UNITED STATES OF AMERICA

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

BOARD OF CONTRACT APPEALS

WASHINGTON, D.C.

In the Matter of:	:	
MICHAEL MILLER,	:	HUDBCA NO. 88-3434-D44 DOCKET NO. 87-1235-DB
RESPONDENT	:	

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DETERMINATION BY ADMINISTRATIVE JUDGE TIMOTHY J. GRESZKO

January 19, 1989

Statement of the Case

By letter dated April 1, 1988, Michael Miller ("Respondent") was notified by the U.S. Department of Housing and Urban Development that it intended to debar him from participation in Departmental programs for a period of three years pursuant to 24 C.F.R § 24.6(c)(3), (11) and (12). The letter stated that the proposed debarment was based on Respondent's participation as a loan closer in 13 enumerated real estate transactions, and asserted that Respondent either knew or should have known that certain broker commission checks were used to pay HUD-required minimum investments for buyers, thus circumventing HUD program requirements. The letter also informed Respondent that, pursuant to 24 C.F.R. § 24.18(a)(2), he was temporarily suspended from participation in all HUD programs, pending the final determination of the issues in this matter.

Respondent made a timely request for a hearing on the proposed debarment pursuant to 24 C.F.R. § 7. A hearing was subsequently held in Colorado Springs, Colorado to determine whether the debarment of Respondent was in the best interests of the public and the Government. Each party has submitted a brief, and this decision is based upon a consideration of the entire record in this case.

Findings of Fact

1. Respondent was employed in the fall of 1985 and the early months of 1986 as a loan officer at the Colorado Springs, Colorado branch office of Compass Mortgage Company ("Compass"), a HUD-approved mortgagee. Respondent has been employed for 17 years in the mortgage lending field and has previous experience as a "loan closer." He was familiar with and understood the rules and regulations applicable to the closing of FHA-insured loans during his tenure at Compass. (Joint Exhibit 1, ¶1 or "Stip. 1"; Tr. 124-126).

2. Monica Davis, now Monica Rodriguez, was employed as the loan closing officer for Compass at all pertinent times. In late 1985 and early 1986, Respondent attended the closings of the 13 loans which are the subject matter of this proceeding. The responsibility for actually closing loans was outside the scope of Respondent's duties as a loan officer, but he was asked by the office manager of the Colorado Springs office of Compass to attend these closings as an ad hoc closing officer due to an overflow of business in the office. Respondent's instructions were to bring the loan closing files, which had been prepared by Davis, to the closings. He was further instructed that he was not to review the closing documents for accuracy, because that function had been performed by others, including the underwriter. Respondent's role in these closings was to obtain the signatures of borrowers, to answer questions of the parties pertaining to the Compass loans, and to return the completed documents to Davis for review. Upon approval by Davis, the Compass mortgage loan proceeds check was given to Respondent, who returned to the closing room and delivered the check to a title company representative for disbursement. Subsequently, Davis prepared and signed the Mortgagee's Closing Certification, which was forwarded to HUD along with a number of other documents. Each certification stated, inter alia, that the mortgagor had made no less than the required statutory cash investment. After review of these documents, HUD endorsed each loan for FHA insurance and issued a Mortgagee Insurance Certificate on each loan. (Stip. 2; Govt. Exh. 1-28; Tr. 80, 86, 94, 97, 116-120).

3. Respondent was not the loan officer for the loans in question, did not process or originate these loans, and did not review the loan files prior to closing. He was given access to these files shortly before closing occurred. (Tr. 86, 118).

4. All of the transactions in question involved sales by builders or contractors to investors who obtained direct endorsement FHA-insured loans as non-occupant owners.

RAM Marketing ("RAM") was the realtor for the sale of the properties. In each transaction, the relevant Form HUD-1 ("the settlement statement") indicated on line 303 that each investor had made a substantial cash payment at settlement of $10,000 or more, but in fact, each investor had paid no more than $100 earnest money to the builder or contractor. There was no indication on any of the settlement statements that any of the borrowers had made payments to RAM prior to closing, other than the small earnest money deposits reflected on line 201 thereof. The settlement statements also indicated on line 701 that RAM was to receive a commission which varied from approximately $16,000 to over $21,000, which was 22.5% to 25.5% of the selling price of the various properties. These commissions were unusually high for the locality, as 10% commissions were typical and commissions in excess of 20% rare in the Colorado Springs area. (Stip. 3; Govt. Exh. 1-13; Tr. 67, 72, 102).

