

Report to Congressional Committees

June 2019

FEDERAL HOUSING ADMINISTRATION

Improved Procedures and Assessment Could Increase Efficiency of Foreclosed Property Conveyances



Highlights of GAO-19-517, a report to congressional committees

Why GAO Did This Study

FHA insures hundreds of thousands of single-family home mortgages annually. When an FHA borrower defaults, the mortgage servicer in many cases forecloses, obtains title to the property, and conveys ownership to FHA. FHA inspects the property, acquires it if it complies with condition standards and title requirements, and lists the property for sale. FHA may reconvey noncompliant properties to servicers. During conveyance, homes may sit vacant for months and can deteriorate, contributing to neighborhood blight.

Senate Report 114-243 included a provision for GAO to review FHA's effectiveness and efficiency in reaching determinations of conveyable condition. This report discusses (1) timelines for FHA property conveyances in 2010-2017 and whether servicers and FHA met time requirements, and (2) changes FHA has made to the conveyance process in recent years and any ongoing process challenges. GAO analyzed FHA data on properties conveyed in 2010-2017, reviewed FHA's policies and procedures, and interviewed 20 randomly selected mortgage servicers accounting for more than one-third of active FHA mortgages.

What GAO Recommends

GAO recommends that FHA (1) enhance the content and communication of policies and procedures on conveyance condition, (2) provide written direction on alternatives to reconveyance, and (3) develop a plan to assess a pilot program. FHA agreed with the second and third recommendations and did not agree or disagree with the first.

View GAO-19-517. For more information, contact Daniel Garcia-Diaz at (202) 512-8678 or garciadiazd@gao.gov.

FEDERAL HOUSING ADMINISTRATION

Improved Procedures and Assessment Could Increase Efficiency of Foreclosed Property Conveyances

What GAO Found

From July 2010 through December 2017, the process for conveying foreclosed properties to the Federal Housing Administration (FHA) took a median of 70 days. The conveyance process—which GAO measured from a mortgage servicer's obtaining title to and possession of the property to FHA's marketing of the property—involves servicers making repairs, transferring ownership, and filing a mortgage insurance claim, and FHA inspecting the property. FHA attributes the length of time to complete the process partly to foreclosure processing delays that left properties vulnerable to damage and vandalism, which can increase the time servicers need to bring properties into conveyance condition. Property damage also may increase the likelihood that FHA will reconvey a property (transfer it to the servicer) for not complying with condition standards, further extending the conveyance process. For about 55 percent of properties conveyed in July 2010-December 2017, servicers exceeded the required time to obtain title and possession of a foreclosed property and convey it to FHA. For 2017 alone, the corresponding figure was 72 percent. As a result, servicers were not eligible to be reimbursed for all repairs and interest expenses for those properties when filing insurance claims with FHA.

In recent years, FHA changed aspects of its conveyance process to help address some of the execution challenges the agency and servicers have faced. For example, in 2016, FHA enhanced its data system for conveyed properties to reduce manual administrative processing. FHA also began a pilot program in 2017 to decrease the number of properties FHA reconveys by inspecting properties before conveyance. However, GAO found shortcomings in FHA policies, procedures, and assessment efforts that are inconsistent with federal evaluation criteria and internal control standards, as follows:

- FHA's policies and procedures lack detail that could help servicers and contractors determine if a property is in compliance, and the agency has not examined alternative methods of communicating this information. Fifteen of the 20 servicers GAO interviewed said existing policies, procedures, and communications often were not clear or specific enough to address property conditions or repair decisions they encountered. FHA also relies on brief written policies to explain standards and makes limited or no use of other methods, such as photographs or industry-wide calls.
- FHA has not provided written direction on when to use alternatives to reconveyance—such as agreements under which servicers make repairs or repay FHA for any repair costs after conveyance—for properties not meeting condition standards. In the absence of such direction, FHA may not be addressing these properties in the most consistent or effective manner.
- FHA has not developed a plan to assess the outcome of its inspection pilot.
 Without rigorous assessment, FHA risks making decisions about the future of the pilot based on inaccurate or incomplete information.

Addressing these shortcomings could help improve the efficiency and effectiveness of FHA's property conveyance process.

Contents

Letter		1
	Background	4
	FHA's Property Conveyance Process Often Takes a Long Time, and Servicers and Contractors Performance against Time	
	Requirements Varied FHA Changed Aspects of the Conveyance Process, but Policies	14
	and a Pilot Program Still Have Limitations	33
	Conclusions	45
	Recommendations Agency Comments and Our Evaluation	46 46
Appendix I	Objectives, Scope, and Methodology	48
Appendix II	Comments from the Department of Housing	
The state of the s	and Urban Development	54
Appendix III	GAO Contact and Staff Acknowledgments	56
Tables		
	Table 1: Number of Properties Conveyed and Reconveyed Annually, 2012–2017	18
	Table 2: Percentage of Compliance Contractor Reviews That Met Federal Housing Administration's (FHA) Time	10
	Requirements, Properties Conveyed, 2011–2017	31
	Table 3: Results of Federal Housing Administration (FHA) Preconveyance Inspection Pilot, as of November 5, 2018	44
Figures		
	Figure 1: Examples of Properties Conveyed to the Federal Housing Administration in 2018	7
	Figure 2: Number of Properties Conveyed to the Federal Housing Administration (FHA), 2010–2017	9
	Figure 3: Federal Housing Administration's Property Conveyance Process	10

Figure 4: Length of the Federal Housing Administration's (FHA)	
Property Conveyance Process, July 2010–December 2017	15
Figure 5: Damage at Properties in the Atlanta and Baltimore Areas That the Federal Housing Administration Designated for	10
Reconveyance	17
Figure 6: Median Length of Conveyance Process for Properties That Were and Were Not Reconveyed to Servicers by the	
Federal Housing Administration (FHA), 2012–2017	19
Figure 7: Use of Federal Housing Administration (FHA) Property	
Disposition Methods, Fiscal Years 2010–2017	21
Figure 8: Length of Default and Foreclosure Period for Properties Conveyed to the Federal Housing Administration (FHA),	
July 2010–December 2017	24
Figure 9: Length of the Federal Housing Administration's (FHA) Conveyance Process from July 2010 through December	
2017, by Default and Foreclosure Period Quartile	26
Figure 10: Number of Days for Servicers to Complete the Federal Housing Administration (FHA) Preconveyance Period for	
Properties Conveyed during July 2010–December 2017	28
Figure 11: Percentage of Properties Conveyed to the Federal	
Housing Administration (FHA) with at Least One	
Overallowable Request, July 2010–December 2017	35
Figure 12: Examples of Flooring Damage at Properties Conveyed	
to the Federal Housing Administration in 2018	40

Abbreviations

asset disposition system P260 Asset Disposition and Management

System

CWCOT Claims without Conveyance of Title program

enterprises government-sponsored enterprises

FAQ frequently asked questions
FHA Federal Housing Administration

HOA homeowners association HOC homeownership center

HUD Department of Housing and Urban

Development

REO real estate-owned servicers mortgage servicers

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

June 20, 2019

The Honorable Susan M. Collins
Chairwoman
The Honorable Jack Reed
Ranking Member
Subcommittee on Transportation, Housing
and Urban Development, and Related Agencies
Committee on Appropriations
United States Senate

The Honorable David E. Price
Chairman
The Honorable Mario Diaz-Balart
Ranking Member
Subcommittee on Transportation, and Housing
and Urban Development, and Related Agencies
Committee on Appropriations
House of Representatives

The Federal Housing Administration (FHA) within the Department of Housing and Urban Development (HUD) facilitates homeownership by insuring lenders against losses on mortgages that finance purchases of properties or refinance existing FHA mortgages. In fiscal year 2018, FHA insured about one million single-family mortgages, providing about \$209 billion in mortgage insurance.

Each year, mortgage servicers (servicers) foreclose on a portion of the FHA-insured mortgages that go into default and file insurance claims with FHA.¹ One method of disposing of foreclosed properties involves a servicer conveying a property's title (transferring ownership) to FHA, which then markets and sells the home. Servicers conveyed about 31,700 foreclosed properties to FHA in calendar year 2017, the most recent year for which data were available when we conducted our analysis. In general, the properties are vacant for some or all of the period between

¹Mortgage servicers are bank or nonbank entities that perform activities such as accepting loan payments, initiating collection actions for delinquent payments, modifying loan terms, and foreclosing if necessary. Mortgages may be serviced by the originator of the loan or another entity.

foreclosure and FHA's sale of the home.² We and others previously reported that vacant properties can deteriorate if not maintained and can contribute to crime, blight, and declining property values in surrounding neighborhoods.³

To convey a foreclosed property to FHA, a servicer must complete several steps that include, but are not limited to, obtaining good and marketable title, ensuring the property is vacant and secured, and removing exterior and interior debris.⁴ Once the servicer conveys the title to FHA, FHA inspects the property to determine whether it meets conveyance requirements before selling the property out of its real estate-owned (REO) inventory.⁵ In this report, we define the conveyance process as beginning when the servicer obtains good and marketable title and takes possession of the property and ending when FHA markets the property.

Timely execution of the conveyance process can help minimize the time properties sit vacant and get foreclosed properties on the market sooner.

²HUD regulations allow occupied properties to be conveyed to FHA in certain cases, such as when state or local law prohibits the eviction of a tenant who is making regular monthly payments. According to FHA, this happens in less than 1 percent of conveyances.

³For example, see GAO, *Vacant Properties: Growing Number Increases Communities' Costs and Challenges*, GAO-12-34 (Washington, D.C.: Nov. 4, 2011); and *Mortgage Foreclosures: Additional Mortgage Servicer Actions Could Help Reduce the Frequency and Impact of Abandoned Foreclosures*, GAO-11-93 (Washington, D.C.: Nov. 15, 2010).

⁴According to HUD regulations, good and marketable title means the title is free from all liens, including any unpaid ground rents, taxes, or special assessments. See 24 C.F.R. § 203.386.

⁵In two prior reports on FHA's REO process, we found that FHA's divided approach to custody of foreclosed properties (between servicers and FHA) could delay the start of steps needed to sell properties and may have contributed to FHA taking substantially longer to market properties than other mortgage entities. As a result, in an April 2002 report, we recommended that HUD determine and implement the optimal method of establishing unified property custody, seeking additional statutory authority if needed. Although HUD generally agreed with the recommendation, it said it would need to research the feasibility of implementation. HUD ultimately determined it would not be advisable to establish unified property custody and did not implement our recommendation. In a June 2013 report, we made 10 recommendations to increase the potential for higher returns on disposed REO properties and improve oversight of the REO disposition program, all of which HUD implemented. See GAO, Single-Family Housing: Opportunities to Improve Federal Foreclosure and Property Sale Processes, GAO-02-305 (Washington, D.C.: Apr. 17, 2002); and Federal Housing Administration: Improving Disposition and Oversight Practices May Increase Returns on Foreclosed Property Sales. GAO-13-542 (Washington, D.C.: June 20, 2013).

Senate Report 114-243, accompanying the Transportation and Housing and Urban Development, and Related Agencies Appropriations Bill, 2017, includes a provision for us to review FHA's effectiveness and efficiency in reaching determinations of conveyable condition on foreclosed properties. This report examines (1) time lines for FHA foreclosed property conveyances from July 2010 through December 2017 and the extent to which servicers and FHA met time requirements, and (2) changes FHA has made to the conveyance process in recent years and any ongoing process challenges.

To examine time lines for property conveyances and the extent to which servicers and FHA met time requirements, we reviewed FHA regulations and policies about the time frames FHA, its contractors, and mortgage servicers must meet for conveyed properties. We also analyzed property foreclosure and conveyance data from two FHA data systems for properties conveyed to FHA in 2010–2017 (2017 was the most recent year for which data were available when we conducted our analysis). Our time line analyses begin in July 2010 because FHA changed how it managed the conveyance process in June 2010. To assess the reliability of FHA's data, we reviewed FHA documentation and conducted electronic testing, including checks for outliers, missing data fields, and erroneous values. We determined these data were sufficiently reliable for purposes of characterizing the length of the conveyance process and servicer and FHA timeliness.

