UNITED STATES OF AMERICA
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
OFFICE OF APPEALS
Washington, D.C.

In the Matter of:	HUDOA No. 10-M-004-D4
DAWN O'HALLORAN,	OGC Case No. 10-3618-DB
Respondent.	
	November 3, 2011

Appearances

For Respondent: Scott D. Burke, Esq. and Bruce E. Alexander, Esq.
Washington, D.C.

For the Government: Stanley E. Field, Esq.
Ana I. Fabregas, Esq.
U.S. Department of Housing and Urban Development
Washington, D.C.

INITIAL DECISION AND ORDER

BEFORE: H. Alexander MANUEL, Administrative Judge

This Initial Decision and Order recommends that a two-year period of debarment be imposed upon Respondent as a result of Respondent's actions in failing to comply with departmental regulations and policy, as detailed in the findings of fact and conclusions of law set forth below.

Statement of Jurisdiction

On or about March 3, 2010, the Office of Hearings and Appeals received and docketed the Referral Order, dated February 26, 2010, and issued by the Debarring Official for the U.S. Department of Housing and Urban Development ("HUD" or "the Department"), in Case Number 10-3618-DB. The Referral Order requested that this Office make official findings of fact in this case, in accordance with 2 C.F.R. § 180.845(c). The administrative judges of this Office are authorized to serve as hearing officers for the purposes of issuing findings of fact and recommended decisions for consideration by the debarring official. 2 C.F.R. §2424.842. The findings of fact and conclusions of law set forth below were reached after considering the entire

record in this case, including the exhibits and written submissions of the parties, the mitigating factors set forth in 2 C.F.R. §180.160, and the evidence adduced at the hearing held in this matter.

Statement of the Case

On October 20, 2009, the HUD Enforcement Center notified Respondent Dawn O'Halloran that she was immediately suspended from participation in all Executive Branch procurement and non-procurement transactions, and that, in order to protect the public interest, HUD proposed to debar Respondent from future participation in federal procurement and non-procurement programs for a period of five years. (Notice of Suspension and Proposed Debarment ("Notice of Suspension" or "Notice"), dated October 20, 2009, at 1.) In addition, pending final determination of the debarment, Respondent was immediately suspended from further participation in such transactions. (*Id.*) The suspension and proposed debarment was based on alleged irregularities in Respondent's decision-making and documentation of her reasons for loan approval while underwriting mortgages as a Direct Endorsement underwriter for HUD. (*Id.*) Specifically, the Notice alleges that various actions by O'Halloran violated the HUD, MORTGAGE CREDIT ANALYSIS FOR MORTGAGE INSURANCE, HANDBOOK 4155.1 REV-5 [hereinafter HUD, HANDBOOK 4155.1 REV-5], and Mortgagee Letters 96-18, 97-26, 00-28, 01-01, 05-43, and 07-11.

The Notice describes a range of alleged misconduct, allegedly committed by Respondent, that includes "approv[ing] loans with credit histories that reflected continuous slow payments, and delinquent accounts without strong offsetting (compensating) factors and supporting documentation." (Notice at 2.) The Notice also alleges that Respondent "failed to document [her] analysis of how previous derogatory credit did not represent a risk of mortgage default to justify approval of the mortgage in violation of HUD requirements." (*Id.*) Other allegations were that Respondent "did not obtain adequate documentation of the borrower's income and/or stability of income" (*id.*) and "failed to document the source of funds used to close the loan and/or satisfy omitted liabilities." (*Id.*, at 3.) The Government further alleges that one of Respondent's loans was "approved ... with a debt to income ratio that exceeded HUD guidelines without significant compensating factors," and that Respondent approved a loan "without obtaining the required documentation to support the decision to approve the loan." (*Id.*)

Respondent appealed the proposed debarment and requested a hearing before a debarring official in accordance with her rights under 2 C.F.R Part 180. She contends that her actions complied with the applicable standards, and that she is "presently responsible" in her ability to do business with HUD. She further contends that HUD's purpose in bringing these allegations is punitive, in violation of 2 C.F.R. § 180.125. The hearing on this matter was conducted on July 28, 2010, pursuant to 24 C.F.R. Part 26, Subpart A. The parties filed their respective Post-Hearing Briefs on November 8, 2010.

Findings of Fact

1. HUD directed its Quality Assurance Division ("QAD") within its Philadelphia Homeownership Center to conduct a review of loans originated by Lend America, an FHA

approved lender. (Tr. 57:9-18.) The purpose of the review was to assess compliance of Lend America loans with the standards set forth by HUD in HUD handbooks and mortgagee letters. (Tr. 114:12-17; Tr. 128:2-6; Tr. 129:4-8.) The QAD conducted its review from December of 2008 to February of 2009. (Tr. 57:19-21.)

2. Respondent was employed with Lend America for approximately seven to ten years, until December 11, 2009, when the company went out of business after HUD revoked its status as an FHA-insured lender. (Tr. 150:20-151:5; 154:10-16.) Loans approved by Respondent were amongst the Lend America loans reviewed by the QAD. (Tr. 30:17-18.)

3. To date, Respondent has been employed in the mortgage industry for 24 years, and has been a mortgage loan underwriter for 20 years. (Tr. 152:5-15.)

4. Respondent became a conventional loan underwriter in the late 1980s and an FHA-approved underwriter in 1992. (Tr. 152:14-15.)

5. Upon becoming an FHA-approved underwriter, Respondent was assigned the Computerized Homes Underwriting Management System (CHUMS) identification number K416 by HUD. (Tr. 32:7-17; Tr. 153:12-20.)

6. The CHUMS ID number is unique to each underwriter and follows the underwriter throughout his or her career. (Tr. 32:6-17; 153:14-20.)

7. During her time as an underwriter, Respondent has underwritten approximately 10,000 loans. (Tr. 151:22.)

8. On October 20, 2009, Respondent received a Notice of Suspension and Proposed Debarment informing Respondent that she was immediately suspended from "participation in procurement and nonprocurement transactions as a participant or principal, with HUD and throughout the Executive Branch of the Federal Government" and that HUD was "proposing [Respondent's] debarment from future participation in procurement and nonprocurement transactions as a participant or principal, with HUD and throughout the Executive Branch of the Federal Government for a period of five years from the date of this Notice." (Tr. 158:7-22; Resp't Ex. 1.)

9. The Notice of Suspension was based upon alleged irregularities in the following loans underwritten by Respondent and reviewed by the QAD: FHA No. 483-3817075 ("Bilyeu Loan"); FHA No. 061-3068308 ("Crump Loan"); FHA No. 352-5560162 ("Herard Loan"); FHA No. 495-7749910 ("O'Neal Loan"); FHA No. 095-0548491 ("Pacheco Loan"); and FHA No. 371-3599681 ("Santiago Loan"). (Resp't Ex. 1.)

10. Respondent admitted to underwriting and approving the following five loans for FHA insurance endorsement: the Crump Loan; the Herard Loan; the O'Neal Loan; the Pacheco Loan; and the Santiago Loan.

11. Respondent denied underwriting or approving the Bilyeu Loan. (Tr. 220:12-13.)

12. A Mortgage Credit Analysis Worksheet ("MCAW") is required for any borrower applying for a mortgage insured under the National Housing Act, except for streamline refinances. HUD, HANDBOOK REV-5 ch. 3, sec. 1, subsec. 3-1, at 3-1.

13. Respondent admitted to signing the MCAWs admitted into evidence by Respondent's counsel for the Herard Loan (Resp't Ex. 3) and the Santiago Loan. (Tr. 194:10-195:5; 172:11-173:3; Resp't Ex. 10.)

14. Respondent denied signing the MCAWs admitted into evidence by the Government for the Herard Loan (Gov't Ex. 1) and the Santiago Loan (Tr. 174:12-175:6; 194:16-21; Gov't Ex. 9.)

A. The Bilyeu Loan

15. Respondent's CHUMS identification number appears on the MCAW for the Bilyeu Loan. (Tr. 61:15-20.)

16. Government witness Patricia Peiffer identified the first name on the signature line of the MCAW for the Bilyeu Loan as "Ellen" but could not read the last name. (Tr. 62:4)

17. Respondent identified the name on the signature line of the MCAW as belonging to Ellen Colomvotos, another underwriter employed at Lend America. (Tr. 220:1-4.)

18. Government witness Peiffer testified that Respondent did not approve the Bilyeu Loan. (Tr. 61:8-9.)

19. The MCAW for the Bilyeu Loan does not bear Respondent's signature, and Respondent did not underwrite the Bilyeu Loan.

B. The Crump Loan

20. The Government alleges that Crump was ineligible for a cash-out refinance based on Mortgagee Letter 05-43, which requires the borrower to have made all of his mortgage payments within the month due for the previous 12 months." Mortgagee Letter 05-43, dated October 31, 2005; (Gov't Post-Hr'g Br. 14-15.)

21. A credit report contained in the FHA binder for the Crump Loan showed that the borrower was 30 or more days late paying his previous mortgage in February of 2006, July of 2006, August of 2006, September of 2006 and December of 2006. (Tr. 84:12-85:4; Gov't Ex. 10; Resp't Ex. 17.)

22. Respondent claims that Mortgagee Letter 05-43 only applies to cash-out refinances with loan to value ratios over 85%. (Resp't Post-Hr'g Br. 4.)

23. Mortgagee Letter 05-43 states that "FHA will insure a cash-out refinance of up to **95%** of the appraiser's estimate of value." (Mortgagee Letter 05-43, emphasis in original.)

24. The Government also alleges that Respondent did not adequately explain the collection accounts and recent credit problems appearing on the credit report. (Gov't Post-Hr'g Br. 16.)

25. The credit report showed that the borrower was over 30 days late paying an auto loan and an installment account with CT Labor Department Federal Credit Union. (Tr. 85:6-10; Gov't Ex. 10; Resp't Ex. 17.)

26. The credit report also showed a GEMB/Walmart account with the last late payment occurring in September 2003. (Resp't Ex. 17.)

27. The Handbook does not require an underwriter to provide written explanations for minor delinquencies, which include delinquencies occurring two or more years in the past. HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3, at 2-5.

28. A copy of the borrower's Family Leave Act approval for the period of October 11, 2005 through March 1, 2006, a medical certificate for the borrower, and a diagnosis from Middlesex Orthopedic Surgeons, P.C., were included in the FHA binder. (Resp't Ex. 15-16; Tr. 186:21-187:9.) An explanatory letter from the borrower stated:

> The late payments on my credit are due to my hip surgery. I was on bed rest and homebound for several months in 2003 and again from October 2005 thru March 2006. I tried my best to keep my payments up but with my mortgage payment rising as well as the cost of living, I was unable to. I am now current and would like to get into a fixed rate and pull out some money for my house and myself.

(Resp't Ex. 13.)

29. The borrower's medical hardship generally coincided with the delinquencies on his collection accounts. (Resp't Ex. 17.)

30. The FHA binder for this loan included a letter from CT Labor Department Federal Credit Union stating that for at least one of the accounts, the borrower co-signed for his daughter and "[p]resently the loan account is in good standing and all the payments are being made by Lashandra not by Richard." (Tr. 188:6-11.)

31. The Government maintains that this letter was inadequate to verify that the loan was in good standing because it did not reference a particular loan and only dated back to 2006. (Gov't Post-Hr'g Br. 16.)

32. The FHA binder also included several bank statements for the borrower's daughter showing that she had been making the payments on the CT Labor Department Federal Credit Union loans. (Resp't Ex. 14.)

33. Statements of account with the CT Labor Department Federal Credit Union show late payments on both loan accounts. (Resp't Ex. 14.)