5. Consistent with the prevailing practice in Colorado, each loan closing attended by Respondent was followed immediately by a real estate closing conducted by a title company representative. In Colorado, title company representatives are responsible for the physical receipt and disbursement of funds at closings, and lenders rely on title company representatives to perform these duties as well as to issue title insurance to the lender subsequent to the closings. The title company representative at a number of the closings was Sharon Myers, an employee of the First American Title Company. In late 1985, Myers was approached by a representative of RAM, who suggested that since many of RAM's clients were investors from outside Colorado, it would be advantageous to all if RAM were permitted to collect the purchaser's funds before closing, and to accept a commission at closing that was reduced by the amount that the purchaser would otherwise have been required to tender at closing. Myers took the RAM proposal to her supervisors and ultimately sought the opinion of the general counsel of her company. The general counsel approved a two-check procedure in which one check would be issued to RAM in the amount due from the borrower, which RAM would immediately endorse back to the title company. The title company representative also issued a second check to RAM, which amounted to the difference between the total commission due RAM on line 701 of the settlement statement, and the cash due from the borrower as set out on line 303 of the settlement statement. Each of the 13 real estate closings was conducted by the title company representative utilizing this two-check procedure. Respondent was present at no less than 5 of the closings when Myers made two-check disbursements. The two-check procedure was highly unusual, as borrowers are typically required to tender at closing the cash due as set out on line 303 of the settlement statement. Neither Respondent nor Davis was informed by Myers that she was utilizing the two-check procedure. In one transaction involving three loan closings with borrowers by the name of Traggiai, Mrs. Traggiai questioned her husband with respect to the buyer's contribution listed on line 303 of their settlement statement. Mr. Traggiai asked the RAM representative about this discrepancy, and was told

that he would discuss the matter with the Traggiais later. Respondent does not remember hearing these statements, and the Traggiais were unable to verify that Respondent, although present at their closing, was aware that these statements were made. There were no other discussions at the closings concerning the borrowers' down payments, and none of the borrowers tendered any payment to Myers at any of the closings. (Stip. 3, 4; Govt. Exh. 1-13; 29-33; Tr. 25-26, 32-35, 38-39, 43-57, 68-71, 120, 123, 126, 129-131, 136, 138, 145).

Discussion

Sanctions such as suspension and debarment are to be used to protect the public, and not for punitive purposes. Gonzalez v. Freeman, 334 F.2d 570, 577 (D.C. Cir. 1964); 24 C.F.R. § 24.5(a). The purpose of debarment is to assure the Government that it only does business with responsible contractors and grantees. 24 C.F.R. § 24.1 Responsibility is a term of art in Government contract law, defined to include not only the ability to perform a contract, but the honesty and integrity of the contractor or grantee as well. Roemer v. Hoffman, 419 F. Supp. 130 (D.C. D.C. 1976); Paul Grevin, HUDBCA No. 85-930-D16 (July 10, 1986).

Respondent is a "participant" in a "specially covered activity" of the Department as defined in 24 C.F.R. §§ 24.3(a)(2) and 24.3(u). Specially covered activities encompass, inter alia, participation in the loan and insurance programs of the Department. The term participant includes mortgagees and persons employed by or in a business relationship with mortgagees. Id. Respondent's activities as an ad hoc loan closer, loan officer, and employee of Compass Mortgage Company fall squarely within these definitions.

The Department's regulations also provide at 24 C.F.R. § 24.6(c), that a debarment may be imposed for:

> (3) Conduct indicating a lack of business integrity or honesty which affects the present responsibility of a...participant;
> * * * * * * * * * * *
> (11) Violation of any law, regulation, or obligation relating to applications for financial assistance, insurance, or guaranties...;
>
> (12) Making or causing to be made any false statement for the purpose of influencing in any way an action of the Government;....

Counts I-XIII of the Government's complaint charge that Respondent knowingly participated in the closing of a loan transaction in which the purchaser did not pay the minimum investment in the property required by Section 203(b)(9) of the National Housing Act, 24 C.F.R. §§ 203.18(c) and 203.19, and by paragraphs 2-6 and 2-7 of HUD Handbook 4000.1, Revision 1. Counts

XIV-XXVI of the complaint charge that Respondent knowingly participated in the execution of Mortgagee Closing Certificates that (1) were falsely signed by another employee of Compass as "loan closer," whereas Respondent actually participated in the transaction as the mortgagee's loan closer; and (2) falsely certified that the mortgagor's required statutory cash investment had been made and that the loan had been closed in accordance with the statutory and regulatory requirements of the National Housing Act and of HUD-FHA.

