



# Selene Finance, LP, Houston, TX

## Servicing of FHA-Insured Loans

**Office of Audit, Region 6  
Fort Worth, TX**

**Audit Report Number: 2016-FW-1005  
July 28, 2016**





**To:** Robert Mulderig, Deputy Assistant Secretary for Housing, HU  
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**From:** William W. Nixon, Acting Regional Inspector General for Audit, 6AGA  
**Subject:** Selene Finance, LP, Houston, TX, Did Not Communicate in a Timely Manner  
With Delinquent Borrowers

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Selene Finance, LP's servicing of its Federal Housing Administration-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, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 817-978-9309.



**Audit Report Number: 2016-FW-1005**

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**Selene Finance, LP, Houston, TX, Did Not Communicate in a Timely Manner With Delinquent Borrowers**

## Highlights

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### What We Audited and Why

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We reviewed Selene Finance, LP's servicing of its Federal Housing Administration-insured loans and its implementation of the U.S. Department of Housing and Urban Development's (HUD) Loss Mitigation program. Our audit objective was to determine whether Selene processed delinquent loans in accordance with HUD's requirements, especially Loss Mitigation program requirements.

### What We Found

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Except for communicating with borrowers, Selene generally complied with applicable HUD servicing requirements. Selene did not communicate in a timely manner with delinquent borrowers for 7 of 14 loans reviewed and did not comply with Federal bankruptcy laws for 1 additional loan. These conditions occurred because of lapses in Selene's internal controls. Although Selene failed to communicate in a timely manner with the seven delinquent borrowers, the borrowers did not express an interest in participating in the Loss Mitigation program. However, if Selene does not correct its internal controls, other delinquent borrowers could miss the opportunity to participate in the program. Further, it improperly made repeated collections calls to one borrower who was under bankruptcy protection.

### What We Recommend

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We recommend that the Deputy Assistant Secretary for Housing require Selene to evaluate and make changes to its internal controls to ensure that it communicates with delinquent borrowers in a timely manner and that it maintains accurate borrower account status information.

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# Background and Objective

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Selene Finance, LP, is a residential mortgage company headquartered in Houston, TX. It is engaged primarily in servicing residential mortgage loans. It was founded in February 2006 as Aegis Loan Servicing, L.P. In January 2008, the partnership name was changed to Selene Finance, LP. Selene has servicing agreements with various third parties and affiliated entities to service residential mortgage loans. Selene refers to itself as a special servicer, providing creative loan resolution strategies designed to preserve home ownership.

Selene was servicing 86,000 loans and 69,000 loans on December 31, 2014 and 2013, respectively, under various servicing agreements and for which it owned mortgage servicing rights.<sup>1</sup>

The U.S. Department of Housing and Urban Development (HUD) established the Loss Mitigation program in 1996 to ensure that distressed Federal Housing Administration (FHA)-insured borrowers would have opportunities to retain their homes and reduce losses to FHA's insurance fund. Loss mitigation is considered critical to FHA because it fulfills the goal of helping borrowers in default retain home ownership, while reducing, or mitigating, the economic impact on the insurance fund. The Loss Mitigation program gives lenders responsibility for managing loan defaults and provides financial incentives to recognize them for their efforts. Lenders have a responsibility to compare the loss mitigation options and take appropriate actions that can generate the smallest financial loss to HUD. The program consists of reinstatement options to allow borrowers to keep their homes and disposition options that assist them in the disposing of their homes.

Our objective was to determine whether Selene processed delinquent loans in accordance with HUD's requirements, especially Loss Mitigation program requirements.

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<sup>1</sup> According to Selene's audited financial statements, mortgage servicing rights are contractual agreements to service residential mortgages held in a securitization.

# Results of Audit

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## Finding: Selene Did Not Communicate in a Timely Manner With Delinquent Borrowers

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Selene did not communicate in a timely manner with delinquent borrowers for 7 of 14 loans reviewed and did not comply with Federal bankruptcy laws for 1 additional loan. These conditions occurred because of lapses in Selene’s internal controls. Although Selene failed to communicate in a timely manner with the delinquent borrowers, we concluded from the file reviews that the sample borrowers did not want to participate in the Loss Mitigation program because servicing notes showed some borrowers verbally declined to participate while the remaining borrowers did not respond to Selene’s letters with the required documentation. Even though the sample borrowers did not want to participate, other delinquent borrowers could miss an opportunity to participate if Selene does not correct its internal controls. Further, Selene improperly made numerous collection calls to one borrower who was under bankruptcy protection.

