



UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

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RESOURCES, COMMUNITY,  
AND ECONOMIC DEVELOPMENT  
DIVISION

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B-214393



The Honorable Mary Rose Oakar  
House of Representatives

RELEASED

Dear Ms. Oakar:

Subject: Excessive Assumption Fees Charged on Federal Home  
Loan Mortgage Corporation Mortgages (RCED-84-119)

On August 25, 1983, you requested an investigation into the fees, points, and other charges levied by lenders on mortgages sold to the Federal Home Loan Mortgage Corporation that are assumed when the mortgaged properties are sold or transferred to a new borrower. Specifically, you asked that we determine the pervasiveness of overcharges, the reasons why corporation auditors did not uncover excessive fees charged by lenders, the feasibility of establishing a flat fee or some regulation of the assumption fee, and the adequacy of corporation oversight and enforcement policies regarding overcharges by savings and loan associations.

In several meetings and telephone conversations with your office, we discussed the Corporation's

- establishment of a "hot line" for complaints on overcharges,
- inquiry process for investigating complaints and ensuring that appropriate refunds are made,
- revisions to its audit procedures requiring seller/servicers (lenders who sell mortgages to and then service mortgages for the Corporation) to include steps to analyze such fees when routine audits are made, and
- efforts to formulate a new policy on assumption fees.

During these discussions, we advised your office that based on our discussions with the Corporation's Director, Loan Servicing; Vice President, Congressional and Governmental Relations; and Northeast Regional Office Loan Servicing Director; our review of corporation procedures and related correspondence; and the results of the Corporation actions discussed earlier, we believe the Corporation is giving the assumption fee problem top priority and that its inquiry procedures appear to be working.

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However, we have suggested that the Corporation make additional efforts to identify overcharges not called to its attention by borrower complaints. We suggested that it ask its seller/servicers to voluntarily review their portfolios to identify overcharges, make appropriate refunds, and report such refunds to the Corporation. The Corporation agreed to consider this suggestion and subsequently told us that it would implement it.

As discussed with your office, we did not perform extensive field work on your request because the Corporation has already taken action. However, in accordance with your office's specific request, this letter summarizes information we have gathered.

BACKGROUND INFORMATION ON THE FEDERAL  
HOME LOAN MORTGAGE CORPORATION

The Corporation is government-sponsored and was chartered by the Congress in 1970 to develop a secondary market in conventional residential mortgages. In doing so, the corporation purchases loans from lenders, pools the loans, and sells securities backed by these loan pools. The Corporation has purchased about 5 percent of all new conventional mortgage loans since it was created in 1970. As a conduit between mortgage lenders and the capital markets, the Corporation attracts funds for housing at lower mortgage costs to homebuyers. Equally important, the Corporation helps to ensure a stable supply of local mortgage credit nationwide through the ability of savings institutions and other lenders to sell mortgages they originate.

After the mortgage lender sells his or her mortgage to the Corporation, he or she continues to service the mortgage as an agent (seller/servicer) of the Corporation. This contractual relationship is embodied in several documents that specify the obligations of both the seller/servicers and the Corporation. Seller/servicers are responsible for being knowledgeable of and complying with the Corporation's policies and procedures. The Corporation uses a number of information sources, including site visits and audits, to ascertain whether seller/servicers are complying with its policies and procedures. Information sources include but are not limited to:

- legal warranties provided to the Corporation by seller/servicers stating compliance with Corporation contract provisions and applicable law,
- routine reports submitted to the Corporation by seller/servicers,
- reports by Corporation regional office staff who periodically visit seller/servicers,
- on-site audit reports,

- general feedback from the marketplace,
- complaints from realtors and homebuyers, and
- news reports.

According to the Corporation officials we interviewed, any finding of abuse or violation of its policies is quickly brought to the seller/servicers' attention. If the problem is not remedied, the Corporation can disqualify the seller/servicer and/or transfer the mortgage servicing to another seller/servicer. However, because the Corporation's purchase of loans from eligible seller/servicers helps to replenish local suppliers of mortgage credit and is important to homebuyers, the officials said that they will not suspend or disqualify seller/servicers without serious reason, such as failure to comply with specific corporation directives.