To determine recent changes FHA made to the conveyance process and any ongoing process challenges, we reviewed updates to FHA regulations, policies, and procedures for conveyances since 2010 and interviewed FHA officials on reasons for the changes. We also interviewed FHA headquarters and field office officials and FHA contractors with responsibilities for property inspections and approving servicer property preservation costs about any challenges they experience executing the conveyance process. We conducted semistructured interviews with a nongeneralizable random sample of 20 large- and medium-sized servicers of FHA-insured mortgages about any challenges they have had with conveyance policies and procedures, including time lines and property preservation allowances. These servicers accounted for more than one-third of active FHA-insured

⁶S. Rep. No. 114-243, at 125 (2016).

⁷Unless otherwise noted, all years in this report are calendar years.

mortgages as of December 31, 2017. We also visited eight recently conveyed or reconveyed properties in the Baltimore, Maryland, and Atlanta, Georgia, areas to observe property conditions and understand any challenges in documenting and addressing condition issues. Appendix I describes our scope and methodology in greater detail.

We conducted this performance audit from September 2017 to June 2019 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Established by the National Housing Act, FHA's single-family mortgage insurance program helps home buyers obtain financing by providing insurance on single-family mortgage loans. The mortgage insurance allows FHA-approved private lenders to provide qualified borrowers with mortgages on properties with one to four housing units and generally compensates lenders for nearly all the losses incurred on such loans. To support the program, FHA imposes up-front and annual mortgage insurance premiums on FHA borrowers. The agency has played a particularly large role among first-time, minority, and low-income home buyers. For example, in fiscal year 2017, about 82 percent of FHA-insured home purchase loans went to first-time home buyers and more than 33 percent went to minority home buyers.

Foreclosure Mitigation and Property Disposition Methods

FHA requires servicers to undertake certain home retention and foreclosure mitigation actions to help delinquent homeowners catch up on late mortgage payments. Before initiating foreclosure actions, FHA requires servicers to contact the borrower, collect information on the borrower's finances, and attempt informal methods of resolving the delinquency. If informal steps are not appropriate for a borrower's circumstances, the servicer evaluates the borrower for a series of home retention actions, which include a formal forbearance and repayment plan and a loan modification. Under certain circumstances, the servicer may

⁸The Mutual Mortgage Insurance Fund, which supports this program, is statutorily required to maintain at least a 2 percent capital ratio, defined as the fund's economic net worth divided by the remaining principal balance on all insured loans in the fund.

consider a foreclosure mitigation option, such as a preforeclosure (short) sale or a deed-in-lieu of foreclosure. If the home retention and foreclosure mitigation actions are unsuccessful, the servicer or mortgage note holder is generally entitled to pursue foreclosure to obtain title to the property. The foreclosure process is governed by state laws, but foreclosed properties are typically auctioned at a foreclosure sale. Most foreclosed properties are disposed of in one of two ways.

- Claims without Conveyance of Title (CWCOT). Through FHA's CWCOT program, the servicer attempts to secure a third-party purchase of an eligible property for an adjusted fair market value that is less than the amount of the servicer's projected claim. 10
- Conveyance. If the foreclosure process is completed and no third
 party purchases the home at the foreclosure sale, the home usually
 becomes the property of the servicer. Servicers convey these
 properties to FHA, which sells them out of its REO inventory.

During the default and foreclosure process, servicers must meet two FHA time requirements. 11 The first requires servicers to initiate a foreclosure (first legal action) or utilize a loss mitigation option within 6 months of borrower default. The second requirement, for the "reasonable diligence" period, requires servicers to obtain good and marketable title and possession of a property within a specified time frame that varies by state. The servicer secures the property and obtains possession once the property is vacant. Servicers are subject to financial penalties for missing these deadlines. In both cases, servicers must curtail the debenture

⁹In a preforeclosure sale, the servicer agrees to accept the proceeds from the sale of the property to a third party, although the sale price is less than the sum of the principal, accrued interest, and other expenses owed. In a deed-in-lieu, a delinquent borrower avoids foreclosure by agreeing to transfer the property title to the lender.

¹⁰In 2014, FHA began utilizing its revised CWCOT program, which requires servicers to offer all eligible properties for sale through CWCOT before using the conveyance process.

¹¹According to FHA servicing guidance, a loan goes into default 30 days after the borrower has missed a full payment.

interest that they otherwise would be entitled to collect from the date of the missed time frame. 12

Servicers are responsible for maintaining vacant foreclosed properties in accordance with FHA requirements, which specify allowable reimbursable amounts to preserve and protect the property. A servicer needing additional funds to complete the required maintenance must submit an "overallowable" request to FHA.

Property Conveyance Process

When a servicer forecloses on a property with an FHA-insured mortgage and the property is not sold to a third party through CWCOT, the property is held in the servicer's name until the servicer conveys the title to FHA. As seen in figure 1, these properties span a range of home types and ages. FHA requires servicers to preserve and protect the property and ensure it meets FHA's conveyance condition standards before conveying title. FHA's preservation and protection requirements include a number of specific steps for securing, maintaining, and repairing properties and documenting property conditions. FHA reimburses the servicer for up to \$5,000 per property for required work, and the servicer may request overallowable funds if needed. FHA's conveyance condition standards are broader requirements, including that a property be undamaged by natural disaster and in "broom swept" condition, have all damage covered by hazard insurance repaired, and be undamaged by the servicer's failure to properly secure or maintain the property. In the property of the propert

¹²Servicers typically use borrowed funds to finance the payment of outstanding debt on mortgages in the process of foreclosure. When servicers bid on properties at foreclosure sales, they continue to use borrowed funds to finance the recovered properties. Servicers pay interest on these borrowings, which is referred to as the cost of funds, until they file claims with FHA when properties are conveyed. FHA compensates servicers for their interest expenses at what is known as the debenture interest rate. The rate is set by statute at the monthly average yield on U. S. Treasury securities for the month in which the default on the mortgage occurred, adjusted to a constant maturity of 10 years. See 12 U.S.C. § 1715o.

¹³Servicers generally hire vendors to complete property preservation and protection work and any work needed to get the property into conveyance condition.

¹⁴Servicers generally are not required to fix damage caused by the borrower.

Figure 1: Examples of Properties Conveyed to the Federal Housing Administration in 2018









Source: GAO. | GAO-19-517

HUD regulations state that the servicer must obtain good and marketable title and convey the property to HUD within 30 days of the date on which the servicer filed the foreclosure deed for record or certain other key dates, whichever is later. ¹⁵ If a servicer does not believe it will be able to convey the property by this time, it may request an extension from FHA. The servicer files an insurance claim with FHA when it conveys the title. If a servicer does not convey the property within the required time frame and has not received an approved extension, the servicer must curtail the

¹⁵For mortgages insured on or after November 19, 1992, servicers must obtain good and marketable title and transfer the property to FHA within 30 days of the later of the filing of the foreclosure deed for record; recording date of the deed-in-lieu of foreclosure; acquiring possession of the property; expiration of the redemption period; or the date of any extension provided by FHA. See 24 C.F.R. § 203.359(b).

debenture interest and property preservation and protection expenses it claims as of the date of the missed deadline. ¹⁶

Shortly after conveyance, FHA pays the Part A claim to the servicer, which includes the unpaid principal balance and debenture interest on the insured mortgage. At this time, FHA becomes responsible for maintaining the property until it is sold. FHA pays the part of the claim that covers eligible property preservation and protection expenses incurred by the servicer once the servicer submits title evidence and documentation of expenses (in Part B of the claim form). FHA inspects the property and reviews title evidence before selling the property out of its REO inventory. In some cases, FHA reconveys the title to the servicer if it finds the servicer did not comply with requirements related to property condition or title. When a property is reconveyed, FHA reassigns the title to the servicer and requests repayment of the claim amount. The servicer then must correct any title or property condition issues before it may convey the property and submit a claim to FHA again.

Throughout this process, FHA and servicers use the P260 Asset Disposition and Management System (asset disposition system) to communicate and upload documentation about the properties. FHA articulates its property preservation and protection requirements and conveyance condition standards in a mortgagee letter and policy handbook that we refer to collectively as FHA's conveyance condition policies and procedures.¹⁷

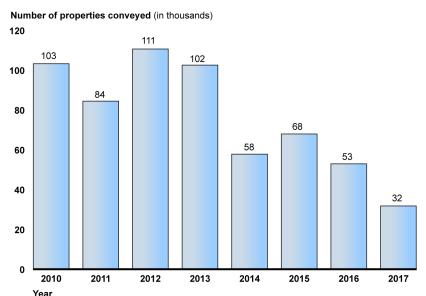
From 2010 through 2017, servicers conveyed about 610,000 properties to FHA. The number of properties conveyed annually peaked in 2012 at about 111,000 (see fig. 2). In 2017, servicers conveyed fewer than 32,000 properties to FHA. The decline in recent years is consistent with improvements in the housing market since the 2007–2011 housing crisis. ¹⁸

¹⁶If the servicer missed one of the earlier deadlines—the first legal action or reasonable diligence time frames—it already should have curtailed debenture interest from that point.

¹⁷See Department of Housing and Urban Development Mortgagee Letter 2016-02 (Washington, D.C.: Feb. 5, 2016); and Handbook 4000.1, Single Family Housing Policy Handbook (Washington, D.C.: Dec. 30, 2016). Mortgagee letters are written instructions that FHA periodically issues to its approved lenders and servicers.

¹⁸According to the S&P/Case Shiller National Home Price Index, average home prices fell each year in 2007–2011, for a total decline of almost 27 percent.

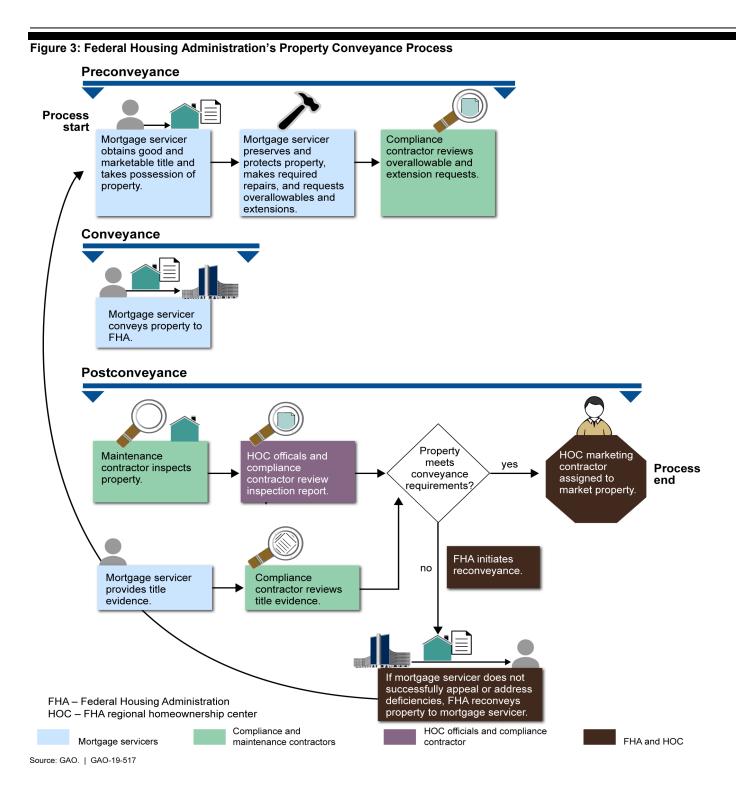
Figure 2: Number of Properties Conveyed to the Federal Housing Administration (FHA), 2010–2017



Source: GAO analysis of FHA data. | GAO-19-517

Roles and Responsibilities in the Conveyance Process

In this report, we define FHA's property conveyance process as beginning when the servicer both obtains good and marketable title and takes possession of a property and ending when FHA assigns a marketing contractor to sell the property out of its REO inventory (see fig. 3).



Page 10

Several FHA contractors and offices play key roles in the conveyance process.

