

Selling Guide Announcement SEL-2013-05

July 30, 2013

Selling Guide Updates

The *Selling Guide* has been updated to include changes to the following:

- Lender Quality Control Requirements
- Miscellaneous *Selling Guide* Updates

Each of the updates is described below. The affected chapters and topics are noted for each policy change. Lenders should review each topic to gain a full understanding of the policy changes. The updated topics are dated July 30, 2013.

Lender Quality Control Requirements

An effective quality control (QC) program is a key component of a strong control environment. Fannie Mae has significantly revised Part D, Subpart D1, Lender Quality Control Requirements, to provide lenders with specific requirements related to their ongoing QC assessment of loan origination activities and associated processes. The revised policies will help lenders identify and remediate loan-level issues, which should help reduce the risk of repurchases.

This Subpart of the Guide has been updated to describe the following key elements that Fannie Mae requires lenders to include in their QC programs and practices:

- QC Plan Contents
- Quality Standards and Measures
- QC File Reviews
- Selection of Loans for QC Review
- Reporting and Remediation

There are numerous new policies and changes and clarifications to existing policies throughout the updated Subpart. Also, like content has been reorganized. The major updates are highlighted in the table below. In addition, there is an Attachment to this Announcement that summarizes the updates to the *Selling Guide*. Lenders should carefully review the language in the *Selling Guide* for the specific changes that are being made and to ensure a full understanding of the requirements.

Part of the <i>Selling Guide</i>	Highlights of Key Updates
Chapter D1-1, Lender Quality Control Program	<ul style="list-style-type: none"> ▪ Requirement that the lender develops and implements a QC program that provides a structure for identifying deficiencies and for implementing plans to quickly remediate those deficiencies and underlying issues. ▪ Requirement that the lender establishes specific standards for loan quality in the form of target defect rates, and to categorize defects by severity levels (with the highest severity level indicating that the loan is not eligible as delivered to Fannie Mae).

Part of the <i>Selling Guide</i>	Highlights of Key Updates
	<ul style="list-style-type: none"> ▪ Clarification of the requirements for the components of prefunding and post-closing loan file reviews, loan selections, reporting on results, and taking action to remediate issues. ▪ Clarification that when a lender's file review identifies discrepancies between the data (including the property value) that was used in the underwriting decision and the data verified through the QC process, the lender must reassess the underwriting decision based on the newly verified information to determine whether the loan remains eligible as delivered. ▪ Clarification of the existing requirement that if the lender determines that the mortgage loan was not eligible as delivered, the lender must advise Fannie Mae of these findings. ▪ Establishment of a new requirement (previously a recommendation) that the lender report on the results of both prefunding and post-closing reviews to senior management on no less than a monthly basis, and that a plan for specific correction action must be developed. ▪ Requirement that the lender establish minimum requirements for the skill set and expertise of the staff performing the QC file reviews. ▪ Establishment of a new requirement that the lender ensure that the QC vendor conducts its reviews in accordance with the lender's QC plan and Fannie Mae's requirements. ▪ Establishment of a new requirement that the lender review at least 10% of the loans reviewed by vendors, including those with and without findings. This review must be conducted by the lender and not contracted out.
Chapter D1-2, Lender Prefunding Quality Control Mortgage Review	<ul style="list-style-type: none"> ▪ Clarification that prefunding QC should operate independently of lender's production, but at a minimum must be conducted by someone independent of the decision on the loan being reviewed. ▪ Clarification that the lender's prefunding QC plan must contain requirements for full reviews of loan files and analysis of data and documents prior to funding once there is sufficient documentation in the file to perform the required review.
Chapter D1-3, Lender Post-Closing Quality Control Mortgage Review	<ul style="list-style-type: none"> ▪ Clarification of the minimum requirements for the evaluation of the loan. ▪ Clarification that the full QC process including rebuttals must be completed within 120 days from the month of the loan closing. ▪ Clarification of the random and discretionary selection requirements and that mortgage loans must be selected for

