-19 loss mitigation options and could have potentially kept his home.

We found that 26 borrowers were eligible for their loss mitigation option but the servicers did not properly calculate the option or did not reinstate all arrearages. The partial claim arrearages should include only amounts needed to bring the loan current. Servicers may include an extra month of arrearages to complete a loan modification. Servicers made several types of errors, such as

- Including additional months of future payments in the partial claim, even though borrowers were ready to resume making payments. As a result, the partial claim was overstated by extra amounts that were not needed.
- Including legal costs in the partial claim for improperly started foreclosure during loss mitigation. (See illustration 2 describing one sampled loan.)
- Not including the escrow shortage to calculate the loss mitigation option and including only past-due

escrow payments, which resulted in an increased payment after the servicer performed an escrow analysis on the loan. The escrow balance was not reinstated to the required amount after the loss mitigation funds were applied to the borrower's account. (See Illustration 3 describing one sampled loan.)
- Delaying application of loss mitigation funds to borrowers' accounts, leaving the loans delinquent after borrowers did not make their first modified payments.

Illustration 2. Improperly calculated loss mitigation option

A borrower was approved for a COVID-19 recovery standalone partial claim and was given 11 days to return the documents. Meanwhile, the borrower's entire family with seven children contracted the COVID-19 virus. As a result, she was unable to notarize and return the documents on time. The servicer denied the partial claim for the borrower and closed the file. The borrower was trying to reapply for the same option, continuously reaching out to the servicer over the phone and afraid of losing her home, but the servicer denied her requests multiple times. While the borrower was in discussion with the servicer to reopen the loss mitigation case, the servicer started foreclosure proceedings, accruing more than $3,000 in foreclosure costs. These costs were later included in a partial claim that the borrower eventually received. All foreclosure proceedings should have been stopped during loss mitigation. The improper foreclosure costs increased the partial claim amount paid by HUD, and the borrower was also expected to repay these costs to HUD.

Illustration 3. Loss mitigation did not reinstate all arrearages

A borrower requested loss mitigation assistance because his COVID-19 forbearance was ending. He was approved for FHA Home Affordable Modification Program (HAMP) loan modification with partial claim in September 2021. He completed the first set of documents but was then informed that the paperwork must be redone due to FHA laws changing. The borrower then signed the new offer and returned completed paperwork and a COVID-19 recovery loan modification was finalized. However, the servicer calculated the arrearages incorrectly and underfunded the escrow account by more than $6,000. The borrower's account was not reinstated after loss mitigation because the escrow account was not properly funded. Several months after the modification, the borrower's monthly mortgage payment increased by $533 per month. The servicer noted that there was an internal operational system issue that caused the error in escrow calculations.

Servicers Did Not Follow HUD's Guidance

Based on the sample projection, while some servicers provided borrowers with the correct loss mitigation option, they did not follow HUD's guidance to help more than one-quarter (28.3 percent) of the borrowers with payments that were missed during forbearance. The issues described in table 2 indicate servicers' noncompliance with HUD's guidance. See appendix C for the total count of each issue.

Table 2. Servicers' noncompliance with HUD's guidance

Issue	Description
Improper HAF notification	Servicers did not inform borrowers about HAF during loss mitigation. HUD required servicers to inform borrowers that these funds could be available through their States. Borrowers could use HAF in conjunction with HUD's loss mitigation. Some borrowers were not informed about HAF, even after the funds became available in their States.

Significant delays	Borrowers experienced significant delays in starting or completing their loss mitigation options. HUD's guidance required servicers to complete a loss mitigation action for borrowers who were on a COVID-19 forbearance no later than 120 days from the end of forbearance. In many cases, servicers did not complete loss mitigation options within 120 days, and these delays were often due to not promptly starting evaluation for loss mitigation. In one case, a borrower had to call at least 17 times to get assistance after forbearance.
Improper waterfall use	HUD's guidance required servicers to follow the loss mitigation waterfall when evaluating borrowers for postforbearance options. Servicers improperly offered multiple options to borrowers, letting them choose the option that they preferred. For example, a borrower was informed about the partial claim and loan modification options at the same time and then was asked which option he preferred. However, the servicer should have asked qualifying questions during the loss mitigation review and then, based on the borrower's responses, offered him the appropriate option.
Failure to review for ALM	Servicers were required to review all borrowers on a COVID-19 forbearance for the COVID-19 ALM and offer it to qualified borrowers. Servicers did not have to contact the borrowers before reviewing them for the COVID-19 ALM or sending out the modification documents. In our sample, servicers sometimes did not perform an ALM review for borrowers who were coming out of forbearance. For example, a servicer discussed postforbearance options with the borrower before his forbearance expired at the end of October 2021. However, the servicer did not perform the ALM review for the loan, which is a prewaterfall step, before presenting the waterfall options.
Unnecessary documentation	Servicers required borrowers to provide unnecessary information when considering them for COVID-19 loss mitigation. HUD introduced streamlined loss mitigation options to assist borrowers who experienced hardships during the COVID-19 pandemic that did not require any financial information. However, servicers required borrowers to provide unnecessary documents, such as a mortgage assistance application, affidavit of hardship, bank statements, tax returns, or earnings statements. These documents presented additional hurdles to the borrowers and could have discouraged them from pursuing loss mitigation.
Late mailing of the modification documents	Borrowers improperly received the modification documents after the due date for the first modified payment had passed. HUD's guidance allows servicers to include an additional month in the total outstanding debt to be resolved to allow time for the borrower to return the executed loan modification documents before the modified mortgage payment. However, in some cases, servicers were so delayed in their actions that they sent the modification documents to the borrowers after the first modified payment due date, even after including an extra month in the loan modification. The borrowers would not have been aware of the modified payment amount and the date when it was due so they would have needed to catch up on mortgage payments, in some cases several months' worth of payments, in a short period to avoid rejection of their loan modification.

FHA Made Rapid Changes to Its Loss Mitigation Requirements and Servicers Were Challenged in Keeping Pace

We contacted 22 servicers to get information needed to review each sample item. Based on the servicer responses, we concluded that the large influx in loss mitigation activity exposed servicers' operational weakness. For example, one servicer had experienced a 600 percent increase in loss mitigation activity since 2019. The servicer automated its processes; however, it had system issues that improperly applied partial claim funds to the borrowers' accounts. Other servicers also indicated issues with their automated processes, including an inability to send out documents on time, improperly applying loss mitigation funds to the loans, or initiating foreclosure during loss mitigation. Several servicers did not include enough arrearages in the partial claim because their system could not account for the projected escrow disbursements. Some servicers had procedural or policy weaknesses. For example, one servicer indicated that when borrowers applied for the standard loss mitigation option, they would no longer be evaluated for COVID-19 options. Other servicers did not include projected escrow disbursements in the partial claim because their internal procedures were not set up properly.