### Selene Did Not Always Communicate in a Timely Manner With Delinquent Borrowers

Selene did not always attempt initial contacts and send loss mitigation information to borrowers who had defaulted on their mortgages as required. Mortgagee Letter 2013-39, pages 2 and 3, required Selene to follow specific timelines and methods for communicating with delinquent borrowers early in their delinquency.<sup>2</sup> In most cases, Selene attempted the contacts and sent the information to the borrowers, but it did not do so in a timely manner as shown in the table below.

#### Violations of communication requirements

FHA number	No phone contact within 20 days	No mail contact within 25 days	Did not assign single point of contact <sup>3</sup> within 45 days	Did not send pamphlets within 32 and 60 days
261-9623657	X			
461-4203231	X	X		X
263-4088896	X	X	X	
221-3921179	X			
361-3728119			X	
241-8222184	X		X	
093-7409568	X		X	
<b>Totals</b>	<b>6</b>	<b>2</b>	<b>4</b>	<b>1</b>

<sup>2</sup> HUD changed the phone contact and mail contact requirements to 17 and 20 days, respectively in HUD Handbook 4000.1 Section III, paragraph A.2.h, pages 576-577 after the audit period.

<sup>3</sup> The single point of contact allowed the borrower to discuss the loan with one Selene agent instead of having to be transferred to any available agent when the borrower contacted Selene.

Selene's average delay in initiating phone contact was 12 days, and the average delay for assigning a single point of contact was 10 days. The delay for sending required pamphlets ranged between 6 and 30 days. According to Selene management, these errors occurred due to lapses in Selene's procedures, including a delay in the "onboarding," or uploading, of loan information into its servicing systems.

Not attempting contact or sending information to a delinquent borrower in a timely manner could result in a borrower missing an opportunity to participate in the Loss Mitigation program and ultimately losing a home.

### **Selene Did Not Comply With Bankruptcy Protection Laws**

Selene made many collection phone calls to a borrower who was granted bankruptcy protection. A court granted bankruptcy protection to the borrower and her husband in 2012, before Selene purchased their loan. In 2013, the borrower's husband was dismissed from the bankruptcy, while the primary borrower was still a part of the bankruptcy and still under bankruptcy protection. Selene's records mistakenly reflected that both had been dismissed from the bankruptcy, and it began making collection calls to the primary borrower. Notes in the loan file showed that beginning in November 2014, the borrower told Selene on several occasions that she was still under bankruptcy protection. The notes further showed that Selene discussed the matter with the borrower's bankruptcy trustee who confirmed that the borrower was still a part of the bankruptcy. The file notes further show that on two occasions the Selene representative noted that the case was being escalated to Selene's Bankruptcy Department and the borrower's single point of contact. However, the matter was not resolved and Selene continued making collection calls. Selene's policy outlines the duties of a single point of contact, one of which is to help clear any internal processing issues. Despite the bankruptcy protection, Selene started a foreclosure process and continued its collection calls until April 2015, when a different Selene collections representative researched the matter and confirmed that the primary borrower had not been dismissed and updated Selene's system. This condition occurred because of an apparent breakdown in communication between Selene departments which resulted in Selene not updating its mortgage servicing system in a timely manner. Selene needs to correct this control to avoid violating Federal and State bankruptcy laws, including 11 U.S.C. (United States Code) 362, which stops most collection actions, and to avoid unwarranted collection calls to borrowers who are protected by those laws.

### **Conclusion**

Selene did not communicate in a timely manner with delinquent borrowers for seven loans and may have violated Federal and State bankruptcy laws for one loan. These conditions occurred because of lapses in Selene's internal controls and could result in borrowers' being unable to participate in loss mitigation efforts and ultimately losing their homes. Further, delinquent borrowers under bankruptcy protection could receive improper collection calls.

## **Recommendations**

We recommend that the Deputy Assistant Secretary for Housing require Selene Finance to

- 1A. Implement procedures to ensure that it contacts delinquent borrowers and provides required information to them within the timeframes specified by HUD Handbook 4000.1.
- 1B. Implement procedures to ensure that it confirms borrower account status information and communicates with other departments to ensure that it takes proper account actions and does not make unwarranted collection calls when borrowers are under bankruptcy protection.