- Compliance contractor. A nationwide compliance contractor called the mortgagee compliance manager is responsible for protecting FHA's interests in properties conveyed to FHA and communicates directly with servicers about the properties. The compliance contractor reviews property inspections to ensure properties meet conveyance condition standards, reviews requests from servicers for extensions of conveyance times or for overallowable expenses, reviews servicer claims for compliance with requirements, and responds to servicer inquiries about pre- and postconveyance responsibilities. The compliance contractor is located in Oklahoma City, Oklahoma, and is overseen by FHA's National Servicing Center.
- Maintenance contractor. Maintenance contractors, called field service managers, are responsible for inspecting properties recently conveyed to FHA and preserving properties in FHA's REO inventory. FHA has multiple maintenance contractors; they are responsible for properties in different regions. Upon conveyance, the maintenance contractor conducts a comprehensive property inspection to determine if the property meets conveyance condition standards and completes the HUD Property Inspection Report. The maintenance contractor also conducts other inspections at a property before conveyance, as warranted, including a preconveyance inspection at the request of the servicer and an overallowable inspection if requested by the compliance contractor. While these contractors conduct general maintenance on the property, they typically do not make major repairs, because FHA generally sells conveyed properties in as-is condition.
- Marketing contractor. Marketing contractors, called asset managers, are responsible for marketing and selling the homes in FHA's REO inventory.
- FHA homeownership centers. FHA carries out its mortgage insurance and REO disposition programs through four regional offices called homeownership centers (HOC). The centers are located in Atlanta, Georgia; Denver, Colorado; Philadelphia, Pennsylvania; and

Santa Ana, California. 19 Officials in each HOC are responsible for overseeing the maintenance and marketing contractors for their region and reviewing HUD Property Inspection Reports to determine if conveyed properties should be reconveyed to the servicer due to condition issues. This determination is then forwarded to the compliance contractor for an additional review.

HUD's Office of Finance and Budget. Staff from this office are
responsible for reviewing servicer mortgage insurance claims for
compliance with FHA requirements. The office selects a sample of
claims from the past 3 years to review whether the property
preservation and protection expenses were within allowable limits and
whether the servicer curtailed debenture interest and property
preservation and protection expenses accurately, among other things.

Other Participants in the Mortgage Market

A number of other federal and federally sponsored entities participate in the mortgage market. Along with FHA, the Department of Veterans Affairs and the Department of Agriculture operate programs that guarantee single-family mortgages made by private lenders. Additionally, two government-sponsored enterprises—Fannie Mae and Freddie Mac (enterprises)—purchase and securitize single-family mortgages.

¹⁹The Atlanta HOC serves Alabama, the Caribbean, Florida, Georgia, Illinois, Indiana, Kentucky, Mississippi, North Carolina, South Carolina, and Tennessee. The Denver HOC serves Arkansas, Colorado, Iowa, Kansas, Louisiana, Minnesota, Missouri, Montana, New Mexico, Nebraska, North Dakota, Oklahoma, South Dakota, Texas, Utah, Wisconsin, and Wyoming. The Philadelphia HOC serves Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, and West Virginia. The Santa Ana HOC serves Alaska, Arizona, California, Hawaii, Idaho, Nevada, Oregon, and Washington.

²⁰The Department of Veterans Affairs Loan Guaranty program is an entitlement for veterans, certain members of the National Guard or Reservists who are currently serving, and spouses of certain veterans. The Department of Agriculture's Single Family Housing Guaranteed Loan Program guarantees mortgages for low- and moderate-income households in eligible rural areas.

²¹Congress established the enterprises as for-profit, shareholder-owned corporations. The enterprises purchase conventional mortgages that meet their underwriting standards. They package the mortgages they purchase into mortgage-backed securities, which are sold to investors in the secondary mortgage market. In exchange for a fee, the enterprises guarantee the timely payment of interest and principal on the securities they issue. In 2008, the Federal Housing Finance Agency placed the enterprises into conservatorships out of concern that their deteriorating financial condition threatened the stability of financial markets.

However, the property disposition programs for these entities are not directly analogous to FHA's. In contrast to FHA, the Department of Veterans Affairs and the enterprises take custody of and are responsible for properties closer to the time of the foreclosure sale. ²² The enterprises require servicers to convey properties to them within 24 hours of foreclosure sale or deed-in-lieu of foreclosure, while the Department of Veterans Affairs requires servicers to provide notice of their intent to convey properties within 15 days of foreclosure sale. Also in contrast to FHA, the Department of Agriculture does not take possession of foreclosed properties with guaranteed loans, but rather oversees their disposition by lenders.

In FHA's case, properties are often held in the lender's or servicer's name for an extended period after the foreclosure sale. Following the foreclosure sale, FHA requires servicers to oversee properties during redemption periods, to evict residents if properties not in redemption periods are occupied, and to continue property preservation and protection activities. In addition, before conveyance, servicers must identify and pay any homeowners association (HOA) fees and utility bills that are due. As described in figure 3, servicers also must make any required repairs, meet other conveyance requirements, and pass an FHA property inspection, or face the prospect of having the property reconveyed. FHA officials said this approach reduces FHA's holding time and costs and that the agency does not have the infrastructure to manage and fund property repairs itself.

²²However, all the entities have property preservation requirements that servicers must follow for vacant properties securing delinquent loans.

²³Certain states provide the previous owners of foreclosed properties with a right of redemption that allows them to pay amounts owed to the lender and reclaim ownership. During redemption periods, the previous owner or current occupant is allowed to remain in the residence and the REO property owner or servicer generally is not permitted to pursue activities such as evicting property residents or securing properties.

FHA's Property
Conveyance Process
Often Takes a Long
Time, and Servicers
and Contractors
Performance against
Time Requirements
Varied

Conveyance Times
Increased after 2011,
Partly Due to Greater Use
of Other Disposition
Methods and Extended
Default and Foreclosure
Periods

Data on Time Frames for Conveyance and Reconveyance

From July 2010 through December 2017, the property conveyance process took a median of 70 days, but this figure varied widely by year. ²⁴ Our analysis of FHA data found that, from 2011 through 2015, the median number of days to complete the conveyance process increased four-fold (from 41 to 161 days) and varied more widely around the median each successive year (see fig. 4). ²⁵ Conveyance time frames declined

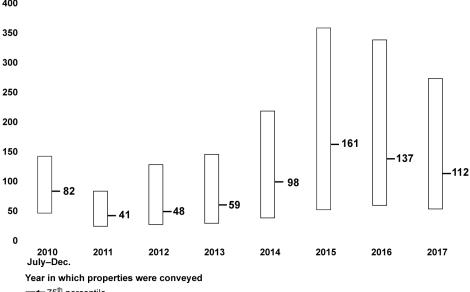
²⁴We collected data on FHA property conveyances from January 2010 through December 2017, but excluded properties conveyed before July 2010 from our analysis because FHA changed the way it managed property conveyances in June 2010. Specifically, at that time FHA launched the third generation of its Management and Marketing contractor program. Under prior arrangements, FHA's contractors were responsible for both the maintenance and marketing of FHA's REO properties. Under the current structure, separate contractors perform these functions. FHA also began a new compliance management contract in June 2010.

²⁵From July 2010 through December 2010, the median length of the conveyance process was 82 days. FHA officials told us the length of the conveyance process that year was affected by program changes, including the introduction of a new Management and Marketing contractor program.

substantially in 2016 and 2017 (to a median of 137 days and 112 days, respectively) while continuing to vary considerably around the median. In comparison, FHA officials said the conveyance process generally should take about 37 days to complete—30 days for servicers to make necessary repairs and convey title to FHA and 7 days for FHA to inspect the property, communicate any condition issues identified during the inspection, and assign a marketing contractor to promote and sell it.²⁶

Figure 4: Length of the Federal Housing Administration's (FHA) Property Conveyance Process, July 2010–December 2017

Days
400



← 75th percentile **—** Median ← 25th percentile

Source: GAO analysis of FHA data. | GAO-19-517

Note: We excluded properties conveyed from January through June 2010 from our analysis because FHA changed how it managed the conveyance process in June 2010.

We also found that the time it took properties to complete the conveyance process varied by HOC region. For the entire July 2010–December 2017 period, the Philadelphia HOC had the highest median time frame (91 days) and the Atlanta HOC the lowest (56 days). The Santa Ana and

²⁶These time frames are consistent with regulatory and contract performance requirements discussed later in this report.

Denver HOCs had medians of 78 and 67 days, respectively. A number of factors may have contributed to differences among the HOCs, such as the number of properties conveyed in each region (which can affect servicer and HOC capacity) and the age of the housing stock (which can affect the time needed to make repairs).

The time to complete the conveyance process includes, when applicable, the time needed for FHA to reconvey a property—that is, transfer ownership to the servicer due to condition or title issues—and for the servicer to convey it to FHA a second time. FHA officials said they try to avoid reconveyances because they prolong the conveyance process and result in FHA incurring additional preservation and protection costs. Figure 5 shows examples of condition issues at properties we visited in the Baltimore, Maryland, and Atlanta, Georgia, metropolitan areas that were in the reconveyance process.

²⁷Our analysis of available FHA data on reconveyance reasons indicates that about 69 percent of properties were reconveyed from October 31, 2016, through December 2017 because of condition issues and about 28 percent due to title issues, such as liens on the property. Less than 2 percent of properties were reconveyed because they had both condition and title issues.

²⁸To reconvey a property, FHA first issues the servicer a preliminary notice of intent to reconvey that lists the reasons for the reconveyance. Servicers may appeal the notices.

Figure 5: Damage at Properties in the Atlanta and Baltimore Areas That the Federal Housing Administration Designated for Reconveyance



Mold and ceiling damage in kitchen



Mold damage in basement



A door that was broken into Source: GAO. | GAO-19-517



Ceiling damage from a roof leak

Our analysis of FHA data found that reconveyances were not common enough to significantly affect median conveyance time frames, but substantially lengthened the conveyance process when they did occur. As shown in table 1, servicers conveyed 406,863 properties to FHA from 2012 through 2017—the period within our scope for which FHA had reliable reconveyance data. In comparison, FHA reconveyed 8,874 properties to servicers during that time frame.²⁹ The annual number of reconveyances rose from 1,019 in 2012 to 1,935 in 2015, before declining to 1,099 in 2017.

²⁹According to FHA officials, data on reconveyances in the asset disposition system were not reliable before calendar year 2012.

Table 1: Number of Properties Conveyed and Reconveyed Annually, 2012–2017

Year	Number of properties conveyed to FHA	Number of properties reconveyed to servicers	
2012	108,852	1,019	
2013	100,434	1,752	
2014	55,287	1,595	
2015	65,170	1,935	
2016	49,101	1,474	
2017	28,019	1,099	
Total	406,863	8,874	

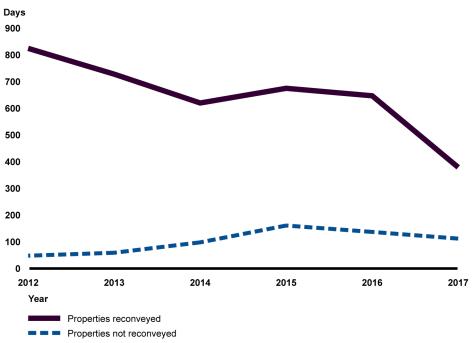
Legend: FHA = Federal Housing Administration

Source: GAO analysis of FHA data. | GAO-19-517

Note: Reconveyances may have not occurred in the same year as the original conveyance.

We also found that the median time to complete FHA's conveyance process in 2012–2017 was more than 614 days longer for reconveyed properties than the median for properties not reconveyed. However, the difference between the medians declined over time, dropping from 777 days in 2012 to 267 days in 2017 (see fig. 6).

Figure 6: Median Length of Conveyance Process for Properties That Were and Were Not Reconveyed to Servicers by the Federal Housing Administration (FHA), 2012–2017



Source: GAO analysis of FHA data. | GAO-19-517

Servicers and FHA must take several steps to complete the conveyance process for reconveyed properties, which may account for some of the length of the time frames. Once the compliance contractor has notified the servicer that a property has condition issues that must be resolved to avoid reconveyance, the servicer may appeal. FHA officials said appeals can add up to 120 days to the conveyance process. If the servicer is unable to resolve the issues and the appeals are denied, FHA reconveys the property and the servicer must reimburse FHA for the original claim amount. The servicer then must complete any required repairs, resolve any title issues, prepare a new evidence package for FHA showing that condition and title issues were addressed, and submit a request to FHA's compliance contractor to convey the property again. FHA's compliance contractor then has 10 business days to review the evidence package and notify the servicer of its decision. Once conveyance is approved, the servicer may resubmit a new mortgage insurance claim form and evidence that the property deed has been filed in FHA's name.