Based on our observations while testing the sample items, we also concluded that some servicers were unprepared for the pace in which FHA changed loss mitigation requirements. While HUD had updated the COVID-19 loss mitigation guidance to simplify the process for the borrowers coming out of forbearance, some servicers appeared to be confused with the new requirements and provided borrowers with conflicting information on eligibility requirements. For example, some servicers' agents gave outdated information to borrowers requesting to be evaluated for postforbearance options. The servicers' agents improperly told borrowers that they were ineligible for COVID-19 loss mitigation options because they had completed another loss mitigation within 24 months of the current loss mitigation request or because they were delinquent before the pandemic. However, the servicers' agents should have offered these borrowers COVID-19 loss mitigation options. HUD issued frequently asked questions (FAQ) to help explain its handbook and mortgagee letter policies. However, HUD did not date these FAQs to show when they were issued or superseded by other guidance and did not update them to include the COVID-19 recovery options.

In addition, HUD did not ensure that servicers adequately informed borrowers of the COVID-19 loss mitigation options. HUD issued a significant amount of guidance to servicers on how to administer COVID-19 loss mitigation, but it did not develop a standardized communication for servicers to send to borrowers on COVID-19 loss mitigation options. HUD required servicers to mail HUD's *Save Your Home – Tips To Avoid Foreclosure* brochure to delinquent borrowers to communicate standard loss mitigation options in a clear and consistent manner. However, following the introduction of COVID-19 loss mitigation options, HUD did not update the brochure for servicers to mail to delinquent borrowers.

Illustration 4. ***Save Your Home – Tips to Avoid Foreclosure*** **brochure**

FEDERAL HOUSING ADMINISTRATION

SHOULD I BE AWARE OF ANYTHING ELSE?

Beware of foreclosure prevention scams! You may be approached by organizations with official sounding names offering a quick fix to your mortgage problems. They often charge hefty fees or require that you "temporarily" sign over your deed to them. Remember solutions that sound too good to be true usually are. These precautions will help you avoid being taken by a scam artist:

1. Never sign any papers you don't fully understand.
2. Check with a lawyer, your lender or trusted advisor, or a HUD approved housing counselor before entering into any deal involving a loan assumption, contract of sale or a transfer of the deed to your home.
3. If you can't afford your current mortgage, don't be talked into refinancing into a new loan with a higher payment.

To find a HUD counselor in your area call:
1 800 569 4287 or TDD 1 800 877 8339.

WHAT IS FHA?

The Federal Housing Administration is part of the U.S. Department of Housing and Urban Development (HUD). FHA provides mortgage insurance to approved lenders who in turn offer mortgage loan financing to individuals and families throughout the United States and territories. The FHA mortgage insurance enables approved mortgagees to provide home loans to eligible borrowers who might not otherwise qualify for other mortgage loan financing. FHA borrowers are often first time homebuyers, moderate income families or folks who can't afford a large downpayment.

To learn more about FHA's programs, please visit:
www.hud.gov/fha or contact the
FHA Resource Center:
1-800-CALL-FHA (1-800-225-5342)

Federally Insured, Always There!

U.S. Department of Housing and Urban Development
Federal Housing Administration
451 Seventh Street S.W.
Washington, D.C. 20410

Your Door to FHA Homeownership

Making Home Affordable.gov
1-888-995-HOPE

HUD-2008-5-FHA
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FHA BUILDING COMMUNITIES BY INSURING THE AMERICAN DREAM OF HOMEOWNERSHIP FOR MILLIONS OF PEOPLE SINCE 1934

HELP! I CAN'T MAKE MY MORTGAGE PAYMENT.

Every day thousands of people like you have trouble making the next mortgage payment. Though things may seem hopeless, help is available. However, you need to take the first step! If you ignore the problem you may lose your home to foreclosure, possibly affecting your ability to qualify for credit or to rent another home.

WHAT SHOULD I DO?

1. Contact your lender right away. You can find a contact number on your mortgage statement. When you call, be prepared to explain:

- ✔ Why you are unable to make your payment.
- ✔ Whether the problem is temporary or permanent.
- ✔ Details about your income, expenses, and other assets like cash in the bank.

2. If you are uncomfortable talking to your lender, a HUD-approved housing counseling agency can help you understand your options. These services are free of charge.

3. Open all of the mail you receive from your lender. It contains valuable information about repayment options. Later mail may have important legal notices. Failing to read the mail will not prevent a foreclosure action.

NOTHING IS WORSE THAN DOING NOTHING!

WHAT OPTIONS WILL HELP ME KEEP MY HOME?

FHA provides, as part of its insurance contract with lenders, loss mitigation actions the lender must evaluate and take, when appropriate, to reduce financial losses on loans in default. Your lender needs information from you to fully evaluate these options. If you want to keep your home, talk to your lender about available workout options for home retention. While the options listed here are for borrowers with FHA-insured loans, most lenders offer similar workout plans designed to help you keep your home.

Special Forbearance. Your lender may provide for a temporary reduction or suspension of your payments to allow you time to overcome the problem that reduced your income. Then you may be offered a payment plan so you can pay back the missed payments a little at a time until you are caught up. An extended forbearance period may be provided to unemployed borrowers who are actively seeking employment.

Mortgage Modification. A modification is a permanent change to your loan through which the overdue payments may be added to your loan balance, the interest rate may be changed or the number of years you have to pay off the loan may be extended.

Partial Claim. In a Partial Claim, a borrower receives a second loan in an amount necessary to bring the delinquent loan current. The loan is interest free and does not need to be repaid until you pay off your first mortgage or sell your house. This option is only available to borrowers with FHA-insured loans. However, if you have a conventional loan, ask your lender if they offer an "advance claim."

FHA-Home Affordable Modification Program (FHA-HAMP). This option combines an enhanced partial claim with a loan modification. Under the FHA-HAMP, the partial claim loan will not only include any amounts necessary to bring your mortgage current but may also include an amount to reduce your existing loan balance by up to 30%. The reduced loan balance will then be modified to lower your monthly mortgage payment to an affordable level. As described above, the partial claim loan is interest free, but must be repaid when you pay off your first mortgage or sell your house.

To qualify for any of these options, you will need to provide your lender with current information about your income and expenses. Also, your lender may require that you agree to a payment plan for three or more months to demonstrate your commitment before you are approved for a modification or partial claim.

WHAT OPTIONS DO I HAVE IF I CAN'T KEEP MY HOME?

If your income or expenses have changed so much that you are not able to continue paying the mortgage even under a workout plan offered by your lender, you should consider the options below.

Pre-foreclosure sale. With your lender's permission you can offer your house for sale and sell it at fair market value even if the amount you receive from the sale is less than the amount you owe. If you meet certain conditions, you may be eligible to receive relocation expenses.

Deed-in-lieu of foreclosure. As a last resort, you may be able to voluntarily give your property back to your lender. If you leave the property clean and undamaged you may be eligible to receive relocation expenses.

