

## ATTACHMENT A

1. Since at least January 2006, Branch Banking and Trust (“BB&T”) has been a Direct Endorsement (“DE”) lender approved by the Federal Housing Administration (“FHA”) and U.S. Department of Housing and Urban Development (“HUD”). As a DE lender with Lender Insurance status, BB&T is 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 any pre-endorsement review of the mortgage application by HUD.

2. HUD required DE lenders, such as BB&T, to follow applicable HUD regulations and underwriting requirements in originating and underwriting mortgage loans for FHA insurance, including those requirements set out in HUD’s Handbooks and Mortgagee Letters.<sup>1</sup>

3. HUD required DE lenders, such as BB&T, to submit certain proposed FHA loan originations through a HUD-approved Automated Underwriting System (“AUS”) in conjunction with a tool known as Technology Open to Approved Lenders (“TOTAL”). According to the FHA’s TOTAL Mortgage Scorecard User Guide, TOTAL evaluated the overall creditworthiness of the applicants based on a number of credit variables. After a proposed loan was submitted, TOTAL would either: (1) approve the mortgage subject to certain eligibility criteria or other conditions, including conditions that the lender validate the information that formed the basis for TOTAL’s determination; or (2) refer the mortgage application for manual underwriting by the lender in accordance

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<sup>1</sup> The requirements referenced in paragraphs two through twelve of this document reflect standard HUD-FHA program requirements for Direct Endorsement lenders as provided in HUD’s Handbooks and Mortgagee Letters.

with HUD requirements. BB&T understood that TOTAL's determination was based upon the data submitted as well as the integrity of the data supplied by the lender. HUD has promulgated requirements for calculating data used by TOTAL.

4. HUD required DE lenders, such as BB&T, to implement and maintain a quality control program in accordance with HUD Handbook requirements for FHA loans in order to maintain DE lender status. HUD required the FHA quality control function to be independent of FHA mortgage origination and underwriting functions. HUD required DE lenders such as BB&T that originated and/or underwrote more than 3,500 loans in a year to review a sample of loans based on the number of FHA loans originated and/or underwritten per year. HUD Handbook 4060.1 REV-2, § 7-6.C. DE Lenders, such as BB&T, were also required to review each FHA mortgage loan that became 60 days delinquent within the first six payments, which HUD defined as "early payment defaults" or EPDs. *Id.* HUD required DE lenders, such as BB&T, in performing these quality control reviews, to review the mortgage loan file, re-verify certain information, review the soundness of underwriting judgments, document the review and any findings in a quality control report, and report the findings to senior management within one month.

5. HUD required DE lenders, such as BB&T, to self-report to HUD all findings related to FHA mortgage loans that constituted "material violations of FHA or mortgagee requirements and represent[ed] an unacceptable level of risk" and all findings of "fraud or other serious violations." HUD Handbook 4060.1 REV-2, §§ 7-3.J & 7-4.D. DE lenders, such as BB&T, were also required to take "prompt action to deal appropriately with any material findings." *Id.* § 7-3.I.

6. In order to obtain DE status, HUD required DE lenders, such as BB&T, to certify as follows:

I certify that, upon the submission of this application, and with its submission of each loan for insurance or request for insurance benefits, [BB&T] has and will comply with the requirements of the Secretary of Housing and Urban Development, which include, but are not limited to, the National Housing Act (12 U.S.C. § 1702 *et seq.*) and HUD's regulations, FHA handbooks, mortgagee letters, and Title I letters and policies with regard to using and maintaining its FHA lender approval.

7. Additionally, HUD required a DE lender, such as BB&T, to submit an Annual Certification stating:

I know, or am in a position to know, whether the operations of [BB&T] conform to HUD-FHA regulations, handbooks, and policies. I certify that to the best of my knowledge, [BB&T] conforms to all HUD-FHA regulations necessary to maintain its HUD-FHA approval, and that [BB&T] is fully responsible for all actions of its employees including those of its HUD-FHA approved branch offices.

Alternatively, HUD required a DE lender, such as BB&T, to submit a statement to HUD that it was unable to so certify and to explain why it could not execute the certification.

8. To qualify as a DE underwriter an underwriter must satisfy several requirements. The DE underwriter “must have a minimum of three years full-time recent experience (or equivalent experience) reviewing both credit applications and property appraisals.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.A.3; *see also* HUD Handbook 4155.2 ch. 2.A.4.a. The underwriter must also be a “reliable and responsible professional skilled in mortgage evaluation” and “must be able to demonstrate his or her knowledge and experience regarding the principles of mortgage underwriting.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.A.1; *see also* HUD Handbook 4155.2 ch. 2.A.4.a.