Factors Likely Contributing to Increased Length of Conveyance Process Two factors that likely contributed to the increase in the time to complete FHA's conveyance process are increased use of other disposition methods and property damage stemming from extended default and foreclosure periods.

Increased use of third-party sales. FHA data indicate that from 2010 through 2017 servicers increasingly disposed of properties through third-party sales using the CWCOT program. As previously noted, in 2014 FHA began requiring servicers to offer all eligible properties for sale through CWCOT before using the conveyance process. According to our analysis of FHA property disposition data, in fiscal years 2010–2017, the share of properties disposed of through CWCOT rose from about 1.4 percent to almost 44 percent, while the share of conveyance and REO sales dropped from about 84 percent to 42 percent (see fig. 7). The remaining properties were disposed of through notes sales or preforeclosure sales. The same sales are properties were disposed of through notes sales or preforeclosure sales.

³⁰Data on FHA property dispositions are published annually in HUD reports to Congress on the Mutual Mortgage Insurance Fund. See Department of Housing and Urban Development, *Annual Report to Congress Regarding the Financial Status of the FHA Mutual Mortgage Insurance Fund, Fiscal Year 2018* (Washington, D.C.: Nov. 15, 2018).

³¹FHA conducts note sales by auctioning pools of defaulted FHA-insured loans through its Distressed Asset Stabilization Program. The loan pools are generally sold at a price below the outstanding principal balance.

Percentage 100 90 80 70 60 50 40 30 20 2010 2011 2012 2013 2014 2015 2016 2017 Fiscal year Real estate-owned (REO) sales (conveyed properties)^a Note sales Third-party sales (claims without conveyance of title program) Preforeclosure sales

Figure 7: Use of Federal Housing Administration (FHA) Property Disposition Methods, Fiscal Years 2010–2017

Source: GAO analysis of FHA data. | GAO-19-517

Increased use of CWCOT may have extended property conveyance time frames for two reasons. First, servicers must attempt to sell all eligible properties through CWCOT while simultaneously preparing them for conveyance, which may add additional time to the conveyance process according to FHA officials. Second, properties conveyed to FHA because they are not eligible for or sold through the CWCOT program are generally in poorer condition and require more repairs, according to servicer representatives.³² This may contribute to extended conveyance

^aData represent the number of properties sold from FHA's REO inventory, which includes properties conveyed to FHA in prior years.

³²Properties that are not eligible for the CWCOT program include those for which the FHA-insured mortgage is subject to indemnification and those for which the servicer's projected conveyance claim amount is less than the FHA Commissioner's adjusted fair market value for the property. Properties with surchargeable damage are also not eligible. Surchargeable damage is caused by fire, flood, earthquake, tornado, boiler explosion (for condominiums only), or mortgagee (servicer) neglect.

time frames. For example, a representative from one mortgage industry group told us that properties ineligible for CWCOT and conveyed to FHA generally require more than the \$5,000 in preservation and protection costs that FHA allows. In these cases, servicers may request additional funds from the compliance contractor, but processing the requests may prolong the conveyance process, as discussed later in this report.

Representatives from one servicer and two mortgage industry groups stated they prefer the CWCOT program because it reduces the need to convey properties. They said the conveyance process is costly and comes with the risk of reconveyance. FHA data show that REO sales generally had higher loss severity rates (the financial loss on a defaulted loan as a percentage of the unpaid principal balance) than properties disposed of through alternative methods, including the CWCOT program. For example, for the last quarter of fiscal year 2017, FHA reported that the loss severity rate for properties sold through REO was 54.8 percent, while the combined loss severity rate for properties disposed of through alternative methods was 43.8 percent. However, some of this difference may be attributable to the poorer condition of conveyed properties, as discussed previously.

National Mortgage Settlement

In February 2012, the Department of Justice and 49 states settled with the five largest mortgage servicers— Ally Financial, Inc. (formerly GMAC), Bank of America Corporation, Citigroup Inc., J.P. Morgan Chase & Co., and Wells Fargo & Company — to address mortgage servicing, foreclosure, and bankruptcy abuses. The agreement settled state and federal investigations finding that these servicers routinely signed foreclosure-related documents without verifying their validity and without the presence of a notary public—a practice known as "robosigning."

Source: GAO and U.S. Department of Justice | GAO-19-517

Extended default and foreclosure periods. According to FHA officials, properties with long default and foreclosure periods may be in poor condition because they deteriorate if servicers delay property maintenance and repairs. ³³ FHA officials said this was common for properties conveyed to FHA after the 2012 National Mortgage Settlement because some servicers delayed foreclosure proceedings to limit their exposure to litigation in 2010 and 2011 (see sidebar).

FHA officials said that after the Department of Justice issued the National Mortgage Settlement in February 2012, servicers who had been delaying default and foreclosure started conveying large numbers of properties.³⁴ According to FHA and servicer representatives, damaged properties can take longer to convey because they require extensive repairs to meet FHA's conveyance condition standards.

The results of our analysis of FHA data are broadly consistent with these observations. The number of properties conveyed to FHA increased by 31 percent (from 84,363 to 110,567) between 2011 and 2012, the year of the settlement. Additionally, the default and foreclosure period for conveyed properties (the time between the borrower defaulting on the mortgage and the servicer obtaining title to and possession of the property) increased over most of the July 2010–December 2017 time frame. As shown in figure 8, the median default and foreclosure period was 416 days for properties conveyed in July–December 2010, peaked at 664 days (about 60 percent higher) for properties conveyed in 2015, and fell to 612 days for 2017 conveyances. The overall upward trend was even more pronounced for properties with default and foreclosure periods at the 75th percentile. The 75th percentile was 555 days for properties conveyed from July through December 2010, peaked at 1,152 days

³³The length of a property's default and foreclosure period is affected by the reasonable diligence requirements in the state in which the property is located. For example, some states have a legally required redemption period. Many states also require servicers to foreclose on the borrower through court proceedings (judicial foreclosure), which may be lengthy.

³⁴In 2015, FHA proposed a change to federal regulations that would have established a maximum amount of time for a servicer to file a claim with FHA and convey the property without the insurance contract being terminated. According to the proposed regulation, this change was meant to address the practice of servicers waiting to file FHA insurance claims for multiple properties at one time. HUD withdrew the proposed change in response to comments expressing concerns about the reasonableness of the proposed limit

(about 108 percent higher) for properties conveyed in 2016, and declined to 1,068 days for 2017 conveyances.

Days 1,200 1,000 800 600 200 2010 2011 2012 2013 2014 2015 2016 2017 July-Dec. Year in which properties were conveyed 75th percentile Median • • 25th percentile

Figure 8: Length of Default and Foreclosure Period for Properties Conveyed to the Federal Housing Administration (FHA), July 2010–December 2017

Source: GAO analysis of FHA data. | GAO-19-517

Note: The default and foreclosure period is the time between the borrower defaulting on the mortgage and the servicer obtaining title to and possession of the property. We excluded properties conveyed from January through June 2010 from our analysis because FHA changed how it managed the conveyance process in June 2010.

Certain regulatory and policy changes also may have increased the default and foreclosure periods since 2013. HUD issued a mortgagee letter in 2013 that increased the reasonable diligence time frames and allowed servicers additional time to complete foreclosures in certain states. For example, the reasonable diligence time frame for properties in New York increased from 13 to19 months. Also, in 2014 mortgage servicing rules issued by the Consumer Financial Protection Bureau went

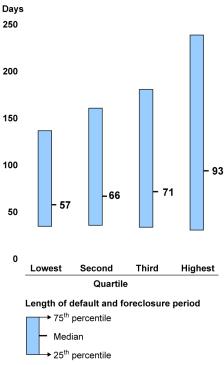
³⁵Department of Housing and Urban Development, Mortgagee Letter 2013-38 (Washington D.C.: Oct. 28, 2013).

into effect that restricted servicers' ability to initiate a foreclosure and gave borrowers additional time to pursue loss mitigation options. Specifically, servicers may not initiate foreclosure proceedings if a borrowers' application is pending for a loan modification or other alternatives to foreclosure.³⁶

In addition, we found that properties with longer default and foreclosure periods generally took longer to complete the conveyance process than properties with shorter default and foreclosure periods (see fig. 9). Specifically, from July 2010 through December 2017 properties with the longest default and foreclosure periods—those in the highest quartile—took 93 days at the median to complete the conveyance process and 238 days at the 75th percentile. In comparison, properties with the shortest default and foreclosure periods—those in the lowest quartile—took 57 days at the median to complete the conveyance process and 136 days at the 75th percentile for that same period. As previously stated, FHA officials told us that properties with long default and foreclosure periods may have deteriorated if servicers were not maintaining them. These properties may have required additional repairs to bring them into conveyance condition.

³⁶Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10696 (Feb. 14, 2013); and Mortgage Servicing Rules Under the Truth in Lending Act (Regulation Z), 78 Fed. Reg. 10902 (Feb. 14, 2013).

Figure 9: Length of the Federal Housing Administration's (FHA) Conveyance Process from July 2010 through December 2017, by Default and Foreclosure Period Quartile



Source: GAO analysis of FHA data. | GAO-19-517

Note: We excluded properties conveyed from January through June 2010 from our analysis because FHA changed how it managed the conveyance process in June 2010.

As previously noted, overall conveyance time frames declined in 2016 and 2017 from their peak in 2015. FHA officials attributed this improvement largely to the decreasing number of conveyances affected by the National Mortgage Settlement. As discussed earlier, the settlement contributed to a wave of properties that took a long time to convey, potentially due to damage sustained during extended default and foreclosure periods. FHA officials also indicated that the improved housing market in recent years has resulted in fewer foreclosures and, therefore, fewer property conveyances to FHA. Consequently, servicers and contractors may be better able to manage the workload associated with property conveyances and complete the process more quickly.

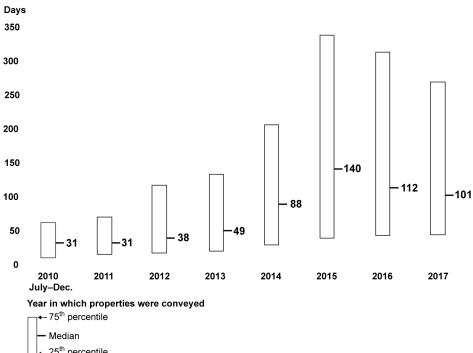
Servicers Often Did Not Convey Properties within the Required Time Frame, but Usually Provided Title Evidence on Time

From July 2010 through December 2017, servicers generally did not convey properties to FHA within the regulatory 30-day time frame (preconveyance period). The preconveyance period, servicers must ensure the property has good and marketable title, conduct routine inspections and maintenance on the property, and ensure the property meets conveyance condition standards. If servicers do not believe they will be able to convey a property within 30 days, they may request an extension. The median number of days servicers took to complete the preconveyance period increased from 31 in July–December 2010 to 140 in 2015 (see fig. 10). This figure declined after 2015, dropping to 101 days in 2017. Variation around the median was considerable, especially in more recent years. For example, in 2017 the time to complete the preconveyance period was 43 days at the 25th percentile, compared with 268 days at the 75th percentile.

³⁷As previously discussed, servicers must obtain good and marketable title and transfer the property to HUD within 30 days of the later of the filing of the foreclosure deed for record; recording date of deed-in-lieu of foreclosure; acquiring possession of the property; expiration of the redemption period; or date of any extension provided by FHA. While FHA does not collect some of the individual dates listed in the regulation, FHA officials said servicers submit a date on their claim forms—the date of possession and acquisition of marketable title—that represents the later of all of the dates except for the extension date. We used this date as the start date for measuring the length of the preconveyance period.