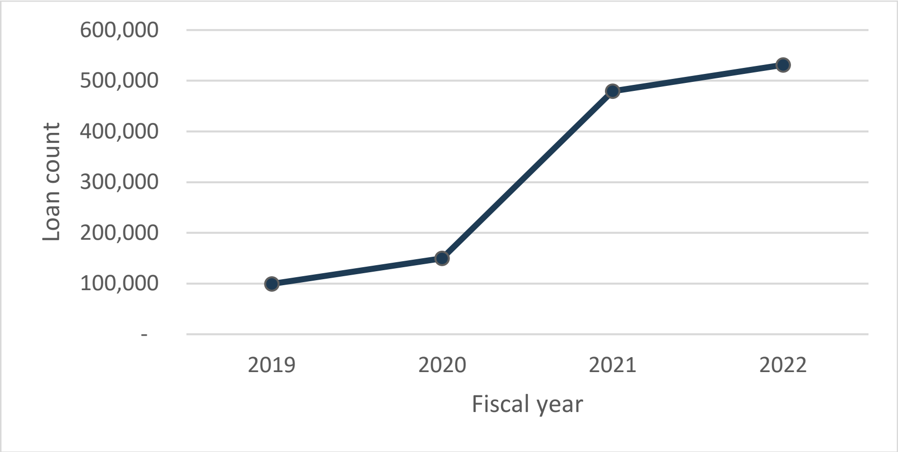
There could be income tax consequences to any plan that reduces the amount of debt you owe so check with a tax advisor before accepting these workout options.

Contact FHA
Struggling homeowners with FHA-insured loans can get assistance by contacting HUD's National Servicing Center at (877) 622-8525. Persons with hearing or speech impairments may reach this number via TDD/TTY by calling (800) 877-8339.

Beware of Scams! If It Sounds Too Good To Be True…It Usually Is.
Report mortgage fraud. Call 1-800-347-3735.

Further, HUD did not adjust its oversight mix of origination compared to servicing based on the increase in loss mitigation activity or escalating change in guidance. Instead, it maintained the same mix of origination and servicing reviews as before the pandemic. HUD's Quality Assurance program is designed to provide continuous and effective monitoring of FHA lender performance to identify the greatest potential sources of risk. Since 2019, there had been a significant increase in loss mitigation activity due to the COVID-19 national emergency, as shown in figure 2 below, while originations activity had recently started to decline. By not increasing the number of servicing reviews, this could negatively impact the FHA insurance fund and the integrity of FHA programs.

Figure 2. Loss mitigation activities (partial claims and loan modifications)



Source: Fiscal Year 2021 and 2022 Annual Report to Congress Regarding the Financial Status of the Federal Housing Administration Mutual Mortgage Insurance Fund.

Borrowers Faced Additional Hardships, and FHA Fund Could Be at Additional Risk

Borrowers for an estimated 155,297 loans with a total unpaid balance of $29.9 billion may have experienced an additional hardship from improper loss mitigation. This represented at least two-thirds of 231,362 FHA-insured loans that were 90 days delinquent and had a COVID-19 forbearance at any time during the pandemic but were no longer in forbearance in October 2021. HUD streamlined postforbearance assistance to borrowers to alleviate their financial stress from the COVID-19 pandemic. By not following all COVID-19 loss mitigation requirements, servicers did not properly assist borrowers in accessing HUD's new mortgage relief options. As a result, some delinquent borrowers faced additional hardship from improper loss mitigation. In some instances, borrowers had to repay their entire past-due amounts in a lump sum or sold their homes after being discouraged by improper loss mitigation.

Further, the FHA insurance fund could be at an increased risk for 100,910 of these loans totaling $20 billion that received a loss mitigation option that was not appropriate, was miscalculated, or did not reinstate arrearages. Improper loss mitigation for borrowers who recently experienced a pandemic-related hardship can increase the risk of future default on their loans and ultimately increase the risk of loss to HUD from potential insurance claims.

Conclusion

HUD introduced several streamlined loss mitigation options to simplify assistance to borrowers exiting COVID-19 forbearance. However, servicers did not provide proper loss mitigation to approximately two-thirds of delinquent borrowers of FHA-insured loans after their COVID-19 forbearance ended. This condition occurred because the large influx of loss mitigation activity and the pace in which FHA changed loss mitigation requirements left servicers unprepared and exposed their operational weaknesses. HUD also needed to adapt to the increase in loss mitigation activity. As a result, borrowers experienced additional hardship, and the FHA insurance fund could be at higher risk of loss from improperly administered loss mitigation. By implementing our recommendations, HUD will be able to ensure that FHA servicers provide borrowers with appropriate and properly calculated loss mitigation options and avoid the risk posed to the FHA insurance fund from these loans.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing

1A. Review the loans in our sample that did not receive appropriate loss mitigation options to ensure that the borrowers were remedied by the servicers, when possible, and take administrative actions if appropriate.

1B. Engage with the servicers in our sample to determine reasons for noncompliance and develop a plan to mitigate it going forward.

1C. Provide additional guidance and training to servicers to address common loss mitigation issues found during this audit.

1D. Update HUD's FHA FAQs to clarify current loss mitigation requirements and ensure that outdated guidance is removed.

1E. Update the *Save Your Home - Tips to Avoid Foreclosure* brochure to include new loss mitigation options as they are introduced and require servicers to send this additional information to delinquent homeowners. This could be done as a redesign of the existing brochure or as addendums to the brochure for temporary programs.

1F. Design and implement a data-driven methodology to determine the appropriate mix of origination and servicing monitoring and desk reviews.

Scope and Methodology

We performed our audit work from March through December 2022. We did not conduct onsite fieldwork for this assignment. Our audit period covered October 2021 through February 2022.

To accomplish our objective, we

- reviewed relevant laws, regulations, and HUD's guidance;
- interviewed HUD's staff to gain an understanding of the program and relevant monitoring controls;
- reviewed HUD's policies and procedures;
- selected and reviewed a statistical sample of FHA-insured loans to determine whether borrowers received proper loss mitigation assistance after the COVID-19 forbearance ended; and
- followed up with servicers on issues found during the audit to determine the reasons for noncompliance.

We relied in part on data contained in HUD's Single Family Data Warehouse (SFDW) system to achieve our audit objective. SFDW is a large and extensive collection of database tables, organized and dedicated to support the analysis, verification, and publication of single-family housing data. Specifically, we relied on the system to identify delinquent loans that were no longer in forbearance in October 2021. Although we did not perform a detailed assessment of the reliability of the data, we performed a minimal level of testing, which included comparing information from SFDW to servicers' records, and found the data to be adequate for our purposes.