# Scope and Methodology

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Our scope generally covered Selene's servicing activities from January 1, 2013, through May 31, 2015. We performed the audit from April to December 2015 at Selene's and our offices in Houston, TX. We expanded the scope as necessary to accomplish our audit objective.

To accomplish our objective, we reviewed

- Relevant laws, regulations, HUD handbooks, and mortgagee letters.
- Selene's written policies and procedures for servicing.
- Selene's organizational chart.
- Selene's audited financial statements.
- Selene's and HUD's data systems.
- HUD monitoring reports.
- Mortgage servicing files for the sampled loans.

We also interviewed Selene staff and one borrower.<sup>4</sup>

As of July 2015, Selene serviced 8,516 loans in HUD's data systems that had experienced defaults of at least 60 days and were not reported as having loss mitigation action taken by Selene. Of these loans, we selected a stratified systematic sample of 125 loans. We used a stratified systematic sample that reflected the total number of months in which loans were in default compared to the life of the loan. We used this method because we intended to project the test results to the population of 8,516 loans and determine why Selene did not put these loans into loss mitigation. We reviewed the electronic servicing documents for 14 loans to determine whether Selene maintained adequate supporting documentation and complied with HUD servicing and loss mitigation requirements. Because we did not identify any significant issues, we did not review the remaining 111 sampled loans. Also, because we did not review the remaining loans we did not project the results to the population. We determined that the loans did not go through loss mitigation because the files showed that defaulted borrowers either did not respond to Selene's loss mitigation efforts, or the case notes showed the borrower declined participation. Through the file reviews, we assessed the reliability of the computer-processed data related to the loan histories and determined that the data were sufficiently reliable for our objective.

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.

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<sup>4</sup> We attempted to contact several borrowers from our sample but were able to contact only one.

# Internal Controls

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Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

## **Relevant Internal Controls**

We determined that the following internal controls were relevant to our audit objective:

- Effectiveness and efficiency of policies and procedures used to ensure compliance with HUD's loan servicing requirements,
- Relevance and reliability of information used for making decisions regarding loss mitigation, and
- Compliance with applicable Federal requirements.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

We evaluated internal controls related to the audit objective in accordance with generally accepted government auditing standards. Our evaluation of internal controls was not designed to provide assurance regarding the effectiveness of the internal control structure as a whole. Accordingly, we do not express an opinion on the effectiveness of Selene's internal control.

# Appendixes

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## Appendix A


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### Auditee Comments and OIG's Evaluation

#### Ref to OIG Evaluation

#### Auditee Comments

#### Comment 1



July 14, 2016

William Nixon  
Acting Regional Inspector General for Audit  
U.S. Department of Housing and Urban Development  
Office of Inspector General  
819 Taylor Street, Suite 13A09  
Fort Worth, TX 76102-6124

RE: Response to Draft Audit "Selene Finance, LP, Houston, TX, Did Not Communicate in a Timely Manner With Delinquent Borrowers"


Dear Mr. Nixon:

Thank you for the opportunity to meet with your staff to discuss the draft audit report and for the opportunity to comment on the report recommendations.

Selene Finance LP ("Selene") supports both Recommendation 1A and 1B, and since the occurrence of these events we have enhanced or implemented processes and controls that support these control objectives. We have reviewed the specific findings and our underlying policies, procedures and controls, and have initiated further enhancements to both management and control reports to provide greater assurance of compliance with these requirements.

While our independent audit functions already have each of these requirements within the scope of their testing, we have shared these findings with each group to reinforce our commitment to supporting these recommendations. As discussed with your staff in our meeting on July 7, 2016, Selene has made significant investments in the technology and resources that directly support an effective and transparent internal control environment. Selene views this investment in resources and technology as fundamental to effective governance, risk management, and compliance and will continue these efforts indefinitely.

We appreciate the cooperation and feedback from your staff throughout this review. Please do not hesitate to contact us if we may be of any further assistance.

Sincerely,  
  
Joseph Pensabene  
President and Chief Executive Officer  
Selene Finance LP

## OIG Evaluation of Auditee Comments

Comment 1 Selene did not disagree with our findings and said it supported our recommendations. Selene also said it had made changes to its processes and controls that would provide greater assurance of compliance with HUD requirements. We appreciate Selene's commitment to improving its servicing operations regarding FHA loans; however, we did not evaluate these changes to its processes and controls as they occurred after completion of our audit fieldwork. Selene will need to provide evidence to HUD that it has implemented the controls to resolve the recommendations during the audit resolution process.