



# SIGTARP

OFFICE OF THE SPECIAL INSPECTOR GENERAL  
FOR THE TROUBLED ASSET RELIEF PROGRAM

ADVANCING ECONOMIC STABILITY THROUGH TRANSPARENCY, COORDINATED OVERSIGHT AND ROBUST ENFORCEMENT

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## BANK OF AMERICA SUED FOR OVER \$1 BILLION FOR MULTI-YEAR MORTGAGE FRAUD AGAINST FANNIE MAE AND FREDDIE MAC

*After Collapse of Subprime Lending Market in 2007, Countrywide Started Alleged Fraudulent Mortgage Origination Program Called the "Hustle" Designed to Sell Defective Loans to Fannie Mae and Freddie Mac*

*Bank of America Continued the "Hustle" After Acquiring Countrywide in 2008*

WASHINGTON, DC - Christy L. Romero, the Special Inspector General for the Troubled Asset Relief Program ("SIGTARP"); Preet Bharara, the United States Attorney for the Southern District of New York; and Steve A. Linick, the Inspector General of the Federal Housing Finance Agency ("FHFA") yesterday announced that the United States has filed a civil mortgage fraud lawsuit against Bank of America Corporation ("Bank of America") and its predecessors Countrywide Financial Corporation and Countrywide Home Loans, Inc. (collectively, "Countrywide"). 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 engaging in a scheme to defraud the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"). Specifically, the Complaint alleges that from at least 2007 through 2009, Countrywide, and later Bank of America after acquiring Countrywide in 2008, implemented a new loan origination process called the "Hustle," which was intentionally designed to process loans at high speed and without quality checkpoints, and which generated thousands of fraudulent and otherwise defective residential mortgage loans sold to Fannie Mae and Freddie Mac that later defaulted, causing over \$1 billion in losses and countless foreclosures.

This is the first civil fraud suit brought by the Department of Justice concerning mortgage loans sold to Fannie Mae or Freddie Mac.

SIGTARP Special Inspector General Christy Romero said: "The complaint alleges serious and significant misrepresentations that Bank of America made before and during the time taxpayers invested \$45 billion in TARP funds in the bank. SIGTARP and its law enforcement partners will investigate allegations of wrongdoing by TARP recipients, particularly conduct that results in substantial losses to the government and taxpayers."

Manhattan U.S. Attorney Preet Bharara said: "For the sixth time in less than 18 months, this Office has been compelled to sue a major U.S. bank for reckless mortgage practices in the lead-up to the financial

crisis. The fraudulent conduct alleged in the complaint was spectacularly brazen in scope. As alleged, through a program aptly named ‘the Hustle,’ Countrywide and Bank of America made disastrously bad loans and stuck taxpayers with the bill. As described, Countrywide and Bank of America systematically removed every check in favor of its own balance – they cast aside underwriters, eliminated quality controls, incentivized unqualified personnel to cut corners, and concealed the resulting defects. These toxic products were then sold to the government sponsored enterprises as good loans. This lawsuit should send another clear message that reckless lending practices will not be tolerated.”

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

For many years, Countrywide, on its own and as part of Bank of America, was the largest provider of residential mortgage loans to the Government-Sponsored Enterprises, Fannie Mae and Freddie Mac (collectively, the “GSEs”). The GSEs were chartered by Congress with a mission to provide liquidity, stability, and affordability to the United States housing and mortgage markets. As part of this mission, Fannie Mae and Freddie Mac purchase single-family residential mortgage loans from lenders and pool them into mortgage-backed securities, which they sell to investors on the open market. The GSEs guarantee payments of principal and interest to investors in the event that any loan in a mortgage-backed security defaults.

Fannie Mae and Freddie Mac rely on the lenders’ representations and warranties that the loans they are delivering for sale comply in all respects with the standards outlined in the Fannie Mae and Freddie Mac selling guides and lender sales contracts, which set forth underwriting, documentation, quality control, and self-reporting requirements. Because Fannie Mae and Freddie Mac do not do a pre-purchase loan review, lender representations that they are underwriting and delivering investment-quality mortgages according to selling guides and contractual requirements are central to the GSEs’ purchase decisions.

Lender representations attest to the credit quality of their loans at the time of sale, the borrower’s ability to repay the loan, and the accuracy of the loan data provided. Among the most basic requirements of an investment-quality mortgage are that: (i) all required loan data is true, correct, and complete; and (ii) no fraud or material misrepresentation has been committed by any party to the loan. A lender must also represent and warrant that its quality control department implements various post-closing measures intended to detect problems with loan quality and fraud. Whenever a lender identifies a material breach of a selling warranty, it must self-report the loan to the GSE.

