



U.S. DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT
OFFICE OF INSPECTOR GENERAL

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Memorandum

TO: Charles S. Coulter
Deputy Assistant Secretary for Single Family, HU

FROM: *Edgar Moore*
Edgar Moore
Regional Inspector General for Audit, Boston Region, 1AGA

SUBJECT: Pysma Lending Group, LLC, Danbury, CT, Complied With HUD-FHA Loan
Origination and Quality Control Requirements

INTRODUCTION

We audited Pysma Lending Group, LLC, a nonsupervised lender,¹ located in Danbury, CT, in support of the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) goal of improving the integrity of the single-family insurance program. We selected Pysma for audit because its 3.28 percent default rate for Federal Housing Administration (FHA)-insured single-family loans with beginning amortization dates between December 1, 2009, and November 30, 2011, was higher than the overall national average of 1.91 percent for the same period and its default rate was generally higher than the average of the States in which the lender originated the majority of its loans.² Our audit objectives were to determine whether Pysma acted in a prudent manner and complied with HUD regulations, procedures, and instructions in the origination of the FHA-insured single-family loans selected for review and implemented a quality control plan in accordance with HUD's requirements.

¹ A nonsupervised lender is a financial institution that has as its principal activity the lending or investment of funds in real estate mortgages. A nonsupervised lender can originate, purchase, hold, and service FHA insured loans and submit applications for insurance.

² As of January 10, 2012, the default rates for the States in which Pysma originated the majority of its loans were Florida 17.86 percent vs. 2.50 percent; Massachusetts 10.00 percent vs. 1.52 percent; South Carolina 8.33 percent vs. 2.05 percent; and Connecticut 1.06 percent vs. 1.95 percent.

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METHODOLOGY AND SCOPE

Our survey generally covered a 3-year period from January 1, 2009, through December 31, 2011. We performed onsite work at the lender's office, located at 10 Precision Drive, Danbury, CT, between January and August 2012. To accomplish the survey objectives, we

- Identified, obtained, and reviewed relevant regulations pertaining to the origination of single-family mortgages, including the Code of Federal Regulations (CFR), HUD handbooks, mortgagee letters, and the United States Code.
- Obtained and reviewed pertinent performance information relating to the lender.
- Obtained, reviewed, and documented whether the lender maintained a quality control plan that met HUD requirements.
- Obtained and reviewed copies of policies and procedures that the lender used in its loan origination processes.
- Obtained FHA case-level data on all properties originated or sponsored during the audit period by the targeted lender and data on associated loans, insurance, claims, defaults, and demographics.
- Assessed other general aspects of the branch's operations to ensure their continued lender approval status.
- Selected a nonstatistical sample of 24 FHA-insured loans for potential review. We initially identified 38 loans with early payment defaults³ and reduced this figure by eliminating (1) loans that were originated before January 1, 2009 (4 loans), (2) loans identified as streamline refinances (9 loans), and (3) loans previously reviewed by HUD's Quality Assurance Division (1 loan).
- Of the 24 loans identified for potential review, performed a detailed review of 18⁴ loans, with a combined mortgage value of more than \$4 million, to identify any that might be ineligible for insurance based on HUD's requirements. We relied on information from systems used by HUD (including Neighborhood Watch and Enterprise Data Warehouse) to target loans for review and verified that the information submitted to HUD was consistent with the information in the lender's own files.
- Identified a total of 22 loans that closed between February and April 2012, of

³ An early payment default is a loan that becomes 60 days past due within the first six payments. Lenders are required to review all loans going into default within the first six payments as part of quality control.

⁴ Although we initially identified 24 loans for potential review, ultimately we reviewed only 18 since we did not identify any significant origination deficiencies with the 18 loans reviewed. We are satisfied that our review provided a sufficient assessment of the lender's origination practices.

which 5 loans were reviewed under Prysma's quality control plan. We evaluated the 5 FHA-insured loans with regard to timeliness, adequacy of the reviews and whether they met HUD requirements. These loans were not part of the 18 loans previously reviewed.

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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

BACKGROUND

The National Housing Act, as amended, established FHA, an organizational unit within HUD. FHA provides insurance to protect lenders against losses on borrowers financing homes. The basic single-family mortgage insurance program is authorized under Title II, section 203(b), of the National Housing Act and is governed by regulations in 24 CFR Part 203. The single-family programs are generally limited to dwellings with one- to four-family units. HUD handbooks and mortgagee letters provide detailed processing instructions and advise the mortgage industry of major changes to FHA programs and procedures.

Prysma is a HUD-FHA-approved Title II nonsupervised lender located in Danbury, CT. HUD authorized the lender to originate FHA loans on August 17, 2004. A nonsupervised lender is a financial institution that has as its principal activity the lending or investment of funds in real estate mortgages. A nonsupervised lender can originate, purchase, hold, and service FHA-insured loans and submit applications for insurance. During our review, Prysma was an authorized agent for one lender and authorized principal for seven lenders.

HUD's Neighborhood Watch system⁵ reported that Prysma officials originated 274 FHA-insured loans with beginning amortization dates between December 1, 2009, and November 30, 2011. As of January 10, 2012, Neighborhood Watch reported that nine of these loans were seriously delinquent, resulting in a default rate for this 2-year period of 3.28 percent, which is higher than the 1.91 percent rate for the rest of the United States. Prysma originated at least one FHA loan in eight different States during this period, with primary originations occurring in the States of Florida and Connecticut.

RESULTS OF REVIEW

Our review determined that Prysma complied with HUD regulations, procedures, and instructions for the origination of the FHA-insured single-family loans selected for review. From January 1, 2009, through December 31, 2011, Prysma originated 512 FHA-insured loans with a

⁵ Neighborhood Watch is a Web-based comprehensive data processing, automated query, reporting, and analysis system that is intended to aid HUD in monitoring lenders and its programs and is designed to highlight exceptions to lending practices regarding high-risk mortgages so that potential problems are readily identifiable.

combined mortgage value exceeding \$109 million. Of those loans, we identified a total of 38 loans that went into early payment default and performed a detailed review of 18 of those loans, with a combined mortgage value of more than \$4 million. We did not identify any material issues that would exclude the loans from being eligible for insurance according to HUD requirements.

Additionally, we determined that Prysma established and implemented a quality control plan that complied with HUD-FHA requirements. HUD Handbook 4060.1, REV-2, chapter 7, requires all FHA-approved lenders to implement and continuously have in place a quality control plan for the origination and servicing of insured mortgages as a condition of receiving and maintaining FHA approval. This chapter also provides that quality control must be a prescribed and routine function of each lender's operations, whether performed by a lender's staff or an outside source.

During the review, Prysma's routine quality control reviews were conducted externally by a quality control contractor, Mortgage Compliance Advisors, LLC. We performed a limited review of Prysma's quality control plan covering the 3-month period February through April 2012. During that time, the lender closed 22 FHA-insured loans, and quality control reviews were performed on 5 of those loans, representing 23 percent of the loans closed. No material deficiencies were reported. Our review of 18 loans selected for detailed review also did not disclose any material concerns.

CONCLUSION

Our review determined that for the loans reviewed, Prysma complied with HUD regulations, procedures, and instructions in the origination of the FHA-insured single-family loans and implemented a quality control plan in accordance with HUD-FHA requirements. We did not identify any origination deficiencies from the specific loans reviewed that would require further detailed review.

RECOMMENDATIONS

Based on the results of the audit, this report contains no recommendations.