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TO: John C. Weicher, Assistant Secretary for Housing, H

Daniel G. Temme

FROM: Daniel G. Temme, Regional Inspector General for Audit, Mid-Atlantic, 3AGA

SUBJECT: Contracts for Endorsement and Post-Endorsement Services

INTRODUCTION

We reviewed the standard contracts that the Office of Single Family Housing used to procure and administer endorsement processing and post-endorsement quality control services over FHA-insured mortgage loans. Our two objectives were to determine whether the terms of the contracts provide adequate controls to ensure efficient and cost effective delivery of these services and to determine if the pricing of those services at the four Homeownership Centers (HOCs) was reasonable.

To accomplish these objectives, we reviewed applicable HUD and OMB guidance on contract procurement and administration; interviewed responsible HUD staff and the Philadelphia HOC's endorsement and post-endorsement contractors; and compared and analyzed terms of the contracts in effect as of April 2004. We performed the audit in accordance with generally accepted government auditing standards.

Should you or your staff have any questions, please contact J. Phillip Griffin, Assistant Regional Inspector General for Audit, at (215) 656-3401, extension 3490.

SUMMARY

We reviewed the contracts that the Office of Single Family Housing used for endorsement and post-endorsement services over FHA-insured mortgage loans to determine whether the terms of the contracts provide adequate controls to ensure efficient and cost effective delivery of the services and to determine if the pricing of the services at the four Homeownership Centers (HOCs) was reasonable. We did not identify any significant deficiencies. Accordingly, this report does not contain any reportable conditions or recommendations for corrective action.

BACKGROUND

In 1993, HUD initiated a reinvention effort that included significant staff reductions and the consolidation of mortgage insurance processing and other activities from 81 Field Offices into four HOCs. HUD established the last of four HOCs in 1999. As a result of these consolidations, the Office of Single Family Housing's HOCs jointly developed and issued standard contracts for the delivery of endorsement and post-endorsement review services.

Since its creation in 1934, FHA has insured almost 32 million single-family mortgages totaling \$1.6 trillion. FHA insurance helps first-time homebuyers and other families who would otherwise have difficulty obtaining a mortgage. About one million households obtain FHA-insured mortgages in an average year. In Fiscal Year 2003, HUD endorsed more than 1.3 million loans valued at almost \$160 billion. Quality control reviews are a significant cornerstone of the FHA's process and a major control over the integrity of the program. During Fiscal Year 2004, HUD will spend approximately \$10.5 million and \$3.7 million for the endorsement and post-endorsement services, respectively.

MANAGEMENT CONTROLS

Management controls include the plan of organization, methods, and procedures adopted by management to ensure that it meets its goals. Management controls include the processes for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

We examined the management control structure that provides the framework for HOCs to administer their system of quality controls over mortgage loans submitted for FHA endorsement. Specifically, we examined the controls specified in the contracts for endorsement and post-endorsement services.

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

Based on our review we believe there are no significant weaknesses in contracting for endorsement and post-endorsement review services. However, we noted some minor conditions that we transmitted to HUD Management in a memorandum dated September 20, 2004.

FOLLOW-UP ON PRIOR AUDITS

The Single Family Production Homeownership Centers (00-SF-121-0001) Audit Report, dated March 30, 2000, reported a number of improvements needed in the post-endorsement technical reviews of lender loan underwriting and property appraisals, monitoring of lenders by the HOCs' Quality Assurance Divisions, oversight of endorsement contractors, and accuracy of information in the automated tracking system. HUD has completed action to address all of the recommendations contained in the report.