Countrywide initiated the Hustle (or “HSSL,” for “High-Speed Swim Lane”) in 2007 through its Full Spectrum Lending Division, just as loan default rates were increasing throughout the country and the GSEs were tightening their loan purchasing requirements to reduce risk. According to internal Countrywide documents, the goals of the Hustle were high speed and high volume, where loans “move forward, never backward” in the origination process. To accomplish these goals, the Hustle removed necessary quality control “toll gates” that could slow down the origination process. For example, the Hustle eliminated underwriters from loan production, even for many high-risk loans, such as stated income loans. Instead, the Hustle relied almost exclusively on unqualified and inexperienced clerks, called loan processors. Although loan processors had not been previously considered competent or knowledgeable enough to be permitted even to answer borrower questions, they were now required to perform critical underwriting duties. If a loan processor entered data from a loan file into an automated underwriting system called CLUES and received a rating that the loan had an acceptable risk of default (or “Accept” rating), no underwriter would ever see the loan. The Hustle also did away with compliance specialists, whose job it was to ensure that any loans that were approved with conditions had the

conditions satisfied before closing. Although loan processors were at the time entrusted with much more responsibility, they were given much less guidance. For example, mandatory checklists for performing important underwriting tasks (such as evaluating an appraisal or assessing the reasonableness of stated income) were eliminated. Loan processors were also financially incentivized to put volume ahead of quality, as Full Spectrum Lending changed its compensation plan to provide bonuses based solely on loan volume. Reductions to compensation for poor loan quality were discontinued.

Full Spectrum Lending's senior management was repeatedly warned that eliminating toll gates for quality control and fraud prevention, and expanding the authority of loan processors and compensating them based on volume without regard to quality, would yield disastrous results. For example, in January 2008, a pre-funding quality review showed an overall defect rate of 57%, and a defect rate of nearly 70% for stated income loans. Full Spectrum Lending senior management, however, made no changes to the Hustle, and instead restricted dissemination of the pre-funding review.

As the warnings about the Hustle went unheeded, Countrywide and later Bank of America knowingly originated loans with escalating levels of fraud and other serious defects and sold them to the GSEs. For example, with loan processors encouraged to put volume before quality, and no underwriters checking loan files that were accepted through CLUES, there was widespread falsification of CLUES data. Loan processors also had no incentive to ensure that conditions on loans were satisfied, resulting in a spike of closed loans with outstanding conditions or without critical documentation. By February 2008, post-closing quality reviews showed defect rates of approximately 37%, far above the industry standard defect rate of 4 to 5%.

Instead of notifying Fannie Mae and Freddie Mac that they had been purchasing large volumes of fraudulent and otherwise defective loans that did not meet GSE guidelines, Countrywide concealed the defect rates and continued the Hustle. In addition, Full Spectrum Lending initiated a one-time bonus to its quality control personnel to "rebut" the defect rates found by corporate quality control. For example, an "unreasonable stated income" finding could be reversed if corporate quality control could not prove that the stated income was actually false. After this "rebuttal" process, the final defect rate was revised down to 13%. Countrywide concealed this bonus plan from the GSEs as well.

In July 2008, Bank of America acquired Countrywide via a merger. After the merger, the Hustle continued unabated through 2009. At no time did Bank of America take any steps to disclose the Hustle to Fannie Mae or Freddie Mac. Throughout the Hustle, Countrywide and Bank of America sold thousands of Hustle loans to the GSEs that they knew did not meet their representations and warranties of quality. And after the loans defaulted, Bank of America has resisted buying many of them back, despite the presence of fraud, misrepresentation, and other obvious violations of GSE requirements.

In September 2008, as a result of massive losses from, among other things, the payment of guarantees to investors on loans that defaulted, Fannie Mae and Freddie Mac were placed in conservatorship under the FHFA pursuant to the Housing and Economic Recovery Act of 2008. Simultaneously with the creation of the conservatorships, the United States Treasury exercised its authority under this Act to purchase Fannie Mae and Freddie Mac stock. As of December 31, 2011, the Treasury had provided \$183 billion in funding to Fannie Mae and Freddie Mac through stock purchases.

Bank of America received \$15 billion in federal funds through the U.S. Department of the Treasury's Troubled Asset Relief Program (TARP) on October 28, 2008; an additional \$10 billion on January 9, 2009;

and \$20 billion on January 16, 2009. Bank of America repaid taxpayers' combined \$45 billion TARP investment in full on December 9, 2009.

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The Complaint seeks civil penalties under FIRREA, as well as treble damages and penalties under the False Claims Act, for more than \$1 billion in losses suffered by Fannie Mae and Freddie Mac for defaulted loans fraudulently sold by Countrywide and Bank of America.

Agents from SIGTARP and FHFA-OIG are investigating the case. FHFA and the Commercial Litigation Branch of the U.S. Department of Justice's Civil Division in Washington, D.C., have also provided support.

Assistant U.S. Attorneys Jaimie L. Nawaday and Pierre G. Armand are in charge of the case.

This prosecution was brought in coordination with President Barack Obama's Financial Fraud Enforcement Task Force, which was established to wage an aggressive and coordinated effort to investigate and prosecute financial crimes. SIGTARP is a member of the task force. To learn more about the President's Financial Fraud Enforcement Task Force, please visit [www.StopFraud.gov](http://www.StopFraud.gov).

#### **About SIGTARP**

The Office of the Special Inspector General for the Troubled Asset Relief Program investigates fraud, waste, and abuse in connection with TARP.

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