



# FEDERAL HOUSING FINANCE AGENCY OFFICE OF INSPECTOR GENERAL

## SEMIANNUAL REPORT TO THE CONGRESS

October 1, 2013, through March 31, 2014





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# OIG's Mission

The mission of the Federal Housing Finance Agency Office of Inspector General (OIG) is to: promote the economy, efficiency, and effectiveness of the programs and operations of the Federal Housing Finance Agency (FHFA or Agency); prevent and detect fraud, waste, and abuse in FHFA's programs and operations; review and, if appropriate, comment on pending legislation and regulations; and seek administrative sanctions, civil recoveries, and criminal prosecutions of those responsible for fraud, waste, or abuse in connection with the programs and operations of FHFA.

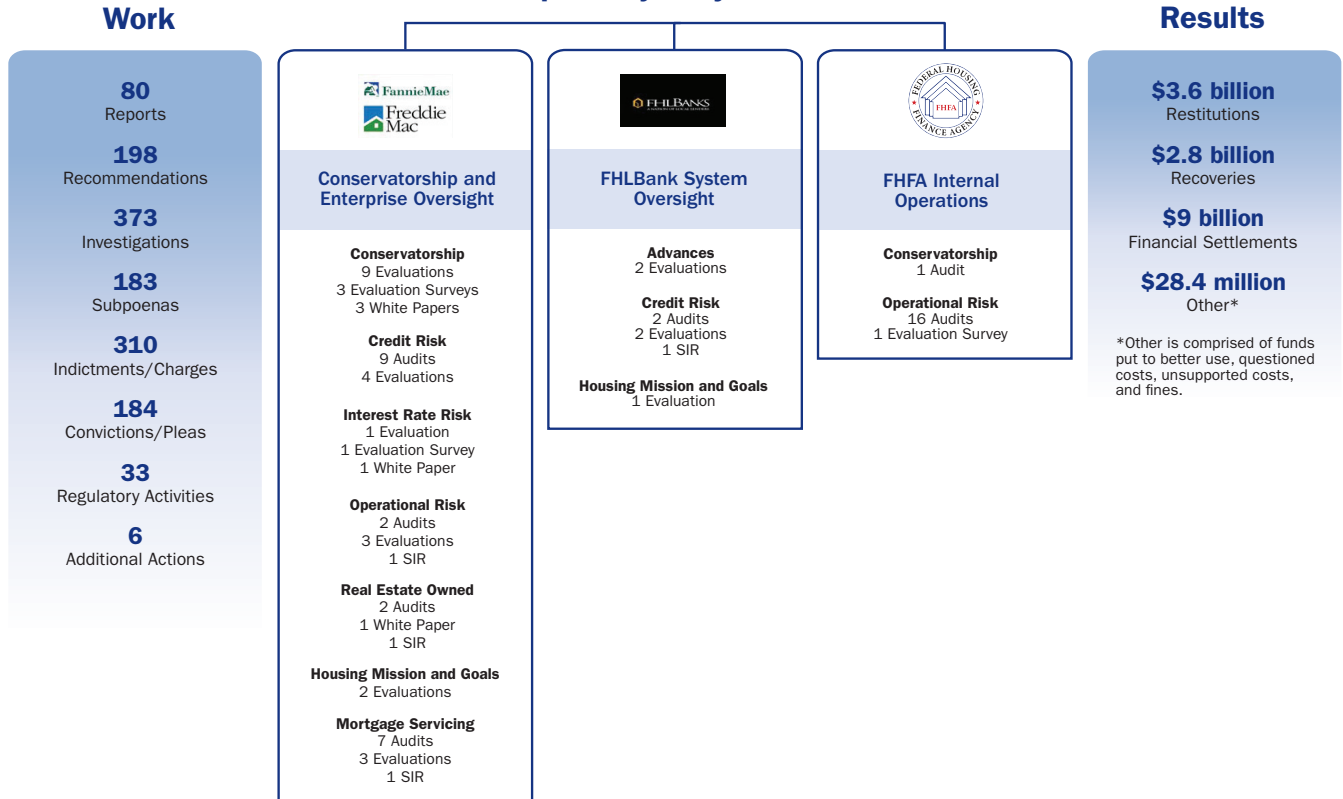
In carrying out this mission, OIG conducts independent and objective audits, evaluations, investigations, surveys, and risk assessments of FHFA's programs and operations; keeps the head of FHFA, Congress, and the American people fully and currently informed of problems and deficiencies relating to such programs and operations; and works collaboratively with FHFA staff and program participants to ensure the effectiveness, efficiency, and integrity of FHFA's programs and operations.

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# OIG's Accomplishments from 2010 to Present



## Reports by Subject Area







# A Message from the Acting Inspector General

I am pleased to present OIG's seventh Semiannual Report to the Congress, which covers our activities and operations from October 1, 2013, to March 31, 2014.

During this semiannual reporting period, OIG continued to promote the effectiveness, integrity, and transparency of FHFA's programs and operations. On one hand, OIG's findings credit FHFA for effectuating positive change in selected areas. Most notably, Fannie Mae and Freddie Mac (collectively, the Enterprises) reported positive financial results, and notably, dividend payments from the Enterprises to the Department of the Treasury (Treasury) now exceed the amount of assistance they received. On the other hand, OIG has provided several recommendations to improve the effectiveness of FHFA programs. An equally important event for the Agency was the change in leadership when Melvin L. Watt was sworn in to a five-year term as Director on January 6, 2014. We look forward to working with the Director and Agency staff in identifying ways to facilitate the mission and goals of FHFA.

OIG has continued to assess high-risk areas at FHFA, the government-sponsored enterprises (GSEs), and their counterparties, and to offer recommendations for improvement. This semiannual period we issued 17 audit and evaluation reports focusing on key mission areas affecting the nation's housing finance system. These reports address a range of topics from better use of appraisal data, to reducing the risk of loss and improving loan quality, to overpayments for pre-foreclosure property inspections, to FHFA compliance with requirements in the Housing and Economic Recovery Act (HERA) to report on Federal Home Loan Bank (FHLBank) director expenses. I am also pleased to report our Office of Audits recently completed its first peer review and received the highest opinion provided on its quality control with no deficiencies identified.

OIG also remains active on the law enforcement front. During this period, OIG's investigative efforts resulted in the indictment of 82 individuals and the conviction of 62 individuals, as well as the award of more than \$46 million in criminal fines and restitution orders. Many of our investigations produced significant results. For example, OIG along with other federal and state agencies reached a \$13 billion settlement with JPMorgan. And, in Denver, the subject of an OIG investigation was sentenced to 14 years in prison for an illegal scheme to take control of foreclosed homes through "home squatting."

In closing, I want to thank all of the dedicated employees at OIG for their efforts in making this report possible. Their efforts ensure that our important public service mission is fulfilled.

Michael P. Stephens  
Acting Inspector General  
April 30, 2014



Michael P. Stephens  
Acting Inspector General of the  
Federal Housing Finance Agency



# Executive Summary

## Overview

This Semiannual Report discusses OIG operations and FHFA developments from October 1, 2013, to March 31, 2014.<sup>1</sup>

During this semiannual reporting period, OIG issued 17 audit and evaluation reports and investigative efforts resulted in the indictment of 82 individuals and the conviction of 62 individuals. FHFA also issued a few key directives and welcomed new leadership.

As the Enterprises began their sixth year in **conservatorships**,\* many of the conditions identified in our prior Semiannual Report remained. The Enterprises continued to occupy a sizeable portion of the secondary mortgage market. Further, the Enterprises continued to report strong profits stemming from stronger credit quality, guarantee fee income, increases in home prices, and reduced **defaults**. Under the arrangement that sweeps these profits back to Treasury, as of the end of the first quarter of 2014, the Enterprises have paid more to Treasury in dividends than the amount of assistance they received.

Meanwhile, throughout 2013, the **FHLBanks** continued to experience demand for advances, particularly by large-asset members. However, average short-term interest rates generally decreased,

resulting in lower returns on interest-bearing assets, which contributed to a decline in the FHLBanks' net income for the year ended December 31, 2013.

Exploring these and other issues, this report is organized as follows. Section 1, *OIG Description, Accomplishments, and Strategy*, highlights several OIG audits, evaluations, and investigations relating to the programs and operations of FHFA. Section 2, *FHFA and GSE Operations*, provides a closer look at FHFA and **GSE** developments during this reporting period.

## Section 1: OIG Description, Accomplishments, and Strategy

This section provides a brief overview of OIG's organization and describes its oversight activities, including audits, evaluations, and investigations. It also discusses OIG's priorities and goals.

For example, in this section we discuss:

- *FHFA's Oversight of the Servicing Alignment Initiative* (EVL-2014-003, February 12, 2014), in which we examined how FHFA oversees the Servicing Alignment Initiative—an initiative it established to improve mortgage **servicers'** performance in managing delinquent loans and limit the Enterprises' financial losses.
- *Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises* (EVL-2014-002, December 19, 2013), in which we evaluated FHFA's efforts to address the concerns from our prior report on the Agency's ability to meet critical responsibilities, including lacking a sufficient number of examiners and assigning many examiners without professional commission program accreditation.

**\*Terms and phrases in bold are defined in Appendix A, Glossary and Acronyms. If you are reading an electronic version of this Semiannual Report, then simply move your cursor to the term or phrase and click for the definition.**

- *Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened* (AUD-2014-003, November 20, 2013), in which we assessed FHFA's oversight of Fannie Mae's controls over borrower eligibility requirements for its **short sale** program.
- *FHFA Oversight of Fannie Mae's Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties* (AUD-2014-004, January 15, 2014), in which we analyzed how FHFA is overseeing Fannie Mae's efforts to refund certain inappropriately collected borrower short sale contributions that came to light in the audit mentioned above.

We also discuss numerous OIG investigations that resulted in indictments and convictions of individuals responsible for fraud, waste, or abuse in connection with FHFA's and the regulated entities' programs and operations, and in fines and restitution orders totaling more than \$46 million.

Further, this section addresses our:

- Audit and Evaluation Plan, which focuses on areas of FHFA operations posing the greatest risks to the Agency and to **Fannie Mae, Freddie Mac**, and the FHLBanks (collectively, the GSEs);
- Regulatory Activities, which include our assessment of proposed legislation, regulations, and policies related to FHFA; and
- Communications and Outreach Efforts, which educate stakeholders—FHFA, Congress, policymakers, and the public—about OIG, FHFA, and GSE developments, as well as broader issues of fraud, waste, and abuse.

## Section 2: FHFA and GSE Operations

This section describes the organization and operations of FHFA, the Enterprises, and the FHLBanks, as well as key developments for each during the reporting period.

Among the most notable developments during the semiannual period was the change in leadership at FHFA when Melvin L. Watt was sworn in to a five-year term as director. He is the first FHFA Director to be confirmed by the Senate.

This section goes on to detail the continued improvement in the Enterprises' financial results. It also discusses the Enterprises' joint venture to build and operate a new common securitization infrastructure for residential mortgage-backed securities (RMBS) and FHFA's changes to mortgage insurance master policy requirements.

Additionally, during this time period, FHFA and other federal financial agencies issued a final rule exempting some higher-priced mortgage loans from certain appraisal requirements; FHFA directed the Enterprises to delay implementation of planned mortgage guarantee fee increases; the Agency solicited public input on a proposal to reduce loan limits; the Enterprises announced transactions conducted in line with FHFA's initiative to transfer credit risk to the private sector; and the Agency terminated the Enterprises' pension plans. These and other developments and OIG's efforts in relation to them are summarized in Section 2.



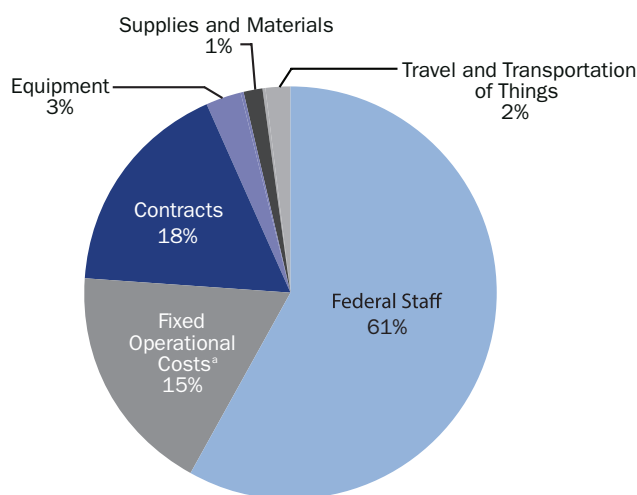
# Section 1: OIG Description, Accomplishments, and Strategy

## Description

OIG began operations on October 12, 2010. It was established by **HERA**, which amended the **Inspector General Act**. OIG conducts audits, evaluations, investigations, and other law enforcement activities relating to FHFA's programs and operations.

OIG's operations are funded by annual assessments that FHFA levies on the Enterprises and the FHLBanks pursuant to 12 U.S.C. § 4516. For fiscal year 2014, OIG's operating budget (see Figure 1, below) was \$48 million, with 150 full-time-equivalent staff.

**Figure 1. OIG's Operating Budget for Fiscal Year 2014**



<sup>a</sup> Fixed operational costs include items such as space rent, shared service agreements with other federal agencies to provide information technology and administrative services, printing, and the hotline.

## Leadership and Organization

On April 12, 2010, President Barack Obama nominated FHFA's first Inspector General, Steve A. Linick, who was sworn into office on October 12,

2010. Mr. Linick resigned on September 29, 2013, and his Principal Deputy Inspector General, Michael P. Stephens, commenced acting in the capacity of Inspector General pursuant to 5 U.S.C. § 3345(a)(1).

Mr. Stephens was appointed as Principal Deputy Inspector General in September 2011. Prior to his joining OIG, Mr. Stephens served as Acting Inspector General and Deputy Inspector General for the Department of Housing and Urban Development (HUD). Earlier, he was the Deputy Assistant Inspector General for Investigations for the Department of Veterans Affairs and a senior criminal investigator for the Office of Inspector General for the Resolution Trust Corporation. Each of these appointments followed a distinguished 20-year career with the Secret Service, during which he held the distinction of being assigned to the Presidential Protection Division at the White House, along with various supervisory positions within the agency.

OIG consists of the Acting Inspector General, his senior staff, and OIG offices, principally: the Office of Audits (OA), the Office of Evaluations (OE), and the Office of Investigations (OI). Additionally, OIG's Executive Office and the Office of Administration provide organization-wide supervision and support. (See Appendix E for OIG's organizational chart and Appendix F for a detailed description of OIG's offices and strategic goals.)

## Accomplishments and Strategy

From October 1, 2013, to March 31, 2014, OIG's significant accomplishments included: (1) issuing 17 audit and evaluation reports; (2) participating in a number of criminal and civil investigations; and (3) reviewing and commenting on FHFA rules.

## Audits and Evaluations

During this semiannual period, OIG released 17 audit and evaluation reports, which are summarized below.

### Audits

#### FHFA Oversight of Enterprise Controls Over Pre-Foreclosure Property Inspections (AUD-2014-012, March 25, 2014)

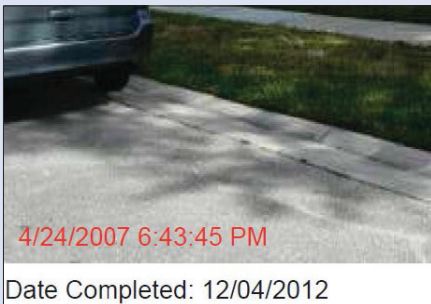
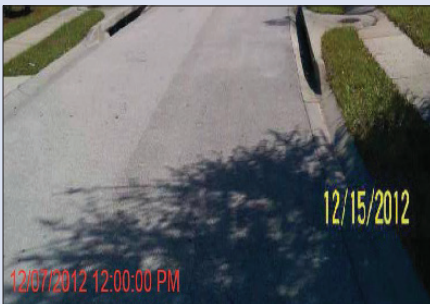
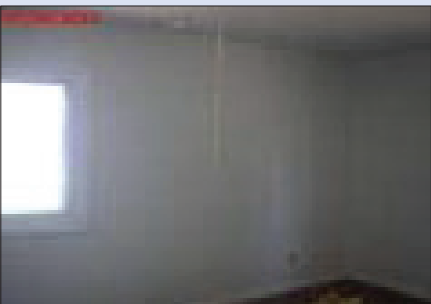
Fannie Mae and its servicers use property inspections, referred to as pre-foreclosure property inspections, when a borrower becomes delinquent. One of the inspections' objectives is to help minimize credit losses and identify any apparent safety hazards. Fannie Mae requires servicers to perform a monthly inspection on all properties where borrowers have become delinquent, subject to reimbursement limits per loan. The Enterprises reimbursed servicers approximately \$91.2 million in 2011-2012 for property inspections performed by contractors related to delinquent loans.

The severity of risk in the property inspection business was recently highlighted by the conviction of a

property preservation contractor whose company created and submitted fraudulent property inspection reports to servicers for reimbursement. The possibility of other property inspection vendors engaging in the same practice presents a potential risk to the Enterprises.

OIG found that the pre-foreclosure property inspection process needs improvement to ensure that pre-foreclosure inspection objectives are achieved in the most effective manner. There is limited assurance that the Enterprises have effective controls in place to ensure the quality of inspections conducted and that inspectors issue reports consistent with contractual requirements. Overall, several servicers reviewed during the audit did not have quality controls in place to ensure contractors provided accurate, complete, and consistent information in property inspection reports. Specifically, OIG identified inspection reports with inconsistent and inaccurate information, missing or blurry photographs, and manipulated date and time stamps on the photographs (see Figure 2, below). OIG also identified unnecessary inspections that did not provide useful information about the properties.

**Figure 2. Blurry and Manipulated Inspection Photographs**

|   |  |  |
|---|--|--|
|                                |    |   |
| <ul style="list-style-type: none"><li>• The inspector used a 2007 picture for a 2012 inspection report.</li></ul> | <ul style="list-style-type: none"><li>• The inspector changed the date on the picture so it appears each picture was taken eight days earlier.</li></ul> | <ul style="list-style-type: none"><li>• The inspector submitted a report wherein each picture was blurry and the date on the picture was not adequately visible.</li></ul> |



Further, the servicers reviewed by OIG inconsistently adopted requirements for inspectors to complete and pass criminal background checks.

These deficiencies in the pre-foreclosure property inspection process occurred, in part, because of minimal attention and oversight provided by both FHFA and the Enterprises, along with limited Enterprise quality standards for inspections conducted by inspectors under contract with servicers.

OIG recommended that FHFA direct the Enterprises to assess jointly the effectiveness of their pre-foreclosure property inspection processes. Based on this assessment, FHFA should direct the Enterprises to establish uniform pre-foreclosure inspection quality standards and quality control processes for inspectors.

FHFA identified corrective actions that address OIG's recommendations.

### **FHFA's Controls to Detect and Prevent Improper Payments FY 2013 (AUD-2014-011, March 20, 2014)**

The Improper Payments Information Act of 2002 (IPIA) initiated the legislation that provides for estimates and reports of improper payments by federal agencies. It was followed by amendments in 2010 and 2012 to help prevent the further loss of billions in taxpayer dollars. IPIA requires federal agencies to periodically review, determine, estimate, and report programs and activities that may be susceptible to significant improper payments. For simplicity, this report referred to the original act and all its amendments as IPIA. We conducted a performance audit to assess FHFA's compliance with IPIA and other financial criteria for fiscal year 2013.

Federal agencies regularly make payments to program beneficiaries (or on behalf of them), grantees, vendors, and contractors. Some of these payments

may be "improper" in one or more respects. For example, they may be made to the wrong recipients, in the wrong amounts, at the wrong times, or for the wrong reasons. Additionally, for improper payments estimated in excess of \$10 million, the agency must report the potential actions it is taking to reduce and recapture improper payments.

OIG is required to review FHFA's improper payment reporting in its annual Performance and Accountability Report (PAR) to determine whether FHFA is in compliance with IPIA and to report this and other findings. However, not all IPIA requirements are applicable to FHFA. In fact, the Agency stated that most requirements of IPIA and implementing guidance are not applicable to them, as noted in Figure 3 (see page 7).

After reviewing applicable statutes, executive orders, and other compliance requirements related to improper payments; reviewing various Government Accountability Office (GAO) audit reports; interviewing key FHFA officials; obtaining sufficient and appropriate evidence regarding compliance actions taken; and reviewing and assessing improper payment element requirements and related activities, we concluded that FHFA complied with the applicable statutory improper payment requirements, as well as related Office of Management and Budget (OMB) criteria. FHFA opined that the remaining requirements were not applicable. OIG recognized that FHFA is acting to achieve the intent of IPIA and related OMB criteria in spite of its determination that it is not required to do so.

FHFA responded to a draft of this report offering no objection to its conclusions.

### **FHFA's Use of Government Travel Cards (AUD-2014-010, March 20, 2014)**

The Government Charge Card Abuse Prevention Act of 2012 (Charge Card Act) requires all executive branch agencies to establish and maintain

safeguards and **internal controls** for charge cards. OMB provided supplemental guidance through Memorandum M-13-21, *Implementation of the Government Charge Card Abuse Prevention Act of 2012*, dated September 6, 2013. OMB’s memorandum requires each agency head to provide an annual certification that all policies and controls are in place or that corrective actions have been taken to mitigate the risk.

Under the Charge Card Act, inspectors general must assess the risk of fraud or inappropriate charges and additionally can perform audits at their discretion. Agencies with more than \$10 million in purchase card spending must jointly report with its office of inspector general to OMB every six months on employee violations of card use per the agency’s policies. FHFA’s purchase and travel card spending was less than \$10 million for fiscal year 2013, so it

**Figure 3. FHFA’s Status of IPIA Compliance for Fiscal Year 2013**

| Compliance Element  | OIG Conclusion  |
|---|---|
| (A) The agency has published an annual PAR or financial statement for the most recent fiscal year and posted that report and any accompanying materials required under guidance of OMB on the agency website.   | FHFA published the 2013 PAR and included relevant information pertaining to improper payments.  |
| (B) If required, the agency has conducted a program-specific risk assessment for each program or activity that conforms with section 2(a) of IPIA (31 U.S.C. § 3321 note).  | FHFA determined that section 2(a) of IPIA is not applicable because FHFA funds are not federal funds for purposes of this provision.  |
| (C) The agency has published improper payments estimates for programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).  | FHFA determined that section 2(b) of IPIA is not applicable because FHFA funds are not federal funds for purposes of this provision.  |
| (D) The agency has published programmatic corrective action plans in the PAR or Agency Financial Report (if required).  | FHFA determined that section 2(c) of IPIA is not applicable because FHFA funds are not federal funds for purposes of this provision.  |
| (E) The agency published, and has met, improper payments reduction targets established under section 2(c) of IPIA (31 U.S.C. § 3321 note) in the accompanying materials to the annual financial statement for each program assessed to be at risk and measured for improper payments. | FHFA determined that section 2(c) of IPIA is not applicable because FHFA funds are not federal funds for purposes of this provision.  |
| (F) The agency has reported a gross improper payment rate of less than 10% for each program and activity for which an estimate was obtained and published in the PAR or Agency Financial Report.  | FHFA determined that section 2(b) of IPIA is not applicable because FHFA funds are not federal funds for purposes of this provision.  |
| (G) The agency has reported information on its efforts to recapture improper payments.  | FHFA stated in its PAR that it has established and maintains internal control procedures for handling improper payments. Furthermore, FHFA stated it pursues the recovery of any improper payments with its vendors. Also, it should be noted that OIG completed an audit of FHFA’s use of government purchase cards and a subsequent audit of government travel cards. These audits include procedures to identify inappropriate purchase and travel card spending and to assess FHFA’s internal controls in place to prevent and/or detect inappropriate card use. <sup>2</sup> |

was not subject to mandatory semiannual reporting. OIG determined audits of FHFA's purchase and travel card spending were warranted precisely because of the absence of targeted audit coverage. This audit report reflects the ongoing efforts of OIG to monitor FHFA's compliance with the Charge Card Act.

OIG did not identify misuse or fraudulent travel card transactions during the audit. We further note that with limited exceptions, FHFA has implemented adequate safeguards and internal controls with respect to travel cards. The audit did identify several instances of minor noncompliance with applicable travel regulations, policies, and procedures. For example:

- FHFA travelers did not always obtain trip authorizations prior to traveling and incurring travel expenses;
- FHFA travelers did not always create and submit travel vouchers in a timely manner upon completion of travel; and
- Cash advances using the travel cards exceeded FHFA limits and did not always correspond in timing to the travel dates.

OIG recommended that FHFA enhance travel card controls to improve compliance with applicable regulations, policies, and procedures by: (1) notifying employees that all travelers should have a properly approved authorization prior to commencing travel; (2) notifying employees to complete travel vouchers in a timely manner upon completion of travel; (3) performing a periodic review of travel cardholder ATM limits; and (4) notifying employees that they should obtain cash advances either during or immediately preceding travel.

FHFA provided comments agreeing with these recommendations.

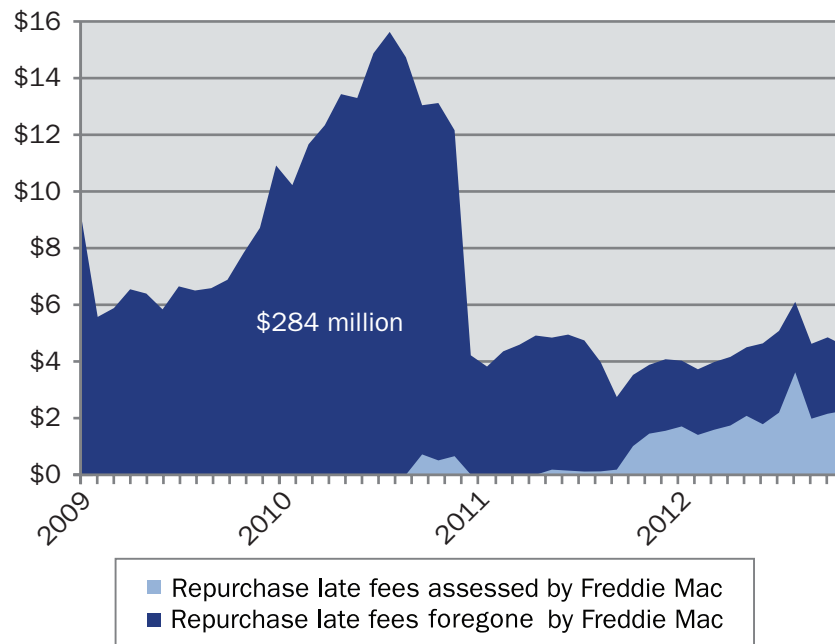
### **FHFA Oversight of Enterprise Handling of Aged Repurchase Demands (AUD-2014-009, February 12, 2014)**

In January 2012, as part of its larger effort to harmonize the Enterprises' operations, FHFA directed the Enterprises to develop "consistent timelines and collection standards" for fees, penalties, and remedies. However, the Agency's published guidance for aged repurchase demands, essentially, let each Enterprise establish its own model for penalizing seller-servicers. As a result, Freddie Mac continued to employ its existing contractual right to assess late fees on seller-servicers for not resolving repurchase demands timely. Fannie Mae, which does not have an equivalent penalty, did not utilize repurchase late fees.

FHFA allowed Fannie Mae to continue without the ability to assess repurchase late fees because the Enterprise claimed that setting up such a program could cost up to \$5.4 million. However, the Enterprise's analysis did not consider the potential benefits of the program, including a continuous stream of penalty fees. As an indication of the program's potential, Freddie Mac could have assessed as much as \$284 million from 2009 through 2012 using its existing right to assess late fees. Further, for much of that time period, Fannie Mae had a larger volume of unresolved repurchase demands than Freddie Mac. Specifically, as of July 2013, more than 10,000 of Fannie Mae's repurchase demands, totaling \$2.5 billion, had been unresolved for at least 120 days. OIG concluded that FHFA should promptly quantify the potential benefit of implementing a repurchase late fee program at Fannie Mae, and then determine whether the potential cost outweighs the potential benefit.

OIG also concluded that Freddie Mac's assessment of repurchase late fees could benefit from stronger Agency supervision. By inconsistently waiving, enforcing, and excepting late fees through 2012, the

**Figure 4. Repurchase Late Fees Foregone Versus Assessed by Freddie Mac 2009 Through 2012 (\$ millions)**



Enterprise missed assessing up to \$284 million (see Figure 4, above). Those fees are now unlikely to be collected—losses that taxpayers ultimately bore. In part, OIG traced the missed assessments to the need for robust FHFA oversight. Before its harmonization work, the Agency largely left the assessment of repurchase late fees unsupervised. Currently, the Agency does not receive sufficient information from Freddie Mac to oversee and assess this part of the Enterprise’s business.

OIG recommended that FHFA direct Freddie Mac to develop a repurchase late fee report and routinely provide the report to the Agency. The report should expand the information currently provided by adding summary information concerning the seller of outstanding repurchases, the aging of repurchases, late fees assessed and collected, discretionary late fee waivers, and global late fee exclusions. Such a report would provide Freddie Mac and FHFA management with needed information to manage and assess

Freddie Mac’s repurchase late fee program more effectively.

Finally, FHFA is not including any uncollected repurchase late fees in settlement negotiations with seller-servicers over defective loans that were sold to or serviced for the Enterprises. Such loans contributed to the Enterprises’ financial difficulties and placement under FHFA conservatorships. Increased Agency oversight can result in additional future recoveries as repurchases are settled. FHFA should direct Freddie Mac to provide the Agency with information on assessed but uncollected late fees associated with the repurchase claims included in the 2013 bulk settlements. FHFA should consider the information provided by Freddie Mac in its negotiations and document the information in accordance with the Office of Conservatorship Operations’ Settlement Policy.

FHFA provided comments agreeing with the recommendations in this report.



## FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages (AUD-2014-008, February 6, 2014)

Assessing the value of **collateral** securing mortgage loans is one of the pillars in making sound **underwriting** decisions. Before loans are presented for the relevant Enterprise to buy, appraisal and appraiser information is collected through a uniform collateral data portal system (portal). If the portal finds signs that the appraisals violate the Enterprises' requirements, it alerts them and the lenders to the problem(s). By using the portal, the Enterprises are striving to improve data quality, ensure compliance with their loan eligibility guidelines, enhance loan reviews, and lower the number of loans that must be bought back by sellers (i.e., repurchased) for not meeting their standards.

FHFA directed the Enterprises to develop the portal in 2010. As of March 2012, the portal analyzes all appraisals for single-family loans before the Enterprises can buy the loans. This is a significant undertaking since, in 2012 alone, the Enterprises collectively purchased and **guaranteed** approximately six million single-family residential mortgages, valued at \$1.3 trillion.

While the Enterprises have progressed in establishing the portal and collecting appraisal data, more remains to be done to use the portal's data to minimize the risk of loss. OIG concluded that increased FHFA oversight can enhance the Enterprises' use of the portal's appraisal data before they buy single-family mortgages and reduce collateral risk.

Specifically:

- From January 2013 through June 2013, Fannie Mae spent \$13 billion buying over 56,000 loans even though the portal's analysis of the associated appraisals warned the Enterprise that the appraisals were potentially in violation of its underwriting requirements; and
- From June 2013 through September 2013, Freddie Mac spent \$6.7 billion buying over 29,000 loans despite the portal warning the Enterprise that either no property value could be provided or the value of the property was in question.

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***In 2013, the Enterprises purchased over \$19 billion worth of loans that the appraisal portal warned may be supported by noncompliant appraisals.***

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In addition, the Enterprises bought nearly \$88 billion in loans although system logic errors in the portal did not allow them to determine if the appraiser was properly licensed. Specifically, the portal alerted the Enterprises and lenders that some appraisers were suspended; however, the Enterprises set the portal to automatically override the messages and accepted the submitted appraisals. Based on OIG's work and the Enterprises' responsive actions, 23 loans, valued at \$3.4 million, may be repurchased based on the "suspended" status of the appraiser, which is a violation of requirements.

OIG made 14 recommendations to help the Enterprises use appraisal data to improve loan quality and to reduce the risk of loss. In

general, the recommendations are geared to improve FHFA's oversight of how the Enterprises use the portal according to the Agency's directive. OIG also recommended that the Enterprises require lenders to resolve key warning messages generated by the

portal's analyses of their submitted appraisal data before buying the associated loans.

FHFA provided comments agreeing with the recommendations in this report.

### **FHFA's Implementation of Active Directory (AUD-2014-007, January 31, 2014)**

FHFA has implemented Microsoft's Active Directory to manage access by FHFA and external users, groups of users, computer systems, and services on its network. Active Directory plays a major role in assuring the confidentiality, integrity, and availability of critical FHFA information and systems by ensuring user authentication and access control to FHFA's network and systems. Accordingly, this audit's objective was to determine whether FHFA has implemented an Active Directory security infrastructure that effectively protects the confidentiality, integrity, and availability of critical systems and information. Because information in this report could be used to circumvent FHFA's internal controls, its contents have not been released publicly.

### **FHFA's Use of Government Purchase Cards (AUD-2014-006, January 31, 2014)**

On October 5, 2012, the President signed into law the Charge Card Act, Public Law 112-194. The Charge Card Act requires all executive branch agencies to establish and maintain safeguards and internal controls for charge cards. OMB provided supplemental guidance through Memorandum M-13-21, *Implementation of the Government Charge Card Abuse Prevention Act of 2012*, dated September 6, 2013.

