



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

September 8, 2016

**MEMORANDUM NO:**  
2016-CF-1801

*Memorandum*

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

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FROM: Christeen Thomas  
Director, Joint Civil Fraud Division, GAW

SUBJECT: Final Civil Action: Franklin American Mortgage Company Settled Allegations of Failing To Comply With HUD's Federal Housing Administration Loan Requirements

**INTRODUCTION**

The U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), assisted the U.S. Department of Justice, Washington, DC, and the U.S. Attorney's Office, District of Colorado, in the civil investigation of Franklin American Mortgage Company. Franklin American has its principal place of business in Franklin, TN.

**BACKGROUND**

The Federal Housing Administration (FHA) is a component of HUD. It 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.

HUD's direct endorsement lender program authorizes private-sector mortgage lenders to approve mortgage loans for FHA insurance. Lenders approved for the program must follow FHA requirements, including providing annual and per loan certifications that the lender complied with these requirements when underwriting and approving loans for FHA insurance.

Franklin American became an FHA-approved direct endorsement lender in 1995. As a direct endorsement lender, Franklin American was 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 requirements. When a borrower defaults on an FHA-insured loan underwritten and endorsed by a direct endorsement lender, such as Franklin American, the lender (or its representative) has the option of submitting a claim to HUD to compensate the lender for any loss sustained as a result of the default. Therefore, once a mortgage loan is endorsed for FHA insurance, HUD insures the risk of the borrower's defaulting on that mortgage, which is realized if an insurance claim is submitted.

### **RESULTS OF INVESTIGATION**

On December 2, 2015, Franklin American entered into a settlement agreement with the Federal Government to pay \$70 million to avoid the delay, uncertainty, inconvenience, and expense of lengthy litigation of certain civil claims the Government contended it had against Franklin American. As part of the settlement, Franklin American agreed that it engaged in certain conduct in connection with its origination, underwriting, and quality control of certain single-family residential mortgage loans insured by FHA.<sup>1</sup> The settlement was neither an admission of liability by Franklin American nor a concession by the United States that its claims were not well founded.

As a result of Franklin American's conduct, HUD insured hundreds of loans approved by Franklin American that were not eligible for FHA mortgage insurance under the direct endorsement lender program and that HUD would not otherwise have insured. HUD incurred substantial losses when it paid insurance claims on the loans covered by the settlement agreement.

### **RECOMMENDATION**

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

- 1A. Acknowledge that the attached settlement agreement for \$70 million represents an amount due HUD.

As of December 2, 2015, the settlement agreement of \$70 million had been reached, and it represents an amount due HUD. Included in the settlement agreement is a repayment agreement that explains an initial payment of \$10 million and the balance in monthly payments of \$1 million, with final payment expected by June 1, 2021. In accordance with HUD Handbook 2000.6, REV-4, the final action target date will be set at July 1, 2021. At issuance of this memorandum, HUD OIG will enter a management decision into HUD's Audit Resolution and Corrective Action Tracking System, along with any supporting payment information received to date.

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<sup>1</sup> Loans covered in the settlement agreement included loans insured by FHA between January 1, 2006, and December 31, 2012, that resulted in claims submitted to HUD on or before July 10, 2015, excluding origination or underwriting of home equity conversion mortgages under 12 U.S.C. (United States Code) 1715z-20 and streamlined refinances under 12 U.S.C. 1715n(a)(7).