34. Respondent stated that she did not feel it was necessary to "punish" the borrower based on the late payments since his daughter had been making all payments, including paying late fees. (Tr. 187:10-20.)

35. The remarks section of the MCAW did not contain any reference to the bad debts in the credit report nor did it reference any other document that discusses or analyzes the bad debts in the credit report. (Tr. 87:22-88:9; Gov't Ex. 12.)

36. The remarks section contained references to compensating factors, including "job stability," "long term ownership," "minimal debt" and "positive loan to value ratio." (Gov't Ex. 12.) However, "job stability" and "long term ownership" are not cognizable compensating factors within the ambit of the HUD guidelines. HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34.

37. The Government affirms that a "positive loan to value ratio" is a compensating factor. (Tr. 88:16-22.)

38. The Government alleges that "minimal debt" should have been further explained. (Tr. 89:7-11.)

39. Respondent included the borrower's credit report in the file, and therefore adequately documented the compensating factor for minimal debt. (Tr. 86:7-22; Resp't Ex. 17; Gov't Ex. 11.)

C. The Herard Loan

40. HUD guidelines state that an applicant's Mortgage-to-Income Ratio may not exceed 31% unless significant compensating factors are present. HUD, Handbook 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-12(A), at 2-33.

41. HUD guidelines state that an applicant's Total Payment-to-Income Ratio may not exceed 43% unless significant compensating factors are present. HUD, Handbook 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-12(B), at 2-33.

42. Two separate MCAWs were entered into evidence. (Gov't Ex. 1; Resp't Ex. 3.)

43. The MCAW submitted by the Government listed a Mortgage-to-Income Ratio of 47.331% and a Total Payment-to-Income Ratio of 52.166%. (Gov't Ex. 1; Gov't Post-Hr'g Br. 18-19.)

44. Respondent asserted that she did not sign or approve the MCAW submitted by the Government. (Tr. 194:20-195:2.)

45. The Government offered no evidence that the MCAW for the Herard Loan contained Respondent's true signature, other than the fact that Respondent's CHUMS ID appeared on the MCAW.

46. Respondent did not sign or approve the MCAW submitted by the Government. (Tr. 194:20-21; Gov't Ex. 1.)

47. Respondent admitted to signing the MCAW admitted into evidence by Respondent's counsel for the Herard Loan (Tr. 194:10-195:5; Resp't Ex. 3.)

48. The MCAW submitted by Respondent listed a Mortgage-to-Income Ratio of 42.228% and a Total Payment-to-Income Ratio of 46.541%. (Gov't Ex. 1; Gov't Post-Hr'g Br. 18-19.)

49. The difference in ratios between the MCAW submitted by the Government and the MCAW submitted by Respondent is due to Respondent including rental income in the calculations. Gov't Post-Hr'g Br. 18.) Respondent's MCAW credited the borrower with $850.00 of net real estate income despite not having received credible evidence (e.g., a lease or income tax returns) that the borrower actually received the money. (Resp't Ex. 3; Tr. 199:16-206:13; Tr. 265:6-266:9.) Rather, Respondent relied on an appraisal, a Fannie Mae Form 216, and an explanation letter from the borrower. (Tr. 202:19-206:21; Resp't Ex. 19, 21, and 22.)

50. The appraisal listed rental income for the unit at $1,000, which was a figure given by the homeowner. (Tr. 200:10-16; Resp't Ex. 19.)

51. Fannie Mae Form 216 shows the expenses a homeowner incurs when renting out the property. It does not actually document the receipt of rental income. (Tr. 203:15-204:8; Resp't Ex. 21.)

52. The only reference to rental income in the explanation letter furnished by the borrower explained that, in 2006, the borrower had leased his apartment to a family member who did not pay the $1,950 per month rent payment that they verbally agreed to. (Resp't Ex. 22.)

53. Respondent's evidence regarding the amount of rental income is inconsistent, not credible, and does not verify that rental income was actually received, according to the applicable HUD guidelines.

54. The Mortgage-to-Income Ratio and the Total Payment-to-Income Ratio for both MCAWS exceeded the maximum acceptable ratios authorized by HUD. (Tr. 32:20-33:2; Tr. 195:9-10; Resp't Ex. 3.)

55. The Remarks section of Respondent's MCAW identified "Job Stability" and "Reserves After Closing" as potential compensating factors. (Resp't Ex. 3; Tr. 34:1-35:5.)

56. Government witness Peiffer testified, and Respondent conceded, that job stability is a qualifying factor and not a compensating factor. (Tr. 34:19-22; 262:7-13.)

57. The only suitable compensating factor that was documented on the MCAW by Respondent, pursuant to HUD Handbook 4155.1 REV-5, was "Reserves After Closing." HUD, MORTGAGE CREDIT ANALYSIS FOR MORTGAGE INSURANCE, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34.

58. To qualify reserves as a compensating factor, the borrower must be able to show reserves equal to three month's worth of fixed monthly expenses. HUD, Handbook 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-13(G), at 2-34.

59. A borrower's 401(k) plan may be included as cash reserves, for up to 60% of the account's value. HUD, Handbook 4155.1 REV-5, ch. 2, sec. 3, subsec. 2-10(K), at 2-28.

60. Respondent relied on the borrower's 401(k) statement that was faxed from an unknown source as evidence of "reserves" to approve the loan with available assets of $6,325.16. (Tr. 196:3-20; Resp't Exs. 3, 18.)

61. Respondent was aware that HUD requires underwriters to be able to identify the source of faxed documents relied upon during the underwriting process. (Tr. 196:21-197:2.) Respondent was also aware that guidelines require three months of reserve assets to constitute a compensating factor. (Tr. 262:13-263:8.) Therefore, based on the borrower's fixed monthly payment of $3,668.63, Respondent was aware that reserve assets in excess of $11,000 were required and needed to be documented. (Resp't Ex. 3; Tr. 263:6-11.)

62. The borrower's total cash reserves of $6,325.16 were not equivalent to three months' worth of fixed monthly expenses.

63. The borrower's Reserves After Closing do not qualify as a compensating factor.

D. The O'Neal Loan

64. The credit report for the O'Neal Loan showed that the borrower, Derrick O'Neal, had been more than 90 days late, twelve times, and over 60 days late, once, for an installment debt for child support. (Gov't Ex. 13; Tr. 91:12-16.)

65. As of the date of the credit report, the borrower was more than 120 days late with child support and the past due amount was $2,908. (Tr. 91:18-22.) The borrower's pay statements and a child support order showed that the borrower's child support obligations were being garnished from his wages. (Resp't Ex. 23, 24; Tr. 208:4-15.)

66. As of the date of the credit report, the borrower was more than 60 days delinquent on a debt payable to Summit Rent. (Gov't Ex. 13; Tr. 92:4-7.)

67. The credit report also identified paid collection accounts, unpaid collection accounts and medical payments. (Tr. 93:2-14.)

68. The borrower explained some of his derogatory credit in an explanation letter that was included in the FHA binder. (Resp't Ex. 26; Tr. 210:4-18.)

69. The credit report also included an auto loan that the borrower had paid in a timely manner for the past 12 months. (Gov't Ex. 13; Tr. 212:17-20.)

70. The FHA binder did not contain Respondent's analysis of the derogatory accounts listed on the borrower's credit report.

71. The FHA binder contained a copy of the borrower's account history for his bank account with Victoria City-County Employee Federal Credit Union. (Gov't Ex. 15; Resp't Ex. 27.)

72. The account history showed numerous Nonsufficient Fund Fees for the period from September 4, 2007 through November 6, 2007. (Gov't Ex. 15; Resp't Ex. 27; Tr. 94:15-95:2.)

73. Respondent made an assumption that the borrower may not have been aware of these fees, as his work on an offshore rig required him to be away from home for two weeks, before spending two weeks at home. (Tr. 211:2-7; 214:8-18.) However, Respondent admitted that she saw no two-week period of time during which the nonsufficient fund charges were not charged against the account, even though the borrower, as per his usual work schedule, should have been at home for approximately two two-week periods from September 4, 2007 through November 6, 2007. (Tr. 270:15-18.)

74. The account history also showed a deposit in the amount of $2,500 made on October 24, 2007. (Gov't Ex. 15; Resp't Ex. 27; Tr. 95:3-10.) There was no reference as to the source of the $2,500 on the MCAW. (Gov't Ex. 16)

75. The FHA binder contained a Gift Certification showing that the borrower's father-in-law, John H. Wormuth, provided a $3,000 gift to the borrower on November 14, 2007. (Gov't Ex. 23; Resp't Ex. 28; Tr. 129:9-130:5, 217:17-218:5.)

76. A Statement of Account for John H. Wormuth that was also included in the FHA binder showed that on October 24, 2007, a withdrawal in the amount of $2,500 was taken from Wormuth's account. (Tr. 130-6-19; Gov't Ex. 22.)

77. A photocopy of a blank check from John H. Wormuth confirmed that the Statement of Account was for his account. (Gov't Ex. 24; Resp't Ex. 29.)

78. The MCAW listed the borrower's base pay as $3,338.40 and his "other earnings (explain)" as $2,064.64. (Gov't Ex. 16; Tr. 98:12-18.)

79. The MCAW listed the borrower's total monthly income as $5,403, indicating that this was the total amount of the borrower's base pay and "other earnings." (Gov't Ex. 16; Tr. 103:1-7.)

80. The Remarks section of the MCAW did not include any explanation as to the source of the borrower's "other earnings," and no documents were attached to the MCAW. (Gov't Ex. 16; Tr. 98:22-99:5.)

81. A lender is allowed to include overtime pay in the monthly income calculation if the overtime income can be averaged for the past two years and the income is likely to continue. A period of less than two years is acceptable if the lender justifies and documents in writing the reason for using the income for qualifying purposes. HUD, Handbook 4155.1 REV-5, ch. 2, sec. 2, subsec. 2-7(A), at 2.14.

82. The Government submitted the borrower's W-2 forms for 2005 and 2006, the two years immediately preceding the loan application. Neither form listed overtime income. (Gov't Exs. 18, 19.)

83. Nothing in the FHA binder listed the borrower's overtime income for 2005 and 2006.

84. Respondent did not assert that the "other earnings" were derived from the borrower's overtime pay and did not include a written explanation claiming to average the overtime pay over eight months.

85. The monthly income of $5,403 listed on the MCAW represents the borrower's 2007 year-to-date gross income, including base pay and overtime pay but does not include the borrower's 2005 or 2006 income. (Tr. 100:11-19.)

E. The Pacheco Loan

86. In the Remarks section of the MCAW, Respondent listed the borrower's gross monthly income as $9,474.22. (Gov't Ex. 12.)

87. The FHA binder included two VOEs for the borrower. (Tr. 165:6-21.) Both VOEs were obtained on January 17, 2008, from The Work Number, an independent employment verification service. (Gov't Ex. 3; Tr. 40:10-12; Tr. 40:20.)

88. The first VOE indicated that the borrower earned $136,220.16 in 2006, or $11,351.68 monthly, while employed with Washington Mutual as a loan consultant. (Gov't Ex. 20; Resp't Ex. 4; Tr. 65:3-11.)

89. The second VOE indicated that the borrower earned a total of $81,688.81 while employed with SunTrust as a mortgage loan consultant in 2007. (Gov't Ex. 3; Tr. 40:13-18; Tr. 41:5-12.)

90. The VOE also indicated that the borrower earned $38,501.33 in 2007 while employed with Washington Mutual. (Gov't Ex. 20; Resp't Ex. 4; Tr. 65:15-17.)

