

Federal Housing Finance Agency  
Office of Inspector General



**The Fair Lending Examination  
Program Was Implemented in  
Accordance with Policies and  
Procedures, But Guidance Needs  
Improvement**

Audit Report • AUD-2024-005 • May 8, 2024



AUD-2024-005

May 8, 2024

## Executive Summary

The Federal Housing Finance Agency (FHFA) enforces compliance with fair lending laws including the Fair Housing Act, Equal Opportunity Act, and Safety and Soundness Act fair housing provision by ensuring that the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (together, the Enterprises) and the Federal Home Loan Banks comply with fair lending laws. In 2018, FHFA formed the Office of Fair Lending Oversight (OFLO) within the Division of Housing Mission and Goals (DHMG) to ensure the Enterprises' compliance with applicable fair lending laws. As part of this effort, OFLO conducts the fair lending examination program.

In 2019, OFLO implemented the Interim Compliance Review Procedures governing its fair lending examination program. In December 2021, FHFA retired these interim procedures and adopted Advisory Bulletin (AB) 2021-04, *Enterprise Fair Lending and Fair Housing Compliance*. This bulletin provides FHFA's supervisory expectations and guidance to the Enterprises on fair lending compliance. In July 2022, DHMG developed Operating Procedures Bulletin (OPB) Enterprise Fair Lending and Fair Housing Compliance Examination Policies and Procedures. It sets forth internal procedures to govern OFLO's fair lending examination program.

We performed this audit to determine whether FHFA implemented its Enterprise fair lending examination program in accordance with applicable policies and procedures. Our audit scope covered OFLO's supervisory activities of the Enterprises' fair lending programs and relevant internal controls from August 1, 2022, through August 31, 2023.

We found that FHFA implemented its fair lending examination program in accordance with policies and procedures. Specifically, OFLO addressed fair lending risks, issued examination findings, and assessed the remediation of Matters Requiring Attention (MRA). While we identified no issues in the fair lending examination program implementation, we found that OFLO has not documented its process for referring potential violations of the Fair Housing Act to the Department of Housing and Urban Development (HUD) and the Department of Justice (DOJ). Furthermore, we found OFLO has not documented its process to perform quality control reviews of adverse examination findings.

We made two recommendations in this report to address our finding. In a written response, FHFA agreed with our recommendations.



AUD-2024-005

May 8, 2024

This report was prepared by Andrea Smith, Audit Director; Marco Uribe, Acting Audit Manager; and Michael Schumann, Auditor; with assistance from Abdil Salah, Assistant Inspector General for Audits. We appreciate the cooperation of FHFA staff, as well as the assistance of all those who contributed to the preparation of this report.

This report has been distributed to Congress, the Office of Management and Budget, and others and will be posted on our website, [www.fhfaoig.gov](http://www.fhfaoig.gov), and [www.oversight.gov](http://www.oversight.gov).

James Hodge, Deputy Inspector General for Audits /s/

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## ABBREVIATIONS .....

AB	Advisory Bulletin
C.F.R.	Code of Federal Regulations
DHMG	Division of Housing Mission and Goals
DOJ	U.S. Department of Justice
Enterprises	Fannie Mae and Freddie Mac
FHFA	Federal Housing Finance Agency
Green Book	Government Accountability Office's <i>Standards for Internal Control in the Federal Government</i>
HUD	U.S. Department of Housing and Urban Development
MOU	Memorandum of Understanding
MRA	Matter Requiring Attention
OFLO	Office of Fair Lending Oversight
OPB	Operating Procedures Bulletin, Enterprise Fair Lending and Fair Housing Compliance Examination Policies and Procedures

