THE MORTGAGE COMPLIANCE MONITOR™

BANKERS ADVISORY

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Key Points to Fannie Mae's Loan Quality Initiative

This article summarizes Fannie Mae's March 2010 Selling Guide Update regarding their ***Loan Quality Initiative***. New steps and other QC changes are described in the sections below.

Fannie Mae's post-funding requirements for Quality Control are relatively consistent with prior directives. Here's the difference: ***lenders must be vigilant*** in carrying out their quality control plan. QC steps are completed on loan-by-loan basis to validate file documents and re-underwrite according to agency guidelines. QC plans must reflect the size, scope and business model of the lender.

Lenders must now think of quality control on two levels; one is the **loan level** and the other is the ***corporate*** level. On a loan level, deficiencies are cured through document correction. On a corporate level, training or process improvement can rectify areas of weakness. QC managers are burdened with making loans insurable and salable; compliance managers are burdened with ever-changing laws. In many companies, this person is one and the same. Sadly this has caused a widening gap in internal controls where lenders have lost sight of the corporate risk management objectives established in their original business plan because they are too busy dealing with QC on a loan level.

Fannie Mae expects lenders to establish a pre-defined set of **risk tolerance levels**, and monitor **defect rates** (quality control errors or exception items) according to a risk classification. Lenders can measure defect rates found in QC reviews according to loan characteristics, such as CLTV's over 90%, for investment properties, condominiums or cash-out refinances. The defect rate according to credit characteristics such as FICO Score or Automated Underwriting Risk Rating can be quantified by Underwriter.

At Bankers Advisory, we have developed a proprietary risk analysis tool for our QC clients to help establish the most effective strategy plan for loan-level and corporate-wide quality assurance. Please email contact me for more information at anna@bankersadvisory.com.

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Key Points to Fannie Mae's LQI

Steps Required Prior to Loan Delivery

1. Confirm Borrower Identity
2. Confirm Social Security Number (SSN) or Individual Taxpayer Identification Number (ITIN)
3. Documentation must conform to U.S.A. Patriot Act and the Department of Treasury's Office of Foreign Assets Control (OFAC)
4. Confirm all parties to the transaction are not on the General Services Administration (GSA) list or the Hud Limited Denial of Participation (LDP) list
5. All liabilities must be documented and included in qualifying ratios
6. All credit inquiries must be explained and, as appropriate, included in qualifying ratios
7. Desktop Underwriter "Potential Red Flag" messages have changed to "verification" message and require additional verification steps
8. Desktop Underwriter "occupancy" message requires lenders to verify the borrower's intended occupancy status of the subject property
9. Adequate controls may include pulling a new credit report prior to closing, MERS check to establish new or undisclosed liabilities / lien
10. Data integrity check to verify consistency of borrower, mortgage and property data before, during and immediately after delivery of loans

Quality Control Requirements

1. Post-funding Quality Control must be completed on a minimum of ten percent (10%) of the residential mortgage loans originated by retail and wholesale channels
2. Post-funding QC must be completed monthly (or more frequent basis)
3. Post-funding QC file selections must be made within 30 days of closing
4. Post-funding QC reviews must be completed within 60 days of selection
5. Fannie Mae must be notified if QC is in arrears by more than one 30-day cycle
6. Pre-funding is a mandatory component of a lender's QC plan
7. Discretionary samplings for pre- and post-funding QC must be completed in accordance with the lender's QC plan, business channels, QC findings/error-rate and modified as necessary. Characteristics included in discretionary audits should include, at a minimum:

   - Third Party Originators
   - Investment Properties
   - Cash-out Refinances
   - Condominium/Co-ops
   - LTV > 90%
   - Credit Score
   - New Hires

8. Data integrity checks must verify borrower, property and mortgage data
9. QC must obtain a borrower's federal tax transcript if the 4506T was not processed
10. Quality Control reviews must monitor compliance to the Home Valuation Code of Conduct (HVCC)