Using data from SFDW, we identified an audit universe of 231,362 FHA-insured forward loans with an unpaid principal balance of more than $41 billion as of October 31, 2021. The universe included loans that were 90 days delinquent and had a COVID-19 forbearance at any time during the pandemic but were no longer in forbearance in October 2021. The universe indicated borrowers who experienced a COVID-19-related hardship and whom servicers could have offered loss mitigation after forbearance. From the universe, we selected a statistical sample of 85 loans totaling $18.1 million from 22 servicers. (See appendix D.) We requested documentation from the 22 servicers for each sampled loan, including servicers' communication records with the borrowers, loan payment history, servicing and claim notes, forbearance and loss mitigation agreements, servicers' evaluation of borrowers for loss mitigation options, and other relevant documents. We reviewed the information provided for the sample loans to determine whether borrowers received proper assistance after the COVID-19 forbearance ended in compliance with FHA's loss mitigation requirements. To determine whether sampled loans completed loss mitigation within 120 days as required by HUD's guidance, we looked at the date on which the loss mitigation funds were applied to the borrowers' accounts, which could have been outside our audit period. When determining whether sampled loans received the appropriate option, we considered loss mitigation to be received when offered, even if it was not finalized during our audit period.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Appendix A - Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation – Auditee Comments

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

OFFICE OF HOUSING

MEMORANDUM TO: Kilah S. White, Assistant Inspector General for Audit, GA

JULIE SHAFFER Digitally signed by: JULIE SHAFFER DN: CN = JULIE SHAFFER C = US O = U.S. Government OU = Department of Housing and Urban Development, Office of Administration Date: 2023.03.31 16:45:31 -04'00'

FROM: Julie A. Shaffer, Deputy Assistant Secretary for Single Family Housing, HU

SUBJECT: Discussion and Comments on Draft Audit: Borrowers of Delinquent FHA-Insured Loans Generally Did Not Receive Proper Loss Mitigation Assistance *OIG Audit Report Number: 2023-KC-000X*

The Office of Inspector General (OIG) has audited loss mitigation assistance received by borrowers of Federal Housing Administration (FHA)-insured loans after their COVID-19 forbearance ended and has provided a draft audit report to the Office of Single Family Housing (Single Family) for comment.

Comment 1 >

Single Family appreciates OIG's work on this audit. While we do not disagree with any specific recommendations, we believe the draft report does not fully capture the unprecedented volume and complexity of the policy and system changes that FHA implemented to sustain an anomalously high number of borrowers struggling to make their mortgage payments during the COVID-19 National Emergency. Between March 2020 and October 2021, which is the period pertaining to OIG's sample of loans, FHA issued a total of 40 mortgagee letters articulating new guidance and extensions of COVID-19 policies for lenders and servicers, along with numerous additional regulatory and policy waivers requiring process and system adaptations from industry partners.[1]

Comment 2 >

Nor does the report capture the broadly successful homeowner outcomes achieved during the COVID-19 emergency. More than two million FHA borrowers became delinquent during the national emergency, and more than 1.8 million borrowers took advantage of FHA's COVID-19 forbearance offering.[2] FHA helped more than one million of these borrowers to enter into a loss mitigation plan to avoid foreclosure and retain their homes.[3] Another 655,000 borrowers cured or paid off their mortgage without the need for a loss mitigation plan.[4]

Meanwhile, FHA maintained unusually strong performance during this period. As of the end of Fiscal Year (FY) 2022, the seriously delinquent rate was less than 10 percent for FHA loans that have been under COVID-19 loss mitigation plans for more than one year.[5] Historically, the

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1 *See* FHA Mortgagee Letters, https://www.hud.gov/program_offices/administration/hudclips/letters/mortgagee.
2 Department of Housing and Urban Development, Annual Report to Congress on the Financial Status of the Mutual Mortgage Insurance Fund 19 (FY2022).
3 *Id.*
4 *Id.*
5 *Id.* at 20-21

www.hud.gov **espanol.hud.gov**

redefault rate at one year for FHA loans under loss mitigation plans has been approximately 20 percent.[6]

Comment 3 >

Pending FHA's comprehensive review of the sample of loans used in this audit, as recommended by OIG, a preliminary check of the outcomes of the loans in the sample appears to show consistency with the general success of FHA's loss mitigation policies. Of the 85 loans from OIG's sample, only one appears to have resulted in a claim termination; three others are currently in foreclosure, and one resulted in a pre-foreclosure sale. Even for those loans that have or may go to claim, it would be difficult to attribute that result to the loss mitigation errors, as many of these borrowers did ultimately receive loss mitigation. More detailed information will follow FHA's comprehensive review.

Response to OIG Findings and Recommendations

Comment 3 >

Finding

Many Borrowers of Delinquent FHA-Insured Loans Did Not Receive Proper Loss Mitigation Assistance

Recommendation 1A – Review the loans in our sample that did not receive appropriate loss mitigation options to ensure that the borrowers were remedied by the servicers, when possible, and take administrative actions if appropriate.

Single Family agrees with this recommendation. In keeping with the standard protocol for OIG audit resolution, Single Family will confirm that OIG findings are supported and constitute material violations of FHA servicing policy, then pursue appropriate remedies.

Recommendation 1B – Engage with the servicers in our sample to determine reasons for noncompliance and develop a plan to mitigate it going forward.

Single Family agrees with this recommendation. After confirming that OIG's findings are supported and constitute material violations of FHA servicing policy, Single Family will engage with the responsible servicers to pursue corrective action plans.

Recommendation 1C - Provide additional guidance and training to servicers to address common loss mitigation issues found during this audit to put $6.8 billion to better use by avoiding potential future losses on FHA-insured loans.

Comment 4 >

Single Family agrees with the substance of this recommendation, but questions how OIG determined the sum of $6.8 billion in funds put to better use. For example, OIG's sampling of approximately .02 percent of the FHA-insured loans that were at least 90 days delinquent at the time does not appear to be a sufficient sample to determine an accurate loss estimate. Moreover, not all these loans will result in a claim. As noted above, the current redefault rate for FHA borrowers who received loss mitigation during COVID is half of the historic rate. For this reason, Single Family

[6] *Id.*

2

requests that OIG leave this dollar amount out of Recommendation 1C, which specifically addresses guidance and training.

Recommendation 1D - Update HUD's FHA FAQs to clarify current loss mitigation requirements and ensure that outdated guidance is removed.

Single Family agrees with OIG's suggestions to update its FAQs.

Recommendation 1E - Update the Save Your Home - Tips to Avoid Foreclosure brochure to include new loss mitigation options as they are introduced and require servicers to send this additional information to delinquent homeowners. This could be done as a redesign of the existing brochure or as addendums to the brochure for temporary programs.

Single Family agrees with OIG's suggestions to update its *Save Your Home – Tips to Avoid Foreclosure* brochure.

Recommendation 1F – Design and implement a data-driven methodology to determine the appropriate mix of origination and servicing monitoring and desk reviews.

Comment 5>

Single Family acknowledges that the number of servicer monitoring reviews did not increase during the pandemic. However, in 2021, Single Family did initiate a significant effort to monitor compliance with COVID loss efforts. These efforts included the Servicing Quality Project, a collaborative effort among the Quality Assurance Divisions in Headquarters, the Homeownership Centers, and the National Servicing Center to enhance FHA's servicing monitoring program. The project resulted in a two-week training session for Homeownership Center staff, an updated Lender Monitoring Review Guide, new job aids to facilitate servicing review processes, and the initiation of 13 reviews focused on COVID loss mitigation compliance by specific high-risk servicers.