Under the Charge Card Act, inspectors general are required to conduct periodic risk assessments of agency purchase card programs to analyze the risks of illegal, improper, or erroneous purchases. Status reports on an inspector general's purchase and travel card audit recommendations, if any,

must be submitted to OMB by January 31, 2014, for compilation and transmission to Congress and the Comptroller General of the United States. This audit report supported our efforts to fulfill these requirements.

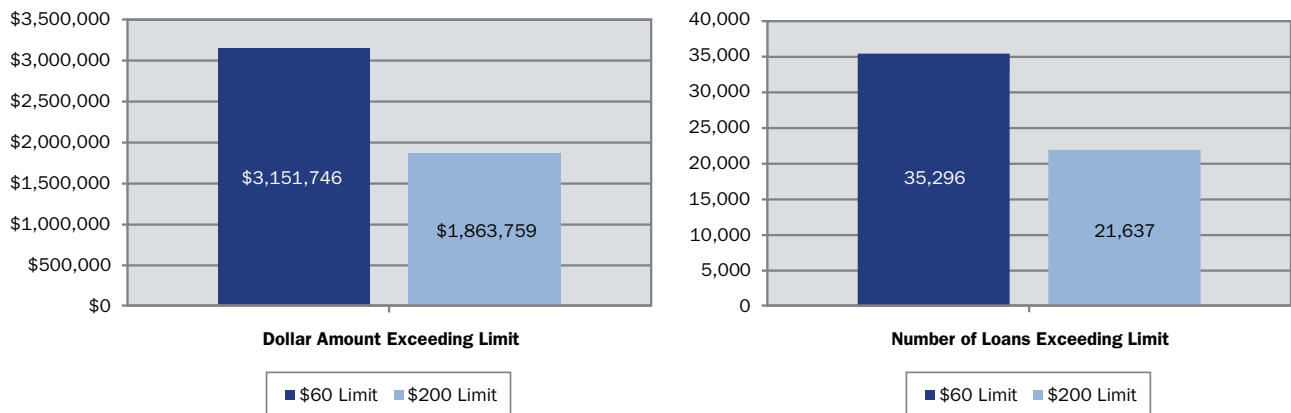
OIG did not identify any instances of noncompliance with applicable laws and regulations or fraudulent or inappropriate charge card practices. With limited exceptions, FHFA implemented adequate purchase card internal controls. OIG noted that FHFA could improve existing controls to ensure purchase cards are used in an efficient, effective, and economical manner and not for illegal, improper, or erroneous purchases by documenting policies and procedures regarding the:

- Solicitation of multiple bids and/or completion of sole-source justifications in conjunction with the purchase of employee training in excess of \$5,000;
- Execution of Continued Service Agreements for high-cost employee training;
- Approval of temporary increases in dollar limits on cardholder purchase authority; and
- Granting and removing of exceptions for card purchases in Merchant Category Codes (MCCs) not otherwise authorized.

OIG recommended that FHFA document purchase card policies and procedures related to: (1) purchase of training above the \$5,000 micro-purchase threshold; (2) use of employee Continued Service Agreements for high-cost training; (3) approval and resetting of temporary increases in transactions limits in a cardholder's purchase authority; and (4) management of MCC exceptions, which should be allowed only on a case-by-case basis and removed in a timely manner after the allowed purchase is transacted.

FHFA provided comments agreeing with the recommendations in this report.

**Figure 5. Total Overpayments and Related Mortgage Loans 2011 Through 2012**



**FHFA Oversight of Fannie Mae’s Reimbursement Process for Pre-Foreclosure Property Inspections (AUD-2014-005, January 15, 2014)**

Fannie Mae and its servicers use property inspections, referred to as pre-foreclosure property inspections, when a borrower becomes delinquent. One of the objectives of the inspections is to help protect the Enterprise’s interest in the mortgaged property from physical conditions that may result in additional credit loss. Fannie Mae requires servicers to perform a monthly inspection on all properties where borrowers have become delinquent, subject to reimbursement limits per loan.

Overall, OIG concluded that additional FHFA oversight is needed regarding pre-foreclosure property inspection claims. Specifically, Fannie Mae’s process for paying servicer property inspection claims has significant control deficiencies. Further, Fannie Mae does not have system controls to automatically approve, curtail, or reject claims based on Fannie Mae’s established reimbursement limits. As a result, Fannie Mae approved inspection claims incorrectly by using processing procedures for other types of reimbursements. These deficiencies caused the

Enterprise to overpay servicers by approximately \$5 million in 2011 and 2012 for pre-foreclosure property inspection claims in excess of established reimbursement limits (see Figure 5, above).

OIG recommended that FHFA direct Fannie Mae to: (1) obtain a refund from servicers for overpayments of property inspection claims; (2) implement system controls to reject property inspection claims over established tolerance limits; and (3) issue guidance to all servicers concerning requirements to adhere to reimbursement limits for property inspection claims. OIG also recommended that FHFA assess the need for additional examination coverage of Fannie Mae’s pre-foreclosure property inspection reimbursement process. FHFA is taking action that is generally responsive to the recommendations except for obtaining refunds for overpayments of property inspection claims.

FHFA disagreed with three of the four recommendations in this report; however, FHFA is taking action that OIG considers responsive to the recommendations except for obtaining refunds for overpayments of property inspection claims.

**FHFA Oversight of Fannie Mae’s Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties (AUD-2014-004, January 15, 2014)**

Through its review of closed short sale transactions in another audit on short sale borrower eligibility (*Fannie Mae’s Controls Over Short Sale Eligibility Determinations Should be Strengthened*, AUD-2014-003, November 20, 2013), OIG found that Fannie Mae and its servicers may have improperly collected borrower contributions for short sales of properties in the state of California and under Fannie Mae’s Home Affordable Foreclosure Alternatives (HAFA) program. The collection of these borrower contributions prompted Fannie Mae to initiate a remediation plan to return up to \$3,173,249 to borrowers who may have been impacted from the short sale of properties located in California (see Figure 6, below) and up to \$53,000 for HAFA short sales.

Based on OIG’s work, Fannie Mae developed a remediation plan. The plan was finalized in October 2013 and requires Fannie Mae to notify its servicers to refund borrowers the amount of any improper contributions for the short sale of properties. The remediation plan will address improper contributions for properties located in California closed on or

after January 1, 2011, and HAFA short sales where borrower contributions were collected. FHFA is currently reviewing Fannie Mae’s remediation plan to ensure that borrowers are protected and made whole due to inappropriate borrower contributions. Additionally, FHFA will determine if similar conditions exist at Freddie Mac, since it uses most of the same servicers as Fannie Mae and also handles defaulted loans in California.

Fannie Mae stated that the decision to pursue refunds rests with each servicer that reviews the identified cases where improper borrower contributions may have been collected. If the servicer validates that a contribution was not collected or if the servicer has a reasonable basis to support the contribution, Fannie Mae may not require a borrower refund. The servicers would also presumably decide whether they believe there was a reasonable basis to collect contributions made while the California law was unclear. As a result, the current remediation plan may not provide for consistent treatment of borrowers by servicers even if borrower circumstances are similar.

OIG recommended that the Agency review Fannie Mae’s remediation plan and ensure contributions are refunded according to a good faith effort and in a consistent manner for borrowers. In addition, OIG

**Figure 6. Borrower Contributions for California Short Sales**

| Contribution Type   | No. of Contributions | Total Amount Collected |
|---|----------------------|------------------------|
| Cash – Delegated <sup>a</sup>                                   | 900                  | \$1,903,880            |
| Cash – Nondelegated   | 288                  | \$897,311              |
| Promissory Note <sup>b</sup>                                    | 34                   | \$372,058              |
| <b>Total Contributions for Properties Located in California</b> | <b>1,222</b>         | <b>\$3,173,249</b>     |

<sup>a</sup> Fannie Mae has two categories of servicers, nondelegated and delegated. Nondelegated servicers have no authority to make short sale decisions on behalf of Fannie Mae. Their role is limited to collecting short sale information and forwarding the information to Fannie Mae for consideration. Delegated servicers have been granted authority to make short sale determinations and complete short sales on behalf of Fannie Mae subject to certain limitations in Fannie Mae’s Servicing Guide.

<sup>b</sup> Cash contributions were also paid by the borrowers for six of these short sales.



recommended that FHFA issue guidance for Fannie Mae to execute the remediation plan, if necessary, and that the Agency review Freddie Mac's controls over borrower contributions in California and issue guidance, if appropriate.

FHFA stated it agreed with OIG's three recommendations; while two of the recommendations are resolved, OIG considers one of the recommendations as unresolved.

### **Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened (AUD-2014-003, November 20, 2013)**

Short sales are part of Fannie Mae's loss mitigation strategy to pursue **foreclosure** alternatives to help minimize the severity of losses it incurs because of loan defaults. Borrowers may be eligible for a short sale if they are experiencing a financial hardship that prevents them from making their mortgage payments, and can be expected to have difficulty in selling their homes because the current value is less than the amount owed on the mortgage. Fannie Mae depends upon its servicers to collect financial information from borrowers and utilize that information to consider whether borrowers are eligible for a short sale. During 2012, Fannie Mae and its servicers approved over 73,000 short sales.

OIG assessed the Agency's oversight of Fannie Mae's borrower eligibility controls. Based on a review of 41 short sale transactions involving multiple Fannie Mae servicers, OIG found that Fannie Mae's servicers did not always collect all of the required documentation before determining eligibility or forwarding the information to Fannie Mae. In addition, servicers did not always conduct adequate reviews supporting borrower eligibility determinations. Further, OIG found that borrowers with potentially significant

financial resources sold multiple non-owner-occupied properties through one of Fannie Mae's programs.

OIG recommended that FHFA direct Fannie Mae to strengthen controls over its short sale eligibility processes, including: enforce servicer submission of all required documentation; ensure sufficient servicer eligibility reviews; consider quality in compensating servicers for their eligibility reviews; and improve controls over borrower data collected and considered in the eligibility decision. Additionally, OIG recommended FHFA consider whether one of Fannie Mae's short sale programs should be available for non-owner-occupied properties, along with increasing its examination coverage of short sales.

FHFA provided comments agreeing with the recommendations in the report.

### **Kearney & Company, P.C.'s Independent Evaluation of the Federal Housing Finance Agency's Office of Inspector General's Information Security Program-2013 (AUD-2014-002, October 31, 2013)**

The Federal Information Security Management Act of 2002 (FISMA) requires FHFA to undergo an annual independent evaluation of its information security program, as well as an assessment of its compliance with FISMA requirements. OIG elected to have an evaluation performed of our information security program since our program is independent of FHFA's information security program. Accordingly, this audit's objective was to evaluate OIG's information security program and practices, including OIG's compliance with FISMA and related information security policies, procedures, standards, and guidelines. Because information in this report could be used to circumvent OIG's internal controls, its contents have not been released publicly.

**Kearney & Company, P.C.’s Independent Evaluation of the Federal Housing Finance Agency’s Information Security Program-2013 (AUD-2014-001, October 3, 2013)**

According to FISMA, FHFA is required to have an annual independent evaluation of its information security program. Accordingly, this audit’s objective was to evaluate the Agency’s information security program and practices, including its compliance with FISMA and related information security policies, procedures, standards, and guidelines. Because information in this report could be used to circumvent FHFA’s internal controls, its contents have not been released publicly.

**Evaluations**

**FHFA’s Reporting of Federal Home Loan Bank Director Expenses (EVL-2014-005, March 20, 2014)**

This evaluation assessed FHFA’s reporting of expenses incurred by the members of the boards of directors of the FHLBanks, in light of a statutory requirement for the Agency to include information about FHLBank director expenses in its annual reports to Congress. We found that FHFA had not met this requirement to date.

We noted that FHFA does require the FHLBanks to submit director expenses to the Agency; accordingly, the Agency receives information that it could use to comply with the reporting requirement. However, we determined that FHFA had not been reviewing the FHLBanks’ data submissions. In addition, we found that the FHLBanks used differing approaches in submitting the data, thus diminishing the utility of the information.

An FHFA official told us that during the course of our evaluation, the Agency realized it should have been reporting this information, and it would begin

doing so with its 2013 annual report, which will be published in 2014. By reporting information about FHLBank director expenses, along with meeting its statutory requirement, FHFA will increase transparency and may deter questionable expenditures.

We recommended that FHFA: (1) review the 2013 director expense data submitted by the FHLBanks to identify and correct any inconsistencies and inaccuracies prior to the publication of the 2013 annual report, to the extent feasible, and disclose in the report any remaining data limitations; and (2) issue guidance to ensure the consistency and utility of the director expense data submitted to the Agency.

FHFA essentially agreed with these recommendations.

**Update on FHFA’s Oversight of the Enterprises’ Non-Executive Compensation Practices (EVL-2014-004, February 25, 2014)**

In December 2012, OIG published an evaluation report on FHFA’s oversight of the Enterprises’ compensation of their nearly 2,100 highest-paid employees, i.e., about 90 executives and 2,000 non-executive senior professionals. We observed that FHFA had increased its control and oversight of the Enterprises’ executive compensation practices in 2012, but its oversight of non-executive pay practices was comparatively limited. For example, the Agency had not reviewed, examined, or tested the structures, processes, or controls by which the Enterprises compensate their senior professionals. Enterprise compensation costs for senior professionals were \$454.6 million in 2011, roughly five times that of their executives’ compensation of \$91.8 million. We recommended that FHFA develop a plan to strengthen its oversight of the Enterprises’ compensation of their senior professionals through reviews or examinations.

In this memorandum report, we provided an update on FHFA's oversight of the Enterprises' non-executive compensation practices. In accordance with our recommendation from the 2012 study, FHFA conducted examinations in 2013 of the Enterprises' compliance with the Agency's directive to freeze employee pay during 2011 and 2012. FHFA examiners found deficiencies in the Enterprises' compliance with the directive and with their controls over senior professional compensation. In response to these deficiencies, the Agency undertook corrective action by issuing binding supervisory directives to the Enterprises. For example, FHFA directed Fannie Mae to improve "its policies, procedures, supporting documentation, and governance over compensation programs in a manner that will ensure its ability to demonstrate that these programs are being implemented in an appropriate, consistent, and transparent manner."

The Agency also instituted a limited oversight regimen for Enterprise senior professional compensation in 2013. Specifically, FHFA reviews quarterly reports prepared by the Enterprises in which the salaries paid to new hires and recently promoted employees are compared to the median pay offered to similar private-sector positions.

We observed that this procedure is a step in the right direction in that it provides FHFA with some ability to assess Enterprise senior professional compensation practices going forward.

## **FHFA's Oversight of the Servicing Alignment Initiative (EVL-2014-003, February 12, 2014)**

As the Enterprises' conservator, FHFA established the Servicing Alignment Initiative (SAI) in April 2011 to improve servicers' performance and thereby limit the Enterprises' financial losses.

SAI consists of a series of FHFA directives that set forth contractual requirements that the Enterprises must incorporate into their servicing guidelines. Servicers must comply with these guidelines when managing the accounts of financially distressed borrowers. For example, servicers are required to respond to borrowers' requests for assistance within specified time frames, and conduct loan modifications and foreclosures pursuant to procedures and deadlines prescribed by FHFA.

Our evaluation assessed FHFA's oversight of SAI since the establishment of the program in 2011. Specifically, we evaluated FHFA's monitoring of Enterprise servicers' compliance with SAI guidelines and found it to be limited.

FHFA's Division of Housing Mission and Goals (DHMG), which established SAI, has primary responsibility within the Agency for overseeing the program. DHMG

reviewed the Enterprises' servicing guidelines prior to publication in 2011 to ensure that FHFA's SAI-related directives were incorporated.

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***In accordance with OIG's recommendation, FHFA conducted examinations of the Enterprises' compliance with the Agency's directive to freeze employee pay and found deficiencies with compliance of the directive and controls over senior professional compensation.***

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However, DHMG's SAI oversight has significant limitations. DHMG has neither reviewed nor evaluated the servicers' overall compliance with SAI's numerous requirements since establishing the program in 2011. Moreover, DHMG does not require the Enterprises to submit for its routine review and assessment their critical reports on servicer compliance with SAI's requirements. Consequently, DHMG has not determined whether the servicers are complying with SAI or if the initiative is achieving its intended purpose.

We analyzed the reports by which the Enterprises monitor their servicers' compliance with SAI. The reports identified servicer compliance deficiencies in key SAI areas, such as responding to borrower requests for assistance and executing loan modifications. DHMG has not received these reports on a regular basis. Consequently, DHMG has missed opportunities to learn about servicer compliance deficiencies that could undermine SAI's effectiveness. It has also compromised FHFA's ability to oversee the Enterprises' efforts to correct their servicers' SAI compliance deficiencies.

We recommended that DHMG's Deputy Director: (1) establish an ongoing process to evaluate servicers' SAI compliance and the effectiveness of the Enterprises' remediation efforts; (2) direct the Enterprises to provide their internal reports and reviews for DHMG's assessment; and (3) regularly review SAI-related guidelines for enhancements or revisions, as necessary, based on servicers' actual versus expected performance.

FHFA partially agreed with all recommendations and committed to providing related documents by February 15, 2015. We concluded from the Agency's response, however, that the Agency did not plan to alter substantively its limited oversight of SAI. We remain concerned as to the Agency's practices in this regard.

### **Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises (EVL-2014-002, December 19, 2013)**

FHFA's examination program is a primary means by which the Agency oversees the GSEs. In a September 2011 evaluation report, we concluded that the Agency lacked a sufficient number of examiners and that many of its examiners had not been accredited through a professional commission program. In this follow-up evaluation, we provided an update on FHFA's efforts to address the issues raised previously.

Since the 2011 report, FHFA had taken initiatives to strengthen its examination capacity, such as restructuring its examination program under new leadership, increasing the number of examiners, and initiating a commission program to provide standardized training for its examiners. These changes have the potential to enhance FHFA's oversight, but it was too early to assess their effectiveness. Additionally, we found that the Agency had not yet developed a systematic process to determine the appropriate size of its examination teams for the Enterprises.

We conducted a limited assessment of FHFA's implementation of its 2013 examination plans for the Enterprises and found many of FHFA's planned activities were either completed or in process. However, about 40% of FHFA's targeted examinations for one Enterprise were rescheduled to begin during the fourth quarter of 2013; some were not anticipated to conclude until 2014. FHFA officials said that examination plans are subject to revision due to changing priorities and resource requirements; however, without a systematic process to set the size of its teams, FHFA cannot be assured that its examinations are adequately staffed. Indeed, FHFA's Examiners-in-Charge for both Enterprises said that limited examination resources and staff turnover adversely affected their operations during 2013.



Accordingly, we recommended that FHFA: (1) review its implementation of the 2013 Enterprise examination plans and document the extent to which resource limitations, among other things, may have impeded their timely and thorough execution; (2) develop a process that links annual Enterprise examination plans with core team resource requirements; and (3) establish a strategy to ensure that the necessary resources are in place to ensure timely and effective Enterprise examination oversight.

FHFA essentially agreed with these recommendations.

### **FHFA's Oversight of Derivative Counterparty Risk (ESR-2014-001, November 20, 2013)**

The Enterprises' combined capital markets businesses manage portfolios of more than \$1 trillion of mortgage-related assets. Among other capital markets activities, the Enterprises enter into a variety of complex financial instruments known as derivatives contracts. A derivative contract is, essentially, an agreement providing parties to the agreement with the obligation or choice to buy, sell, or exchange something at a future date. It can be used to offset other risks in a portfolio, such as the interest rate and prepayment risks associated with the Enterprises' mortgage assets. Derivative counterparty risk refers to the risk that one's counterparty in a derivative contract may be unable to pay the amount due at a specified date. OIG conducted this evaluation to assess FHFA's oversight of the Enterprises' management of counterparty risk associated with their investments in derivatives.

We considered FHFA's oversight of the Enterprises' management of derivative counterparty risk in conjunction with the mitigation of that risk resulting from the implementation of the central clearing mandate under Title VII of the **Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank)**. We concluded that FHFA's oversight is such that no additional study of this topic is needed.

At the same time, we found that implementation of Dodd-Frank was not uniformly applied to all regulated entities. In contrast to its oversight of the FHLBanks, FHFA did not issue to the Enterprises an Advisory Bulletin providing regulatory guidance for the implementation of Dodd-Frank.

We recommended that FHFA's Advisory Bulletins that provide guidance regarding implementation of critical regulatory changes be issued to all the impacted regulated entities.

FHFA generally agreed with our recommendation.

## **Recommendations**

A complete list of OIG's audit and evaluation recommendations is provided in Appendix B.

## **Peer Reviews**

In addition to its audits and evaluations, OIG participated in external peer review activities.

Audit organizations that perform audits of federal government programs and operations are required by *Generally Accepted Government Auditing Standards* (GAGAS) to undergo an external peer review every three years. The objectives of an external peer review are to determine, during the period under review, whether: (1) the audit organization's system of quality control was suitably designed and (2) the audit organization was complying with its own quality control system to provide reasonable assurance that it was conforming to applicable professional standards. Federal audit organizations can receive a peer review rating of pass, pass with deficiencies, or fail.

The Inspector General Act of 1978, as amended by Dodd-Frank, mandates that offices of inspector general report semiannually the results of peer reviews of their operations conducted by other offices of inspector general, the date and results of the last peer

review, outstanding recommendations from peer reviews, and peer reviews conducted by the inspector general of another office of inspector general. Peer reviews of federal offices of inspector general are conducted by member organizations of the Council of the Inspectors General on Integrity and Efficiency (CIGIE). Offices of inspector general are required to include in their semiannual reports the following information:

- ***The results of any peer review conducted by another office of inspector general during the reporting period.***

The Federal Communications Commission Office of Inspector General (FCC OIG) conducted an external peer review of OIG's OA and issued a final System Review Report on March 20, 2014. OIG received a peer review rating of pass, the best rating an audit organization can receive. No deficiencies were identified in OIG's

audit operations and the System Review Report contained no recommendations. FCC OIG identified one enhancement in a Letter of Comment accompanying its System Review Report. Copies of the System Review Report and Letter of Comment can be viewed at [www.fhfaig.gov/Content/Files/FHFA-OIG%20audit%20peer%20review\\_0.pdf](http://www.fhfaig.gov/Content/Files/FHFA-OIG%20audit%20peer%20review_0.pdf).

- ***Outstanding recommendations from any peer review conducted by another office of inspector general that have not been fully implemented, including a statement describing the status of the implementation and why implementation is not complete.*** In its Letter of Comment dated March 20, 2014, FCC OIG concluded that OIG can enhance its quality control monitoring activities by ensuring full implementation of its

quality control plan related to the review of all GAGAS requirements for selected performance audits. OIG agreed with the benefit of such reviews and included the reviews as an annual quality control review requirement in its Quality Control Plan for fiscal years 2014-2016 published in August 2013. Additionally, OIG announced the first annual review and will consider the recommendation closed upon its completion scheduled for June 30, 2014.

- ***Ongoing OIG audit peer review activity.***

No external peer reviews of another federal audit organization were conducted by OIG during this semiannual reporting period. OIG is preparing to conduct a peer review of the audit organization of the Legal Services Corporation Office of Inspector General. We will report the results of that review in an upcoming semiannual report.

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***OIG received a peer review rating of pass, the best rating an audit organization can receive.***

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## **Civil Fraud Initiative**

OA launched its Civil Fraud Initiative in June 2013. OA, with support from OI and the Office of Counsel, conducts civil fraud reviews (also known as nonaudit services) to identify fraud and make referrals for civil actions and administrative sanctions against entities and individuals who commit fraud against FHFA, Fannie Mae, Freddie Mac, or the FHLBanks.

Currently, OA is working with various Assistant U.S. Attorneys on reviews of lenders' loan origination practices to determine their compliance with Enterprise requirements. Lenders are considered for review through the use of data-mining techniques and requests from government agencies.

## Audit and Evaluation Plan

OIG maintains an Audit and Evaluation Plan that focuses strategically on the areas of FHFA's operations that pose the greatest risks to the Agency and the GSEs. The plan responds to current events and feedback from FHFA officials, members of Congress, and others. The plan is available for inspection at [www.fhfaig.gov/Content/Files/audit%26evaluation%20plan\\_0.pdf](http://www.fhfaig.gov/Content/Files/audit%26evaluation%20plan_0.pdf).

## Investigations

During the semiannual period, OIG investigators participated in numerous criminal, civil, and administrative investigations, which resulted in the indictment of 82 individuals and the conviction of 62 individuals. In many of these investigations, we worked with other law enforcement agencies, such as the Department of Justice (DOJ), the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), the Postal Inspection Service (USPIS), the FBI, the Department of Housing and Urban Development Office of Inspector General (HUD-OIG), the Secret Service, and state and local entities nationwide. Further, in several investigations, OIG investigative counsels were appointed as Special Assistant U.S. Attorneys and supported prosecutions. Figure 7 (see above) summarizes the criminal and civil recoveries from our investigations. Although most of these investigations remain confidential, details about several of them have been publicly disclosed and are summarized below.

### Fraud Committed Against the Enterprises, FHLBanks, or FHLBank Member Institutions

Investigations in this category involved multiple schemes that targeted Fannie Mae, Freddie Mac, the FHLBanks, or members of FHLBanks.

**Figure 7. Criminal and Civil Recoveries from October 1, 2013, Through March 31, 2014**

|              | Criminal Recoveries    | Civil Recoveries          |
|--------------|------------------------|---------------------------|
| Fines        | \$2,468,757.26         | \$-                       |
| Settlements  | \$-                    | \$9,000,000,000.00        |
| Restitutions | \$44,090,151.01        | \$-                       |
| <b>Total</b> | <b>\$46,558,908.27</b> | <b>\$9,000,000,000.00</b> |

### Fannie Mae Insider Removes/Sells Personal Identifying Information, Dallas, Texas

On January 21, 2014, Spetial Collins pled guilty to one count of conspiracy to commit bank fraud in the U.S. District Court for the Northern District of Texas. Then on February 7, 2014, a federal indictment was unsealed in the same district charging seven more individuals as follows:

- Anthony Minor was charged with conspiracy to commit bank fraud, bank fraud (six counts), conspiracy to commit fraud and related activity in connection with identification documents, using or trafficking an unauthorized access device, and aggravated identification theft (two counts);
- Tilisha Morrison was charged with conspiracy to commit bank fraud, bank fraud (three counts), and conspiracy to commit fraud and related activity in connection with identification documents;
- Kario Butler was charged with conspiracy to commit bank fraud and bank fraud;
- Jamilah Karriem was charged with conspiracy to commit bank fraud and bank fraud;
- Karen Mendoza was charged with conspiracy to commit bank fraud and bank fraud;
- Katrina Thomas was charged with conspiracy to commit bank fraud, conspiracy to commit

fraud, and related activity in connection with identification documents; and

- Cyrus Pritchett was charged with conspiracy to commit bank fraud and bank fraud.

Between October 2009 and July 2013, the indictment alleges Minor and Morrison led a conspiracy that resulted in the theft of the personal identifying information (PII) of over 1,000 Fannie Mae customers and others, and caused monetary damages to involved financial institutions, including JPMorgan Chase and Bank of America. As part of this conspiracy, Minor and Morrison purchased PII that Thomas illegally obtained in the course of her employment at Fannie Mae. They then utilized other co-conspirators to misuse the PII to commit bank fraud.

This ongoing investigation is being worked jointly with the Secret Service Dallas Field Office and the Dallas County District Attorney's Office.

#### **Fraud at Failed FHLBank Member Bank, San Diego, California**

On October 8, 2013, Annand Sliuman pled guilty to bank bribery charges in the U.S. District Court for the Southern District of California. A few weeks later, on October 22, 2013, Laura Ortuondo was indicted by a grand jury in the same district for alleging false statement.

From late 2007 to early 2008, Sliuman loaned \$10,000 to a La Jolla Bank manager in an endeavor to corruptly increase a loan from La Jolla Bank to Sliuman's company by \$100,000. Sliuman then gave the same manager an additional \$15,000, and

forgave the previous \$10,000 loan, to try and increase a second loan from La Jolla Bank to a Sliuman company by approximately \$600,000.

During 2008, Ortuondo worked as Sliuman's assistant and allegedly helped prepare fraudulent tax lien releases to help Sliuman obtain the La Jolla Bank loans. Ortuondo then allegedly lied to investigators about preparing the lien releases and the destruction of a laptop that contained incriminating information.

La Jolla Bank was a member of the FHLBank of San Francisco until February 2010, when it failed and was taken over by the Federal Deposit Insurance Corporation (FDIC). At the time of failure, La Jolla Bank had outstanding debt of over \$1 billion, including approximately \$700 million in outstanding advances from the FHLBank of San Francisco.

This was a joint investigation with the FBI, Federal Deposit Insurance Corporation Office of Inspector General (FDIC-OIG), Small Business Administration Office of Inspector General, and Treasury Inspector General for Tax Administration.

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### *Minor and Morrison led a conspiracy that resulted in the theft of PII of over 1,000 Fannie Mae customers and others.*

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#### **Property Management and REO Schemes**

The wave of foreclosures following the housing crisis left the Enterprises holding a large inventory of **real estate owned (REO)** properties. To minimize losses associated with REO, the GSEs rely heavily on contractors to secure, maintain and repair, price, and ultimately sell their properties. In addition, they also count on realtors to sell the REO properties and thus have contracts with those realtors.



### **Fannie Mae Employee Receives Kickback in Exchange for Listings, Los Angeles, California**

On March 14, 2014, Armando Granillo was convicted of three counts of wire fraud and deprivation of honest services in the U.S. District Court for the Central District of California after a jury trial.

From November 2012 to March 2013, Granillo, a former foreclosure specialist/REO sales associate for Fannie Mae, attempted to enrich himself by soliciting payments of at least \$11,000 in exchange for favorable arrangements. Granillo then offered to increase the number of REO listings assigned to particular realtors in exchange for 20% of the real estate sales commission received at closing when the properties sold. After monitored meetings in which Granillo solicited and accepted \$11,200 in a kickback, he was arrested and found in possession of the funds.

### **Fannie Mae REO Realtor Defrauds Enterprises, Detroit, Michigan**

On October 1, 2013, in a court of the state of Michigan, Samer Salami pled nolo contendere to one count each of conducting a criminal enterprise, embezzlement, and computer crimes and two counts of false pretenses. On January 29, 2014, Salami was ordered to pay \$1 million in restitution, and on February 19, 2014, he was sentenced to 1 year in the Wayne County Jail and 5 years of probation.

From 2006 to 2010, Salami, an REO broker for the Enterprises, misrepresented the value of foreclosed properties he sold for the Enterprises. He sold them to companies his family and friends owned or controlled before flipping them to legitimate purchasers and keeping the illicit profit. He also collected an extra round of real estate commissions in this scheme. In addition, Salami falsely billed the

Enterprises for maintenance services not rendered and collected kickbacks from real estate brokers for steering properties to them. Enterprise losses in this scheme were \$989,400.

This was a joint investigation with the FBI and the Wayne County Prosecutor's Office.

### **Condo Conversion and Builder Bailout Schemes**

These schemes begin with sellers or developers seeking out investors with good credit who want low-risk investment opportunities. Investors are offered deals on properties with no money down and other lucrative incentives, such as cash back and guaranteed and immediate rent collection. To fund these incentives, the sellers use complicit appraisers to inflate the sales price. The incentives are not disclosed to lenders, who are defrauded into making loans far exceeding property values. When the properties go into foreclosure, lenders suffer large losses.

### **Builder Bailout Defendants Plead Guilty, Dallas, Texas**

On March 19, 2014, Anthony Jones was sentenced to 27 months of incarceration, 5 years of supervised release, forfeiture of \$152,795.83, and ordered to pay restitution of \$348,918.44. He had previously pled guilty to one count of bank fraud on October 23, 2013, in the U.S. District Court for the Eastern District of Texas. On February 18, 2014, Herbert Williams pled guilty to two counts of conspiracy to commit bank fraud and three counts of aggravated identity theft in the U.S. District Court for the Eastern District of Texas.

From on or about September 2007 through October 2007, Jones conspired with Williams to inflate the sales prices of two homes Jones sold and kicked back a portion of the proceeds to the buyers, who

were recruited by Williams. One of these homes was purchased by Jones using a stolen identity and sold to two separate buyers within a week of each other. The scheme caused a loss of approximately \$456,601.68 to the financial institutions involved. The loss included approximately \$272,300 of loss exposure to the Enterprises, which bought or secured mortgages on two of these transactions. Williams participated in a scheme without Jones on four other properties. The scheme caused a loss of approximately \$636,257.01 to involved financial institutions, which included approximately \$435,802.19 of loss exposure to the Enterprises.

This was a joint investigation with the Secret Service.

### **Seven Indicted in Condo Conversion Scheme, Miami, Florida**

On March 13, 2014, Luis Mendez, Luis Michael Mendez, Stavroula Mendez, Lazaro Mendez, Marie Mendez, Enrique Angulo, and Wilkie Perez were indicted in the U.S. District Court for the Southern District of Florida for bank and wire fraud and conspiracy to commit bank and wire fraud.

Between mid-2006 and December 2010, Luis Mendez and co-conspirators owned or controlled various real estate properties in the Miami area. They allegedly enlisted mortgage brokers and other individuals, including Perez and Angulo, to recruit **straw buyers** to act as qualifying mortgage applicants to fraudulently purchase condominiums at the various properties. The defendants prepared and caused to be prepared loan documents containing false statements and representations relating to the buyers' income, assets, and other information necessary to enable lenders to assess the buyers' qualifications to borrow money, which induced the lenders to make loans to finance the condominiums.