Part of the <i>Selling Guide</i>	Highlights of Key Updates
	<p>post-closing QC reviews on at least a monthly basis through both a random and a discretionary selection process.</p> <ul style="list-style-type: none"> ▪ Changes to requirements for post-closing reviews, including those related to the review of approval conditions, credit reports, owner-occupancy, reverifications of assets, data integrity reviews, and review of closing documents. ▪ Clarification that the lender must have a process for an annual review of an appraiser's state licensing or certification status, a procedure for suspending or terminating business with individual appraisers, and a procedure for referrals of appraisers to the applicable state appraiser licensing and regulatory board. ▪ Establishment of a new requirement for the lender to only use Fannie Mae's appraisal field review forms. ▪ Establishment of new requirements for the contents of the monthly post-closing QC reports. ▪ Addition of the Lender Self-Report Mailbox as the method for lenders to notify Fannie Mae of loans that were determined to be ineligible as delivered to Fannie Mae. ▪ Establishment of a new requirement that the lender provide a copy of the QC audits and the audits of the QC process to Fannie Mae upon request.

NOTE: *The requirement in D1-3-05, Lender Post-Closing Quality Control Review of Closing Documents, to take steps to correct any data errors in Fannie Mae's systems (DU[®] or Loan Delivery) has been removed. Further guidance will be provided in a future announcement and Selling Guide update with updated processes on data corrections when errors are identified through the QC review process, including when errors are identified through the review of closing documents. In the meantime, lenders should continue their current processes for notifying Fannie Mae of any data corrections that need to be made.*

Effective Date

Lenders may implement these changes immediately and must implement them no later than January 1, 2014.

Miscellaneous Selling Guide Updates

The following miscellaneous changes have been made to the *Selling Guide*:

- [A2-3.3-01](#), Compensatory Fees. This topic now includes a link to [C2-2-01](#), General Requirements for Good Delivery of Whole Loans. As stated in that topic, the amount delivered for a whole loan commitment may not exceed or fall below the original commitment amount by more than the greater of \$10,000 or 2.5% of the original commitment amount. If the actual delivery falls outside of that tolerance, Fannie Mae may charge a compensatory fee.
- [B3-3.1-06](#), Requirements and Uses of IRS Form 4506-T. When this topic was updated in May 2013, it contained potentially conflicting requirements regarding the need for IRS transcripts for all loans when tax returns are used to document income. The language of concern was removed. The *Selling Guide* clearly states that lenders may use IRS transcripts in lieu of tax returns in certain instances, but transcripts are not required for *all* loans with tax returns.

- [B4-1.1-05](#), Field Reviews. The policy related to the refusal to accept appraisals from specific appraisers was revised to complement the changes made to D1-3-04, Lender Post-Closing Quality Control Review of Appraisers and Appraisals.
- [B5-2.2-06](#), Manufactured Housing Legal Considerations and [E-1-01](#), References to Fannie Mae's Website. Fannie Mae will no longer provide information concerning titling requirements for manufactured housing loans. As a result, the references to state titling requirements resources have been removed from the *Selling Guide* and from Fannie Mae's website.
- [B5-5.2-02](#), DU Refi Plus™ and Refi Plus™ Underwriting. As announced in the May 2013 *Selling Guide*, the dates in this topic have been updated to indicate that the mortgage insurance flexibilities available for DU Refi Plus and Refi Plus apply only to mortgage loans with application dates on or before December 31, 2015, and whole loans that are purchased by Fannie Mae no later than September 30, 2016, or in an MBS pool with an issue date no later than September 1, 2016.
- [C2-2-06](#), Authorization to Transfer Funds, and [C2-2-07](#), Purchase Payee Codes. The *Seller's Designation of Wire Transfer Instructions* (Form 482) has been updated and re-titled (it was formerly known as the *Lender's Designation/Deletion of Payee Information*). The updates allow the Form to be submitted via email, making the process easier for lenders and more efficient for Fannie Mae. The new version of Form 482 is available on [Fannie Mae's website](#) and should be employed by lenders immediately.
- [E-1-03](#), List of Contacts. As a result of the changes to Subpart D1, Lender Quality Control Requirements, added a row and an email link to the Lender Self-Report Mailbox.
- [E-3-12](#), Glossary of Fannie Mae Terms: L. The definition of "last paid installment date," as defined in [Appendix D](#) of the Uniform Loan Delivery Dataset (ULDD) *Implementation Guide*, was added to the Glossary.
- [E-3-21](#), Glossary of Fannie Mae Terms: U. The definition of "unpaid principal balance," as defined in the Uniform Loan Data Delivery (ULDD), was added to the Glossary. The definition also states that "outstanding principal balance" is synonymous with "unpaid principal balance."