# BACKGROUND.....

## FHFA’s Office of Fair Lending Oversight

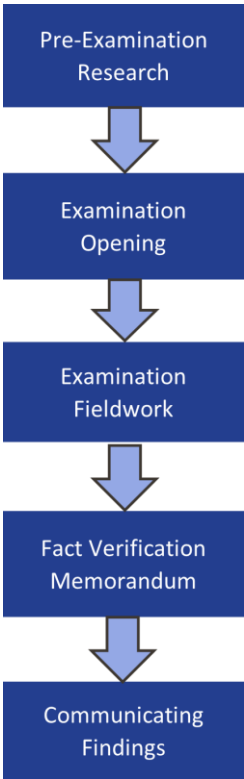
FHFA considers the Enterprises’ compliance with fair lending laws part of its responsibilities to enforce the Fair Housing Act. In 2018, FHFA’s DHMG formed OFLO to ensure the Enterprises’ compliance with applicable fair lending laws.<sup>1</sup> As part of this effort, OFLO conducts the fair lending examination program.

### *Fair Lending Examination Program*

In 2019, OFLO implemented the Interim Compliance Review Procedures to govern its fair lending examination program. These interim procedures were intended to guide OFLO’s initial compliance reviews of the Enterprises. OFLO evaluated these interim procedures based on its initial five compliance reviews and feedback from the Enterprises and internal FHFA stakeholders. In December 2021, FHFA retired them and adopted AB 2021-04, *Enterprise Fair Lending and Fair Housing Compliance*. This bulletin provides FHFA’s supervisory expectations and guidance to the Enterprises on fair lending compliance. In July 2022, DHMG developed OPB, Enterprise Fair Lending and Fair Housing Compliance Examination Policies and Procedures, based on lessons learned from the interim procedures. It sets forth internal procedures to govern OFLO’s fair lending examination program.

The OPB provides OFLO personnel with the fair lending examination process flow, shown in the figure on the right, that includes procedures for: (1) performing pre-examination research, (2) opening an examination, (3) conducting fieldwork, (4) issuing fact verification memoranda, and (5) communicating adverse examination findings, including Matters Requiring Attention (MRA).<sup>2</sup> OFLO’s pre-examination research may include reviews of monitoring information and data, academic papers, applicable referrals, past examination findings, press reports, and other appropriate resources to identify

**FIGURE 1: FAIR LENDING EXAMINATION PROCESS**



Source: FHFA’s OPB, Enterprise Fair Lending and Fair Housing Compliance Examination Policies and Procedures.

<sup>1</sup> The Enterprises are subject to fair lending laws, including the Fair Housing Act, the Equal Credit Opportunity Act, and the fair housing provisions of the Federal Housing Enterprises Financial Safety and Soundness Act. These laws cover Enterprise operations related to mortgage credit and housing and prohibit discrimination based on several protected characteristics.

<sup>2</sup> FHFA, AB 2017-01, *Classifications of Adverse Examination Findings*, classifies adverse examination findings as Matters Requiring Attention, Recommendations, and Violations.

Enterprise activities for targeted examinations.<sup>3</sup> The examination team then develops an examination plan to design how the team will conduct fieldwork. The examination opening occurs when OFLO's Associate Director authorizes the start of a fair lending examination of an Enterprise. This phase includes data requests and briefings from the Enterprise. OFLO's examination team uses the OPB guidance to conduct policy and procedure analysis, file reviews, data analysis, and interviews as part of examination fieldwork. Subsequently, OFLO issues a draft fact verification memorandum or preliminary findings letter to communicate its findings and for the Enterprise's review and comment.<sup>4</sup> This allows the Enterprise to dispute or discuss the findings, including OFLO's application of fair lending laws. For any MRA or violation issued, the Enterprise submits a remediation plan with proposed timeframes. Once OFLO concurs with the plan, a non-objection letter is sent to the Enterprise.

Throughout remediation, the Enterprises are expected to provide quarterly status updates for all ongoing remediation activities that include an explanation of each action taken in the quarter toward the remediation goals. The OPB allows the Enterprises to request extensions for their proposed remediation due dates. The request must include the rationale for the extension and proposed alternative dates. OFLO personnel explained that adverse examination findings are subject to supervisory review and, as needed, FHFA counsel review and collaboration.