Luis Michael Mendez and Marie Mendez are alleged to have submitted their own fraudulent loan applications for two condominiums, and they, as well as Luis Mendez and Stavroula Mendez, advanced the buyers cash to close the transactions. After the loans were funded, the defendants allegedly caused fraudulent payments to be made from the loan proceeds to pay kickbacks through shell companies to the brokers, recruiters, and straw buyers, as well as to pay the mortgages to conceal the conspiracy. Eventually, the conspirators were unable to make mortgage payments, causing many of the condominium units to go into foreclosure and leading to losses by the lenders. In total, the scheme caused losses of over \$20 million, including loss exposure to Fannie Mae of approximately \$5,216,873.14 and loss exposure to Freddie Mac of approximately \$5,646,264.02.

This is a joint investigation with HUD-OIG.

### **Charges Filed in Builder Bailout Scheme, Houston, Texas**

On January 22, 2014, Theodoros Ezanidis, Christopher Hopper, and Robert Rendino, co-owners of Flatiron Development, were indicted in the U.S. District Court for the Southern District of Texas for conspiracy to commit wire fraud. On January 31, 2014, Susan Rendino was charged with making a false statement in the same district. On February 7, 2014, she pled guilty to the false statement charge.

In the scheme, Rendino purchased a home from homebuilder Flatiron Development. Flatiron and its corporate directors were selling homes to straw buyers at inflated prices. These homes quickly fell into foreclosure, causing losses to lending institutions of approximately \$5.7 million. The loss to Freddie Mac was \$590,989.64.

This is a joint investigation with the Secret Service.

### **Developer Sentenced to 42 Months, Dallas, Texas**

On December 16, 2013, Larry Reisman was sentenced to 42 months of imprisonment and ordered to pay restitution of \$1,500,000; he paid the full amount to the court on that day.

From January 2006 to October 2008, Reisman inflated the sales prices of 53 homes he built and then kicked back a portion of the proceeds to recruiters and buyers. The scheme caused a loss of approximately \$5.5 million to involved financial institutions, including losses of over \$500,000 to the Enterprises, which bought or secured mortgages on four of these homes.

This was a joint investigation with HUD-OIG, IRS-Criminal Investigation (IRS-CI), the FBI, the Secret Service, and USPIS.

### **Condo Conversion/Builder Bailout Scheme, Orlando, Florida**

On November 14, 2013, Avi Levy was charged with one count of conspiracy to commit wire fraud in the U.S. District Court for the Middle District of Florida. On December 4, 2013, Levy entered a plea of guilty before a U.S. Magistrate in the same district.

From March 2008 through January 2009, Levy and co-conspirators provided false information to financial institutions to obtain mortgage loans for buyers to purchase condominiums at inflated prices. The proceeds from the condominium sales were used to pay undisclosed incentives and bonuses to buyers, brokers, and other real estate professionals involved in the transaction. The undisclosed disbursements were not reflected on the HUD-1 form submitted to the financial institution. Levy was involved in

approximately 23 fraudulent loan transactions that caused a loss of roughly \$3,675,839 to involved institutions. The loss to Fannie Mae was estimated at \$199,000, and Freddie Mac's loss was \$1,362,684.

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***Developer pays \$1,500,000 in restitution and is sentenced to 42 months incarceration.***

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This was a joint investigation with the FBI and the Florida Office of Financial Regulation.

### **Defendant Sentenced to Over 16 Years in \$39 Million Florida Builder Bailout Fraud, Ft. Lauderdale, Florida**

On October 16, 2013, in the U.S. District Court for the Southern District of Florida, Quelyory Rignal was sentenced to 16 years and 8 months of incarceration and 3 years of supervised release.

Rignal and others participated in condo conversion schemes in the Florida cities of Ft. Lauderdale, Orlando, and Tampa. Of the 165 transactions involved in their schemes, 131 have been foreclosed and another 26 are in foreclosure. The targeted lenders have lost \$34 million of the \$39 million loaned. Freddie Mac's loss exposure is \$8.5 million.

### **Two Plead in Condo Conversion Scheme, West Palm Beach, Florida**

On October 7, 2013, Jose Aller and Ernesto Rodriguez pled guilty to conspiracy to commit bank fraud in the U.S. District Court for the Southern District of Florida. Aller and Rodriguez were co-owners of JAER Guaranteed Investments.

Between February and December 2008, Aller and Rodriguez conspired with others to provide condominium buyers at Kensington of Royal Palm Beach with incentives that were not disclosed on the HUD-1 forms. Financial institutions were unaware of the incentives and funded mortgage loans based

on materially false and fraudulent information. The mortgages were sold to Freddie Mac by the financial institutions. The scheme caused losses to Freddie Mac and Wells Fargo in the amount of \$2.78 million.

This ongoing investigation is being worked jointly with the FBI.

### **Adverse Possession Schemes**

Adverse possession schemes occur when individuals or entities illegally use adverse possession (also known as “home squatting”) or fraudulent documentation to control distressed homes, foreclosed homes, and REO properties.

#### **Title Fraud, Chicago, Illinois**

On January 17, 2014, Anatoly Moore was indicted in the State of Illinois Circuit Court of Cook County for one count of burglary and one count of theft by deception.

On May 3, 2013, Moore filed an apparently fraudulent affidavit/notice, affidavit of adverse

possession, notice of claim of title to real estate, mechanic’s lien, and notice of non-abandonment and secured interest of property with the Cook County Recorder of Deeds. This property was owned by Fannie Mae, and the recording of the documents on the property made the title “cloudy,” thus making it difficult for Fannie Mae to sell the property. The scheme caused an unknown exposure to Fannie Mae at the time, as Fannie Mae was in negotiations to sell the property until the title became unclear and the negotiations ceased.

This was a joint investigation with the Cook County State’s Attorney’s Office, Chicago Police Department, and FBI Chicago Field Office.

#### **Colorado Adverse Possession Scheme, Denver, Colorado**

On January 16, 2014, Alfonso Carrillo was found guilty on 18 of 24 counts in a Colorado State court, including racketeering, conspiracy to commit theft, criminal trespass, burglary, forgery, and attempts to



On February 3, 2014, in Denver, Colorado, OIG presented plaques to the Denver District Attorney’s Office investigators and attorneys for their outstanding contributions in the prosecution of Alfonso Carrillo and for their support of the OIG mission. From left to right: Criminal Investigator Brad Uyemura, Criminal Investigator (Retired) Dan Chun, Criminal Investigator Ruben Fragoso, OIG Acting Inspector General Michael P. Stephens, Deputy District Attorney Darryl Shockley, Deputy District Attorney Phillip Geige, Denver District Attorney Mitch Morrissey, and OIG Special Agent David Riordon.



influence public servants. Maria Carrillo (wife of Alfonso Carrillo) was found not guilty of all counts.

These charges stemmed from Carrillo's and other unindicted co-conspirators' illegal use of adverse possession of distressed homes, foreclosed homes, and REO in order to rent or sell the homes to unwitting victims. Many of these properties were owned by or had mortgages secured by the Enterprises. The total harm to the victims was approximately \$200,000.

This was a joint investigation with the Denver District Attorney's Office.

### **Home Squatting, Broward County, Florida**

On January 14, 2014, Wonsik Paul and Marlene Jean Baptiste were charged in the 17th Judicial Circuit Court of Florida with grand theft, filing of false documents, and identity theft.

Paul and Baptiste are Sovereign Citizens who are alleged to have been illegally residing in a Fannie Mae REO property since late 2012, after the filing of a fraudulent quit claim deed on the property in Broward County, Florida, on December 20, 2012. Paul has appeared before a Broward County Foreclosure Magistrate Judge in support of being able to remain in the property. The unpaid principal balance on the property is \$223,771. The loss to Fannie Mae is undetermined at this time.

This is a joint investigation with the Broward Sheriff's Office Economic Crimes Unit.

### **Two Charged in Adverse Possession/Rent to Own Scheme, Martin County, Florida**

On January 2, 2014, Robert Allen Tribble and Mary Revoller-Chavez were charged via complaint in the 19th Judicial Circuit Court of Florida with operating an organized scheme to defraud, criminal use of personal identification, and money laundering.

Tribble and Revoller-Chavez are alleged to have engaged in a conspiracy to commit deed fraud on properties owned by the Enterprises. The conspiracy involved the filing of fraudulent quit claim deeds on properties and then targeting victims who believed that they were purchasing the properties via a rent-to-own agreement. Tribble and Revoller-Chavez never legally owned the properties and allegedly misappropriated the money paid to them by victims. The scheme targeted at least 11 Enterprise-owned properties with unpaid principal balances of \$2.47 million. Losses are undetermined at this time.

This is a joint investigation with the Florida Department of Law Enforcement.

### **Adverse Possession Scheme, Broward County, Florida**

On December 12, 2013, Louis Lewis was charged via complaint in the 17th Judicial Circuit Court of Florida with grand theft, filing of false documents, and identity theft.

Lewis is alleged to have submitted fraudulent special warranty and quit claim deeds on numerous properties throughout the state of Florida utilizing different fraudulent "trusts." Lewis allegedly filed the false deeds with the local county register's office and then attempted to locate a buyer and sell the property in an all-cash deal within a very short turnaround time. This process was all completed in a manner to circumvent the property recording system and have the property "sold" in an all-cash transaction, before it was discovered to have been filed under a fraudulent deed. The scheme targeted at least three Fannie Mae properties with unpaid principal balances of \$664,250; the loss is undetermined at this time.

This is a joint investigation with the Florida Department of Law Enforcement, St. Lucie County Sheriff's Office, Martin County Sheriff's

Office, Broward Sheriff's Office, Florida Statewide Prosecutor's Office (State Attorney General), and Broward County State Attorney's Office Economic Crime Unit.

## **Loan Origination Schemes**

Loan or mortgage origination schemes are the most common type of mortgage fraud. These schemes typically involve misrepresentations of buyers' income, assets, employment, and credit profile to make them more attractive to lenders. Bogus Social Security numbers and fake or altered documents such as W-2 forms and bank statements are often used. These schemes are designed to defraud lenders into making loans they would not otherwise make. Perpetrators pocket origination fees or inflate home prices and divert proceeds.

### **Four Guilty Pleas in Loan Origination Scheme, Eastern District, Texas**

Lawrence Day, Michael Edwards, Scott Sherman, and Donald Mattox all pled guilty to conspiracy to commit mail and wire fraud affecting a financial institution in the U.S. District Court for the Eastern District of Texas on March 25, 2014; October 22, 2013; February 11, 2014; and October 3, 2013, respectively.

From September 2005 through July 2008, the above subjects conspired to defraud lending institutions by inducing them to fund mortgage loans by using material misrepresentations and omissions of fact on the HUD-1 forms, loan applications, and other loan documents. There were approximately 28 properties involved in this investigation. The HUD-1 forms reflected false purchase prices, disbursements, and falsely indicated the buyers had provided the down payment funds. With the assistance of loan officer Michael Edwards, false information was submitted on loan applications, including the buyers' employment, income, assets, rental property information, and

occupancy information. The estimated loss to Fannie Mae is \$967,989.43, and the estimated loss to Freddie Mac is \$130,265.

This was a joint investigation with the FBI.

### **Loan Officer Indicted, St. Louis, Missouri**

On March 19, 2014, Robert Poynter was indicted in the U.S. District Court for the Eastern District of Missouri on one count of wire fraud and one count of making false statements.

Poynter is a former mortgage broker who operated the net branch office of First Continental Mortgage and also owned America One Finance and A-1 Closing Services. In February 2010, Poynter allegedly diverted \$38,000 in loan proceeds to be used as a down payment by the borrower for the same transaction. The loan was funded by Freddie Mac, and unbeknownst to Freddie Mac and the lender, Freddie Mac had already foreclosed on the property and held the mortgage. Poynter also allegedly made false statements on a **Federal Housing Administration (FHA)** loan by arranging for false employment and income documents to be used. The alleged fraudulent activity caused losses of approximately \$300,000.

This was a joint investigation with HUD-OIG.

### **Appraiser Convicted, Chicago, Illinois**

On March 17, 2014, Olabode Rotibi pled guilty to wire fraud in the U.S. District Court for the Northern District of Illinois.

From 2007 to 2008, Rotibi was a licensed appraiser who produced fraudulent appraisal reports as part of a mortgage fraud scheme to sell condominium units at 1351 N. Ashland Ave., Chicago, Illinois. The individuals who participated in the scheme made misrepresentations in loan applications of straw buyers, leading lenders to approve loans they

would not normally approve. The scheme caused loss exposure of over \$1 million to the GSEs, with no actual loss at this time. Other properties were involved in the investigation, with higher exposure and potential loss to the GSEs.

This is a joint investigation with the U.S. Attorney's Office, the Northern District of Illinois, and the FBI Chicago Field Office.

### **Numerous Indictments and Pleas in \$3.5 Million Loan Origination Fraud, Baltimore, Maryland**

The defendants listed below allegedly participated in schemes to fraudulently obtain residential mortgage loans for properties in Maryland. They allegedly diverted \$3.5 million in funds, which resulted in losses of over \$1 million to lenders, FHA, Fannie Mae, and Freddie Mac.

- On March 6, 2014, Flavia Makundi pled guilty in the U.S. District Court for the District of Maryland to conspiracy to commit wire fraud.
- On February 24, 2014, Larry Johnson was sentenced to 8 months of imprisonment, 3 years of supervised release, and ordered to pay \$352,091 in restitution.
- On February 12, 2014, Mokorya Wambura pled guilty to aggravated identity theft and conspiracy to commit wire fraud.
- On January 27, 2014, Abdallah Kitwara, Raymond Abraham, Annika Boas, Cane Mwiwaha, Carmen Johnson, Makundi, and Ayoub Luziga were all indicted in the U.S. District Court for the District of Maryland on charges of conspiracy to commit wire fraud, wire fraud, and aiding and abetting.
- On December 30, 2013, Edgar Tibakweitira pled guilty in the U.S. District Court for the District of Maryland to aggravated identity theft and

conspiracy to commit wire fraud. On the same day, Johnson also pled guilty to one count of making false statements to a bank.

- On December 18, 2013, Peter Ligate and Mwiwaha were indicted in the U.S. District Court for the District of Maryland for conspiracy to commit wire fraud, wire fraud, and aiding and abetting.
- On October 21, 2013, Mrisho Mseze and Wambura were indicted in the U.S. District Court for the District of Maryland for wire fraud, conspiracy to commit wire fraud, mail fraud, and aggravated identity theft.

This was a joint investigation with HUD-OIG, the Secret Service, IRS-CI, the Department of the Treasury Office of the Inspector General, and Immigration and Customs Enforcement-Homeland Security Investigations.

### **Plea in \$2 Million Loan Origination Fraud Scheme, Newark, New Jersey**

On February 4, 2014, Klary Arcentales pled guilty in the U.S. District Court for the District of New Jersey to conspiracy to commit bank fraud and four counts of bank fraud.

From March 2007 until September 2012, Arcentales, a loan officer at Premier Mortgage Services, conspired with others to defraud numerous mortgage lenders of over \$2 million by utilizing straw buyers and causing fraudulent loan applications containing false misrepresentations of inflated assets, employment and rental incomes, and fraudulent HUD-1 forms to be submitted to financial institutions. Arcentales profited illegally in this loan origination fraud scheme by receiving a commission from Premier Mortgage Services for each mortgage loan she closed, and by diverting portions of the fraudulently obtained mortgage proceeds for herself. The Enterprises

purchased over \$1,150,000 in loans associated with this investigation.

This was a joint investigation with the FBI and IRS.

### **Defendants Sentenced in Fraud Involving Inflated Loans and Kickbacks, Dallas, Texas**

On January 22, 2014, Christi Wyatt was sentenced to 37 months of imprisonment and 3 years of supervised release for her earlier plea to one count of conspiracy to commit mail fraud. She was also ordered to pay restitution in the amount of \$1,032,650. On February 6, 2014, Ronzell Mitchell was sentenced to 46 months of imprisonment, 3 years of supervised release, and ordered to pay \$1,408,402.96 in restitution. On February 26, 2014, Lacie Devine pled to one count of conspiracy to commit mail fraud. All dispositions occurred in the U.S. District Court for the Eastern District of Texas.

From about March 2008 through February 2010, Devine conspired with others to recruit buyers to purchase properties from sellers at inflated sales prices, to help the buyers obtain mortgage loans based on these inflated sales prices, to cause the sellers to kickback portions of the loan proceeds, to pay portions of the loan proceeds to the buyers, and to cause the escrow officer not to disclose these payments to the lender. Devine was involved with fraudulent transactions on 28 homes, Wyatt was involved with fraudulent transactions on 8 homes, and Mitchell was involved with fraudulent transactions on 7 other homes. The scheme caused a loss of approximately \$3,718,702 to involved financial institutions, which included losses of approximately \$1,555,484 to Fannie Mae and \$239,989 to Freddie Mac.

The case resulted from a joint investigation with the FBI, HUD-OIG, and the Texas Department of Insurance Fraud Unit.

### **Plea in Loan Origination Fraud, Sacramento, California**

On January 17, 2014, Shing Yuan Yang (also known as Jack Yang) pled guilty to one count of conspiracy to commit wire fraud in the U.S. District Court for the Central District of California.

Starting in late 2006 and continuing until early 2007, co-conspirator SH, whom Yang knew from previous business dealings, approached Yang and asked if SH could use Yang's company, Red Gate Enterprises, for false verification of employment for home buyers applying for home loans. Yang agreed and subsequently forwarded all lender employment verification calls to SH's cell phone number. Using Red Gate Enterprises, SH was able to have two additional co-conspirators act as straw buyers and obtain loans on eight properties. The plea details one of the straw buyers and four properties purchased by the straw buyer. The loss to the lenders on the four properties is approximately \$1.24 million. One of the eight loans was purchased by Freddie Mac, which suffered a loss of approximately \$245,000.

### **Former Loan Officer Falsifies Loan Documents, St. Louis, Missouri**

On December 23, 2013, Michael Wallis, a former loan officer, pled guilty to one count of conspiracy to commit bank fraud and one count of making false statements in the U.S. District Court for the Eastern District of Missouri.

Wallis admitted in his plea that from early 2007 through January 2010, he conspired to cause false statements to be submitted to FHA, Fannie Mae, and FDIC-insured banks. Specifically, Wallis admitted to causing the submission of false gift letters and false invoices that disguised the nature of the down payment and the destination of the proceeds. Wallis conspired with two others who worked in the St. Louis real estate market. Wallis' activity caused



losses of approximately \$800,000 to the United States and financial institutions. The scheme involved over 14 Enterprise loans and 21 FHA loans.

This was a joint investigation with HUD-OIG and USPIS.

### **Two Sentenced in \$5 Million Loan Origination Fraud, Newark, New Jersey**

On December 20, 2013, in the U.S. District Court for the District of New Jersey, Christopher Woods and Matthew Amento were each sentenced to 18 months of incarceration, 3 years of supervised release, and ordered to pay \$1,267,851.51 in restitution jointly and severally.

The pair previously pled guilty to committing wire fraud and conspiracy to commit wire fraud.

From March 2008 to February 2010, Woods, owner of Champs Construction; Amento, owner of Residential Real Estate Construction; and other individuals conspired to defraud numerous mortgage lenders of over \$5 million in a loan origination and property flipping scheme. They used fraudulent loan applications and HUD-1 forms containing misrepresentations, including borrowers having cash down payments, inflated assets and incomes, and nonexistent liens listed on the HUD-1 forms. Three fraudulent mortgages were sold to the Enterprises for \$1,519,000. The Enterprises required all three lenders to make them whole. Defaults on mortgages associated with this investigation caused a loss of \$1,267,851.51 to various financial institutions.

This was a joint investigation with HUD-OIG, USPIS, the FBI, and SIGTARP.

### **A \$100 Million Nationwide Loan Origination Fraud, San Diego, California**

On December 2, 2013, Audrey Yeboah was sentenced to 3 years of probation, 15 months of home confinement, and ordered to pay a \$2,500 fine. On December 9, 2013, Justin Mensen was sentenced to 5 years of probation. On January 3, 2014, Teresa Rose was sentenced to 15 months of incarceration and 36 months of supervised release. Mensen and Rose, along with another co-defendant, are also jointly and severally liable for restitution in the amount of \$532,687. The pleas occurred in the U.S. District Court for the Southern District of California.

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***Realtor sentenced to 15 months incarceration and ordered to pay over \$500,000 in restitution.***

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Rose (a realtor), Yeboah, and Mensen (a loan broker) participated in a nationwide loan origination fraud and kickback scheme, defrauding lenders through the sale of \$100 million of real estate at inflated prices. Purchasers of the fraudulently originated loans, including the Enterprises, suffered losses of up to \$20 million.

This was a joint investigation with the FBI.

### **Mortgage Company Employees Sentenced for Loan Origination Fraud, Allentown, Pennsylvania**

On November 21, 2013, Angela Diaz was sentenced to 5 years of probation, 60 hours of community service, and ordered to pay \$227,000 in restitution. On December 18, 2013, Ghovanna Gonzalez was sentenced to 7 days of incarceration, 3 years of probation, and ordered to pay \$762,616.20 in restitution. Both were employed as loan processors at Madison Funding. On December 20, 2013, bank representative Princess Rosario and realtors Jose Antigua and Melquisedec Caraballo were

charged with conspiracy. On January 15, 2014, Caraballo pled guilty to one count of conspiracy. On January 24, 2014, Rosario pled guilty to one count of conspiracy. On January 31, 2014, Antigua pled guilty to one count of conspiracy, and Jason Boggs, a branch manager at Madison Funding, was sentenced to 16 months of incarceration, 3 years of probation, and ordered to pay \$383,384.21 in restitution, of which \$20,368.13 will go to Fannie Mae and \$97,380.52 to Freddie Mac. On March 27, 2014, Florentina Peralta was sentenced to 3 months of incarceration, 12 months of supervised release, and ordered to pay \$586,705.95 in restitution, of which \$251,455.95 will be paid to Fannie Mae. All dispositions were in the U.S. District Court for the Eastern District of Pennsylvania.

From October 2006 until at least June 2008, numerous individuals conspired to defraud mortgage lenders by submitting loan applications supported by falsified, forged, and altered documents. Over 60 loans originated during the fraud scheme were sold to the Enterprises. Defaults on these mortgages caused losses of over \$1 million to the Enterprises.

This was a joint investigation with HUD-OIG and FDIC-OIG.

#### **Defendant Charged and Sentenced in \$1 Million Bank Fraud Conspiracy, Dallas, Texas**

On November 13, 2013, Marcus Carr was indicted for conspiracy to commit bank fraud in the U.S. District Court for the Eastern District of Texas.

On February 6, 2014, Michael Burnham was sentenced to 4 years and 3 months of imprisonment, 5 years of supervised release, and restitution in the amount of \$1,393,129.91.

On February 13, 2014, Carr pled guilty to conspiracy to commit bank fraud in the U.S. District Court for the Eastern District of Texas.

From July 2008 through August 2010, Burnham and Carr conspired with others, including the seller of a property, to sell the property at an inflated price to straw buyers. Burnham and Carr supplied straw buyers with down payment funds needed to close the transactions. The seller received his proceeds after the closing on the property and kicked back a portion of the proceeds to Burnham outside of closing. Burnham then paid a portion of the funds to Carr outside of closing. Burnham and Carr were involved in similar fraudulent transactions on seven other homes. The scheme caused a loss of \$1,393,129.91 to involved financial institutions, including losses of approximately \$1,125,907.69 to the Enterprises, which bought or secured mortgages on six of these properties.

This indictment resulted from a joint investigation with HUD-OIG.

#### **Suspended Real Estate Agent Pleads Guilty and Six Co-conspirators Sentenced, Kansas City, Kansas**

On November 5, 2013, in the U.S. District Court for the District of Kansas, Manjur Alam, a suspended real estate agent, pled guilty to conspiracy to commit wire and bank fraud. On November 25, 2013, in the same court, his co-conspirators were sentenced to time served, 2 years of supervised release, and ordered to pay restitution as follows:

- Henry Pearson Sr., \$55,180;
- Chris Ginyard, \$40,000;
- Henry Pearson Jr., \$50,000;
- Allen Dykes, \$14,872; and
- Steven Pelz, \$31,924.

On March 5, 2014, Janice Young was sentenced in the same court to time served, 5 years of supervised release, and ordered to pay \$60,332 in restitution.

From 2006 to present, Alam's co-conspirators agreed to be straw buyers in a scheme in which false employment, income, and other documents would be used to qualify them for residential mortgage loans. The listed individuals pled guilty to knowingly submitting false loan applications and various other false documents in order to qualify for conventional mortgage loans, including loans purchased by Fannie Mae (nine) and Freddie Mac (two), as well as loans insured by FHA. Losses to financial institutions related to this scheme exceeded \$795,000.

This was a joint investigation with IRS-CI and HUD-OIG.

**Realtor Pleads Guilty in \$7 Million Loan Origination Fraud, Sacramento, California**

On October 21, 2013, James Lee Lankford pled guilty to seven counts of mail fraud. On January 27, 2014, Lankford was sentenced to 10 years and 1 month in prison, 36 months of supervised release, and ordered to pay \$986,826 in restitution. Also on January 27, 2014, Jon McDade was sentenced to 5 years of supervised release and ordered to pay \$1,443,826 in restitution after his conviction for bank fraud. All proceedings took place in the U.S. District Court for the Eastern District of California.

In his plea, Lankford admitted that, while working as a realtor and broker, he fraudulently induced elderly property owners to sell their homes to him and provide seller-backed financing. Unbeknownst to the elderly sellers, Lankford would also obtain mortgages from lending institutions by making material misstatements on the loan applications. Lankford caused an estimated loss to lending

institutions of more than \$7 million. In his plea, McDade admitted to knowingly submitting a loan application containing materially false and fraudulent information, including inflated income. As a result of the false statements, a loan was funded for \$880,000. One property in this case was sold to Fannie Mae, which lost approximately \$185,000 on the transaction.

This was a joint investigation with the FBI and the Stanislaus County District Attorney's Office.

**Loan Officer Indicted for Money Laundering, Dallas, Texas**

On October 9, 2013, loan officer Euneisha Hearn was indicted for conspiracy to commit money laundering in the U.S. District Court for the Eastern District of Texas.

During April 2008, Hearn and others allegedly conspired to launder proceeds from fraudulent real estate transactions. The fraudulent real estate transactions scheme caused a loss of \$865,940 to involved financial institutions, including the Enterprises, which purchased mortgages that funded the fraudulent transactions.

This was a joint investigation with IRS-CI.

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*Real estate broker sentenced to 10 years incarceration and ordered to pay nearly \$1,000,000 in restitution.*

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**Real Estate Agent and Loan Officer Indicted for Money Laundering, Dallas, Texas**

On October 9, 2013, Hoa Lee Perkins and Brigette Ellis were indicted in the U.S. District Court for the Eastern District of Texas for conspiracy to commit money laundering.

From December 2006 through November 2008, Perkins, a real estate agent; Ellis, a loan officer; and

others were involved in an illegal property flipping scheme. Perkins would purchase homes in north Texas cities in her name or in her associate's parents' names at market value. The homes were then flipped using straw buyers with bogus appraisals reflecting much higher values. False notarized loan documents were submitted to lenders, and Perkins paid the down payment, which was not disclosed on HUD-1 forms. The loan proceeds were paid to Perkins through an entity she controlled, Manda Homes LLC. Perkins and her co-conspirators flipped 26 properties, resulting in fraudulent loans totaling over \$8 million. All of the properties were foreclosed or sold by short sale. The scheme caused a loss of approximately \$2,041,439 to Fannie Mae and \$4,308,000 to Freddie Mac.

This indictment resulted from a joint investigation with the FBI and IRS-CI.

### **Short Sale Schemes**

Short sales occur when a lender allows a borrower who is “**underwater**” on his/her loan—that is, the borrower owes more than the property is worth—to sell his/her property for less than the debt owed. Short sale fraud usually involves a borrower intentionally misrepresenting or not disclosing material facts to induce a lender to agree to a short sale to which they would not otherwise agree.

### **Attorneys Sentenced in Short Sale Fraud, New Haven, Connecticut**

On March 20, 2014, attorney Lawrence Dressler was sentenced to 20 months of incarceration, 3 years of supervised release, ordered to pay \$403,450.75 in restitution, and ordered to forfeit \$5,100. On October 3, 2013, in the U.S. District Court for

the District of Connecticut, Dressler pled guilty to conspiracy to commit mail, wire, and bank fraud. On November 19, 2013, in the same court, attorney Genevieve Salvatore pled guilty to mail fraud. On March 11, 2014, Salvatore was sentenced to 24 months of incarceration, 3 years of supervised release, and ordered to forfeit \$19,000.

From December 2006 to February 2008, Dressler, Salvatore, and others conspired to defraud mortgage lenders and financial institutions by obtaining over \$10 million in fraudulent mortgages for the purchase of 20 multifamily properties in New Haven, Connecticut. The Enterprises purchased or secured mortgages for multiple homes.

This was a joint investigation with the FBI, USPIS, and HUD-OIG.

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***Attorney sentenced to 20 months incarceration and ordered to pay more than \$400,000 in restitution.***

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### **Realtor Assists Homeowner in Committing Short Sale Fraud, Sacramento, California**

On December 19, 2013, in the U.S. District Court for the Eastern District of California, Minerva Sanchez was indicted for one count of conspiracy to commit bank fraud.

In March 2010, Sanchez, a licensed real estate agent, represented Agustin Simon in the sale of his

home in Patterson, California; Simon also pled guilty to conspiracy to commit bank fraud in June 2013. Sanchez allegedly recommended that Simon undertake a short sale of his home using her son as a straw buyer. Simon submitted to Tri Counties Bank and Freddie Mac alleged fraudulent short sale applications that caused them to approve the charge off of funds for the sale of his home. Sanchez allegedly claimed falsely that the transaction was “arm’s length” and allegedly assisted Simon in making false statements about Simon’s assets and ownership



of other real estate. Sanchez wrote a “hardship letter” for Simon to include with the short sale application that misrepresented his inability to make monthly mortgage payments. As a result of her conduct, Tri Counties Bank suffered a loss of \$247,000, and Freddie Mac lost \$107,348.

This was a joint investigation with the FBI, IRS-CI, and the Stanislaus County District Attorney’s Office.

### **Las Vegas Realtors Use Straw Buyer to Commit Short Sale Fraud, Las Vegas, Nevada**

On November 26, 2013, Robert and Cynthia Hosbrook pled guilty to bank fraud in the U.S. District Court for the District of Nevada.

On June 7, 2010, a short sale was approved for the Hosbrooks’ personal residence based on fraudulent representations that the short sale was due to personal hardships, the transaction was arm’s length, the sellers and buyers were not family members, and the seller would not remain in the property subsequent to the sale. In contrast, the Hosbrooks, real estate professionals, made a cash sale of their personal residence to a relative acting as a straw buyer and remained in their home after the sale. Freddie Mac suffered a loss of \$174,000 as a consequence of the short sale.

This was a joint investigation with the Nevada Attorney General’s Office.

### **Nine Charged in Short Sale Fraud, Denver, Colorado**

On November 7, 2013, Wendy Thomas, Christina Nicole Smith, Kurt Smith, Sheila Gaston, Sheila Giberti, Duane Thomas, Christopher Consol, Janice Gardner, and Joseph Slowey were indicted by a grand jury sitting in the state of Colorado for the Denver District Court on charges of theft, forgery, and violations of the Colorado Organized Crime Control Act.

From 2008 to 2013, Wendy Thomas, operator of Home Support Solutions, and her co-conspirators are alleged to have devised a scheme to acquire control of distressed properties and negotiate with the respective mortgage servicers using fraudulent documents to acquire the properties at less than full market value. The defendants then allegedly flipped the properties for profit through the use of straw buyers. Some properties were held in the Enterprises’ portfolios, while others were insured by FHA. Overall, 18 properties flipped by the defendants were held in the Enterprises’ portfolios. The alleged fraud resulted in over \$500,000 in losses on the properties, including over \$100,000 in theft of commissions for the fraudulent short sales.

This was a joint investigation with the Colorado State Attorney General’s Office, the Colorado Bureau of Investigation, and HUD-OIG.

### **Escrow Diversion Schemes**

An escrow diversion scheme relates to individuals, usually in positions of trust such as real estate attorneys or title agents, diverting funds from restrictive escrow accounts for their own benefit rather than using the restricted funds for their intended purposes, such as to pay property taxes.

### **Guilty Plea and Sentences in Multimillion Dollar Diversion, Denver, Colorado**

On November 4, 2013, Benjamin Velasquez pled guilty to forgery in the City and County of Denver District Court and was sentenced to 18 months of probation. On January 10, 2014, Michael Martinez was sentenced to 5 years of incarceration and 5 years of probation (concurrent) in the same court.

From 2010 to 2011, Martinez and a co-conspirator participated in a scheme to divert funds designated for specific real estate transactions. The scheme resulted in over \$2 million in losses by Quantum Title. Velasquez committed loan origination fraud

on three Enterprise-owned properties by acting as a straw buyer and providing false employment, income, and residency documents to lenders. As a result, the Enterprises lost \$201,000 collectively.

This was a joint investigation with the Colorado State Attorney General's Office.