Effective Date

These changes are effective immediately.

Lenders who have questions about this Announcement should contact their Account Team.

John Forlines
Senior Vice President
Chief Credit Officer for Single-Family

Attachment

This table briefly describes the policy changes that have been made in the July 30, 2013, *Selling Guide* for the lender quality control requirements. Additional updates were made to clarify existing policies, reorganize like content, and remove redundant text. These are also described below. (Minor grammatical or other formatting changes are not identified.) Refer to the specific topics in the *Selling Guide* to see the actual changes. In the event of any discrepancy between the information in this Attachment and the *Selling Guide*, the provisions in the *Selling Guide* will prevail.

Topic Number and Title	Summary of Policy Changes, Clarifications, and Updates
Part D, Subpart D1, Lender Quality Control Requirements	
D1-1-01 , Lender Quality Control Programs, Plans, and Processes	<p>QC Plan Requirements</p> <ul style="list-style-type: none"> ▪ Required that the lender’s QC program must include a documented QC plan that outlines requirements for validating that loans are originated in accordance with its established policies and procedures and established standards for quality, and incorporates systems and processes for achieving those standards. Established and described the minimum information that must be contained in the lender’s QC plan. ▪ Removed the requirement that the training for the QC staff be documented in the QC plan. ▪ Clarified that the QC file review process must include a process for <ul style="list-style-type: none"> • confirming compliance with the <i>Selling Guide</i>, all related contractual terms and agreements, and that the loans are in all respects eligible for delivery to Fannie Mae; and • confirming compliance with applicable federal, state, and local laws and regulations. ▪ Clarified and established new requirements for the written procedures for reporting on the results of the QC file reviews, and to require a timely response to, and resolution of, findings identified in the QC review process. ▪ Required that lenders identify in the QC plan the location of where the QC findings and all related documentation are kept. <p>Quality Standards and Measures</p> <ul style="list-style-type: none"> ▪ Established new requirements for the lender to identify any loan with a defect (loans not in compliance with the <i>Selling Guide</i> or other related contractual terms and agreements). ▪ Established a new requirement that the lender develop severity levels to categorize defect severity. ▪ Established new requirements for target defect rates to be established and if necessary, reset at least annually. <p>QC File Review Overview</p> <ul style="list-style-type: none"> ▪ Clarified that the lender must establish a process to evaluate and monitor the overall quality of mortgage production through prefunding and post-closing reviews, and that the reviews include, at a minimum <ul style="list-style-type: none"> • compliance with Fannie Mae’s requirements by confirming that <ul style="list-style-type: none"> ○ the loan meets eligibility and underwriting requirements,

