
THE UNITED STATES ATTORNEY'S OFFICE
SOUTHERN DISTRICT *of* NEW YORK

PRESS RELEASES

Manhattan U.S. Attorney Files Mortgage Fraud Lawsuit Against Wells Fargo Bank, N.A. Seeking Hundreds Of Millions Of Dollars In Damages For Fraudulently Certified Loans

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***Suit Alleges Longstanding Practice of Reckless Underwriting and
Fraudulent Loan Certification for Thousands of FHA-Insured Loans That
Ultimately Defaulted***

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, Inspector General of HUD, announced today that the United States has filed a civil mortgage fraud lawsuit against WELLS FARGO BANK, N.A. (“WELLS FARGO”). 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 more than 10 years of misconduct in connection with WELLS FARGO’s participation in the Federal Housing Administration (“FHA”) Direct Endorsement Lender Program. The lawsuit alleges that, as a result of

WELLS FARGO's false certifications, FHA has paid hundreds of millions of dollars in insurance claims on thousands of mortgages that defaulted.

Manhattan U.S. Attorney Preet Bharara said: "As the complaint alleges, yet another major bank has engaged in a longstanding and reckless trifecta of deficient training, deficient underwriting and deficient disclosure, all while relying on the convenient backstop of government insurance. As also alleged, Wells Fargo's bonus incentive plan – rewarding employees based on the sheer number of loans approved – was an accelerant to a fire already burning, as quality repeatedly took a back seat to quantity. What's more, even after concerns were raised internally at the bank, Wells Fargo began self-reporting bad loans in a significant way, as required, only after this Office issued a subpoena last year. Now a jury will have to weigh the facts to determine the bank's liability and the scope of the damages it must pay."

HUD General Counsel Helen Kanovsky said: "Wells Fargo has been a valued participant in the FHA-mortgage lending program. Unfortunately, as alleged in the government's complaint, there was a time when Wells Fargo placed profits over people, corporate results over corporate integrity, and did not consider the effect its actions would have on the FHA program as well as the overall economy. Today's complaint and others like it are necessary, not only to deter future improper acts, but to recover damages on behalf of the FHA mortgage fund and the American taxpayer."

HUD Inspector General David A. Montoya said: "As long as these companies fail to exercise ethical corporate responsibility to their customers and their obligations as participants in the Direct Endorsement Lender program administered by FHA, we will endeavor to investigate and hold them accountable. I commend the alliance of efforts between my office and the Departments of Housing and Urban Development and Justice, and especially U.S. Attorney Preet Bharara."

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

WELLS FARGO, the largest originator of home mortgages in the United States, has been a participant in the Direct Endorsement Lender program – a federal program administered by FHA – since 1986. As a Direct Endorsement Lender (“DEL”), WELLS FARGO has the authority to originate, underwrite, and certify mortgages for FHA insurance. If a DEL 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, which HUD must then pay. Under the DEL program, neither the FHA nor HUD reviews a loan before it is endorsed for FHA insurance. DELs are therefore required to follow program rules designed to ensure that they are properly underwriting and certifying mortgages for FHA insurance, and maintaining a quality control program that can prevent and correct any deficiencies in their underwriting. The quality control program requirements include conducting a full review of all loans that go into default within the first six payments (“early payment defaults”); taking prompt and adequate corrective action upon discovery of fraud or serious underwriting problems; and disclosing to HUD, within 60 days of initial discovery, all loans containing evidence of fraud or other serious underwriting problems. WELLS FARGO failed to comply with all three of these basic requirements.

First, between May 2001 and October 2005, WELLS FARGO engaged in a regular practice of reckless origination and underwriting of its retail FHA loans. Nonetheless, WELLS FARGO certified that over 100,000 retail FHA loans met HUD’s requirements and therefore were eligible for FHA insurance. During this period, although WELLS FARGO certified to HUD that its retail FHA loans met HUD’s requirements for proper origination and underwriting, and were therefore eligible for FHA insurance, the bank knew that a very substantial percentage of those loans – nearly half in certain months – had not been properly underwritten, contained unacceptable risk, did not meet HUD’s requirements, and were ineligible for FHA insurance. In fact, WELLS FARGO knew that its underwriters routinely failed to perform basic due diligence, failed to verify information in the loan file that bore directly on the borrower’s ability to make payments on the mortgage, and repeatedly certified mortgage loans that contained serious defects and departures from HUD’s underwriting standards. The extremely poor quality of

WELLS FARGO's loans was a function of management's nearly singular focus on increasing the volume of FHA originations – and the bank's profits – rather than on the quality of the loans being originated.