3

OIG Evaluation of Auditee Comments

Comment 1 HUD did not disagree with any specific recommendations but stated that the draft report does not fully capture the unprecedented volume and complexity of the policy and system changes that FHA implemented to sustain the high number of borrowers struggling to make their mortgage payments during the COVID-19 national emergency. We updated the background section to include more information on the changes to loss mitigation that HUD made throughout the national emergency. We identified the relevant policies that HUD implemented at a high level in the background of the audit report and in more detail in appendix C, but due to the volume of changes and policies put forth we did not include them all. We also mentioned in the finding that HUD issued a significant amount of guidance to servicers on how to administer COVID-19 loss mitigation. As clarification, our audit period covered October 2021 through February 2022 and not March 2020 through October 2021 as stated in HUD's comments.

Comment 2 HUD stated that the report does not capture the broadly successful homeowner outcomes achieved during the COVID-19 emergency or the strong performance of the FHA fund during this period. To make it clearer that we tested compliance rather than outcomes, we reworded our audit objective from determining whether borrowers of FHA-insured loans received proper assistance to help them stay in their homes after the COVID-19 forbearance ended, to determining whether servicers provided borrowers with proper loss mitigation after the COVID-19 forbearance ended and removing reference to the loss mitigation purpose of helping borrowers stay in their homes.

Based on that objective, during the audit we tested a stratified sample of 85 loan files that were 90 days delinquent and had a COVID-19 forbearance at any time during the pandemic (beginning March 2020) but were no longer on forbearance in October 2021. The audit sample targeted delinquent loans to be tested for servicer compliance with FHA's loss mitigation requirements during the period October 2021 through February 2022. We did not test the outcomes or success of the loss mitigation programs designed by HUD, and we did not continue to follow the outcomes for the sampled loans beyond the audit period to the present date. Therefore, we cannot comment on the outcomes of all FHA borrowers during the COVID-19 emergency. We can only comment on the sampled loans and information obtained during our audit.

Comment 3 HUD agreed to implement each of the recommendations in the report, including reviewing the loans included in the audit and improving guidance, training, and monitoring. We look forward to working with HUD during the audit resolution process.

Comment 4 HUD questioned how we determined the $6.8 billion in funds to be put to better use because it does not believe our sample size was sufficient. It pointed out that not all the identified loans will go to claim and those that do will not necessarily be caused by the improper loss mitigation.

To determine sample size, we used computer simulations to model the true sampling distribution of possible audit findings. This ensured that the sampling distribution of possible audit findings conformed to the central limit theorem and that this design was sufficient. We revised appendix D to provide information on the modeling and precision estimates related to our sample. Additionally, for a static population, larger sample sizes produce lower precision estimates relative to lower sample sizes. Therefore, given the size of the deficiencies found, if more records were reviewed, undoubtedly the final precision would be lower than our current estimates and the final one-sided projection with a confidence interval of 95 percent would be higher for each condition tested.

Furthermore, our sample projection was intended to show the overall exposure to the insurance fund from the loans that were serviced improperly, incorporating the FHA-provided loss rate of 34 percent for insurance claims ($6.8 billion being 34 percent of the $20 billion in our projected principal loan balance with increased risk). Based on HUD's comments, we have removed reference to HUD putting $6.8 billion to better use by implementing our recommendations.

Comment 5 HUD described efforts that it made in 2021 to increase monitoring of servicers' compliance with COVID loss mitigation efforts. To address this recommendation, HUD needs to determine the appropriate proportion of origination to servicing lender monitoring reviews to conduct.

Appendix B - Criteria

American Rescue Plan Act of 2021 (Enacted on March 11, 2021)

Section 3206 Homeowner Assistance Fund

Establishment of Fund

(1) Establishment; Qualified Expenses—There is established in the Department of the Treasury a Homeowner Assistance Fund to mitigate financial hardships associated with the coronavirus pandemic by providing such funds as are appropriated by subsection (a) to eligible entities for the purpose of preventing homeowner mortgage delinquencies, defaults, foreclosures, loss of utilities or home energy services, and displacements of homeowners experiencing financial hardship after January 21, 2020, through qualified expenses related to mortgages and housing.

Handbook 4000.1, FHA Single Family Housing Policy Handbook (Issued October 26, 2021)

III. Servicing and Loss Mitigation

A. Title II Insured Housing Programs Forward Mortgages

2. Default Servicing

h. Early Default Intervention

x. Required Notices to Borrower by 60th Day of Delinquency

(A) Standard

Beginning on the 32nd Day but no later than the 60th Day from the date the Mortgage Payment was due, the Mortgagee must send the:

- Delinquency Notice Cover Letter; and
- *Save your Home – Tips to Avoid Foreclosure* brochure (form HUD-2008-5-FHA).

(2) Save Your Home: Tips to Avoid Foreclosure Brochure

The *Save Your Home: Tips to Avoid Foreclosure* brochure (form HUD-2008-5-FHA) is available in English, Spanish, Chinese, and Vietnamese. Mortgagees may either obtain the brochure by accessing HUD's Direct Distribution Center or reproduce electronic versions of the brochure at their own expense.

The Mortgagee may not change the contents of the brochure in any way.

o. Presidentially-Declared COVID-19 National Emergency

iii. COVID-19 Recovery Loss Mitigation Options

(B) Standard

The Mortgagee must review eligible Borrowers for the COVID-19 Recovery Options. Eligible Borrowers may receive more than one COVID-19 Recovery Option.

(1) Borrowers who were on a COVID-19 Forbearance

The Mortgagee must review all Borrowers who were on a COVID-19 Forbearance for the COVID-19 Recovery Options after the completion or expiration of the Borrower's forbearance period. Mortgagees may review the Borrower for the COVID-19 Recovery Options prior to the completion or expiration of the Borrower's forbearance period. A Borrower does not need to exit their forbearance to be reviewed for the COVID-19 Recovery Options. The Mortgagee must complete a loss mitigation option for these Borrowers no later than 120 Days from the earlier of the date of completion or expiration of the forbearance. The 120-Day period to complete a loss mitigation option includes the COVID-19 ALM.

Mortgagee Letter 2021-05 (Issued February 16, 2021, and Effective Immediately)

Loss Mitigation for Borrowers Affected by the COVID-19 National Emergency

i. Definitions

The following COVID-19 Home Retention Options provide options to reinstate the Mortgage for Borrowers who are able to resume monthly or modified monthly Mortgage payments:

- Owner-Occupant Borrowers are eligible to be reviewed for the:
  - COVID-19 Standalone Partial Claim;
  - COVID-19 Owner-Occupant Loan Modification;
  - COVID-19 Combination Partial Claim and Loan Modification; and
  - COVID-19 FHA Home Affordable Modification Program (FHA-HAMP) Combination Loan Modification and Partial Claim with Reduced Documentation, which may include principal deferment and requires income documentation.
- Non-Occupant Borrowers are eligible to be reviewed for the COVID-19 Non-Occupant Loan Modification.

ii. Standard

(A) Borrowers who were on a COVID-19 Forbearance or other forbearance related to the COVID-19 Pandemic

The Mortgagee must review all Borrowers who were on a COVID-19 Forbearance or other forbearance related to the COVID-19 pandemic, for COVID-19 Loss Mitigation Home Retention and Home Disposition Options after the completion or expiration of the Borrower's forbearance period. The Mortgagee must complete a Loss Mitigation Option for these Borrowers no later than 120 Days from the earlier of the date of completion or expiration of the forbearance.