9. HUD has considered the DE underwriter to be “the focal point of the Direct Endorsement program.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.C. The DE underwriter must assume the following responsibilities: (1) compliance with HUD instructions, the coordination of all phases of underwriting, and the quality of decisions made under the program; (2) the review of appraisal reports, compliance inspections and credit analyses performed by fee and staff personnel to ensure reasonable conclusions, sound reports and compliance with HUD requirements; (3) the decisions relating to the acceptability of the appraisal, the inspections, the buyer’s capacity to repay the mortgage, and the overall acceptability of the mortgage loan for HUD insurance; (4) the monitoring and evaluating of the performance of fee and staff personnel used for the DE program; and (5) ; awareness of the warning signs that may indicate irregularities, and an ability to detect fraud, as well as the responsibility that underwriting decisions are performed with due diligence in a prudent manner.

10. With respect to each mortgage loan submitted or endorsed by BB&T for FHA insurance, either a BB&T mortgagee representative or a BB&T DE underwriter was required to certify that the mortgage “is eligible for HUD mortgage insurance under the Direct Endorsement program.” For each loan that was approved using AUS, a BB&T mortgagee representative was required to certify to the “integrity of the data supplied by [BB&T] used to determine the quality of the loan [and] that a Direct Endorsement Underwriter reviewed the appraisal.” For each FHA loan that BB&T approved using manual underwriting, a BB&T DE underwriter was required to certify that he or she “personally reviewed the appraisal report (if applicable), credit application, and all associated documents and ha[s] used due diligence in underwriting the[e] mortgage.”

11. For every mortgage loan approved by BB&T, whether through manual underwriting or the use of an AUS, a BB&T employee was required to certify that:

I, the undersigned, as authorized representative of BB&T at this time of closing of this mortgage loan, certify that I have personally reviewed the mortgage loan documents, closing statements, application for insurance endorsement, and all accompanying documents. I hereby make all certifications required for this mortgage as set forth in HUD Handbook 4000.4.

12. When a borrower defaults on an FHA-insured loan underwritten and endorsed by a DE lender, such as BB&T, the lender, or if the mortgage or servicing rights were transferred after closing, the mortgage holder or servicer, has the option of submitting a claim to HUD to obtain compensation for any loss sustained as a result of the default. As such, once a mortgage loan has been endorsed for FHA insurance, HUD insures the risk of the borrower defaulting on that mortgage, which is realized if an insurance claim is submitted.

13. The Department of Justice has investigated BB&T with regard to its origination, underwriting, quality control, and endorsement practices, as well as its submissions of certifications, related to certain FHA-insured single-family residential mortgage loans originated between January 1, 2006 and September 30, 2014 that resulted in claims submitted to FHA on or before February 15, 2016 (the "Released Loans"). The following statements apply to the Released Loans only.

14. BB&T certified for FHA mortgage insurance, pursuant to the DE Program, certain Released Loans that did not meet all HUD requirements, and therefore were not eligible for FHA mortgage insurance under the DE Program. Certain Released Loans that BB&T certified for FHA mortgage insurance, but were in fact ineligible for FHA mortgage insurance, defaulted and were submitted to HUD for mortgage insurance

benefits, and claims were paid out of the Mutual Mortgage Insurance Fund. The following are examples of loans that BB&T submitted for FHA insurance which did not meet all HUD requirements, and resulted in claims for FHA insurance being paid:

a) FHA Case Number 381-7982115 relates to a mortgage BB&T endorsed for FHA mortgage insurance in 2006. BB&T underwrote the mortgage for this property using an AUS, and certified that the loan was eligible for FHA mortgage insurance and the data BB&T supplied to the AUS had integrity. This loan was not eligible for FHA insurance as the borrower did not meet HUD's statutory minimum investment requirement. BB&T's Quality Control Department reviewed this loan and rated it 'Serious-Marketability', the highest deficiency rating used by BB&T and an indication that the loan was not eligible for FHA insurance. HUD relied on BB&T's certification that FHA Case Number 381-7982115 was eligible for FHA insurance when HUD insured the mortgage, and would not have insured the mortgage if HUD was aware of BB&T's failure to satisfy HUD requirements and the loan's ineligibility for FHA mortgage insurance.