### **Mortgage Company Owner Sentenced for Diverting Over \$18 Million Owed to Enterprises, Ft. Lauderdale, Florida**

On October 17, 2013, in the U.S. District Court for the Southern District of Florida, Patrick Mansell was sentenced to 5 years of imprisonment to be followed by 3 years of supervised release.

Starting in April 2007, Mansell used his position as vice president, secretary, and director of Coastal States Mortgage Corporation to defraud the Enterprises. Through February 2012, Coastal States withheld mortgage loan payoffs owed to the Enterprises for extended periods. Coastal States used these funds for their own business purposes and to make monthly mortgage payments on paid-off loans, misrepresenting them as performing loans. Payoffs fraudulently retained by Coastal States were also used to remit funds owed to the Enterprises for previously withheld payoffs. Daily and monthly servicing reports were supplied to the Enterprises containing false information and altered loan-identifying numbers, which enabled the scheme to go undetected. The Enterprises lost more than \$18 million as a result.

The Florida Office of Financial Regulation provided assistance to OIG during the initial stages of the investigation.

### **Loan Modification and Property Disposition Schemes**

Many companies claim to be able to secure loan modifications for desperate homeowners. Some even claim affiliation with the government. Unfortunately, the offers usually come with upfront fees and little action, leaving homeowners even worse off. Additionally, various fraud schemes can impact sales of Enterprise REO.

### **Four Arrested in Mortgage Rescue/Bankruptcy Scheme, Van Nuys, California**

On March 25, 2014, Efren Velasquez, Eugene Fulmer, Panik Karikorian, and Shara Surabi (also known as Sean Parsi) were arrested for their roles in a mortgage rescue scheme. Arrest warrants had been issued on March 19, 2014, for the four and an additional fifth co-conspirator, Juan Velasquez.

Efren Velasquez, Juan Velasquez, Karikorian, and Surabi are each charged with 1 count of conspiracy and 25 counts of forgery, while Fulmer is charged with 1 count of conspiracy and 2 counts of forgery. The individuals worked for and operated Trustee Sale Stoppers, Property Assistance, Asset Help, and additional businesses out of Los Angeles. The complaint alleges that from early 2011 to present, the co-conspirators collected more than \$2 million in proceeds from their foreclosure-delay and eviction-delay scheme, which involved hundreds of fraudulent **bankruptcies** and deeds of trust. Fulmer, Karikorian, and Surabi allegedly contacted homeowners who were in foreclosure and facing a trustee's sale and promised that they would delay the trustee's sale for up to 36 months for an initial payment ranging from \$750 to over \$1,000 and a fee of \$750 per month thereafter.

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*Vice president of mortgage company sentenced to 5 years incarceration.*

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The same three also allegedly caused a series of fraudulent bankruptcies to be filed in order to delay the trustee's sales, in addition to filing backdated short-form deed of trust and assignment of rent documents against the clients' homes; Efren and Juan Velasquez were listed as beneficiaries on these documents.

The overall exposure to financial institutions is approximately \$4.4 million. At least 11 of the properties involved were owned by Freddie Mac, resulting in a loss of \$817,955.

This is a joint investigation with the Alameda County District Attorney's Office and the FBI.

### **Two Defendants Sentenced in Mortgage Rescue Scheme, San Bernardino, California**

On March 18, 2014, in the Stanislaus County Superior Court, Blas Arreola pled nolo contendere to one count of offering false/forged instruments for filing and was sentenced to 1 year of imprisonment, 5 years of probation, and a fine of \$300. On the same date in the same jurisdiction, Nancy Arreola pled nolo contendere to one count of identity theft and was sentenced to 60 days of imprisonment, 3 years of probation, and a fine of \$150.

Personnel at Document Recovery Forensic, LLC, assisted the Arreolas with the preparation of numerous fraudulent documents to include several fractional interest grant deeds to unknown individuals who were in bankruptcy, a scheme referred to as "bankruptcy dumping." The bankruptcy dumping allowed the Arreolas to keep possession of their homes, while not paying their mortgages. The Arreolas paid Document Recovery Forensic at least \$6,000 in fees and continued filing fraudulent documents despite being warned by local law enforcement of their illegality. The scheme resulted in a loss to Freddie Mac of \$125,738. The investigation of Document Recovery Forensic is continuing.

This is a joint investigation with the Stanislaus County District Attorney's Office and the California Attorney General's Office.

### **Defendants Sentenced in \$1.3 Million Mortgage Rescue Scheme, Los Angeles, California**

On November 5, 2013, Stephen Benjamin (also known as Steven Benjamin) was sentenced in the U.S. District Court for the Central District of California to 3 years of probation and 40 hours of community service.

On February 24, 2014, Jeremy Lloyd was sentenced in the U.S. District Court for the Central District of California to 6 months of home confinement, 5 years of probation, 100 hours of community service, and a \$4,000 fine.

From July 2011 through August 2012, Benjamin, Lloyd, and others conspired to commit bankruptcy fraud and operated businesses that falsely purported to provide assistance to homeowners seeking to delay or avoid foreclosure and/or eviction proceedings. They would advise homeowners that, for a fee, they could assist the clients in delaying such proceedings. After receiving fees from clients, Benjamin and others would cause false documents to be prepared in order to make it appear as if a tenant resided at the property owned by the client/homeowner. Benjamin would also cause false bankruptcy petitions to be prepared, signed, and filed in the names of the fictitious tenants with the bankruptcy court. In total, Benjamin and others collected over \$1.3 million in upfront fees and targeted approximately 250 homeowners, including homeowners whose mortgages were owned by Fannie Mae.

This is a joint investigation with the FBI and the U.S. Attorney's Office for the Central District of California.

## Civil Cases

During the reporting period, OIG continued to actively participate in the RMBS Working Group, which was established by the President in 2012 to investigate those responsible for misconduct contributing to the financial crisis through the pooling and sale of RMBS. The Working Group is a collaborative effort of dozens of federal and state law enforcement agencies.

OIG's participation has included acting as a source of information about the secondary finance market, providing strategic litigation advice, supporting witness interviews, and obtaining and reviewing documents and other evidence. To date, OIG has played a significant role in investigations undertaken by members of the Working Group. The following investigations have resulted in civil settlements:

- The Working Group closed its first investigation in the fourth quarter of 2013 when JPMorgan Chase agreed to pay a total of \$13 billion in order to settle charges of fraud in the RMBS markets brought by the U.S. Attorneys for the Eastern District of California and the Eastern District of Pennsylvania, the Civil Division of DOJ, FHFA, the New York Attorney General, and others;
- The New York Attorney General also instituted a civil proceeding against Credit Suisse alleging fraud in connection with the sale of RMBS; and
- The U.S. Attorney for the Western District of North Carolina instituted a civil proceeding against Bank of America alleging violations of

the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA).

In October 2013, a federal jury in New York found Bank of America, Countrywide, and one of Countrywide's former executives liable in a civil proceeding brought under FIRREA alleging that the defendants had engaged in a scheme to defraud the Enterprises in connection with the sales of mortgage loans. OIG agents and attorneys supported the U.S. Attorney for the Southern District of New York in investigating the case.

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*JPMorgan Chase  
agreed to pay a  
total of \$13 billion  
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charges of fraud  
in the RMBS  
markets.*

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## Investigations Strategy

OIG has developed and intends to further develop close working relationships with other law enforcement agencies, including DOJ and the U.S. Attorneys' Offices; state attorneys general; mortgage fraud working groups; the Secret Service; the FBI; HUD-OIG; the FDIC-OIG; the IRS-CI division; SIGTARP; the Financial Crimes Enforcement Network; and other federal, state, and local agencies.

During this reporting period, OI provided 47 fraud awareness briefings to various audiences.

## Regulatory Activities

Consistent with the Inspector General Act, OIG assesses whether proposed legislation, regulations, and policies related to FHFA are efficient, economical, legal, and susceptible to fraud and abuse. During the semiannual period, OIG advised FHFA that it had not implemented the government-wide suspension



and debarment system and the Program Fraud Civil Remedies Act of 1986 (PFCRA), and made substantive comments on a proposed rule and three advisory bulletins. Additionally, FHFA published a final rule that OIG had previously commented upon.<sup>3</sup>

### **1. Implementation of the Government-wide Suspension and Debarment System and PFCRA**

The government-wide suspension and debarment system was established in 1986 by Executive Order 12549. Section 1 of the Executive Order requires agencies to participate in the nonprocurement suspension and debarment system, and section 3 provides that executive agencies “shall issue regulations governing their implementation” of it.<sup>4</sup> The regulations were to be issued no later than 12 months after OMB issued appropriate guidance to the agencies.<sup>5</sup> OMB issued such guidance in 1987.<sup>6</sup> Thus, the requirement that agencies issue suspension and debarment regulations has been fully effective since at least 1988. Further, the Federal Acquisition Regulation (FAR) specifically directs agencies to “establish appropriate procedures to implement” FAR’s policies and procedures on procurement-related suspensions and debarments.<sup>7</sup>

PFCRA provides agencies with an administrative remedy for low-dollar frauds (i.e., \$150,000 or less) involving false claims and statements.<sup>8</sup> PFCRA permits agencies to recover up to twice the amount of the loss (i.e., potentially up to \$300,000), plus a penalty per false claim or statement. Section 3809 of Title 31 of the U.S. Code requires agencies to “promulgate rules and regulations necessary to implement” PFCRA within 180 days from the statute’s enactment in 1986.

The applicability of Executive Order 12549 and PFCRA do not hinge upon an agency’s size,

whether it distributes funds, or whether it is funded with taxpayer dollars. FHFA is an executive agency, and therefore, it is subject to the Executive Order and PFCRA. Yet, it has not implemented either provision.

OIG apprised FHFA of its responsibility to implement the government-wide suspension and debarment system and PFCRA, and requested that the Agency advise what it intends to do to remedy these deficiencies.

On April 2, 2014, FHFA advised OIG that it would implement PFCRA but would not implement the government-wide suspension and debarment system. In the latter regard, FHFA explained that as a non-appropriated agency it is not required to comply with FAR and that it does not make grants, cooperative agreements, loans, loan guarantees, or subsidies that invoke the application of the Executive Order.

### **2. Enforceability of Advisory Bulletins: Liquidity Risk Management (AB 2014-01), Operational Risk Management (AB 2014-02), and Collateralization of Advances and Other Credit Products to Insurance Company Members (AB 2013-09)**

FHFA forwarded to OIG draft advisory bulletins concerning liquidity and **operational risk** management and collateralization of advances and other credit products to **insurance companies**, and requested OIG’s comments on them. OIG responded that it is concerned that the bulletins are not legally or practically enforceable. In the former regard, the bulletins were not issued in accordance with the Administrative Procedure Act.<sup>9</sup> They are not the output of adjudications, they are not legislative rules issued in compliance with notice-and-comment rulemaking procedures, and they are not interpretive rules that interpret law or clarify duties found in existing statutes or regulations.<sup>10</sup>

Yet, in spite of the lack of adjudication or notice-and-comment, and in contrast to merely interpreting existing duties, the draft bulletins seek to establish guidelines reflecting the Agency's expectations for safe and sound operations. With respect to practicality, OIG noted that the plentiful expectations included in the draft bulletins tend to be expressed equivocally. For example, the liquidity risk management draft bulletin repeatedly describes what an Enterprise "should" do, rather than advising what it "must do" or "is required to do"—over the course of six pages, "should" is used 73 times. This begs the question of whether a failure to abide by one of the 73 "shoulds" will warrant a sanction.

FHFA published the collateralization of advances and other credit products to insurance companies on December 23, 2013, and the liquidity and operational risk management bulletins on February 18, 2014, without making changes to address OIG's concerns. With respect to the liquidity and operational risk management bulletins, FHFA explained that "Agency staff ... are satisfied that advisory guidance, rather than a set of regulatory mandates, is the appropriate vehicle to communicate the agency's expectations with respect to the subject matter of the draft bulletins." In support of its position, FHFA advised that other financial regulators often rely upon unenforceable guidance and noted:

... modern financial institutions operate in complex environments with many possible sources of changing risk, and complex operation that must be effectively managed. As a general proposition, it is the appropriate competency and responsibility of financial institution management, rather than government, to determine how best to do that.

OIG appreciates that all Agency supervisory expectations do not have to be promulgated in

a manner that ensures their enforcement; some expectations can be expressed as guidance with the understanding that different subjects of the supervision can satisfy Agency expectations in different ways. However, it is plain to us that some things are so important that they warrant bright-line and inflexible requirements. Clearly, there are topics within the curricula of collateralization of advances and other credit products to insurance companies and liquidity or operational risk management that are so important or well established that they are susceptible to an enforceable standard. Further, FHFA is not just a supervisor/regulator of the Enterprises; it is also a conservator, and thus, it has the authority—and, in our view, a responsibility—to be more explicit and insistent in its caretaking. Yet, as previously reported by OIG, FHFA has often afforded undue deference to Enterprise decision making.<sup>11</sup>

### **3. Proposed Rule: Responsibilities of Boards of Directors, Corporate Practices and Corporate Governance Matters (79 Fed. Reg. 4414 (January 28, 2014))**

On December 17, 2013, OIG expressed its concern regarding four sections of a draft version of a proposed rule entitled *Responsibilities of Boards of Directors, Corporate Practices and Corporate Governance Matters* (RIN 2590-AA59). OIG noted that the draft proposed rule was too vague with regard to FHFA's authority to limit or bar indemnification payments and failed to provide specific examples of circumstances under which such action could be taken. FHFA did not propose an alternative standard to the draft standard that allows FHFA to limit or prohibit indemnification payments "in furtherance of safe and sound operations of the regulated entity" or include any explanatory examples in the published version of the proposed rule. It did, however, add a sentence to its preamble noting some examples under which

FHFA could limit or prohibit indemnification payments.

OIG also recommended that as a condition of indemnification, FHFA consider requiring directors, officers, and employees to purchase a bond to protect the regulated entity in the event that an indemnification claim is declined. FHFA rejected this suggestion as contrary to industry practice and an inappropriate inclusion in a rulemaking that is intended to merely carry over predecessor regulations (i.e., according to FHFA, the purpose of the rulemaking was not to introduce significant changes in policy). Additionally, FHFA rejected OIG's request that it be specifically mentioned in the regulatory report section of the rule that requires the entities to file reports, information, and raw or summary data to determine compliance with laws, orders, rules, or regulations. FHFA claimed that OIG can obtain the same information using its authority under the Inspector General Act and that OIG has no need for such information as it has no safety or soundness responsibilities for the regulated entities.

In contrast, OIG believes that, because the Inspector General Act guarantees our access to all information to which FHFA has access, it is more efficient to require filers to provide copies to OIG, and that OIG has a much better grasp of the information that it needs to carry out its mission. Likewise, FHFA rejected OIG's request that FHFA consider including non-executive/senior professionals in the proposed rule to ensure effective monitoring and enforceable penalties for violators, particularly in light of an OIG evaluation report finding that FHFA should enhance its current non-executive/senior professional compensation oversight. FHFA's view is that it is sufficient to oversee the compensation arrangements for the executives of the regulated

entities and to review the compensation policies that those executives develop and implement for the non-executive/senior professionals.

#### **4. Final Rule: Removal of References to Credit Ratings in Certain Regulations Governing the FHLBanks (78 Fed. Reg. 67,004 (November 8, 2013))**

During this reporting cycle, FHFA published a final rule on the removal of references to credit ratings in certain FHLBank regulations which, aside from some technical adjustments, is the same as the proposed rule which was published in the prior reporting cycle. OIG neither concurred nor nonconcurred on the draft version of the final rule but reiterated the concerns it raised during the draft proposed rule phase. Specifically, OIG commented that the section implementing section 939A of Dodd-Frank lacked sufficient discussion about what factors the FHLBanks should consider (and how) when assessing investing quality, and that the proposed rule did not include any criteria for assessing investment quality. The final rule does not address OIG's concerns.

#### **5. Final Rule: Stress Testing of Regulated Entities (78 Fed. Reg. 59,219 (September 26, 2013))<sup>12</sup>**

As was evident from FHFA's inclusion in its proposed rule (October 5, 2012) of a reporting requirement for baseline, adverse, and severely adverse conditions, FHFA was aware that Dodd-Frank requires primary financial regulators for certain nonbank financial institutions to conduct annual stress tests under "at least 3 different sets of conditions, including baseline, adverse, and severely adverse ... [and] to publish a summary of the results of the required stress tests." See 12 U.S.C. § 5365(i)(2)(C)(ii) and 5365(i)(2)(C)(iv). Yet, after the FHLBanks and Freddie Mac requested that FHFA "conform with other

regulatory agencies” by changing the rule to require the regulated entities to publish only the results of the severely adverse scenario, FHFA dropped the baseline and adverse publication requirements (purportedly because the results of such scenarios could be misinterpreted as earnings projections) in their draft final rule. On July 15, 2013, OIG commented that although FHFA’s draft version of the final rule provided for stress testing, it only required reporting of the severely adverse scenario. OIG expressed its concern that FHFA’s draft final rule did not appear to be in compliance with section 165(i)(2) of Dodd-Frank, which requires, without exception, reporting in all three stress testing areas. The final rule published on September 26, 2013, maintained the requirement to publish results on only the most severely adverse scenario.

## Communications and Outreach

A key component of OIG’s mission is to communicate clearly with the GSEs, industry groups, other federal agencies, Congress, and the public. OIG facilitates clear communications through its targeted outreach efforts, hotline, coordination with other oversight organizations, and congressional statements and testimony.

### Outreach

During the reporting period, OIG staff made over 35 presentations to law enforcement agencies,

prosecutors, industry groups, and homeowners. The presentations to law enforcement officials were made to multiple mortgage fraud working groups across the country and individual federal agencies responsible for investigating mortgage fraud, such as HUD-OIG and USPIS. In addition, OI continued its partnership with the National Association of District Attorneys to train local and state law enforcement officials and prosecutors throughout the country, putting on presentations in four cities: Austin, Texas; Washington, DC; Columbus, Ohio; and Los Angeles, California.

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***Report fraud,  
waste, or abuse  
related to FHFA’s  
programs and  
operations  
by visiting  
[www.fhfaoig.gov](http://www.fhfaoig.gov)  
or calling (800)  
793-7724.***

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With respect to presentations to housing professionals, OIG staff made presentations to professional organizations, such as the Mortgage Bankers Association, bankruptcy trustee officials, and the National Association of Realtors. The presentations focused on fraud trends in the mortgage industry.

### Hotline

OI operates a hotline that allows concerned parties to report directly and in confidence information regarding possible fraud, waste, or abuse related to FHFA or the GSEs. We honor all applicable whistleblower protections. As part of our effort to raise awareness of fraud and how to combat it, OIG

promotes the hotline through our website, posters, emails targeted to FHFA and GSE employees, and our semiannual reports.

During the reporting period, the hotline received over 250 tips.



## Coordinating with Other Oversight Organizations

OIG shares oversight of federal housing program administration with several other federal agencies, including HUD, the Department of Veterans Affairs, the Department of Agriculture, and Treasury's Office of Financial Stability (which manages the Troubled Asset Relief Program); their inspectors general; and other law enforcement organizations. To further the oversight mission, we coordinate with these entities to exchange best practices, case information, and professional expertise. During the semiannual period ended March 31, 2014, we participated in the following cooperative activities:

- **RMBS Working Group.** OIG continued to take part in the activity of the RMBS Working Group, as discussed in "Civil Cases" (see page 37).
- **CIGIE.** OIG actively participates in several CIGIE committees and working groups.
  - The Inspection and Evaluation Committee established a working group to conduct a pilot "peer review" program for Inspection and Evaluation units in the inspector general community. The peer review is designed to assess organizations' work under CIGIE's *Quality Standards for Inspection and Evaluation* (January 2012) and to promote credibility of such work by validating the organizations' work processes and evaluating their objectivity, independence, and rigorous adherence to applicable standards.
  - The Investigation Committee advises the inspector general community on issues involving criminal investigations, criminal investigations personnel, and establishing criminal investigative guidelines. During this semiannual period, the committee considered modifications to the Inspector

General Criminal Investigator Academy training process for investigative personnel.

- **Council of Inspectors General on Financial Oversight.** The Council of Inspectors General on Financial Oversight (CIGFO) was created by Dodd-Frank to oversee the Financial Stability Oversight Council (FSOC), which is charged with strengthening the nation's financial system. OIG is a permanent member of CIGFO, along with the inspectors general of Treasury, the FDIC, the SEC, and others. FSOC has issued a transparency policy that formalizes the commitment to conducting its business as openly and transparently as practicable, given the confidential supervisory and sensitive information at the center of its work. OIG participates in a CIGFO working group conducting a review of FSOC's compliance with its transparency policy. The objective for this review is to assess the extent to which FSOC is operating consistent with the expectations outlined in the transparency policy, including such requirements as holding open meetings on an annual basis and recording all votes on final and proposed rules, then reflecting those votes in the FSOC minutes.
- **Mortgage Fraud Conference.** In February 2014, DOJ and FHFA sponsored a mortgage fraud conference, and OIG supported it. The conference was attended by approximately 125 representatives from various government regulators, DOJ prosecutors, and assorted law enforcement officials, and included presentations on all aspects of mortgage fraud—from loan origination to **securitization**. OIG representatives made presentations on fraud investigation in the primary and secondary markets; the Taylor, Bean, & Whitaker investigation; investigative techniques; and the RMBS Working Group.

## **Communicating with Congress**

In fulfilling our mission, OIG works in close partnership with Congress and is committed to keeping it fully apprised of our oversight of FHFA. OIG met regularly with members of Congress and provided briefings to key congressional committees and offices. Briefing topics included recommendations from OIG reports and FHFA's progress in implementing them, themes emerging in OIG's body of work, OIG's organization and strategy, and areas of ongoing work.

Additionally, we endeavor to inform Congress through responses to numerous technical assistance and information requests, as well as replies to formal written inquiries from members of Congress on various topics.

Copies of the Inspector General's written testimony to Congress are available at [www.fhfaig.gov/testimony](http://www.fhfaig.gov/testimony).

## Section 2: FHFA and GSE Operations

### Overview

In July 2008, HERA created FHFA to oversee vital components of our nation's secondary mortgage market.<sup>13</sup> FHFA is responsible for the effective supervision, regulation, and housing mission oversight of Fannie Mae, Freddie Mac, the FHLBanks, and the FHLBanks' Office of Finance to promote their safety and soundness and to support housing finance, affordable housing, and a stable and liquid market.<sup>14</sup>

In this section, we provide an overview of FHFA and its relationship with the GSEs; a brief discussion of the GSEs' business models and the primary reasons for their improved financial results; and a summary of selected FHFA and GSE activities.

### FHFA and the Enterprises

Under HERA, FHFA was appointed conservator of the Enterprises on September 6, 2008, and it serves as their regulator and conservator. As regulator, the Agency's mission is to ensure the Enterprises operate in a safe and sound manner and that their operations and activities contribute to a liquid, efficient, competitive, and resilient housing finance market.<sup>15</sup> As conservator, the Agency seeks to conserve and preserve Enterprise assets.

FHFA accomplishes its mission by performing onsite examinations of the Enterprises; coordinating congressional, public, and consumer inquiries; assisting the Enterprises with foreclosure prevention actions; and developing and implementing a strategic plan for the future of the Enterprises' conservatorships.<sup>16</sup>

The Enterprises were chartered by Congress to provide stability and liquidity in the secondary market for home mortgages. They fulfill this charter by purchasing residential loans from loan originators that can use the sales proceeds to make additional loans.

Under HERA, the Enterprises receive financial support from Treasury to prevent their liabilities from exceeding their assets, subject to a cap.<sup>17</sup>

### FHFA and the Enterprises' Role in Housing Finance

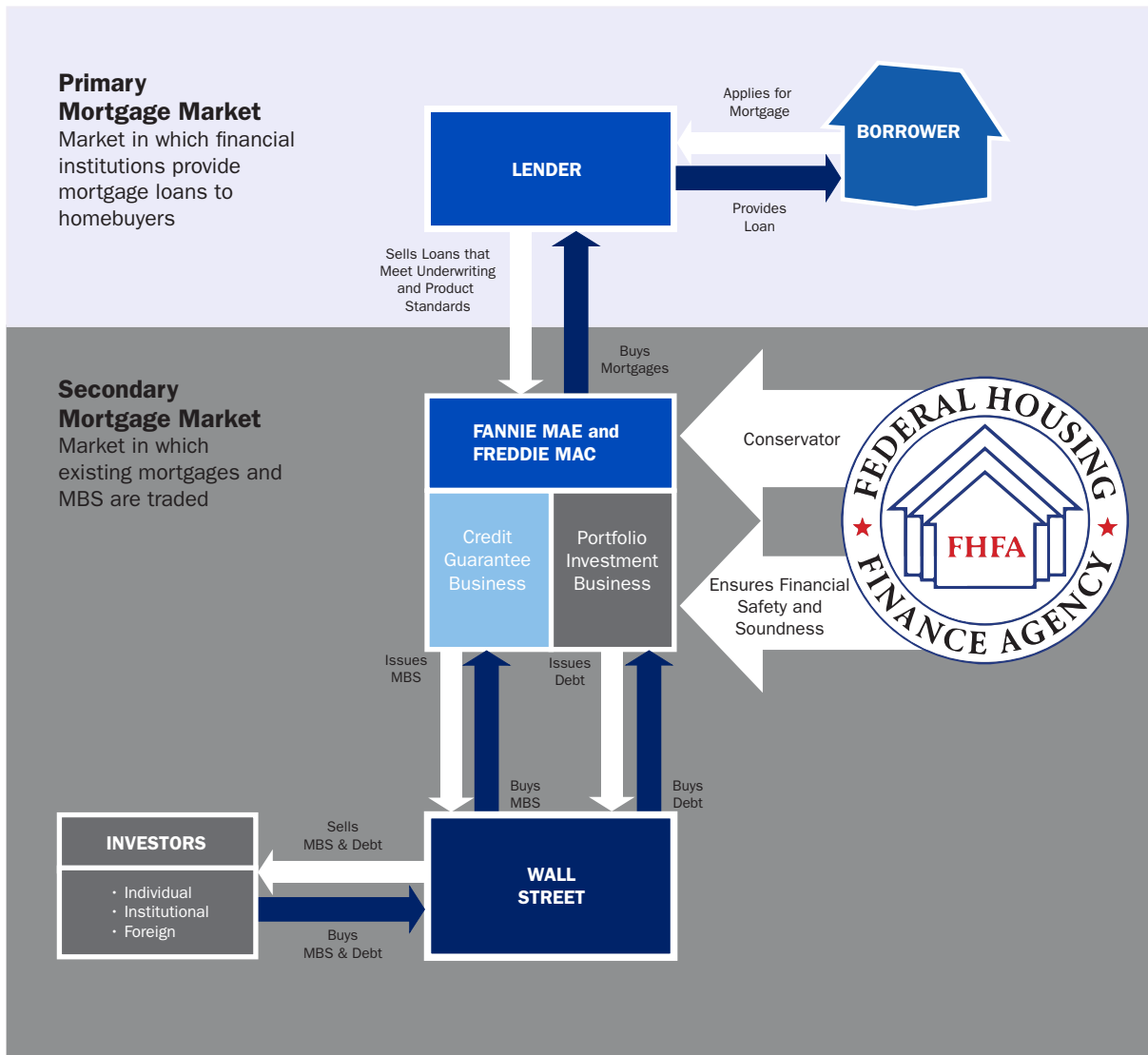
As the regulator of the Enterprises, FHFA has a statutory responsibility to ensure that they operate in a safe and sound manner and that their activities support a stable and liquid housing finance market.<sup>18</sup>

As Figure 8 (see page 45) illustrates, the Enterprises support the nation's housing finance system by providing liquidity to the secondary mortgage market. Liquidity is created when the Enterprises purchase mortgages that lenders—such as banks, **credit unions**, and other retail financial institutions—originated for homeowners.

These mortgages are securitized by pooling and packaging them into **mortgage-backed securities (MBS)** and are either sold or kept by the Enterprises as an investment. As part of this process, the Enterprises—for a fee—guarantee payment of principal and interest on the mortgages.

Historically, the Enterprises have benefited from an **implied guarantee** that the federal government would prevent default on their financial obligations, and the Enterprises assumed dominant positions in the residential housing finance market.<sup>19</sup>

**Figure 8. Overview of the Enterprises and FHFA's Role**



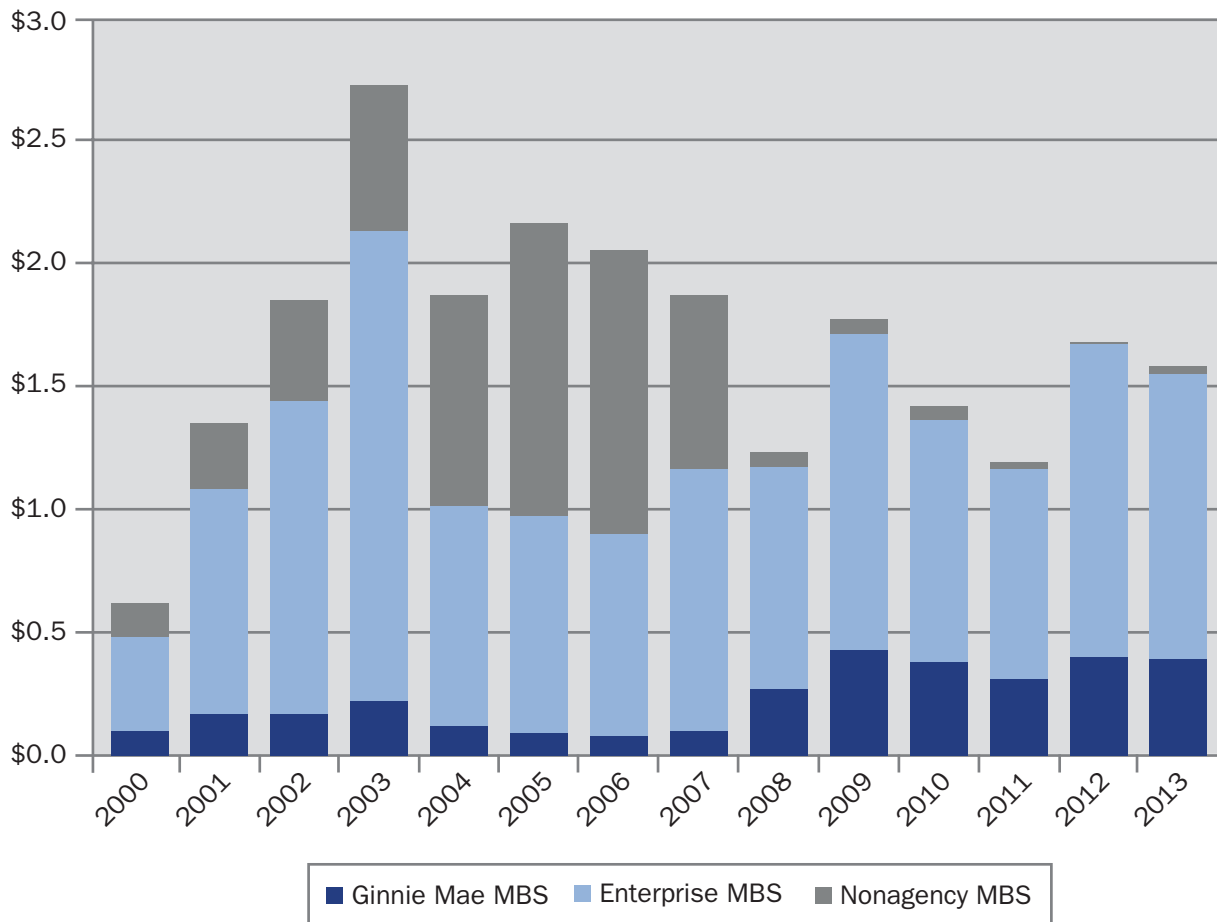
**Enterprises' Market Share of the Secondary Market**

As Figure 9 (see page 46) illustrates, after losing market share to nonagency competitors during the housing boom from 2004 through 2007, the Enterprises regained dominant positions in the residential housing finance market (with the federal government's financial support) as the financial

crisis continued and private-sector financing for the secondary market nearly disappeared.<sup>20</sup> Since entering conservatorships in September 2008, the Enterprises have bought and guaranteed approximately three out of every four mortgages originated in the United States. By providing a majority of the liquidity to the housing finance market, the Enterprises (and, therefore, the taxpayers) own a majority of the mortgage credit risk.<sup>21</sup>



**Figure 9. Primary Sources of MBS Issuances from 2000 to 2013 (\$ trillions)**



## Enterprises’ Financial Performance

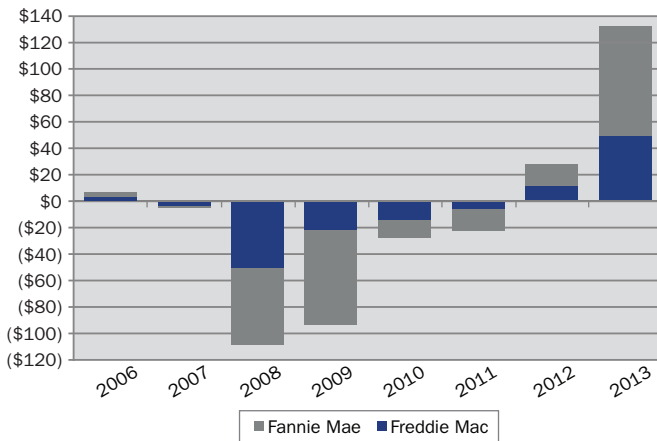
The Enterprises continued to report record profits over the year ended December 31, 2013. Their profits have risen since 2012 (see Figure 10, page 47) and continue to offset the losses that began in 2007 (see Figure 11, page 47).<sup>22</sup>

As shown in Figure 12 (see page 47), Fannie Mae reported net income of \$84 billion for the year ended December 31, 2013, compared with net income of \$17.2 billion for the same period in 2012.<sup>23</sup> Freddie Mac reported net income of \$48.7 billion for the year ended December 31, 2013, compared with net income of \$11 billion for the same period in 2012.<sup>24</sup>

A key factor underlying the increase in both Enterprises’ net income over the year ended December 31, 2013, was the release of substantial portions of their **valuation allowances** against **deferred tax assets**—with Fannie Mae releasing the majority of its valuation allowance and Freddie Mac releasing its full valuation allowance. The Enterprises are required to maintain valuation allowances for deferred tax assets that they determine may not be realized. This caused them to establish substantial valuation allowances during the years that they experienced net losses.<sup>25</sup>

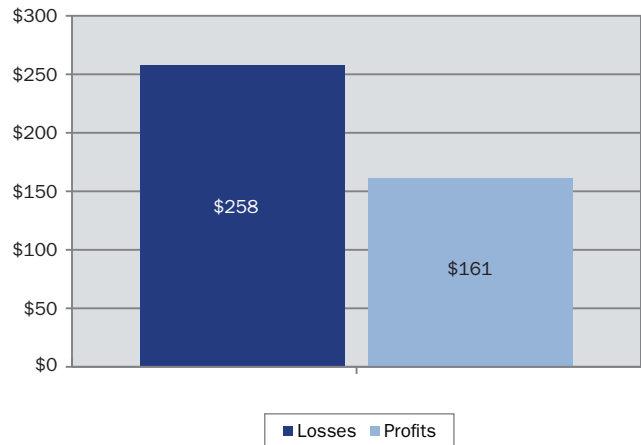
During the first quarter of 2013, however, Fannie Mae determined that the factors in favor of releasing the allowance outweighed the factors in favor of

**Figure 10. Enterprises' Annual Net Income (Loss) 2006 to 2013 (\$ billions)**



maintaining it. Therefore, Fannie Mae released a substantial portion of its valuation allowance during this period, which resulted in the recognition of \$45.4 billion as a federal income tax benefit for the year ended December 31, 2013, but retained \$525 million of its valuation allowance that pertains to **capital loss carryforwards**, which it believes will expire unused.<sup>26</sup> Similarly, in the third quarter of 2013, Freddie Mac released its entire valuation allowance against its deferred tax assets, recognizing \$23.3 billion as a federal income tax benefit, as of December 31, 2013.<sup>27</sup> For future quarters,

**Figure 11. Enterprises' Combined Losses from 2007 Through 2011 and Combined Profits from 2012 Through 2013 (\$ billions)**



Freddie Mac will continue to evaluate its ability to realize their deferred tax assets and will reestablish a valuation allowance should it determine that it is more likely the deferred tax assets will not be realized.<sup>28</sup>

Other key factors in the Enterprises' continued profitability are discussed below. These factors include: (1) continued improvements in the single-family business segment driven by stronger credit quality, (2) increases in guarantee fee income as a result of FHFA direction, (3) an increase in home

**Figure 12. Enterprises' Summary of Net Income for the Years Ended December 31, 2013 and 2012 (\$ billions)**

|  | Fannie Mae    |                    | Freddie Mac   |               |
|--|---------------|--------------------|---------------|---------------|
|  | 2013          | 2012               | 2013          | 2012          |
| Net Interest Income                                      | \$22.4        | \$21.5             | \$16.5        | \$17.6        |
| Credit-related Income (Expenses)                         | 11.8          | 1.1                | 2.6           | (1.9)         |
| Gain (Loss) on Derivative Agreements                     | 3.3           | (3.6) <sup>a</sup> | 2.6           | (2.4)         |
| Impairment of Securities Considered Other than Temporary | (0.1)         | (0.7)              | (1.5)         | (2.2)         |
| Other Income (Expense)                                   | 1.2           | (1.1)              | 5.2           | (1.6)         |
| Income Tax Benefit                                       | 45.4          | -                  | 23.3          | 1.5           |
| <b>Net Income</b>  | <b>\$84.0</b> | <b>\$17.2</b>      | <b>\$48.7</b> | <b>\$11.0</b> |

<sup>a</sup> Loss on derivatives referenced to Table 11, p. 76, in the Fannie Mae 2013 10-K Report.

prices causing a reduction in defaults, (4) **derivative gains** due to an increase in swap rates, and (5) additional non-interest income as a result of settlement proceeds related to private-label securities litigation and gains on securities.

