

A Renewed Focus on Quality Control

As the mortgage industry works to restore stability and confidence in the housing market, it is prudent for lenders to adopt a strategy that will ensure the production of investment-quality mortgages. A strong quality control (QC) program should be at the forefront of that strategy and should cover all aspects of the loan processing workflow – from origination and underwriting to delivery of mortgages.

With robust back- and front-end QC functions your institution will be able to:

- Enhance the quality of mortgages you originate
- Reduce operational deficiencies and repurchase risk
- More effectively identify and prevent fraud
- Protect borrowers and support their success as long-term homeowners
- Help promote a resilient mortgage industry that is likely to withstand market fluctuations

Quality control requirements and processes at Freddie Mac

Freddie Mac's research has shown that a mortgage that does not meet Freddie Mac *Single-Family Seller/Servicer Guide* (Guide) requirements is substantially more likely to go into default than a mortgage that meets our requirements. Delivering loans that meet our Guide requirements lowers the risk that lenders will face costly borrower defaults and repurchases.

We encourage our Seller/Servicers to become familiar with the requirements outlined in the Guide, including the requirements to implement a QC program that will help ensure the delivery of investment-quality mortgages. The emphasis we place on the QC function is evident in our:

- **Post-funding QC review.** This review is an important part of our business process, which helps us better understand the loans we buy and the risks associated with them. This review process is also critical to supporting responsible lending practices. During post-funding QC reviews, we look at a sample of the loans we purchase to ensure they comply with the terms under which you agreed to sell them to us. Guide Chapter 46 provides detailed requirements and timelines related to this review process.
- **Required Seller in-house QC program.** We require our Sellers to have their own QC program with processes and controls that support compliance with our purchase requirements. In general, your in-house QC program must have written procedures, operate independently of the origination and underwriting functions, include re-verification and/or re-underwriting processes, regularly monitor the overall quality of mortgage production, and employ effective sampling and reporting procedures. You will find complete requirements for the in-house Seller QC program in Guide Chapter 48.
- **Review of Seller in-house programs.** Freddie Mac reviews, monitors and provides feedback on Sellers QC and origination practices in a variety of ways including performing on-site reviews. QC programs are evaluated primarily for compliance with our requirements and suitability to the institution's business volume and operations. Fortify your QC program with best practices

Quality Control is a critical part of our business process as evidenced in our:

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- **Required Seller in-house QC program.** We require our Sellers to have their own QC program with processes and controls that support compliance with our purchase requirements.
- **Review of Seller in-house programs.** We review, monitor and provide feedback on Sellers QC and origination practices in a variety of ways.

Fortify your QC program with best practices

While there is no single QC program that can meet the needs of every lender, there are industry best practices that you can consider and customize to enhance the effectiveness of your QC program. Here are some examples:

- Designate one individual in your company to be the quality control representative. This representative will have overall responsibility for implementing and coordinating activities under your quality control program and should not be responsible for any mortgage origination, processing, or underwriting functions.
- If you hire a third party to perform all or part of your QC program, monitor and evaluate its performance regularly to make sure the work it does serves your QC objectives and complies with Freddie Mac requirements.
- Provide your QC staff and/or third-party QC service provider easy access to copies of your contracts and Freddie Mac Guide Bulletins. It is helpful for QC staff to receive training on new requirements and be informed when there are changes in Freddie Mac's standard purchase programs or your negotiated terms of business.
- Revise your QC program on a timely basis when there are:
 - › Significant changes in your origination process or products
 - › Changes to your eligibility or underwriting requirements
 - › Changes to your investor or mortgage insurer eligibility or underwriting requirements
- Your QC program should include the use of checklists to promote consistency and efficiency in your reviews. Checklists should be designed to assist the reviewer in:
 - › Ensuring accuracy and completeness of the origination documents
 - › Evaluating underwriting decisions and the acceptability of the mortgage
 - › Verifying existence of required legal documentation
 - › Determining your company policies are met
- Incorporate in your QC process controls or reviews that promote fair lending principles and ensure compliance with anti-predatory lending requirements. At Freddie Mac, non-compliance with our anti-predatory lending requirements, including HOEPA and state anti-predatory lending laws, results in a repurchase request. The mortgage loan, the mortgage transaction and the mortgaged property itself must comply with all federal, state and local laws, rules and regulations.
- Use a combination of pre- and post-closing QC reviews with targeted and random sampling. Your sampling approach and how often you select your sample should depend on your origination volume, operations, and specific needs. Many Sellers prefer to select a QC sample at least once a month to help ensure corrective actions may be taken as soon as possible.
- Strengthen your re-verification process. Your re-verification process should be the centerpiece of your QC program. Re-verifications should be initiated as soon as possible after a sample is selected to facilitate the review of the mortgage file. Effective follow-up procedures for re-verification requests that are not returned in a timely fashion should be part of your process.
- Always protect a borrower's personal information against accidental disclosure to unauthorized recipients, especially during re-verification. Limit disclosure of a borrower's personal information to what is needed for the intended purpose. For example, you may require only the last four digits of a Social Security number; or, before you fax or mail documents with sensitive or private borrower information, confirm the accuracy of the fax number or mailing address.
- For Freddie Mac Relief Refinance MortgagesSM, run the loan being refinanced through your quality control process prior to Freddie Mac delivery to ensure it met our purchase requirements. Sellers are still liable for the representations and warranties of the mortgages that are being refinanced.

Use feedback from your in-house QC program or from Freddie Mac QC reviews to:

- Identify weaknesses and develop plans to improve your origination, underwriting, delivery, and QC processes.
- Complement your efforts to prevent and detect fraud in your operations.
- Improve your training programs for staff involved in the loan manufacturing process.

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- The effectiveness of your QC program is also largely determined by your documentation and reporting procedures. The reports should:
 - › Be filed in a timely manner. We recommend reporting on a monthly or quarterly basis. The Guide requires that the results of quality control reviews be reported in writing to the Seller's senior management within 90 days of selection of the mortgage files for review.
 - › Be distributed to the proper areas of management.
 - › Contain useful information in the right amount of detail.
 - › Elicit an appropriate response, including timely corrective action.
 - › Provide tracking and trending of results to monitor the quality of originations and underwriting.
- Feedback from your in-house program or from Freddie Mac QC reviews is valuable information. Use this feedback to:
 - › Identify weaknesses and develop plans to improve your origination, underwriting, delivery, and QC processes.
 - › Complement your efforts to prevent and detect fraud in your operations.
 - › Improve your training programs for staff involved in the loan manufacturing process.

For more information

We recognize the strain the market environment is placing on you and your staff. Now, more than ever, we are committed to working with you to help improve loan quality, address underwriting deficiencies and enhance your ability to deal with areas of concern. Here are important resources to help you learn more about our purchase requirements and gain additional QC insights:

- The [Freddie Mac Learning Center](#) offers a variety of learning opportunities and valuable resources on underwriting, QC processes and fraud prevention.
- The Guide, which you can access through the AllRegs® link on [FreddieMac.com](#), details all the requirements for doing business with Freddie Mac.