WELLS FARGO aggravated its widespread underwriting violations by: hiring temporary staff to churn out and approve an ever-increasing quantity of FHA loans; failing to provide its inexperienced staff with proper training; paying improper bonuses to its underwriters to incentivize them to approve as many FHA loans as possible; and applying pressure on loan officers and underwriters to originate and approve more and more FHA loans as quickly as possible. In addition, WELLS FARGO senior management repeatedly ignored its own Quality Assurance department's efforts to have management correct the practices leading to the material violations it found in a significant portion of WELLS FARGO's retail home loans, and failed to report loans to HUD that it knew were rife with serious violations or fraud. By certifying tens of thousands of ineligible mortgages and falsely certifying its compliance with HUD rules, WELLS FARGO wrongfully obtained endorsement of these seriously deficient mortgages for FHA insurance, thereby putting billions of FHA dollars at risk. As a result, HUD has paid hundreds of millions of dollars in FHA benefits on claims for defaulted loans that WELLS FARGO never should have certified for FHA insurance in the first place.

Second, WELLS FARGO failed to conduct adequate quality control and comply with its self-reporting requirements to HUD. In particular, WELLS FARGO failed to report to HUD even a single loan with material underwriting violations or fraud until after a HUD lender review in 2005. When HUD inquired about WELLS FARGO's self-reporting practices in 2005, WELLS FARGO attempted to cover up its misdeeds by falsely suggesting to HUD that the bank actually had been reporting bad loans. And, in a continued effort to avoid indemnification claims from HUD on these bad loans, WELLS FARGO's self-reporting even after HUD's inquiry was woefully and purposefully inadequate. From October 2005 through the time of the subpoena from the U.S. Attorney's Office for the Southern District of New York in this investigation, in June 2011, WELLS FARGO reported only about 300 of its seriously deficient loans to HUD.

WELLS FARGO's self-reporting of its loans stands in stark contrast to WELLS FARGO'S findings from its own internal reviews of the quality of its loans. From January 1, 2002 through December 31, 2010, WELLS FARGO internally identified 6,558 seriously deficient loans that it was required to self-report, including 3,142 that had been identified as early payment defaults, or loans which were 60 days into default within the first six months. However, instead of reporting as required, WELLS FARGO concealed 6,320 of these improperly certified loans. WELLS FARGO also failed to conduct reviews of all early payment defaults, as required, and failed to report loans that had been referred to its fraud risk management department ("FRM"), including those loans for which FRM conducted a "deep dive" review – reviews which, according to a former WELLS FARGO FRM manager, exposed a "dirty underbelly of bad loan officers."

As a result of WELLS FARGO's intentional concealment of the 6,320 loans internally identified as containing material violations, WELLS FARGO avoided indemnification to HUD on approximately \$190 million dollars in FHA benefits paid on claims for defaults on those loans. WELLS FARGO additionally avoided indemnification on millions more for the early payment defaults it improperly failed to review and report, and the FRM-identified fraudulent loans it failed to report.

The Complaint seeks treble damages and penalties under the False Claims Act, 31 U.S.C. §§ 3729 et seq., as well as FIRREA penalties, for hundreds of millions of dollars in insurance claims already paid by HUD for mortgages wrongfully certified by WELLS FARGO. In addition, the United States seeks compensatory damages under the common law theories of breach of fiduciary duty, gross negligence, negligence, unjust enrichment, and payment under mistake of fact, for the hundreds of millions of dollars in insurance claims that HUD has paid, and expects to pay in the future, for mortgages wrongfully certified by WELLS FARGO.

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.

To date, the Office's Civil Frauds Unit has brought five civil fraud lawsuits against major lenders under the False Claims Act alleging reckless residential mortgage lending. Three of the five cases have settled. On February 15, 2012, the Government settled its civil fraud lawsuit against CitiMortgage, Inc. for \$158.3 million. On February 24, 2012, the Government settled its civil fraud suit against Flagstar Bank, F.S.B. for \$132.8 million. On May 10, 2012, the Government settled its civil fraud suit against Deutsche Bank and MortgageIT for \$202.3 million. The Government's lawsuit against Allied Home Mortgage Corp. and two of its officers remains pending. In each settlement, the defendants have admitted and accepted responsibility for certain conduct alleged in the Governments' Complaint. The Office's Civil Frauds Unit is handling these cases as part of its continuing investigation of reckless 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.