



June 7, 2019

U.S. Department of Housing & Urban Development
Federal Housing Administration
451 7th Street S.W.
Washington, DC 20410

RE: Proposed FHA Lender Annual Certification Statements

To whom it may concern:

The Housing Policy Council¹, the Mortgage Bankers Association², the American Bankers Association³, and the Bank Policy Institute⁴ are jointly writing in response to the U.S. Department of Housing and Urban Development's ("HUD" or "Department") request for comments on the proposed amendments to Federal Housing Administration ("FHA") annual and loan-level certification language, as well as the Defect Taxonomy, that HUD published on May 9, 2019. This letter focuses on the annual certifications. We expect to submit a second letter with comments on the proposed loan-level certifications and Defect Taxonomy on or before June 30, 2019. We appreciate HUD's extension of the deadline to provide comments on these two additional proposals.

Importantly, we want to thank the Department for restarting the critical policy conversation regarding the role of the annual and loan-level certifications, as well as the Defect Taxonomy, in FHA's own risk management and enforcement regime. We share in HUD's view that creating an environment in which lenders can operate within the FHA program with clarity and certainty regarding both FHA requirements and the potential

¹ The Housing Policy Council is a trade association comprised of leading national mortgage lenders, servicers, mortgage insurers, and title and data companies. HPC advocates for the mortgage and housing marketplace interests of its members in legislative, regulatory, and judicial forums. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable home ownership opportunities leading to long-term wealth-building and community-building for families.

² MBA is the only national association representing all segments of the real estate finance industry—an industry that employs more than 280,000 people throughout the country. The association works to ensure the continued strength of the nation's residential and commercial real estate markets and to extend access to affordable housing to all Americans.

³ The American Bankers Association is the voice of the nation's \$18 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard nearly \$14 trillion in deposits, and extend more than \$10 trillion in loans.

⁴ The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

penalties for noncompliance is critical to lenders' participation in this program. To accomplish this goal, FHA should strike a balance that encourages responsible lenders to participate in the FHA single-family insurance program, while at the same time protects the FHA Mutual Mortgage Insurance Fund. We believe that implementation of a coordinated and complementary annual certification, loan-level certification, and Defect Taxonomy that meets FHA's goals and lenders' needs is a good first step to achieve this objective.

We greatly appreciate FHA's efforts thus far to enact reforms intended to provide the clarity and certainty necessary to increase lender participation in the FHA program. To meet these objectives, as we will discuss in more detail below and in our forthcoming letter, we believe all three elements need to be further amended in ways that complement each other and reduce, rather than create layers of, potential liability under the False Claims Act.

For the reasons explained below, we strongly believe FHA will be best positioned to achieve the twin goals of optimizing program participation and maximizing compliance by either rescinding the annual certification requirement or replacing the current annual certifications with a certification that reinforces the obligation of each mortgagee to establish and operate in accordance with a corporate risk management plan, an approach that would more meaningfully foster compliance by each mortgagee with FHA requirements.

Again, we thank you for the opportunity to comment on these documents, and we look forward to continuing this dialogue with HUD representatives in furtherance of our shared crucial objectives.

Background on the Annual Recertification Process

The risks associated with originating FHA-insured loans have increased significantly over the last several years with the Department of Justice's reliance on loan-level and annual compliance certifications to pursue lenders for treble damages under the False Claims Act based upon alleged defects in FHA loans. The annual certifications currently require the mortgagee to attest to compliance with certain regulatory and Handbook provisions regarding its operations and adherence to FHA requirements using broad statements of absolute compliance without any qualifiers. These statements hold lenders to an impossible-to-meet standard of strict adherence to all program requirements, which is subject to a threat of liability under the False Claims Act. This regulatory framework has caused many lenders to retreat from the FHA program.

In order to maximize participation in the FHA program, thereby expanding access to credit for FHA borrowers, FHA must take steps to eliminate the causes of unnecessary risk and at times frivolous litigation. For lenders to resume participation, revisions are needed to the annual certifications to reflect the subjective realities of all mortgage lending, including FHA lending, and to assure lenders that they will be held accountable only for errors that directly impact the FHA Mutual Mortgage Insurance Fund. We understand that FHA's ultimate, underlying purpose for the annual certifications is to ensure mortgagees comply with policies and procedures on a day-to-day basis as part of a well-designed compliance management system for the FHA program. We also understand that it is not FHA's intent to use the certification to subject mortgagees to the risk of liability under the False Claims Act for subsequently-identified inaccuracies that either represent immaterial variances from FHA

requirements or are based on facts that the signer of the certification could not reasonably have known at the time of signing the certification. With this as a guidepost, and to assist in optimizing participation in the FHA program, which will, in turn, expand access to credit for FHA borrowers, we recommend approaching the annual certifications anew.

