OFFICE of INSPECTOR GENERAL
UNITED STATES DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

loanDepot.com Did Not Have a Sufficient Quality Control Program for FHA-Insured Loans

Audit Report Number: 2025-NY-1002

March 04, 2025

Office of Audit | Office of Inspector General
U.S. Department of Housing and Urban Development

To: Julie A. Shaffer
Associate Deputy Assistant Secretary for Single Family Housing, HU

From: Kilah S. White
Assistant Inspector General for Audit, Office of Inspector General, GA

Subject: loanDepot.com Did Not Have a Sufficient Quality Control Program for FHA-Insured Loans, Irvine, CA

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our audit of loanDepot.com's quality control program for originating and underwriting Federal Housing Administration (FHA)-insured loans.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, as amended, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at https://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call Kimberly S. Dahl, Audit Director, at (202) 617-6886.

Highlights

loanDepot.com Did Not Have a Sufficient Quality Control Program for FHA-Insured Loans | 2025-NY-1002

What We Audited and Why

We audited loanDepot.com to evaluate its quality control (QC) program for originating and underwriting Single Family FHA-insured loans. We selected loanDepot for review based on its loan volume and delinquency rate and because its rate of self-reporting loans to HUD when it identified fraud, material misrepresentations, and other material findings that it could not mitigate was below average for more than a 5-year period.

What We Found

loanDepot's QC program for originating and underwriting FHA-insured loans was not sufficient. Specifically, loanDepot (1) did not select the proper number of loans for review and maintain complete and accurate data to document its loan selection process; (2) missed material deficiencies; and (3) did not adequately assess, mitigate, and report loan review findings, which included self-reporting loans to HUD when required. These issues occurred because loanDepot had insufficient controls over its QC program. As a result, HUD did not have assurance that loanDepot's QC program fully achieved its intended purposes, which include, among other things, protecting the FHA insurance fund and lender from unacceptable risk, guarding against fraud, and ensuring timely and appropriate corrective action.

What We Recommend

We recommend that HUD require loanDepot to (1) update its QC plan and related procedures to align with HUD requirements; (2) provide training to its staff and management on HUD requirements for lender QC programs; (3) review the loans that it had not selected and take appropriate actions when applicable; and (4) evaluate its QC files for the loans in which it identified material findings to confirm whether it self-reported to HUD all findings of fraud or material misrepresentation, along with any other material findings that it did not acceptably mitigate.

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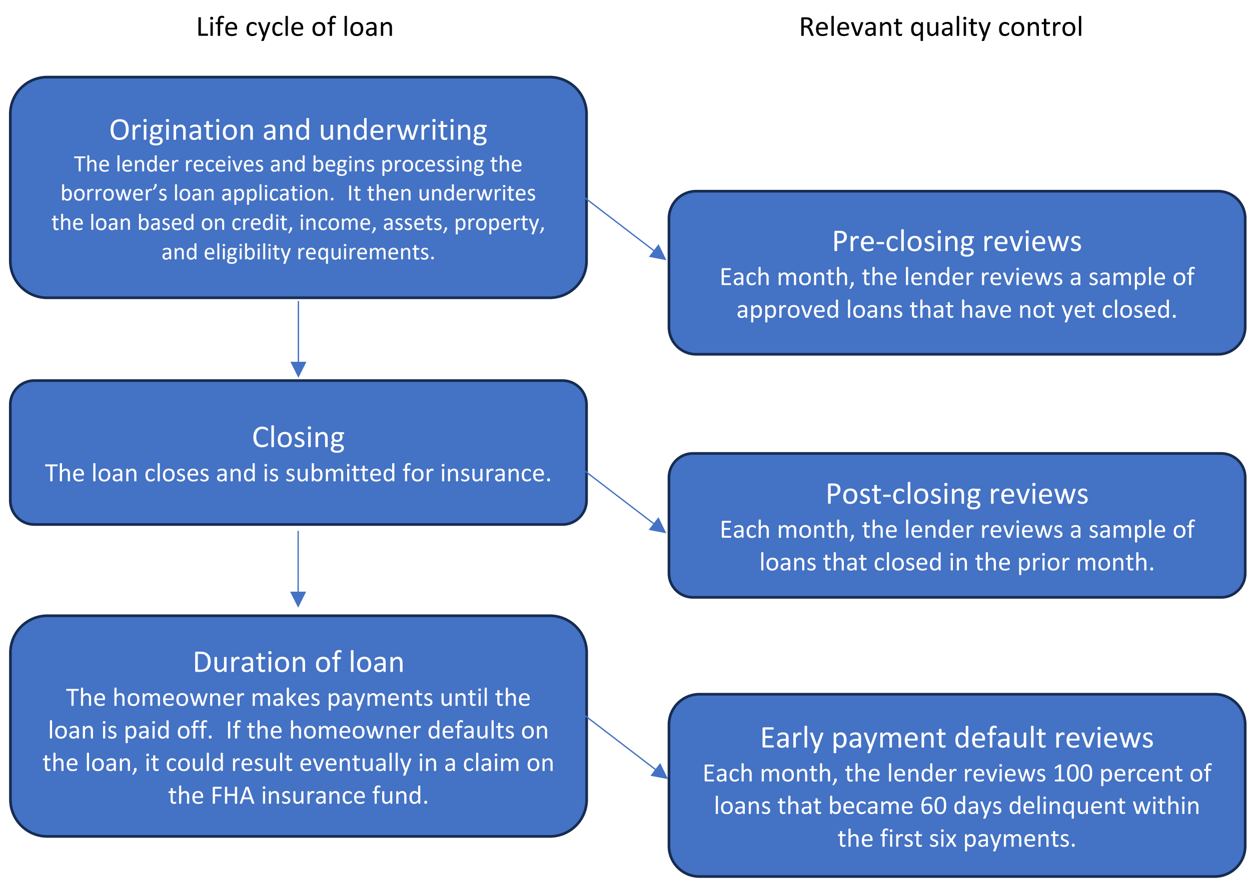
Background and Objective

FHA, a part of HUD, provides mortgage insurance on single family loans made by FHA-approved lenders throughout the United States and its territories. This insurance protects lenders against losses as a result of homeowners' defaulting on their mortgage loans. The lenders bear less risk because HUD will pay a claim to the lender in the event of a homeowner's default.

HUD monitors a number of lenders each year and performs random and targeted reviews of loans throughout the year. Further, HUD requires each lender to implement a quality control (QC) program to (1) ensure compliance with policy and guidelines; (2) protect FHA and the lender from unacceptable risk; (3) guard against errors, omissions, negligence, and fraud; (4) determine the root cause of any deficiencies and identify potential internal and external control weaknesses; (5) alert lender management to patterns of deficiencies; (6) ensure timely and appropriate corrective action; (7) ensure the existence of required documentation that is the basis of underwriting decisions; (8) ensure that loans are secured by properties with values sufficient to support the loan; and (9) ensure compliance with fair lending laws.