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	<ul style="list-style-type: none"> ○ the underwriting decision is adequately supported and all documentation required to support the decision is contained in the file, and ○ the loan is secured by a property that provides acceptable collateral; and ● compliance with all federal, state, and local laws and regulations. <ul style="list-style-type: none"> ■ Clarified that the lender must reassess the underwriting decision when the file review process identifies discrepancies between the data or information used in the underwriting decision and the data or information verified through the QC process, and determine whether the loan remains eligible as delivered to Fannie Mae. ■ Clarified that if the lender determines that the mortgage loan was not eligible as delivered, the lender must advise Fannie Mae of these findings. ■ A new reference to the Lender Self-Report Mailbox is provided. <p>Selection of Loans for QC Review</p> <ul style="list-style-type: none"> ■ Clarified that lenders should understand and assess the holistic risk inherent in their origination processes when considering elements to target for prefunding or post-closing discretionary reviews. ■ Clarified that the sampling methodology for prefunding and post-closing discretionary reviews must be flexible to target loans with higher potential for risk and be regularly re-evaluated and adjusted as these risks change over time. ■ Required that review cycles be structured to ensure transactions originated by each third-party originator are reviewed at least once annually. <p>Reporting and Remediation</p> <ul style="list-style-type: none"> ■ Established a new requirement (previously a recommendation) that the lender report on the results of both prefunding and post-closing reviews to senior management on no less than a monthly basis, and that a plan for specific correction action must be developed, including the expected resolution and the time frames for implementation.
<p>D1-1-02, Lender Quality Control Staffing and Outsourcing of the Quality Control Process</p>	<p>Requirements for QC Operations Reporting Structure and Staffing</p> <ul style="list-style-type: none"> ■ Clarified that post-closing QC employees must operate independently of the production, underwriting, and closing departments and provided an exception to this requirement in situations when the size of the lender's organization is insufficient to support adequate resources to allow for separation. ■ Established a new requirement that lenders establish minimum requirements for the skill set and expertise of the staff performing the QC file reviews by documenting minimum job qualifications. ■ Clarified that all employees conducting QC reviews must be adequately trained and have sufficient experience levels relative to the reviews being conducted, including manual underwriting and use of automated underwriting systems, as applicable. <p>Outsourcing of the QC File Review Process</p>

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	<ul style="list-style-type: none"> ▪ Established a new requirement that the lender must ensure that the QC vendor conducts its reviews in accordance with the lender's QC plan. ▪ Established a new requirement that the lender establish a process to review at least 10% of the loans reviewed by vendors, including those with and without findings. This review must be conducted by the lender and not contracted out.
<p>D1-2-01, Lender Prefunding Quality Control Mortgage Review Process</p>	<ul style="list-style-type: none"> ▪ Clarified that prefunding QC should operate independently of lender's production, but at a minimum, must be conducted by someone independent of the decision on the loan being reviewed. ▪ Clarified that the lender's prefunding QC plan must contain requirements for full reviews of loan files and analysis of data and documents prior to funding. ▪ Clarified that targeted reviews, control points, or third-party data checks conducted during the origination process are not a substitute for the full file review requirement. <p>Timing of Mortgage Loan File Reviews</p> <ul style="list-style-type: none"> ▪ Established a new requirement that prefunding reviews be conducted once there is sufficient documentation in the file to perform the required review of data and documents. <p>Loan Selection Process</p> <ul style="list-style-type: none"> ▪ Established new requirements (previously recommendations) that the lender establish a process for prefunding QC loan selection, and that the process be regularly re-evaluated to ensure that the sample, including sample size, selected is appropriate. <p>Verification of Data and Documents</p> <ul style="list-style-type: none"> ▪ Clarified that the lender's prefunding QC review process must include a review of the stated data and documents to ensure the documents are present and complete, and that the data relied upon in making the underwriting decision is accurate. <p>Reporting</p> <ul style="list-style-type: none"> ▪ Established a new requirement (previously a recommendation) that the lender establish and implement a process to report defects identified in the prefunding QC reviews, and established minimum required elements for the reports.
<p>D1-3-01, Lender Post-Closing Quality Control Review Process</p>	<p>Loan File Review Process</p> <ul style="list-style-type: none"> ▪ Clarified that the post-closing mortgage loan file review process must include a review of the loan to assess the accuracy and integrity of the information used to support the lending decision, the documentation of any defects, and an assessment as to whether or not the loan complies with the <i>Selling Guide</i>, all related contractual terms and agreements, and is in all respects eligible for delivery to Fannie Mae. ▪ Clarified the minimum requirements for the evaluation of the loan. ▪ Clarified that the full QC process including rebuttals must be completed within 120 days from the month of the loan closing. <p>Loan Selection</p> <ul style="list-style-type: none"> ▪ Clarified that Fannie Mae may require changes to the lender's