The ultimate questions in this case are whether Respondent either knew, or should have known, that the borrowers in question had not made the minimum 15 per cent investment required by law[1], and whether Respondent should be held responsible for the subsequent inaccurate Mortgagee's Closing Certifications, as a result of his participation in the closings.

The burden is on the Government to prove by a preponderance of the evidence that cause for debarment exists. 24 C.F.R. § 24.13(c); James J. Burnett, HUDBCA No. 80-501-D42, 82-1 BCA ¶15,716. Proof of the Government's allegations would clearly be sufficient to demonstrate a lack of integrity and present responsibility on the part of Respondent, as the record reveals an invidious and fraudulent scheme to evade a most critical aspect of the laws and regulations governing the issuance of mortgage insurance by the FHA. However, I find on this record that, notwithstanding the seriousness of the allegations, the Government has failed to carry its burden of proof with respect to the misconduct alleged, and consequently has also failed to carry its burden of proof with respect to Respondent's present lack of responsibility.

There is no direct evidence of record that is sufficient to prove that Respondent was aware of either the two-check procedure or the scheme to evade FHA minimum investment requirements. Respondent denied the allegations, and his denial was not refuted by the testimony of any of the witnesses called at the hearing. Likewise, the indirect, or circumstantial evidence of record is also inconclusive with respect to what Respondent knew or should have known about these transactions.

The utilization of circumstantial evidence and inference to establish fact is permissible, under Federal law, "so long as the inference is reasonable and, in the context of known facts, is one which springs readily and logically to mind, and is not one of two or more inferences, both or all of which are equally probable." Martin A. Gleason, 534 F.2d 466 (2d Cir. 1975)(emphasis supplied).

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1 See 12 U.S.C. § 1709(b)(9); 24 C.F.R. §§ 203.18(c) and 203.19.

The evidence of record is undisputed that: (1) the commissions payable to RAM on the settlement statements were atypically high for the locality; (2) the two-check procedure was highly unusual; (3) Respondent had opportunities to observe the two-check procedure at several closings; (4) one borrower raised a question about the downpayment at a closing which Respondent attended; and, (5) Respondent understood the laws and regulations applicable to FHA-insured loans. However, there is also credible evidence, which was provided in substantial part by the Government's witnesses, which indicates that Respondent was initially provided with the loan files just shortly before each loan closing, and which further indicates that Respondent's instructions did not require him to audit the closing figures or to verify that the minimum required investments were tendered at closing. The borrower's question referred to above was neither directed toward nor answered by Respondent, and the parties have stipulated that the borrowers cannot verify that Respondent was aware that the question was raised. In addition, it does not appear on the evidence of record that the title company representative or the RAM representatives made any efforts at closing to highlight the two-check procedure.

While the Government asserts that the record establishes that it is likely that Respondent knew or had reason to know of the two-check procedure, I find on the record before me that it is no less probable that the converse is true. There is no persuasive proof for the Government's assertions with respect to Respondent's knowledge. Moreover, the evidence does not establish that Respondent was duty bound by law, regulation, or local custom and practice to have personally verified the requisite certifications made by Monica Davis, solely because he attended the loan closings and she did not.[2] I accordingly further determine that the evidence is insufficient to prove that Respondent knowingly participated in the execution of Mortgagee's Closing Certificates containing false information. Consequently, I find that the Government has failed to show that Respondent is not presently responsible.

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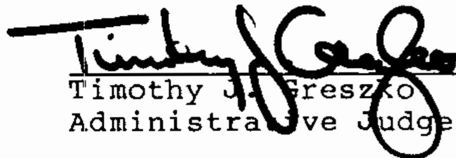
2 The Mortgagee's Closing Certifications for these loans indicates that "the mortgagee at the time of the closing of this loan certif[ies] that we have <u>reviewed</u> the outstanding commitments, legal instruments, closing statements, and other documents of closing," and that "<u>our review</u> indicated that the loan has been closed in accordance with the statutory and regulatory requirements of the National Housing Act and HUD-FHA...." (Govt. Exh. 14-26)(emphasis supplied). Conspicuously absent from this certification is a statement that the certifying officer attended the loan closing. The Government has not attacked the sufficiency of this certification, and there is no evidence in the record that the loan closing procedure utilized by Compass was improper, <u>per se</u>, or so imprudent as to raise an inference that Respondent is not presently responsible.

Conclusion

For the above reasons, it is my determination that Respondent's debarment is not warranted under the circumstances of this case. It is hereby **ORDERED** that Respondent's suspension from participation in the programs of this Department shall be lifted immediately.



Timothy J. Greszko
Administrative Judge