Lender QC programs must cover the life cycle of an FHA-insured loan for any functions that the lender performs. As shown below, lenders who originate and underwrite loans must review samples of loans before closing, after closing, and if they default early in the life of the loan.



To help ensure that lender QC programs meet their intended purposes, Section V of HUD's FHA Single Family Policy Handbook requires lenders to have written QC plans setting forth the procedures they will use. It also sets parameters for how many loans lenders must review each month and requires them to document the results of each loan review performed, including any corrective actions taken. Lenders must review all loan files selected for compliance with the handbook's requirements related to debts, employment, income, sources of funds, the property, how documents were handled, underwriting accuracy and completeness, etc. Further, they must do additional analysis when conducting post-closing and early payment default (EPD) reviews by obtaining new credit reports, reverifications of borrower information, and appraisal field reviews if relevant based on the type of loan.

As shown below, lenders must also meet key requirements when their reviews identify findings.

Requirement	Description
Loan sample risk assessment	Loans must be evaluated based on the severity of the violations found using prescribed risk categories, and lenders must use this information to conduct trend analyses over time.
Reporting to lender management	Initial findings and final reports must be shared with senior lender management. The lender must respond to each instance of fraud, material misrepresentation, or other material finding.
Reporting to HUD	Lender management must self-report to HUD all findings of fraud or material misrepresentation, along with any other material findings that it is unable to mitigate.

loanDepot.com is a nonsupervised lender based in Irvine, CA.[1] It is a nonbank entity and has been approved to conduct business with FHA since 2009. Over the past 5 years, loanDepot has originated or underwritten approximately 125,000 FHA-insured loans. It conducts pre-closing and EPD reviews in-house. Post-closing reviews are conducted by a QC contractor.

Our objective was to evaluate loanDepot's QC program for originating and underwriting FHA-insured loans.

[1] Nonsupervised lenders are lending institutions that have as their principal activity the lending or investing of funds in real estate mortgages, consumer installment notes, similar advances of credit, or the purchase of consumer installment contracts. In contrast, supervised lenders are banks, savings banks, or credit unions that are members of the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), or the National Credit Union Administration (NCUA). Nonsupervised lenders do not fall under the supervision of the FDIC, OCC, or NCUA.

Results of Audit

loanDepot's Quality Control Program Did Not Fully Achieve Its Purpose

loanDepot's QC program for originating and underwriting Single Family FHA-insured loans was not sufficient. Specifically, loanDepot (1) did not select the proper number of loans for review and maintain complete and accurate data to document its loan selection process; (2) missed material deficiencies; and (3) did not adequately assess, mitigate, and report loan review findings, which included self-reporting loans to HUD when required. These issues occurred because loanDepot had insufficient controls over its QC program. As a result, HUD did not have assurance that loanDepot's QC program sufficiently protected the FHA insurance fund and lender from unacceptable risk, guarded against fraud, and facilitated timely and appropriate corrective action.

loanDepot's Loan Selection Process Was Insufficient

While loanDepot selected a sufficient number of loans for pre-closing reviews, it did not always select the proper number of loans for post-closing and early payment default (EPD) reviews. Further, it did not maintain complete and accurate data to document its loan selection process.

Post-Closing Review Sampling Was Insufficient

HUD requires lenders who originate or underwrite more than 3,500 FHA-insured loans per year, such as loanDepot, to select either 10 percent of those loans for pre-closing and post-closing reviews or to determine their sample size using a statistical stratified random sample that would ensure a 95 percent confidence level with a confidence interval not to exceed 2 percent on an annual basis, based on defect rates for FHA loans recently reviewed.[2] Further, HUD requires that lenders perform post-closing reviews on at least 90 percent of the sample size.[3] This is important because post-closing reviews are more thorough. While loanDepot chose to determine its sample size using a statistical sampling method, it did not select a sufficient number of loans for post-closing reviews.

Based on information provided by loanDepot, we estimate that it should have performed at least 3,566 post-closing reviews on loans thatit originated or underwrote over the 2-year period covering October 2020 through September 2022.[4] However, it performed only 2,376 post-closing reviews, which means that it failed to conduct approximately 1,190 post-closing reviews. This condition occurred because loanDepot used a flat 5 percent defect rate stated in its QC plan rather than defect rates on loans recently reviewed as HUD required, such as the percentage of loans in which it identified material findings.[5] In addition, its plan did not require it to stratify loans based on mortgage product type and how the loans were originated, and loanDepot could not provide detailed information that would allow us to recreate its

[2] HUD Handbook 4000.1, section V.A.3.a.iii.(B)

[3] HUD Handbook 4000.1, section V.A.3.a.iii.(C)

[4] We estimated the minimum sample size using loanDepot's loan volume for the 2-year period, the percent of material findings that it identified in post-closing reviews of FHA loans, and the same 95 percent confidence level and 2 percent confidence interval used by loanDepot.

[5] loanDepot uses low, moderate, high, and critical risk assessment categories. Based on a comparison of HUD's definition for material findings and loanDepot's definitions for its high and critical risk categories, we considered loans that loanDepot classified as high or critical risk to have material findings.

sample sizes. As a result of the issues noted above, loanDepot did not develop relevant and timely insights on at least 1,190 loans with estimated original mortgage amounts totaling approximately $329 million that could have been used to mitigate risks and strengthen its operations over time.[6]

Some EPD Loans Were Not Reviewed As Required

HUD requires lenders to review 100 percent of early payment default (EPD) loans when they become 60 days delinquent within the first six payments.[7] These reviews are important because they can provide valuable insight into what caused the borrowers to default on their loans and identify underwriting weaknesses. From October 2020 through September 2022, loanDepot reviewed 2,395 of the 2,432 loans in which borrowers went into early payment default.[8] loanDepot did not perform approximately 1.5 percent of the required EPD reviews primarily because its staff excluded loans either due to selection errors or because it was not properly notified through the Neighborhood Watch system when the defaults happened.[9] We acknowledge that default information may not always be correctly reported by the servicing lenders in a timely manner. However, loanDepot should have known that most of these loans were EPDs because it held or serviced the loans at the time. As a result, loanDepot was unable to develop relevant and timely insights on 37 loans with original mortgage amounts totaling more than $10.6 million that could have been used to mitigate risks and strengthen its operations over time.

Selection Data Accuracy Could Be Improved

loanDepot did not maintain complete and accurate data to document its pre-closing, post-closing and EPD loan selection process as required by HUD.[10] For example, the sample universe data for pre-closing reviews it provided accidentally excluded 237 loans, and the sample universe data for post-closing reviews excluded 206 loans. Further, loanDepot did not realize that 536 FHA loans financed with bonds were excluded from its sample data for post-closing or EPD reviews, until we noted the discrepancy between the data and the QC reports.[11] In addition, the sample universe data of pre-closing loans it initially provided did not reconcile with the list of sampled loans provided, omitting 157 sampled loans. Finally, the sample universe and sampled loans data provided did not always contain accurate FHA case numbers and were not always provided in a proper format.

