



Issue Date March 31, 2010

Audit Report Number 2010-PH-1005

TO: Vicki Bott, Deputy Assistant Secretary for Single Family Housing, HU

//signed//

FROM: John P. Buck, Regional Inspector General for Audit, Philadelphia Region,
3AGA

SUBJECT: Infinity Home Mortgage Company, Inc., Cherry Hill, NJ, Did Not
Implement a Quality Control Plan in Accordance With HUD Requirements

HIGHLIGHTS

What We Audited and Why

We audited Infinity Home Mortgage Company, Inc. (Infinity Home Mortgage), a nonsupervised¹ lender approved to originate Federal Housing Administration (FHA) single-family mortgage loans. We selected Infinity Home Mortgage because its default rate for the State of Pennsylvania was significantly higher than the average default rate for the State. Our objective was to determine whether Infinity Home Mortgage complied with U.S. Department of Housing and Urban Development (HUD) regulations, procedures, and instructions in the origination and quality control review of FHA loans.

What We Found

Infinity Home Mortgage generally complied with HUD requirements, procedures, and instructions in the origination of FHA loans. However, it did not implement a quality control plan in accordance with HUD requirements. It did not review all loans that defaulted within the first six payments as required by HUD. It also did

¹ A nonsupervised lender is an FHA-approved lending institution that has as its principal activity the lending or investing of funds in real estate mortgages.

not follow HUD requirements related to the minimum percentage, frequency, and timeliness of quality control reviews. In addition, Infinity Home Mortgage was not able to support all of the quality control reviews that it stated it performed. These conditions occurred because Infinity Home Mortgage disregarded HUD requirements and did not adequately implement its quality control plan. Consequently, the effectiveness of the plan, which was designed to ensure accuracy, validity, and completeness in its loan underwriting process, was lessened.

What We Recommend

We recommend that HUD's Deputy Assistant Secretary for Single Family Housing direct Infinity Home Mortgage to implement its quality control functions as required and follow up in 6 months to ensure the lender's compliance.

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

We provided a draft report to Infinity Home Mortgage on March 4, 2010. We discussed the audit results with Infinity Home Mortgage during the audit and at an exit conference on March 17, 2010. Infinity Home Mortgage provided written comments to our draft report on March 25, 2010. It agreed with our report. The complete text of its response can be found in appendix A of this report.

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BACKGROUND AND OBJECTIVE

The U.S. Department of Housing and Urban Development's (HUD) strategic plan states that part of its mission is to increase homeownership, support community development, and increase access to affordable housing free from discrimination.

The National Housing Act, as amended, established the Federal Housing Administration (FHA), an organizational unit within HUD. FHA provides insurance for lenders against loss on single-family home mortgages.

In 1983, HUD implemented the direct endorsement program, which authorized approved lenders to underwrite loans without HUD's prior review and approval. There are three types of approved direct endorsement lenders—supervised, nonsupervised and governmental institutions. A supervised lender is an FHA-approved financial institution that is a member of the Federal Reserve System or an institution with accounts insured by the Federal Deposit Insurance Corporation or the National Credit Union Administration. A nonsupervised lender is an FHA-approved lending institution that has as its principal activity the lending or investing of funds in real estate mortgages. A governmental institution includes a Federal, State or municipal government agency, Federal Reserve Bank, Federal Home Loan Bank, Federal Home Loan Mortgage Corporation and Federal National Mortgage Association. HUD requires lenders to use its Neighborhood Watch system to monitor and evaluate their performance and has many sanctions available for taking actions against lenders or others who abuse the direct endorsement program.

Infinity Home Mortgage Company, Inc. (Infinity Home Mortgage), is a nonsupervised direct endorsement lender for FHA loans. Its main office is located in Cherry Hill, NJ. Infinity Home Mortgage originated 29 loans between June 2007 and May 2009 that defaulted within the first 2 years. Of the 29 loans valued at about \$4.4 million, 21 valued at approximately \$2.8 million defaulted after 12 payments or fewer. We reviewed 8 of the 21 loans valued at more than \$1.5 million.