Mortgagees accept full responsibility for conducting their operations in accordance with FHA's operational, origination, and servicing requirements and facing HUD's administrative enforcement penalties in the event that mortgagees do not meet that responsibility. Mortgagees cannot, however, face the threat of treble damages under the False Claims Act by attesting to overly broad annual certification statements of strict adherence to program requirements, regardless of the impact on the FHA Mutual Mortgage Insurance Fund. Penalties must be appropriately calibrated to wrongdoing to create the clarity and certainty that HUD is striving to achieve, and that lenders need to foster increased program participation.

Concerns with the Proposed Annual Certification Statements

As noted in the comparison document that HUD released on May 9, 2019, the proposed annual certification language would eliminate redundancy by reducing the number of certifications required of mortgagees and amending the annual certification language to reference general certifications of compliance with the requirements set forth in 24 C.F.R. § 202.5, but remove references to FHA Handbook sections. The proposed annual certifications would also delete the existing Certification Statement #5, as this provision was brought over to the annual certifications from the loan-level certification during a previous revision. While we appreciate and support the Department's efforts to eliminate redundancy and streamline the certification language, the proposed amendments do not accomplish the primary goal of addressing the above-described unnecessary False Claims Act risk that lenders are exposed to as a result of overbroad certification statements. The proposed amendments change the certification language itself, but do not concurrently streamline the annual certification process or the operational impact of the overbroad certification statements.

Specifically, the proposed annual certifications would continue to require FHA-approved mortgagees to certify to strict compliance with "all HUD regulations and requirements necessary to maintain the Mortgagee's FHA approval as codified in 24 CFR § 202.5."⁵ The referenced regulatory section contains broad compliance requirements that include, among other things, compliance with all servicing regulations,⁶ HUD's Quality Control requirements,⁷ and the full range of ineligibility criteria, which includes that the lender did not engage in any practices that did not conform to generally accepted practices of prudent

⁵ See proposed Certification Statement #4.

⁶ See 24 C.F.R. § 202.5(e) ("A lender shall service or arrange for servicing of the loan in accordance with the requirements of 24 CFR part 201. A mortgagee shall service or arrange for servicing of the mortgage in accordance with the servicing responsibilities contained in subpart C of 24 CFR part 203 and in 24 CFR part 207, with all other applicable regulations contained in this title, and with such additional conditions and requirements as the Secretary may impose.").

⁷ See *id.* § 202.5(h) ("The lender or mortgagee shall implement a written quality control plan, acceptable to the Secretary, that assures compliance with the regulations and other issuances of the Secretary regarding loan or mortgage origination and servicing.").

mortgagees or that demonstrate irresponsibility.⁸ Thus, despite the proposed certifications' reference to compliance with regulations and requirements necessary to maintain the mortgagee's FHA approval, mortgagees would continue to be required to certify to strict compliance with the full set of each and every discrete FHA requirement. Importantly, any instance of a variance from any referenced FHA requirement would render this certification inaccurate, without regard to whether that non-adherence impacted the mortgagee's ability to participate in the FHA program or impacted the FHA Mutual Mortgage Insurance Fund. Given the breadth and detail of these FHA requirements, no corporate officer can know with complete certainty that a mortgagee has met all of these standards, even though HUD has qualified this certification with the signer's knowledge after a reasonable investigation. As a result, no mortgagee would be able to meaningfully complete the certification.

The proposed annual certifications would continue to present many of the same issues as the current certifications. As you know, because the certifications' overarching standards can seldom, if ever, be met with perfection, most lenders choose to submit "Unable to Certify" responses along with necessary qualifiers. Often, these qualifiers take the form of referencing the mortgagee's quality control and risk management processes utilized to identify, resolve, and, when required, report instances of noncompliance with FHA requirements. To the extent a mortgagee describes its general systems and processes for compliance in an "Unable to Certify" statement, HUD generally requests additional supporting information regarding instances of noncompliance. If the mortgagee cannot identify any specific instances of noncompliance, HUD will force the mortgagee to check the certification box in order to move through the recertification process, despite the mortgagee's attempt to avoid making a broad certification of compliance. As a result, the annual recertification process is unnecessarily burdensome and expensive for both mortgagees and HUD. The Department's most recent proposed amendments to these statements also will not close the circular loop within the Lender Electronic Assessment Portal ("LEAP") reporting system that requires lenders to re-certify to statements previously deemed as "Unable to Certify" with qualifiers already approved by HUD but not reflected in the system.

