



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

August 21, 2017

MEMORANDUM NO:
2017-AT-1801

Memorandum

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

//signed//

FROM: Nikita N. Irons
Regional Inspector General for Audit, Atlanta Region, 4AGA

SUBJECT: Final Civil Action: Prospect Mortgage, LLC, Settled Alleged
Violations of Federal Housing Administration Loan Requirements

INTRODUCTION

The U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), assisted the U.S. Department of Justice (DOJ) Washington D.C., and the U.S. Attorney's Offices of the Northern District of Georgia and Northern District of California, in the civil investigation of Prospect Mortgage, LLC. Prospect has its principal place of business in Sherman Oaks, CA.

BACKGROUND

The Federal Housing Administration (FHA) is a component of HUD. It provides mortgage insurance for a person to purchase or refinance a principal residence. The mortgage loan is funded by a lending institution, such as a mortgage company or bank, and the mortgage is insured by FHA.

HUD's direct endorsement lender program authorizes private-sector mortgage lenders to approve mortgage loans for FHA insurance. Lenders approved for the program must follow FHA

requirements, including providing annual and per loan certifications that the lender complied with these requirements when underwriting and approving loans for FHA insurance.

Prospect (or its predecessor(s)) has been an FHA-approved direct endorsement lender since at least January 2006. As a direct endorsement lender, Prospect was authorized by HUD to originate and underwrite mortgage loans on HUD's behalf, including determining a borrower's creditworthiness and whether the proposed loan met all applicable HUD requirements, without a preendorsement review of the mortgage application by HUD. When a borrower defaults on an FHA-insured loan underwritten and endorsed by a direct endorsement lender, such as Prospect, the lender (or its representative) has the option of submitting a claim to HUD to compensate the lender for any loss sustained as a result of the default. Therefore, once a mortgage loan is endorsed for FHA insurance, HUD insures the risk of the borrower's defaulting on that mortgage, which is realized if an insurance claim is submitted.

RESULTS OF INVESTIGATION

Based in part on our review, the Federal Government alleged that Prospect violated the False Claims Act when it originated and underwrote FHA mortgage loans that did not meet applicable requirements. The Federal Government also alleged that Prospect did not maintain a quality control program that complied with requirements. As a result of Prospect's conduct, HUD insured certain loans approved by Prospect that were not eligible for FHA insurance under the direct endorsement program and that HUD would not otherwise have insured. HUD incurred substantial losses when it paid insurance claims on certain defaulted loans.

On June 30, 2017, Prospect entered into a settlement agreement with the Federal Government to pay \$4.157 million to avoid the delay, uncertainty, inconvenience, and expense of lengthy litigation of certain civil claims the Government stated it had against Prospect. As part of the settlement, Prospect agreed that it engaged in certain conduct in connection with its origination, underwriting, quality control, and endorsement of single-family residential mortgage loans insured by FHA.¹ The settlement was neither an admission of liability by Prospect nor a concession by the United States that its claims were not well founded.

Of the total settlement of \$4.157 million, HUD FHA was to receive \$2.93 million, and the remaining funds will be paid to other Federal entities.

¹ Loans covered in the settlement agreement included loans insured by FHA between December 2007 and December 2009, which resulted in claims submitted to HUD on or before October 16, 2015, excluding origination or underwriting of home equity conversion mortgages under 12 U.S.C. (United States Code) 1715z-20 and streamline refinances under 12 U.S.C. 1715n(a)(7).

RECOMMENDATION

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

- 1A. Acknowledge that \$2.93 million in the attached settlement agreement represents an amount due HUD, less DOJ's civil debt collection fees.²

As of June 30, 2017, the settlement agreement of \$4.157 million had been reached, and HUD's portion of \$2.93 million plus interest represents an amount due HUD. Under the terms of the repayment agreement, Prospect must pay \$2,078,500 by July 30, 2017. A second installment of \$2,078,500 is due no later than 60 calendar days after initial payment. In accordance with HUD Handbook 2000.6, REV-4, the final action target date will be set at October 28, 2017 (30 days from the date on which final payment is expected). At issuance of this memorandum, HUD OIG will enter a management decision into HUD's Audit Resolution and Corrective Action Tracking System, along with any supporting payment information received to date.

² DOJ's 1994 Appropriation Act (Public Law 103-121) authorized DOJ to retain up to 3 percent of all amounts collected as the result of its civil debt collection litigation activities.