



**UNITED STATES ATTORNEY'S OFFICE**  
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**MANHATTAN U.S. ATTORNEY SUES FLAGSTAR BANK FOR  
FRAUDULENT MORTGAGE LENDING PRACTICES AND SETTLES  
FOR \$132.8 MILLION AND OTHER CONCESSIONS**

*Bank Admits and Accepts Responsibility for Submitting False Certifications to HUD and Also  
Agrees to Reform Practices*

Preet Bharara, the United States Attorney for the Southern District of New York, Helen Kanovsky, General Counsel of the U.S. Department of Housing and Urban Development ("HUD"), and David A. Montoya, the Inspector General of HUD, announced today that the United States has filed, and simultaneously settled, a civil fraud lawsuit against FLAGSTAR BANK, F.S.B. ("FLAGSTAR"), one of the nation's largest savings banks and originators of mortgage loans, for improperly approving residential home mortgage loans for government insurance. In the settlement, FLAGSTAR admitted, acknowledged, and accepted responsibility for submitting false certifications to HUD. The false certifications induced the Federal Housing Administration ("FHA") to accept loans for government insurance that were not eligible and that resulted in losses to HUD when the loans defaulted. FLAGSTAR 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. The settlement was approved today by United States District Judge Katherine B. Forrest.

Manhattan U.S. Attorney Preet Bharara stated: "The lawsuit filed today is another stark example of how certain lenders put profit ahead of responsibility by recklessly churning out mortgage loans without regard to the risk that those loans would default or the significant consequences for the individual homeowners who would inevitably default on their loans, the housing market, and in the aggregate, our nation's economy. With today's settlement FLAGSTAR has accepted responsibility for its conduct, and committed to reform its business practices to ensure compliance with HUD requirements. Participation in this federally subsidized program is a privilege, not a right, and the cases this office has filed against banks that abuse this privilege should underscore our commitment to holding them to account."

HUD General Counsel Helen Kanovsky stated: “It is absolutely fundamental that lending institutions that earn the authority to directly endorse FHA-insured mortgages apply our standards. Lenders that play fast and loose with FHA requirements, placing families at unnecessary risk, do so at their own peril.”

HUD Inspector General David A. Montoya stated: “Today’s settlement is the latest example of our continued work of holding FHA Direct Endorsement Lenders accountable for adhering to strict underwriting standards. I laud the cooperation between my office and the Departments of Housing and Urban Development and Justice to bring this matter to closure. This success could not have happened without the untold energy and effort of my audit, investigative and legal staff, and their foundational role in enabling today’s settlement.”

The following allegations are based on the Complaint filed today in Manhattan federal court:

FLAGSTAR has been a participant in the Direct Endorsement Lender program (“DEL program”), a federal program administered by the FHA, since 1988. The DEL program authorizes private-sector mortgage lenders (“Direct Endorsement Lenders”) to approve mortgage loans for insurance by the FHA. If a Direct Endorsement Lender approves a mortgage loan for FHA insurance and the loan later defaults, the holder of the loan may submit an insurance claim to HUD for the costs associated with the defaulted loan that HUD must then pay. Under the DEL program, neither the FHA nor HUD reviews a loan before it is endorsed for FHA insurance. Consequently, it is crucial that Direct Endorsement Lenders follow the DEL program rules in determining which loans to approve for FHA insurance. One such rule requires that Direct Endorsement Lenders employ experienced underwriters who have demonstrated knowledge and skill in mortgage evaluation and the principles of mortgage underwriting (“DE underwriters”) to conduct due diligence on loans before they are endorsed for FHA insurance.

From January 1, 2002 to the present (the “Covered Period”), FLAGSTAR routinely delegated key underwriting functions to staff employees who were not DE underwriters. Notwithstanding the fact that these “underwriting assistants” lacked the qualifications necessary to be DE underwriters, they were frequently assigned by FLAGSTAR to review conditions that had been placed on FHA loans and to make the final decision on whether the requisite conditions for FHA insurance had been met. Even though FLAGSTAR permitted these key underwriting responsibilities and decisions to be delegated to underwriting assistants, FLAGSTAR’s DE underwriters falsely certified to HUD, for each loan they manually underwrote and endorsed for government insurance, that the DE underwriters had themselves reviewed all of the loan documents and had exercised due diligence in underwriting the loans.

The Complaint also alleges that FLAGSTAR’s DE underwriters repeatedly endorsed loans for FHA insurance that did not comply with HUD’s underwriting requirements and thus were not eligible for government insurance. FLAGSTAR’s DE underwriters nevertheless falsely certified to HUD, for each loan they endorsed for FHA insurance, that it was eligible for such insurance.

FLAGSTAR also set daily quotas for its DE underwriters and underwriting assistants, specifying the number of loans and conditions that they had to process per day, and paid these employees substantial incentive awards for exceeding their daily quotas. For example, in 2008, 10 FLAGSTAR DE underwriters earned at least \$30,000 in incentive awards, with the top earner

receiving \$82,180.33 in extra compensation. The default rates on the loans that these 10 DE underwriters manually underwrote and approved for FHA insurance in 2008 were higher than the average default rate for all of the manually-underwritten loans that Flagstar approved for FHA insurance that year.