### Continued Improvement in Credit Quality of New Single-Family Business

Fannie Mae’s **credit-related income** (comprised of foreclosed property income and the benefit for credit losses) for the year ended December 31, 2013, was \$11.8 billion, compared with credit-related income of \$1.1 billion over the same period in 2012.<sup>29</sup> Freddie Mac’s credit-related income for the year ended December 31, 2013, was \$2.6 billion, compared with credit-related expenses of \$1.9 billion over the same period in 2012.<sup>30</sup> The increase in credit-related income is primarily the result of continued improvements in the credit quality of each Enterprise’s single-family book of business—as higher credit quality leads to fewer loan delinquencies—and the increase in home prices.<sup>31</sup>

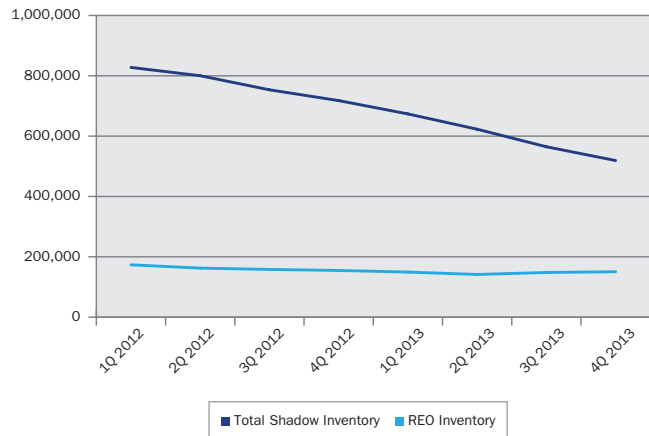
The Enterprises’ single-family books of business consist of loans purchased and guaranteed that generate interest and guarantee fee income. The credit quality of the single-family loans acquired by the Enterprises beginning in 2009 is significantly better than that of loans acquired from 2005 to 2008, as measured by **loan-to-value (LTV)** ratios, FICO scores, and the proportion of loans underwritten with fully documented income.<sup>32</sup>

This improved credit quality is attributed to:

(1) more stringent credit policies and underwriting standards, (2) tighter mortgage insurers’ and lenders’ underwriting practices, and (3) fewer purchases of loans with higher-risk attributes (e.g., **Alt-A**, interest-only, credit scores below 620, and LTV ratios above 90%).<sup>33</sup>

Further, the Enterprises are now holding more loans with higher credit quality acquired from 2009 to

**Figure 13. Decline in Seriously Delinquent Loans and REO Inventory**



present in their single-family books of business. As of December 31, 2013, loans acquired after 2008 comprised 77% and 75%, respectively, of Fannie Mae’s and Freddie Mac’s books of business.<sup>34</sup> Conversely, the legacy housing boom loans acquired from 2005 through 2008, which have a higher probability of credit defects, have declined to 15% of the single-family book of business for Fannie Mae and 16% for Freddie Mac as of December 31, 2013, compared with 22% and 24%, respectively, as of December 31, 2012.<sup>35</sup>

As the credit quality in the Enterprises’ single-family books of business has improved, the number of seriously delinquent loans (also known as the shadow inventory) has declined (see Figure 13, above).<sup>36</sup>

For the year ended December 31, 2013, the Enterprises’ combined shadow inventory (loans that are considered to be 180 or more days delinquent) totaled 519,156 loans, compared with 717,841 for the same period in 2012—a 28% decrease.<sup>37</sup> However, as the number of properties acquired through foreclosure has declined, the disposition of total properties has also decreased. For the year ended December 31, 2013, Fannie Mae disposed of 146,821 single-family properties, compared with 187,341 for the same period in 2012.<sup>38</sup> For the year

ended December 31, 2013, Freddie Mac disposed of 72,445 single-family properties, compared with 94,276 for the same period in 2012.<sup>39</sup>

### Increase in Guarantee Fee Prices

A significant source of income for the Enterprises comes from receiving guarantee fees.<sup>40</sup> The Enterprises receive these fees for taking the risk of loan default and providing MBS investors with a guarantee for the principal and interest payment.<sup>41</sup> In 2012, FHFA directed the Enterprises to increase their guarantee fees.<sup>42</sup> As a result, guarantee fee income increased for the year ended December 31, 2013.

Fannie Mae’s combined single-family and multifamily guarantee fee income for the year ended December 31, 2013, was \$11.7 billion, compared with \$9.2 billion for the same period in 2012—a 27% increase; Freddie Mac’s combined single-family and multifamily guarantee fee income for the year ended December 31, 2013, was \$5.1 billion, compared with \$4.5 billion for the same period in 2012—a 13% increase.<sup>43</sup>

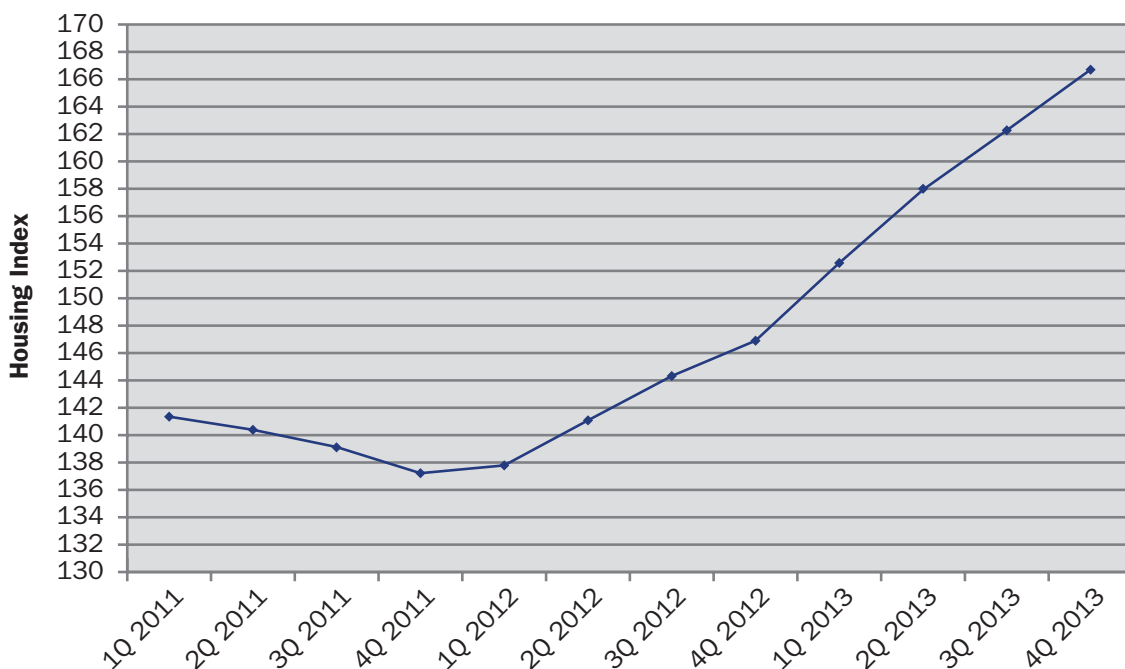
Additionally, Fannie Mae’s guarantee fee income increase for the year ended December 31, 2013, is a result of liquidating loans with lower guarantee fees while adding loans with higher guarantee fees to their multifamily book of business.<sup>44</sup>

Additional increases to the guarantee fees were planned to take effect in March and April 2014. However, on January 8, 2014, FHFA announced that it directed the Enterprises to delay these increases until further evaluation could be completed.<sup>45</sup>

### Impact of Home Prices on Credit Losses

Another factor positively influencing credit-related expenses, i.e., credit losses, is home prices. An increase in home prices can decrease the likelihood that loans will default and reduce the estimated credit losses on the loans that default.<sup>46</sup> The S&P/Case-Shiller Home Price Index shows a decrease in the index for each quarter in 2011; however, it shows a steady increase in the index since the first quarter of 2012 through 2013 (see Figure 14, below).<sup>47</sup>

**Figure 14. Home Price Index 2011 Through 2013**





## Higher Increases in Swap Rates Lead to Derivative Gains

The Enterprises use **derivative** instruments to manage the interest rate and prepayment risk associated with their investments in mortgage loans and mortgage-related securities.<sup>48</sup> Derivative instruments include written options, interest rate guarantees, and short-term default guarantee commitments.<sup>49</sup>

Fannie Mae's derivative gains for the year ended December 31, 2013, were \$3.3 billion, compared with a loss of \$3.6 billion for the same period in 2012. Freddie Mac's derivative gains for the year ended December 31, 2013, were \$2.6 billion, compared with a loss of \$2.4 billion for the same period in 2012.<sup>50</sup>

These overall derivative gains were primarily due to gains in risk management derivatives and mortgage commitment derivatives. The gains in risk management derivatives were a result of increases on swap rates. The increases in mortgage commitment derivatives were a result of gains on commitments to sell mortgage-related securities, as a consequence of a decrease in prices as interest rates increased during the commitment period.<sup>51</sup>

## Proceeds from Private-Label Securities Litigation and Gains on Securities

In 2011, FHFA, on behalf of the Enterprises, initiated litigation against 18 financial institutions alleging private-label securities violations. FHFA recovered \$7.5 billion from six of these financial institutions through litigation settlements in 2013. In addition, FHFA, on behalf of Freddie Mac, recovered \$335 million from a private-label securities non-litigation settlement in 2013—separate from the 18 lawsuits initiated in 2011.<sup>52</sup>

Settlement proceeds related to private-label securities litigation are recorded as other non-interest income and affect the non-interest income portion of the

income statement. The proceeds from the settlement agreements contributed to the Enterprises' continued financial improvement.<sup>53</sup>

Fannie Mae's non-interest income for the year ended December 31, 2013, was \$8.1 billion, compared with a loss of \$2 billion for the same period in 2012.<sup>54</sup> Freddie Mac's non-interest income for the year ended December 31, 2013, was \$8.5 billion, compared with a loss of \$4.1 billion for the same period in 2012.<sup>55</sup> These non-interest income amounts do not include the valuation allowance (income tax benefit) released against the deferred tax assets.

Additionally, gains on sales of securities increased substantially. As a result, available-for-sale securities gains increased significantly, adding additional income for the Enterprises.<sup>56</sup>

For the year ended December 31, 2013, Fannie Mae realized gains of \$1.6 billion on sales of securities, compared with \$40 million for the same period in 2012; likewise, Freddie Mac realized gains of \$1.9 billion on sales of securities, compared with \$152 million.<sup>57</sup>

## Government Support

Due to their continued profitability, as of March 31, 2014, the Enterprises did not request a draw from Treasury in 2013 or 2014 to date and are paying significant dividends.

## Draw Requests and Dividend Payments Due Under the Senior Preferred Stock Purchase Agreements

In August 2012, FHFA and Treasury agreed to a third amendment to the **Senior Preferred Stock Purchase Agreements (PSPAs)** that, among other things, replaced the fixed dividend rate the Enterprises pay as of the first quarter of 2013. The modification called for a full net worth sweep of all

future Enterprise earnings, with a quarterly sweep of every dollar of net worth, instead of a fixed percentage dividend payment. This was intended to end the circular practice of the Enterprises drawing funds from Treasury in order to pay dividends back to Treasury. The Enterprises' net worth (above a specified initial buffer amount, which was \$3 billion) is now effectively distributed to Treasury; for the year ended December 31, 2013, approximately \$130.1 billion was distributed, with an additional \$17.6 billion paid in the first quarter of 2014.<sup>58</sup>

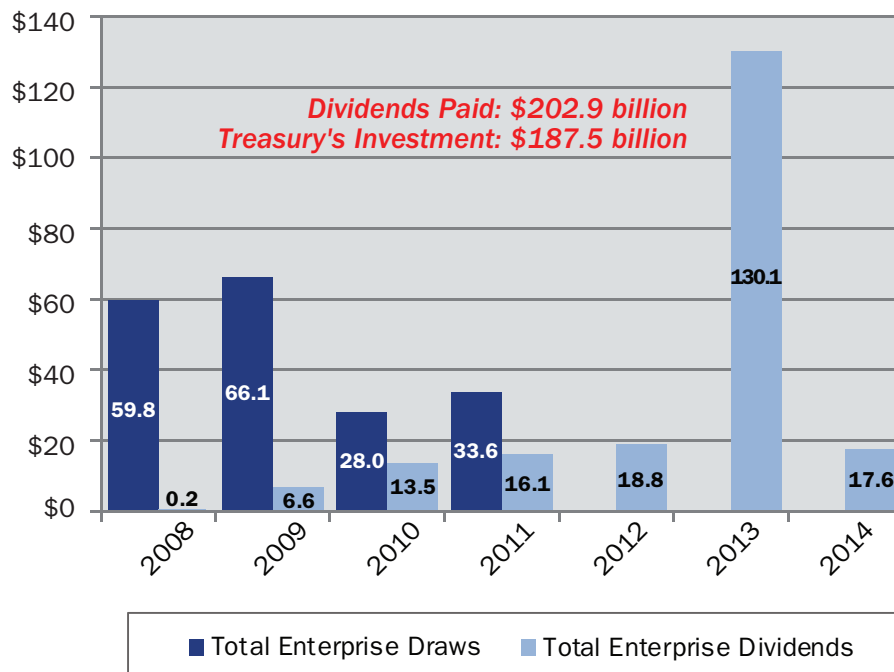
Fannie Mae's net worth as of December 31, 2013, was approximately \$9.5 billion, resulting from comprehensive net income of \$84.8 billion for the year ended December 31, 2013, and a beginning equity balance of \$7.2 billion—i.e., the Enterprise's net worth as of December 31, 2012—less \$82.5 billion paid to Treasury in senior **preferred stock** dividends during 2013. As a result, Fannie Mae did not request a draw from Treasury in 2013 under the PSPA.<sup>59</sup>

Freddie Mac's net worth as of December 31, 2013, was \$12.8 billion, resulting from comprehensive net income of \$51.6 billion for the year ended December 31, 2013, and a beginning equity balance of \$8.8 billion less \$47.6 billion paid to Treasury in senior preferred stock dividends during 2013. As a result, Freddie Mac did not request a draw from Treasury in 2013 under the PSPA.<sup>60</sup>

For the first quarter of 2014, Fannie Mae and Freddie Mac made additional payments of \$7.2 billion and \$10.4 billion, respectively, under the terms of the PSPAs. As of March 31, 2014, Fannie Mae and Freddie Mac have paid Treasury a total of \$121.1 billion and \$81.8 billion, respectively, in dividends on the senior preferred stock.<sup>61</sup> These dividend payments do not reduce the principal balance of Treasury's investments in the Enterprises.<sup>62</sup>

Since the conservatorships began in 2008 through March 31, 2014, the Enterprises have drawn a total of \$187.5 billion from Treasury and paid \$202.9 billion in dividends (see Figure 15, below).

**Figure 15. Enterprises' Treasury Draws and Dividend Payments Due Under PSPAs (\$ billions)**



As of March 31, 2014, Fannie Mae’s total draws from Treasury under the PSPA remain at \$116.2 billion and Freddie Mac’s remain at \$71.3 billion.<sup>63</sup>

### Return on Treasury’s Investment

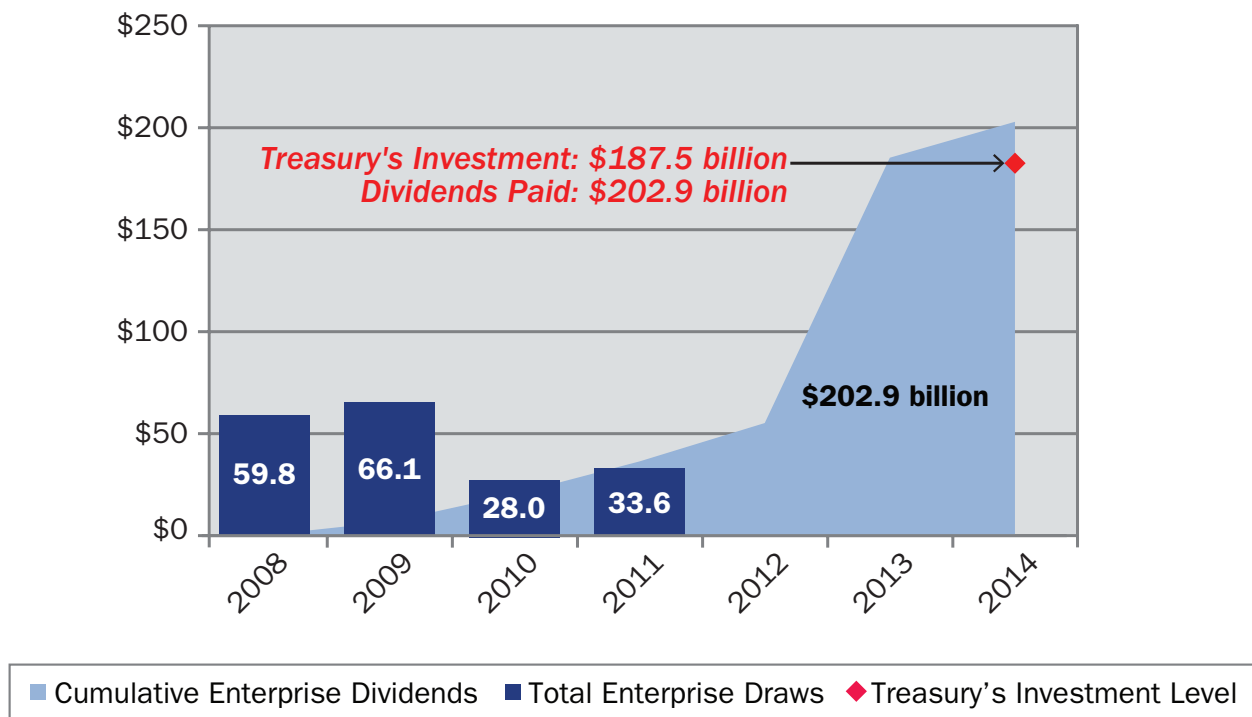
The full net worth sweep set up by the third amendment to the PSPAs may result in Treasury receiving a larger sum than it would have under the previous 10% dividend structure, making a speedier gain on Treasury’s investment possible (see Figure 16, below, and Figure 17, page 53).<sup>64</sup> Beginning in 2013, the Enterprises began paying dividends equal to their net worth over a specified buffer, and at least for 2013, the Enterprises paid Treasury significantly more than would have been required prior to the August 2012 PSPA amendments (see Figure 16, below).<sup>65</sup> For comparison, using the fixed dividend rate of 10% for the year ended December 31, 2013, and the three months ended March 31, 2014, the Enterprises would have paid Treasury \$23.7 billion,

whereas, under the new full net worth sweep, the Enterprises paid more than five times that amount—or \$147.7 billion (see Figure 17, page 53).<sup>66</sup>

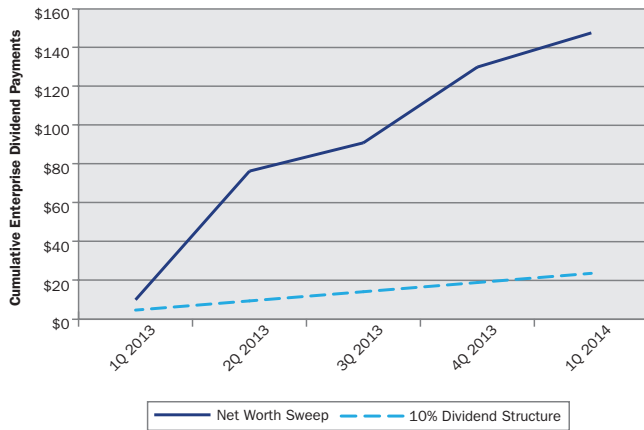
Changes in the valuation allowance impact the income tax benefits, which in turn influence net income and the quarterly dividend payments to Treasury.<sup>67</sup> The Enterprises’ large 2013 cumulative dividend payments were driven by the release of their valuation allowances, resulting in year-end income tax benefits of \$68.7 billion. Because the release of the valuation allowances played a significant part in the Enterprises’ record 2013 profits, it is anticipated that the income tax benefits and dividend payment levels will not be sustainable over the long term.<sup>68</sup>

Additionally, the full net worth sweep makes it impossible for the Enterprises to build up any capital because their net worth, except for the specified buffer amount, will be zero after they make each quarterly dividend payment to Treasury. For each

**Figure 16. Enterprises’ Advance on Treasury’s Investment as of March 31, 2014 (\$ billions)**



**Figure 17. Enterprises' Full Net Worth Sweep Versus 10% Dividend Structure 2013 Through First Quarter 2014 (\$ billions)**



Enterprise, the buffer was initially set at \$3 billion but will be reduced by \$600 million every year until 2018—i.e., the buffer will reach zero in five years. For 2014, the buffer has been reduced to \$2.4 billion.<sup>69</sup>

### Additional Government Support

The Enterprises also benefited from extraordinary government measures to support the housing market overall. During the period from September 2008 through March 2010, the Federal Reserve and Treasury purchased more than \$1.3 trillion in Enterprise MBS through the **GSE MBS Purchase Facility**. Additionally, the Federal Reserve purchased \$135 billion of **bonds** issued by the Enterprises.<sup>70</sup> The Federal Reserve became the predominant purchaser of MBS during its purchase programs, and its purchases helped to prime the nation's housing finance system.<sup>71</sup>

Treasury's last purchase of Enterprise MBS, through the purchase facility, was in December 2009, while the Federal Reserve last purchased Enterprise MBS through the same facility in March 2010. However, as of March 31, 2014, the Federal Reserve continues to purchase Enterprise MBS through the Open

Market Trading Desk at the Federal Reserve Bank of New York at a pace of \$30 billion a month. This pace does not include purchases to replace paid down principal.<sup>72</sup>

## FHLBank System

The FHLBanks are GSEs, federally chartered but privately **capitalized** and independently managed. The 12 regional FHLBanks together with the Office of Finance, the fiscal agent of the FHLBanks, comprise the FHLBank System. All FHLBanks operate under the supervisory and regulatory framework of FHFA.<sup>73</sup> FHFA's stated mission with respect to the FHLBanks is to provide effective supervision, regulation, and housing mission oversight to promote the FHLBanks' safety and soundness, support housing finance and affordable housing, and facilitate a stable and liquid mortgage market.<sup>74</sup>

The FHLBank System was created in 1932 to improve the availability of funds for home ownership, and its mission is to provide local lenders with readily available, low-cost funding to finance housing, jobs, and economic growth.<sup>75</sup> The 12 FHLBanks fulfill this mission primarily by providing secured loans known as advances to their members, resulting in an increased availability of credit for residential mortgages, community investments, and other housing and community development services.<sup>76</sup>

The FHLBanks are cooperatives that are owned privately and wholly by their members. Each FHLBank operates as a separate entity within a defined geographic region of the country, known as its district, with its own board of directors, management, and employees. Each member of an FHLBank must purchase and maintain capital stock as a condition of its membership.<sup>77</sup> FHLBank members include financial institutions such as



**commercial banks, thrifts**, insurance companies, and credit unions.<sup>78</sup> Figure 18 (see below) provides a map of the districts of the 12 FHLBanks.

The primary business of the FHLBanks is to raise funds in the capital markets by issuing debt, known as consolidated obligations, through the Office of Finance and to use the consolidated obligations to provide their members with advances. The primary source of each FHLBank's earnings is net interest income, which is the interest earned on advances, investments, and mortgage loans, less the interest paid on consolidated obligations, deposits, and other borrowings.<sup>79</sup>

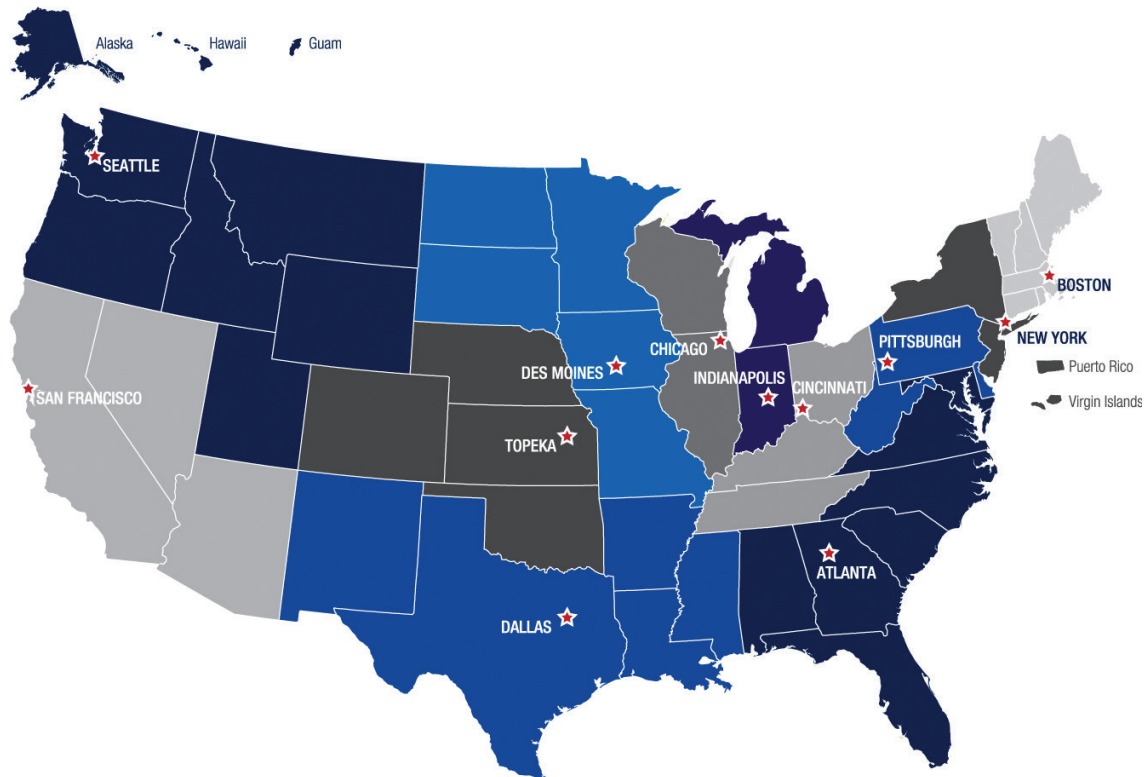
In the event of a default on a consolidated obligation, each FHLBank is **jointly and severally liable** for losses, which means that each individual FHLBank is responsible for the principal and interest on all consolidated obligations issued by the FHLBanks.<sup>80</sup> However, like the Enterprises, the FHLBank System has historically enjoyed benefits (e.g., debt costs akin

to those associated with Treasury bonds) stemming from an implicit government guarantee of its consolidated obligations.<sup>81</sup>

### The FHLBanks' Combined Financial Performance

The regional housing markets affect the FHLBanks' demands for advances from member institutions to fund residential mortgage loans. During 2013, FHLBank members' borrowing increased, but remained below historical levels due in part to a slow economic recovery combined with higher consumer deposits and weakened lending. Further, during this period, the demand for advances continued to increase due to high member borrowing, particularly by large-asset members. However, many member institutions continue to experience high deposit levels and low loan demand. Although the average balances of advances increased, the demand was generally in lower-yielding advances, which contributed to the overall decline in interest income.<sup>82</sup>

**Figure 18. Regional FHLBanks**



The main source of the FHLBanks' income is interest earned on advances, mortgage loans, and investments (i.e., assets).<sup>83</sup> Fluctuations in short-term interest rates affect the FHLBanks' interest income and expense because a considerable portion of the FHLBanks' assets and liabilities are either directly or indirectly tied to short-term interest rates.<sup>84</sup>

For the year ended December 31, 2013, compared with the same period in 2012, average short-term interest rates generally decreased, resulting in lower returns on mortgage loans, advances, and investments. This was partially offset by lower interest expense on interest-bearing liabilities that were the result of the issuance of new consolidated obligations, including the effect of redemptions and refinancings of higher-cost consolidated obligations.<sup>85</sup> These combined effects contributed to the 3% decrease in the FHLBanks' net income.<sup>86</sup>

As shown in Figure 19 (see above), during 2013, the FHLBanks experienced a decrease in profitability, compared with the same period in 2012. Their net income was \$2.5 billion for the year ended December 31, 2013, a decrease of approximately \$80 million, compared with the same period in 2012.<sup>87</sup>

Lower returns on interest-earning assets—the main factor influencing net income—largely derive from decreases in interest income on advances, **held-to-maturity securities**, prepayment fees, and mortgage loans. Interest income on advances decreased from \$3.1 billion to \$2.5 billion—or 18%—and interest income on held-to-maturity securities decreased from \$2.6 billion to \$2.2 billion—a 16% decline—for the year ended December 31, 2013, compared with the same period in 2012. Also during this period, interest income on prepayment fees was reduced from \$341 million to \$138 million—or 60%—and interest income on mortgage loans decreased from \$2.2 billion to \$1.9 billion—a 15% decline—compared with the same period in 2012.<sup>88</sup>

**Figure 19. FHLBanks' Net Income for the Years Ended December 31, 2013 and 2012 (\$ millions)**

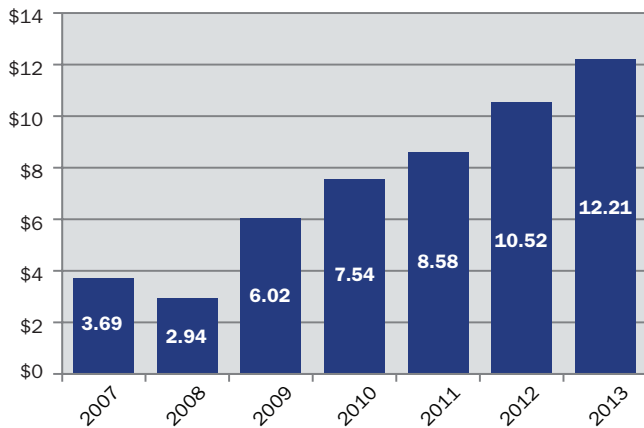
|   | 2013           | 2012           |
|---|----------------|----------------|
| Net Interest Income                                 | \$3,415        | \$4,052        |
| Reversal of (Provision for) Credit Losses           | 19             | (21)           |
| Other-than-Temporary Impairment Losses <sup>a</sup> | (15)           | (112)          |
| Derivative and Hedging Gains                        | 416            | 47             |
| Other Income (Loss)                                 | (72)           | (89)           |
| Total Non-interest Expense                          | (943)          | (975)          |
| Total Assessments                                   | (293)          | (296)          |
| <b>Net Income</b>                                   | <b>\$2,527</b> | <b>\$2,606</b> |

<sup>a</sup> Of the other-than-temporary impairment losses, private-label MBS comprised \$14 million and \$109 million for the years ended December 31, 2013 and 2012, respectively.