#### ASSUMPTION FEE POLICY

The Corporation operates by purchasing mortgages after they have been originated by private lenders. It then pools these mortgages and sells securities backed by those loan pools. The homebuyer continues to make monthly payments to the original lender and usually does not know his or her mortgage has been purchased by the Corporation. In addition, if the homeowner sells his or her home and the mortgage is assumed by another buyer, the original lender who processes the assumption is not required to notify the Corporation of the assumption. Accordingly, the Corporation does not know how many of its 1.6 million mortgages have been assumed by subsequent buyers. The Corporation has a policy on fees that seller/servicers (original lenders) can charge for processing such assumptions. Prior to November 10, 1980, its policy stated:

"In no event may the total amount charged exceed \$50 for processing a change of name in a sale subject to an existing mortgage or one percent (1%) of the unpaid principal balance for the assumption of any mortgage loan in which FHLMC [the Corporation] retains an ownership interest after the assumption."

However, because of seller/servicer complaints that the fee resulting from this policy was too small to cover costs, the Corporation changed its policy on November 10, 1980, to state:

"Such fee should bear a close relationship to the actual costs involved and be in accordance with amounts allowed by FHA, VA, or any other authority having jurisdiction."

Subsequent to this policy change, Corporation records show that the Corporation received periodic complaints from regional officials, realtors, and others that seller/servicers were charging excessively high assumption fees, perhaps to capitalize on the fact that the loans being assumed had interest rates much lower than current market rates. The Corporation dealt with these complaints on an individual basis, which resulted in some reductions in fees and isolated refunds to borrowers. On January 4, 1983, the Corporation sent a letter to all its seller/servicers in an effort to clarify its policy. The revised policy stated:

"Such fee must reflect no more than the actual or a reasonable estimate of the processing costs involved, except that in no case shall the fee exceed permissible amounts allowed under applicable law or regulation."

During the period January 4, 1983, through August 24, 1983, the Corporation continued to receive complaints of excessive fees, which it continued to deal with on an individual basis. Articles concerning the problem began appearing in several newspapers, including the Cleveland Plain Dealer. The Corporation also received inquiries from several members of the Congress. Because of the publicity and congressional interest, the Corporation decided on August 24, 1983, to increase its efforts to enforce refunds of excessive fees even though its opinion was still that the bulk of lenders had acted in compliance with its policy and that the magnitude of the problem was being exaggerated.

#### CORPORATION ACTIONS AND RESULTS

Pursuant to your request, we met with Corporation officials to discuss the problem of excessive assumption fees, ongoing actions, planned actions, and results obtained to date. On August 24, 1983, the Corporation held a press conference and announced that it had taken steps to correct a practice by some seller/servicers who may have charged excessive fees in processing the assumption of mortgage loans purchased by the Corporation. It then notified all its seller/servicers by mailgram that overcharging violates Corporation policies covering assumptions and borrowers who have paid excessive fees should be given refunds.

In addition to their actions, the Corporation established a free telephone call-in system to take calls from consumers who believed they may have been overcharged. This number was publicized in several publications. The information received was used by the Corporation to help check on the alleged abuses through an assumption fee inquiry process it developed. We were later told that this system became operable in late September and that the regional offices were playing a key role. In brief, the responsibilities of the Corporation regions under the system are to

- receive assumption fee inquiries from the home office;
- monitor the response of seller/servicers;
- review seller/servicers reports to examine their cost justifications for fees charged and the amount of any refunds, if appropriate;
- monitor disbursements of refunds;
- follow up possible additional assumption fee violations for each lender for which a violation was discovered; and
- report results weekly to the headquarter's office.

In our meetings with the Director, Loan Servicing, and the Vice President, Congressional and Governmental Relations, of the Corporation's headquarters office and the Northeast Regional Office Loan Servicing Director, we were told that top priority was being given to ensuring that all inquiries called to their attention were quickly and thoroughly analyzed and that appropriate refunds were made. During our last meeting with headquarter's officials, we were informed that as of January 26, 1984, the following had resulted since the Corporation established its toll free call-in line and inquiry process:

Consumer assumption fee calls	2,848
Consumer questionnaires returned	1,239
Questionnaires terminated	167
Questionnaires pending resolution	301
Questionnaires pending in home office	8
Primary refunds issued <sup>1</sup>	300
Secondary refunds issued <sup>1</sup>	883
Dollar amount of primary refunds issued	\$ 207,993.48
Dollar amount of secondary refunds issued	\$ <u>511,465.89</u>
Total dollar amount of refunds	<u>\$ 719,459.37</u>

<sup>1</sup>Primary cases are those resulting from a specific consumer inquiry. Secondary cases are those resulting from a portfolio review by the lender following a primary refund, as required by the Corporation's assumption fee inquiry process.