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	<p>statistical sampling methodology.</p> <ul style="list-style-type: none"> ▪ Clarified that the lender must establish a process for discretionary QC loan selections, taking into account the lender's assessment of risks. ▪ Established a new requirement that the discretionary selection process must be regularly re-evaluated and adjusted to ensure the sample, including sample size, is appropriate. ▪ Clarified the requirement that loans selected for post-closing discretionary QC reviews target areas that the lender identifies as having a higher potential for errors, misrepresentation, or fraud.
<p>D1-3-02, Lender Post-Closing Quality Control Review of Approval Conditions, Underwriting Decisions, and Documentation</p>	<ul style="list-style-type: none"> ▪ Allowed reverification documentation to be retained either in the underwriting file or in the lender's QC records. ▪ Clarified that, when information obtained through the reverification process differs from the information utilized in the underwriting of the loan, the lender must re-underwrite the loan to verify that the loan remains eligible as delivered to Fannie Mae. ▪ Clarified that for all loans the lender must determine that the loan was underwritten in accordance with Fannie Mae's underwriting requirements and that adequate support for the underwriting decision is contained in the loan file. ▪ Clarified that the lender must confirm that all loan approval conditions were satisfied, and that information on the closing documents, including the HUD-1 Settlement Statement, is consistent with the underwriting decision and the final terms of the mortgage loan. ▪ Clarified that for DU loans, the lender must confirm that all DU Verification Messages/Approval Conditions that appear in the DU Underwriting Findings report were satisfactorily resolved and adequately supported by appropriate documentation. <p>Requirements for Reverifications</p> <ul style="list-style-type: none"> ▪ Clarified that reverifications must be done for all loans selected through the random selection process. ▪ Provided new guidance on targeted discretionary loan selections and required that the lender consider the purpose of the targeted selection and conduct the appropriate reverifications or reviews. ▪ Clarified the expectation for the execution of IRS Form 4506-T for all loans selected through the random selection process. ▪ Clarified that transcripts must be obtained for all income types used in the underwriting process, and that if tax returns were required in the underwriting of the loan, the lender must obtain transcripts for the same tax years as documented by the borrower's returns. ▪ Established a new requirement (previously a recommendation) that the lender attempt to reverify the borrower(s)' assets and reconcile the information from the financial institution with the information in the underwriting file. ▪ Established a new requirement that when conducting the reverification of the borrower's credit history, the lender must obtain a new tri-merge credit report (rather than an in-file) in all cases. ▪ Removed the requirement that when conducting the reverification of the borrower's credit history, the new credit report must be obtained through a source other than the original credit reporting agency. ▪ Clarified that the liability information obtained on the new credit report