³⁸As previously noted, we excluded properties conveyed to FHA before July 2010 from our analysis because they were managed using different systems and contractors than currently used.

Figure 10: Number of Days for Servicers to Complete the Federal Housing Administration (FHA) Preconveyance Period for Properties Conveyed during July 2010-December 2017



25th percentile

Source: GAO analysis of FHA data. | GAO-19-517

Note: We excluded properties conveyed from January through June 2010 from our analysis because FHA changed how it managed the conveyance process in June 2010.

The percentage of properties for which servicers did not convey in 30 days plus any approved extension grew from about 31 percent in July-December 2010 to about 72 percent in 2017. For the entire period from July 2010 through December 2017, the corresponding percentage was 55 percent. Representatives of 13 of the 20 servicers we interviewed said that meeting the 30-day timeline was one of their top challenges with the conveyance process.

Representatives of servicers and mortgage industry groups cited several reasons for servicers needing additional time to convey. For example, representatives of 11 servicers cited the heavily damaged condition of the properties they acquired as one of the primary reasons for not conveying properties within 30 days. Servicer representatives also noted other reasons, including four who cited waiting for responses on hazard insurance claims and five who cited difficulty in obtaining HOA bills to

pay. In addition, representatives of two mortgage industry groups and three servicers told us that meeting all the conveyance and title requirements simultaneously is a major challenge. For example, representatives of one mortgage industry group said a servicer may have completed required property repairs and paid HOA fees and utility bills, but if the property were subsequently vandalized, the servicer would have to delay conveyance to complete repairs. By that point, the servicer might no longer be current on HOA and utility payments. Servicers have the option to request an extension to the preconveyance time frame if they think they will be unable to convey a property in 30 days. Servicers requested a conveyance extension for about 40 percent of the properties conveyed from July 2010 through December 2017. FHA approved the extensions in about 40 percent of these cases.³⁹

In addition, representatives from six of the 20 servicers we interviewed said FHA's process for reviewing servicers' overallowable requests (additional funds needed to complete work) negatively affected their ability to convey properties in 30 days. Once a servicer makes an overallowable request, FHA's compliance contractor has 5 business days to review it and either reject the request or approve all or some of the requested amount. (We discuss the compliance contractor's ability to meet this and other time requirements in the following section.) Servicers may appeal any rejections, in which case the compliance contractor has 3 business days to make a final determination. Six servicer representatives said that the time it takes the compliance contractor to make overallowable decisions may cause them to exceed the 30-day time frame, especially when they submit multiple requests for the same property. For context, our analysis of FHA data found that in 2017, the median number of servicer overallowable requests per property was 13. and the median number of appeals per property was six.

In contrast to the preconveyance requirement, servicers usually met the time requirement for giving title evidence to FHA. Title evidence includes documentation that FHA is the legal owner of the property, including a copy of the mortgage documentation, a legal description of the property, and a copy of the recorded deed in FHA's name. Servicers may provide title evidence to FHA at any point during the conveyance process up to 45

³⁹FHA officials told us that most conveyance extension requests are submitted so the servicer can file a hazard insurance claim, but they also receive such requests when the servicer believes preservation and protection work at a property will take longer than 30 days to complete.

days after filing the deed. If servicers believe they will be unable to provide title evidence within 45 days, they may submit an extension request to the compliance contractor. According to FHA data, servicers were able to provide title evidence within 45 days plus any approved extension for 84 percent of properties conveyed from July 2010 through December 2017.

FHA Contractors Involved in Property Conveyances Largely Met Time Requirements

FHA's compliance and maintenance contractors generally met the required time frames for key conveyance tasks for properties conveyed from 2011 through 2017.⁴¹ However, when the contractors did not meet their required time frames, the delays may have lengthened the time to complete the conveyance process for some properties.

Compliance contractor. FHA established a time frame of 5 business days for the compliance contractor to conduct various reviews in the preand postconveyance periods. In the preconveyance period, the compliance contractor reviews requests for overallowables, conveyance extensions, and conveyance of a property with surchargeable damage. The contractor also reviews title evidence and extension requests for title evidence, which are generally submitted after conveyance. Table 2 shows the percentage of properties conveyed from 2011 through 2017 for which the compliance contractor met the 5 business day requirement, according to our analysis of FHA data.

⁴⁰According to FHA regulations, if the servicer is unable to provide title evidence, it is considered out of compliance with conveyance requirements and FHA may reconvey the property, cancel the servicer's claim for insurance benefits, and request reimbursement for any expenses incurred for acquisition, holding, and reconveyance from the date the claim is filed. If the title documentation the servicer provides is insufficient, the servicer may provide additional evidence in 10 days. If FHA identifies a title defect, the servicer has 60 days to correct it.

⁴¹We excluded July–December 2010 from this analysis because, as previously noted, FHA revised its Management and Marketing contractor program in June 2010. The revisions involved changing the requirements and scope of the contracts and hiring new contractors. According to FHA, the transition to the revised Management and Marketing program may have led to work backlogs that caused conveyance tasks to take longer to complete than in prior periods. We excluded data from this atypical period to avoid skewing the results our compliance analysis.

Table 2: Percentage of Compliance Contractor Reviews That Met Federal Housing Administration's (FHA) Time Requirements, Properties Conveyed, 2011–2017

	Preconveyance Reviews		Postconveyance Re	views
Overallowable requests	Conveyance extensions	Surchargeable damage	Title evidence extensions	Title evidence
90.8%	93.3%	94.2%	94.5%	86.7%

Source: GAO analysis of FHA data. | GAO-19-517

Note: FHA has a time frame of 5 business days for the compliance contractor to conduct these reviews.

Although the contractor mostly met the required time frames, when it did not, the delay may have lengthened the time to complete the conveyance process. Our analysis of FHA data indicates that when the compliance contractor missed the deadlines, it missed them by a median of 4–10 days, depending on the requirement.⁴² The compliance contractor's review of overallowable requests, conveyance extension requests, and surchargeable damage requests generally occurs during the preconveyance period when servicers have 30 days to convey the property to FHA. As noted earlier, some servicer representatives we interviewed said that waiting for the compliance contractor to approve or deny overallowable requests hindered their ability to convey the property in 30 days.

The compliance contractor must complete at least 95 percent of the reviews within the 5-day time frame to meet FHA's standard for minimum acceptable performance. FHA uses monthly scorecards when reviewing the contractor's performance against this standard. ⁴³ FHA officials told us they had not issued any deficiency notices to the current compliance contractor, but that discussions with the contractor can occur when it does not meet the 95 percent standard in particular months. FHA officials also noted that some of the contractor's reviews may take longer than 5

⁴²For perspective, the median length of the conveyance process for properties conveyed from July 2010–December 2017 was 70 days. Our analysis of FHA data indicates that for properties conveyed in 2011–2017, when the compliance contractor missed the 5 business day deadline, at the median it missed the deadline to review title evidence by 4 days, overallowable requests by 7 days, conveyance extension requests by 8 days, and surchargeable damage and title extension requests by 10 days.

⁴³Although a detailed assessment of FHA's contractor oversight was outside the scope of our review, we requested and reviewed examples of these scorecards to determine how FHA monitored contractor performance.

days if resolving them requires obtaining additional documentation or substantial back-and-forth communications with the servicer.

Maintenance contractors. After conveyance, FHA's maintenance contractors have 2 calendar days from the date they are assigned a property to conduct the comprehensive property inspection and upload the results into a HUD Property Inspection Report in FHA's asset disposition system. ⁴⁴ They then have 5 calendar days to complete a Property Condition Report, which details the functionality of the property's systems, the existence of any transferable warranties, and any legal actions, such as code violations or pending demolition orders. FHA starts measuring compliance with these time requirements 24 hours after the properties are assigned to the compliance contractor (to account for holidays and late afternoon assignments).

According to our analysis of FHA data, the maintenance contractors completed property inspections and uploaded the results within 3 days (the 2-day requirement plus 24 hours) for about 90 percent of properties conveyed from 2011 through 2017. The contractors met the 5-day requirement to complete the Property Condition Report about 77 percent of the time. When the maintenance contractors missed these time frames, they missed them by a median of 1 and 2 days, respectively. The longer a property remains uninspected after the servicer has conveyed it, the greater the chance that it will be damaged or vandalized before inspection. If a property is damaged during this period, disputes may arise between FHA and the servicer about which entity is responsible for the damage. FHA is responsible for maintaining the property once the servicer complies with all HUD regulatory requirements leading to conveyance, including filing the deed (in FHA's name) for record and filing the conveyance claim. However, FHA may hold the servicer responsible for the damage if the claim was suspended due to the need for review or correction resulting from certain types of noncompliance with HUD requirements or if the servicer could not prove the damage occurred after FHA became responsible for maintaining the property. Disagreement over this issue can add time to the conveyance process.

FHA measures each maintenance contractor's performance monthly using a formula that considers both the contractor's timeliness in

⁴⁴According to FHA officials, the asset disposition system automatically assigns a conveyed property to the maintenance contractor when the servicer files the conveyance claim.

completing property inspections and uploading the results (2-day requirement plus 24 hours) and in completing the Property Condition Report (7-day requirement plus 24 hours) for each property. If the contractor misses either deadline, it is not considered timely for that property. FHA considers timeliness for 95 percent of properties each month as satisfactory. According to FHA officials, FHA has taken actions when the performance of maintenance contractors was not satisfactory. A HOC official said that the actions may include issuing a defective performance letter, which requires the contractor to provide a remedy plan, and issuing a cure notice in coordination with HUD's contracting office.

FHA Changed
Aspects of the
Conveyance Process,
but Policies and a
Pilot Program Still
Have Limitations

FHA's Updates to Property Preservation Allowances and Data Systems Partly Addressed Certain Servicer Challenges

FHA updated aspects of the conveyance process in recent years to help address some of the challenges experienced by servicers and the agency. For example, FHA increased property preservation and protection allowances in 2016 to help address servicer feedback and to better align allowances with other mortgage industry participants, according to FHA officials. In February 2016, FHA issued Mortgagee Letter 2016-02, which increased allowance amounts that servicers may claim for specific types of property preservation and protection work. It also increased the total maximum amount servicers may claim for a property without submitting an overallowable request from \$2,500 to \$5,000. However, the mortgagee letter eliminated all exclusions from the maximum amount, which previously included one-time major repairs, such as a roof replacement. FHA officials said the agency increased the allowance amounts to account for the standard increases in property

preservation costs over time, and to align allowances with those of the enterprises and the Department of Veterans Affairs. 45

Seventeen of the 20 servicers we interviewed said that FHA's current property preservation and protection allowances are not sufficient to complete the work needed to convey properties. While representatives of eight of the 20 servicers told us the changes FHA made to allowances in 2016 helped them complete work within allowance amounts, representatives of the remaining 12 servicers said the changes did not help or helped in some ways but presented more challenges in other ways. Representatives of an association of mortgage lenders and servicers said that they preferred the previous system, because some work was excluded from the maximum allowance. For example, representatives of one servicer said that due to the 2016 changes, they now must submit an overallowable request for standard maintenance items, such as grass cuts, once they have exceeded the maximum allowance amount.

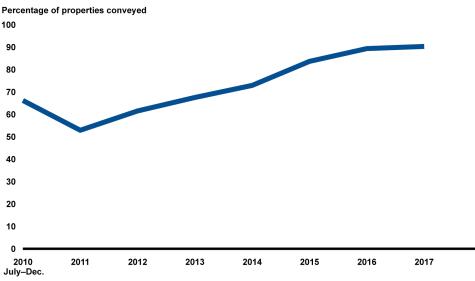
Our analysis of FHA data found that the percentage of properties with at least one overallowable request increased steadily from 2011 through 2017—from about 53 percent to about 90 percent—despite the 2016 changes (see fig. 11). 46 For properties with at least one overallowable request, the median number of requests before the 2016 changes (from July 1, 2010, through February 4, 2016) was seven, compared with eight after the changes (from February 5, 2016, through the end of 2017). 47 In 2017 alone, the median number of overallowable requests per conveyed property was 13. However, it may be too early to tell what effect the 2016 mortgagee letter will have on servicer's ability to conduct work within the allowances. FHA officials said that although the change in the allowance amounts was partly intended to reduce overallowable requests, the poor condition of many properties with extended default and foreclosure periods may have increased such requests. The officials stated that some of these properties were still being conveyed to FHA in 2017.