This condition occurred because loanDepot did not have an adequate process for documenting and maintaining data on its monthly sample selection. loanDepot employed a manual process for documenting loans subject to QC reviews and compiling the requested information for this audit, and human errors occurred during the process. In addition, loanDepot's policy required the final approval

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[6] We estimated the original mortgage amount of the 1,190 loans based on the average original mortgage amount for FHA-insured loans that were originated or underwritten by loanDepot and closed during our audit period.

[7] HUD Handbook 4000.1, section V.A.3.a.iv.(B)

[8] loanDepot reviewed an additional 43 loans that did not meet HUD's definition for EPD. While lenders may choose to conduct reviews on additional loans that do not meet HUD's definition, these would not satisfy its responsibility to review all EPD loans.

[9] While lenders may use HUD's system to help identify EPD loans, they remain responsible for obtaining sufficient data to identify EPD loans, which could require them to coordinate with other lenders that service loans that they hold. loanDepot also has used data from servicing lenders, which we encourage it to continue doing.

[10] HUD Handbook 4000.1, section V.A.3.a.v

[11] loanDepot did not distinguish FHA bond loans and non-FHA bond loans in its QC reports.

date, a critical data field for QC sample selection, to be changed if a correction was made during a post-closing QC review; consequently, the data incorrectly showed that some loans were closed or funded and associated post-closing QC reviews were conducted before they were approved by the underwriter. Further, loanDepot had a policy in which loans that were not yet endorsed at the time of post-closing sample selection would not be included in the sample universe, which would have prevented late endorsement loans from being considered for review. As a result, it was initially difficult to reconcile loanDepot's data and ensure that it had adequate coverage. While we were able to confirm the information through communication with the lender, the absence of quality data could compromise the integrity of loanDepot's QC program by making it difficult to confirm compliance and adequate coverage.

loanDepot's Loan Reviews Were Inadequate

While loanDepot generally completed its loan-level reviews within established timeframes for the 2-year period covering October 2020 through September 2022, the reviews were not always of sufficient quality. Lenders must review selected loans for compliance with requirements, such as those related to debts, employment, income, sources of funds, the property, how documents were handled, and underwriting accuracy and completeness. Further, for post-closing and EPD reviews, HUD requires lenders to conduct a deeper analysis using new credit reports, reverifications of borrower information, and appraisal field reviews when relevant based on the loan type. loanDepot's loan reviews sometimes failed to identify material deficiencies that would have affected loan approval and insurance eligibility.

Material Deficiencies Were Missed

loanDepot did not always detect origination and underwriting deficiencies that would have affected loan approval and insurance eligibility during its QC reviews. A comparison of loanDepot's QC data with data from HUD's quality assurance reviews found 33 loans in which HUD identified material deficiencies that resulted in indemnification agreements, but loanDepot's reviews had failed to detect the deficiencies.[12] These issues occurred because loanDepot did not adequately review some files for compliance with requirements. As a result, HUD did not have assurance that loanDepot's loan reviews sufficiently supported compliance with underwriting requirements and protected the FHA insurance fund and lender from unacceptable risk.

loanDepot's Assessment, Mitigation, and Reporting of Review Findings Were Inadequate

While loanDepot established a risk assessment methodology for its QC reviews and generally reported loan-level findings to internal management as required for the 2-year period covering October 2020 through September 2022, it did not adequately assess the risk of findings identified and mitigate or report them to HUD when necessary. In addition, it lacked evidence showing that loanDepot's senior management responded to findings as required by HUD.

[12] Indemnification agreements protect HUD against loss associated with a loan should it result in a claim against the FHA insurance fund. We identified 538 loans that had both a QC review by loanDepot and a HUD quality assurance review. HUD identified material deficiencies that resulted in indemnification agreements for 68 of the 538 loans. However, as noted above, for 33 of these loans, loanDepot did not detect these material deficiencies during its QC reviews. For the remaining 35 loans, loanDepot detected the deficiencies but had failed to adequately mitigate or self-report them to HUD.

Assessment of Risk Was Inadequate

HUD requires lenders to establish a risk assessment methodology to evaluate violations found during QC reviews. At a minimum, lenders must include low, moderate, and material risk categories in their risk assessment methodology.[13] loanDepot uses low, moderate, high, and critical risk assessment categories. While it's QC plan includes definitions for each of the risk levels used, loanDepot did not always adequately assess the risk of findings identified in the 20 loans we sampled. For example, while its QC plan says that high-level findings are those that result in a significant eligibility violation that must be addressed, mitigated, or cured, it sometimes classified findings as high-level that were not significant eligibility violations, such as a phone number provided by the borrower on a clearance form not matching the phone number shown on the credit report. Additionally, while loanDepot explained that findings resulting in debt-to-income ratio increases between 2 to 2.99 percent represent a moderate risk, it classified a finding related to a 2 percent increase as high. In contrast, it classified an income finding that would have resulted in an increase of more than 3 percent as moderate when it should have been classified as a higher-level finding. These issues occurred because loanDepot did not consistently follow HUD requirements and its risk assessment methodology when reviewing loans. As a result, HUD did not have assurance that loanDepot's loan reviews protected the FHA insurance fund and lender from unacceptable risk.

Lender Officials Did Not Respond to Findings

HUD requires all QC review findings to be reported to lender senior management, including sharing initial findings with senior management within 30 days of the initial finding report, followed by providing final findings reports within 60 days. Further, senior management must review and respond to each instance of fraud, material misrepresentation, or other material finding. While loanDepot documented that it provided initial findings and final findings reports to senior management, it did not provide sufficient data or reports showing that senior management had responded to findings when required.

Material Findings Were Not Adequately Mitigated or Reported to HUD

HUD requires lenders to self-report to HUD all findings of fraud or material misrepresentation, along with any other material findings that it is unable to mitigate.[14] As discussed above, findings are considered material if disclosure of them would have altered the lender's decision to approve the loan or seek FHA endorsement for it.[15] Material findings are considered mitigated only if the deficiencies have been remedied so that the loan approval and insurance endorsement decisions are considered acceptable.[16] Further, HUD requires lenders to retain all QC results and documentation, including actions taken to mitigate findings.[17] loanDepot did not adequately mitigate findings or report them to HUD when necessary.

While loanDepot identified material findings during its QC reviews for 18 of the 20 loans we sampled, it only complied with HUD's requirement to mitigate or self-report the findings for 4 of these 18 loans, or 22 percent. For each of the four loans, they complied with the requirement by documenting mitigation

[13] HUD Handbook 4000.1, section V.A.2.d.i.(B) and V.A.3.b.iii
[14] HUD Handbook 4000.1, section V.A.2.d.iv
[15] HUD Handbook 4000.1, section V.A.2.d.i.(B)
[16] HUD Handbook 4000.1, section V.A.2.d.i.(C)
[17] HUD Handbook 4000.1, section V.A.2.d.v

of the material findings. For the remaining 14 of 18 sampled loans with material findings, loanDepot's records did not show that it acceptably mitigated the findings or self-reported the loans to HUD. For example, for one of the loans, loanDepot's QC review discovered that the borrower materially did not meet the cash requirement to close the loan. The QC review verified a portion of the assets needed to close, but the borrower remained about $6,000 short of that amount. loanDepot incorrectly only considered loans with critical risk findings, the highest severity level in its risk assessment methodology, for potential self-reporting instead of all loans with material findings as required by HUD.