As a result, the proposed annual certification language does not adequately address the mortgage industry's valid concerns regarding use of the annual certification statements as the basis for pursuing draconian penalties under the False Claims Act. As you know, the False Claims Act is an important tool for the federal government and *qui tam* relators to impose liability on persons or entities who defraud governmental programs; however, as a fraud prevention statute with significant penalties, it should be used as was intended – only to combat actual fraud, not minor divergence from agency program requirements that do not amount to a fraudulent scheme or otherwise negatively impact government funds. Using the annual certification to support a False Claims Act case would be wrong, as both its language and HUD's stated position limits the scope of the certification to general program operations, not to loan-level origination, servicing or claims issues. For this reason, any certifications in the FHA program should include language that is narrowly tailored to cover only actual fraudulent acts or schemes against the government, rather than instances of noncompliance

⁸ See *id.* § 202.5(j)(4) ("For a lender or mortgagee to be eligible for FHA approval, neither the lender or mortgagee, nor any officer, partner, director, principal, manager, supervisor, loan processor, loan underwriter, or loan originator of the lender or mortgagee shall: ... Be engaged in business practices that do not conform to generally accepted practices of prudent mortgagees or that demonstrate irresponsibility.").

that do not rise to the level of fraud that materially impacts the FHA Mutual Mortgage Insurance Fund.

Unfortunately, as currently drafted, the proposed amendments to the annual certification statements could permit any variance from the broad regulatory provisions referenced in the certifications to be evidence to assert that the annual certification statements constituted a “false statement” under the False Claims Act, regardless of the impact on the mortgagee’s ability to participate in the FHA program and/or the FHA Mutual Mortgage Insurance Fund. As a result, to the disappointment of the industry, even if a lender maintains a robust system of internal controls that is, in large measure, effective, one-off errors could become the foundation for a False Claims Act allegation. Consequently, the proposed amendments will not give lenders the assurance needed to expand their program participation. We understand that this outcome does not reflect FHA’s intent.

Recommendations for Annual Certification Process and Statements

In light of these concerns, we strongly urge the Department to consider using this opportunity to revise its regulations to remove the annual certification requirement and instead rely on the existing oversight and enforcement regime. In the alternative, we recommend that HUD amend the annual certification language to require a certification that a lender maintains policies, procedures, and internal controls that are reasonably designed to assure compliance in all material respects with FHA regulations, as part of an FHA compliance management system. HUD can hold lenders strictly accountable under such a certification; however, the certification would not include statements to which an individual corporate officer could not attest, even after a reasonable investigation of the mortgagee’s operations.

Amend the Regulations to Remove the Annual Certification Requirement

FHA regulations contain both general approval and specific eligibility requirements dependent on an entity’s organizational structure, which all FHA-approved entities must meet, and continue to meet, to maintain FHA approval notwithstanding the act of annual certification⁹. Nothing in the National Housing Act, however, requires a mortgagee to make any specific certifications to the Department regarding the mortgagee’s eligibility to participate in the FHA program. Similarly, the regulations do not require that applicants and approved mortgagees certify their compliance with all eligibility criteria.

HUD regulations require that the application for approval and each recertification must be made “on a form prescribed by the Secretary.”¹⁰ While the mortgagee must consent to comply with the general approval requirements set forth in Section 202 of the regulations as part of the application process, the regulations set forth only one specific requirement regarding the contents of the application and annual recertification forms. Specifically, Section 202.5(m) requires that, upon approval and with each annual certification, the mortgagee “must submit a certification that it has not been refused a license and has not

⁹ See 24 C.F.R. §§ 202.5 through 202.10.

¹⁰ See 24 C.F.R. §§ 202.3(a), 202.5(m).

been sanctioned by any state or states in which it will originate insured mortgages or Title I loans.” We are not aware of any additional regulatory provision regarding initial approval or annual recertification that requires the approval or recertification form to include additional specific language or certifications. Rather, certifications were left to the more specific loan-level process, which will be the subject of our second letter.