⁴⁵While property disposition processes at the enterprises and the Department of Veterans Affairs differ from FHA's, those entities have preservation allowances for maintenance servicers must complete on vacant properties that may be compared to FHA's.

⁴⁶Sixty-six percent of the properties conveyed from July through December 2010 had at least one overallowable request.

 $^{^{47}}$ FHA instituted the previous allowance schedule on July 13, 2010, in Mortgagee Letter 2010-18.

Figure 11: Percentage of Properties Conveyed to the Federal Housing Administration (FHA) with at Least One Overallowable Request, July 2010–December 2017



Year in which properties were conveyed

Source: GAO analysis of FHA data. | GAO-19-517

Note: We excluded properties conveyed from January through June 2010 from our analysis because FHA changed how it managed the conveyance process in June 2010.

FHA enhanced the information system servicers and contractors use to manage conveyed properties, but officials noted the need to update another system FHA uses to process and pay claims. In March 2018, FHA incorporated its preconveyance inspection pilot, discussed in more detail later in this report, into the asset disposition system, the information system servicers use to convey properties to FHA. FHA officials and contractors also use the system to track properties from conveyance through REO sale. With the update, servicers may request a preconveyance inspection and see the results of the inspection in the system, according to FHA officials. Before FHA added the pilot to the asset disposition system, servicers and FHA used email to communicate about properties in the pilot.

⁴⁸In the preconveyance inspection pilot, FHA conducts physical inspections of certain properties prior to conveyance and provides the servicer the opportunity to fix any issues before conveying the property.

In October 2016, FHA added a feature to the asset disposition system that enables FHA officials, contractors, and servicers to electronically monitor the status of reconveyed properties. According to FHA officials, all communication between FHA and servicers on reconveyed properties previously was by email, including the servicer's notification to FHA that it was ready to convey a property again, and the photographs required to document property condition. However, according to FHA officials, FHA's claims system is not equipped to process more than one claim per property, so claims for properties FHA reconveys and which the servicer then conveys to FHA a second time must be processed manually. Officials from FHA's Office of Financial Services said that manual processing delays claim payments to servicers—sometimes by more than a year. Seven of the 20 servicers we interviewed identified delayed claim payments for reacquired properties as a challenge. FHA officials said that they have made an internal business case for funding to modernize the system, but have not succeeded in securing the funding in prior years.

FHA Updated Its Policies and Procedures on Conveyance Condition, but Limitations Remain

FHA updated its written direction to servicers on conveyance condition in 2016, but limitations in the contents and methods of communicating these policies and procedures have contributed to compliance challenges for some servicers. In its February 2016 mortgagee letter, FHA reemphasized its existing directions to servicers about property conveyance, provided additional details on how to calculate claim amounts and document property preservation and protection work, and clarified descriptions of some preservation and protection requirements. Additionally, in December 2016, FHA issued an updated single-family housing policy handbook that consolidated all policies and procedures for servicers into one document, including those on maintaining and conveying foreclosed properties. However, servicers and other industry stakeholders with whom we spoke and our review of FHA's policies and procedures on conveyance condition identified several limitations, as follows.

Lack of clarity or specificity. Representatives from 15 of the 20 servicers we interviewed said they found FHA's policies and procedures on conveyance condition to be unclear or subjective, and 13 cited specific parts of the conveyance condition standards they found to be unclear or missing. For example, one servicer was unsure about the extent of repairs required when a property had water seepage in the basement. We found that FHA's policies and procedures include information on how to treat a basement that is flooded or a property with moisture damage, but does not address basement leaks, cracks, or seepage. Representatives

of four servicers said that FHA's policies and procedures do not sufficiently address how servicers should handle properties with potential structural or foundation damage. Consistent with this viewpoint, we found that FHA's handbook and mortgagee letter do not explain what a servicer should do if it believes a property has damage affecting its structural integrity. In addition, representatives of three servicers said FHA's expectations of them are unclear when a roof is damaged but does not currently have a leak. According to FHA's policies and procedures, servicers must ensure all roofs "are free of active leaks or other sources of water intrusion." However, FHA does not specify what servicers should do if there is roof damage but no active leak. Two of the servicers said they were uncertain whether they should replace the damaged roof that is not leaking, or convey the property and risk reconveyance if it rains before FHA inspects the property and the roof leaks.

Perceived inconsistency in interpretation. Representatives from 10 of the 20 servicers we interviewed said FHA is somewhat or not at all consistent in determining whether properties meet FHA's conveyance requirements. Among the remaining 10, one stated that FHA is completely consistent and nine said that FHA is mostly consistent. In addition, two of the 20 servicers said the answers they receive from FHA to the same question differ depending on whom they ask. HOC officials also noted cases in which their interpretation of policies and procedures differed from the compliance contractor's. For example, officials from three HOCs told us that the compliance contractor sometimes disagrees with their determination that a property is not in conveyance condition when the contractor reviews the HOC's reconveyance decision.⁴⁹

Limited communication methods. In addition to formal written policies and procedures on conveyance condition, FHA fields servicer questions, primarily through its compliance contractor, by phone. The compliance contractor also issues an annual newsletter on topics such as common reconveyance triggers and best practices for submitting successful overallowable and extension requests. However, some servicers we interviewed suggested other possible ways to communicate policies and procedures that they said they would find helpful, including the following:

⁴⁹According to FHA's Director of the National Servicing Center, although the compliance contractor may point out issues, the HOCs have the final say in determining if a property gets reconveyed.

- Representatives of five servicers said they would like FHA to publish an authoritative set of frequently asked questions (FAQ) on conveyance condition. FHA has an FAQ web page that includes information on conveyance condition, but, as of April 2019, did not include FAQs about the specific property preservation and protection issues discussed above (water seepage, structural integrity, and roof damage with no active leaks). In addition, a link in the web page labeled "foreclosure/conveyance" led to a few FAQs on conveyance condition and property preservation requirements, but the answers consisted solely of language from FHA's existing policies and procedures.
- One servicer's representatives suggested that FHA could issue policies and procedures in a format similar to Fannie Mae's Property Preservation Matrix and Reference Guide. This guide has features that FHA's policies and procedures do not have, as discussed below, including photographic examples, detailed requirements for photographic documentation, and "if-then" statements detailing what servicers should do if they encounter certain challenges at a property.
- Representatives of two servicers suggested that FHA host regular industry calls. While the compliance contractor told us that it takes ad hoc calls and holds regular teleconference calls with a number of individual servicers, an FHA official told us the contractor is only authorized to respond to servicer questions by providing relevant parts of FHA's written policies and procedures and is not supposed to respond with interpretations (clarifications, or explanations) of existing policies and procedures. Representatives from one servicer said industrywide calls with FHA staff would give servicers a way to obtain fuller explanations of FHA's expectations.
- One servicer suggested that FHA provide training to servicers about the conveyance process. The servicer noted that while FHA provides training on other aspects of its program, including loss mitigation, it does not do so for the conveyance process or submitting claims.

Limited direction on photographic evidence. FHA's policies and procedures provide instructions for servicers and contractors on how to document property conditions, but contain limited direction on photographic evidence. Servicers must thoroughly document the condition of the property when they first obtain possession so that FHA does not hold them responsible for damage caused by the borrower. Servicers also must take before and after pictures of any work they do on the property. FHA's policies and procedures on photographic documentation say only that the servicer must use digital photography,

ensure a date-stamp is printed within each photograph, and ensure that each photograph is labeled to describe the contents of the photograph. FHA has not communicated in writing any requirements for photograph dimensions, color, distance, framing, or content or suggestions for documenting conditions that may be difficult to see.

Servicers and FHA officials stated that they face challenges in documenting property conditions in a way that most accurately informs the compliance contractor about the property. The compliance contractor reviews documentation, including photographs, uploaded into the asset disposition system by servicers to make decisions on overallowable and extension requests. The compliance contractor also reviews documentation from maintenance contractors on inspection results and reconveyance recommendations by HOC officials. An FHA maintenance contractor told us that the compliance contractor sometimes responds that the condition described is not apparent from the photographs in the asset disposition system. According to members of an industry group representing servicers, in some cases this may result in FHA requiring servicers to repair damage caused by the borrower, because the servicers' photographs did not prove the damage was present when they first gained possession of the property.

To illustrate how photographs can effectively or ineffectively capture property condition problems, figure 12 provides two examples of flooring issues at properties conveyed to FHA. In one photograph, the buckling of the floor is apparent, but in the other, the waterlogged and warped condition of floor is harder to discern. An experienced FHA maintenance contractor told us there are creative ways to document some conditions that are difficult to photograph. For example, to document a damp floor, one can photograph a piece of paper (which darkens when wet) before and after placing it on the floor. This method is not included in FHA's handbook or mortgagee letter.

Figure 12: Examples of Flooring Damage at Properties Conveyed to the Federal Housing Administration in 2018



Buckled flooring over a wet subfloor at a property in the Atlanta area.

Waterlogged and warped flooring from a roof leak at a property in the Baltimore area. The damage is not visible in the photo—a challenge servicers may face in documenting property condition.

Source: GAO. | GAO-19-517

Limitations in the content and delivery of FHA's policies and procedures on conveyance condition suggest room for improvement and are inconsistent with the federal internal control standard for communicating externally. This standard calls for management to externally communicate the necessary quality information to achieve an entity's objectives. ⁵⁰ Federal agencies can help ensure compliance by communicating with and obtaining information from external parties and by periodically evaluating and selecting appropriate methods of communication, taking into account factors such as the audience, the purpose and type of information being given, and legal or regulatory requirements.

However, FHA has not identified where the conveyance condition policies and procedures could be improved because it has not assessed information from servicers—for example, the frequency or content of their questions to the compliance contractor. FHA also has not thoroughly evaluated its methods for communicating its policies and procedures. As a result, FHA has limited assurance that servicers understand FHA's

⁵⁰GAO, Standards for Internal Control in the Federal Government, GAO-14-704G (Washington, D.C.: Sept. 10, 2014).

expectations for conveyed properties and that contractor decisions are made consistently. Weaknesses in these areas can contribute to inefficiencies such as delays in executing conveyances and reconveyance of properties to servicers.

FHA Has Not Provided
Direction on Alternatives to
Reconveyance for
Properties That Do Not
Meet Conveyance
Condition Standards

FHA has not provided written direction to HOC officials on choosing among alternatives to address conveyed properties that do not meet FHA's condition standards.⁵¹ According to officials from FHA headquarters and the National Servicing Center, HOC officials can (1) reconvey the property's title to the servicer, (2) issue a demand letter establishing a debt to FHA for the cost of the work needed, or (3) enter into a reconveyance bypass agreement with the servicer that requires the servicer to complete repairs within a certain number of days. The latter two options avoid reconveyance and therefore may expedite resale of the property. These three options are mentioned in different parts of FHA's policies and procedures, but the agency has not outlined the circumstances that would warrant use of each method.

FHA has not provided direction to the HOCs, partly because HOC officials have the authority to choose a method based on the expected financial return on the property. However, HOC officials with whom we spoke differed in the factors that they considered when deciding how to address properties that do not meet FHA's conveyance condition standards. Officials from three HOCs cited criteria that any property with more than \$5,000 in damage due to servicer neglect should be considered for reconveyance, while a bypass agreement or demand letter may be issued if the amount of servicer neglect is less than \$5,000. However, FHA officials were not able to tell us where this criterion is written. An official from the fourth HOC said the decision to reconvey partly depends on the strength of the housing market. If the HOC believes it can sell the property in its current condition—even if the condition does not meet FHA's conveyance standards—the HOC will be more likely to issue the servicer a demand letter than reconvey the property. In contrast, an official from one of the other HOCs told us the state of the housing market did not factor into decisions on reconveyance. Furthermore, according to FHA officials, HOCs may also reconvey a property with only small amounts of damage if the servicer frequently conveys properties not in

⁵¹FHA may allow properties to be conveyed damaged in certain prescribed situations with prior approval.

conveyance condition, in order to impress on the servicer the importance of complying with FHA requirements.

