



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

September 2, 2014

**MEMORANDUM NO:**  
2014-CF-1807

## *Memorandum*

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

*//signed//*

FROM: Kimberly Randall  
Director, Joint Civil Fraud Division, GAW

SUBJECT: Final Civil Action: JPMorgan Chase Settled Allegations of Failing To Comply  
With HUD's FHA Loan Requirements

### **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 an investigation of JPMorgan Chase Bank, N.A., and JPMorgan Chase & Co. (Chase). The investigation began due to a *qui tam*<sup>1</sup> filing in the U.S. District Court for the Southern District of New York. The relator alleged that Chase had not followed Federal Housing Administration (FHA) requirements when underwriting loans under the FHA insurance program, and the insurance fund incurred significant losses when the borrowers defaulted on the loans.

### **BACKGROUND**

The FHA program is a component of HUD. The program 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.

Chase has participated in the FHA program since 1964 and became a direct endorsement lender in 1983. The direct endorsement lender program authorizes private-sector mortgage lenders to

---

<sup>1</sup> The False Claims Act allows private persons to file suit for violations of the False Claims Act on behalf of the Government. A suit filed by an individual on behalf of the Government is known as a *qui tam* action, and the person bringing the action is referred to as a "relator."

approve mortgage loans for insurance by FHA. Lenders approved for the program must follow FHA requirements and provide annual and per loan certifications that the lender complied with these requirements when underwriting and approving loans for FHA insurance.

## **RESULTS OF INVESTIGATION**

On February 4, 2014, the U.S. Attorney's Office of the Southern District of New York filed suit against Chase for not complying with FHA requirements based, in part, on our review of the underwriting and refinancing of FHA loans.<sup>2</sup> The U.S. Attorney's Office sought damages and civil penalties under the False Claims Act and common law. The lawsuit alleged that during the period January 1, 2002, through February 4, 2014, Chase routinely approved loans for FHA insurance and refinancing that did not meet applicable underwriting requirements and were, therefore, ineligible for insurance. However, FHA had insured the loans based on per loan certifications submitted by Chase that it had complied with FHA requirements when underwriting the loans. When the borrowers defaulted on the loans, FHA incurred substantial losses.

On February 4, 2014, Chase entered into a settlement agreement to pay \$614 million to end the lawsuit, which the U.S. District Judge for the Southern District of New York approved. Of the settlement total, \$564.6 million was attributable to FHA's direct endorsement lender program. The FHA insurance fund was to receive \$336 million of the \$564.6 million, before incurring related costs; and the remaining \$228.6 million was to be remitted to other Federal entities and the relator.<sup>3</sup>

As part of the settlement, Chase admitted, acknowledged, and accepted responsibility for certain conduct, including that

- It failed to report to HUD nearly 600 loans that it identified in a 3-year period that had been affected by borrower or correspondent (broker) fraud or other material deficiencies.
- It approved for FHA insurance or refinancing thousands of loans that did not meet one or more rules of the direct endorsement lender program and, therefore, were not eligible for FHA insurance or refinancing.
- Certain Chase employees submitted data to HUD's Technology Open To Approved Lenders (TOTAL) Mortgage Scorecard<sup>4</sup> that lacked integrity. Specifically, when loans

---

<sup>2</sup> The U.S. Attorney's Office for the Southern District of New York filed the lawsuit on behalf of HUD, FHA, the U.S. Department of Veterans Affairs, and the relator in connection with Chase's residential mortgage lending business. This memorandum addresses only the results directly related to HUD's FHA program.

<sup>3</sup> The Department of Justice (DOJ) will remit to the FHA insurance fund that portion of a False Claims Act recovery that equals single damages ( i.e., FHA's actual damages), to compensate FHA for its losses. DOJ will retain up to 3 percent of the total amount recovered pursuant to 28 U.S.C. §527. The FHA fund retains single damages less the DOJ retained portion. DOJ remits the balance of the damages into the general fund of the U.S. Treasury as miscellaneous receipts. If the lawsuit is a *qui tam*, the Court may award the relator a share of the False Claim Act award, based on the contributions the relator made to the investigation.

<sup>4</sup> HUD's TOTAL Mortgage Scorecard interacts with proprietary automated underwriting systems (AUS) to assess the credit worthiness of FHA borrowers by evaluating certain mortgage application and mortgage credit information. TOTAL is not an AUS; rather, it is a mathematical equation intended for use within an AUS.

did not receive an *accept-approve* rating from TOTAL, these employees resubmitted the loans through TOTAL multiple times over a short period, each time entering hypothetical data that had not been appropriately corroborated to determine that data would generate an *accept-approve* rating. These employees communicated the qualifying data to borrowers, thus increasing the risk of borrower fraud.

- It submitted loan-level certifications to HUD for each FHA loan it approved for insurance and thus certified to HUD that the loan was eligible for FHA insurance or refinancing under the direct endorsement lender program. It also certified to the integrity of the data supplied to its AUS and TOTAL in obtaining loan approval and applying for FHA insurance.
- It induced HUD to accept for FHA insurance or refinancing thousands of loans that were not eligible for the FHA program and that HUD otherwise would not have accepted for insurance or refinancing. This resulted in substantial losses to the Government when the borrowers defaulted on the loans.

Additionally, Chase agreed to comply with all rules of the direct endorsement lender program and implement an enhanced quality control program to review FHA loans that it underwrites using TOTAL.

### **RECOMMENDATION**

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

- 1A. Allow HUD OIG to post the \$336 million recovery to HUD's Audit Resolution and Corrective Actions Tracking System as ineligible costs.

HUD's Office of General Counsel, Office Program Enforcement has agreed to the recommendation. No further action is required.