b) FHA Case Number 381-8069044 relates to a mortgage BB&T endorsed for FHA mortgage insurance in 2007. BB&T underwrote the mortgage for this property using an AUS, and certified that the loan was eligible for FHA mortgage insurance and the data BB&T supplied to the AUS had integrity. This loan was not eligible for FHA insurance as the data BB&T supplied to the AUS did not have integrity. Specifically, the

loan file does not contain all required documentation to verify the borrower's purported assets (a gift) used to close the loan. As a result, BB&T could not verify the asset information that it entered into the AUS. HUD relied on BB&T's certification that FHA Case Number 382-8069044 was eligible for FHA insurance when HUD insured the mortgage, and would not have insured the mortgage if HUD was aware of BB&T's failure to satisfy all HUD requirements and the loan's ineligibility for FHA mortgage insurance.

c) FHA Case Number 381-8681165 relates to a mortgage BB&T endorsed for FHA mortgage insurance in 2008. BB&T manually underwrote the mortgage for this property, and certified that the loan was eligible for FHA mortgage insurance and that BB&T had used due diligence in underwriting the mortgage. This loan was not eligible for FHA mortgage insurance and was not underwritten with due diligence as BB&T did not confirm whether the borrower had the funds necessary to close the loan or the borrower's housing payment history, and approved the loan with a debt-to-income ratio of 78 percent —above HUD's maximum of 43 percent—without adequate compensating factors. BB&T certified that the loan was eligible for FHA insurance. HUD relied on BB&T's certification that FHA Case Number 381-8681165 was eligible for FHA insurance when HUD insured the mortgage, and would not have insured the mortgage if HUD was aware of BB&T's failure to fulfill HUD requirements and the loan's ineligibility for FHA mortgage insurance.

d) FHA Case Number 241-8777588 relates to a mortgage BB&T endorsed for FHA mortgage insurance in 2009. BB&T underwrote the mortgage for this property using an AUS, and certified that the loan was eligible for FHA mortgage insurance and the data BB&T supplied to the AUS had integrity. This loan was not eligible for FHA mortgage insurance as the data BB&T supplied to the AUS did not have integrity because the loan file does not contain documentation—paystubs, W-2s, and payoff statements—required by the AUS and HUD. As a result, BB&T could not verify the income information that it entered into the AUS. HUD relied on BB&T’s certification that FHA Case Number 241-8777588 was eligible for FHA insurance when HUD insured the mortgage, and would not have insured the mortgage if HUD was aware of BB&T’s failure to fulfill all HUD requirements and the loan’s ineligibility for FHA mortgage insurance.

e) FHA Case Number 541-9018084 relates to a mortgage BB&T endorsed for FHA mortgage insurance in 2010. BB&T underwrote the mortgage for this property using an AUS, and certified that the loan was eligible for FHA mortgage insurance and the data BB&T supplied to the AUS had integrity. This loan was not eligible for FHA mortgage insurance as the data BB&T supplied to the AUS did not have integrity because the loan file does not contain documentation to verify the borrower’s assets—particularly the amount of assets the borrower would have in reserve after the loan closed—used to obtain approval from the AUS. As a result,



BB&T could not verify the asset information that it entered into the AUS. HUD relied on BB&T's certification that FHA Case Number 541-9018084 was eligible for FHA insurance when HUD insured the mortgage, and would not have insured the mortgage if HUD was aware of BB&T's failure to satisfy all HUD requirements and the loan's ineligibility for FHA mortgage insurance.

f) BB&T endorsed for FHA insurance numerous other loans that were not eligible for FHA insurance, and submitted claims for mortgage insurance on these loans when borrowers defaulted on their mortgages. HUD relied on BB&T's certifications that these loans were eligible for FHA insurance when HUD insured the mortgages, and would not have insured the mortgages if HUD was aware of BB&T's failure to satisfy all HUD requirements and the loans' ineligibility for FHA mortgage insurance.

15. The monthly QC reviews and reports that BB&T's QC department shared with management alerted BB&T to deficiencies in many of its FHA loans. One of the most severe ratings BB&T assigned to loans was a rating of Serious-Marketability,<sup>2</sup> which BB&T defined as: "exceptions to BB&T's policies and investor requirements that significantly affect a loan's marketability. These exceptions could render a loan unmarketable, necessitate repurchase or jeopardize the loan collateral." BB&T's QC Manager understood that if a loan's Serious-Marketability rating was valid, that loan would not be eligible for FHA mortgage insurance. Between 2007 and 2011, the percentage of loans underwritten in each year rated Serious-Marketability by BB&T's

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<sup>2</sup> BB&T also rated loans Serious-Regulatory and Serious-Combination.