The HOC officials generally agreed that bypass agreements offer a way for small repairs to be fixed quickly. However, an official from one HOC said the HOC did not issue bypass agreements often because servicers' property preservation and protection vendors may take longer than the time specified in the agreement to complete repairs and, since the title is in FHA's name, FHA has no recourse with the servicer. An official from another HOC also said that he did not like issuing bypass agreements because servicers do not always complete repairs quickly.

FHA does not produce reports on the HOCs' use of reconveyance, demand letters, and bypass agreements, so the frequency with which the HOCs employ these methods is unknown. Some servicer representatives with whom we spoke noted apparent inconsistency among the HOCs. For example, representatives of three servicers said that some HOCs do not issue bypass agreements at all. Similarly, representatives of one servicer told us they have infrequently, if ever, received a demand letter for small condition issues at properties; rather, FHA reconveys the properties for minor condition issues.

FHA's lack of written direction on alternatives to reconveyance is inconsistent with federal internal control standards, which call for designing control activities, including policies, to achieve objectives.⁵² Granting HOC officials discretion in dealing with properties that do not meet condition standards gives them flexibility to respond to specific circumstances. However, without written direction on factors to consider when determining whether they should reconvey a property, issue a demand letter, or enter into a bypass agreement with the servicer, FHA lacks reasonable assurance that HOCs make determinations consistently and in line with the agency's regulatory goals for the REO program—to dispose of properties in a manner that expands home ownership, strengthens neighborhoods and communities, and ensures a maximum return to the mortgage insurance fund.⁵³ Balancing these goals may require using different methods to address properties that do not meet conveyance standards. For example, in some cases issuing a demand letter or a bypass agreement for certain properties may result in FHA

⁵²GAO-14-704G.

⁵³²⁴ C.F.R. § 291.1(a)(2).

marketing and selling the property more quickly than it would by reconveying the property. A quicker sale, in turn, may help avoid the negative effects of a vacant property on the surrounding neighborhood. However, if FHA accepts a property in poor condition, it may receive less in proceeds when selling the property, which negatively affects FHA's mortgage insurance fund.

FHA Does Not Have a Plan to Evaluate Its Preconveyance Inspection Pilot

FHA began a pilot program in 2017 to inspect properties that meet certain criteria before conveyance, but has not developed a plan to assess the results of the pilot program. FHA selected three large servicers to participate in this preconveyance inspection pilot. These servicers may request preconveyance inspections for properties with characteristics that increase their chances of being reconveyed, according to FHA officials. For example, eligible properties include those that experienced recurring vandalism, received overallowable repairs of greater than \$5,000, or have potential structural defects, foundation issues, or damp or wet basements. Based on the inspection results, the properties are approved to convey, approved to convey subject to repair with no additional inspection, or denied conveyance through the pilot (see table 3). After conveyance, FHA inspectors conduct a thorough inspection to confirm that the property meets conveyance condition standards. Properties that do not meet the standards may be reconveyed.

violations—for which the mortgagee requests approval to convey as-is; insurable claims with completed repairs in excess of \$5,000; unrepaired borrower neglect affecting mechanical, electrical, or plumbing, or having excessive mold; uninsurable and unfinished renovations the servicer has requested to convey as-is; and completed roof repairs in excess of \$2,500 that have unrepaired interior ceiling or wall damage. Properties with borrowers 35 or more months delinquent on the mortgage or that were vacant more than 12 months also are eligible, as are properties in a presidentially declared disaster zone with completed repairs exceeding \$5,000 or in Puerto Rico or Washington State. Reoccurring vandalism is defined as at least two completed vandalism repairs (paid with insurance proceeds) on a property the servicer has requested to convey as-is.

Table 3: Results of Federal Housing Administration (FHA) Preconveyance Inspection Pilot, as of November 5, 2018

Inspection result	Number of properties	Percentage of inspected properties
Approved to convey	190	27.3
Approved to convey subject to repairs	260	37.3
Denied conveyance	247	35.4
Total inspections	697	100.0

Source: FHA. | GAO-19-517

As of November 2018, FHA had not developed plans for evaluating the effectiveness of the pilot in achieving the goals of reducing the number of properties reconveyed due to property condition and minimizing the time it takes to convey properties. FHA officials told us that they will develop a plan to assess pilot outcomes when sufficient data are available. However, without an evaluation plan, FHA may not collect the right information during the pilot to rigorously assess results. GAO's guide for designing evaluations states that key components of an evaluation design include the evaluation questions or objectives; information sources and measures; data collection methods; an analysis plan, including evaluative criteria or comparisons; and an assessment of study limitations.⁵⁵

Certain characteristics of FHA's pilot underscore the importance of incorporating these components into evaluation design. For example, because the pilot is intended to expedite the conveyance process through preconveyance inspections, it will be important to isolate the impact of the inspections, potentially by making comparisons to a control group. A properly selected control group can rule out competing explanations for observed outcomes. Additionally, because the pilot may affect participating servicers in ways that extend beyond the speed of the conveyance process or the probability of reconveyance, it will be important for FHA to thoroughly consider the information sources and measures it uses, including participant feedback. For example, representatives of the three participating servicers told us they had concerns about FHA holding properties in the pilot to higher conveyance condition standards than nonpilot properties and the time it takes to complete the preconveyance inspection process. According to the representatives, this process, which includes 7 calendar days for the

⁵⁵GAO, *Designing Evaluations: 2012 Revision*, GAO-12-208G (Washington, D.C.: Jan. 31, 2012).

inspection and 5 business days for the HOCs to review the inspection report, has resulted in longer holding times and increased vandalism risks.

Without a well-designed evaluation, FHA risks making decisions about preconveyance inspections based on incorrect or incomplete information on the pilot's benefits and drawbacks.

Conclusions

While FHA increased the use of other property disposition methods in recent years, servicers still convey thousands of foreclosed properties to FHA annually. If the process of transferring ownership from the servicer to FHA is not efficient, these properties may sit vacant for prolonged periods, deteriorate, and contribute to neighborhood decline. As a result, it is critical for FHA to have effective and efficient policies and procedures for the conveyance process. While FHA has made recent updates to its handbook, mortgagee letters, and information systems, additional improvements would better align its processes and procedures with federal internal control standards and GAO guidance on designing evaluations:

- By addressing limitations in the content (including its detail) and communication of its policies and procedures on conveyance condition, FHA could help reduce uncertainty and inconsistency in the conveyance process that may contribute to inefficiencies, such as reconveyance of properties to servicers.
- Second, by providing direction to HOC officials on factors to consider when deciding whether to use alternatives to reconveyance for properties that do not meet conveyance condition standards, FHA could increase the likelihood that alternatives will be used consistently and in line with FHA's goals for the REO program.
- Third, by developing a plan for how it will evaluate the outcomes of the pilot to inspect certain properties prior to conveyance, FHA could help ensure the pilot generates the performance information needed to make effective management decisions about future policies.

By addressing these issues, FHA could make the conveyance process more efficient and therefore help reduce negative impacts on neighborhoods.

Recommendations

We are making the following three recommendations to FHA:

The Commissioner of FHA should enhance the content and communication of FHA's policies and procedures on conveyance condition, including by considering the program stakeholder views discussed in this report and other stakeholder input. (Recommendation 1)

The Commissioner of FHA should provide written direction to HOC REO directors on factors to consider when determining whether to reconvey a property with condition issues, issue a demand letter, or enter into a bypass agreement with the servicer. (Recommendation 2)

The Commissioner of FHA should develop a formal plan for evaluating the outcomes of the preconveyance inspection pilot that includes key elements of evaluation design—such as evaluation objectives and measures—and utilizes participant feedback and control groups, as appropriate. (Recommendation 3)

Agency Comments and Our Evaluation

We provided a draft of this report to FHA, the Department of Veterans Affairs, and the Federal Housing Finance Agency (the conservator and regulator of Fannie Mae and Freddie Mac) for their review and comment. The Department of Veterans Affairs and the Federal Housing Finance Agency did not provide comments. FHA provided written comments reproduced in appendix II. FHA neither agreed nor disagreed with our first recommendation to enhance the content and communication of its policies and procedures on conveyance condition. FHA cited the 2016 updates to its policy handbook and mortgagee letter and said it recognized the importance of external communication, training, and inperson meetings to ensure servicers have the information they need to operate in compliance with FHA programs. Our report discusses these updates, but also identifies areas for additional improvements to address limitations in the clarity and comprehensiveness of FHA's policies and procedures and methods for communicating them. FHA agreed with our second and third recommendations to provide written direction on considering alternatives to reconveyance and to develop a plan for evaluating the preconveyance inspection pilot.

We are sending copies of this report to the appropriate congressional committees, the Secretary of the Department of Housing and Urban Development, and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-8678 or garciadiazd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report are listed in appendix III.

Daniel Garcia-Diaz

Director, Financial Markets and

Community Investment

Appendix I: Objectives, Scope, and Methodology

Our objectives were to examine (1) timelines for Federal Housing Administration (FHA) foreclosed property conveyances in June 2010—December 2017 and the extent to which servicers and FHA met time requirements and (2) changes FHA has made to the conveyance process in recent years and any ongoing process challenges.

Time Lines for Property Conveyances

To address the first objective, we obtained data from FHA's Single Family Insurance System–Claims Subsystem and from the P260 Asset Disposition and Management System (asset disposition system) on the 610,802 foreclosed properties mortgage servicers conveyed to FHA from January 1, 2010, through December 31, 2017. For purposes of our analysis, we generally excluded properties conveyed to FHA from January 2010, through June 2010 because they were managed using different data systems and contractors than FHA currently uses.¹

After excluding these properties, we analyzed data for 544,421 properties conveyed to FHA from July 2010 through December 2017. (We use calendar years in this report unless otherwise noted.) We calculated the number of days it took each property to complete the conveyance process. We defined the start of the conveyance process as the date the servicer obtained possession and acquired marketable title for a property and the end of the process as the date on which FHA assigned a marketing contractor to sell the property. For each annual cohort of conveyed properties, we calculated the 25th, 50th (median), and 75th percentile time frames and compared these statistics across years.

To analyze the effect that reconveyances had on the length of the conveyance process, we compared length of time for conveyance in 2012–2017 for properties that were reconveyed to those that were not. According to FHA staff, data on reconveyances were unreliable prior to 2012, so we excluded those properties from this comparative analysis.

¹FHA launched the asset disposition system in April 2010 to manage the property conveyance process. Additionally, in June 2010, FHA launched the third generation of its Management and Marketing contractor program. Under prior arrangements, FHA's contractors were responsible for both the maintenance and marketing of FHA's real estate-owned properties. Under the current structure, separate contractors perform these functions. FHA also began a new compliance management contract in June 2010.

²Servicers submit a date on their claim forms indicating when they obtained possession and marketable title for the property, according to FHA officials. We used this date as the start of the conveyance process.

We interviewed FHA officials about factors that may have affected conveyance time frames from 2010 through 2017, including increased use of other disposition methods and servicers delaying foreclosure actions and the resulting impact on property conditions, since the asset disposition system does not disclose the reasons for any delays. To analyze changes in the use of different property disposition methods and to examine the loss severity rates for these methods, we reviewed FHA data for fiscal years 2010–2017. To understand the relationship between properties with long default and foreclosure periods and conveyance time frames, we measured the time between the borrower defaulting on the mortgage and the servicer obtaining title to and possession of the property (effectively, the end of the foreclosure process) for properties conveyed to FHA from July 2010 through December 2017. We divided the range of default and foreclosure periods into four quartiles. For each quartile, we calculated the length of the conveyance process at the median and at the 25th and 75th percentiles. We then compared these statistics across quartiles.