91. Pacheco terminated his employment with Washington Mutual on May 29, 2007. (Tr. 66:1-3.)

92. Pacheco's total income in 2007, including income from both SunTrust and Washington Mutual, was approximately $120,000, or $10,000 monthly. (Tr. 71:6-10.)

93. The FHA binder contained two pay statements, one for the pay period ending February 15, 2008 and the other for the pay period ending December 15, 2007. (Gov't Ex. 3b, 3c; Resp't Ex. 7; Tr. 42:9-43:12.)

94. Both pay statements show that the borrower earned a gross pay of $3,000 for each two-week pay period. (Gov't Ex. 3b, 3c; Resp't Ex. 7; Tr. 42:9-43:12.) The pay statement for the period ending February 15, 2008 showed that the borrower's year-to-date gross earnings totaled $9,000. (Gov't Ex. 3b; Resp't Ex. 7; Tr. 167:5-10.)

95. The Handbook requires commission to be averaged over the previous two years. HUD, HANDBOOK REV-5 ch. 2, sec. 2, subsec. 2-7(D), at 2-15.

96. The Government states that Respondent did not adequately document the borrower's income since there was no paystub to support the $9,474.24 that Respondent used. (Notice of Suspension 3.) The paystubs indicate that Respondent earned $3,000 bi-weekly. (Gov't Ex. 3b, 3c; Resp't Ex. 7.)

97. Respondent admits that she did not document how she determined the borrower's monthly income, although she stated that she averaged his income over the years of 2006, 2007, and part of 2008. (Tr. 169: 7-9; 232:19-22; Tr. 233:1-2.) When calculating the borrower's income, Respondent placed greater weight on the borrower's prior two years' earnings and averaged those amounts. (Tr. 169:7-9.)

98. Respondent incorrectly states that the borrower earned $9,000 per month in 2008. (Tr. 231:4-9.) The borrower earned $9,000 year to date, not monthly. (*Id.*)

99. The FHA binder contained two W-2 forms and pay statements, but no signed tax returns.

100. The Handbook requires signed tax returns for the previous two years when attempting to include commission income in the borrower's income analysis. HUD, HANDBOOK REV-5 ch. 2, sec. 2, subsec. 2-7(C), at 2-15.

101. Respondent failed to adequately document her decision to approve the Pacheco loan.

F. The Santiago Loan

102. There were two MCAWs entered into evidence, one submitted by the Government (Gov't Ex. 9) and another submitted by Respondent (Resp't Ex. 10.) (Tr. 174:7-11.)

103. Respondent asserted that she did not sign or approve the MCAW submitted by the Government. (Tr. 174:12-175:6.)

104. The Government offered no evidence that the MCAW it submitted contained Respondent's true signature, other than the fact that Respondent's CHUMS ID appeared on the MCAW.

105. Respondent did not sign or approve the MCAW submitted by the Government.

106. Respondent admitted to signing the MCAW admitted into evidence by Respondent's counsel for the Santiago Loan. (Tr. 172:11-173:3; Resp't Ex. 10.)

107. The Government asserts that the loan was problematic because "the borrower's funds to go to closing were not verified." (Gov't Post-Hr'g Br. 29.) However, only the MCAW submitted by the Government, which does not contain Respondent's signature and was not approved by Respondent, indicated funds were needed to go to closing. The MCAW submitted by Respondent did not indicate funds were needed. (Gov't Ex. 9; Resp't Ex. 10.)

108. The FHA binder for the Santiago Loan included a credit report for the borrower. (Tr. 47:6-10.) The credit report bore evidence of derogatory credit, which included at least ten collection accounts. (Gov't Ex. 5; Tr. 47:16-48:6.)

109. Ten of the collection accounts were for medical collections. Respondent and Government witness Joyce Tate-Cech both testified that medical collection accounts are not required to be paid before approval of a loan. (Gov't Ex. 5; Tr. 67:6-12; Tr. 236:15-18.)

110. The remarks section of the MCAW did not include Respondent's analysis of how the borrower's negative credit was resolved. (Gov't Ex. 9; Resp't Ex. 10; Tr. 53:19-54:5; Tr. 178:22-179:2.) Rather, Respondent included, in the FHA binder, the written explanation and medical documentation submitted by the borrower to explain the borrower's derogatory credit. (Tr. 178:17-179:6; Resp't Ex. 8.)

111. The credit report also shows an open rental account "with Laura at 518-283-8400." (Gov't Ex. 5.) Respondent used the credit report and a letter from the borrower's landlord to verify the borrower's rental history. (Tr. 183:10-184:12; Gov't Ex. 5; Resp't 9; Resp't 11.)

112. The borrower's loan application, credit report, telephone certification of employment, and verification of employment showed that the borrower's property was rented from the same business that employed her. (Gov't Ex. 6; Gov't Ex. 7; Gov't Ex. 8; Resp't 9; Resp't 11; Tr. 48:16-49:8; Tr. 49:17-50:9; Tr. 50:18-51:10.) The Government asserts that this

established an "identity of interest," which required Respondent to obtain canceled checks to determine the borrower's payment history of housing obligations.

113. The HUD Handbook states that the lender "must determine the borrower's payment history of housing obligations through *either* the credit report, verification of rent directly from the landlord (with no identity-of-interest with the borrower) or verification of mortgage directly from the mortgage servicer, or through canceled checks covering the most recent 12-month period." HUD, Handbook 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3(A), at 2-6 (emphasis added).

114. Respondent verified the borrower's rental history via her credit report and thus did not need to obtain any direct verification from the borrower's landlord. (Tr. 183:14-16.)

Applicable Regulations

Under 2 C.F.R. § 180.800, HUD may debar Respondent for:

> (b) Violation of the terms of a public agreement or transaction so serious as to affect the integrity of an agency program, such as –
> (1) A willful failure to perform in accordance with the terms of one or more public agreements or transactions;
> (2) A history of failure to perform or of unsatisfactory performance of one or more public agreements or transactions; or
> (3) A willful violation of a statutory or regulatory provision or requirement applicable to a public agreement or transaction;
>
> ....
>
> (d) Any other cause of so serious or compelling a nature that it affects [Respondent's] present responsibility.

2 C.F.R. § 180.800(a)-(d) (2010). HUD has the burden of establishing the cause for debarment by a preponderance of the evidence. 2 C.F.R. § 180.855 (a). Even if a cause for debarment is determined to exist, the debarring official need not impose a sanction, and may consider the seriousness of the Respondent's acts or omissions and the mitigating or aggravating factors set forth at 2 C.F.R. §180.860 when making a decision regarding the severity of any imposed sanction. 2 C.F.R. § 180.845 (a). Once the Federal agency has established a cause for debarment, the Respondent has the burden of "demonstrating to the satisfaction of the debarring official that [he or she is] presently responsible and that debarment is not necessary." 2 C.F.R. § 180.855 (b).

For the purpose of protecting the public interest by ensuring the integrity of federal programs, the federal government only conducts business with responsible persons. 2 C.F.R. § 180.125(a). The term "responsible," as used in the context of administrative sanctions such as Limited Denials of Participation ("LDPs"), debarments, and suspensions, is a term of art that includes not only the ability to perform a contract satisfactorily, but the honesty and integrity of

the participant[1] as well. *William D. Muir and Metro Cmty. Dev. Corp.*, 00-2 BCA ¶ 31.140, HUDBCA No. 97-A-121-D15 (Nov. 6 1997) (citing 48 Comp. Gen. 769 (1969)).

Determining "responsibility" requires an assessment of the current risk that the government will be injured in the future by doing business with a respondent. (*In re: Benjamin J. Roscoe Geraldine M. Roscoe*, HUDALJ 93-2007-DB (June 26, 1995)(citing *Shane Meat Col., Inc. v. U.S. Dep't of Defense*, 800 F.2d 334, 338 (3rd Cir. 1986).) LDPs, debarments, and suspensions are serious sanctions that should only be utilized for the purposes of protecting the public interest and may not be used as punishment. 2 C.F.R. § 180.125(c).

The test for determining whether a proposed sanction is warranted is "present responsibility," although lack of present responsibility may be inferred from past acts. *Schlesinger v. Gates*, 249 F.2d 111 (D.C. Cir. 1957); *Stanko Packing Co. v. Bergland*, 489 F. Supp. 947, 949 (D.D.C. 1980)).

Discussion

I. Violations of HUD Guidelines

HUD claims that "Respondent's acts and omissions as a Direct Endorsement underwriter are cause for debarment under 2 C.F.R. §§ 180.800(b) and 180.800(d)." (Gov't Post-Hr'g Br. 32.)

Mortgages insured by the Federal Housing Administration are largely underwritten within the auspices of the Direct Endorsement Program. The program allows Direct Endorsement underwriters the freedom to assess risk factors associated with prospective homebuyers and to approve or reject those applicants without prior review by HUD officials. In short, underwriters in the Direct Endorsement Program possess the autonomy to financially obligate HUD to provide housing insurance to applicants. In so doing, Direct Endorsers act as agents for HUD. Respondent's employer, and by extension Respondent herself, were Direct Endorsers for HUD-FHA loans. 24 C.F.R. §203.5.

To minimize the risk to HUD, Direct Endorsement underwriters are required to comply with the guidelines set forth by HUD as "the minimum standard of due diligence in underwriting mortgages." 24 C.F.R. § 203.5(c)(2010). Accordingly, failure to comply with HUD guidelines for underwriting FHA insured loans is a cause for debarment, absent mitigating circumstances.

As a threshold matter, Respondent contends that the allegations contained in the Notice of Suspension are not specific enough to inform Respondent of the bases for her proposed debarment. I find that the allegations are sufficiently specific. Each alleged violation consists of a one-sentence statement of the allegedly improper act, followed by "See" and a listing of HUD documents; HUD Handbook 4155.1 REV-5 and either one or several Mortgagee Letters. Next,

[1] It is uncontested that Respondent was, at all times relevant, a participant in a HUD program as defined by 2 C.F.R. § 180.980.

the Notice lists each applicable loan and recites the alleged deficiencies in each. For example, the third charge of the Notice of Suspension reads:

> In the following transactions, you failed to document the source of funds used to close the loan and/or satisfy omitted liabilities. *See* HUD Handbook 4155.1 REV-5, Chapter 2 and Mortgagee Letters 97-26 and 00-28.
>
> (1) FHA Case No. 483-3817075: In this case, the HUD-1, dated February 25, 2008, indicated $2,838.76 was due from the borrower. The file only contained a print out from February 21, 2008, but the account was not identified with the borrower's name. Furthermore, a deposit of $1,000 was shown on February 21, 2008. The source of the $1,000 deposit was not documented or explained.
> (2) FHA Case No. 495-7749910: In this case, the file did not document the source of funds used to satisfy collection accounts totaling $2,373.52 with Colonial Finance, Summit Rental & Management Company, and Talbott, Adams, and Moore, Inc. In addition the bank printout from Victoria City Employee Federal Credit Union indicated a lump sum deposit of $2,500 on October 42, 2007, but the file failed to document the source of funds.
> (3) FHA Case No. 371-3599681: In this case, the HUD-1, dated September 9, 2006, indicated $1,521.56 was paid at closing. The file did not contain a Verification of Deposit (VOD), bank statement, or any other documentation of the source of funds needed to close.

Respondent interprets this construction to mean she has allegedly violated each listed HUD document. (Resp't Post-Hr'g Br. 13, ¶ 62.) As Respondent notes, many of the identified Mortgagee Letters do not apply to the facts of a particular listed case, or the applicable language from the Mortgagee Letter was incorporated into the HUD Handbook before a particular loan was approved. (*See generally* Resp't Post-Hr'g Br.)