Infinity Home Mortgage received a termination of origination approval agreement notice, dated December 11, 2009, because its early default and claim rate in HUD's Philadelphia jurisdiction exceeded the termination thresholds. The termination of origination approval agreement precludes the office from originating single-family loans within the stated geographic area. Infinity Home Mortgage can present an appeal to HUD regarding the termination notice. After consideration of the material presented to HUD by Infinity Home Mortgage, and if warranted, the termination notice may be sustained or withdrawn pursuant to 24 CFR (Code of Federal Regulations) 202.3 (c) (2) (iii). The effect of the termination notice is not yet known.

Our objective was to determine whether Infinity Home Mortgage complied with HUD requirements, procedures, and instructions in the origination and quality control review of FHA loans. Minor findings noted in relation to Infinity Home Mortgage's origination of FHA loans were separately communicated to Infinity Home Mortgage in a letter, dated March 16, 2010.

RESULTS OF AUDIT

Finding 1: Infinity Home Mortgage Did Not Implement a Quality Control Plan in Accordance With HUD Requirements

Infinity Home Mortgage did not review all loans that defaulted within the first six payments (early payment defaults) as required by HUD. It also did not follow HUD requirements related to the minimum percentage, timeliness, and frequency of quality control reviews. In addition, Infinity Home Mortgage was not able to support all of the quality control reviews that it stated it performed. These conditions occurred because Infinity Home Mortgage disregarded HUD requirements and did not adequately implement its quality control plan. Consequently, the effectiveness of the plan, which was designed to ensure accuracy, validity, and completeness in its loan underwriting process, was lessened.

Early Payment Default Loans Not Reviewed as Required

HUD Handbook 4060.1, paragraph 7-6D, requires that lenders review all loans going into default within the first six payments. Also, Infinity Home Mortgage's quality control plan states that all loans going into default within the first 6 months must be reviewed. Infinity Home Mortgage did not review all early payment defaults as required by HUD and its own quality control plan. It did not conduct quality control reviews for 23 of the 38 early payment defaults. Infinity Home Mortgage acknowledged that it did not review early payment defaults as required and stated that the requirement would be enforced going forward.

Minimum Percentage of Reviews Not Performed

HUD Handbook 4060.1, paragraph 7-6C, requires lenders to perform quality control reviews on 10 percent of loans originated. Infinity Home Mortgage did not perform the minimum percentage of quality control reviews required by HUD. In 2008 for example, Infinity Home Mortgage originated 372 loans and, therefore, should have selected 10 percent or 37 of the loans for quality control reviews. However, it only selected 30 of the loans for reviews and could only provide documentation to show that 5 of the loans were reviewed. Therefore, we were only able to verify that it performed 5 of the 37 required reviews. Infinity Home Mortgage acknowledged the deficiency and obtained quality control software to ensure a sample selection process in compliance with HUD requirements and to improve its overall quality control process.

Reviews Not Within the Required Timeframe

HUD Handbook 4060.1, paragraph 7-6A, states that loans must be reviewed within 90 days from the end of the month in which the loan closed. This requirement is intended to ensure that problems left undetected before closing are identified as early after closing as possible. Infinity Home Mortgage did not always perform quality control reviews in a timely manner as required by HUD. We randomly selected 12 of 45 FHA loans, which Infinity Home Mortgage indicated that it had reviewed, to determine whether the quality control reviews were conducted in a timely manner. Infinity Home Mortgage could only provide documentation on reviews for 5 of the 12 loans. We determined that one of the five loans was not reviewed in a timely manner. The loan was reviewed 112 days from the end of the month in which it closed.

Reviews Not Performed Monthly

According to HUD Handbook 4060.1, paragraph 7-6B, lenders closing more than 15 loans monthly must conduct quality control reviews at least monthly and must address 1 month's activity. Lenders closing 15 or fewer loans monthly may perform quality control reviews on a quarterly basis. Also, Infinity Home Mortgage's quality control plan states that the purpose of its quality control procedures is to ensure that all loans acquired meet the company's standards and HUD guidelines. However, Infinity Home Mortgage did not conduct quality control reviews on a monthly basis as required by HUD and in accordance with its quality control plan. From July 2007 through December 2008 (with the exception of January 2008 when it closed only four loans), Infinity Home Mortgage closed more than 15 loans monthly and, therefore, should have performed quality control reviews on a monthly basis. However, the lender admitted that it only performed quality control reviews on a quarterly basis and indicated that it had not adjusted its process since the early 2000s when it was not closing as many loans and, therefore, performed quality control reviews on a quarterly basis. During the audit, Infinity Home Mortgage provided an updated quality control plan that includes a policy for performing reviews on a monthly or quarterly basis based on the volume of its loans closed each month.