To determine the extent to which mortgage servicers and FHA contractors met their respective time requirements for the conveyance process, we identified relevant time requirements in Department of Housing and Urban Development (HUD) regulations and policies. We also reviewed the performance work statements for FHA's mortgagee compliance manager (compliance contractor) and field service managers (maintenance contractors) to identify the contractors' time requirements for the conveyance process. For servicers and contractors, we selected key time requirements for which electronic data were available, including the following:

Servicers

- Thirty calendar days from acquiring title and possession of a property, plus the length of any approved time extension, to convey property to FHA.
- Forty-five days from conveying a property to FHA, plus the length of any approved time extension, to provide FHA with title evidence.

Compliance contractor

- Five business days to review each overallowable request submitted by a servicer.
- Five business days to review the sufficiency of title documentation submitted by the servicer.

- Five business days to determine whether a servicer can convey a property with surchargeable damage.
- Five business days to approve or deny a servicer's conveyance or title extension request.

Maintenance contractor

- Two calendar days, plus an additional 24 hours, to complete and upload the HUD Property Inspection Report from the date the property was assigned.
- Five calendar days to complete a Property Condition Report from the date the Property Inspection Report was completed.

For each property, we calculated the number of days it took servicers and contractors to complete these required steps in the conveyance process and compared that number to the maximum number of days FHA allows for each step. For each annual cohort of properties conveyed in 2010–2017, we calculated the 25th, 50th (median), and 75th percentile time frames for completing the steps. We also calculated the percentage of properties for which servicers or FHA contractors met their time requirements for each step. We reviewed FHA's procedures for monitoring the performance of compliance and maintenance contractors for conveyed properties. We also reviewed examples of contractor quality control plans and FHA quality control reports and scorecards used to assess the contractors' compliance with minimum time frames and other requirements. Additionally, we interviewed FHA officials about the contractors' compliance with their respective time requirements and what steps FHA took, if any, to address any noncompliance.

We assessed the reliability of data from the Single Family Insurance System–Claims Subsystem and the asset disposition system by reviewing FHA documentation about the data systems and data elements. We interviewed FHA staff and contractors knowledgeable about the data to discuss interpretations of data fields and trends we observed in our analysis. We also conducted electronic testing, including checks for outliers, missing data fields, and erroneous values. We excluded from each analysis properties with missing or erroneous information in the applicable data fields. We also excluded from each analysis properties for which the applicable data fields were five absolute deviations from the median (which we consider to be outliers). In addition, we excluded certain properties conveyed in calendar years 2010–2017 that had conveyance dates that were out of sequence. For example, we excluded properties for which the date a servicer obtained possession

and good and marketable title occurred after the date the servicer conveyed the property to FHA. The number of properties we excluded in any analysis using these methods represents no more than 3.2 percent of properties conveyed from July 2010 through December 2017, which we consider to be insignificant when compared to the remaining properties included in the analysis. After taking these steps, we believe that the data were sufficiently reliable for purposes of characterizing the overall length of FHA property conveyances and compliance with key time requirements.

Changes to Conveyance Process and Ongoing Challenges

To determine what changes FHA made to the conveyance process in recent years, we reviewed relevant FHA regulations, policies, and procedures issued in 2010 or later, including FHA's February 2016 mortgagee letter (a written instruction to FHA-approved lenders) on conveyances. We compared the requirements and property preservation and protection allowance amounts in the mortgagee letter to those in the prior mortgagee letter. We also reviewed FHA documentation on changes to the asset disposition system, FHA's data system for conveyed properties, and on FHA's preconveyance inspection pilot program that began in 2017. We interviewed FHA officials on the reasons for the recent changes and on the extent to which they reviewed any analogous requirements and property preservation and protection allowances of other mortgage entities (including Fannie Mae, Freddie Mac, and the Department of Veterans Affairs) when making the updates. To supplement our review of FHA's recent changes to property preservation and protection allowances, we used the asset disposition system data to analyze changes in the frequency and number of servicer overallowable requests since the 2016 mortgagee letter went into effect.

To examine what, if any, challenges exist with the conveyance process, we randomly selected a nongeneralizable sample of 20 large- and medium-sized, bank and nonbank servicers of FHA-insured mortgages. We defined large-sized servicers as those with 100,000 or more active FHA-insured mortgages as of December 31, 2017, and medium-sized servicers as those with 10,000–99,999 active FHA-insured mortgages as of that date. These servicers accounted for more than one-third of active FHA-insured mortgages as of December 31, 2017. We conducted semistructured interviews with the servicers about their experience with FHA property conveyances, including the sufficiency of FHA's policies and procedures, time lines, and allowance amounts and any challenges they experienced with the process. We also discussed the extent to which the 2016 mortgagee letter assisted or hindered their conveyance efforts.

In addition, we spoke with two national industry groups representing mortgage servicers about recent changes and any challenges their members experienced with the conveyance process.

We reviewed FHA's requirements for servicers and contractors on conveyed properties. In cases in which servicers stated that FHA's policies and procedures on particular conveyance requirements was insufficient or unclear, we examined the 2016 mortgagee letter, HUD's single-family housing policy handbook, and frequently asked questions on HUD's website—to determine whether it addressed the topics and was sufficiently thorough to be applied to properties with different circumstances. We assessed whether the policies and procedures were consistent with federal internal control standards for external communication. In particular, we examined whether the policies and procedures communicated necessary quality information to achieve program objectives and whether FHA had evaluated appropriate methods to communicate them.3 Where applicable, we also compared FHA's policies and procedures to features of Fannie Mae's guide for servicers on how to preserve and protect vacant properties. We also assessed FHA's policies and procedures on reconveyances and alternatives to reconveyance against federal internal control standards for designing control activities.

To review the preconveyance inspection pilot that FHA began in 2017 and any challenges with the pilot, we interviewed the three participating servicers about FHA's implementation of the pilot and the extent to which preconveyance inspections reduced the likelihood of reconveyance or addressed other challenges. We spoke with FHA National Servicing Center officials about their monitoring of pilot outcomes and their plans for assessing results. We assessed FHA's planning and evaluation efforts against key components of evaluation design from GAO's guide for designing evaluations.⁴

Furthermore, we interviewed a number of individuals and entities about challenges they experienced in implementing their property conveyance responsibilities, the sufficiency of FHA's policies and procedures, and

³GAO, Standards for Internal Control in the Federal Government, GAO-14-704G (Washington, D.C.: Sept.10, 2014).

⁴GAO, *Designing Evaluations: 2012 Revision*, GAO-12-208G (Washington D.C.: Jan. 31, 2012).

Appendix I: Objectives, Scope, and Methodology

methods for assessing contractor performance. These included FHA headquarters and National Servicing Center officials with responsibilities for aspects of the conveyance process; FHA's compliance contractor; and Real Estate-Owned Division officials, the largest maintenance contractor, and staff responsible for overseeing the maintenance contractors at each of FHA's four homeownership centers.

Finally, we visited eight recently conveyed or reconveyed properties in the Baltimore, Maryland, and Atlanta, Georgia, areas to observe property conditions, learn about the maintenance contractors' property inspection processes, and understand challenges in documenting and addressing condition issues. We chose these locations to provide some geographic dispersion and coverage of different FHA homeownership centers. The properties were selected by Philadelphia and Atlanta homeownership center staff based on our request to visit a mix of recently conveyed and reconveyed properties in metropolitan areas and time periods that we chose. As a result, the conditions we observed are illustrative rather than representative of all conveyed properties.

We conducted this performance audit from September 2017 to June 2019 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Department of Housing and Urban Development



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

OFFICE OF HOUSING

JUN 0 5 2019

Daniel Garcia-Diaz Director, Financial Markets and Community Investment Government Accountability Office 441 G Street NW Washington, DC 20548

Dear Mr. Garcia-Diaz:

Thank you for the opportunity to respond to the Draft Report GAO-19-517 entitled Federal Housing Administration (FHA) – Improved Procedures and Assessment Could Increase Efficiency of Foreclosed Property Conveyance. This letter communicates the Department of Housing and Urban Development (HUD), FHA's response to the draft report.

FHA reviewed the Government Accountability Office's (GAO) draft report and submits the following responses to the three recommendations on page 40:

Recommendation 1:

The Commissioner of FHA should enhance the content and communication of FHA's policies and procedures on conveyance condition considering the program stakeholder views discussed in this report and other stakeholder input.

FHA's Response:

HUD has made significant changes to improve the delivery of clear policy guidance into the market through the publication of HUD Handbook 4000.1 (Handbook) which is the primary source for policy on Single Family program requirements. HUD also updated Mortgagee Letter (ML) 2016-02 on property preservation requirements and expense reimbursements. Both the Handbook and ML 2016-02 are publicly available on HUD's website. The National Servicing Center (NSC) also creates open lines of communication through meetings with FHA servicers to discuss conveyance procedures. The NSC has made clear that as policy changes are considered, FHA will continue to enforce current regulations to ensure compliance and to protect the Mutual Mortgage Insurance (MMI) Fund.

FHA recognizes that policy changes and staff changes both require consistent outreach in terms of external communications, training and in-person meetings in order to ensure that servicers have the information and understanding they need to operate in compliance with our programs. It has been, and will continue to be, a central goal of FHA to meet these needs.

www.hud.gov

espanol.hud.gov

Recommendation 2:

The Commissioner of FHA should provide written direction to the Homeownership Center (HOC) Real Estate Owned (REO) directors on factors to consider when determining whether to reconvey a property with conveyance condition issues, issue a demand letter, or enter into a bypass agreement with the servicer.

FHA's Response:

HUD agrees that written guidance will help Homeownership Centers' REO Directors in applying consistent factors related to reconveyances, which will be determined based on a clearly defined set of criteria. This same guidance will be shared with HUD's Mortgagee Compliance Monitor (MCM) to help: (1) the MCM validate the HOC's decision for re-conveyance; and (2) the MCM to finalize the process of notifying the mortgagee of the reconveyance; and (3) the mortgagee with remedying its non-compliance with HUD's conveyance standards by issuing a Demand Letter or entering into a Bypass Agreement.

It is important to note; however, that over the past five years, HUD has been leveraging less costly upstream disposition strategies (e.g., Third Party Sales, Note Sales, etc.) with higher recovery rates which have resulted in fewer foreclosed properties getting re-conveyed. From FY2019 through June 3, 2019, the Department has only re-conveyed 613 properties out of 34,330 foreclosures processed through Third Party or REO sales' transactions.

Recommendation 3:

The Commissioner of FHA should develop a formal plan for evaluating the outcomes of the preconveyance inspection pilot that includes the key elements of evaluation design—such as evaluation objectives and measures—and utilizes participant feedback and control groups, as appropriate.

FHA's Response:

HUD agrees with the recommendation to formalize a plan to evaluate the existing data and inspection outcomes of its pre-conveyance inspection pilot.

We appreciate GAO's review and discussions regarding recommended improvements of FHA's property conveyance procedures.

Sincerely,

John Garvi

General Deputy Assistant Secretary for Housing

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact	Daniel Garcia-Diaz, (202) 512-8678 or garciadiazd@gao.gov
Staff Acknowledgments	In addition to the contact named above, Steve Westley (Assistant Director); Melissa Kornblau (Analyst in Charge); Rachel Batkins; William Chatlos; Emily Flores; John McGrail; Samuel Portnow; Barbara Roesmann; Tovah Rom; and Jena Sinkfield made key contributions to this report.

GAO's Mission	The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.
Obtaining Copies of GAO Reports and Testimony	The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (https://www.gao.gov). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to https://www.gao.gov and select "E-mail Updates."
Order by Phone	The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, https://www.gao.gov/ordering.htm.
	Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.
	Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.
Connect with GAO	Connect with GAO on Facebook, Flickr, Twitter, and YouTube. Subscribe to our RSS Feeds or E-mail Updates. Listen to our Podcasts. Visit GAO on the web at https://www.gao.gov.
To Report Fraud,	Contact FraudNet:
Waste, and Abuse in	Website: https://www.gao.gov/fraudnet/fraudnet.htm
Federal Programs	Automated answering system: (800) 424-5454 or (202) 512-7700
Congressional Relations	Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548
Public Affairs	Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800 U.S. Government Accountability Office, 441 G Street NW, Room 7149 Washington, DC 20548
Strategic Planning and External Liaison	James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707 U.S. Government Accountability Office, 441 G Street NW, Room 7814, Washington, DC 20548

