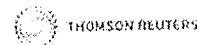


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Clinton R. Rockwell on mortgage litigation and the False Claims Act

5/13/2011

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On May 3, the United States filed a complaint in Manhattan federal court against Deutsche Bank and its wholly owned subsidiary, MortgageIT Inc., seeking damages and civil penalties under the False Claims Act.

The suit alleges that the entities made repeated false certifications to the U.S. Department of Housing and Urban Development (HUD), incorrectly claiming that loans submitted for insurance under the Federal Housing Administration's (FHA) Direct Endorsement Lender program complied with FHA requirements.

Specifically, the U.S. alleges that MortgageIT submitted more than 39,000 mortgages for FHA insurance between 1999 and 2009, certifying that each complied with all HUD rules.

MortgageIT also filed annual certifications attesting to its compliance with HUD regulations in order to maintain its HUD-FHA approval as a Direct Endorsement Lender.

Contrary to these certifications, the complaint alleges that MortgageIT underwriters wrongfully endorsed mortgages for FHA insurance that did not meet HUD-FHA guidelines by falsely certifying that they had conducted the due diligence required.

Additionally, the U.S. alleges that MortgageIT and Deutsche Bank falsely certified to HUD that MortgageIT had implemented the quality control procedures HUD requires of direct endorsement lenders. As a result, the suit claims that MortgageIT and Deutsche Bank wrongfully obtained approval of these ineligible mortgages for FHA insurance and were able to make substantial profits through the resale of the subject FHA-insured mortgages.

The United States is seeking treble damages and penalties of more than \$1 billion under the False Claims Act for the insurance claims already paid by HUD on the subject mortgages, and compensatory and punitive damages for those claims that HUD expects to pay in the future. It is also seeking recovery for breach of fiduciary duty, gross negligence, negligence and indemnification.

While the allegations in the case are the same as the issues that the government has been combating for years, this use of the False Claims Act (with its heightened penalties) is new in the mortgage space.

This ups the ante, showing the government's increasing aggressiveness and intolerance of violations, even technical violations.

There are also other areas that the False Claims Act can be used against lenders, including the timely and compliant remittance of premium payments and notification of FHA insurance termination.

Although there are weaknesses in the government's case, it raises the potential risk and thus the need to remain diligent in connection with risk assessment, underwriting, compliance and quality control.

This is one of the first salvos in a new type of mortgage challenge that will likely become more prevalent in the months and years ahead.

Clinton R. Rockwell heads BuckleySandler's Los Angeles office and advises a variety of financial services clients, including banks, mortgage companies, secondary market loan purchasers, commercial lenders, and securities broker-dealers, regarding regulatory, licensing, compliance and transactional matters. Mr. Rockwell's practice has a special focus on Federal Housing Administration (FHA) lending-including the formation of FHA lending platforms and representing clients before HUD in connection with approval, program administration, and enforcement issues. Mr. Rockwell received an LL.M. in Cross-Border Banking and Finance from the University College London and the London School of Economics, his J.D. from the George Washington University, and a B.A. from the University of California at San Diego. The firm's website is www.buckleysandler.com.

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