Conclusion

Infinity Home Mortgage officials did not ensure that (1) all early payment default loans were reviewed, (2) quality control reviews were conducted in a timely manner, (3) quality control reviews were performed on a monthly basis, and (4)

the minimum percentage of reviews was performed. These conditions occurred because Infinity Home Mortgage disregarded HUD requirements and did not adequately implement its quality control plan. As a result, the effectiveness of the plan, which was designed to ensure accuracy, validity, and completeness in its loan underwriting process, was lessened.

Recommendations

We recommend that HUD's Deputy Assistant Secretary for Single Family Housing direct Infinity Home Mortgage to

- 1A. Implement its quality control functions as required and follow up with the lender in 6 months to ensure its compliance.

SCOPE AND METHODOLOGY

We performed our audit work between August and November 2009 at Infinity Home Mortgage's office located at 660 North Kings Highway, Suite 203, Cherry Hill, NJ. Our review period was from June 2007 through May 2009.

We queried HUD's Neighborhood Watch system for information on lenders' default rates. HUD's Neighborhood Watch system is a Web-based software application that displays loan performance data for lenders and appraisers by loan types and geographic areas, using FHA-insured single-family loan information. The loan information is displayed for a 2-year origination period and is updated on a monthly basis. HUD requires lenders to use the Neighborhood Watch system to monitor and evaluate their performance.

Based on the Neighborhood Watch query results, we identified and selected Infinity Home Mortgage, located in Cherry Hill, NJ, for review because its percentage of defaults by 2 years for the State of Pennsylvania was 9.6 percent, compared with the State average of 3.94 percent.

Infinity Home Mortgage originated 29 FHA loans, valued at approximately \$4.4 million, between June 2007 and May 2009 that defaulted within the first 2 years. After eliminating refinanced loans, terminated loans, and loans with more than 12 payments before default, 21 defaulted loans remained. The 21 loans, valued at more than \$2.8 million, defaulted after 12 payments or fewer. We selected the top eight loans with the highest mortgage amounts, valued at approximately \$1.5 million, for review. To determine whether Infinity Home Mortgage complied with HUD regulations, procedures, and instructions in its origination and quality control of FHA loans, we performed the following:

- Reviewed applicable HUD handbooks and mortgagee letters,
- Performed detailed testing and review of the underwriting procedures for the eight sample loans (our detailed testing and review included (1) analysis of borrowers' income, assets, and liabilities; (2) review of borrowers' saving abilities and credit history; (3) verification of selected data on the settlement statements; and (4) confirmation of employment and gifts),
- Examined records and related documents of Infinity Home Mortgage,
- Reviewed and tested Infinity Home Mortgage's quality control plan, and
- Conducted interviews with officials of Infinity Home Mortgage and discussed issues with HUD employees.

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

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following controls are achieved:

- Program operations,
- Relevance and reliability of information,
- Compliance with applicable laws and regulations, and
- Safeguarding of assets and resources.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. They include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

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

- Loan origination process – Policies and procedures that management has in place to reasonably ensure that the loan origination process complies with HUD program requirements.
- Quality control plan – Policies and procedures that management has in place to reasonably ensure implementation of HUD quality control requirements.

We assessed the relevant controls identified above.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

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

- Infinity Home Mortgage did not adequately implement its quality control plan to ensure compliance with HUD's quality control requirements.

Appendix A

AUDITEE COMMENTS



March 19, 2010

US Department of Housing and Urban Development
Office of OIG
Philadelphia, PA

Re: Audit Results and Findings

Dear Mr. Buck;

I offer the following as our formal response to the items noted in the finding report as a result of the audit performed by your staff:

- 1) Infinity Home Mortgage's QC Control manual and policies are in compliance with HUD regulations. After careful review by your staff it was brought to my attention that the proper number of loans were not reviewed in accordance to the guidelines. Specifically the early payment defaults. Infinity as a policy performs audits on early payment defaults from the reports pulled from the Neighborhood Watch that can be found while accessing the FHA Connection. Unfortunately, we were selecting loans from the report sorted by the entire US instead of by field office. We performed random selection from this report instead of adhering to the guideline of all loans that are report as early payment defaults in the first (6) months. Infinity has implemented a policy August 2009 going forward that all early payment defaults reported within the first (6) months will be fully audited. In addition, Infinity Home Mortgage also has implemented a policy to perform audits on loans going into default within the first (12) months as well as our own policy.
- 2) Infinity Home Mortgage has made proper revisions to our QC Plan and they all have been implemented. Examples of these changes are as follows:
 - A) 4506T's are pulled on all loans prior to closing and are reviewed prior to closing and reviewed during the QC process as well. Policy was implemented August 2009.
 - B) Verbal Verification of Employment are completed (10) days prior to closing and then again the day of closing. They are also verified during the QC process. Policy was implemented June 2009