Government witness Joyce Tate-Cech testified that the references in the Notice "refer to all or some of the loans that fall underneath that paragraph." (Tr. 109:18-19.) She went on to explain that "[W]hat we do in the opening paragraphs is we list all of the regulations, all the Mortgagee Letters that could or could not apply to the various cases underneath that opening paragraph." (Tr. 110:19-111:1.)

The exclusive use of the signal "See" in each allegation supports the Government's argument that the allegations are to be broadly applied to each listed loan. (*Id.*) "See" is used to "introduce an authority that clearly supports, but does not directly state, the proposition." *The Bluebook*, 18th ed., p. 4, B4.2. While it is widely understood in the legal profession that a citation beginning with the signal "See" contemplates some degree of additional investigation on the part of the reader - the exclusive use of such a signal in a Notice of Suspension can lead to confusion among lay persons as to which specific citation or provision is being referred to. However, in all allegations contained in the Notice the opening sentence uses direct language from the relevant provisions, giving Respondent a clear indication of what is being alleged and

which document provides the critical language. Additionally, the citations are brief and narrowly focused, allowing Respondent to quickly ascertain whether a given citation applies to a specific loan.

While the Government might have simplified matters by specifying the precise provision that was violated for each loan, I find the language of the Notice to be reasonably specific to apprise Respondent of the factual and legal basis for each allegation. I further note that Respondent has been represented by able counsel in this case who has no doubt been available to assist Respondent in understanding the charges contained in the Notice of Suspension.

Respondent also argues that several of the Mortgagee Letters are no longer actionable because they have been incorporated into HUD Handbook 4155.1 REV-5. This is immaterial, because the Handbook was included in the citation for each allegation. The incorporation of the Mortgagee Letters, therefore, had no impact upon the validity of the language derived from the Mortgagee Letters or the allegations contained in the Notice of Suspension. Respondent further asserts that the inclusion of inapplicable or previously incorporated Mortgagee Letters was "deliberately designed to falsely inflate the charges against Mrs. O'Halloran." (Resp't Post-Hr'g Br. 5, ¶ 28.) This claim is not supported by evidence and is dismissed as immaterial, since the Court's inquiry is one of determining the gravity of Respondent's actions, in fact, as opposed to counting the number of legal violations that may or may not have occurred.

A. The Bilyeu Loan

The Notice of Suspension states that Respondent was the Direct Endorsement underwriter for the Bilyeu Loan, FHA Case Number 483-3817075. At the hearing, however, the Government's counsel addressed alleged violations of five loans, omitting the Bilyeu Loan. Respondent maintains that she did not sign the Mortgage Credit Analysis Worksheet ("MCAW") for the Bilyeu Loan, although Respondent's CHUMS ID, K416, appears on the MCAW. (Resp't Post-Hr'g Br. 4.) The MCAW is the primary document containing an underwriter's analysis of the credit worthiness of an applicant. (HUD, Handbook 4155.1 REV-5, ch. 3, 3-6.) The Government's witness, Patricia Peiffer, stated during the hearing that the CHUMS ID is unique to an individual underwriter. (Tr. 32:7-9.) However, she admitted on cross examination that the signature on the MCAW did not belong to Respondent, and that the name on the signature line appears instead to be "Ellen." (Tr. 61:18-62:6.) Respondent testified that the signature on the contested MCAW in fact belongs to "Ellen Colomvotos," whom she identified as another underwriter at Lend America. (Tr. 219:15-220:4.)

The Government did not present any evidence to refute Respondent's contention that she did not sign the MCAW. (Gov't Post-Hr'g Br. 14.) Further, the Government did not state that Respondent signed the Bilyeu MCAW and does not list any violation of the Bilyeu Loan among its proposed Findings of Fact in its Post-Hearing Brief. (Gov't Post-Hr'g Br. 13.) It appears that the Government does not seek a finding of fact that Respondent was responsible for this loan at all.

Because the Government has failed to present any evidence that Respondent underwrote or approved the Bilyeu Loan, and the Government's own witness conceded that Respondent did

not sign the MCAW, this Court finds that any allegations contained in the Notice of Suspension regarding the Bilyeu Loan should be dismissed. As Respondent's counsel recognized, the Government did not attempt to prove during the hearing that the Bilyeu Loan was improperly underwritten. Instead, the Government merely established that Respondent's CHUMS ID appears on the MCAW, a fact that is not in dispute.[2] Accordingly, the allegations associated with the Bilyeu Loan should be dismissed in their entirety.

B. The Crump Loan

The Government alleges that Respondent approved the Crump Loan despite the presence of multiple credit obligations that had been at least 30 days past due in the previous 12 months, in violation of Mortgagee Letter 05-43. (Gov't Post-Hr'g Br. 14.) Of specific importance, the Government states that the borrower's mortgage payment was more than one month late in February, July, August, September, and December of 2006. (*Id.*, at 15.) Further, the Government states that the borrower's explanation for his derogatory credit did not sufficiently explain the late mortgage payments, in violation of HUD Handbook 4155.1 REV-5, chs. 2, 3. (*Id.*)

Mortgagee Letter 05-43 states that, to be eligible for a cash-out refinance, "the borrower must have made all of his/her mortgage payments within the month due for the previous 12 months." (*Id.*, at 15; HUD, Mortgagee Letter 05-43, dated Oct. 31, 2005.) Respondent maintains that the borrower's recurring medical illness created a hardship, preventing him from making timely payments. (Resp't Post-Hr'g Br. 6.) However, she asserts that Crump's "overall payment history on the mortgage was satisfactory, and was rated by the lender for ninety-nine months. Hence, the overall good payment history on the mortgage outweighed the isolated late payments that were clearly the result of medical hardship." (*Id.* at 7; Tr. 187-92.) After the borrower's December 2006 delinquency, Respondent states that Crump "caught-up for at least seven months," and any late payments on his credit report were a result of his illness. (Resp't Post-Hr'g Br. 7.)

Respondent further contends that Mortgagee Letter 05-43 is inapplicable to the Crump Loan because "this Mortgagee Letter applies to cash-out refinances with loan to value ratios over 85%. The loan to value for this loan was only 80.44%." (Resp't Post-Hr'g Br. 5.) The Government does not specifically address this issue, but simply states that Mortgagee Letter 05-43 applies and requires the borrower to have made all of his mortgage payments within the month due for the previous 12 months. (Gov't Post-Hr'g Br. 15.)

As a threshold matter, I find that Mortgagee Letter 05-43 is applicable to the Crump Loan. Mortgagee Letter 05-43 states that "FHA will insure a cash-out refinance of up to **95%** of the appraiser's estimate of value." Mortgagee Letter 05-43, dated October 31, 2005. The Letter does not state, as Respondent argues, that its requirements only apply to loans with value ratios of more than 85%.

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[2] Respondent has contested the authenticity of her signature on two other MCAWs, relating to the Herard and Santiago loans. (Tr. 194:20-21; 175:3-4.) The fact that the Government did not present any evidence to prove that Respondent signed either of those MCAWs, as they did not provide evidence in support of Respondent's signing the Bilyeu MCAW, strongly supports Respondent's argument that the mere presence of her CHUMS ID is not persuasive evidence that she signed the MCAW or approved the loan.

According to the credit report contained in the FHA binder, the borrower was more than 30 days late paying his mortgage for February, July, August, September, and December of 2006. (Gov't Ex. 10; Resp't Ex. 17.) Because three of these late payments occurred within 12 months of August 15, 2007, the date Respondent approved Crump's loan, the borrower failed to meet the eligibility requirement for receiving a cash-out refinance. (Gov't Post-Hr'g Br. 4.) This is a clear violation of HUD guidelines.

As stated, 12 consecutive months of on-time mortgage payments is an initial eligibility requirement for a cash-out refinance. Respondent's argument that the borrower's mortgage had been current for approximately seven months since the last late payment is therefore inadequate to justify the borrower's failure to meet the eligibility requirement. (Gov't Ex. 10; Resp't Ex. 17.) Similarly, Respondent's reference to the borrower's medical explanation for the late payments on his mortgage carries no weight. (Resp't Ex. 13.) Mortgagee Letter 05-43 does not provide an exception for financial hardships. Simply put, either the borrower has been current on his mortgage for the past 12 months, or he is not eligible for a cash-out refinance.

The Government further alleges that Respondent failed to provide a sufficient written explanation from the borrower regarding collection accounts appearing on the borrower's credit report. (Gov't Post-Hr'g Br. 16.) Specifically, the Government refers to five accounts: (1) an auto loan from the CT Labor Department Federal Credit Union, (2) an installment account with the CT Labor Department Federal Credit Union, (3) a Sprint collection account, (4) a Comcast collection account, and (5) an HSBC collection account charge-off. (*Id.* at 15-16.)

In response, Respondent states that the "documents in the Crump file from the borrower's creditors state [that] the loans were in good standing and all of the payments had been made by the borrower's daughter." (Resp't Post-Hr'g Br. 6.) Further, Respondent argues that "Crump had favorable credit" and that he "had no fewer than nine satisfactory accounts on his credit with long term satisfactory histories, and his FICO scores of 646, 678, and 659 also confirmed the borrower was an acceptable credit risk." (Resp't Post-Hr'g Br. 6.) In addition, Respondent states that any delinquent payments on the credit report were due to the borrower's illness. (*Id.* at 7)

Even assuming, *arguendo*, that the borrower met the initial eligibility requirement, an analysis of the borrower's credit report should still have prevented approval of this loan.

The HUD Handbook states that "[p]ast credit performance serves as the most useful guide in determining a borrower's attitude toward credit obligations and predicting a borrower's future actions." HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3, at 2-5. Underwriters are instructed to "examine the overall pattern of credit behavior, rather than isolated occurrences of unsatisfactory or slow payments." *Id.* A borrower with a credit history that reflects a period of financial difficulty may still be approved if the borrower has "maintained a good payment record for a considerable time period since the difficulty." *Id.* Underwriters are required to "document their analysis as to whether the late payments were based on a disregard for financial obligations, an inability to manage debt, or factors beyond the control of the borrower." *Id.*

Respondent incorrectly states that "documents in the Crump file from the borrower's creditors state the loans were in good standing and all of the payments had been made by the borrower's daughter, Lashanda Crump." (Resp't Post-Hr'g Br. 6.) Respondent's Exhibit 12 contains a letter from the Operations Manager at CT Labor Department Federal Credit Union, stating that, "[p]resently the loan account is in good standing and all the payments are being made by Lashandra not by Richard." (Resp't Ex. 12.) However, the credit report indicates that the borrower has two accounts with CT Labor Department Federal Credit Union. (Resp't Ex. 17.) The letter from the Federal Credit Union does not state which of these two loan accounts was in "good standing," as noted by the Operations Manager. (*Id.*) Moreover, the borrower's daughter's statements of account with the Federal Credit Union indicate that both accounts incurred late payments in October and November 2006. (Resp't Ex. 14.)

Respondent testified that she "did not really feel it was necessary to hold [the borrower] responsible" for the late payments on the loan, since the borrower's daughter had been making all payments, including late fees. The fact remains, however, that the borrower was a co-signer and, was, therefore, ultimately responsible for the loan. (Tr. 187:10-20.) Accordingly, Respondent was required to "hold [the borrower] responsible" for any delinquent activity associated with the loan. I find that Respondent violated HUD Handbook Chapter 2, Subsection 2-3 by failing to adequately explain the late payments on the Federal Credit Union accounts.