In addition, we identified 35 loans in which HUD and loanDepot had separately reviewed the files and identified material deficiencies, and HUD's review had resulted in indemnification agreements. loanDepot did not evaluate 30 of the 35 loans, which had high risk findings for potential self-reporting. Further, loanDepot determined that the remaining 5 loans that had critical risk findings were not required to be self-reported, although it did not provide documentation showing mitigation. For example, loanDepot did not properly justify that the finding of borrower's undisclosed liabilities was not self-reportable.

In total, we identified 49 loans in which loanDepot failed to mitigate or self-report findings identified during its QC reviews. These issues occurred because loanDepot did not adequately implement HUD requirements for mitigation and self-reporting. As a result, HUD did not have assurance that loanDepot's QC program guarded against fraud, ensured appropriate corrective action, and protected the FHA insurance fund and lender from unacceptable risk, including for the fourteen loans with original mortgage balances totaling more than $3.5 million that were not self-reported and had not yet been indemnified. In addition, we identified 1,735 other loans with original mortgage amounts totaling more than $497 million that were reviewed by loanDepot and contained material findings that may not have been adequately mitigated or required self-reporting to HUD.

Conclusion

loanDepot's QC program did not fully achieve its intended purposes, which include, among other things, protecting HUD and itself from unacceptable risk, guarding against fraud, and facilitating timely and appropriate corrective action. These issues occurred because loanDepot had insufficient controls over its QC program, including that its QC plan and policies did not always cover HUD requirements. If loanDepot updates its QC plan and related procedures, and provides training to its staff and management, it will help ensure that its QC program complies with requirements and better achieves its intended purposes going forward.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing require loanDepot to

1A. Update its QC plan and related processes and procedures to align with requirements for loan selection, including maintaining data and documentation showing how sample sizes and loan selections were determined.

1B. Update its QC plan and related processes and procedures to align with requirements for (1) loan file reviews, (2) assessment of findings, (3) mitigation of findings, and (4) reporting findings to HUD when required.

1C. Provide annual training to its staff and management on HUD requirements for lender QC programs and provide proof of training to HUD.

1D. Conduct up to 1,190 additional post-closing QC reviews to meet sample size and composition requirements and submit the results to HUD, including all findings of fraud or material misrepresentation, along with any other material findings that it is unable to mitigate. If required, loanDepot should execute indemnification agreements or reimburse claims paid to help protect the FHA insurance fund from unacceptable risk.

1E. Review the 32 EPD loans not previously selected for review and submit the results to HUD, including all findings of fraud or material misrepresentation, along with any other material findings that it is unable to mitigate.[18] If required, loanDepot should execute indemnification agreements or reimburse claims paid to help protect the FHA insurance fund from unacceptable risk.

1F. Evaluate its QC files for the 1,579 loans in which it identified material findings to confirm whether it self-reported to HUD all findings of fraud or material misrepresentation, along with any other material findings that its records did not show have been acceptably mitigated.[19] If required, loanDepot should execute indemnification agreements or reimburse claims paid to help protect the FHA insurance fund from unacceptable risk.

1G. Provide indemnification agreements or documentation to support the 14 loans in which it identified material findings that it did not acceptably mitigate or self-report to HUD. Implementation of this recommendation will protect the FHA insurance fund from an estimated loss of $1,136,089.[20]

[18] While we identified 37 EPD loans that loanDepot did not review during our audit period as required, we reduced this figure to 32 to account for those loans that were terminated without a claim, such as when a loan is paid in full.

[19] While we identified 1,735 loans in which loanDepot had identified material findings and might need to self-report them, we reduced this figure to 1,579 to account for those loans that were terminated without a claim, such as when a loan is paid in full.

[20] This amount was based on the most recent unpaid balances of the loans, which totaled more than $3,341,441 , and FHA's average loss experience of about 34 percent.

Scope and Methodology

We performed our audit work between February 2023 and April 2024. We did not conduct onsite fieldwork for this audit. Our audit covered the period October 2020 through September 2022 and was expanded to include loan statuses as of November 2024.

To accomplish our objective, we

- reviewed relevant requirements, including handbooks, and mortgagee letters;
- reviewed the lender's QC plan and related policies, procedures, and other relevant documentation to obtain sufficient background information on the program and lender;
- reviewed monthly QC summary reports from the lender covering the 2-year audit period;
- reviewed the lender's QC data for pre-closing, post-closing, and EPD reviews;
- compared the lender's QC data and data from HUD's Single Family Data Warehouse (SFDW) to determine whether the lender reviewed the correct quantity of loans; whether the reviews were performed in a timely manner; and whether the lender obtained new credit reports, reverifications, and appraisal field reviews for the correct quantity of loans each month;
- compared the lender's QC data and data from HUD's Loan Review System (LRS) to identify loans in which the lender could have missed material deficiencies during its QC reviews, failed to properly categorize or correct deficiencies identified, or failed to self-report the loans to HUD;
- reviewed loan data from Neighborhood Watch;
- interviewed key lender officials to obtain an understanding of its operations, data, and documentation and to discuss potential issues identified during the audit.

For the period October 2020 through September 2022, loanDepot performed QC reviews on 6,100 loans. We selected a targeted sample of 20 loans based on various factors, such as whether the loans were currently or previously in default, especially those 3 months or more delinquent or in foreclosure; the default reason listed in HUD's SFDW system; when the loans closed; and the highest lender finding level. For each of the 20 loans, we reviewed the lender's QC and loan files to determine whether loanDepot looked at all required QC elements, missed any significant deficiencies, reasonably categorized deficiencies identified, mitigated deficiencies, took appropriate corrective action, self-reported loans to HUD if required, and completed its review and followup in a timely manner. When considering whether deficiencies identified or missed by loanDepot would have affected loan approval and insurance eligibility, we considered information in FHA's Defect Taxonomy. Our results were limited to the loans in our sample and cannot be projected to the universe.

Of the 6,100 loans that loanDepot originated or underwrote and for which it conducted QC reviews, HUD had reviewed 538 loans as of May 2023. We identified 68 loans in which HUD found indemnifiable deficiencies despite the lender's not having self-reported the loans. We performed limited scope reviews of the 68 loans to confirm whether the lender found the deficiencies identified by HUD, how it categorized and corrected the findings, and whether it self-reported the loans to HUD.

We relied on computer-processed data provided by loanDepot as well as data contained in HUD's Neighborhood Watch system, SFDW, and LRS. We assessed the reliability of the computer-processed data and determined that the data were sufficiently reliable to achieve our audit objective. We also assessed the relevant internal controls to the extent necessary to determine whether they were logical, reasonably complete, and likely to deter or detect potential problems or indicators.