Regie Plaza Suite 200 Cherry Hill, NJ 08003
one (856) 470-1101 • Fax (856) 470-1128

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- C) Fraud Reports are pulled and verified on all loans prior to closing for verification of social security numbers, addresses, telephone numbers and proper identity of the borrowers. Policy was implemented July 2009.

- D) AVM's – evaluations are pulled on all loans prior to closing for verification of comparables used during the appraisal process and insurance of the value being reported by the appraiser. Policy was implemented August 2009.

- E) Fico score requirements have also changed and all borrowers must have a minimum of 620 middle score reported on their credit reports. – Policy was implemented August 2008.

We feel these implemented policy changes will enhance our processing and underwriting of loans and will decrease the number of loans that go into default.

- 3) Infinity Home Mortgage acquired Quality Control Software in October 2009 from a company by the name of, Tena Corporation. In addition, Infinity has hired a QC Specialist in November 2009. The employee has well over 15 years of experience specifically with Quality Control. With hiring the new employee and utilization of the software, Infinity's QC Plan and work related to QC is in compliance and will remain so going forward.

- 4) As explained during our audit, Infinity holds monthly training meetings and seminars with all loan officers to insure that all guidelines are reviewed properly and adhered to. These meetings are performed by Senior Management and on occasion if necessary with Underwriting and Closing Management for further implementation.

- 5) Infinity Home Mortgage moved our location in December 2008 to 660 N. Kings Highway Cherry Hill, NJ 08034. During this period boxes were moved from our location and moved either into storage or our new office. During the course of the move, boxes were placed into our outside storage location. Infinity Home Mortgage currently has 2 storage facilities located outside of the office. Located in the storage units are all loans closed, originated, cancelled or rejected since

660 N. Kings Highway Cherry Hill, NJ 08034
Reggie Plaza Suite 200 Cherry Hill, NJ 08003
Phone (856) 470-1101 • Fax (856) 470-1128
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INFINITY

HOME MORTGAGE COMPANY, INC.
*A Licensed Mortgage Banker of New Jersey and Pennsylvania
Department of Banking and Insurance*

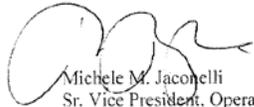
Infinity Home Mortgage opened for business. During the audit period we were asked to provide the auditors with QC Files, QC Findings and all results of same on certain files. We were able to provide all the finding reports and selection lists, but were unable to provide all of the files containing the QC result paperwork. Unfortunately, during the move, we did begin to Shred older files from 2002, 2003 and 2004. After several attempts to locate these files we were unsuccessful. However, as mentioned above, we did produce all finding reports and reports to senior management as these are kept in the office with Senior Management.

- 6) Infinity performs QC audits on a monthly basis. At the time that Infinity opened for business we were auditing files on a quarterly basis as we did not close the minimum required amount of loans (15) monthly to perform them monthly. However, Infinity Home Mortgage performs audits on an ongoing basis each and every month. There was occasion that they were not completed timely as stated in the report. This occurred as mentioned in the report on 1 file that was reviewed over the time period of 90 days.
- 7) Audits were performed on 8 loan files by your office. There were no deficiencies or discrepancies found with any of the underwriting performed by Infinity Home Mortgage on any of the 8 files that the audit was performed on. We feel that this is a very positive outcome of the audit performed by your office and are very proud same.

Thank you and your staff as the experience that we had during the audit as they were very helpful, understanding and informative throughout the whole procedure.

Should you have any questions, or require any additional information, do not hesitate to contact me directly.

Thank you,



Michele M. Jaconelli
Sr. Vice President, Operations

Infinity Home Mortgage Company, Inc. 200 Cherry Hill, NJ 08003
Phone (856) 470-1101 • Fax (856) 470-1128