On the other hand, a decrease in interest expense from \$6.1 billion to \$5 billion—or 18%—prevented additional declines in net interest income. The decrease was driven by lower yields on new consolidated obligations, including the effect of redemptions and refinancings of higher-cost consolidated obligations. The refinancing of consolidated obligations, which resulted in lower interest payments, was a key contributor to this decline. Due to these lower payments, consolidated obligation expenses decreased from \$6 billion to \$4.8 billion—or 21%—for the year ended December 31, 2013, compared with the same period in 2012.<sup>89</sup>

The FHLBanks are exposed to interest rate risk primarily from the effect of interest rate changes on their interest-earning assets, as well as the funding sources for these assets. The goal of the FHLBanks is not to eliminate interest rate risk entirely but to manage it within appropriate limits. To achieve this goal, the FHLBanks use derivatives (e.g., **interest rate swaps, options, and swaptions**), which help reduce funding costs, maintain favorable interest rates, and manage overall assets and liabilities.<sup>90</sup>

**Figure 20. FHLBanks' Retained Year-end Earnings 2007 Through 2013 (\$ billions)**



Derivative and **hedging** activities gains accounted for additional non-interest income of \$416 million for the year ended December 31, 2013, compared with \$47 million for the same period in 2012—a substantial increase.<sup>91</sup>

As shown in Figure 20 (see above), the FHLBanks' combined year-end retained earnings have increased every year for the last six years and now exceed \$12 billion as of December 31, 2013.<sup>92</sup> As long as the FHLBanks are profitable, retained earnings should continue to increase because of the joint capital enhancement plan provisions adopted by the FHLBanks in 2011. The plan calls for the FHLBanks to set aside 20% of their net income into a separate, restricted retained earnings account.<sup>93</sup> The joint capital enhancements help to provide members' access to liquidity during times of economic stress, create an additional buffer to absorb FHLBank losses, provide protection on members' capital investments, and provide additional assurance that the FHLBanks will meet their consolidated obligations.<sup>94</sup>

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***Melvin L. Watt***  
***sworn in as the***  
***director of FHFA.***

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## Selected FHFA and GSE Activities

Over the last six months, there were several notable FHFA and GSE developments related to: the confirmation of a new FHFA Director; FHFA's progress toward developing a common securitization infrastructure; new mortgage insurance policy requirements; requirements for appraisal management companies and exemptions to appraisal requirements for higher-priced mortgages; guarantee fee changes; a proposed decrease of the Enterprises' loan purchase limits; sharing credit risk with private investors; the recovery of Enterprise losses; and tracking GSE performance. These developments and OIG's efforts in relation to them are summarized below.

### FHFA Leadership

#### Melvin L. Watt Sworn In as FHFA Director

On January 6, 2014, Melvin L. Watt was sworn in for a five-year term as the director of FHFA.

Watt, 68, served more than 21 years in the U.S. Congress as the representative from North Carolina's 12th congressional district. He was a member of the House Judiciary Committee, the Committee on Financial Services, and its Subcommittee on Capital Markets and Government

Sponsored Enterprises. He is the first FHFA Director to be confirmed by the Senate.<sup>95</sup>

#### FHFA Announces Departure of Edward J. DeMarco

In March 2014, FHFA announced that Edward J. DeMarco had submitted a letter indicating he will depart the Agency at the end of April 2014. DeMarco was appointed acting director of FHFA on August 25, 2009, by President Obama and served in that role until Director Watt was sworn in on January 6, 2014.<sup>96</sup>

## Mortgage Industry Standards

### Common Securitization Infrastructure

In October 2013, FHFA reported progress in the Enterprises' joint venture to build and operate the Common Securitization Platform (CSP). The joint venture, which is called Common Securitization Solutions, LLC (CSS), was formally established as a limited liability company in the state of Delaware. Officials from the Enterprises also signed a lease for office space for CSS in Bethesda, Maryland, and an executive recruitment firm was hired to identify candidates to serve as CSS's CEO and Chairman of the Board of Managers.<sup>97</sup>

CSS will own the CSP currently being developed. FHFA states that the CSP will consist of integrated hardware architecture and software applications that the Enterprises will use—and private firms may use—to perform aspects of the securitization process. FHFA reported that the team that is building the platform has been making progress in developing the design, scope, and functional requirements for the CSP's five modules—data acceptance, security issuance, disclosure, master servicing, and bond administration.<sup>98</sup>

### Mortgage Insurance

#### Overhaul of the Enterprises' Mortgage Insurance Master Policy Requirements

In December 2013, FHFA announced an overhaul of the mortgage insurance master policy requirements for the Enterprises. The Agency claims the new requirements will, among other things, facilitate timely and consistent claims processing. Additionally, FHFA believes that these changes will result in improvements such as requiring master policies to support loss mitigation strategies that were developed during the housing crisis; establishing specific time frames for processing claims, including requests for

additional documentation; setting standards for determining the timing and circumstances when coverage under the mortgage insurance policy must be maintained and when it may be revoked; and promoting information sharing among mortgage insurers, servicers, and the Enterprises.<sup>99</sup> The mortgage insurance overhaul was one of the targets set forth in FHFA's *Conservatorship Strategic Plan: Performance Goals for 2013*. Specifically, it called for the development of “counterparty risk management standards for mortgage insurers that include uniform master policies and eligibility requirements.”<sup>100</sup>

#### FHFA Directs the Enterprises to Restrict Lender-Placed Insurance Practices

In November 2013, FHFA directed the Enterprises to prohibit servicers from receiving reimbursement for expenses involving lender-placed insurance policies, i.e., policies that involve imposing property insurance on a property that lacks the coverage required by their mortgage instruments.<sup>101</sup>

In March 2013, FHFA issued a notice in the *Federal Register* regarding lender-placed insurance. The notice provided that the Enterprises would prohibit sellers and servicers from receiving payments for placing coverage with particular insurance providers. Additionally, the Enterprises would prohibit sellers and servicers from receiving payments associated with an insurance provider ceding premiums to a reinsurer owned or affiliated with the sellers or servicers.<sup>102</sup>

#### Requirements for Appraisal Management Companies

In March 2014, FHFA and five other federal agencies jointly issued a proposed rule that would implement minimum requirements for state registration and supervision of appraisal management companies (AMCs). An AMC is an entity that serves as an intermediary between appraisers and lenders and provides appraisal management services.<sup>103</sup>



Under Dodd-Frank, the minimum requirements in the proposed rule would apply to states that elect to establish an appraiser-certifying and -licensing agency with the authority to register and supervise AMCs. The proposed rule would not compel a state to establish an AMC registration and supervision program, and there is no penalty imposed on a state that does not establish a regulatory structure for AMCs. Additionally, under the proposed rule, an AMC would be barred from providing appraisal management services for federally related transactions in a state that has not established such a regulatory structure.<sup>104</sup>

### **Appraisal Requirements for Higher-Priced Mortgages**

In December 2013, FHFA and five other federal financial agencies jointly issued a final rule exempting some higher-priced mortgage loans from certain appraisal requirements. Mortgage loans are considered higher priced if they are secured by a consumer's home and have interest rates above a certain threshold. The agencies explained that the exemptions are intended to save borrowers time and money while still ensuring that the loans are financially sound. The appraisal requirements were established as part of Dodd-Frank, which requires creditors to obtain a written appraisal based on a physical visit to the home's interior.<sup>105</sup>

The final rule provides that loans of \$25,000 or less and some "streamlined" refinancings are exempt from the appraisal requirements, which took effect January 18, 2014. The requirements involving manufactured homes will not take effect until July 18, 2015, when loans secured by a new manufactured home and land will be exempt from the requirement that the appraiser visit the home's interior. For loans secured by manufactured homes without land, creditors will be allowed to use other valuation methods, such as third-party valuation services or "book values."<sup>106</sup>

### **Guarantee Fees**

On January 8, 2014, FHFA directed the Enterprises to delay implementation of planned increases in the guarantee fees that they charge for mortgages.<sup>107</sup> The base guarantee fee had been scheduled to rise by 10 **basis points**; the upfront guarantee fee grid was to have been updated to better align pricing with the credit risk characteristics of the borrower; and the upfront 25 basis point adverse market fee was to have been eliminated except in New York, Florida, New Jersey, and Connecticut.<sup>108</sup>

When announcing the delay in implementation, the FHFA Director said he wanted to conduct a thorough evaluation of the proposed increases and would give no less than 120 days' notice before implementing any changes.<sup>109</sup>

The proposed fee increases were announced following FHFA's *A Strategic Plan for Enterprise Conservatorships*, which called for gradually contracting the Enterprises' dominant presence in the marketplace while simplifying and shrinking their operations.<sup>110</sup>

In July 2013, OIG released an evaluation report entitled *FHFA's Initiative to Reduce the Enterprises' Dominant Position in the Housing Finance System by Raising Gradually Their Guarantee Fees*. OIG performed this evaluation to: (1) provide an independent analysis of FHFA's initiative to increase private-sector investment in mortgage credit risk and reduce the Enterprises' dominant position in housing finance through gradual increases in guarantee fees, and (2) assess FHFA's communication and interaction with FHA on pricing initiatives. OIG concluded that FHFA's initiative to encourage private-sector investment in mortgage credit risk and reduce the Enterprises' dominant presence in the housing finance system through guarantee fee increases has the potential to reduce taxpayer exposure to mortgage-related losses by spreading risk to private-sector participants. However, the initiative



faces trade-offs and external challenges that FHFA will have to address to help ensure success.<sup>111</sup>

### Loan Purchase Limits

In December 2013, FHFA sought public input on a proposal to reduce the maximum size of loans that the Enterprises may purchase. The proposal would reduce the statutory maximum loan limit for one-unit properties by approximately 4%. In areas where the maximum is \$417,000, the plan would reduce the loan purchase limit to \$400,000, and in areas where the current limit is \$625,500, the new limit would be set at \$600,000.<sup>112</sup>

According to FHFA, lowering the Enterprises' loan purchase limits would help to reduce the market presence of the Enterprises, which is a key objective of the Agency's strategic plan for the conservatorships. It also addresses President Obama's August 2013 request that FHFA reduce the loan limits in order to shrink the government's footprint in the mortgage market.<sup>113</sup>

### Risk Reduction Initiatives

In October 2013, Fannie Mae completed its first risk-sharing transaction that provided mortgage insurance coverage on a pool of more than \$5 billion in single-family mortgages.<sup>114</sup> The Enterprise also priced its first Connecticut Avenue Securities (C-deals) series transaction—a \$675 million note offering. C-deal notes are unsecured and unguaranteed bonds issued by Fannie Mae that transfer some credit risk to private investors.<sup>115</sup> The amount of periodic principal repayment is determined by the performance of a reference pool of more than 112,000 single-family mortgage loans with an outstanding unpaid principal balance of \$27 billion.<sup>116</sup>

Freddie Mac priced its second credit risk sharing transaction in November 2013, selling \$630 million in Structured Agency Credit Risk (STACR) securities notes, tied to a reference pool of single-family mortgage loans with an outstanding unpaid principal balance of \$23.3 billion. Freddie Mac had previously sold \$500 million in STACR notes in July.<sup>117</sup> Like the Fannie Mae C-deal notes, STACR notes transfer some credit risk to private investors. The notes are unsecured and unguaranteed bonds issued by Freddie Mac, whose principal payments are determined by the delinquency and principal payment experience on a reference pool of mortgages.<sup>118</sup> Freddie Mac also completed a risk-sharing transaction in November by purchasing an insurance policy underwritten by Arch Reinsurance Ltd. to cover up to \$77.4 million of credit losses.<sup>119</sup>

The Enterprises completed these risk-sharing transactions to meet FHFA's *Conservatorship Strategic Plan: Performance Goals for 2013*, which called on each Enterprise to test the viability of multiple types of risk transfer transactions involving single-family mortgages.<sup>120</sup>

### Lawsuits/Settlements

#### FHFA Private-Label MBS Lawsuits

As of March 2014, FHFA had recovered nearly \$16 billion on behalf of taxpayers in 2013 and 2014 through settlements with financial institutions that sold private-label securities to the Enterprises between 2005 and 2007 (see Figure 21, page 60). FHFA had sued 18 institutions alleging securities law violations, and in some cases, fraud.<sup>121</sup>

Three institutions reached settlements during the fourth

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***FHFA has recovered nearly \$16 billion through private-label securities litigation.***

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**Figure 21. FHFA’s Private-Label Securities Settlements to Date**

| Bank                                | Settlement Amount      | Settlement Announcement Date |
|-------------------------------------|------------------------|------------------------------|
| General Electric Company            | \$6.25 million         | January 2013                 |
| CitiGroup Inc.                      | \$250 million          | May 2013                     |
| UBS Americas Inc.                   | \$885 million          | July 2013                    |
| Wells Fargo Bank, N.A. <sup>a</sup> | \$335.23 million       | September 2013               |
| JPMorgan Chase & Co.                | \$4 billion            | October 2013                 |
| Ally Financial Inc.                 | \$475 million          | October 2013                 |
| Deutsche Bank AG                    | \$1.925 billion        | December 2013                |
| Morgan Stanley                      | \$1.25 billion         | February 2014                |
| Société Générale                    | \$122 million          | February 2014                |
| Credit Suisse                       | \$885 million          | March 2014                   |
| Bank of America Corp.               | \$5.83 billion         | March 2014                   |
| <b>Total</b>                        | <b>\$15.96 billion</b> |                              |

<sup>a</sup> The Wells Fargo Bank settlement is a non-litigation private-label securities settlement.

quarter of 2013: JPMorgan Chase & Co., which paid a \$5.1 billion settlement, including \$4 billion to address claims of alleged violations of state and federal securities laws in connection with private-label residential mortgages; Deutsche Bank AG, which agreed to pay \$1.925 billion; and Ally Financial Inc., which agreed to pay \$475 million. Earlier in 2013, three other institutions agreed to settlements: General Electric Company, CitiGroup Inc., and UBS Americas Inc. Further, Wells Fargo Bank, N.A., reached a non-litigation private-label securities settlement and agreed to pay \$335.23 million.<sup>122</sup>

In the first quarter of 2014, additional settlements were made. Bank of America Corp. reached an agreement to pay approximately \$5.83 billion to settle cases involving Bank of America, Countrywide Financial, and Merrill Lynch. Bank of America now owns Countrywide and Merrill Lynch. The agreement provides for an aggregate payment of approximately \$9.33 billion by Bank of America that includes litigation resolution, as well as a purchase of securities by Bank of America from the Enterprises.<sup>123</sup> In addition, Swiss bank Credit Suisse agreed to pay \$885 million in a settlement, Morgan Stanley agreed

to a \$1.25 billion settlement, and French bank Société Générale agreed to pay \$122 million in a settlement.<sup>124</sup>

### **Enterprise Lawsuits Concerning the Conservatorships and the PSPAs**

Between June 2013 and February 2014, several lawsuits were filed by Enterprise shareholders against FHFA disputing the 2012 PSPA amendments. In particular, the lawsuits challenge the net worth sweep dividend provisions.<sup>125</sup>

### **FHFA and GSE Performance and Accountability**

In order to assess FHFA’s and the GSEs’ performance, OIG reviews and analyzes FHFA’s strategic goals and accountability reports. For this period, FHFA released the *2013 Performance and Accountability Report* and the *Progress Report on the Implementation of FHFA’s Strategic Plan for Enterprise Conservatorships*. The key results of these reports, as well as summaries of two notable FHFA directives related to performance and accountability, are discussed below.

## **FHFA's 2013 Performance and Accountability Report**

FHFA's *2013 Performance and Accountability Report* discusses the Agency's accomplishments, challenges, and ongoing initiatives. The following is a list of accomplishments FHFA reported for the fiscal year:

- Provided results and conclusions of 2012 examinations of the Enterprises. The Enterprises were both deemed "critical concerns" but generated positive annual income for the first time since 2006.
- Established CSS, which will manage the development of the CSP and associated data and legal infrastructure.
- Achieved FHFA 2013 Scorecard goals, including the Enterprises' execution of multiple risk-sharing transactions.
- Worked with the Enterprises to complete more than 2.97 million foreclosure prevention actions and launched a national public awareness campaign to educate homeowners about the Home Affordable Refinance Program to increase refinancings.
- Achieved third consecutive year of profitability for all 12 FHLBanks in fiscal year 2013.<sup>126</sup>

## **FHFA's Progress Report on the Implementation of Its Strategic Plan for Enterprise Conservatorships**

In November 2013, FHFA released a progress report on the implementation of initiatives outlined in *A Strategic Plan for Enterprise Conservatorships* and the *Conservatorship Strategic Plan: Performance Goals for 2013*. FHFA summarized the progress that has been made including:

- FHFA and the Enterprises have made progress in the development and initial testing of the CSP; however, challenges remain before full implementation, including necessary changes to the Enterprises' technology and business processes;
- The Enterprises have formally established CSS as the joint venture that will own the CSP and related business and operational functions;
- The Enterprises have each executed multiple risk-sharing transactions totaling more than \$30 billion;
- The Enterprises have been gradually reducing the less liquid portions of their retained portfolios; and
- The Enterprises have completed a review of pre-conservatorship loan acquisitions and have recovered more than \$18 billion in restitution for breaches of selling representations and warranties.<sup>127</sup>

## **Termination of the Enterprises' Pension Plans**

In October 2013, FHFA directed the Enterprises to terminate their defined benefit retirement plans effective December 31, 2013. The plans were previously closed to new entrants. FHFA explained that it terminated the pension plans to reduce risk to the Enterprises and to help conserve the Enterprises' assets.<sup>128</sup>

## **Dodd-Frank Stress Tests**

In November 2013, FHFA sent orders to the GSEs requiring them to report on the results of annual stress tests to determine whether the entities have the capital necessary to absorb losses as a result of adverse economic conditions. Dodd-Frank requires these tests annually for financial companies that have total consolidated assets of \$10 billion or more and are regulated by a primary federal financial regulatory agency.<sup>129</sup>

The GSEs are required to submit the results of stress tests based on three scenarios: baseline, adverse, and severely adverse. The Enterprises and FHLBanks are required to publish their results by April 30, 2014, and July 30, 2014, respectively. For 2013, the Enterprises were also required to conduct additional FHFA-required stress tests—the results of which will be released in the second quarter of 2014.<sup>130</sup>





# Appendices

## Appendix A: Glossary and Acronyms

### Glossary of Terms

**Alternative A:** A classification of mortgages in which the risk profile falls between prime and subprime. Alternative A (also known as Alt-A) mortgages are generally considered higher risk than prime due to factors that may include higher loan-to-value and debt-to-income ratios or limited documentation of the borrower's income.

**Bankruptcy:** A legal procedure for resolving debt problems of individuals and businesses; specifically, a case filed under one of the chapters of Title 11 of the U.S. Code.

**Basis Points:** A hundredth of 1 percentage point. For example, 1 basis point is equivalent to 1/100 of 1 percentage point.

**Bonds:** Obligations by a borrower to eventually repay money obtained from a lender. The buyer of the bond (or "bondholder") is entitled to receive payments from the borrower.

**Capital Gain (Loss):** When a capital asset (e.g., stocks or bonds held as investments) is sold, the difference between the amount paid for the asset and the amount it is sold for is a capital gain or loss. Capital gains occur when the asset sells for more than paid, while capital losses occur when the asset is sold for less than the purchase price.

**Capitalization:** In the context of bank supervision, capitalization refers to the funds a bank holds as a buffer against unexpected losses. It includes

shareholders' equity, loss reserves, and retained earnings. Bank capitalization plays a critical role in the safety and soundness of individual banks and the banking system. In most cases, federal regulators set requirements for adequate bank capitalization.

**Carryforwards:** A provision of tax law that allows current losses or certain tax credits to be utilized in future tax returns.

**Collateral:** Assets used as security for a loan that can be seized by the lender if the borrower fails to repay the loan.

**Commercial Banks:** Commercial banks are establishments primarily engaged in accepting demand and other deposits and making commercial, industrial, and consumer loans. Commercial banks provide significant services in originating, servicing, and enhancing the liquidity and quality of credit that is ultimately funded elsewhere.

**Conforming Loan Limit:** A conforming loan is a conventional loan with an origination balance that does not exceed a specified amount (i.e., conforming loan limit). The Enterprises are restricted by law to purchasing conforming loans, with the loan limits varying by unit size and region, e.g., high-cost areas. The loan limits for 2014 remain unchanged from 2013. For 2014, the maximum general loan limit for a single-family one-unit dwelling is \$417,000, while the maximum high-cost area loan limit for a single-family one-unit dwelling is \$625,500.

**Conservatorship:** Conservatorship is a legal procedure for the management of financial institutions for an interim period during which the institution's conservator assumes responsibility for operating the institution and conserving its assets. Under the Housing and Economic Recovery Act of

2008, the Enterprises entered into conservatorships overseen by FHFA. As conservator, FHFA has undertaken to preserve and conserve the assets of the Enterprises and restore them to safety and soundness. FHFA also has assumed the powers of the boards of directors, officers, and shareholders; however, the day-to-day operational decision making of each company is delegated by FHFA to the Enterprises' existing management.

**Credit-Related Income (Expense):** Comprised of foreclosed property income (expense) and the benefit (provision) for credit losses.

**Credit Unions:** Member-owned, not-for-profit financial cooperatives that provide savings, credit, and other financial services to their members. Credit unions pool their members' savings deposits and shares to finance their own loan portfolios rather than rely on outside capital. Members benefit from higher returns on savings, lower rates on loans, and fewer fees on average.

**Default:** Occurs when a mortgagor misses one or more payments.

**Deferred Tax Assets:** Deferred tax assets are recognized for temporary differences that will result in deductible amounts and for carryforwards. For example, a temporary difference is created between the reported amount and the tax basis of a liability for estimated expenses if, for tax purposes, those estimated expenses are not deductible until a future year.

**Derivatives:** A financial contract whose value depends on that of another asset, such as a stock or bond. A derivative contract is, essentially, an agreement providing parties to the agreement with the obligation or the choice to buy, sell, or exchange

something at a future date. They may be used to hedge interest rate or other risks related to holding a mortgage.

**Derivative Gains (Losses):** The Enterprises acquire and guarantee primarily longer-term mortgages and securities that are funded with debt instruments. The companies manage the interest rate risk associated with these investments and funding activities with derivative agreements. The gains (losses) on derivative agreements are caused by changes in interest rates that, in turn, cause a net increase (decrease) in the fair value of these agreements.

**Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010:** Legislation that intends to promote the financial stability of the United States by improving accountability and transparency in the financial system, ending "too big to fail," protecting the American taxpayer by ending bailouts, and protecting consumers from abusive financial services practices.

**Emergency Economic Stabilization Act of 2008:** Legislation that authorizes Treasury to undertake specific measures to provide stability and prevent disruption in the financial system and the economy. It also provides funds to preserve homeownership.

**Fannie Mae:** A federally chartered corporation that purchases residential mortgages and pools them into securities that are sold to investors; by purchasing mortgages, Fannie Mae supplies funds to lenders so they may make loans to homebuyers.

**Federal Home Loan Banks:** The FHLBanks are 12 regional cooperative banks that U.S. lending institutions use to finance housing and economic development in their communities. Created by Congress, the FHLBanks have been the largest

source of funding for community lending for eight decades. The FHLBanks provide loans (or “advances”) to their member banks but do not lend directly to individual borrowers.

**Federal Housing Administration:** Part of HUD, FHA insures residential mortgages made by approved lenders against payment losses. It is the largest insurer of mortgages in the world, insuring over 34 million properties since its inception in 1934.

**Foreclosure:** A legal process used by a lender to obtain possession of a mortgaged property in order to repay part or all of the debt.

**Freddie Mac:** A federally chartered corporation that purchases residential mortgages, pools them into securities, and sells them to investors. By purchasing mortgages, Freddie Mac supplies funds to lenders so they make loans to homebuyers.

**Ginnie Mae:** A government-owned corporation within HUD. Ginnie Mae guarantees investors the timely payment of principal and interest on privately issued MBS backed by pools of government-insured and -guaranteed mortgages.

**Government-Sponsored Enterprises:** Business organizations chartered and sponsored by the federal government.

**Government-Sponsored Enterprise Mortgage-Backed Securities Purchase Facility:** The function of the GSE MBS Purchase Facility was to help improve the availability of mortgage credit to American homebuyers and mitigate pressures on mortgage rates. To promote the stability of the mortgage market, Treasury purchased GSE MBS in the secondary market. By purchasing these securities, Treasury sought to broaden access to mortgage funding for current and prospective homeowners, as well as to promote market stability.

**Guarantee:** A pledge to investors that the guarantor will bear the default risk on a pool of loans or other collateral.

**Hedging:** The practice of taking an additional step, such as buying or selling a derivative, to offset certain risks associated with holding a particular investment, such as MBS.

**Held-to-Maturity Security:** A debt security (obligation or liability) that management intends to hold to its maturity or payment date and whose cash value is not needed until that date.

**Housing and Economic Recovery Act of 2008:** Legislation that establishes OIG and FHFA, which oversee the GSEs’ operations. HERA also expanded Treasury’s authority to provide financial support to the GSEs.

**Implied Guarantee:** The assumption, prevalent in the financial markets, that the federal government will cover Enterprise debt obligations.

**Inspector General Act of 1978:** Legislation that authorizes establishment of offices of inspectors general, “independent and objective units” within federal agencies, that: (1) conduct and supervise audits and investigations relating to the programs and operations of their agencies; (2) provide leadership and coordination and recommend policies for activities designed to promote economy, efficiency, and effectiveness in the administration of agency programs and to prevent and detect fraud, waste, or abuse in such programs and operations; and (3) provide a means for keeping the head of the agency and Congress fully and currently informed about problems and deficiencies relating to the administration of such programs and operations and the necessity for and progress of corrective action.

**Inspector General Reform Act of 2008:** Legislation that amends the Inspector General Act to enhance the independence of inspectors general and

to create the Council of the Inspectors General on Integrity and Efficiency.

**Insurance Company:** A company whose primary and predominant business activity is the writing of insurance and issuing or underwriting “covered products.”

**Interest Rate Swap:** An interest rate swap is an agreement in which two parties make interest payments to each other for a set period based upon a notional principal. The notional principal is only used to calculate the interest payments; no risk is attached to it. Interest rate swaps commonly involve exchanging payments based on a fixed interest rate for payments based on a floating rate (e.g., London Interbank Offered Rate). The fixed rate is known as the swap rate.

**Internal Controls:** Internal controls are an integral component of an organization’s management that provide reasonable assurance that the following objectives are achieved: (1) effectiveness and efficiency of operations, (2) reliability of financial reports, and (3) compliance with applicable laws and regulations. Internal controls relate to management’s plans, methods, and procedures used to meet its mission, goals, and objectives and 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.

**Joint and Several Liability:** The concept of joint and several liability provides that each member in a group is responsible for the debts of all in that group. In the case of the FHLBanks, if any individual FHLBank were unable to pay a creditor, the other 11—or any 1 or more of them—would be required to step in and cover that debt.

**Loan-to-Value:** A percentage calculated by dividing the amount borrowed by the price or appraised value of the home to be purchased; the higher the

loan-to-value (also known as LTV), the less cash a borrower is required to pay as down payment.

**Mortgage-Backed Securities:** MBS are debt securities that represent interests in the cash flows—anticipated principal and interest payments—from pools of mortgage loans, most commonly on residential property.

**Operational Risk:** Exposure to loss resulting from inadequate or failed internal processes, people, and systems or from external events (including legal events).

**Options:** Contracts that give the buyer the right, but not the obligation, to buy or sell a specified quantity of a commodity or other instrument at a specific price within a specified period of time, regardless of the market price of that instrument.

**Preferred Stock:** A security that usually pays a fixed dividend and gives the holder a claim on corporate earnings and assets superior to that of holders of common stock but inferior to that of investors in the corporation’s debt securities.

**Private-Label Mortgage-Backed Securities:** MBS issued or guaranteed by entities other than GSEs or federal government agencies. They do not carry an explicit or implicit government guarantee, and the private-label MBS investor bears the risk of losses on its investment.

**Real Estate Owned:** Foreclosed homes owned by government agencies or financial institutions, such as the Enterprises or real estate investors. REO homes represent collateral seized to satisfy unpaid mortgage loans. The investor or its representative then must sell the property on its own.

**Securitization:** A process whereby a financial institution assembles pools of income-producing assets (such as loans) and then sells securities representing an interest in the assets’ cash flows to investors.

**Securitization Platform:** A mechanism that connects capital market investors to borrowers by bundling mortgages into securities and tracking loan payments.

**Senior Preferred Stock Purchase Agreements:** Entered into at the time the conservatorships were created, the PSPAs authorize the Enterprises to request and obtain funds from Treasury, among other matters. Under the PSPAs, the Enterprises agreed to consult with Treasury concerning a variety of significant business activities, capital stock issuance, dividend payments, ending the conservatorships, transferring assets, and awarding executive compensation.

**Servicers:** Servicers act as intermediaries between mortgage borrowers and owners of the loans, such as the Enterprises or MBS investors. They collect the homeowners' mortgage payments, remit them to the owners of the loans, maintain appropriate records, and address delinquencies or defaults on behalf of the owners of the loans. For their services, they typically receive a percentage of the unpaid principal balance of the mortgage loans they service. The recent financial crisis has put more emphasis on servicers' handling of defaults, modifications, short sales, and foreclosures, in addition to their more traditional duty of collecting and distributing monthly mortgage payments.

**Short Sale:** The sale of a mortgaged property for less than what is owed on the mortgage.

**Straw Buyer:** A straw buyer is a person whose credit profile is used to serve as a cover in a loan transaction. Straw buyers are chosen for their ability to qualify for a mortgage loan, causing loans that would ordinarily be declined to be approved. Straw buyers may be paid a fee for their involvement in purchasing a property and usually never intend to own or occupy the property.

**Swaption:** An option on a swap that gives the holder the right, but not the obligation, to enter, for example, into an interest rate swap as either the payer or the receiver of the fixed side of the swap.

**Thrift:** A financial institution that ordinarily possesses the same depository, credit, financial intermediary, and account transactional functions as a bank but that is chiefly organized and primarily operates to promote savings and home mortgage lending rather than commercial lending.

**Underwater:** Term used to describe situations in which the homeowner's equity is below zero (i.e., the home is worth less than the balance of the loan(s) it secures).

**Underwriting:** The process of analyzing a loan application to determine the amount of risk involved in making the loan; it includes a review of the potential borrower's credit worthiness and an assessment of the property value.

**Valuation Allowance:** Method of lowering or raising an object's current value by adjusting its acquisition cost to reflect its market value by offsetting another account. A valuation allowance is recognized if, based on the weight of available evidence, it is more likely than not that some portion or all of a deferred tax asset will not be realized.