Aside from the Federal Credit Union accounts, the borrower's credit report also indicates three collection accounts and a GEMB/Wal-Mart account with late payments. (Resp't Ex. 17.) However, the credit report indicates that the last late payment on the GEMB/Wal-Mart account occurred in September of 2003, more than two years before this loan. (*Id.*) The HUD Handbook states:

> While minor derogatory information occurring two or more years in the past does not require explanation, major indications of derogatory credit — including judgments, collections, and any other recent credit problems — require sufficient written explanation from the borrower.

HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3, at 2-5. Therefore, I find that Respondent was not obligated to obtain a written explanation of this minor derogatory account.

I further find that the period of time that the borrower was unable to work due to his injury was generally consistent with his late payments on his Sprint, Comcast, and HSBC accounts. (Resp't Ex. 17.) The borrower's explanation was supported by medical records, as well as a Family and Medical Leave Act approval. (Resp't Exs. 13, 15, 16.) Respondent, therefore, appropriately explained these accounts and did not violate HUD guidelines.

Additionally, Respondent claims there were "numerous compensating factors reflected on the credit analysis." (Resp't Post-Hr'g Br. 6.) Respondent listed "positive loan to value ratio," "job stability," "long term ownership," and "minimal debt" as compensating factors in the Remarks section on the MCAW.

Both Government witnesses, Joyce Tate-Cech and Patricia Peiffer, separately testified, and Respondent subsequently agreed, that "job stability" is a qualifying factor for this type of loan, and so cannot be considered a compensating factor. (Tr. 35:19-22; 88:18-22; 262:10-12.); HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34; ch. 2, sec. 2, subsec. 2-6, at 2-13. The HUD Handbook supports this conclusion. Similarly, Tate-Cech stated that long-term ownership is not a compensating factor, and her testimony also finds support in the HUD Handbook. (Tr. 89:1-3); *see* HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34.

"Minimal debt" and "positive loan to value ratio" are compensating factors. HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34. However, Tate-Cech explained that in order for "minimal debt" to be a compensating factor, Respondent would have had to explain and justify how the borrower has more of his income to apply toward the mortgage payment due to his lack of significant outstanding debt. (Tr. 89:7-11); HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13, at 2-33 to 2-34. While Tate-Cech asserts that Respondent should have explained and justified the minimal debt, Respondent did provide the borrower's credit report in the file, which showed nine accounts that had been paid in full. (Resp't Ex. 17.) Further, when the loan settled on August 15, 2007, the borrower's 2006 taxes, a judgment to Middlesex, and a payment to the tax collector of Middletown were all paid from the borrower's funds. (Tr. 86:7-22; Gov't Ex. 11.) Neither the Government nor Tate-Cech indicated that Respondent's documentation of "positive loan to value ratio" as a compensating factor was insufficient. (*Id.*)

The Government also claims that late charges on the borrower's payoff documents were not explained. However, no evidence supporting this claim was presented at the hearing or addressed in the Government's Post-Hearing Brief. Instead, the Government claimed that the borrower's credit report showed collection accounts, which were not explained. (Gov't Post-Hr'g Br. 15-16.) This claim was not included in the Notice and therefore shall not now be considered as a cause for debarment.

C. The Herard Loan

The Government alleges that Respondent approved the Herard loan "with a debt to income ratio that exceeded HUD guidelines without significant compensating factors." (Resp't Ex. 1), in violation of HUD HANDBOOK 4155.1 REV-5, Chapter 2. Section 5 of the Handbook states that HUD guidelines regarding debt-to-income ratios "can be exceeded when significant compensating factors exist." HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-12, at 2-33. The Handbook requires the lender to compute two ratios: the Mortgage Payment Expense to Effective Income Ratio ("Mortgage-to-Income Ratio") and the Total Fixed Payment to Effective Income Ratio ("The Total Payment-to-Income Ratio"). *Id.*

A Mortgage-to-Income Ratio of 31% is considered acceptable. *Id.* "A ratio exceeding 31 percent may be acceptable only if significant compensating factors are documented and are recorded on the [MCAW]." *Id.* The Handbook considers 43% to be the appropriate benchmark for the Total Payment-to-Income Ratio. Any ratio exceeding 43% must comply with the same procedure stated above for the Mortgage-to-Income Ratio. *Id.* If compensating factors are

considered, they must be recorded in the Remarks section of the MCAW and be supported by documentation. HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-13, at 2-33, 34.

Two MCAWS have been entered into evidence for Herard. (Tr. 194:15-195:5; Gov't Ex. 1; Resp't Ex. 3.) Both MCAWs contain Respondent's CHUMS ID and both bear a signature that appears to be Respondent's. However, Respondent contends that she did not sign Government's Exhibit 1. (Tr. 194:20-21.) Respondent does acknowledge signing Respondent's Exhibit 3. (Tr. 195:5.)

The MCAW submitted by the Government ("Government's Herard MCAW") lists the borrower's gross monthly income at $7,032.59; the Mortgage-to-Income Ratio at 47.331%; and the Total Payment-to-Income Ratio at 52.166%. (Gov't Ex. 1, Boxes 11f, 14b, 14c.) Both ratios exceed HUD guidelines. The Remarks section of Government's Herard MCAW states:

> 30 year fixed fi/fa fico 482 537 489 b2 563 539 557
> JOB STABILITY
> RESERVES AFTER CLOSING
> Using subject rental income as a compensating factor reduces ratios to 42/46
> Total debt payments being reduced
> Currently living at a higher debt ratio

(Gov't Ex. 1.)

The MCAW submitted by Respondent ("Respondent's Herard MCAW") lists the borrower's gross monthly income at $7,882.59 and includes $850 in monthly net income from real estate. (Resp't Ex. 3, Boxes 11f, 11e.) The MCAW lists the Mortgage-to-Income Ratio at 42.228% and the Total Payment-to-Income Ratio at 46.541%. (*Id.*, Boxes 14b, 14c.) Both ratios exceed HUD guidelines. The Remarks section of Respondent's Herard MCAW repeats the first three lines of the Government's Herard MCAW, but does not refer to rental income, reduced debt payments, or a higher debt ratio.[3]

Respondent stated, under oath that the signature on the Herard MCAW was not hers, thus creating a question of fact as to whether Respondent actually approved the Herard Loan. The Government must therefore present evidence (ordinarily, that of a hand-writing expert or other evidence), tending to show that the MCAW bears Respondent's true signature. As with the Bilyeu Loan, the Government has offered no such proof, other than the fact that the MCAW contains Respondent's CHUMS ID. The discrepancy between the CHUMS ID and the corresponding underwriter's signature on the Bilyeu Loan's MCAW indicates, however, that the presence of the CHUMS ID on a MCAW is not persuasive evidence that the underwriter associated with that ID in fact approved that loan. I therefore find that the Government has not

[3] Respondent's Post-Hearing Brief states, "the correct MCAW for the Herard loan, Respondent's 3, further states that compensating factors include: job stability, the borrower's debt payment reduction, and the borrower's debt ratio reduction." (Resp't Post-Hr'g Br. 10, ¶ 53.) Respondent's Exhibit 3 does not include these compensating factors. Rather, these factors are present on Government's Exhibit 1, which Respondent testified, and this Court found, was not the MCAW signed by Respondent.

shown that Respondent signed the Government's Herard MCAW. Accordingly, that MCAW, without more, is not found to be credible, on the Herard Loan must be based on information contained in the MCAW submitted by Respondent.

Because both ratios in Respondent's MCAW exceeded the HUD guidelines, Respondent could only approve the loan by documenting significant compensating factors. Respondent acknowledged during the hearing that she identified only "job stability" and "reserves after closing" as compensating factors. (Tr. 262:4-6.) As previously discussed, the Government's witnesses testified, and Respondent conceded, that job stability is not a valid compensating factor. (Tr. 35:19-22; 88:18-22; 262:10-12.)

"Reserves after closing" is a HUD-approved compensating factor, but only if the underwriter can document enough reserves to cover three months' worth of the borrower's total fixed payment. HUD, HANDBOOK 4155.1 REV-5 ch. 2, sec. 5, subsec. 2-13(G), at 2-34; *see also id.* subsec. 2-10(K), at 2-28 (stating that assets from 401(k)'s may be included in the underwriting analysis up to only *60 percent* of value). Respondent's MCAW lists the borrower's fixed payment as $3,668.63, meaning reserves of $11,005.89 would be required to qualify as a suitable compensating factor. (Resp't Ex. 3, Box 13j.)

As evidence of the borrower's reserves, Respondent submitted a faxed copy of the borrower's 401(k) statement, which listed $10,541.93 as a vested balance. (Resp't Ex. 18.) The HUD Handbook allows only 60% of a 401(k)'s value to be included as reserve income due to the severe tax ramifications of early withdrawal. HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 5, subsec. 2-10(K), at 2-28. Respondent, therefore, credited borrower with only $6,324.60 from his 401(k) Plan. (Tr. 263:12-13.) This figure falls well below the necessary reserve amount.

Additionally, the Government argues that the 401(k) statement is not credible because it was sent from an unverified source. The HUD Handbook states that the lender is accountable for determining the authenticity of faxed documents by examining the information included in the headers and footers of the document. HUD, HANDBOOK 4155.1 REV-5, ch. 3, sec. 1, subsec. 3-1, at 3-1. Respondent acknowledged that she should have verified the source of the fax, and admitted she did not do so. (Tr. 198:3-10.) Yet, Respondent argues that she was "reasonable in using the 401(k) Plan to support her underwriting decision" (Resp't Post-Hr'g Br. 10, ¶ 50) because "[i]t has what you would normally see on a 401(k) statement. I saw them all the time. ... The borrower's name is on it .. it tells you the beginning balance, the ending balance ... it tells you the time frame, who it's from. Unfortunately, it came from a fax machine that didn't have their header programmed, basically." (Tr. 198:18-199:4.)

Respondent's testimony as to her general familiarity with such documents, and recognition that the document in question had all of the usual and pertinent information she would expect to see on a 401(k) statement, may mitigate the seriousness of Respondent's failure to determine the authenticity of the 401(k).[4] However, it fails to ameliorate the fact that the assets were insufficient to constitute "substantial cash reserves" as required by the HUD

[4] Respondent's Post-Hearing Brief argues that "HUD has failed to offer any evidence at all that the 401k Plan was not accurate, true, or correct." (Resp't Post-Hr'g Br. 10, ¶ 50.) This is immaterial, as HUD's argument centered on the verification of the source of the 401k Plan, not on its accuracy.

Handbook. Accordingly, I find that Respondent's approval of the Herard loan with debt-to-income ratios that exceeded HUD guidelines and lack of significant compensating factors constitutes a violation of the HUD Handbook.

The Government further alleges that there was no documentation to support Respondent's inclusion of the borrower's rental income in Respondent's MCAW. (Gov't Ex. 1.) The HUD Handbook requires lenders to document stable rental income if rent received for properties owned by the borrower is to be used as income. HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 2, subsec. 2-7(M), at 2-17. Stability of rental income may be determined by a current lease, an agreement to lease, a rental history over the previous 24 months that is free of unexplained gaps greater than three months, or tax returns. *Id.*

Respondent stated that she could not obtain a lease for the rental unit because it had been rented on a month-to-month basis, for which a lease is not required. (Tr. 266:3-5.) She also acknowledged that she did not request cancelled checks or receipts from the borrower documenting his receipt of rent. (Tr. 265:6-18.) Respondent further acknowledged that "under normal circumstances" she "would have gotten the tax returns or something else." (Tr. 265:22-266:2.) In this case, she declined to request tax returns because the unit had been rented by a member of the borrower's family. (*Id.*, at 266:2-3.)

