



U.S. DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT
OFFICE OF INSPECTOR GENERAL

MEMORANDUM NO.
2012-CF-1810

June 27, 2012

MEMORANDUM FOR: Dane M. Narode, Associate General Counsel, Office of Program Enforcement, CACC

FROM: Kim Randall, Director, Civil Fraud Division, GA

SUBJECT: Final Civil Action: Flagstar Bank, FSB, Settled False Claims Act Allegations of Submitting False Certifications to HUD on FHA Loans

INTRODUCTION

The U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), assisted the U.S. Attorney's Office, Southern District of New York, in conducting a review of Flagstar Bank, FSB. The objective of the review was to determine whether Flagstar conducted its operations in the underwriting of Federal Housing Administration (FHA) loans in accordance with HUD-FHA regulations.

SCOPE AND METHODOLOGY

To assist the U.S. Attorney's Office, we performed the following:

- Obtained loan-level data from HUD's Single Family Data Warehouse and Neighborhood Watch systems;
- Obtained FHA loan files from Flagstar;
- Obtained FHA loan files from HUD's Homeownership Centers;
- Identified Flagstar underwriter information from HUD's systems;
- Provided a 2005 OIG audit report on Flagstar's operations;
- Provided information on various HUD reviews of Flagstar;
- Researched and provided guidance regarding underwriter qualification requirements and responsibilities and the allowable use of assistant underwriters;

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- Provided various HUD handbooks, mortgagee letters, and other guidance;
 - Interviewed HUD staff; and
 - Provided copies of Flagstar's annual lender certifications required for participation in the FHA program.

BACKGROUND

Flagstar Bank, FSB, is a supervised direct endorsement lender headquartered in Troy, MI. Since 1988, Flagstar has been a participant in the direct endorsement lender program, a Federal program administered by FHA. The direct endorsement lender program authorizes private-sector mortgage lenders to approve mortgage loans for FHA insurance. Lenders approved for the program must follow various HUD-FHA requirements and provide annual and per loan certifications that the lender complies with these requirements when underwriting and approving loans for FHA insurance.

RESULTS

Flagstar did not conduct its operations in the underwriting of FHA loans in accordance with HUD-FHA regulations. On February 24, 2012, Flagstar admitted, acknowledged, and accepted responsibility for submitting false certifications to HUD about the eligibility of its loans for FHA insurance. In a settlement reached with the U.S. Attorney's Office, the lender agreed to pay \$132.8 million to the United States in damages and penalties under the False Claims Act and to reform its business practices.

Flagstar admitted that during the period January 1, 2002, to February 24, 2012, it delegated underwriting decisions to unauthorized staff. The lender also admitted that it underwrote and approved for FHA insurance loans that did not comply with certain HUD-FHA underwriting requirements, and HUD paid insurance claims on these ineligible loans. Further, the U.S. Attorney's Office announced that Flagstar set daily quotas for its HUD-approved underwriters and underwriting assistants and paid these employees substantial incentive awards for exceeding daily quotas.

Flagstar agreed to pay \$132.8 million and to other concessions to resolve the U.S. Government's claims. The lender agreed to pay \$15 million within 30 days after approval of the settlement by the court and make additional payments totaling \$117.8 million as soon as it met certain financial benchmarks. Additionally, Flagstar agreed to (1) comply with all relevant HUD-FHA rules applicable to direct endorsement lenders, (2) the completion of a 1-year period in which Flagstar's compliance with HUD-FHA rules would be monitored by a third party at Flagstar's expense, and (3) implementation of a training program for all employees involved in the origination and underwriting of FHA loans. Flagstar also agreed to certify to HUD that the individuals in senior leadership positions who previously had primary responsibility for initiating and overseeing Flagstar's manual underwriting process were no longer employed by the lender.

RECOMMENDATION

We recommend that HUD's Office of General Counsel, Office of Program Enforcement,

- 1A. Agree to allow HUD OIG to post the \$14,550,000 (the amount received by HUD as of April 2012) recovery to HUD's Audit Resolution and Corrective Actions Tracking System.