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## Acronyms and Abbreviations

|                        |   |                       |   |
|------------------------|---|-----------------------|---|
| <b>Agency</b>          | Federal Housing Finance Agency                                    | <b>FHLBank System</b> | Federal Home Loan Bank System   |
| <b>AMC</b>             | Appraisal Management Company                                      | <b>FIRREA</b>         | Financial Institutions Reform, Recovery and Enforcement Act of 1989     |
| <b>ATSC</b>            | Advanced Technology Systems, Inc.                                 | <b>FISMA</b>          | Federal Information Security Management Act of 2002                     |
| <b>Blue Book</b>       | <i>Quality Standards for Inspection and Evaluation</i>            | <b>FSOC</b>           | Financial Stability Oversight Council                                   |
| <b>C-deals</b>         | Connecticut Avenue Securities                                     | <b>GAGAS</b>          | <i>Generally Accepted Government Auditing Standards</i>                 |
| <b>Charge Card Act</b> | Government Charge Card Abuse Prevention Act of 2012               | <b>GAO</b>            | Government Accountability Office  |
| <b>CIGFO</b>           | Council of Inspectors General on Financial Oversight              | <b>GSEs</b>           | Government-Sponsored Enterprises  |
| <b>CIGIE</b>           | Council of the Inspectors General on Integrity and Efficiency     | <b>HAFA</b>           | Home Affordable Foreclosure Alternatives                                |
| <b>CSP</b>             | Common Securitization Platform                                    | <b>HERA</b>           | Housing and Economic Recovery Act of 2008                               |
| <b>CSS</b>             | Common Securitization Solutions, LLC                              | <b>HUD</b>            | Department of Housing and Urban Development                             |
| <b>DHMG</b>            | Division of Housing Mission and Goals                             | <b>HUD-OIG</b>        | Department of Housing and Urban Development Office of Inspector General |
| <b>Dodd-Frank</b>      | Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 | <b>IPIA</b>           | Improper Payments Information Act of 2002                               |
| <b>DOJ</b>             | Department of Justice   | <b>IRS-CI</b>         | IRS-Criminal Investigation  |
| <b>Enterprises</b>     | Fannie Mae and Freddie Mac  | <b>LTV</b>            | Loan-to-Value   |
| <b>EO</b>              | Executive Office  | <b>MBS</b>            | Mortgage-Backed Securities  |
| <b>FAR</b>             | Federal Acquisition Regulation                                    | <b>MCC</b>            | Merchant Category Code  |
| <b>FCC OIG</b>         | Federal Communications Commission Office of Inspector General     | <b>MSR</b>            | Mortgage Servicing Rights   |
| <b>FDIC</b>            | Federal Deposit Insurance Corporation                             | <b>OA</b>             | Office of Audits  |
| <b>FDIC-OIG</b>        | Federal Deposit Insurance Corporation Office of Inspector General | <b>OAd</b>            | Office of Administration  |
| <b>FHA</b>             | Federal Housing Administration                                    | <b>OC</b>             | Office of Counsel   |
| <b>FHFA</b>            | Federal Housing Finance Agency                                    | <b>OE</b>             | Office of Evaluations   |
| <b>FHLBanks</b>        | Federal Home Loan Banks   | <b>OI</b>             | Office of Investigations  |



|              |   |                        |  |
|--------------|---|------------------------|--|
| <b>OIG</b>   | Federal Housing Finance Agency<br>Office of Inspector General | <b>REO</b>             | Real Estate Owned  |
| <b>OMB</b>   | Office of Management and Budget                               | <b>RMBS</b>            | Residential Mortgage-Backed Securities   |
| <b>OQA</b>   | Office of Quality Assurance                                   | <b>SAI</b>             | Servicing Alignment Initiative   |
| <b>OR</b>    | Office of Oversight and Review                                | <b>SEC</b>             | Securities and Exchange Commission   |
| <b>PAR</b>   | Performance and Accountability Report                         | <b>SIGTARP</b>         | Office of the Special Inspector General<br>for the Troubled Asset Relief Program |
| <b>PFCRA</b> | Program Fraud Civil Remedies Act of<br>1986                   | <b>STACR</b>           | Structured Agency Credit Risk  |
| <b>PII</b>   | Personal Identifying Information                              | <b>Treasury</b>        | Department of the Treasury   |
| <b>PSPAs</b> | Senior Preferred Stock Purchase<br>Agreements                 | <b>USPIS</b>           | Postal Inspection Service  |
|              |   | <b>Yellow<br/>Book</b> | <i>Government Auditing Standards</i>   |



## **Appendix B: OIG Recommendations**

In accordance with the provisions of the Inspector General Act, one of the key duties of OIG is to provide to FHFA recommendations that promote the transparency, efficiency, and effectiveness of the

Agency's operations and aid in the prevention and detection of fraud, waste, or abuse. Figure 22 (see page 77) summarizes OIG's formal recommendations that were made, pending, or closed during the reporting period. Figure 23 (see page 98) lists OIG's audit and evaluation reports for which all of the recommendations were closed in prior semiannual periods.

**Figure 22. Summary of OIG Recommendations**

| No.                   | Recommendation  | Report   | Status  |
|-----------------------|---|--|---|
| <b>AUD-2014-012-1</b> | FHFA should direct the Enterprises to jointly assess the effectiveness of their pre-foreclosure property inspection processes. OIG identified several specific areas to review as part of the assessment, including: (1) identifying pre-foreclosure property inspection risk and objectives, (2) identifying cost-effective control alternatives for achieving the objective(s), and (3) recommending inspection standards and quality controls with regard to the content and frequency of inspections. | <i>FHFA Oversight of Enterprise Controls Over Pre-Foreclosure Property Inspections</i> | Recommendation partially agreed to by FHFA; implementation of recommendation pending.               |
| <b>AUD-2014-012-2</b> | Based on the results of the Enterprises' assessment of their pre-foreclosure property inspection processes, FHFA should direct the Enterprises to establish uniform pre-foreclosure inspection quality standards and quality control processes for inspectors.  | <i>FHFA Oversight of Enterprise Controls Over Pre-Foreclosure Property Inspections</i> | Recommendation not accepted by FHFA; recommendation remains open and will continue to be monitored. |
| <b>AUD-2014-010-1</b> | FHFA should enhance travel and travel card controls to improve compliance with applicable regulations, policies, and procedures by notifying employees that all travel should have properly approved authorizations prior to commencing travel.   | <i>FHFA's Use of Government Travel Cards</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-010-2</b> | FHFA should enhance travel and travel card controls to improve compliance with applicable regulations, policies, and procedures by notifying employees to complete travel vouchers in a timely manner upon completion of travel.  | <i>FHFA's Use of Government Travel Cards</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-010-3</b> | FHFA should enhance travel and travel card controls to improve compliance with applicable regulations, policies, and procedures by performing a periodic review of travel cardholder ATM limits.  | <i>FHFA's Use of Government Travel Cards</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |

| No.                   | Recommendation   | Report  | Status  |
|-----------------------|--|---|---|
| <b>AUD-2014-010-4</b> | FHFA should enhance travel and travel card controls to improve compliance with applicable regulations, policies, and procedures by notifying employees that they should obtain cash advances either during or immediately preceding travel.  | <i>FHFA's Use of Government Travel Cards</i>                            | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-009-1</b> | FHFA should promptly quantify the potential benefit of implementing a repurchase late fee program at Fannie Mae, and then determine whether the potential cost of from \$500,000 to \$5.4 million still outweighs the potential benefit.   | <i>FHFA Oversight of Enterprise Handling of Aged Repurchase Demands</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-009-2</b> | FHFA should direct Freddie Mac to develop a repurchase late fee report to be given routinely to FHFA that expands on information already provided by adding summary information by seller on outstanding repurchases, aging of repurchases, late fees assessed and collected, discretionary late fee waivers, and global late fee exclusions. Such a report would provide Freddie Mac and FHFA management with needed information to manage and assess Freddie Mac's repurchase late fee program more effectively. | <i>FHFA Oversight of Enterprise Handling of Aged Repurchase Demands</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-009-3</b> | FHFA should direct Freddie Mac to provide FHFA with information on any assessed but uncollected late fees associated with the repurchase claims that are included in the 2013 bulk settlements so that these fees can be considered in the negotiations and documented in accordance with the Office of Conservatorship Operations' Settlement Policy.   | <i>FHFA Oversight of Enterprise Handling of Aged Repurchase Demands</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |



| No.                   | Recommendation  | Report  | Status  |
|-----------------------|---|---|---|
| <b>AUD-2014-008-1</b> | FHFA should perform supervisory review and follow-up to ensure that Fannie Mae takes action to change the portal message type from automatic override to manual override or fatal for the 25 proprietary messages related to underwriting requirements, which will require lenders to take action to address the appraisal-related messages warning of potential underwriting violations prior to delivering the loans. | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-2</b> | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to develop and implement additional proprietary messages related to its property underwriting requirements.  | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-3</b> | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to establish the additional proprietary messages related to property underwriting requirements as manual override or fatal, which will require the lenders to take action to address the messages prior to delivering the loans.   | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-4</b> | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to review the type of message related to the existing nine proprietary messages for consideration of converting the type of message from automatic override to manual override or fatal, which will require the lenders to take action to address the messages prior to delivering the loans.                              | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-5</b> | FHFA should perform supervisory review of both Enterprises to ensure the portal warning messages distinguish between inactive appraisers and unverified appraisers, as of the date the appraisal is performed.  | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |

| No.                    | Recommendation  | Report  | Status  |
|------------------------|---|---|---|
| <b>AUD-2014-008-6</b>  | FHFA should perform supervisory review of both Enterprises to ensure that the portal tests whether appraisers are licensed and active at the time the appraisal is performed.   | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-7</b>  | FHFA should perform supervisory review of both Enterprises to change the message type, for messages relating to appraiser license status, from automatic override to manual override or fatal, which will require lenders to take action to address the message prior to delivering the loan. This action can be taken once the system logic is fixed and the historical records are available to determine the status of an appraiser's license at the time the appraisal work is performed, and the states are updating in real time. | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-8</b>  | FHFA should perform supervisory review of both Enterprises to seek remedy for the 23 loans, valued at \$3.4 million, delivered to the Enterprises by the two suspended appraisers in violation of underwriting requirements.  | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-9</b>  | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to implement an internal control policy and related procedures to follow up on appraisal license status messages generated by the portal.  | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-10</b> | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to review loans purchased since the portal's inception that generated messages related to the appraiser's license status.  | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |

| No.                    | Recommendation  | Report  | Status  |
|------------------------|---|---|---|
| <b>AUD-2014-008-11</b> | FHFA should perform supervisory review and follow-up to ensure that Freddie Mac takes action to use the results of the review to repurchase the loans that contained appraisals that were performed by unlicensed appraisers, as appropriate. | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-12</b> | FHFA should pursue retention of historical records of the status of appraisers' licenses in the National Registry of Appraisers sufficient to determine the status of appraisers' licenses at the time the appraisal work is performed.       | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-13</b> | FHFA should pursue having the National Registry of Appraisers updated to reflect the status of state-certified and -licensed appraisers on a real-time basis.   | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-008-14</b> | FHFA should perform supervisory review and follow-up to ensure that the Enterprises develop and implement the portal as intended by FHFA's uniform mortgage data program directive.   | <i>FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-006-1</b>  | FHFA should document purchase card policies and procedures related to the purchase of training above the \$5,000 micro-purchase threshold.  | <i>FHFA's Use of Government Purchase Cards</i>  | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-006-2</b>  | FHFA should document purchase card policies and procedures related to the use of employee Continued Service Agreements for high-cost training.  | <i>FHFA's Use of Government Purchase Cards</i>  | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-006-3</b>  | FHFA should document purchase card policies and procedures related to the approval and resetting of temporary increases in transactions limits in a cardholder's purchase authority.  | <i>FHFA's Use of Government Purchase Cards</i>  | Recommendation agreed to by FHFA; implementation of recommendation pending. |

| No.                   | Recommendation  | Report   | Status  |
|-----------------------|---|--|---|
| <b>AUD-2014-006-4</b> | FHFA should document purchase card policies and procedures related to the management of MCC exceptions, which should be allowed only on a case-by-case basis and removed in a timely manner after the allowed purchase is transacted.   | <i>FHFA's Use of Government Purchase Cards</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-005-1</b> | FHFA should direct Fannie Mae to obtain a refund from servicers for improperly reimbursed property inspection claims, resulting in estimated funds put to better use of \$5,015,505.  | <i>FHFA Oversight of Fannie Mae's Reimbursement Process for Pre-Foreclosure Property Inspections</i>                         | Closed—Final action taken by FHFA.  |
| <b>AUD-2014-005-2</b> | FHFA should direct Fannie Mae to implement controls in the invoice management system to reject pre-foreclosure property inspection claims over established tolerance limits.  | <i>FHFA Oversight of Fannie Mae's Reimbursement Process for Pre-Foreclosure Property Inspections</i>                         | Recommendation not accepted by FHFA; recommendation remains open and will continue to be monitored. |
| <b>AUD-2014-005-3</b> | FHFA should direct Fannie Mae to submit guidance to all servicers that reminds them of requirements to adhere to reimbursement tolerance limits for pre-foreclosure property inspection claims.   | <i>FHFA Oversight of Fannie Mae's Reimbursement Process for Pre-Foreclosure Property Inspections</i>                         | Closed—Final action taken by FHFA.  |
| <b>AUD-2014-005-4</b> | FHFA should assess the need for examination coverage related to reimbursement of pre-foreclosure property inspection claims.  | <i>FHFA Oversight of Fannie Mae's Reimbursement Process for Pre-Foreclosure Property Inspections</i>                         | Closed—Final action taken by FHFA.  |
| <b>AUD-2014-004-1</b> | FHFA should review Fannie Mae's remediation plan to ensure that the plan provides for the return of borrower contributions to borrowers in a consistent manner by Fannie Mae and its servicers, and issue guidance as deemed appropriate regarding the execution of the remediation plan. | <i>FHFA Oversight of Fannie Mae's Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties</i> | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |

| No.                   | Recommendation  | Report   | Status  |
|-----------------------|---|--|---|
| <b>AUD-2014-004-2</b> | FHFA should oversee the execution of Fannie Mae's remediation plan to ensure that a good faith effort is made to promptly refund inappropriately collected borrower contributions to borrowers.   | <i>FHFA Oversight of Fannie Mae's Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties</i> | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-004-3</b> | FHFA should examine Freddie Mac's controls over the collection of borrower contributions for the short sales of properties located in California, and issue guidance to strengthen controls as deemed appropriate based on the results of the examination.  | <i>FHFA Oversight of Fannie Mae's Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties</i> | OIG deems recommendation unresolved. Resolution is still pending, and recommendation is still open. |
| <b>AUD-2014-003-1</b> | To strengthen controls over short sales, FHFA should direct Fannie Mae to enforce the requirement that all borrowers not eligible for the Streamlined Documentation Program provide a borrower-certified Uniform Borrower Assistance Form and supporting documentation in order to make eligibility determinations and assess borrower contributions. | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i>                               | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-003-2</b> | To strengthen controls over short sales, FHFA should direct Fannie Mae to establish controls to identify and resolve inconsistencies between the Uniform Borrower Assistance Form and supporting information used in making short sale eligibility determinations.  | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i>                               | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>AUD-2014-003-3</b> | To strengthen controls over short sales, FHFA should direct Fannie Mae to assess its servicer compensation structure to determine if it should consider the quality of borrower eligibility determinations for short sales and success in limiting losses including through contributions by borrowers with the ability to pay.                       | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i>                               | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |



| No.                   | Recommendation  | Report   | Status  |
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| <b>AUD-2014-003-4</b> | To strengthen controls over short sales, FHFA should direct Fannie Mae to enhance controls over collection and use of electronic information from servicers on the financial condition of borrowers to ensure data is reliable and effectively used in both borrower eligibility and servicer performance evaluation processes. | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2014-003-5</b> | FHFA should review the Streamlined Documentation Program to determine whether the program should be available to borrowers seeking approval to short sell non-owner-occupied properties.  | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2014-003-6</b> | FHFA should provide examination coverage of Fannie Mae's short sale activities with particular emphasis on identifying systemic deficiencies related to borrower submissions, Enterprise eligibility determinations, servicer compensation structure, and reliability of electronic information used in managing short sales.   | <i>Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-1</b> | FHFA should update the policy of the Office of Quality Assurance (OQA) to require management to provide written responses and corrective action timelines to OQA findings.  | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>                       | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-2</b> | FHFA should track the corrective action timelines provided by management and follow up on corrective actions based on those timelines.  | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>                       | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-3</b> | FHFA should implement a policy to escalate to the appropriate level of management when corrective action is not implemented by the reported deadline.   | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>                       | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-4</b> | FHFA should evaluate management corrective actions and document evidence supporting closure of its recommendations.   | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>                       | Recommendation agreed to by FHFA; implementation of recommendation pending. |

| No.                   | Recommendation  | Report   | Status  |
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| <b>AUD-2013-013-5</b> | FHFA should evaluate the roles and responsibilities of OQA across the Agency and revise OQA's charter accordingly.  | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-6</b> | FHFA should assess risks across all Agency operations for purposes of planning OQA review coverage.   | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-013-7</b> | FHFA should direct performance of reviews of those areas that pose the most significant risk to FHFA.   | <i>FHFA Can Strengthen Controls over Its Office of Quality Assurance</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-012-1</b> | FHFA should establish verification controls to ensure Enterprise contractors are performing in accordance with agreed criteria and that any proposed waivers to the criteria are documented and submitted for FHFA review and approval.   | <i>Additional FHFA Oversight Can Improve the Real Estate Owned Pilot Program</i>   | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-012-2</b> | FHFA should clarify guidance regarding submission of financial statements and explanation of adverse financial events as part of the bidder qualification process.  | <i>Additional FHFA Oversight Can Improve the Real Estate Owned Pilot Program</i>   | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-012-3</b> | FHFA should issue formal guidance for the REO disposition program, including the REO Pilot Program, requiring a program plan with clearly defined goals and objectives, a program monitoring and oversight mechanism, criteria to measure and evaluate program success, and the means to assess alternative REO disposition strategies. | <i>Additional FHFA Oversight Can Improve the Real Estate Owned Pilot Program</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-010-1</b> | FHFA should evaluate periodically the efficiency and effectiveness of Freddie Mac's deficiency recovery strategies for the pursuit of borrowers with the ability to repay.  | <i>FHFA Can Improve Its Oversight of Freddie Mac's Recoveries from Borrowers Who Possess the Ability to Repay Deficiencies</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |

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| <b>AUD-2013-010-2</b> | FHFA should review Freddie Mac's monitoring controls over its servicers, foreclosure attorneys, and collection vendors involved in deficiency recovery activities to ensure that oversight across these counterparties is maintained.   | <i>FHFA Can Improve Its Oversight of Freddie Mac's Recoveries from Borrowers Who Possess the Ability to Repay Deficiencies</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-010-3</b> | FHFA should direct Freddie Mac to enforce controls for its counterparties to deliver timely documents to deficiency recovery vendors necessary to calculate and pursue deficiencies, and provide for financial consequences for counterparties that fail to meet delivery deadlines.  | <i>FHFA Can Improve Its Oversight of Freddie Mac's Recoveries from Borrowers Who Possess the Ability to Repay Deficiencies</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-010-4</b> | FHFA should direct Freddie Mac to implement a control to consider time frames in state statutes of limitations when prioritizing, coordinating, and monitoring deficiency collection activity for borrowers with the ability to repay.  | <i>FHFA Can Improve Its Oversight of Freddie Mac's Recoveries from Borrowers Who Possess the Ability to Repay Deficiencies</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-009-1</b> | To strengthen its Enterprise information security and privacy programs, FHFA should define and issue Enterprise information security and privacy program requirements.  | <i>Action Needed to Strengthen FHFA Oversight of Enterprise Information Security and Privacy Programs</i>                      | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-009-2</b> | To strengthen its Enterprise information security and privacy programs, FHFA should implement the workforce plan and ensure the plan of action addresses the need to have an adequate number of information technology examiners. Specifically, FHFA should provide an appropriate level of management oversight during the annual supervisory examination planning and execution processes to ensure completion of the annual plan and compliance with established information technology examination policies and procedures. | <i>Action Needed to Strengthen FHFA Oversight of Enterprise Information Security and Privacy Programs</i>                      | Recommendation agreed to by FHFA; implementation of recommendation pending. |

| No.                   | Recommendation  | Report  | Status  |
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| <b>AUD-2013-009-3</b> | To strengthen its Enterprise information security and privacy programs, FHFA should ensure that planning for future information technology examinations is based on fully executed risk assessments, as required by FHFA policy.  | <i>Action Needed to Strengthen FHFA Oversight of Enterprise Information Security and Privacy Programs</i>   | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-009-4</b> | To strengthen its Enterprise information security and privacy programs, FHFA should consistently deploy the automated tools needed for ongoing monitoring and tracking of previously identified security and privacy issues in order to enhance the efficiency and effectiveness of the examination process.                          | <i>Action Needed to Strengthen FHFA Oversight of Enterprise Information Security and Privacy Programs</i>   | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-009-5</b> | To strengthen its Enterprise information security and privacy programs, FHFA should establish and document a process for placing formal reliance on the work of internal audit divisions at the Enterprises.  | <i>Action Needed to Strengthen FHFA Oversight of Enterprise Information Security and Privacy Programs</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-008-1</b> | FHFA should develop a risk-based plan to monitor the Enterprises' oversight of their counterparties' compliance with contractual representations and warranties, including those related to federal consumer protection laws.   | <i>FHFA Should Develop and Implement a Risk-Based Plan to Monitor the Enterprises' Oversight of Their Counterparties' Compliance with Contractual Requirements Including Consumer Protection Laws</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-1</b> | To improve servicer compliance with escalated case requirements, FHFA should perform supervisory review and follow up to ensure that Freddie Mac requires its servicers to report escalated consumer complaint information—to include a negative response if servicers have not received any escalated complaints—on a monthly basis. | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i>   | Recommendation agreed to by FHFA; implementation of recommendation pending. |

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| <b>AUD-2013-007-2</b> | To improve servicer compliance with escalated case requirements, FHFA should perform supervisory review and follow up to ensure that Freddie Mac requires its servicers to resolve escalated consumer complaint information within 30 days.  | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-3</b> | To improve servicer compliance with escalated case requirements, FHFA should perform supervisory review and follow up to ensure that Freddie Mac requires its servicers to categorize resolved escalated consumer complaint information in accordance with resolution categories defined in the servicing guide.                                 | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-4</b> | To enhance Freddie Mac's oversight of its servicers, FHFA should perform supervisory review and follow up to ensure that Freddie Mac includes testing of servicers' performance for handling and reporting escalated cases as part of its reviews of servicers' performance.   | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-5</b> | To enhance Freddie Mac's oversight of its servicers, FHFA should perform supervisory review and follow up to ensure that Freddie Mac identifies and addresses servicer operational challenges with implementing the escalated case requirements as part of the testing of the servicers' performance for handling and reporting escalated cases. | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-6</b> | To enhance Freddie Mac's oversight of its servicers, FHFA should perform supervisory review and follow up to ensure that Freddie Mac establishes penalties in the servicing guide, such as fines or fees, for servicers' lack of reporting escalated cases.  | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |



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| <b>AUD-2013-007-7</b> | To enhance Freddie Mac's oversight of its servicers, FHFA should perform supervisory review and follow up to ensure that Freddie Mac expands the servicer scorecard and servicer performance evaluations to include reporting of escalated cases.  | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-8</b> | To enhance Freddie Mac's oversight of its servicers, FHFA should perform supervisory review and follow up to ensure that Freddie Mac provides information on escalated cases received from servicers to internal staff (the counterparty operational risk evaluation team) responsible for testing servicer performance. | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-007-9</b> | To improve its own oversight, FHFA should develop and implement FHFA examination guidance related to Enterprise implementation and compliance with FHFA directives.  | <i>Enhanced FHFA Oversight Is Needed to Improve Mortgage Servicer Compliance with Consumer Complaint Requirements</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2013-002-1</b> | The FHFA contracting officer should review the total unallowable payments of \$256,343 made to Advanced Technology Systems, Inc. (ATSC), under the contract/task order and recapture the amounts identified as not allocable (\$21,329), unreasonable (\$47,743), and unsupported (\$187,271).                           | <i>FHFA's Oversight of Contract No. FHF-10-F-0007 with Advanced Technology Systems, Inc.</i>                          | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2013-002-2</b> | The FHFA contracting officer should determine whether additional corrective actions are warranted to recapture additional unreasonable costs billed by ATSC to FHFA after November 2011. (OIG did not review charges submitted after November 30, 2011.)   | <i>FHFA's Oversight of Contract No. FHF-10-F-0007 with Advanced Technology Systems, Inc.</i>                          | Recommendation agreed to by FHFA; implementation of recommendation pending. |

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| <b>AUD-2013-002-3</b> | <p>The FHFA contracting officer's representative should revisit this contract/task order and perform the necessary analysis to ensure that ATSC employees had the education background and experience as required under the General Services Administration master contract. The FHFA contracting officer should recapture all expenses, when applicable, paid to the contractor for employees working in positions without proper qualifications.</p>  | <p><i>FHFA's Oversight of Contract No. FHF-10-F-0007 with Advanced Technology Systems, Inc.</i></p> | <p>Recommendation agreed to by FHFA; implementation of recommendation pending.</p> |
| <b>AUD-2013-002-4</b> | <p>The Director of the Office of Budget and Financial Management should issue guidance to all acquisition staff and approving officials, including contracting officers and contracting officer's representatives, on:</p> <ul style="list-style-type: none"> <li>• cost allocation and proper procedures for assigning costs to contracts in accordance with benefits received and based on the appropriate cost objective;</li> <li>• proper procedures for ensuring that contract employees meet labor category qualifications specified in time and material/labor hour contracts;</li> <li>• proper procedures for obtaining sufficient justification prior to increasing funds, adjusting fixed labor rates, and approving payments on time and material contracts;</li> <li>• appropriate procedures for evaluating contractor price proposals and documenting the Agency's pre-negotiation position prior to awarding contract modifications; and</li> <li>• appropriate use of contractor employees to substitute for internal Agency positions and approving invoices based on contractual terms and provisions.</li> </ul> | <p><i>FHFA's Oversight of Contract No. FHF-10-F-0007 with Advanced Technology Systems, Inc.</i></p> | <p>Closed—Final action taken by FHFA.</p>  |

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| <b>AUD-2013-002-5</b>  | The FHFA contracting officer should remove the \$105,000 of excess funds from contract line item number 1 to account for technical writing services ATSC was no longer required to perform under the contract line item number. Thereafter, the contracting officer should compare the new contract ceiling to the actual amount ATSC billed against contract line item number 1 and recapture any unallowable costs that exceed the new ceiling price.   | <i>FHFA's Oversight of Contract No. FHF-10-F-0007 with Advanced Technology Systems, Inc.</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2012-008-1</b>  | FHFA should reassess the nondelegated authorities to ensure sufficient FHFA involvement with major business decisions.  | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA.  |
| <b>AUD-2012-008-2</b>  | FHFA should evaluate the internal controls established by the Enterprises, including policies and procedures, to ensure they communicate all major business decisions requiring approval to the Agency.   | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>AUD-2012-008-3A</b> | FHFA should evaluate Fannie Mae's mortgage pool policy commutations to determine whether these transactions were appropriate and in the best interest of the Enterprise and taxpayers. This evaluation should include an assessment of Fannie Mae's methodology used to determine the economic value of the seven mortgage pool policy commutations. This assessment should include a documented review of Fannie Mae's analysis, the adequacy of the model(s) and assumptions used by Fannie Mae to determine the amount of insurance in force, fair value of the mortgage pool policies, premiums forgone, any other factors incorporated into Fannie Mae's analysis, and the accuracy of the information supplied to FHFA. | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA.  |

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| <b>AUD-2012-008-3B</b> | FHFA should evaluate Fannie Mae's mortgage pool policy commutations to determine whether these transactions were appropriate and in the best interest of the Enterprise and taxpayers. This evaluation should include a full accounting and validation of all of the cost components that comprise each settlement discount (risk in force minus fee charged), such as insurance premiums and time value of money applicable to each listed cost component. | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |
| <b>AUD-2012-008-4</b>  | FHFA should develop a methodology and process for conservator review of proposed mortgage pool policy commutations to ensure that there is a documented, sound basis for any pool policy commutations executed in the future.   | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |
| <b>AUD-2012-008-5</b>  | FHFA should complete actions to establish a governance structure at Fannie Mae for obtaining conservator approval of counterparty risk limit increases.   | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |
| <b>AUD-2012-008-6</b>  | FHFA should establish a clear timetable and deadlines for Enterprise submission of transactions to FHFA for conservatorship approval.   | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |
| <b>AUD-2012-008-7</b>  | FHFA should develop criteria for conducting business case analyses and substantiating conservator decisions.  | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |
| <b>AUD-2012-008-8</b>  | FHFA should issue a directive to the Enterprises requiring them to notify FHFA of any deviation from any previously reviewed action so that FHFA may consider the change and revisit its conservatorship decision.  | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Closed—Final action taken by FHFA. |

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| <b>AUD-2012-008-9</b> | FHFA should implement a risk-based examination plan to review the Enterprises' execution of and adherence to conservatorship decisions.   | <i>FHFA's Conservator Approval Process for Fannie Mae and Freddie Mac Business Decisions</i> | Recommendation agreed to by FHFA; implementation of recommendation pending.                                |
| <b>EVL-2014-005-1</b> | FHFA should review the 2013 director expense data submitted by the FHLBanks to identify and correct any inconsistencies and inaccuracies prior to the publication of the 2013 annual report, to the extent feasible, and disclose in the report any remaining data limitations. | <i>FHFA's Reporting of Federal Home Loan Bank Director Expenses</i>                          | Recommendation agreed to by FHFA; implementation of recommendation pending.                                |
| <b>EVL-2014-005-2</b> | FHFA should issue guidance designed to ensure the consistency and utility of the director expense data submitted to the Agency.   | <i>FHFA's Reporting of Federal Home Loan Bank Director Expenses</i>                          | Recommendation agreed to by FHFA; implementation of recommendation pending.                                |
| <b>EVL-2014-003-1</b> | FHFA's Deputy Director of DHMG should establish an ongoing process to evaluate servicers' SAI compliance and the effectiveness of the Enterprises' remediation efforts.   | <i>FHFA's Oversight of the Servicing Alignment Initiative</i>                                | Recommendation partially agreed to by FHFA; recommendation remains open and will continue to be monitored. |
| <b>EVL-2014-003-2</b> | FHFA's Deputy Director of DHMG should direct the Enterprises to provide routinely their internal reports and reviews for DHMG's assessment.   | <i>FHFA's Oversight of the Servicing Alignment Initiative</i>                                | Recommendation partially agreed to by FHFA; recommendation remains open and will continue to be monitored. |
| <b>EVL-2014-003-3</b> | FHFA's Deputy Director of DHMG should regularly review SAI-related guidelines for enhancements or revisions, as necessary, based on servicers' actual versus expected performance.  | <i>FHFA's Oversight of the Servicing Alignment Initiative</i>                                | Recommendation partially agreed to by FHFA; recommendation remains open and will continue to be monitored. |
| <b>EVL-2014-002-1</b> | FHFA should review its implementation of the 2013 Enterprise examination plans and document the extent to which resource limitations, among other things, may have impeded their timely and thorough execution.   | <i>Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises</i>        | Recommendation agreed to by FHFA; implementation of recommendation pending.                                |



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| <b>EVL-2014-002-2</b> | FHFA should develop a process that links annual Enterprise examination plans with core team resource requirements.  | <i>Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises</i>        | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>EVL-2014-002-3</b> | FHFA should establish a strategy to ensure that the necessary resources are in place to ensure timely and effective Enterprise examination oversight.   | <i>Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises</i>        | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>ESR-2014-001-1</b> | FHFA's Advisory Bulletins that provide guidance regarding implementation of critical regulatory changes should be issued to all the impacted regulated entities.  | <i>FHFA's Oversight of Derivative Counterparty Risk</i>                                      | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>EVL-2013-012-1</b> | FHFA should ensure Fannie Mae takes the actions necessary to reduce servicer reimbursement processing errors. These actions should include utilizing its process accuracy data in a more effective manner and implementing a red flag system.   | <i>Evaluation of Fannie Mae's Servicer Reimbursement Operations for Delinquency Expenses</i> | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>EVL-2013-012-2</b> | FHFA should require Fannie Mae to: <ul style="list-style-type: none"> <li>• quantify and aggregate its overpayments to servicers regularly;</li> <li>• implement a plan to reduce these overpayments by (1) identifying their root causes, (2) creating reduction targets, and (3) holding managers accountable; and</li> <li>• report its findings and progress to FHFA periodically.</li> </ul> | <i>Evaluation of Fannie Mae's Servicer Reimbursement Operations for Delinquency Expenses</i> | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |
| <b>EVL-2013-012-3</b> | FHFA should publish Fannie Mae's reduction targets and overpayment findings.  | <i>Evaluation of Fannie Mae's Servicer Reimbursement Operations for Delinquency Expenses</i> | Recommendation not accepted by FHFA; recommendation remains open and will continue to be monitored. |
| <b>EVL-2013-009-1</b> | FHFA should establish a formal review process for compensatory fee settlements and significant mortgage servicing rights (MSR) transfers.   | <i>FHFA's Oversight of Fannie Mae's 2013 Settlement with Bank of America</i>                 | Recommendation agreed to by FHFA; implementation of recommendation pending.                         |

| No.                   | Recommendation  | Report  | Status  |
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| <b>EVL-2013-008-1</b> | FHFA's Deputy Director, Division of Home Loan Bank Regulation, should ensure that Agency examiners thoroughly assess FHLBank compliance with matters requiring attention and other supervisory requirements to remediate unsecured credit violations and risk management deficiencies during the 2013 and 2014 examination cycles.  | <i>FHFA's Oversight of the Federal Home Loan Banks' Compliance with Regulatory Limits on Extensions of Unsecured Credit</i>                   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>EVL-2013-008-2</b> | FHFA's Deputy Director, in consultation with the General Counsel and others, should consider the use of informal or formal enforcement actions as appropriate to ensure the remediation of any further regulatory violations or failures to adhere to supervisory requirements.   | <i>FHFA's Oversight of the Federal Home Loan Banks' Compliance with Regulatory Limits on Extensions of Unsecured Credit</i>                   | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>EVL-2013-005-1</b> | FHFA should, preferably in consultation with FHA, develop definitions and performance measures that would permit Congress, financial market participants, and the public to assess the progress and the effectiveness of its initiative.  | <i>FHFA's Initiative to Reduce the Enterprises' Dominant Position in the Housing Finance System by Raising Gradually Their Guarantee Fees</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>EVL-2013-005-2</b> | <p>FHFA should assess the feasibility of establishing a formal working arrangement with FHA to assess such critical issues as:</p> <ul style="list-style-type: none"> <li>• (1) the implementation of their pricing initiatives and prospects for success in achieving their objectives, and (2) the potential for shifts of mortgage business and risks between government-supported or -guaranteed markets;</li> <li>• briefing the Federal Housing Finance Oversight Board and/or FSOC on the findings of the assessment; and</li> <li>• disclosing the assessment publicly in an appropriate format.</li> </ul> | <i>FHFA's Initiative to Reduce the Enterprises' Dominant Position in the Housing Finance System by Raising Gradually Their Guarantee Fees</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |

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| <b>EVL-2012-008-1</b> | FHFA should consider revising FHFA's delegation of authorities to require FHFA approval of unusual, high-cost, new initiatives, like the High Touch Servicing Program.   | <i>Evaluation of FHFA's Oversight of Fannie Mae's Transfer of Mortgage Servicing Rights from Bank of America to High Touch Servicers</i> | Recommendation agreed to by FHFA; implementation of recommendation pending. |
| <b>EVL-2012-008-2</b> | FHFA should ensure that Fannie Mae does not have to pay a premium to transfer inadequately performing portfolios.  | <i>Evaluation of FHFA's Oversight of Fannie Mae's Transfer of Mortgage Servicing Rights from Bank of America to High Touch Servicers</i> | Closed—Final action taken by FHFA.  |
| <b>EVL-2012-008-3</b> | <p>Consistent with the control issues found in Fannie Mae's internal audit report on the High Touch Servicing Program, FHFA should ensure that Fannie Mae applies additional scrutiny and rigor to pricing significant MSR transactions. Specifically, FHFA should:</p> <ul style="list-style-type: none"> <li>• consider requiring Fannie Mae to assess the valuation methods of multiple MSR valuers in order to discern best practices; and</li> <li>• consider requiring two independent valuations in the case of larger MSR transactions (at a threshold to be determined by FHFA).</li> </ul> | <i>Evaluation of FHFA's Oversight of Fannie Mae's Transfer of Mortgage Servicing Rights from Bank of America to High Touch Servicers</i> | Closed—Final action taken by FHFA.  |
| <b>EVL-2012-008-4</b> | FHFA should assess the efficacy of the program and direct any necessary modifications. As the portfolios purchased under the program approach the five-year mark, FHFA should review both the underlying assumptions and the performance criteria for the High Touch Servicing Program.  | <i>Evaluation of FHFA's Oversight of Fannie Mae's Transfer of Mortgage Servicing Rights from Bank of America to High Touch Servicers</i> | Closed—Final action taken by FHFA.  |

| No.                   | Recommendation  | Report  | Status  |
|-----------------------|---|---|---|
| <b>EVL-2012-005-1</b> | <p>FHFA should continue its ongoing horizontal review of unsecured credit practices at the FHLBanks by:</p> <ul style="list-style-type: none"> <li>• following up on any potential evidence of violations of the existing regulatory limits and taking supervisory and enforcement actions as warranted; and</li> <li>• determining the extent to which inadequate systems and controls may compromise the FHLBanks' capacity to comply with regulatory limits and taking any supervisory actions necessary to correct such deficiencies as warranted.</li> </ul> | <i>FHFA's Oversight of the Federal Home Loan Banks' Unsecured Credit Risk Management Practices</i>                              | Closed—Final action taken by FHFA.  |
| <b>EVL-2012-005-2</b> | <p>FHFA should strengthen the regulatory framework around the FHLBanks' extension of unsecured credit by considering the utility of:</p> <ul style="list-style-type: none"> <li>• establishing maximum overall exposure limits;</li> <li>• lowering the existing individual counterparty limits; and</li> <li>• ensuring that the unsecured exposure limits are consistent with the FHLBank System's housing mission.</li> </ul>  | <i>FHFA's Oversight of the Federal Home Loan Banks' Unsecured Credit Risk Management Practices</i>                              | Recommendation agreed to by FHFA; implementation of recommendation pending.           |
| <b>EVL-2011-006-1</b> | <p>FHFA should promptly act on the specific, significant concerns raised by FHFA staff and Freddie Mac internal auditors about its loan review process.</p>   | <i>Evaluation of the Federal Housing Finance Agency's Oversight of Freddie Mac's Repurchase Settlement with Bank of America</i> | Recommendation partially agreed to by FHFA; implementation of recommendation pending. |
| <b>EVL-2011-006-2</b> | <p>FHFA should promptly initiate management reforms to ensure that senior managers are apprised of and timely act on significant concerns brought to their attention, particularly when they receive reports that the normal reporting and supervisory process is not working properly.</p>   | <i>Evaluation of the Federal Housing Finance Agency's Oversight of Freddie Mac's Repurchase Settlement with Bank of America</i> | Closed—Final action taken by FHFA.  |

**Figure 23. Summary of OIG Reports Where All Recommendations Are Closed**

| Report   | No. of Recommendations |
|--|------------------------|
| <i>FHFA Can Improve Its Oversight of Fannie Mae's Recoveries from Borrowers Who Possess the Ability to Repay Deficiencies (AUD-2013-011)</i>   | 1                      |
| <i>FHFA Can Enhance Its Oversight of FHLBank Advances to Insurance Companies by Improving Communication with State Insurance Regulators and Standard-Setting Groups (AUD-2013-006)</i> | 2                      |
| <i>FHFA's Oversight of the Asset Quality of Multifamily Housing Loans Financed by Fannie Mae and Freddie Mac (AUD-2013-004)</i>  | 2                      |
| <i>FHFA's Oversight of the Enterprises' Efforts to Recover Losses from Foreclosure Sales (AUD-2013-001)</i>  | 3                      |
| <i>FHFA's Oversight of the Enterprises' Management of High-Risk Seller/Servicers (AUD-2012-007)</i>  | 2                      |
| <i>FHFA's Call Report System (AUD-2012-006)</i>  | 3                      |
| <i>FHFA's Supervisory Risk Assessment for Single-Family Real Estate Owned (AUD-2012-005)</i>   | 1                      |
| <i>FHFA's Supervisory Framework for Federal Home Loan Banks' Advances and Collateral Risk Management (AUD-2012-004)</i>  | 7                      |
| <i>FHFA's Oversight of Fannie Mae's Single-Family Underwriting Standards (AUD-2012-003)</i>  | 2                      |
| <i>FHFA's Supervision of Freddie Mac's Controls over Mortgage Servicing Contractors (AUD-2012-001)</i>   | 5                      |
| <i>FHFA's Oversight of Fannie Mae's Default-Related Legal Services (AUD-2011-004)</i>  | 3                      |
| <i>Clifton Gunderson LLP's Independent Audit of the Federal Housing Finance Agency's Privacy Program and Implementation - 2011 (AUD-2011-003)</i>                                      | 9                      |
| <i>Clifton Gunderson LLP's Independent Audit of the Federal Housing Finance Agency's Information Security Program - 2011 (AUD-2011-002)</i>  | 5                      |
| <i>Audit of the Federal Housing Finance Agency's Consumer Complaints Process (AUD-2011-001)</i>  | 3                      |
| <i>FHFA's Oversight of the Federal Home Loan Banks' Affordable Housing Programs (EVL-2013-04)</i>  | 3                      |
| <i>Case Study: Freddie Mac's Unsecured Lending to Lehman Brothers Prior to Lehman Brothers' Bankruptcy (EVL-2013-03)</i>   | 3                      |
| <i>FHFA's Oversight of the Enterprises' Compensation of Their Executives and Senior Professionals (EVL-2013-001)</i>   | 1                      |
| <i>FHFA's Oversight of Freddie Mac's Investment in Inverse Floaters (EVL-2012-009)</i>   | 4                      |
| <i>Follow-up on Freddie Mac's Loan Repurchase Process (EVL-2012-007)</i>   | 1                      |



| Report  | No. of Recommendations |
|---|------------------------|
| <i>FHFA's Certifications for the Preferred Stock Purchase Agreements (EVL-2012-006)</i>   | 2                      |
| <i>Fannie Mae's and Freddie Mac's Participation in the 2011 Mortgage Bankers Association Convention and Exposition (ESR-2012-004)</i>                       | 2                      |
| <i>FHFA's Oversight of the Enterprises' Charitable Activities (ESR-2012-003)</i>  | 2                      |
| <i>Evaluation of FHFA's Management of Legal Fees for Indemnified Executives (EVL-2012-002)</i>  | 2                      |
| <i>FHFA's Oversight of Troubled Federal Home Loan Banks (EVL-2012-001)</i>  | 3                      |
| <i>Evaluation of Whether FHFA Has Sufficient Capacity to Examine the GSEs (EVL-2011-005)</i>  | 4                      |
| <i>Evaluation of FHFA's Oversight of Fannie Mae's Management of Operational Risk (EVL-2011-004)</i>   | 3                      |
| <i>Evaluation of FHFA's Role in Negotiating Fannie Mae's and Freddie Mac's Responsibilities in Treasury's Making Home Affordable Program (EVL-2011-003)</i> | 1                      |
| <i>Evaluation of Federal Housing Finance Agency's Oversight of Fannie Mae's and Freddie Mac's Executive Compensation Programs (EVL-2011-002)</i>            | 8                      |
| <i>Federal Housing Finance Agency's Exit Strategy and Planning Process for the Enterprises' Structural Reform (EVL-2011-001)</i>                            | 2                      |

# Appendix C: Information Required by the Inspector General Act and Subpoenas Issued

Section 5(a) of the Inspector General Act provides that OIG shall, not later than April 30 and October 31 of each year, prepare semiannual reports summarizing our activities during the immediately preceding six-month periods ending March 31 and

September 30. Further, section 5(a) lists more than a dozen categories of information that we must include in our semiannual reports.

Below, OIG presents a table that directs the reader to the pages of this report where the information required by the Inspector General Act may be found.

The text that follows further addresses the status of OIG’s compliance with sections 5(a)(6), (8), (9), (10), (11), (12), and (13) of the Inspector General Act. Finally, OIG provides information concerning administrative subpoenas that it issued during the semiannual period.

| Source/Requirement   | Pages          |
|--|----------------|
| Section 5(a)(1)- A description of significant problems, abuses, and deficiencies relating to the administration of programs and operations of FHFA.  | 5-18           |
| Section 5(a)(2)- A description of the recommendations for corrective action made by OIG with respect to significant problems, abuses, or deficiencies.   | 5-18<br>77-97  |
| Section 5(a)(3)- An identification of each significant recommendation described in previous semiannual reports on which corrective action has not been completed.  | 84-91<br>93-97 |
| Section 5(a)(4)- A summary of matters referred to prosecutive authorities and the prosecutions and convictions that have resulted.   | 20-37          |
| Section 5(a)(5)- A summary of each report made to the Director of FHFA.  | 5-18           |
| Section 5(a)(6)- A listing, subdivided according to subject matter, of each audit and evaluation report issued by OIG during the reporting period and for each report, where applicable, the total dollar value of questioned costs (including a separate category for the dollar value of unsupported costs) and the dollar value of recommendations that funds be put to better use. | 5-18<br>101    |
| Section 5(a)(7)- A summary of each particularly significant report.  | 5-18           |
| Section 5(a)(8)- Statistical tables showing the total number of audit and evaluation reports and the total dollar value of questioned and unsupported costs.   | 5-18<br>101    |
| Section 5(a)(9)- Statistical tables showing the total number of audit and evaluation reports and the dollar value of recommendations that funds be put to better use by management.  | 5-18<br>101    |
| Section 5(a)(10)- A summary of each audit and evaluation report issued before the commencement of the reporting period for which no management decision has been made by the end of the reporting period.  | 101            |
| Section 5(a)(11)- A description and explanation of the reasons for any significant revised management decision made during the reporting period.   | 101            |
| Section 5(a)(12)- Information concerning any significant management decision with which the Inspector General is in disagreement.  | 101            |
| Section 5(a)(13)- The information described under section 05(b) of the Federal Financial Management Improvement Act of 1996.   | 102            |

## Audit and Evaluation Reports with Recommendations of Questioned Costs, Unsupported Costs, and Funds to Be Put to Better Use by Management

Section 5(a)(6) of the Inspector General Act, as amended, requires that OIG list its reports during the semiannual period that include questioned costs, unsupported costs, and funds to be put to better use. Section 5(a)(8) and section 5(a)(9), respectively, require OIG to publish statistical tables showing the dollar value of questioned and unsupported costs, and of recommendations that funds be put to better use by management. Figure 24 (see below) discloses OIG's questioned and unsupported cost findings, and recommendations that funds be put to better use for the reporting period.

## Audit and Evaluation Reports with No Management Decision

Section 5(a)(10) of the Inspector General Act, as amended, requires that OIG report on each audit and evaluation report issued before the commencement of the reporting period for which no management decision has been made by the end of the reporting period. There were no audit or evaluation reports issued before October 1, 2013, that await a management decision.

## Significantly Revised Management Decisions

Section 5(a)(11) of the Inspector General Act, as amended, requires that OIG report information concerning the reasons for any significant revised management decision made during the reporting period. During the six-month reporting period ended March 31, 2014, FHFA significantly revised its management decisions on OIG's July 16, 2013, evaluation titled *FHFA's Initiative to Reduce the Enterprises' Dominant Position in the Housing Finance System by Raising Gradually Their Guarantee Fees* (EVL-2013-005). Management, which had previously disagreed with OIG's recommendations, changed its position and has taken subsequent actions accordingly.

## Significant Management Decision with Which the Inspector General Disagrees

Section 5(a)(12) of the Inspector General Act, as amended, requires that OIG report information concerning any significant management decision with which the Inspector General is in disagreement. During the current reporting period, there were no management decisions with which the Acting Inspector General disagreed.

**Figure 24. Funds to Be Put to Better Use by Management, Questioned Costs, and Unsupported Costs for the Period October 1, 2013, to March 31, 2014**

| Report Issued | Recommendation No. | Date      | Potential Monetary Benefits |                   |                         |
|---------------|--------------------|-----------|-----------------------------|-------------------|-------------------------|
|               |                    |           | Questioned Costs            | Unsupported Costs | Funds Put to Better Use |
| AUD-2014-005  | 1                  | 1/15/2014 | \$-                         | \$-               | \$5,015,505             |
| <b>Total</b>  |                    |           | <b>\$-</b>                  | <b>\$-</b>        | <b>\$5,015,505</b>      |

## Federal Financial Management Improvement Act of 1996

The provisions of HERA require FHFA to implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

For fiscal year 2013, FHFA received from GAO an unqualified (clean) audit opinion on its annual financial statements and internal control over financial reporting. GAO also reported that it identified no material weaknesses in internal controls or reportable instances of noncompliance with laws or regulations. HERA requires GAO to conduct this audit.

Several OIG reports published during the semiannual period identified specific opportunities to strengthen FHFA's internal controls. These reports are summarized on pages 5 through 18.

## Subpoenas Issued

During the reporting period, OIG issued 51 subpoenas as summarized in Figure 25 (see below).

**Figure 25. Subpoenas Issued for the Period October 1, 2013–March 31, 2014**

| Issuing Office | Number of Subpoenas |
|----------------|---------------------|
| OA             | 12                  |
| OE             | 0                   |
| OI             | 39                  |
| <b>Total</b>   | <b>51</b>           |

## Appendix D: OIG Reports

See [www.fhfa.ig.gov](http://www.fhfa.ig.gov) for OIG's reports.

### Audit Reports

*FHFA Oversight of Enterprise Controls Over Pre-Foreclosure Property Inspections* (AUD-2014-012, March 25, 2014).

*FHFA's Controls to Detect and Prevent Improper Payments FY 2013* (AUD-2014-011, March 20, 2014).

*FHFA's Use of Government Travel Cards* (AUD-2014-010, March 20, 2014).

*FHFA Oversight of Enterprise Handling of Aged Repurchase Demands* (AUD-2014-009, February 12, 2014).

*FHFA's Oversight of the Enterprises' Use of Appraisal Data Before They Buy Single-Family Mortgages* (AUD-2014-008, February 6, 2014).

*FHFA's Implementation of Active Directory* (AUD-2014-007, January 31, 2014).

*FHFA's Use of Government Purchase Cards* (AUD-2014-006, January 31, 2014).

*FHFA Oversight of Fannie Mae's Reimbursement Process for Pre-Foreclosure Property Inspections* (AUD-2014-005, January 15, 2014).

*FHFA Oversight of Fannie Mae's Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties* (AUD-2014-004, January 15, 2014).

*Fannie Mae's Controls Over Short Sale Eligibility Determinations Should be Strengthened* (AUD-2014-003, November 20, 2013).

*Kearney & Company, P.C.'s Independent Evaluation of the Federal Housing Finance Agency's Office of Inspector General's Information Security Program-2013* (AUD-2014-002, October 31, 2013).

*Kearney & Company, P.C.'s Independent Evaluation of the Federal Housing Finance Agency's Information Security Program-2013* (AUD-2014-001, October 3, 2013).

### Evaluation Reports

*FHFA's Reporting of Federal Home Loan Bank Director Expenses* (EVL-2014-005, March 20, 2014).

*Update on FHFA's Oversight of the Enterprises' Non-Executive Compensation Practices* (EVL-2014-004, February 25, 2014).

*FHFA's Oversight of the Servicing Alignment Initiative* (EVL-2014-003, February 12, 2014).

*Update on FHFA's Efforts to Strengthen its Capacity to Examine the Enterprises* (EVL-2014-002, December 19, 2013).

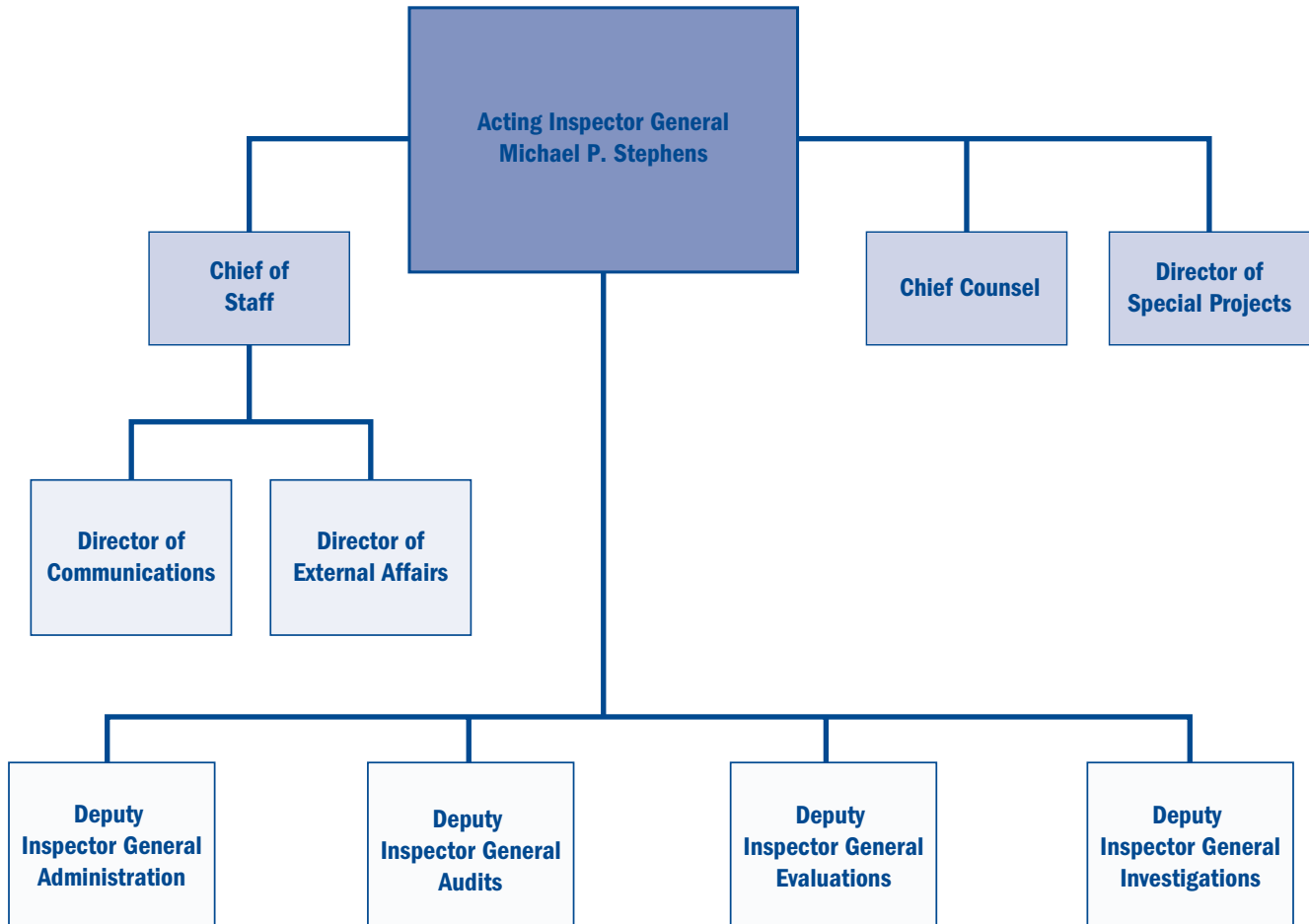
*FHFA's Oversight of Derivative Counterparty Risk* (ESR-2014-001, November 20, 2013).

### Other Reports

*Strategic Plan: Fiscal Years 2015–2017* (February 26, 2014).



# Appendix E: OIG Organizational Chart



# Appendix F: Description of OIG Offices and Strategic Plan

## OIG Offices

### Office of Audits

OA provides a full range of professional audit and attestation services for FHFA's programs and operations. Through its performance audits and attestation engagements, OA helps FHFA: (1) promote economy, efficiency, and effectiveness; (2) detect and deter fraud, waste, and abuse; and (3) ensure compliance with applicable laws and regulations. Under the Inspector General Act, inspectors general are required to comply with GAO's *Government Auditing Standards*, commonly referred to as the "Yellow Book." OA performs its audits and attestation engagements in accordance with the Yellow Book.

### Office of Evaluations

OE provides independent and objective reviews, studies, survey reports, and analyses of FHFA's programs and operations. The **Inspector General Reform Act of 2008** requires that inspectors general adhere to the *Quality Standards for Inspection and Evaluation*, commonly referred to as the "Blue Book," issued by CIGIE. OE performs its evaluations in accordance with the Blue Book. Included within OE is the Office of Oversight and Review (OR), which provides advice and consultation

services across OIG. OR also produces special reports and white papers that address complex housing finance issues.

### Office of Investigations

OI investigates allegations of misconduct and fraud involving FHFA and the GSEs in accordance with CIGIE's *Quality Standards for Investigations* and guidelines that the Attorney General issues.

OI's investigations may address administrative, civil, and criminal violations of laws and regulations. Investigations may relate to FHFA or GSE employees, contractors, consultants, and any alleged wrongdoing involving FHFA's or the GSEs' programs and operations. Offenses investigated may include mail, wire, bank, accounting, securities, or mortgage fraud, as well as violations of the tax code, obstruction of justice, and money laundering.

To date, OI has opened over 370 criminal and civil investigations, but by their nature, these investigations and their resulting reports are not

generally made public. However, if an investigation reveals criminal activity, OI refers the matter to DOJ for possible prosecution or recovery of monetary damages and penalties. OI reports administrative misconduct to management officials for consideration of disciplinary or remedial action.

OI also manages OIG's hotline that receives tips and complaints of fraud, waste, or abuse in FHFA's programs and operations. The hotline allows concerned parties to report their allegations to OIG directly and confidentially. OI honors all applicable whistleblower protections. As part of its effort to raise awareness of fraud, OI actively

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***Report fraud,  
waste, or abuse  
related to FHFA's  
programs and  
operations  
by visiting  
[www.fhfa.oig.gov](http://www.fhfa.oig.gov)  
or calling (800)  
793-7724.***

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promotes the hotline through OIG’s website, posters, emails to FHFA and GSE employees, and OIG’s semiannual reports.

### **Executive Office**

The Executive Office (EO) provides leadership and programmatic direction for OIG’s offices and activities.

EO includes the Office of Counsel (OC), which serves as the chief legal advisor to the Acting Inspector General and provides independent legal advice, counseling, and opinions to OIG about its programs and operations. OC also reviews audit and evaluation reports for legal sufficiency and compliance with OIG’s policies and priorities. Additionally, it reviews drafts of FHFA regulations and policies and prepares comments as appropriate. OC also coordinates with FHFA’s Office of General Counsel and manages OIG’s responses to requests and appeals made under the Freedom of Information Act and the Privacy Act.

The Office of External Affairs is within EO, and it responds to inquiries from members of Congress.

The Office of Communications is within EO, and it responds to inquiries from the press and public.

OIG’s Equal Employment Opportunity Program is also within EO.

The Office of Special Projects is also within EO, and it supports other OIG offices on high-impact projects.

### **Office of Administration**

The Office of Administration (OAd) manages and oversees OIG administration, including budget, human resources, safety, facilities, financial management, information technology, and continuity of operations. For human resources, OAd develops policies to attract, develop, and retain exceptional

people, with an emphasis on linking performance planning and evaluation to organizational and individual accomplishment of goals and objectives. Regarding OIG’s budget and financial management, OAd coordinates budget planning and execution and oversees all of OIG’s procedural guidance for financial management and procurement integrity.

OAd also administratively supports the Chief of Staff and the Deputy Inspector General for Audits as they implement OIG’s Internal Management Assessment Program, which requires the routine inspection of each OIG office to ensure that it complies with applicable requirements.

## **OIG’s Strategic Plan**

OIG’s Strategic Plan for fiscal years 2015-2017 sets out OIG’s plan to ensure the integrity, transparency, effectiveness, and soundness of FHFA’s operations and the operations of the organizations that FHFA oversees. OIG will continue to monitor events; make changes to the Strategic Plan as circumstances warrant; and strive to remain relevant regarding areas of concern to FHFA, the GSEs, Congress, and the American people.

Within the Strategic Plan, OIG has established several goals that will be used as a blueprint for OIG’s oversight of FHFA and independent reporting.

### **Strategic Goal 1—Promote FHFA’s Effective Oversight of the GSEs’ Safety and Soundness and Housing Missions**

OIG will promote effective risk oversight by FHFA, assess FHFA’s oversight of the GSEs’ housing mission and goal responsibilities, and assess the effectiveness of FHFA’s operations.

**Strategic Goal 2—Promote FHFA’s Effective Management and Conservatorship of the Enterprises**

OIG will assess FHFA’s and the Enterprises’ plans and progress on their strategic goals; assess FHFA’s effectiveness in controlling the costs of the conservatorships; and detect and deter fraud, waste, and abuse.

**Strategic Goal 3—Promote Effective FHFA Internal Operations**

OIG will detect and deter fraud, waste, and abuse.

**Strategic Goal 4—Promote Effective OIG Internal Operations**

OIG will maintain workforce expertise and collaboration to meet goals, maintain access and data security protocols with FHFA and the GSEs, and ensure reporting processes are useful to stakeholders.

## **Organizational Guidance**

OIG has developed and promulgated policies and procedural manuals for each of its offices. These manuals set forth uniform standards and guidelines for the performance of each office’s essential responsibilities and are intended to help ensure the consistency and integrity of OIG’s operations.

## Appendix G: Figure Sources

- Figure 2.** Federal Housing Finance Agency Office of Inspector General, “Inappropriate Property Inspection Reports and Photographs,” *FHFA Oversight of Enterprise Controls Over Pre-Foreclosure Property Inspections*, AUD-2014-012, at 19 (March 25, 2014). Accessed: April 15, 2014, at [www.fhfaog.gov/Content/Files/AUD-2014-012.pdf](http://www.fhfaog.gov/Content/Files/AUD-2014-012.pdf).
- Figure 3.** Federal Housing Finance Agency Office of Inspector General, “OIG Conclusion,” *FHFA’s Controls to Detect and Prevent Improper Payments FY 2013*, AUD-2014-011, at 9, 10 (March 20, 2014). Accessed: March 20, 2014, at [www.fhfaog.gov/Content/Files/AUD-2014-011.pdf](http://www.fhfaog.gov/Content/Files/AUD-2014-011.pdf).
- Figure 4.** Federal Housing Finance Agency Office of Inspector General, “FHFA Did Not Examine Freddie Mac’s Use of its Contractual Right to Assess Late Fees on Repurchase Demands Resulting in Missed Opportunities to Minimize Losses,” *FHFA Oversight of Enterprise Handling of Aged Repurchase Demands*, AUD-2014-009, at 20 (February 12, 2014). Accessed: March 20, 2014, at [www.fhfaog.gov/Content/Files/AUD-2014-009.pdf](http://www.fhfaog.gov/Content/Files/AUD-2014-009.pdf).
- Repurchase late fees calculated by OIG using Freddie Mac’s monthly outstanding repurchase reports from January 2009 through December 2012 and applying repurchase late fee policies from Freddie Mac’s seller-servicer guide, chapter 72.3.
- Figure 5.** Federal Housing Finance Agency Office of Inspector General, “Conclusion,” *FHFA Oversight of Fannie Mae’s Reimbursement Process for Pre-Foreclosure Property Inspections*, AUD-2014-005, at 12 (January 15, 2014). Accessed: March 20, 2014, at [www.fhfaog.gov/Content/Files/AUD%202014-005.pdf](http://www.fhfaog.gov/Content/Files/AUD%202014-005.pdf).
- OIG calculations using Fannie Mae’s: (1) *571 Servicer Processing Guide* and (2) 2011 and 2012 total disbursements.
- Figure 6.** Federal Housing Finance Agency Office of Inspector General, “Finding: FHFA Should Oversee Fannie Mae’s Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties,” *FHFA Oversight of Fannie Mae’s Remediation Plan to Refund Contributions to Borrowers for the Short Sale of Properties*, AUD-2014-004, at 4 (January 15, 2014). Accessed: March 20, 2014, at [www.fhfaog.gov/Content/Files/AUD-2014-004\\_0.pdf](http://www.fhfaog.gov/Content/Files/AUD-2014-004_0.pdf).
- Figure 8.** Federal Housing Finance Agency, “The Housing Government-Sponsored Enterprises,” *2011 Performance and Accountability Report*, at 14. Accessed: April 24, 2014, at [www.fhfa.gov/AboutUs/Reports/ReportDocuments/2011\\_PAR\\_508.pdf](http://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2011_PAR_508.pdf).
- Figure 9.** Inside Mortgage Finance, “Mortgage & Asset Securities Issuance,” *Mortgage Market Statistical Annual 2014 Yearbook*, at 106 (2014).
- Figure 10.** Federal Housing Finance Agency, “Table 3. Fannie Mae Earnings,” “Table 12. Freddie Mac Earnings,” *2012 Report to Congress*, at 80, 97 (June 13, 2013). Accessed: April 24, 2014, at [www.fhfa.gov/AboutUs/Reports/ReportDocuments/2012\\_AnnualReportToCongress\\_508.pdf](http://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2012_AnnualReportToCongress_508.pdf). Fannie Mae, “Table 7: Summary of Consolidated Results of Operations,” *Form 10-K for the Fiscal Year Ended December 31, 2013*, at 71. Accessed: March 7, 2014, at [www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/10k\\_2013.pdf](http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/10k_2013.pdf). Freddie Mac, “Table 8 — Summary Consolidated Statements of Comprehensive Income,” *Form 10-K for the Fiscal Year Ended December 31, 2013*, at 61. Accessed: March 7, 2014, at [www.freddiemac.com/investors/er/pdf/10k\\_022714.pdf](http://www.freddiemac.com/investors/er/pdf/10k_022714.pdf).
- Figure 11.** Federal Housing Finance Agency, “Table 3. Fannie Mae Earnings,” “Table 12. Freddie Mac Earnings,” *2012 Report to Congress*, at 80, 97 (June 13, 2013). Accessed: April 24, 2014, at [www.fhfa.gov/AboutUs/Reports/ReportDocuments/2012\\_AnnualReportToCongress\\_508.pdf](http://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2012_AnnualReportToCongress_508.pdf). Fannie Mae, “Table 7: Summary of Consolidated Results of Operations,” *Form 10-K for the Fiscal Year Ended December 31, 2013*, at 71. Accessed: March 7, 2014, at [www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/10k\\_2013.pdf](http://www.fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2013/10k_2013.pdf). Freddie Mac, “Table 8 — Summary Consolidated Statements of Comprehensive Income,” *Form 10-K for the Fiscal Year Ended December 31, 2013*, at 61. Accessed: March 7, 2014, at [www.freddiemac.com/investors/er/pdf/10k\\_022714.pdf](http://www.freddiemac.com/investors/er/pdf/10k_022714.pdf).
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## Appendix H: Endnotes

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