### ***Enterprise Quarterly Reporting***

To facilitate FHFA in carrying out statutory oversight obligations,<sup>5</sup> the Enterprises are required to submit quarterly reports to OFLO describing their fair lending program performance.<sup>6</sup> These reports describe the Enterprises' fair lending program activities, fair lending risk assessments, testing plan and results, and underwriting and acquisition data. FHFA Fair Lending & Equity Policy Analysis Policy and Procedures provides guidance on OFLO's process to perform data validation and review of quarterly fair monitoring reports.

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<sup>3</sup> Targeted fair lending examinations are in-depth supervisory examinations of one or more Enterprise activities. They typically require an interdisciplinary examination team to analyze data, policies, procedures, and overall legal compliance.

<sup>4</sup> According to the OPB, the OFLO Associate Director may waive the fact verification memorandum at their discretion. For the two OFLO examinations completed during our scope period, the Associate Director did waive the fact verification memoranda and issued preliminary findings letters in their place.

<sup>5</sup> Statutory oversight obligations include those to exercise general supervisory and regulatory authority under 12 U.S.C. § 4511(b), examination authority under 12 U.S.C. § 4517(b), and authority to analyze and make referrals of mortgage interest rate disparities under 12 U.S.C. § 4561(d)(1).

<sup>6</sup> Fair lending monitoring information may be collected pursuant to FHFA's supervisory and regulatory authority, including 12 U.S.C. § 4514(a), which authorizes FHFA to order regulated entities to submit both regular and special reports.

***FHFA’s Coordination with the Department of Housing and Urban Development and the Department of Justice***

In August 2021, FHFA and HUD signed a memorandum of understanding (MOU) to enhance the enforcement of the Fair Housing Act and oversight of the Enterprises.<sup>7</sup> The MOU promotes interagency consultation and coordination regarding the regulated entities, prevents duplication of federal efforts, enhances oversight of the regulated entities, and supports enforcement of the Fair Housing Act. According to the MOU, FHFA will make best efforts to provide HUD an opportunity to comment on any significant adverse examination finding of a violation or enforcement action related to the Enterprises’ appraisal or underwriting guidelines that may impact HUD’s enforcement of the Fair Housing Act or section 4545 of the Safety and Soundness Act, before FHFA takes final action.

In addition to the requirements of the MOU, according to AB 2021-04 and FHFA’s Policy Statement on Fair Lending, in certain circumstances, FHFA provides notification to HUD and DOJ of information that suggests a violation or a possible pattern or practice of discrimination in violation of the Fair Housing Act. This is consistent with Executive Order 12892 on Leadership and Coordination of Fair Housing in Federal Programs: Affirmatively Furthering Fair Housing.

**FACTS AND ANALYSIS .....**

**The Fair Lending Examination Program Was Implemented in Accordance with Policies and Procedures, but Guidance Needs Improvement**

We determined that OFLO implemented its fair lending examination program in accordance with applicable policies and procedures. Specifically, OFLO addressed fair lending risks, issued examination findings, and assessed the remediation of MRAs. Since 2019, OFLO initiated five examinations, two of which were completed during our scope period. We reviewed OFLO’s examination plans, which described the objectives, rationale, and review procedures, and confirmed that they were reviewed and approved by the appropriate officials.

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<sup>7</sup> The Enterprises are subject to section 4545 of the Safety and Soundness Act. Section 4545 requires HUD, by regulation, to prohibit Enterprises from discriminating in the purchase of mortgages on the basis of race, color, religion, sex, disability, familial status, age, or national origin. This includes any consideration of the age or location of the dwelling, or the age of the neighborhood or census tract where the dwelling is located, in a manner that has a discriminatory effect.



