



**UNITED STATES ATTORNEY'S OFFICE**  
*Southern District of New York*

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**MANHATTAN U.S. ATTORNEY SUES ALLIED HOME MORTGAGE,  
CEO, AND EXECUTIVE VICE PRESIDENT FOR FRAUDULENT  
LENDING PRACTICES CURRENTLY ASSOCIATED WITH \$834  
MILLION IN INSURANCE CLAIMS PAID BY HUD**

*One of the Nation's Top Privately Held Mortgage Lenders Operated 'Shadow Branches' and  
Allegedly Lied About Its Compliance With HUD Regulations*

PREET BHARARA, the United States Attorney for the Southern District of New York; TONY WEST, the Assistant Attorney General for the Civil Division of the U.S. Department of Justice; HELEN KANOVSKY, General Counsel of the U.S. Department of Housing and Urban Development ("HUD"); and JOHN P. MCCARTY, Acting Deputy Inspector General of HUD, announced today that the United States has filed a civil mortgage fraud lawsuit against ALLIED HOME MORTGAGE CAPITAL CORPORATION, its affiliate, ALLIED HOME MORTGAGE CORPORATION (collectively ("ALLIED")), as well as ALLIED President and CEO JIM C. HODGE and Executive Vice President JEANNE L. STELL. The Government's Complaint seeks damages and civil penalties under the False Claims Act and the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") for nearly a decade of concealed misconduct in connection with the residential mortgage lending practices of ALLIED, which bills itself as one of the nation's largest privately held mortgage lenders. In the past decade, ALLIED originated more than 110,000 FHA mortgages, more than 30% of which are in default. For loans originated in 2006 and 2007, ALLIED's default rate climbed to 55%. To date, the Federal Housing Administration ("FHA") has paid insurance claims totaling \$834 million for mortgages originated and fraudulently certified by ALLIED that are now in default. An additional 2,509 loans are currently in default but not yet in claims status, which could result in additional insurance claims paid by HUD amounting to \$363 million.

Manhattan U.S. Attorney PREET BHARARA stated: "As described in the Complaint, Allied and its CEO exploited a government insurance program to engage in a wholesale shifting

of risk away from itself – playing a lending industry equivalent of heads-I-win and tails-you-lose. The losers here were American taxpayers and the thousands of families who faced foreclosure because they could not ultimately fulfill their obligations on mortgages that were doomed to fail. The alleged conduct in this case is egregious and our investigation is ongoing."

Assistant Attorney General TONY WEST stated: "During the past decade, these defendants allegedly engaged in conduct that caused substantial losses to the FHA program. The filing of this lawsuit is the Government's first step to hold them accountable to the taxpayers for the damage their conduct has caused. "

HUD General Counsel HELEN KANOVSKY stated: "We will not tolerate mortgage lenders who play fast and loose with FHA's standards. These defendants demonstrated a pattern of recklessness and utter disregard for how we do business. They've harmed FHA, hurt homeowners, and now they'll be held to account for their actions."

HUD Acting Deputy Inspector General JOHN P. MCCARTY stated: "The allegations contained in this filing highlight the lengths to which corrupt lenders will go to put profits before prudence, while violating the trust placed in them by the U.S. Department of Housing and Urban Development, the Federal Housing Administration, and ultimately American taxpayers. Lenders who engage in deceitful practices and circumvent the basic "check and balance" approval system pose a significant threat to our already troubled mortgage industry. The HUD Office of Inspector General considers the integrity of the FHA process and the protection of FHA assets to be a priority of our investigative mission. Today's filing underscores our unwavering commitment to working with the US Attorney's Office and our law enforcement partners to bring the full weight of our legal system to bear in holding unscrupulous lenders responsible for their actions. "

According to the Complaint filed today in Manhattan Federal court:

FHA mortgage insurance makes home ownership possible for millions of American families by protecting lenders against defaults on mortgages, thereby encouraging lenders to make loans to borrowers who might not be able to meet conventional underwriting requirements. FHA mortgage insurance also makes mortgage loans valuable in the resale market. To protect the continued availability of FHA mortgage insurance funds, HUD must accurately assess the risk of default on the loans it insures. To accomplish this task, HUD relies on assurances by lenders that they, and the loans they submit for insurance, comply with HUD requirements.