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	<p>be reconciled against the credit report or references used at the time of underwriting the loan.</p> <ul style="list-style-type: none"> ▪ Clarified that any 'potential red flag' messages must be addressed and documented. ▪ Removed the requirement to verify owner-occupancy for second homes. ▪ Added a new requirement to review the hazard insurance policy and other documentation to confirm that there are no indicators that the property is not the borrower's principal residence.
<p>D1-3-03, Lender Post-Closing Quality Control Review of Data Integrity</p>	<ul style="list-style-type: none"> ▪ Clarified that both DU loans and manually underwritten loans must be reviewed to ensure the final terms of the loan align with the data on which the underwriting was based. When discrepancies are identified, the lender must reassess the underwriting decision to determine if the loan remains eligible as delivered to Fannie Mae. ▪ For DU loans, the specific data elements that must be reviewed have been replaced with the comprehensive requirement that the lender must ensure all data submitted to DU is true, correct, and complete, and that the loan file must contain documentation that supports all data submitted to DU to process the loan. ▪ Clarified the steps that the lender must follow if inconsistencies are identified between the data used in underwriting and the source documents, and provided new guidance for manually underwritten loans.
<p>D1-3-04, Lender Post-Closing Quality Control Review of Appraisers and Appraisals</p>	<ul style="list-style-type: none"> ▪ Clarified that the lender's evaluation of the quality of its appraisals includes the normal underwriting of all appraisal reports as well as field reviews and desk reviews conducted through the QC process and the use of third-party tools and information to help identify areas of inaccuracy or inconsistencies that may be indicators of appraisal deficiencies. <p>Oversight of Appraisers</p> <ul style="list-style-type: none"> ▪ Clarified that the lender's QC plan must include requirements for monitoring and assessing the overall quality of work performed by an appraiser. ▪ Clarified that the lender is accountable for the quality of the QC appraisal reviews regardless of whether the work is performed by the lender or by an outsourced service provider. ▪ Clarified that the lender must have a process for an annual review of an appraiser's state licensing or certification status and a procedure for suspending or terminating business with individual appraisers. ▪ Established a new requirement that the lender have a procedure for referrals of appraisers to the applicable state appraiser licensing and regulatory board. <p>Verification of Appraisals by Field Review</p> <ul style="list-style-type: none"> ▪ Clarified that the lender must obtain an appraisal field review to evaluate the appraisal for 10% of the mortgage loans selected for QC review via the random selection process. ▪ Removed property inspections and retrospective appraisals as eligible reverification tools. ▪ Established a new requirement for Fannie Mae's appraisal forms to be

Topic Number and Title	Summary of Policy Changes, Clarifications, and Updates
	<p>used for field reviews.</p> <p>Verification of Appraisals by Desk Review</p> <ul style="list-style-type: none"> ▪ Clarified that lenders are permitted to use automated valuation models (AVM) as tools in the completion of the valuation assessment for desk reviews, and eliminated the requirement for a field review or retrospective appraisal to be ordered if the AVM identifies discrepancies between the appraisal and the AVM. <p>Reporting</p> <ul style="list-style-type: none"> ▪ Established that the lender must review the results of the QC reviews to determine whether any defects identified would result in the loan not being eligible as delivered to Fannie Mae. ▪ Established the requirement that if the lender determines that the loan was not eligible as delivered, the lender must advise Fannie Mae via the Lender Self-Report Mailbox.
<p>D1-3-05, Lender Post-Closing Quality Control Review of Closing Documents</p>	<ul style="list-style-type: none"> ▪ Clarified that the lender is responsible for reviewing each transaction and closing document for completeness, accuracy, and compliance with all underwriting and eligibility requirements, and to ensure adherence to the loan transaction. ▪ The list of documents requiring QC review has been updated to include the <i>Uniform Residential Loan Application</i> (Form 1003 or 1003(S)) and the signed sales contract and any applicable addenda. ▪ The requirement to take steps to correct any data errors in Fannie Mae's systems (DU or Loan Delivery) has been removed. Further guidance will be provided in a future announcement and <i>Selling Guide</i> update. Lenders should continue their current processes for notifying Fannie Mae of any data corrections that need to be made.
<p>D1-3-06, Lender Post-Closing Quality Control Reporting, Record Retention, and Audit</p>	<ul style="list-style-type: none"> ▪ Established new requirements for the content of the monthly internal post-closing QC reports. ▪ Aligned with Part A of the <i>Selling Guide</i> the lender's responsibility for self-reporting immediately to Fannie Mae if it learns about any misrepresentation or possible breach of a selling warranty, including fraud. ▪ Added QC reports as a record that the lender must retain and provide a copy to Fannie Mae upon request. ▪ Established a new requirement that the lender must provide a copy of the QC audits and the audit of the QC process to Fannie Mae upon request.