As part of the settlement, FLAGSTAR has admitted, acknowledged, and accepted responsibility for the following conduct:

- Notwithstanding loan-level certifications to the contrary, a Flagstar DE underwriter did not, in every instance, ‘personally review’ ‘all associated documents’ for the loans that Flagstar manually underwrote and endorsed for FHA insurance during the Covered Period.
- In a number of instances, underwriting assistants were the only ones to review documents associated with material conditions on the loans that Flagstar manually underwrote and approved for FHA insurance during the Covered Period.
- In a number of instances, underwriting assistants cleared material conditions — without DE underwriter supervision — relating to the borrower’s income, assets and credit.
- In a number of instances, notwithstanding loan-level certifications to the contrary, loans that Flagstar underwrote and approved for FHA insurance during the Covered Period, and for which HUD has paid insurance claims, did not comply with certain underwriting requirements contained in HUD’s handbooks and Mortgage Letters and were therefore ineligible for mortgage insurance under the DEL program.
- Flagstar made false certifications on loans that induced the FHA to accept for Government insurance loans that were ineligible and that the FHA otherwise would not have insured, and that resulted in losses to HUD when the loans defaulted.

Under the settlement, FLAGSTAR has agreed to pay \$15 million within 30 days after approval of the settlement by the Court, and to make additional payments totaling an additional \$117.8 million as soon as FLAGSTAR meets certain financial benchmarks. The settlement payments represent the maximum that FLAGSTAR can pay, consistent with its banking regulatory requirements and other requirements, including capital requirements imposed by the Office of the Comptroller of the Currency and the obligation of its parent holding company to satisfy its obligations in connection with the Troubled Asset Relief Program.

FLAGSTAR has also agreed to comply with all relevant HUD/FHA rules applicable to Direct Endorsement Lenders. FLAGSTAR has further agreed that, in addition to complying with all relevant HUD/FHA rules applicable to Direct Endorsement Lenders, FLAGSTAR’s continued participation in the DEL program is conditioned on: (1) FLAGSTAR’s completion of a one-year period during which FLAGSTAR’s compliance with all HUD/FHA rules applicable to Direct Endorsement Lenders shall be monitored by a third party at FLAGSTAR’s own expense (under certain conditions, this monitoring period may be extended by HUD for an additional two years); (2) FLAGSTAR’s implementation of a training program for all employees involved in the origination and underwriting of FHA loans regarding all relevant HUD/FHA rules applicable to Direct Endorsement Lenders; and (3) FLAGSTAR’s certification to HUD that the individuals in senior leadership positions who previously had primary responsibility for,

respectively, initiating and overseeing FLAGSTAR's manual underwriting process are no longer employed by FLAGSTAR.

The case is being handled by the Office's Civil Frauds Unit. Mr. Bharara established the Civil Frauds Unit in March 2010 to bring renewed focus and additional resources to combating financial fraud, including mortgage fraud.

The Complaint filed today against FLAGSTAR represents the fourth civil fraud lawsuit brought by this Office in the last nine months alleging reckless or fraudulent lending practices by residential mortgage lenders. On May 3, 2011, the Government sued DEUTSCHE BANK and its subsidiary, MORTGAGEIT, INC., in connection with \$386 million of FHA insurance claims paid by HUD for defaulted mortgage loans. On November 1, 2011, the Government sued ALLIED HOME MORTGAGE CORPORATION and its CEO in connection with \$834 million of FHA insurance claims paid by HUD. On February 15, 2012, the Government sued and settled with CITIMORTGAGE, INC. ("CITIMORTGAGE"), a subsidiary of CITIBANK, N.A., for engaging in over six years of misconduct in connection with CITIMORTGAGE's participation in the DEL program. In the settlement, CITIMORTGAGE admitted and accepted responsibility for failing to comply with certain DEL program requirements, and agreed to pay \$158.3 million in damages. The Office's Civil Frauds Unit is handling all four cases as part of its continuing investigation of reckless mortgage lending practices.

The Civil Frauds Unit works in coordination with President Barack Obama's Financial Fraud Enforcement Task Force, on which Mr. Bharara serves as a Co-Chair of the Securities and Commodities Fraud Working Group. President Obama established the interagency Financial Fraud Enforcement Task Force to wage an aggressive, coordinated, and proactive effort to investigate and prosecute financial crimes. The task force includes representatives from a broad range of federal agencies, regulatory authorities, inspectors general, and state and local law enforcement who, working together, bring to bear a powerful array of criminal and civil enforcement resources. The task force is working to improve efforts across the federal executive branch, and with state and local partners, to investigate and prosecute significant financial crimes, ensure just and effective punishment for those who perpetrate financial crimes, combat discrimination in the lending and financial markets, and recover proceeds for victims of financial crimes.

Mr. Bharara thanked HUD and HUD-OIG for their extraordinary assistance in this case. He also expressed his appreciation for the support of the Commercial Litigation Branch of the U.S. Department of Justice's Civil Division in Washington, D.C.

Assistant U.S. Attorney Christopher B. Harwood is in charge of the case.