Given this regulatory framework and HUD’s enforcement authority, rather than attempt to hold lenders accountable for each and every operational, lending, and servicing requirement identified in 24 C.F.R. § 202.5, we believe that HUD should amend its regulations to remove the requirement that FHA lenders make annual certifications to HUD. The current required certification regarding license refusals and state sanctions are business changes that HUD obligates a mortgagee to report to FHA within mere days of occurrence, and HUD actively enforces this reporting requirement. If mortgagees are already obligated to report these specific events to HUD, a certification regarding the absence of such events would appear to have little utility to the Department and should be removed from the regulations. If, as we understand to be the case, FHA’s goal for the certifications is to incent lenders to conduct reasonable reviews designed to ensure compliance, that incentive already exists as a result of loan-level certifications. Alternatively, HUD could simply impose an independent obligation on an approved lender to conduct annual reviews without requiring the submission of a certification.

Amend the Annual Certification Language to Reflect a Reasonable Corporate Governance Standard

As discussed, HUD does not need annual certification statements to hold mortgagees accountable for adherence to FHA requirements. HUD has the requisite authority to enforce FHA’s operational, lending, and servicing requirements either internally or by referral to the Department of Justice when appropriate. If, however, HUD continues to require an annual certification statement, we strongly recommend amending the proposed language to require a certification regarding the existence of procedures reasonably designed to ensure material compliance and a reporting function to alert HUD to instances of material noncompliance.

As discussed above, a mortgagee, regardless of size, cannot know if there are any variances from the full array of FHA requirements referenced in the proposed annual certification statements. As a matter of corporate governance, a mortgagee cannot sign certifications that it knows or should know may not be true and should not ask its officers and employees to do so either. It is not in HUD’s or the lender’s best interest to have flawed certifications to which no person can reasonably attest. Approved mortgagees are required to comply with requirements regardless of whether they certify to such, and FHA may use its enforcement powers and administrative remedies to address alleged violations of FHA requirements. Certifications cannot be used as a guaranty or warranty of perfect and strict adherence to FHA general program requirements, irrespective of materiality or as an independent basis for sanctions absent intentional and material fraud. To do so is unfair, exposes lenders to undue risks, and results in a lack of full lender participation in the FHA program to the detriment of borrowers.

Rather than require a mortgagee’s corporate officer to certify to perfect compliance with any portion of FHA regulations and requirements, the annual certification instead could be limited to certifying the existence of policies and procedures that are reasonably designed

to ensure material compliance. Such a certification would drive a mortgagee to investigate and identify areas of material noncompliance and ensure that it maintains a robust risk management program, such that a corporate officer would be able to confidently sign the certification. We recommend the following language for the annual certification:

I certify that, to the best of my knowledge and after conducting a reasonable investigation, the Mortgagee maintains policies, procedures, and internal controls that are reasonably designed to assure compliance in all material respects with the general regulations and program requirements of HUD-FHA that are applicable to the Mortgagee's continued approval and operations, including those contained in HUD Handbook 4000.1 regarding the Mortgagee's obligation to make all reports pursuant to HUD Quality Control requirements.

We believe such a certification would meet HUD's goal of fostering compliance to protect FHA and homebuyers and allow it to take action against mortgagees that fail to report material noncompliance and/or maintain a robust quality control process using its available administrative enforcement authority. This certification, which would require mortgagees to design and implement a comprehensive compliance management system to ensure adherence to FHA requirements, would align HUD with the approaches of other federal agencies responsible for lender oversight, including the Consumer Financial Protection Bureau and the prudential regulators. At the same time, it would help to increase lender participation in the FHA program, which would benefit FHA and homeowners, as well.

Conclusion

We thank the Department for the opportunity to offer comments on the proposed amendments to the annual certifications announced by HUD on May 9, 2019. We would welcome the opportunity to meet with HUD representatives to discuss the proposed amendments to the annual certifications and the recommendations set forth in this letter in more detail. If you have any questions regarding our recommendations, please feel free to contact MBA's Fran Mordi, AVP for Tax, Accounting, and Financial Management, at (202) 557-2860 and HPC's Meg Burns, SVP for Mortgage Policy at 202-589-1926

Thank you for your consideration.

Sincerely,

Housing Policy Council
Mortgage Bankers Association
American Bankers Association
Bank Policy Institute