



U.S. Department of Housing and Urban Development
Office of Inspector General, Region VI
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September 17, 2010

**MEMORANDUM NO:
2010-FW-1805**

MEMORANDUM FOR: Vicki B. Bott
Deputy Assistant Secretary for Single Family Housing, HU

//signed//

FROM: Gerald R. Kirkland
Regional Inspector General for Audit, Fort Worth Region, 6AGA

SUBJECT: Financial Freedom Senior Funding Corporation, Irvine, CA, Improperly Funded
One Ineligible HECM Loan

INTRODUCTION

While performing an internal audit¹ of the U. S. Department of Housing and Urban Development's (HUD) Home Equity Conversion Mortgage (HECM) program, we noted one HECM loan underwritten by Financial Freedom Senior Funding Corporation, (Financial Freedom) of Irvine, CA, that was improperly insured as the property had several years of deferred property taxes, which is a violation of the HECM regulations.

METHODOLOGY AND SCOPE

As part of our internal audit, we selected a random sample of deferred HECM loans in the general Dallas/Fort Worth, TX, area for review. We interviewed 9 borrowers regarding their experience with their HECM loan and reviewed 11 lender files to determine servicer efforts to resolve unpaid taxes and insurance with borrowers. We used Lexis Nexis and property records to assist in determining eligibility, status of property taxes, and approximate value of the properties of the selected loans.

We conducted our audit from December 2009 through June 2010 at our office in Fort Worth, TX, and at various homes in the general Dallas/Fort Worth, TX, area. Our audit period was January 1, 2008, through December 31, 2009. We expanded the scope as necessary to accomplish our objective.

¹ Audit Report No. 2010-FW-0003, "HUD Was Not Tracking Almost 13,000 Defaulted HECM Loans With Maximum Claim Amounts of Potentially More Than \$2.5 Billion," issued on August 25, 2010.

BACKGROUND

The HECM program enables homeowners to obtain income by accessing the equity in their homes. To be eligible for a HECM loan, homeowners must be 62 years of age or older, have significant equity in their home, and have received HUD-approved reverse mortgage counseling to learn about the program. There are no minimum income or credit requirements. A HECM loan provides homeowners with cash payments or credit lines. The maximum amount they can receive is determined by the borrowers' age, interest rate, and value of their home or HUD's loan limits, whichever is less. The loan is secured by the home's equity. Borrowers are not required to repay the loans as long as the borrower continues to live in the home, maintains the property, and pays the property taxes and homeowners insurance premiums. However, the servicer may file a claim with HUD for the property when the loan principal reaches 98 percent of the maximum claim amount.

HUD regulations also require that properties be free and clear of all liens other than the Federal Housing Administration (FHA) HECM mortgage.² In addition, HECM regulations prohibit the borrower from participating in a real estate tax deferral program and do not permit any liens to be recorded against the property unless such liens are subordinate to the insured mortgage and any second mortgage held by the HUD Secretary.³

RESULTS OF REVIEW

Financial Freedom improperly originated 1⁴ of the 11 HECM loans reviewed because the property did not meet program requirements. Neither Financial Freedom's loan correspondent, 1ST AA Reverse Mortgage, Inc., nor the title company found that the property had property tax deferments totaling \$14,285 covering approximately 20 years. As neither the originating lender nor the borrower had paid the taxes before the loan closed, HECM regulations were not followed, and the loan should not have been FHA insured. As of February 28, 2010, the loan's unpaid principal balance was \$74,906, and the maximum claim amount was \$77,900.

RECOMMENDATION

We recommend that HUD's Deputy Assistant Secretary for Single Family Housing

- 1A. Require Financial Freedom to indemnify HUD for HECM loan number 491-8453315, with a principal balance of \$74,906.

² 24 CFR (Code of Federal Regulations) 203.32

³ 24 CFR 206.27

⁴ HECM loan number 491-8453315

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments



September 3, 2010

U.S. Department of Housing and Urban Development
Office of Inspector General, Region VI
Attention: Gerald R. Kirkland
Regional Inspector General for Audit, Fort Worth Region, 6AGA
819 Taylor Street, Suite 13A09
Fort Worth, TX 76102

RE: Draft Memorandum dated August 9, 2010 (Memorandum No. 2010-FW-180X)
Subject: Financial Freedom Senior Funding Corporation, Irvine, CA, Improperly Funded One Ineligible
HECM Loan (Memorandum No. 2010-FW-180X)

Dear Mr. Kirkland:

We are in receipt of your letter dated August 9, 2010, and accompanying draft Memorandum with the referenced Subject matter identified as "Financial Freedom Senior Funding Corporation (FFSFC), Irvine, CA, Improperly Funded One Ineligible HECM Loan." On March 19, 2009, Financial Freedom Acquisition LLC (FFA) acquired certain assets of FFSFC, including the servicing rights with respect to the loan listed in the Background Section of your Memorandum. Although FFA did not originate this loan, FFA as servicer, is working with FFSFC to address the outstanding issue. Following the receipt of HUD's initial inquiry, FFA reviewed FFSFC's origination file for this loan. Based on further review, and at the direction of FFSFC, we are providing a response to your Memorandum and supporting documentation for this originated file.