We determined that examinations assessed the Enterprise’s non-multifamily residential home appraisal activities, a risk described in AB 2021-04.<sup>8</sup>

In accordance with the OPB, OFLO officials communicated findings, including MRAs, in the form of finding letters to the Enterprises based on examinations of their non-multifamily residential home appraisal activities. In response, the Enterprises submitted remediation plans that included interim targets with proposed completion dates, to which OFLO issued non-objection letters expressing agreement. Additionally, OFLO assessed corrective actions for 24 open MRAs.<sup>9</sup> The Enterprises requested to extend interim target remediation due dates for 5 of the 24 open MRAs. We determined that the Enterprises provided appropriate rationale, including legal review and additional coordination between its business functions, supporting OFLO’s granting of requested extensions in accordance with the OPB.

OFLO also documented its Quarterly Report Data Validation Memoranda and Fair Lending Quarterly Report Review Memoranda in accordance with FHFA Fair Lending & Equity Policy Analysis Policy and Procedures. We reviewed these reports and noted that OFLO documented its validation of the Enterprises’ data, including aggregate loan acceptance rates and counts, which reflected the Enterprises’ fair lending program performance. OFLO also documented significant changes in the Enterprises’ fair lending risk profile, concerns with the quality of the Enterprises’ risk management and internal controls, and new emerging risks.

As described below, we found that OFLO lacked documented procedures for HUD and DOJ referrals and its quality control review process.

***OFLO’s Guidance Lacks Procedures for Referrals to HUD and DOJ and Quality Control Reviews of Adverse Examination Findings***

Since 2019, OFLO made 19 referrals to HUD and two referrals to DOJ for potential violations of the Fair Housing Act as required by AB 2021-04. We inquired about the process to make referrals and were told by OFLO officials that referrals are a result of examinations with adverse findings. DHMG’s Deputy Director approves adverse findings for issuance, and OFLO’s Associate Director communicates those findings in the form of a referral letter to HUD or DOJ as applicable. The referral includes the findings letter, supporting documentation, and the associated Enterprise remediation plan. OFLO officials stated that

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<sup>8</sup> According to FHFA, non-multifamily residential home appraisal activities were risk areas identified in public HUD fair housing cases, news articles, and academic studies.

<sup>9</sup> OFLO, in accordance with the Interim Compliance Review Procedures, issued “material fair lending concerns” for two of its examinations. OFLO considered these to be broadly equivalent to MRAs and the Enterprises treated them as such. We included open material fair lending concerns in our testing of MRAs.

updates on the Enterprise's remediation efforts are communicated to HUD during coordination meetings.

We requested documented procedures that describe this process flow, but none existed. OFLO's Associate Director stated that due to the limited number of referrals, documented procedures may not be necessary. Additionally, OFLO's referral process does not have a central tracking mechanism in place if follow-up is required. OFLO maintains individual records of each referral on a shared drive, including deferral letters from DOJ where applicable, but does not monitor referral outcomes that may result in a pattern or practice of discrimination under the Fair Housing Act. In a discussion with OFLO officials, they stated that they understood our concerns with not having documented referral procedures.

We also found that OFLO lacked documented policy and procedures for its quality review of adverse examination findings. OFLO stated that adverse examination findings undergo a quality control process that includes supervisory review and, as needed, outside counsel review. Legal review of adverse examination findings occurs throughout the examination process because examination teams include FHFA fair lending legal support. While the OPB states that OFLO can include outside counsel review, as appropriate, OFLO's current process does not prescribe when outside counsel should be included in the review process. As part of its quality control review process, OFLO also provides a draft findings letter to the Enterprises for their review and comment on OFLO's conclusions and the application of fair lending laws. We confirmed that these quality reviews were performed for the examinations of the Enterprises' non-multifamily residential home appraisal activities within the scope of this audit. However, OFLO officials stated that they have not documented the quality control process and had not committed to an addendum to the OPB because they are confident in their current review process. They also recognized the importance of documenting their review process.