As evidence of the borrower's rental income, Respondent instead submitted an appraisal report indicating a month-to-month tenancy with a monthly rent of $1,000. (Resp't Ex. 19.) The rent figure was provided by the borrower, and Respondent stated she did not have any reason to doubt its accuracy. (Tr. 200:16-21.) Respondent also submitted the borrower's loan application, which listed the monthly rent at $850, the same figure Respondent indicated on her MCAW as the borrower's rental income. (Resp't Ex. 20; Resp't Ex. 3, Box 11e.)

Finally, Respondent submitted a separate appraisal form, the Fannie Mae Small Residential Income Property Appraisal and Operating Income Analysis ("Form 216")(Resp't Ex. 21.) The form "tells you the expenses in relationship to the rent." (Tr. 203: 15-16.) As Respondent testified, Form 216 only shows the expenses of the rent, it "is not a document to show its receipt." (Tr. 204:1-2.) Indeed, when Respondent was asked on direct examination whether Form 216 documents the receipt of rental income, she replied "No." (Tr. 203, 17-19.) In light of this testimony, Respondent's statement in her Post-Hearing Brief that the Form 216 "fully documented the receipt of rental income for the subject property's other unit, thus verifying the rental income," (Resp't Post-Hr'g Br. 10, ¶ 52), is highly suspect, at best, and casts a pall of discredit upon Respondent's legal argument.

Respondent's exhibits 19 and 21 tend to show that the borrower had a tenant. However, neither document shows that the borrower actually received rental income from the tenant. In fact, a letter written by the borrower and used by the Respondent to verify rental income stated that the family member/tenant had failed to fulfill his obligation to pay $1,950 per month in rent. Despite Respondent's testimony that the family member eventually left and the borrower found a new tenant who did pay the rent, documentation to support the receipt of rental income from either tenant was never produced in the appraisal or elsewhere in the record of this case. (Tr. 206:4-13.

Because Respondent did not utilize her admitted best options[5] to verify rental income, did not resolve the inconsistent rental figures, and did not seek any independent verification of the borrower's rental claim, I find that Respondent's documentary evidence is insufficient to prove the claimed rental income. Therefore, Respondent's decision to include the borrower's rental income on the MCAW constituted a violation of the HUD Handbook.

D. The O'Neal Loan

The Government alleges that Respondent's approval of the loan for Derrick O'Neal violated HUD Handbook 4155.1 REV-5 and Mortgagee Letter 00-28. (Gov't Post-Hr'g Br. 21.) Specifically, the Government charges that Respondent approved the loan without documenting how she determined the borrower's monthly income, without "adequate documentation that the borrower was able to manage his financial affairs responsibly," and without adequate explanation for the borrower's derogatory credit. (*Id.*) The Government further alleges that Respondent failed to investigate and identify the source of funds used to pay the borrower's collection accounts. (Notice of Suspension, at 3.)

HUD Handbook 4155.1 REV-5, Section 2 states that "[T]he anticipated amount of income, and the likelihood of its continuance, must be established to determine a borrower's capacity to repay mortgage debt." HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 2, at 2-13. The lender *must* verify the borrower's employment for the two most recent full years. *Id.* (emphasis added). In most cases, income is limited to salary or wages; however, overtime can be included if the lender can deduce an average overtime amount for the previous two years. *Id.*, at 2-14.

The borrower's pay statement for the period ending August 31, 2007 indicated "Regular Wages" of $770.40 and "Hourly Overtime" of $1,271.15. (Gov't Ex. 17; Resp't Ex. 23.) The gross "Year to Date" earnings stated the borrower had earned $43,224.80 up to August 31, 2007. (Gov't Ex. 17; Resp't Ex. 23.) On the MCAW for the loan, Respondent listed the borrower's monthly base pay at $3,338.40 and "Borrower's Other Earnings" at $2,064.60, for a total monthly income of $5,403. (Gov't Ex. 16, at Boxes 13a, 13b, and 13f.) The word "explain" appears in parentheses after "Borrower's Other Earnings" in Box 13b of the MCAW's form instructions. (*Id.*) It is undisputed that Respondent did not attach an explanation of the monthly income computation to the MCAW and did not offer an explanation in the Remarks section. A Government witness testified that Respondent appeared to arrive at the monthly income figure by dividing the borrower's year-to-date earnings by eight, the number of months already elapsed in the year. (Tr. 102:2-15.) The witness also stated that she could not tell from the MCAW how Respondent derived the monthly base pay versus the "Other Earnings" pay. (*Id.* at 102:22.)

The Government asserts that Respondent incorrectly calculated O'Neal's base pay. (Gov't Post-Hr'g Br. 22.) Respondent testified that O'Neal, who worked on an offshore oil rig, had a work schedule of two weeks on and two weeks off. (Tr. 270:2.) O'Neal's credit union statement showed pay deposits for the first two weeks of September and October, 2007, but none for the second two weeks of either month. (Gov't Ex. 15; Resp't Ex. 27.) The Government

[5] On cross-examination, Government's counsel asked: "So really the best option could have been receipts or cancelled checks, right, practically speaking?" Respondent replied: "Yes." (Tr. 266:6-9.)

therefore concludes that "based on Respondent's testimony and the borrower's account statement, the borrower worked 26 out of 52 weeks per year." (Gov't Post-Hr'g Br. 22.) With a weekly regular wage of $770.40, O'Neal should thus have earned regular wages of $1,669.20 per month. (*Id.*) The $3,338.40 listed under Box 13a on the MCAW is exactly double this amount.

Additionally, the Government argues that the borrower's W-2 statements for 2005 and 2006 do not support Respondent's calculation of $2,064.60 in "Other Earnings," even assuming those earnings represent overtime pay. The 2005 statement listed his total wages as $26,517.15, and his 2006 statement listed total wages of $45,393.51. (Gov't Ex. 18, 19.) Neither W-2 identifies overtime earnings. (*Id.*) There is thus nothing in the file that would allow Respondent to deduce the borrower's average overtime income over the preceding two years.

Respondent did not offer any evidence during the hearing or in her exhibits to explain her computation of the borrower's base pay. Respondent's Post-Hearing Brief instead contends that the borrower's compensation "does not fit with a rote calculation," due to his unusual work schedule. (Resp't Post-Hr'g Br. 18, ¶ 82.) Citing the significant increase in the borrower's income between 2005 and 2006, as evidenced by his W-2 statements, Respondent argues that the borrower's 2007 earnings suggested a similarly large increase and so "using anything less than what [O'Neal] was currently earning would not have been appropriate." (*Id.*) Respondent further claims that "4155.1 REV-5 does not require a two-year average and allows underwriters to use shorter average periods when the underwriter feels it is appropriate and documents in the case file support the decision." (*Id.*)

The Court finds Respondent's argument on this point to be without basis. As excerpted above, HUD Handbook 4155.1 REV-5 unambiguously states that the lender *must* verify employment for the most recent two full years. More importantly, the section of the Handbook upon which Respondent appears to base her argument clearly speaks only to the computation of overtime and bonus income. HUD, HANDBOOK REV-5 ch. 2, sec. 2, subsec. 2-7(A), at 2-14. A borrower's base salary or wages are objectively verifiable for any given year, and so would not need to be averaged. This section therefore cannot plausibly be read to apply to a borrower's base pay, as argued by Respondent.

Because Respondent has not offered any credible explanation for her computation of the borrower's monthly income, I find that she has violated HUD Handbook 4155.1 REV-5 in this instance, as well.

The Government also alleges that Respondent did not sufficiently investigate or explain the borrower's derogatory credit before approving the loan. The borrower's credit report showed he had been more than 90 days late on his child support payments 12 times in the year immediately prior to closing this loan, and more than 150 days late once during that period. (Tr. 92:11-16; Gov't Ex. 13.) The credit report also showed several paid and unpaid collection accounts. (Tr. 93:4-14.) Additionally, between September 4, 2007, and November 6, 2007, the borrower's Victoria City Employee Federal Credit Union ("VCEFCU") account incurred $1,075 dollars in Non-Sufficient Fund fees ("NSF fees"), comprised of 43 separate $25 penalty charges. (Gov't Post-Hr'g Br. 21.)

Section 2-3 of the HUD Handbook requires the documentation of strong compensating factors when approving a loan with judgments or delinquent accounts. HUD HANDBOOK 4155.1 REV-5, Sec. 1, Subsec. 2-3, 2-5. The Handbook also states that, when delinquent accounts are present, the lender "must document their analysis as to whether the late payments were based on a disregard for financial obligations, an inability to manage debt, or factors beyond the control of the borrower, including delayed mail delivery or disputes with creditors."[6] (*Id.*)

Respondent offered several documents as evidence of compensating factors, including pay statements and a Notice of Administrative Writ of Withholding showing that the child support payments were being paid out of the borrower's wages; an explanation letter from the borrower; and a printout of the borrower's VCEFCU account history. (Resp't Exs. 23, 24, 26, 27.)

Respondent's documentation shows that child support payments were being garnished from the borrower's paycheck. (Resp't Exs. 23, 24; Tr. 209:4-10.) Respondent interpreted the garnishment as evidence that the deficiency had been, or was being, resolved. (Tr. 209:4-10.) However, neither the garnishment nor the borrower's written explanation address or explain the borrower's previous failures to make child support payments. (Gov't Post-Hr'g Br. 24 ¶ 11.) Respondent agreed that the borrower had a history of being late with his child support payments (Tr. 208:19), but neglected to provide the necessary analysis as to the reason for his delinquent payments. Indeed, she stated during cross-examination that she did not recall investigating why a court-ordered wage garnishment was necessary to secure child support payments from the borrower, who had been gainfully employed for at least two years. (Tr. 269.)

The mere existence of a garnishment should have prompted Respondent to inquire into the borrower's attitude toward credit obligations, which is the stated purpose of the requirements set forth in Handbook Section 2-3. The omission of any mention of the delinquent child support payments in the borrower's written explanation should have prompted further inquiry. Respondent's failure to act on these warning signs — or even to recognize them as such — is a serious dereliction of her duties.

Additionally, the borrower's explanation only addressed three of the five delinquent accounts on the borrower's credit report. However, Respondent testified that, "there was additional paperwork to show letters from the companies that he had satisfied these accounts. All the accounts should have been either current or paid." (Resp't Exs. 25, 26; Tr. 211:17-20.) This additional documentation was never produced.

Notably, the borrower takes no responsibility for the three delinquent accounts addressed in the explanation letter. Instead, he blamed his mother,[7] whom he had entrusted to handle his

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[6] Respondent's Post-Hearing Brief asserts that the borrower "encountered delayed mail" as a result of his divorce. (Resp't Post-Hr'g Br. 16, ¶ 77.)(citing Resp't Ex. 26.) The record bears no evidence of this claim, and Respondent later argues only that "it is reasonable to believe that relocation would result in delayed mail." (Resp't Post-Hr'g Br. 17-18, ¶81.) Nevertheless, Respondent did not document a mail delay, as required by the Handbook. This claimed compensating factor therefore remains unsubstantiated.

[7] As the Government notes, there is some ambiguity as to whether the borrower's mother or his mother-in-law was in control of his accounts during this period. The explanation letter identifies his mother, while Respondent, in referring to the letter, repeatedly identifies the woman as his "ex-wife's mother." This Court will rely on the

finances. (Resp't Ex. 26.) As evidence of his current reliability, the letter states "[N]ow that I have re-married I no longer depend on help from my Mother and my finances are handled by my wife ... whom [sic] is more responsible in caring for this." (*Id.*) The Government correctly questions how the borrower's reliance on his wife to handle his financial affairs can be interpreted as evidence that he is capable of handling his own finances. (Gov't Post-Hr'g Br. 23.) Nevertheless, Respondent testified that she was satisfied that the borrower was a good credit risk and that he had satisfactorily explained the derogatory credit report.