We conducted the audit 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 objective(s). We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Appendixes

Appendix A – Schedule of Funds To Be Put to Better Use

Recommendation number	Funds to be put to better use 1/
1G	$1,136,089

1/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. In this case, if HUD implements our recommendation, it could avoid potential losses for 14 loans in which loanDepot identified material findings that it did not acceptably mitigate or self-report to HUD. The amount above reflects that upon paying a claim on defaulted loans, FHA's average loss experience is about 34 percent based on statistics provided by HUD.

Appendix B – Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation – Auditee Comments

loanDepot
NMLS#174457

Delivery via Electronic Mail

February 18, 2025

Kilah S. White
Assistant Inspector General for Audit
Office of Inspector General
451 7th Street, SW
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Re: loanDepot's Response to HUD OIG's Draft Audit Report of the Company's Quality Control Program for FHA-Insured Loans from October 1, 2020 to September 30, 2022

Dear Ms.White,

Comment 1 >

loanDepot, Inc. ("loanDepot" or the "Company") submits this response to the draft audit report ("Draft Report") prepared by the U.S. Department of Housing and Urban Development ("HUD") Office of Inspector General ("OIG") related to the Company's Quality Control ("QC") Program for FHA-insured loans. loanDepot values its long standing relationship with HUD and appreciates this opportunity to respond to the Draft Report. However, loanDepot respectfully disagrees that the facts support OIG's characterization of loanDepot's QC program. The Draft Report focuses on one-off human errors, a misunderstanding of the Company's risk rating methodology, and prior indemnifications, none of which support the OIG's claim that the Company's QC program fails to achieve its purpose. In addition, the title page does not reflect that the audit findings are specific to the audit period referenced above. loanDepot respectfully requests that the audit period be included in the title of the report as the absence of the audit period could lead to misinterpretation of loanDepot's current quality control program. To the contrary, loanDepot's QC program operated to protect FHA and loanDepot from unacceptable risk by ensuring the Company reviewed loans to identify, mitigate, and where necessary, report Material Defects to HUD.

loanDepot continually invests significant resources into its QC program and, although it disagrees with HUD's sweeping assertions in the Draft Report, loanDepot has already undertaken efforts to enhance its QC Program in the more than two years since OIG began its review. As detailed below, the Company is also taking steps to address the Draft Report's recommendations.

I. <u>**The Draft Report bases its claims regarding loanDepot's loan selection process on a misunderstanding of the Company's loan selection criteria and overstates immaterial and inadvertent errors that did not increase risk to FHA or loanDepot.**</u>

loanDepot conducted post-closing reviews of a larger sample of loans than required by FHA, and the isolated and inadvertent errors described in the Draft Report are not representative of loanDepot's QC program as a whole and did not result in an unacceptable risk to the FHA insurance fund or to loanDepot. Nevertheless, the Company has already conducted additional loan-level reviews and is in the process of enhancing its QC plan as described in more detail below.

a. ***loanDepot performed post-closing reviews on a larger sample of loans than required by the FHA Single Family Handbook.***

Comment 2 >

Contrary to the allegation in the Draft Report, loanDepot *over-sampled* loans to be reviewed in post-closing QC. The OIG misunderstands loanDepot's QC risk rating methodology, and as a result, overstated the Company's historical defect rate when it estimated the appropriate sample size for post-closing review. The

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loanDepot
NMLS#174457

Comment 2 >

OIG, therefore, incorrectly concluded that loanDepot under-sampled when selecting loans for post-closing QC reviews, when in fact the Company sampled and reviewed more loans than required.

FHA requires Mortgagees to monitor loans for potential fraud, material misrepresentations, and other Material Findings.[1] A lender of loanDepot's size may either use a flat 10% QC rate for post-closing reviews, or base the sample size in part "on the defect rates for FHA-insured Mortgages recently reviewed by the Mortgagee."[2] Although the Handbook does not define "defect rates" in this context, the OIG indicated in the Draft Report that it calculated the defect rate using the percentage of "material findings"[3] identified in loanDepot's post-closing reviews of FHA loans. This statement, however, is not accurate.

loanDepot categorizes loans using a four-tiered risk rating methodology and assigns loans with material defects a "Critical" rating. The remaining three categories are assigned to loans with varying levels of defects, none of which constitute Material Findings as defined by the FHA Single Family Handbook (the "Handbook"). loanDepot uses this four-tiered approach to separately identify and track potentially serious defects that do not otherwise require self-reporting. For example, the Company may assign a High rating to an income calculation error that results in an increase in the borrower's debit-to-income ("DTI") ratio, but which does not result in an unacceptably high DTI. Separately categorizing these types of defects allows loanDepot to identify non-Material findings that are nonetheless important to address.

Consistent with its risk rating methodology, loanDepot properly excluded High-rated loans and considered only Critical-rated loans to be Material for purposes of the Company's material defect rate. By contrast, the OIG used the number of Critical *and* High-rated loans to calculate a material defect rate that overstated loanDepot's actual defect rate by more than 20%. The OIG therefore incorrectly concluded that loanDepot should have reviewed a total of 3566 loans and consequently failed to conduct approximately 1,190 post-closing reviews. When the defect rate is corrected to properly include only loans with Critical findings, the defect rate was 7.99%, which required loanDepot to review 1,241 loans. As the OIG noted in the Draft Report, loanDepot performed 2,376 post-closing reviews, or 1,135 more than required.

To further support its claim, the OIG pointed to loanDepot's use of a "flat 5 percent defect rate" in calculating sample sizes and incorrectly stated that the Company's QC Plan did not require it to stratify loans based on product type and source of origination. loanDepot acknowledges that it used a flat 5% defect rate during the audit period and that its QC Plan lacked certain details regarding how to stratify specific categories of loans; however, it disagrees that either of these practices increased the risk to FHA or to loanDepot. Using the same calculations with a flat 5% defect rate, the minimum sample size over two years is 808 loans. Had loanDepot only reviewed 808 loans, the OIG's assertion that the Company under sampled would be valid. However, this was not the case as loanDepot increased the sample size by 1,568 loans. In total, loanDepot reviewed 2,376 FHA-insured loans over a two-year period. This oversampling allowed for a more representative understanding of the overall risk within the FHA-insured population of loans and complied with HUD's minimum sample size requirements. Finally, loanDepot's QC Plan specifically states that QC reviews must include mortgage loans originated using all underwriting methods, as well as mortgage loans from all product lines, from all states of origination, and from each branch office. Therefore, as the OIG acknowledged, the Company's QC Program provided sufficient coverage, even if its QC Plan lacked certain details regarding its methods to stratify its loan samples.

Nevertheless, loanDepot is updating its QC Plan to require consideration of the specific defect rate for recently reviewed FHA-insured loans when determining its QC review sample sizes. The Company is also adding language to its QC Plan to include additional detail describing how to stratify loans based on mortgage product type and how loans were originated.

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[1] HUD Handbook 4000.1, Section V.A.2.d.ii.

[2] 4000.1, Section V.A.3.a.iii.(B).

[3] Material findings are those that, had they been identified earlier, would have altered the loanDepot's decision to approve the loan or seek FHA endorsement. 4000.1, Section V.A.2.d.i.(B).