The Federal Records Act and 36 C.F.R. Part 1222 require each federal agency to make and preserve records necessary to document the agency's policies, decisions, procedures, and essential transactions, as well as to protect the legal and financial rights of the federal government. In addition, FHFA's Records and Information Management Policy requires all employees and contractor personnel to manage FHFA information, including records, throughout its lifecycle to facilitate and document FHFA's mission and functions.

According to the Green Book, management should design control activities to achieve objectives and response to risks and should also implement those control activities through policies. Specifically, documentation is a necessary part of an effective internal control system. It helps ensure consistency, as well as an accurate and timely recording of events. Without documented procedures, OFLO increases the risk that examiners may not consistently: (1) comply with its responsibilities for making referrals to HUD and DOJ,

(2) monitor and track violations or potential violations of the Fair Housing Act that suggest a possible pattern or practice of discrimination, and (3) perform or document their quality control review of adverse examination findings.

## **FINDING** .....

OFLO’s guidance lacks procedures for monitoring and tracking referrals to HUD and DOJ that suggest a violation or potential violation of the Fair Housing Act and performing quality control reviews of adverse examination findings.

## **CONCLUSIONS** .....

OFLO has implemented its fair lending examination program in accordance with applicable policies and procedures. These examinations assessed the Enterprise’s non-multifamily residential home appraisal activities, a risk described in AB 2021-04. We reviewed OFLO’s examination plans for these examinations that described the objectives, rationale, and review procedures. As noted above, we found that OFLO’s guidance lacks procedures for making referrals to HUD and DOJ and performing quality control reviews of adverse examination findings.

## **RECOMMENDATIONS** .....

We recommend the following for DHMG’s Deputy Director:

1. Ensure OFLO documents its process for monitoring and tracking referrals to HUD or DOJ.
2. Ensure OFLO documents its quality control review process of adverse examination findings in policy and procedures.

## FHFA COMMENTS AND OIG RESPONSE.....

We provided FHFA management an opportunity to respond to a draft of this audit report. FHFA management provided technical comments, which we considered in finalizing this report. FHFA management also provided a written response that is included as an Appendix to this report. In its management response, FHFA agreed with our recommendations and plans to:

1. Issue updated guidance to include the process for monitoring and tracking referrals to HUD and DOJ by January 31, 2025.
2. Document the quality control review process with adverse fair lending findings by January 31, 2025.

We consider FHFA’s planned corrective actions responsive to our recommendations.

## OBJECTIVE, SCOPE, AND METHODOLOGY .....

Our objective was to determine whether FHFA’s Enterprise fair lending examination program was implemented in accordance with applicable policies and procedures. The audit scope covered OFLO’s supervisory activities of the Enterprises’ fair lending program and relevant internal controls from August 2022 through August 2023.

To accomplish our objective, we performed the following procedures.

- Reviewed GAO’s Green Book (GAO-14-704G; September 2014). Determined that the risk assessment, control activities, and information and communication components of internal control were significant to this objective and focused on the underlying principles that management should: (1) identify, analyze, and respond to risks related to achieving defined objectives; (2) design control activities to achieve objectives and respond to risks; (3) implement control activities through policies; and (4) use quality information to achieve the entity’s objectives.
- Reviewed and assessed OFLO’s compliance with the following FHFA and DHMG guidance:
  - FHFA, Policy Statement on Fair Lending, 86 FR 36199 (July 9, 2021);
  - FHFA, AB 2021-04, *Enterprise Fair Lending and Fair Housing Compliance* (December 20, 2021);
  - DHMG, OPB, Enterprise Fair Lending and Fair Housing Compliance Examination Policies and Procedures (July 31, 2022); and,
  - OFLO, Fair Lending & Equity Policy Analysis Policy and Procedures (June 6, 2021).
- Reviewed the Memorandum of Understanding between HUD and FHFA set forth to enhance effective and efficient enforcement of the Fair Housing Act and oversight of the Enterprises.
- Compared the OPB to AB 2021-04 to determine whether the OPB is consistent with AB 2021-04 to provide examiners with guidance to address the Enterprises’ fair lending risks.
- Reviewed two examinations of the Enterprises’ non-multifamily residential home appraisal activities completed during our scope period for their compliance with the OPB. This included a review of OFLO’s examination workpapers, findings letters,