Respondent also failed to produce any documentation that explained the NSF fees the borrower incurred on his VCEFCU account. Instead, Respondent testified that "it appeared on the statement that the NSF fees were always the results of very small withdrawals, possibly someone going with a debit card or something to the store while he was on the rig." (Tr. 214:12-16; Resp't Ex. 27.) The HUD Handbook states that:

> When standard documentation does not provide enough information to support [the lender's decision to approve the mortgage loan], the lender must provide additional explanatory statements, consistent with other information in the application to clarify or to supplement the documentation submitted by the borrower.

HUD, HANDBOOK 4155.1 REV-5 ch. 3, sec. 1, subsec. 3-1, at 3-1.

Respondent's testimony with regard to the NSF fees were her own assumptions, and were not supported by any documentation in the FHA binder. For example, she suggests that the NSF fees were the fault of the borrower's financially irresponsible then-wife and occurred while the borrower was working on the offshore oil rig "without any access to a bank." (Resp't Post-Hr'g Br. 16, ¶ 78.) However, the fees were incurred consistently over a two-month period. As Respondent has admitted, the borrower was only on the rig for two weeks at a time. Presumably then, he must have had access to his account for the other two weeks each month. In any case, additional documentation should have been sought to ascertain the circumstances surrounding the derogatory credit information.

I find that Respondent's failure to obtain sufficient explanation from the borrower for his derogatory credit and to provide additional explanatory statements to clarify her decision to approve the O'Neal loan constitute violations of the Handbook.

The Government next claims that Respondent "failed to document the source of funds used to close the loan and/or satisfy omitted liabilities." (Resp't Ex. 1.) The HUD Handbook requires that "[a]ll funds for the borrower's investment in the property must be verified and documented." HUD, HANDBOOK 4155.1 REV-5, ch. 2, sec. 3, subsec. 2-10, 2-24. If there is a large increase in the borrower's checking or savings account, the underwriter must obtain a credible explanation of the source of those funds, regardless of their purpose. *Id.*

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borrower's explanation letter because no documentary evidence exists to show that the woman who oversaw his finances was actually his mother-in-law.

Specifically, the Government alleges that:

> [T]he file did not document the source of funds used to satisfy collection accounts totaling $2,373.52 with Colonial Finance, Summit Rental & Management Company, and Talbott, Adams, and Moore, Inc. In addition the bank printout from [VCEFCU] indicated a lump sum deposit of $2,500 on October 24, 2007, but the file failed to document the source of funds.

(Resp't Ex. 1.)

Respondent testified that "the balance that was in [the borrower's] account on November 6 is what would have been indicated as the money to close." (Tr. 216:2-5.) The borrower's account at that time listed a $2,500 deposit from the borrower's father-in-law, which Respondent characterized as a gift. (Resp't Ex. 27.) Respondent stated that the deposit "quite possibly" was used to satisfy the collection accounts, and that she "believed that's what happened." (Tr. 219:4, 8.) She could not, however, definitively identify that deposit as the source of the funds. (Tr. 216:17-18.)

Although Respondent appears to accept that the $2,500 deposit was a gift from the borrower's father-in-law that was used to satisfy the collection accounts, she did not stipulate to that factual finding. It therefore remains a disputed fact, and the Government must still offer adequate evidence that the $2,500 was used to purchase the home. The Government introduced no such evidence. Accordingly, I find that the Government has failed to meet its burden of proof that the $2,500 deposit was "for the borrower's investment in the property." As a result, any insufficiency in Respondent's efforts to document the source of this deposit did not violate HUD HANDBOOK 4155.1 REV-5, ch.2, sec.3, subsec. 2-10, 2-24.

Section 2-10B of the Handbook states that the lender must obtain a credible explanation of the source of funds for every large increase in an account. Here, $2,500 was deposited into the borrower's account on October 24, 2007, mere days before the borrower was to close the loan. The deposit amount is very near the amount the borrower needed to satisfy his outstanding collection accounts. A sudden, large deposit of this kind is precisely the sort of activity that Respondent should have investigated. The record indicates that she did so. Respondent testified that she obtained a checking account statement from John Wormuth, the father-in-law, in which she noted a wire transfer of $2,500 from Wormuth into the borrower's account. (Resp't Ex. 28; Tr. 218:15-18.) Respondent also obtained a blank check from Wormuth, enabling Respondent to verify that the $2,500 did indeed emanate from Wormuth's account.

I find the fact that the borrower's account and his father-in-law's account contained consistent financial records, to be credible evidence of the source of the $2,500. Respondent need not have investigated further. I therefore find that Respondent did not violate section 2-10B of the HUD Handbook.

During the hearing and in its post-hearing brief, the Government stated that Respondent failed to identify the source of a $10,000 deposit in Wormuth's account one day before Wormuth

deposited the $2,500 in the borrower's account. When gift funds are to be provided at closing, the Handbook requires that lenders determine whether the funds were provided by an unacceptable source. (HUD HANDBOOK 4155.1 REV-5, Ch. 2, Sec. 2-10, Subsec. C, 2-26.) As a general rule, however, the source of the donor's funds is only questionable if the source is a party in the sales transaction. *Id.*

The Government argues that Respondent should have inquired into the identity of the person who deposited the $10,000 in Wormuth's account. (Gov't Post-Hr'g Br. 25.) The $2,500 deposit cannot fairly be considered to have been "provided at closing," as it came three weeks before the closing date. The $3,000 gift, however, was clearly provided at closing; but the Government does not offer any evidence suggesting that the $3,000 gift was derived from the $10,000 deposit. Wormuth's bank statements show that he had ample personal funds with which to give the $3,000 gift to the borrower. Moreover, the gift certification expressly states that the gift "was not made available to the donor from any person ... with an interest in the sale of the property." (Resp't Ex. 28.) The Government offers no evidence to rebut this statement.

Accordingly, I find that, even if the $3,000 gift was provided at closing, Respondent has met her obligation to inquire into the source of the gift funds and has not violated section 2-10, subsec. C, 2-26 of the Handbook.

E. The Pacheco Loan

For the Pacheco loan, the Government claims that "the income was not adequately documented. The file contained a Verification of Employment ("VOE") from The Work Number to document the borrower's employment as a mortgage loan consultant with Sun Trust Bank, but did not contain a copy of a pay statement or any other documentation to support the $9,474.22 used." (Gov't Ex. 1, at 3.)

The Government also alleges that Respondent failed to include copies of signed tax returns in the file. (Gov't Post-Hr'g Br. 26.) The Government's witness testified that although the VOEs showed that the borrower earned more than $10,000 monthly in 2006 and 2007, the borrower's current pay statement showed bi-monthly earnings of only $3,000. (Tr. 65:6-67:2.) The witness also testified that Respondent was required to include an explanation for why she decided to credit the borrower with a monthly income of $9,474.22 when the pay statements did not support that amount. (Tr. 45:14-46:2.)

Respondent contends that "[t]he employment and income documentation actually supports a higher income average than [Respondent] used in underwriting this loan, according to generally accepted underwriting practices as well as the provisions of 4155.1 REV-5." (Resp't Post-Hr'g Br. 8, ¶ 42.)

The HUD Handbook requires commission income to be:

> averaged over the previous two years. The borrower must provide copies of signed tax returns for the last two years, along with the most recent pay statement.

> ... Individuals whose commission income shows a decrease from one year to the next require significant compensating factors to allow for loan approval.

HUD, Handbook REV-5 ch. 2, sec. 2, subsec. 2-7(C), at 2-15.

Respondent appears to interpret the borrower's pay statement as supporting evidence of an income of $9,000 *per month*, when the $9,000 instead refers to the borrower's *year-to-date* earnings. (Resp't Ex. 7.) When questioned during the hearing as to whether Respondent agreed that the borrower's 2008 starting income was $6,000 per month, Respondent replied, "No. The year-to-date pay statement shows $9,000." (Tr. 169:1-6.) Respondent's reading of the pay statement is incorrect. The pay statement reflects three pay periods — two in January 2008 and one in February 2008. The borrower earned $3,000 per pay period, and therefore made only $6,000 in January 2008. (Tr. 231:13-17.)

Respondent may be correct in crediting the borrower with a higher average monthly income, despite a decline in 2008, since his income may have fluctuated due to the business dynamics of his profession. (Resp't Post-Hr'g Br. 9.) However, without explaining how she arrived at the $9,474.22 figure, Respondent's attempt to justify her analysis of Pacheco's income is insufficient. (Tr. Resp't Post-Hr'g Br. 9.) Respondent states that she averaged the borrower's monthly incomes during 2006 ($11,351.657), 2007 ($10,000), and part of 2008 ($9,000). (Tr. 71:6-14; 167:11-20; 229:17-22; 230:1-9.) However, this results in an average monthly income of $10,117.23, rather than $9,474.22. Respondent admits that she did not document how she determined the borrower's monthly income. (Tr. 232:19-22; Tr. 233:1-2.)

Additionally, while Respondent provided a pay statement and W-2 forms, she failed to provide copies of signed tax returns for the past two years. HUD guidelines specifically require this documentation when attempting to include commission income as effective income. HUD, Handbook REV-5, ch. 2, sec. 2, subsec. 2-7(C), at 2-15.

Accordingly, I find that Respondent's failure to explain her decision to credit the borrower with an income of more than $9,000, and her failure to provide copies of signed tax returns as required, violated HUD guidelines.

As a final point, Respondent stated that "HUD conceded at the hearing that the income documented on Respondent's 3 and 4 supported the income used to qualify the borrower." (Resp't Post-Hr'g Br. 9, ¶ 43.) Respondent refers to the cross examination of Pieffer, the Government's witness. However, Pieffer does not "concede" that Respondent correctly calculated the borrower's income. Rather, Pieffer simply stated that Respondent's Exhibit 4 and Government's Exhibit 3 indicated that Pacheco earned approximately $10,000 per month in 2006 and 2007. (Tr. 65:6-14.) Pieffer immediately qualified these statements by adding, "[b]ut his current pay statement only showed him as making $3,000." (Tr. 67:1-2.) Respondent's mischaracterization of the Government's position by alleging that it "conceded" Respondent's calculation of the borrower's income, here, further strains the credibility of Respondent's evidence.

F. The Santiago Loan

The Government alleges that Respondent's actions with regard to the Santiago loan violate Chapters 2 and 3 of HUD Handbook 4155.1 REV-5 and Mortgagee Letters 96-18, 97-26, 00-28, 05-43, and 07-11. Specifically, the Government argues that Respondent did not provide an analysis of the borrower's credit history, that the borrower's Verification of Rent was insufficient because the landlord and the borrower had an identity of interest relationship, and that Respondent did not verify the source of funds for the borrower's closing. (Gov't Post-Hr'g Br. 27.)

The credit report contained in the file for Amanda Santiago showed no less than 10 collection accounts. (Gov't Ex. 5; Tr. 47-48.) The credit report showed only one open account, with the remaining accounts listed as either derogatory or in collection. (Tr. 47:16-18; 52:4.) The HUD Handbook states:

> Past credit performance serves as the most useful guide in determining a borrower's attitude toward credit obligations and predicting a borrower's future actions. A borrower who has made payments on previous and current obligations in a timely manner represents reduced risk. Conversely, if the credit history, despite adequate income to support obligations, reflects continuous slow payments, judgments, and delinquent accounts, *strong* compensating factors will be necessary to approve the loan.