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b. *loanDepot's QC Plan requires review of 100% of Early Payment Default ("EPD") loans and its inadvertent exclusion of a small number of EPD loans from QC review is not indicative of a larger issue.*

Comment 3 >

Consistent with the Handbook, loanDepot's QC Plan requires review of all FHA-insured EPD[4] loans.[5] loanDepot generally identifies these loans using FHA's Neighborhood Watch platform, which generates reports based on data supplied by mortgage servicers responsible for directly servicing the loans. The Draft Report claims that loanDepot failed to review 37 EPD loans during the audit period. As a result of human error in pulling and filtering an FHA Neighborhood Watch Report, loanDepot inadvertently did not identify 6 EPD loans for review. Additionally, 31 loans subserviced on loanDepot's behalf were not included in the report pulled from FHA Neighborhood Watch and therefore were not selected for QC review. While loanDepot has a policy of leveraging FHA Neighborhood Watch data in its EPD reviews, the Company is implementing an additional procedure to leverage internal servicing reports to confirm that data pulled from FHA Neighborhood Watch is complete and that all EPD loans are selected for review.

Comment 4 >

Despite the small and inadvertent exclusion, and contrary to the Draft Report's allegations, loanDepot reviewed 98.5% of EPD loans during the audit period. Additionally, loanDepot reviewed 29 of the 37 EPDs originally excluded from its QC reviews. As of January 1, 2025, 8 loans had been paid in full with no loss claims filed against the FHA insurance fund.[6] Of the remaining 29 loans, loanDepot did not identify *any* findings for six of the loans reviewed and identified only non-Material findings for the remaining 23. Additionally, a majority of these loans appear to have defaulted due to events occurring after origination, including national emergencies such as hurricanes, illness, and unexpected loss of income. This validates loanDepot's decision to originate and submit these loans for endorsement was sound and that its inadvertent failure to review these loans did not increase the risk to the FHA fund.

Comment 5 >

c. *loanDepot's QC selection data criteria was accurate.*

The Draft Report's claim that "selection data accuracy could be improved" mischaracterizes the substance of the OIG's finding and conflates three issues: (1) the accuracy of loanDepot's loan selection process, (2) loanDepot's recordkeeping around loan selection, and (3) the accuracy of the data initially provided to the OIG during the audit. As to the first issue, and as described in this letter, loanDepot's loan selection process was overwhelmingly accurate. The issues described in this section of the Draft Report relate not to the accuracy of loanDepot's selection of loans for QC review, but to the accuracy of the data loanDepot provided to OIG during the initial stages of the exam (the third issue). As to the second issue, the Company has implemented improved recordkeeping practices specific to the selection process so that any future reviewers can more quickly confirm this information (as the OIG acknowledges it was ultimately able to do).

The third issue pertains to limited, initial mistakes in the information loanDepot provided to the OIG—such as the inadvertent omission of certain bond loans from sample data. While loanDepot takes these mistakes seriously, concerns that "the absence of quality data could compromise the integrity of loanDepot's QC program" are overstated. Indeed, loanDepot's QC department did not compile the data the Company submitted to OIG. Instead, personnel responsible for responding to regulatory requests mistakenly pulled incomplete reports for the audit. As the Draft Report states, the Company ultimately provided the full list of sampled loans showing, for example, that loans financed with bonds were in fact included in the Company's QC reviews. In the more than two years since the OIG started its review, the Company has reorganized certain functions, and now compiles these types of reports in direct consultation with QC personnel to ensure the Company produces data that accurately and completely reflects the Company's selection criteria and processes for the same.

[4] "Early Payment Defaults (EPD) are all Mortgages that become 60 Days delinquent within the first six payments." 4000.1, Section V.A.3.a.iv.(B)(1).

[5] "The Mortgagee must review all EPDs underwritten by the Mortgagee, regardless of which Mortgagee services the Mortgage." 4000.1, Section V.A.3.a.iv.(B)(2).

[6] Consistent with the OIG's guidance to exclude paid-in-full loans with no insurance claims from the Company's review, loanDepot did not review these 8 loans.

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Comment 6 >

II. <u>loanDepot identified and reported Material Findings to HUD.</u>

loanDepot acknowledges that it indemnified HUD in connection with 33 loans reviewed by the OIG; however, loanDepot disagrees that all loans contained Material Findings that required self-reporting to HUD. In connection with this audit, the Company conducted a further review of the loan files and determined that 11 loans did not contain Material Findings warranting indemnification. For various business reasons, the Company may agree to HUD's request for indemnification in connection with HUD deficiency reviews, notwithstanding the fact that the Company did not identify Material Findings as part of its QC review. This was the case for 11 loans reviewed by OIG. In addition, the Company's review identified 1 loan that was reviewed in the Prefund process, not the post close process, and the material finding was outside the scope of a prefund review as it related to a debt not paid off after closing. As a result, the existence of an indemnification agreement is not per se evidence that a Material Finding requiring indemnification existed.

III. <u>loanDepot established a QC Program that included appropriate assessment, mitigation, and reporting of defects identified during QC reviews.</u>

Comment 7 >

OIG's characterization of loanDepot's QC program disregards a number of instances in which loanDepot's approach was overly protective of FHA rather than creating increased risk. It also fails to acknowledge instances in which loanDepot attempted to provide supporting documentation to OIG during the course of this audit, only for OIG to fail to provide a response to loanDepot's follow up inquiries on this issue. As a result, loanDepot disagrees that the Draft Report's findings support concluding that the Company's QC Program did not comply with HUD requirements. To the contrary, the Company's QC Program guarded against fraud, errors, and omissions, and facilitated timely and appropriate corrective action, all of which served to protect FHA and loanDepot from unacceptable risk.

a. loanDepot maintains a risk assessment methodology that the OIG acknowledges assigned conservative risk ratings to loan-level defects.

Comment 8 >

loanDepot disagrees that the Draft Report supports the OIG's characterization of the Company's risk assessments as inadequate. HUD requires that Mortgagees include low, moderate, and material risk categories in their risk assessment methodology.[7] loanDepot's risk assessment methodology, discussed in Section I(a) of this letter, includes an expanded scale that enables the Company to identify and track risks with more specificity than the minimum required by HUD while also meeting HUD's requirements. Nevertheless, in support of its conclusion that HUD did not have assurance that loanDepot's loan reviews protected the FHA insurance fund, the OIG cites two examples where, in the OIG's view, loanDepot assigned inappropriately *high* risk ratings to defects that the OIG apparently believed were not Material Findings. Rather than evidencing unacceptable risk to FHA, these examples demonstrate that loanDepot took a conservative approach to its QC reviews, thus mitigating risks to the FHA fund, even from potentially immaterial defects.

b. loanDepot management receives and responds to reports of material defects.