Mortgagee Letter 2021-15 (Issued June 25, 2021, and Effective No Later Than 60 Days From the Publication Date)

iv. COVID-19 Home Retention Options

(A) COVID-19 Advance Loan Modification

The Mortgagee must review eligible Borrowers for a COVID-19 Advance Loan Modification (COVID-19 ALM).

(1) Definition

A COVID-19 ALM is defined as a permanent change in one or more terms of a Borrower's Mortgage that achieves a minimum 25 percent reduction to the Borrower's monthly Principal & Interest (P&I) payment that does not require Borrower contact. The COVID-19 ALM is not incentivized.

(2) Eligibility

The Property may be owner-occupied or non-owner occupied. The Borrower must be 90 or more Days Delinquent. A 30-year loan modification at the most recent Freddie Mac [Federal Home Loan Mortgage Corporation] Weekly Primary Mortgage Market Survey (PMMS) Rate rounded to the nearest one-eighth of 1 percent (0.125 percent) will achieve a minimum 25 percent reduction in the Borrower's monthly P&I.

(3) Standard

The Mortgagee must review eligible Borrowers for the COVID-19 ALM as follows:

- The Mortgagee must review all Borrowers on a COVID-19 forbearance for a COVID-19 ALM within 30 days of the expiration of the Forbearance.
- No later than August 24, 2021, the Mortgagee must review the following Borrowers for a COVID-19 ALM where the Mortgagee has not yet sent out the final documents to the Borrower to complete a Loss Mitigation Option as of June 25, 2021:
  - Borrowers who have exited or requested to exit their COVID-19 Forbearance;
  - Borrowers whose COVID-19 Forbearance has expired or will expire by August 24, 2021; or
  - Borrowers who were not on a COVID-19 Forbearance.

If the Borrower is eligible, the Mortgagee must:

- prepare and send out the loan modification documents to the Borrower; and
- provide a cover letter...

The Mortgagee does not have to contact the Borrower prior to reviewing the Borrower for the COVID-19 ALM or sending out the modification documents.

Borrowers who do not qualify for the COVID-19 ALM must be evaluated for the other COVID-19 Loss Mitigation Options.

Mortgagee Letter 2021-18 (Issued on July 23, 2021, and Effective No Later Than 90 Days From the Publication Date)

iii. COVID-19 Recovery Loss Mitigation Options

(B) Standard

The Mortgagee must review eligible Borrowers for the COVID-19 Recovery Options. Eligible Borrowers may receive more than one COVID-19 Recovery Option.

(1) Borrowers who were on a COVID-19 Forbearance

The Mortgagee must review all Borrowers who were on a COVID-19 Forbearance for the COVID-19 Recovery Options after the completion or expiration of the Borrower's forbearance period.

(4) Homeowner Assistance Fund

The Mortgagee must inform the Borrower, utilizing any available method of communication, that they can apply for the Department of Treasury's Homeowner Assistance Fund (HAF), if HAF is available in their jurisdiction. As permitted by the jurisdiction's HAF program, HAF funds may be used in connection with the Borrower's FHA-insured Mortgage or any Partial Claim Mortgage in a manner consistent with the respective mortgage documents and FHA requirements.

(C) COVID-19 Recovery Home Retention Options

(1) COVID-19 Recovery Standalone Partial Claim

The COVID-19 Recovery Standalone Partial Claim reinstates the Mortgage through the use of a Partial Claim for Borrowers impacted by COVID-19 who are able to resume their Mortgage Payments. The Mortgagee must evaluate Owner-Occupant Borrowers impacted by COVID-19 for a COVID-19 Recovery Standalone Partial Claim.

(a) Eligibility

The Mortgagee must ensure that:

- The Borrower indicates they have the ability to resume making on-time Mortgage Payments; and
- The Property is owner-occupied.

(b) Terms

The Mortgagee must ensure that:

- the COVID-19 Recovery Standalone Partial Claim fully reinstates the Mortgage;
- the COVID-19 Recovery Standalone Partial Claim amount includes only arrearages, which refers to any amounts needed to bring the Borrower current and includes:
  - Mortgagee advances for escrow items;
  - Projected escrow shortage amount; and
  - related legal fees and foreclosure and bankruptcy costs not higher than the foreclosure-related fees and costs HUD has identified as customary and reasonable; and
- for a COVID-19 Recovery Standalone Partial Claim, the Partial Claim must not exceed 25 percent of the unpaid principal balance as of the date of Default at the time of payment of the initial Partial Claim less any previous Partial Claims paid.

Eligible Borrowers may receive more than one COVID-19 Recovery Standalone Partial Claim.

(2) COVID-19 Recovery Modification

For Borrowers who do not meet the requirements for a COVID-19 Recovery Standalone Partial Claim, the Mortgagee must review the Borrower for the COVID-19 Recovery Modification.

(a) Definition

The COVID-19 Recovery Modification is a 360-month Loan Modification, which must include a Partial Claim, if Partial Claim funds are available. The COVID-19 Recovery Modification targets a reduction in the P&I portion of the Borrower's monthly Mortgage Payment.

(b) Eligibility

The Mortgagee must ensure that:

- the Borrower indicates they have the ability to make the modified monthly payment; and
- the Property is owner-occupied.

Eligible Borrowers may receive more than one COVID-19 Recovery Modification.

(c) Standard

Step 2 – Arrearages

The Mortgagee must calculate the arrearages. Arrearages refers to any amounts needed to bring the Borrower current and includes:

- unpaid accrued interest;
- mortgagee advances for escrow items;
- projected escrow shortage amount; and
- related legal fees and foreclosure and bankruptcy costs not higher than the foreclosure-related fees and costs HUD has identified as customary and reasonable.

Mortgagees may include an additional month in the total outstanding debt to be resolved to allow time for the Borrower to return the executed Loan Modification documents before the modified Mortgage Payment.

(d) Terms

The Mortgagee must ensure that the COVID-19 Recovery Modification fully reinstates the Mortgage including all arrearages.

(3) COVID-19 Recovery Non-Occupant Loan Modification

The Mortgagee must review Non-Occupant Borrowers for a COVID-19 Recovery Non-Occupant Loan Modification.

(a) Definition

The COVID-19 Recovery Non-Occupant Loan Modification is a rate and term loan modification.

(b) Eligibility

The Mortgagee must ensure that:

- the Borrower indicates they have the ability to make the modified mortgage payments; and
- the Property is not owner-occupied. The Property can be used as a Rental Property, Secondary Residence, or Vacation Home for the Borrower.