QC Department always exceeded 30 percent, and exceeded as much as 50 percent in 2010 and 2011. In October 2010, 68 percent of BB&T's loans were rated either Serious-Marketability, Serious-Regulatory, or Serious-Combination, while in January 2011, 89 percent of BB&T's loans were rated either Serious-Marketability, Serious Regulatory, or Serious-Combination. BB&T nevertheless endorsed many of these loans for FHA insurance and, if they defaulted, sought payment from HUD for the insured loans. During this time period, BB&T's QC review did not include a rebuttal process, which would have given BB&T's production staff an opportunity to research and potentially cure observed defects, thereby potentially reducing the defect rate. In addition, during this time BB&T did not compile or report a defect rate specific to FHA loans.

16. The increase in the percentage of loans with a rating of Serious-Marketability corresponded to an increase in loan volume at BB&T. Loan volume at BB&T more than doubled from 2006 to 2009, while the percentage of loans with a rating of Serious-Marketability doubled as well, increasing from 23 percent in 2006 to 54 percent in 2010. An internal BB&T memorandum from 2009 recognized the effect that the significant increase in volume was having on the underwriters—while underwriters were expected to underwrite between 100-125 loan files a month per BB&T's Standard Metric expectations for underwriters, in 2009, BB&T underwriters underwrote up to 205 loan files a month. Consistent with overall industry trends, BB&T saw an even greater increase in FHA loan volume, as the number of loans endorsed for FHA mortgage insurance increased six fold between 2006 and 2009. An internal BB&T memorandum from 2010 stated that “increased volume of FHA requests and changes to regulatory requirements have resulted in origination, processing and underwriting errors. Some

employees are not applying current and accurate FHA guidelines.” The accompanying proposal to improve BB&T’s underwriting of FHA loans with additional training as well as a testing and certification process for underwriters was not implemented until after 2014.

17. Between 2006 and 2014, BB&T’s QC process did not satisfy certain FHA QC requirements. BB&T’s QC Director expressed his, admittedly biased, opinion that quality control was not a priority at BB&T. Because loan volume more than doubled from 2006 to 2009, yet the number of QC employees remained the same, the QC Department was unable to perform the necessary amount of quality control. The QC Department requested an additional 3.5 employees to allow it to meet investor requirements in 2009; yet new employees were not added until 2013. Because BB&T’s QC Department did not have adequate staff, it instituted a cap on the number of loans it reviewed due to staffing capacity. The result was that, between 2009 and 2014, the QC Department did not always review the number of loans necessary to comply with HUD’s sampling requirements. Additionally, BB&T reduced its QC Department’s travel budget and did not perform reviews of its lender branch offices, as required by HUD at the time, before beginning the reviews again in late 2014.

18. The EPD QC that BB&T did perform did not satisfy all HUD requirements for several reasons. First, prior to 2014, BB&T did not ensure that production (origination and underwriting) employees reviewed the EPD loan audits, nor did BB&T require production employees to respond to loan defect findings. Second, prior to 2014, BB&T did not assign any quality ratings to the EPD loans that it reviewed. Third, the origination and underwriting reviews of EPD loans were performed by

employees of the loan servicing QC Department who were not experienced with underwriting loans. In early 2011, the QC Department requested additional staffing for Production Quality Control so that “early payment defaults are reviewed by more knowledgeable credit risk personnel.” Not until late 2012 was the QC Department granted the additional staffing it requested and EPD reviews were transitioned to Production Quality Control.

19. BB&T’s QC Plan required it to self-report in writing to investors—including HUD—the “discovery of any discrepancies, or findings, including but not limited to confirmed fraud, that could significantly affect the investment quality of their loan.” Since at least 2006, HUD has required self-reporting. However, despite BB&T’s QC Department’s ratings showing that 30 percent or more of BB&T’s loans underwritten between 2007 and 2011 had Serious-Marketability findings, and were thus ineligible for FHA insurance, BB&T did not self-report any materially deficient loans resulting from underwriting errors until 2013. BB&T began to routinely self-report deficient loans to HUD in 2014 when it made key changes to its mortgage lending practices.

20. As a result of BB&T’s conduct and omissions, HUD insured hundreds of loans approved by BB&T that were not eligible for FHA mortgage insurance under the Direct Endorsement Program, and that HUD would not otherwise have insured. HUD subsequently incurred substantial losses when it paid insurance claims on those Released Loans.

21. The statements herein apply only to certain mortgages which are the subject of the release in this Agreement. This document is not an admission as to any conduct related to any mortgage not released in this Agreement, nor is it an admission of

any legal liability. BB&T reserves the right to contest the use or application of this document in any future litigation.