Comment 9 >

loanDepot's QC Plan requires monthly reporting of QC defects to senior management. Consistent with the QC Plan and FHA requirements, loanDepot provides initial QC reports to managers and relevant stakeholders, including underwriters, to review and respond to loan-level defects. Those personnel provide responses to each finding, which the QC team reviews prior to issuing a final report. On a parallel basis, the initial QC reports are also shared with senior management at monthly meetings during which senior management reviews and provides feedback on the defects identified. Therefore, contrary to the Draft Report's claims, loanDepot management is aware of and engaged with all defects uncovered during the QC process and receives regular updates about loan-level cures, self-reporting decisions, and process updates designed to prevent future defects.

The OIG's Draft Report fails to distinguish between a failure to engage management regarding defects—which loanDepot does on at least monthly basis—and a failure to adequately document that engagement. loanDepot takes both seriously and is updating its QC Plan and processes to better document management's communications regarding QC findings. However, a failure to document an existing process

[7] 4000.1, Sections V.A.2.di.(B) and V.A.3.b.iii.

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does not increase the risk to the FHA fund as the Draft Report suggests. Moreover, loanDepot worked with OIG in good faith to respond to these claims. On August 7, 2024, loanDepot provided the OIG with a file that included responses to loan-level defects identified during the Company's QC reviews. Senior management discussed those loan-level defects at monthly meetings and the loan-level responses incorporated senior management's feedback, as well as information received from managers and senior underwriters. Although the OIG acknowledged receipt of the information, it did not indicate that loanDepot's response was incomplete or that it had outstanding questions. Therefore, loanDepot believed this information satisfied the OIG's request and that further information was not required. Instead, the OIG restates in the Draft Report that loanDepot did not provide responsive documentation and incorrectly concludes that senior management did not respond to Material Findings. For the reasons described above, loanDepot respectfully disagrees, although it acknowledges that the face of the documented submitted to support senior management engagement did not clearly indicate that the loan-level responses reflected senior management's feedback.

c. loanDepot self-reported or mitigated Material Findings identified through its QC reviews.

loanDepot's QC Plan requires it to report to HUD any loans that present an unacceptable level of risk, based on HUD's criteria, through HUD's lender reporting platform.[8] The OIG included loans with a "High" severity rating in the 18 of 20 loans sampled. As stated previously, loans assigned a High rating do not constitute a material defect and do not require self-reporting to HUD. Therefore, loanDepot respectfully disagrees with the OIG's statement that 18 of the 20 loans sampled included Material Findings. In addition, upon receipt of the OIG's review findings in February 2024, loanDepot provided the OIG with additional information supporting its conclusion that a majority of these loans did not require self-reporting to HUD. As that information showed, of the 20 loans sampled, the Company identified no findings for 5 loans, High rated findings for 12 loans, and Critical findings for only 3 loans. The Company has self-reported all 3 loans with Critical (i.e. Material) findings.[9]

loanDepot acknowledges that it executed indemnification agreements for 35 loans but disagrees with the OIG's assertion that the Company did not review 30 of those loans for potential self-reporting. As described in loanDepot's QC Plan, the Company evaluates all loans reviewed as part of the QC process for self-reporting and appropriately self-reports loans assigned a Critical risk rating, the Company's equivalent of a Material Finding. As a result of the Company's re-evaluation of the defects of these loans, loanDepot will self-report 34 of the 35 loans to HUD.

IV. <u>loanDepot has already taken steps to address the Draft Report and is in the process of enhancing its QC Plan and Program to address the OIG's recommendations.</u>

In its Draft Report, the OIG recommends that HUD require loanDepot to take certain actions. loanDepot has already implemented, or is in the process of implementing, many of the recommendations in the Draft Report.

- 1A & 1B: loanDepot is in the process of updating its QC plan and related processes to align with HUD's requirements for loan selection (including maintaining data and documentation about sample size and loan selection). It is also revising its QC Plan to align with requirements for loan file reviews, assessment of findings, mitigation of findings, and reporting to HUD.
- 1C: loanDepot will provide annual training to its staff and management on HUD requirements for lender QC programs, and will provide proof of training to HUD.
- 1D: For the reasons described above, loanDepot disagrees that an additional 1,190 post-closing QC reviews are required.

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[8] *See* loanDepot Origination Quality Control Plan at 37-38.

[9] The Company self-reported 1 loan prior to receiving the Draft Report, and 2 loans after receiving the Draft Report.

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- 1E: loanDepot already reviewed the EPD loans not initially selected for review and confirmed that no self-reporting or indemnification is required.
- 1F: loanDepot has re-evaluated its QC files with High severity ratings and will take appropriate actions based on those findings. loanDepot will evaluate all loans with Critical findings and take appropriate actions based on those findings, including but not limited to self-reporting and executing indemnifications as applicable.
- 1G: loanDepot will provide indemnification agreements or documentation to support the loans in which loanDepot identified material findings.

loanDepot is committed to a maintaining a comprehensive QC Program that guards against unacceptable risks to the FHA insurance fund, and as a long time FHA-approved Mortgagee, loanDepot steadfastly supports HUD's mission and its programs. loanDepot also recognizes and values the OIG's role in furthering those goals and therefore appreciates its engagement during the audit.

If you have questions about this response, please do not hesitate to contact me directly.

Sincerely,
Joseph Grassi
Joe Grassi
Chief Risk Officer

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OIG Evaluation of Auditee Comments

Comment 1 loanDepot disagreed with our characterization of its QC program and stated that the draft report focuses on one-off human errors, a misunderstanding of its risk rating methodology, and prior indemnifications, which do not support OIG's claim that the QC program failed to achieve its purpose. It also noted that the title of the report should include the audit period to show that the findings were specific to the audit period. Although we disagree with loanDepot's assertion that the issues identified did not impact whether its QC program achieved purpose, we addressed the key concerns raised in the comments below. Further, although we did not add the audit period to the title page, it was discussed on pages 4 and 9 of the report, and we added additional references to the period on pages 3 and 5. We also commend loanDepot's efforts to begin enhancing its QC program in response to this audit.

Comment 2 loanDepot questioned our conclusion that it under-sampled when selecting loans for post-closing QC reviews and stated that we overstated the company's historical defect rate when estimating the approximate sample size that should have been used. While loanDepot acknowledged that it incorrectly used a flat 5 percent defect rate when calculating sample sizes, it disagreed that this practice increased the risk to FHA or loanDepot. It categorizes loans using a four-tiered risk rating methodology and explained its belief that its critical risk category is the only category that contains material defaults or findings. We agree that if only the historical critical risk default rate were used to calculate samples sizes, loanDepot would have oversampled. However, we believe that the historical default rate for both its high and critical risk categories should have been used when calculating sample sizes. As shown in the table below, loanDepot's definitions for these two categories align with HUD's guidance for material risk. loanDepot defines high risk as loans with findings resulting in a significant eligibility violation that ***must*** be addressed, mitigated, or cured. HUD's guidance explains that material findings represent an unacceptable level of risk and must be mitigated or self-reported.