Thank you for giving us an opportunity to provide a response to the finding.

1) Audit Finding

Financial Freedom Senior Funding Corporation (FFSFC) improperly originated 1 of 11 HECM loans reviewed because the property did not meet program requirements. Neither FFSFC's loan correspondent, 1st AA Reverse Mortgage, Inc., nor the title company found that the property had property tax deferrals totaling \$14,285 covering approximately 20 years. As neither the originating lender nor the borrower had paid the taxes before the loan closed, HECM regulations were not followed and the loan should not have been FHA insured.

Comment 1



The mortgagor shall not participate in a real estate tax deferral program or permit any liens to be recorded against the property, unless such liens are subordinate to the insured mortgage and any second mortgage held by the Secretary.

3) Response and Analysis

Comment 1

FFA respectfully disagrees with this finding as FFSFC followed HECM regulations in accordance with the HUD regulations as described above based on the following analysis:

As is standard industry practice before a loan is originated a lender identifies whether or not there are any delinquent deferred taxes only if a lien is filed on the property. In this case, there was only one tax lien identified on the title policy issued on June 22, 2004 with an effective date of June 8, 2004 to the Dallas County Tax Collector in the amount of \$9,539.80. As a lender requirement, this tax lien was paid at closing as referenced in the Final HUD-1 Settlement Statement. If there was a lien for the \$14,285, FFSFC would have required them to be paid at closing. However, the School District did not record a lien on the property prior to FFSFC's mortgage recording as evidenced by the final Title Policy reflecting FFSFC in first position. Therefore, we believe that FFSFC did accurately follow the HUD regulations regarding mortgage liens and HECM rules.

While not part of the originating process, it is important to note that in August 2007, FFSFC was notified by its tax service provider that the School District taxes were delinquent in the amount of \$14,285.11 for years covering 1987-2006. On September 18, 2007 FFSFC paid those taxes and added the amount to the unpaid principal balance.

For your convenience, the following is attached as Exhibit A:

- o Title commitment
- o Title policy
- o Tax Certification for the \$9,539.80 Dallas County unpaid taxes
- o Final HUD-1 Settlement Statement
- o Copy of check showing when the \$14,285.11 was paid through Servicing
- o Copy of School District's Payment history and statement reflecting current balance due of \$0.

Again, thank you for the opportunity to provide a response. If you have any questions, please do not hesitate to contact me at (949) 923-4221.

Sincerely,



OIG Evaluation of Auditee Comments

Comment 1

Financial Freedom Acquisition, LLC⁵ disagreed that Financial Freedom improperly originated the HECM loan. It contended that it is a standard industry practice that before a loan is originated a lender identifies whether or not there are any delinquent or deferred taxes only if a lien is filed on the property. In this case, the title company identified one tax lien for \$9,539.80 and paid it off at closing. Additional taxes for \$14,285 owed to the Dallas School District were not recorded as a lien on the property and could not be identified prior to the mortgage origination. Attachments provided with the response are not included as they included nondisclosable personal information.

OIG disagrees with the auditee response. Both HUD's Single Family Mortgage Insurance and HUD's Home Equity Conversion Mortgage requirements⁶ state that for a mortgage to be eligible for insurance there cannot be restrictions on conveyance. Additionally, HECM requirements state that the property must be "freely marketable." The State of Texas has a tax deferral program that allows a homeowner who is 65 or older or a disabled person to defer payment of property taxes on the person's residence homestead until he or she no longer owns or occupies the home as a residence. However, a deferral merely postpones when the taxes must be paid. Generally, once the homeowner dies or no longer occupies the residence, all accrued taxes, penalties, and interest must be paid. Further, on the 181st day, the entire amount becomes delinquent and the taxing unit can pursue foreclosure. In addition, a lien may not be filed, as property taxes do not have to be delinquent when a deferral affidavit is submitted. For this loan, the outstanding deferred school district taxes were a restriction on the conveyance and prohibited the home from being freely marketable; thus, the loan was not eligible for insurance.

⁵ According to Financial Freedom Acquisition, on March 19, 2009, it acquired certain assets of Financial Freedom Senior Funding, including the servicing rights with respect to loan number 491-8453315.

⁶ 24 CFR 203.41(b) and 206.45