As a HUD-approved loan correspondent and Direct Endorsement Lender, ALLIED originated HUD-insured mortgage loans for sale or transfer to other qualifying mortgagees, known as "sponsor mortgagees." ALLIED was required to seek HUD approval for each office from which it originated FHA loans. ALLIED was also required to certify that it maintained a quality control program that reviewed loans that went into early payment default, and that it faced no sanctions in the states in which it operated. Although ALLIED certified to HUD that it complied with these key requirements, its certifications were knowingly false.

According to the Complaint, ALLIED operated hundreds of "shadow," unapproved branch offices that originated FHA loans. To deceive HUD about this practice, ALLIED submitted loans from those branches to HUD substituting the ID number of a HUD-approved branch. ALLIED's undisclosed shadow branches could not be audited by HUD and their default

rates were disguised by the default rates of branches whose IDs they were using – IDs that were based on false certifications. While some senior managers questioned this practice, it was continued under the direction of HODGE.

As further alleged in the Complaint, when ALLIED sought approval from HUD for new branches – at one time they had 600 branches with HUD IDs – it was based on fraudulent information. ALLIED falsely certified that it complied with HUD requirements and maintained financial and supervisory control over the branch. In reality, ALLIED's branch offices were not subject to ALLIED's oversight, and ALLIED bore little risk of loss for poor lending practices by the branches. Well aware that ALLIED's branch operations violated HUD requirements, and that both she and HODGE had legal exposure, ALLIED's Executive Vice President routinely had another senior manager sign the certifications to HUD because she knew they were false.

For example, in an email exchange between STELL and a former employee about a 2009 HUD audit report finding that ALLIED was not in compliance with HUD rules relating to branch operations, STELL wrote, "I had [another senior manager] sign the 'add a branch' form for years for HUD as I knew this would eventually happen. It required that you swear the branches meet and will continue to meet HUD's regulations. Jim [Hodge] has to be the biggest target personally for his disregard for the regulations. Serves him right never listening and thinking he didn't have to play by the rules."

Even while it operated more than 600 branches, ALLIED's quality control program was either dysfunctional or entirely nonexistent. The corporation maintained only a handful of quality control employees to review its thousands of mortgages, most of whom were located in St. Croix, in the U.S. Virgin Islands, and employed by a company that HODGE set up to obtain tax benefits. According to the Complaint, when the quality control manager visited her staff in St. Croix, she discovered that they did not know what HUD was or even what a mortgage was.

HODGE's offshore entity earned millions of dollars in management fees from ALLIED, but conducted little substantive loan review. When HUD auditors asked for up-to-date quality control reports and ALLIED could not provide them, it provided fraudulent reports at HODGE's direction. Finally, in the annual certifications ALLIED submitted to HUD to maintain its HUD-approved status, ALLIED falsely certified that none of its employees had been convicted of a crime and that it had a clean record in the states in which it operated. In fact, ALLIED faced serious sanctions from numerous states and employed numerous convicted felons, having hired more than a dozen in a single year.

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The Complaint seeks treble damages and penalties under the False Claims Act for the hundreds of millions of dollars in insurance claims already paid by HUD for mortgages originated by ALLIED, as well as compensatory damages under common law for the hundreds of millions of dollars in insurance claims that HUD expects to pay in the future. In addition, the United States seeks damages and civil penalties under FIRREA for the hundreds of false statements that ALLIED submitted to HUD. Under FIRREA, the United States may recover up to \$1 million per violation, or (if greater) the amount of the pecuniary gain from the violation or the amount of the pecuniary loss to a person other than the violator.

By filing its Complaint, the Government also joined and expanded upon a *qui tam* private whistleblower lawsuit that had been filed against ALLIED HOME MORTGAGE CAPITAL CORPORATION under the False Claims Act in May of this year.

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 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 thanked the New York State Department of Financial Services. Mr. BHARARA 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 JAIMIE L. NAWADAY is in charge of the case.