Enterprise remediation action plans, and non-objection letters to determine whether: (1) OFLO transmitted the findings with sufficient detail to enable remediation, (2) remediation action plans included interim and final corrective action deliverables with proposed timelines, (3) documents were approved, and (4) documents were issued to the Enterprises, as applicable.

- Reviewed Enterprise quarterly status updates to determine whether they provided appropriate explanation of action taken to address interim remediation points of 24 open MRAs and the status of future remediation points.
- Reviewed all Enterprise requests to extend 11 interim remediation point due dates for 5 of 24 MRAs to determine whether the requests were made prior to the due dates and included rationales for the extensions.
- Reviewed OFLO's Quarterly Report Validation Memoranda and Fair Lending Quarterly Report Review Memoranda to determine whether they were documented in accordance with FHFA Fair Lending & Equity Policy Analysis Policy and Procedures.
- Interviewed OFLO personnel to understand OFLO's process for assessing the risk, planning examination work, and assessing Enterprise MRA remediation related to the examinations of the Enterprises' fair lending programs. OFLO personnel included the Associate Director, Supervisory Attorney Advisor, Supervisory Policy Analyst, and Principal Financial Analyst.
- Evaluated written responses from OFLO personnel in reply and support for our information requests and interview follow-up questions.

We conducted this performance audit from September 2023 to April 2024 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: FHFA MANAGEMENT RESPONSE.....

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# Federal Housing Finance Agency

## MEMORANDUM

TO: James Hodge, Deputy Inspector General for Audits

FROM: Naa Awaá Tagoe, Deputy Director, Division of Housing Mission and Goals  
NAA AWAA TAGOE  
Date: 2024.04.24 13:35:24 -04'00'

SUBJECT: *OIG Draft Report: The Fair Lending Examination Program Was Implemented in Accordance with Policies and Procedures, But Guidance Needs Improvement*

DATE: April 24, 2024

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Thank you for the opportunity to respond to the Office of Inspector General (OIG) draft report. The objective of the OIG audit was to determine whether FHFA implemented its Enterprise fair lending examination program in accordance with applicable policies and procedures.

As background, in 2018, FHFA formed the Office of Fair Lending Oversight (OFLO), housed within the Division of Housing Mission and Goals (DHMG), to ensure the Enterprises' compliance with applicable fair lending laws. As part of this effort, OFLO conducts the fair lending examination program.

The report noted that FHFA implemented its fair lending examination program in accordance with policies and procedures. Specifically, OFLO addressed fair lending risks, issued examination findings, and assessed the remediation of Matters Requiring Attention (MRAs). OIG had no issues with the implementation of the Fair Lending Program but recommended that OFLO improve the documentation surrounding its processes. FHFA agrees with the recommendations and proposes the following corrective actions:

**Recommendation 1:** *Ensure OFLO documents its process for monitoring and tracking referrals to HUD or DOJ.*

**Management Response:** FHFA agrees with the recommendation and will take the following action by January 31, 2025. FHFA will issue updated guidance to include the process for monitoring and tracking referrals to the Department of Housing and Urban Development (HUD) and the Department of Justice (DOJ).



**Recommendation 2:** *Ensure OFLO documents its quality control review process of adverse examination findings in policy and procedures.*

**Management Response:** FHFA agrees with the recommendation and will take the following action by January 31, 2025. FHFA will document the quality control review process with adverse fair lending findings.

If you have any questions relating to our response, please contact Shelly Blackston, DHMG Audit Liaison.

cc: Edom Aweke  
John Major  
Mark David  
Shelly Blackston

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