The Corporation's headquarters' officials told us that inquiries are still being received. These inquiries, plus the 301 questionnaires pending resolution, may raise the total amount of refunds to more than a million dollars. Refunds have averaged about \$608 per case, so far. However, it should be noted that the Corporation has contracts with over 2,800 seller/servicers and the inquiries received related to only 300. The Corporation does

not know whether the other seller/servicers overcharged borrowers.

The Corporation's headquarters' officials said that they have asked all seller/servicers to review their assumption fee policy and voluntarily refund excessive charges. They said that they were unaware of any such voluntary refunds and had not set up a reporting system to collect such information. They stated, however, that they have amended their audit program for their on-site reviews of seller/servicers to include an analysis of the appropriateness of assumption fees. If noted, the Corporation planned to require refunds to be made by the seller/servicers even though borrowers have not requested them. Officials said that hopefully all 2,800 seller/servicers will be audited within the next 2 years. Until that time, the actual number and total amount of overcharges and refunds will not be known.

We suggested that, in the interim, to try to obtain appropriate refunds for borrowers, the Corporation should request each seller/servicer to report voluntary refunds, emphasizing that the Corporation has authority to disqualify them if fees are excessive and that the Corporation plans to audit each one's fees within the next 2 years in any case. The officials said that they planned to discuss this suggestion with their Board of Directors.

We were subsequently contacted by the Vice President, Congressional and Governmental Relations, who said that the Corporation agrees with our suggestion and plans to require each seller/servicer on whom no complaints of excessive assumption fees have been received to certify that its fees comply with Corporation policy or make and report appropriate refunds. The official said the Corporation plans to make certain all seller/servicers comply with this policy through the Corporation's required annual audits of seller/servicers by private accounting firms.

The Corporation took one final action concerning this issue-- a policy fee change. As a result of its assumption inquiry procedures, it has had occasion to examine the processing costs of many seller/servicers, and it changed the assumption fee policy again based on this experience. Effective February 1, 1984, the policy for new assumptions is as follows:

"The Servicer may charge and retain a fee of the greater of \$400 or 1 percent of the unpaid principal balance, with a maximum fee of \$900."

It should be noted that the Corporation does not allow the mortgages it purchased to be assumed except for (1) those fixed-rate mortgages subject to so called "window periods"--periods during which assumptions are still permitted--established due to laws in a few states under the Garn-St. Germain Depository Institutions

Amendments of 1982 and (2) all adjustable rate mortgages written on Corporation documents which allow assumptions and which are purchased by the Corporation.

SUMMARY OF CORPORATION ACTIONS  
AND GAO OBSERVATIONS

Although the Corporation was aware of the charging of excessive assumption fees by some seller/servicers as early as September 1981, it said in its August 24, 1983 press release that it believed the problem was not widespread, and it handled complaints individually. After considerable publicity and congressional interest, the Corporation assigned top priority to identifying overcharges in August 1983. We believe its actions since then have been adequate within the Corporation's organizational constraints. In the future, the possibility of excessive fees being charged should be diminished because its fee policy has been clarified and because fewer assumptions will be permitted. The Corporation plans to:

- continue using its assumption fee inquiry process to make certain that appropriate refunds are made as long as complaints are being regularly received and
- make certain that all seller/servicers are audited and that overcharges are refunded to borrowers not yet identified.

Because it may be several years before the Corporation audits each of its seller/servicers, we suggested that it request seller/servicers to voluntarily identify and refund overcharges and report to it so that appropriate refunds are made to at least some of the borrowers who have not contacted the Corporation.

Corporation officials agreed with our suggestion and said that they plan to:

- require each seller/servicer on whom no complaints of excessive assumption fees have been received to certify that its fees comply with corporation policy and make and report appropriate refunds and
- review the appropriateness of such assumption fees through its required annual audits of seller/servicers by private accounting firms.

Until these actions are completed, it will be impossible to determine the total number and amount of excessive assumption fees and refunds. We plan to continue to meet with Corporation officials periodically as part of our ongoing oversight responsibility, but do not plan any further work on this issue.

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As arranged with your office, we did not obtain written agency comments on this report. We did, however, discuss its contents with Corporation officials who concluded that the report accurately describes the issue. Unless you publicly announce its contents earlier, we will not make any further distribution of this report for 5 days after the date of signature. At that time we will send copies to the Corporation and make copies available to other interested parties.

Sincerely yours,



J. Dexter Peach  
Director