Requests for Waiver of Housing Directive – Office of Single Family Housing

Waiver Item: Handbook 4000.1, Section III.A.o.iv(A)(3), COVID-19 Advance Loan Modification Standard, Bullet 2; Mortgagee Letter (ML) 2021-18, III.A.2.o.ii(C), Bullet 3

Relief Sought:

A waiver of the following requirement under the "Standard" for the COVID-19 Advance Loan Modification (COVID-19 ALM): "No later than August 24, 2021, the Mortgagee must review the following Borrowers for a COVID-19 ALM where the Mortgagee has not yet sent out the final documents to the Borrower to complete a Loss Mitigation Option as of June 25, 2021: Borrowers who have exited or requested to exit their COVID-19 Forbearance; Borrowers whose COVID-19 Forbearance has expired or will expire by August 24, 2021; or Borrowers who were not on a COVID-19 Forbearance."

Employee Justification

Since the establishment of the COVID-19 Advance Loan Modification (COVID-19 ALM) option in Mortgagee Letter (ML) 2021-15, published June 25, 2021, some Mortgagees have indicated that it is difficult for them to timely operationalize a portfolio level review of Borrowers prior to August 24, 2021, to determine which Borrowers would qualify for a 25% reduction in their monthly payment of Principal and Interest from a rate and term modification at market rate. Mortgagees further indicated that due to their inability to perform this level of review, certain Borrowers would face delays in receiving loss mitigation documents until the Mortgagee performs this calculation. Further, on July 23, 2021, HUD published ML 2021-18, which established the COVID-19 Recovery Options and expanded eligibility for the COVID-19 ALM to all Borrowers who are 90 or more Days Delinquent and not on a COVID-19 Forbearance through the end of the COVID-19 National Emergency. This expansion mitigated the need for Mortgagees to review Borrowers for the COVID-19 ALM by the August 24, 2021, date. Therefore, Mortgagees no longer need to re-review:

- Borrowers where the Mortgagee has not yet sent out the final documents to the Borrower to complete a Loss Mitigation Option as of June 25, 2021;
- Borrowers who have exited or requested to exit their COVID-19 Forbearance;
- Borrowers whose COVID-19 Forbearance has expired or will expire by August 24, 2021;
- Borrowers who were not on a COVID-19 Forbearance by August 24, 2021.

Mortgagees are reminded they must still implement the COVID-19 ALM for all eligible Borrowers no later than 60 days from the publication date of ML 2021-15.

Waiver Item: Mortgagee Letter (ML) 2021-18, COVID-19 Recovery Loss Mitigation Options, III.A.2.o.iii(B)(3), Bullet 1

Relief Sought

A Waiver of the requirement under bullet 1 of the "Standard" for the COVID-19 Recovery Loss Mitigation Options: Re-Review of Borrowers, which reads: "the Mortgagee has not yet sent out the final documents to the Borrower to complete one of the COVID-19 Home Retention Options found in ML 2021-05 as of August 22, 2021."

Employee Justification

On July 23, 2021, HUD published ML 2021-18 establishing the COVID-19 Recovery Options, which included the COVID-19 Recovery Loan Modification that targeted a 25% reduction to a Borrower's principal and interest portion of their monthly mortgage payment. FHA also implemented, in that same ML, policies for the COVID-19 Recovery Standalone Partial Claim, which is the same as the existing COVID-19 Standalone Partial Claim except for a limitation on the maximum partial claim amount available. Pursuant to that ML, Mortgagees were required to ensure Borrowers who were not sent final loss mitigation documents by August 22, 2021, are provided the opportunity to receive COVID-19 Recovery Options. Following the publication of the ML, feedback from Mortgagees has been, in part, that complying with that time frame puts them in the difficult position of either resolving Borrower delinquency quickly or complying with the requirements of the ML. Further, Mortgagees have indicated that Borrowers may have already agreed to a loss mitigation option under the existing policy and would be confused by a revised loss mitigation offer. This waiver will allow Mortgagees to continue with the current loss mitigation options prior to the effective date of ML 2021-18 that is October 21, 2021.

Appendix C – Sample Results

	FHA case number (first six digits)	Borrowers received incorrect loss mitigation		Servicers did not follow HUD's guidance					
		Improper option	Miscalculated or did not reinstate	Improper HAF notification[3]	Significant delays	Improper waterfall	No ALM review	Unnecessary documents	Late mailing of documents
1	091-662				X				
2	221-555					X	X		
3	374-838						X		
5	048-478		X						
6	094-838	X							
7	061-530		X		X			X	
8	514-166				X				
9	352-627	X							
10	105-955	X							
11	512-209		X		X		X	X	
12	461-702	X							
13	461-700	X							
14	052-922	X							
15	351-774				X				
16	023-785		X			X			
17	156-424		X		X		X		
18	095-561		X						
19	111-165	X							
20	181-336	X							
21	512-374		X		X				
22	197-698	X							
23	244-157	X							

[3] Only marked if HAF was available in the borrower's jurisdiction. Not marked if HAF was not yet available.

	FHA case number (first six digits)	Borrowers received incorrect loss mitigation		Servicers did not follow HUD's guidance					
		Improper option	Miscalculated or did not reinstate	Improper HAF notification[3]	Significant delays	Improper waterfall	No ALM review	Unnecessary documents	Late mailing of documents
24	374-795			X	X		X		
25	544-175		X						
27	413-446	X							
28	263-633	X							
29	494-488				X				
30	105-805		X		X				
31	413-720		X				X		
32	138-050		X			X			
33	512-247		X						
34	249-657		X		X	X	X		
35	352-939	X							
38	061-522								X
39	061-540		X						X
41	181-310				X	X			
45	094-837				X				
46	044-557				X				
47	091-667		X	X	X	X			
48	061-478		X						
49	048-919			X					
50	071-198		X						
51	011-936		X						
52	291-546				X	X			
53	049-109	X							
55	023-720	X							
57	483-567	X							

	FHA case number (first six digits)	Borrowers received incorrect loss mitigation		Servicers did not follow HUD's guidance					
		Improper option	Miscalculated or did not reinstate	Improper HAF notification[3]	Significant delays	Improper waterfall	No ALM review	Unnecessary documents	Late mailing of documents
60	094-766				X				
62	548-575			X					
63	045-965							X	
64	011-726		X						
66	281-490		X						
67	291-546	X							
68	106-241		X		X				
69	544-210	X							
70	352-840	X							
73	137-955						X	X	
74	138-037	X							
75	092-719	X							
77	221-479								X
78	352-842		X						
80	071-135							X	
81	241-961	X							
82	451-120		X						
83	081-087		X						
84	461-566		X						
85	249-557		X						
	Total	22	26	4	18	7	8	5	3

Appendix D – Statistical Projection – Results and Methodology

Audit Universe

The audit universe consisted of 231,362 delinquent loans with an unpaid principal balance of more than $41 billion. These loans were 90 days delinquent and had a COVID-19 forbearance at any time during the pandemic (beginning March 2020) but were no longer on forbearance in October 2021.

Sampling Methodology

We identified a stratified sample of 85 records for auditing from the universe. We designed the strata to group sampling units by the size of their valuation. Therefore, we rank ordered the sampling units by the unpaid balance for each loan. The strata breakpoints encompassed the following ranges by percentile: 0-10, 10-30, 30-50, 50-70, 70-90, 90-95, and 95-100. We employed a systematic sort in the final sample design to help control for differences across servicers and the default status date of a given loan. The table below lists the strata boundaries and other key data related to this sample design.