loanDepot risk level definitions	Relevant HUD guidance
Low risk: Very minor findings that do not affect loan eligibility.	Low risk: No issues or minor variances were identified with the origination, underwriting, or servicing of the mortgage.
Moderate risk: Minor to moderate findings that should be addressed, but do not affect overall eligibility.	Moderate risk: The records contained unresolved questions or missing documentation. Issues were identified pertaining to processing, documentation, or decisions made during loan administration, but none were material. Failure to resolve these issues created a moderate risk to the mortgagee and FHA.
High risk: Findings resulting in a significant eligibility violation that must be addressed, mitigated, or cured. Critical risk: Fraud, misrepresentation, or eligibility violation resulting in an unsalable loan.	Material risk: The issues identified during the review contained material findings which represent an unacceptable level of risk. In the context of mortgage origination and underwriting, a finding is material if disclosure of the finding would have altered the mortgagee's decision to approve the mortgage or to endorse or seek endorsement from FHA for insurance of the mortgage. In the context of servicing, a finding is material if it has an adverse impact on the property and/or FHA. Note that HUD's guidance indicates that the mortgagee must report to FHA all findings of fraud or material misrepresentation. The mortgagee must report to FHA any material findings concerning the origination, underwriting, or servicing of a mortgage that the mortgagee is unable to mitigate.

We added a footnote number 5 on page 3 of the report to explain that based on this comparison, we considered loans that loanDepot classified as high or critical risk to have material findings. We acknowledge loanDepot's commitment to updating its QC Plan to require consideration of the specific defect rate of recently reviewed loans and include more detail about how to stratify loans, it should consider working with HUD to help ensure that its methodology for assessing risk aligns with HUD requirements.

Comment 3 We acknowledge loanDepot's plan to implement an additional procedure related to data pulled from Neighborhood Watch to ensure that all EPD loans are selected for review. Further, we updated a figure on page 4 of the report to acknowledge that it had only failed to perform approximately 1.5 percent of the required EPD reviews.

Comment 4 loanDepot explained that 8 of the 37 EPD loans in question have now been paid-in-full without loss claims against the FHA insurance fund. Further, it explained that it has reviewed the remaining 29 loans and did not identify any material findings. While we commend loanDepot's efforts to review the 29 loans, we disagree that the remaining 8 loans were all paid in full without loss claims. In the loan status data used during the audit, 32 loans were still active or had been terminated with a claim filed against the insurance fund. Based on a brief review of data available in February 2025, we believe that at least 31 loans are still active or had been terminated with a claim against the insurance fund. During the audit resolution process, loanDepot can provide documentation to show how it arrived at the number of loans it believes have been paid-in-full without a claim against the insurance fund and to support the results of the additional EPD reviews completed.

Comment 5 loanDepot stated that the draft report's claim that its selection data could be improved mischaracterizes the substance of OIG's finding and explained that our finding conflated several issues. While loanDepot agreed that the data provided earlier in the audit was inaccurate and explained that it has implemented improved recordkeeping practices, it insisted that the issues described in the draft report do not relate to the accuracy of its selection of loans for review. While we acknowledge loanDepot's efforts to improve recordkeeping and to change how it compiles reports in response to regulatory requests, we disagree that our concerns that the absence of quality data could compromise the integrity of its QC program were overstated. For example, as explained in the finding, the post-closing sample universe data excluded 206 loans because they were not endorsed at the time of sample selection. This compromised loanDepot's QC program because by not including these loans in its sample universe, the loans did not have a chance to be selected for review.

Comment 6 While loanDepot acknowledged that it indemnified HUD in connection with the 33 loans, it disagreed that all 33 contained material findings. For example, upon further review, it found that 11 of the 33 loans did not contain material findings warranting indemnification. Since HUD identified findings that it considered material in each of these loans, loanDepot's explanation may indicate that it needs to revisit how it assesses the risk of findings. loanDepot's comments confirm upon its reexamination of the 33 loans identified, some had material findings, which aligns with our finding that loanDepot's initial reviews sometimes missed material deficiencies.

Comment 7 loanDepot asserted that our characterization of its QC program disregards a number of instances in which its approach was overly protective of FHA rather than creating increased risk. Further, it noted that during the course of this audit, there were instances in which it attempted to provide supporting documentation to us and that proper follow up did not occur. Our goal is to present audit results in a fair and objective manner. For example, we acknowledged on page 3 that loanDepot completed a sufficient number of pre-closing reviews, and on page 6 that it had classified some findings as representing a higher risk than needed. Throughout the audit, we reviewed all requested documentation received. Although we may not agree that some of the documentation provided resolved issues raised, we held followup discussions with loanDepot and HUD for clarification when necessary.

Comment 8 loanDepot disagreed that the draft report supports our conclusion that its risk assessments were inadequate. Specifically, it noted that the two examples cited in our draft report demonstrated that it took a conservative approach to its QC reviews. Our review found that loanDepot sometimes classified findings as higher or lower than it should have based on the definitions contained in its risk assessment methodology. We added a third example on page 6 to more clearly demonstrate this. During the audit resolution process, loanDepot should consider obtaining technical assistance from HUD to help ensure that it more consistently follows HUD requirements and its risk assessment methodology.

Comment 9 loanDepot stated that management was aware of and engaged with all defects uncovered during the QC process and received regular updates but agreed that it did not adequately document the engagement and the documentation provided to OIG did not support that senior management responded to material findings. Although we agree that a failure to document does not necessarily increase the risk to the FHA fund and acknowledge that loanDepot provided various responses during the audit, the data and reports provided did not show that senior management had responded to findings when required. We commend loanDepot's commitment to updating its QC plan and processes to better document management's communications regarding QC findings.

Comment 10 loanDepot stated that findings it assigned a high risk rating do not constitute material defects or require self-reporting to HUD. However, as explained in comment 2 above, we believe that loanDepot's definition for high risk aligns with HUD's guidance for material risk. This is supported by loanDepot's acknowledgment that its re-evaluation of defects resulted in it deciding to self-report some loans. We commend loanDepot for its efforts to start re-evaluating defects to determine whether loans should have been self-reported. As part of the audit resolution process for recommendation 1B, loanDepot should consider working with HUD to help ensure that its methodology for assessing risk and reporting loans aligns with HUD requirements.

Comment 11	We commend loanDepot for the actions it is taking to begin implementing recommendations 1A, 1B, 1C, 1E, 1F, and 1G. We will work with loanDepot and HUD during the audit resolution process to resolve any outstanding items related to these recommendations and close them. We acknowledge that loanDepot disagrees with recommendation 1D. During the audit resolution process, it can work with HUD to finalize the number of additional post-closing reviews needed, which should include consideration of the historical default rate for both its high and critical risk categories, as discussed in comment 2.

Appendix C – Summary of Significant Issues Identified

The table below summarizes the significant issues identified in key areas of loanDepot's QC program.

Key area		Issue identified
Loan selection	Pre-closing reviews	
	Post-closing reviews	X
	EPD reviews	X
	Selection data	X
Loan reviews	Timeliness of reviews	
	Document review and reverification	
	Identification of material deficiencies	X
Loan review findings	Assessment of risk	X
	Mitigation and reporting of findings	X