Sample design table

Stratum	Amount	Total count in stratum	Sample count	Probability of selection	Sampling weight
0-10pct	≥	23,136	10	0.00043	2313.6
10-30pct	≥ $67834	46,273	10	0.00022	4627.3
30-50pct	≥ $112762	46,269	10	0.00022	4626.9
50-70pct	≥ $127034	46,276	14	0.00030	3305.4
70-90pct	≥ $211430	46,272	21	0.00045	2203.4
90-95pct	≥ $311204	11,567	10	0.00086	1156.7
95-100pct	≥ $372696	11,569	10	0.00086	1156.9
Total	N/A	231,362	85	N/A	N/A

We tested the sample design with various rates of error to confirm that we could obtain a reliable projection answer with this sample design and that the confidence intervals as specified would provide an accurate probabilistic statement. Based on the testing and simulated sampling distributions, we found a stratified sample of 85 to be more than sufficient, and we selected that sample size.

Dollar Projection Results

We found that in 67 of the 85 loan records reviewed, borrowers met the overall condition. This amounts to a weighted average per loan of $141,650. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that this amounts to at least $129,299 per loan. In the context of the universe of 231,362 loans, this amounts to $32.7 billion in loans. Therefore, after deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least $29.9 billion in FHA-insured loans met the overall condition, and this dollar amount could be higher.

Per loan calculation: $141,650.44 – (1.665 ⨯ $7,419.43) ≈ $129,299.88 LCL
Universe projection: 231,362 ⨯ ($141,650.44 – (1.665 ⨯ $7,419.43)) ≈ $29,915,079,811.79 LCL

Subcondition 1

We found that in 48 of the 85 loan records reviewed, borrowers met the first subcondition. This amounts to a weighted average per loan of $101,898. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that this amounts to at least $86,539 per loan. In the context of the universe of 231,362 loans, this amounts to $23.5 billion in loans. Therefore, after deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least $20 billion in FHA-insured loans met the first subcondition, and this dollar amount could be higher.

Per loan calculation: $101,898.79 – (1.665 ✕ $9,226.82) ≈ $86,539.59 LCL
Universe projection: 231,362 ✕ ($101,898.79 – (1.665 ✕ $9,226.82)) ≈ $20,021,971,674.35 LCL

Subcondition 2

We found that in 31 of the 85 loan records reviewed, borrowers met the second subcondition. This amounts to a weighted average per loan of $67,997. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that this amounts to at least $51,805 per loan. In the context of the universe of 231,362 loans, this amounts to $15.7 billion in loans. Therefore, after deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least $11.9 billion in FHA-insured loans met the second subcondition, and this dollar amount could be higher.

Per loan calculation: $67,997.54 – (1.665 ✕ $9,726.87) ≈ $51,805.95 LCL
Universe projection: $231,362 ✕ ($67,997.54 – (1.665 ✕ $9,726.87)) ≈ $11,985,928,648.67 LCL

Percentage-Count Projection Results

We found that in 67 of the 85 loan records reviewed, borrowers met the overall condition. This amounts to a weighted average of 75.2 percent. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least 67.1 percent of the loans met the overall condition. Extending this percentage to the universe of 231,362 loan records, at least 155,297 FHA loans met the overall condition, and the count of loans could be higher.

Percentage calculation:	75.29% – (1.665 ✕ 4.90%) ≈ 67.12% LCL
Total loans projection:	231,362 ✕ (75.29% – (1.665 ✕ 4.90%)) ≈ 155,297.72 LCL

Subcondition 1

We found that in 48 of the 85 loan records reviewed, borrowers met the first subcondition. This amounts to a weighted average of 53.0 percent. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least 43.6 percent of the loans met the first subcondition. Extending this percentage to the universe of 231,362 loan records, at least 100,910 FHA loans met the first subcondition, and the count of loans could be higher.

Percentage calculation:	53.02% – (1.665 ✕ 5.65%) ≈ 43.62% LCL
Total loans projection:	231,362 ✕ (53.02% – (1.665 ✕ 5.65%)) ≈ 100,910.21 LCL

Subcondition 2

We found that in 31 of the 85 loan records reviewed, borrowers met the second subcondition. This amounts to a weighted average of 37.26 percent. Deducting for a statistical margin of error, we can say – with a one-sided confidence interval of 95 percent – that at least 28.3 percent of the loans met the second subcondition. Extending this percentage to the universe of 231,362 loan records, at least 65,580 FHA loans met the second subcondition, and the count of loans could be higher.

Percentage calculation:	37.26% – (1.665 ✕ 5.36%) ≈ 28.35% LCL
Total loans projection:	231,362 ✕ (37.26% – (1.665 ✕ 5.36%)) ≈ 65,580.59 LCL

Modeling and Precision

To determine sample size, we used computer simulations to model the true sampling distribution of possible audit findings. This ensures that the sampling distribution of possible audit findings conform to the central limit theorem and that this design is dependable enough to rely on a traditional confidence interval of $\mu \pm z_{(1-\alpha/2)} * SE$. To parameterize the computer simulations (or replicated sampling), we modeled the behavior and accuracy of possible audit findings. To do this, we used the audit universe of 231,362 loan records and modeled circumstances where the likelihood of error (how often the audit team found a material deficiency in their test questions per sampling unit) ranged from 15 percent to 50 percent of the time in 5 percent increments over various sample sizes. For each of these error ranges, we treated each individual loan's unpaid balance as the sampling unit valuation. Our results indicated that the sample size of 85 met the one-sided 95 percent confidence interval, the likelihood of a negative result happened no more than 1 in 1,000 simulations, and the precision result always yielded less than 50 percent.

In addition to the diligence taken in designing this sample and selecting a count of 85 records, below are the precision estimates for each of our projection estimates:

Overall condition

Per loan calculation:	\$141,650.44 – (1.665 × \$7,419.43) ≈ \$129,299.88 LCL
Universe projection:	231,362 × (\$141,650.44 – (1.665 × \$7,419.43)) ≈ \$29,915,079,811.79 LCL
Precision calculation:	(\$141,650.44 – \$129,299.88) / \$141,650.44 ≈ 8.72 percent

First subcondition

Per loan calculation:	\$101,898.79 – (1.665 × \$9,226.82) ≈ \$86,539.59 LCL
Universe projection:	231,362 × (\$101,898.79 – (1.665 × \$9,226.82)) ≈ \$20,021,971,674.35 LCL
Precision calculation:	(\$101,898.79 – \$86,539.59) / \$101,898.79 ≈ 15.07 percent

Second subcondition

Per loan calculation:	\$67,997.54 – (1.665 × \$9,726.87) ≈ \$51,805.95 LCL
Universe projection:	231,362 × (\$67,997.54 – (1.665 × \$9,726.87)) ≈ \$11,985,928,648.67 LCL
Precision calculation:	(\$67,997.54 – \$51,805.95) / \$67,997.54 ≈ 23.81 percent