HUD, Handbook 4155.1 REV-5, ch. 2, sec. 1, subsec. 2-3, at 2-5 (emphasis added).

When a collections account appears on a prospective borrower's credit report, the HUD Handbook requires the lender to obtain an explanation from the borrower that "makes sense" and is "consistent with the other credit information in the file." HUD, Handbook 4155.1 REV-5, ch. 2, sec. 1, subsec. 2-3, at 2-5. All collection accounts must also be explained by the borrower in writing. *Id.* ch. 2, sec. 1, subsec. 2-3(C), at 2-6. A written explanation from the borrower was submitted to Respondent on September 22, 2006, explaining that the derogatory credit was a result of the borrower's 2003 bout with cancer. (Resp't Ex. 8.) The explanation also included several medical records documenting the diagnosis and treatment.

The Government, while acknowledging the borrower's written explanation, nevertheless argues that the explanation is inadequate and that the "lender failed to provide an analysis of the borrower's credit history examining the overall pattern of credit behavior." (Gov't Post-Hr'g Br. 26.)

In contrast, Respondent maintains that, prior to Santiago's illness, there was no "adverse or derogatory credit history" and that, after recovering from a "bona fide hardship," Santiago "returned to the work force and had made enormous efforts to bring her accounts up to date." (Resp't Post-Hr'g Br. 13; Tr. 171) (internal quotation marks omitted). For example, Respondent states that Santiago "paid creditors and satisfied two judgments within the prior twelve months."

(Resp't Post-Hr'g Br. 14.) Additionally, Santiago "focused on making rental payments and not incurring additional debts." (*Id.*)

As the Handbook states, "[w]hen delinquent accounts are revealed, the lender *must* document their analysis" and that "*major* indications of derogatory credit — including judgments, *collections*, and any other recent credit problems — require sufficient written explanation from the borrower." HUD, Handbook 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3, at 2-5 (first and third emphases added).

The borrower's credit report is replete with derogatory accounts. (Gov't Ex. 5; Resp't Ex. 9.) In light of this particularly poor credit report, Respondent was required to include a written analysis providing strong or compelling justification for approving this loan. Instead, Respondent chose to forego any analysis at all, and simply relied upon the borrower's explanation letter, which failed to account for delinquent account activity occurring well after the borrower's cancer diagnosis. (Gov't Post-Hr'g Br. 28; Resp't Ex. 9.) When asked during the hearing why she chose not to file any analysis, Respondent stated that she "didn't feel it was necessary" (Tr. 179:13) and that "[i]n my opinion the underwriting is my analysis when I review the entire file." (Tr. 234:4-5.) Respondent's assessment of her responsibilities as to what type of written analysis she is required to provide is off base. Not only is the failure to provide explanatory analysis a clear violation of the guidelines, but Respondent's disregard for the rationale behind this requirement draws into question her understanding of the role of a Direct Endorsement underwriter. Accordingly, I find that Respondent's failure to document her explanation and analysis of the borrower's credit history constitutes a violation of sec.1, subsec. 2-3 at 2-5, of the Handbook.

As an additional argument, Respondent maintains that medical accounts are "not required to be paid" pursuant to FHA guidelines. (Tr. 172:2.) However, Respondent fails to point to any HUD/FHA requirement stating that medical accounts are exempt from the underwriter's analysis of a borrower's credit history. Respondent further argues that Santiago's satisfaction of two judgments and payment of credit accounts within the prior 12 months should be considered as "additional non-traditional credit references." (Resp't Post-Hr'g Br. 14.) The HUD Handbook, however, requires that underwriters consider both positive *and* negative credit history.

Furthermore, Respondent's contention that non-traditional credit references are appropriate considerations for this loan is misplaced, as the Handbook only permits such references when the borrower does not have credit. HUD, Handbook 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3, at 2-5. The borrower here has a well-established — though problematic — credit history. To suggest, as Respondent does, that a lone open account on a credit report otherwise comprised entirely of derogatory account information is akin to having "an overall lack of current credit" once again indicates Respondent's failure to comprehend certain elements of the HUD guidelines. (Resp't Post-Hr'g Br. 14.)

The Government also claims that Respondent "failed to document the source of funds used to close the loan and/or satisfy omitted liabilities." (Resp't Ex. 1.) The HUD Handbook requires that "[a]ll funds for the borrower's investment in the property must be verified and documented." HUD, Handbook 4155.1 REV-5, Ch. 2, Sec. 3, Subsec. 2-10, at 2-24.

There are, again, two MCAWs in the record for this loan, Government's Exhibit 9 ("Gov't Ex. 9" or "Government's Santiago MCAW") and Respondent's Exhibit 10, ("Resp't Ex. 10" or "Respondent's Santiago MCAW"). The Government's MCAW lists cash reserves of $1,713.18 and states in the Remarks section that "should borrower need funds to close, cash on hand will be used." (Gov't Ex. 9.) Respondent's MCAW, by contrast, lists cash reserves in the amount of $31.30. (Resp't Ex. 10.) The Remarks section does not mention any funds to close. (*Id.*)

The Government argues that "the HUD-1, dated September 19, 2006, indicated $1,521.56 was paid at closing. [Gov't Ex. 9] did not contain a VOD, bank statement, or any other documentation of the source of funds needed to close." (Gov't Post-Hr'g Br. 27.) Respondent asserts that the Government's MCAW does not bear her true signature, but admits that she signed Respondent's Exhibit 10. (Resp't Post-Hr'g Br. 14, ¶ 67; Tr. 173-77; Gov't Ex. 9; Resp't Ex. 10.)

As with the Bilyeu and Herard loans, the Government did not offer any appreciable evidence to overcome Respondent's denial that her signature appears on the contested MCAW. I find that Respondent did not sign Government's Santiago MCAW (Gov't Ex. 9), and Respondent bears no responsibility for any alleged violations associated with that document. Instead, this Court must look to Respondent's Santiago MCAW (Resp't Ex. 10), to determine whether the source of funds to close was inadequate for this loan. The MCAW submitted by Respondent demonstrates that the borrower did not require any closing funds for this loan. Accordingly, I find that Respondent's actions did not violate HUD guidelines with regard to the requirement to document the source of funds to close on this loan.

The Government also claims that Respondent "approved the loan without obtaining the required documentation to support the decision to approve the loan." (Notice of Suspension, 3-4.) Specifically, the Government argues that the file contained "a Verification of Rent ("VOR") and evidence of an acceptable rental history, but the landlord was the borrower's employer and had an identity of interest relationship with the borrower. The file did not contain canceled checks covering the most recent twelve month period." (*Id.*)

Respondent claims she verified that the borrower had acceptable rental history by examining her credit report. (Tr. 183-85; Resp't Post-Hr'g Br. 15; Resp't Ex. 9.)

The HUD Handbook states that the lender

> must determine the borrower's payment history of housing obligations through *either* the credit report, verification of rent directly from the landlord (with no identity-of-interest with the borrow) or verification of mortgage directly from the mortgage servicer, or through canceled checks covering the most recent 12-month period."

HUD, Handbook 4155.1 REV-5 ch. 2, sec. 1, subsec. 2-3(A), at 2-6 (emphasis added).

Testimony from both Government's witness, Peiffer, and Respondent confirmed that the borrower's rental history was verified through the credit report, which was included in the FHA binder. (Tr. 51:18-52:10, 183:10-16; Gov't Ex. 5.) Because the credit report was used to verify the borrower's rental history, it is not necessary to determine whether there was an identity of interest between borrower and her landlord. Accordingly, I find that Respondent did not violate sec. 1, subsec. 2-3(A), at 2-6's requirement for a determination of identity-of-interest where VORs are used to verify rent payment history.

Lastly, the Government alleges that Respondent's actions violate Mortgagee Letters 96-18, 05-43, 07-11, 97-26, and 00-28. (Gov't Post-Hr'g Br. 26.) In response, Respondent correctly notes that Mortgagee Letters 96-18, 05-43, and 07-11 apply to refinance transactions, not to purchase money mortgage loans like Santiago's loan. (Resp't Post-Hr'g Br. 12.) Further, Respondent states that Mortgagee Letters 96-18, 97-26, and 00-28 have been incorporated into HUD Handbook 4155.1 REV-5. (*Id.*) Moreover, 07-11 was not issued until September 5, 2007, almost a year after the Santiago loan was closed. (*Id.* at 12-13.)

While Respondent is correct that Mortgagee Letters 96-18, 97-26, and 00-28 were incorporated into HUD Handbook 4155.1 REV-5, the Government cited to the HUD Handbook alongside each of those Mortgagee Letters. Any violation of the Mortgagee Letters, therefore, would have been a violation of the corresponding sections of the Handbook. As previously discussed, Mortgagee Letters 05-43 and 07-11, though still in force at the time of the loan, are inapplicable to this loan. The guidelines contained in Mortgagee Letters 00-28 and 97-26, on the other hand, were applicable to the current loan. However, both Mortgagee Letters refer to funds for closing. All allegations against Respondent for violations of Mortgagee Letters 96-18, 97-26, and 00-28, are predicated on the validity of the Government's MCAW, which this Court has determined was not proven to be signed by Respondent. Accordingly, I find that Respondent has not violated any of the Mortgagee Letters or their corresponding sections in HUD Handbook 4155.1 REV-5, with respect to her completion of Respondent's Santiago MCAW (Resp't Ex. 10).

II. Determination of Debarment and Period of Debarment

A. When Debarment is Appropriate

LDPs ("limited denials of participation"), debarments, and suspensions are serious sanctions. 2 C.F.R. § 180.125(c) (2010). Such sanctions have been found to be warranted in cases where: a participant, who had previously been issued an LDP did nothing to correct the deficiency and admitted to misusing funds, to the detriment of HUD, *Otis Stewart Jr.*, HUDALJ 98-8054-DB (Nov. 8, 2001); an executive director of a HUD participant had a duty to discourage the participant's board members from taking actions that violated HUD regulations, but failed to do so, *McKinley v. Copeland*, HUDBCA No. 00-C-113-D14 (Nov. 29, 2001); a participant's false certification was a material misrepresentation even when there was a lack of intent to mislead HUD, *Gabe Brooks*, HUDBCA No. 99-A-104-D3 (Sept. 15, 2000); a loan officer falsified loan documents, forged signatures on loan documents, and made false statements for the purpose of influencing loan underwriting decisions in which HUD insured the loans, *Marcus Payne*, HUDBCA No. 99-9014-DB (May 14, 1999); a respondent made a misrepresentation, that

even if it was an "honest mistake, [was], nevertheless, a very serious mistake because HUD must rely upon the truthfulness of the representations made by those who participate in its program and who certify to the accuracy of their representations," *William D. Muir and Metro Cmty. Dev. Corp.*, HUDBCA No. 97-A-121-D15 (Nov. 6, 1997); respondents were found to have "failed, repeatedly, to meet their contractual and programmatic obligations to HUD" when they entered into four sales contracts with HUD that never went to closing, *M. Brett Young and Allied Hous. Grp., Ltd.*, HUDALJ 96-0036-DB (Sept. 13, 1996).

On the other hand, less onerous sanctions have been imposed in cases where: a respondent made good-faith efforts to remedy a difficult and disorganized situation and bring her office into compliance with HUD regulations but was unable to do so because she lacked the staff and necessary resources, *Marilee Jackson*, HUDBCA No. 05-K-112-D7 (Oct. 13, 2005) and; a lender's remedial measures demonstrated that they were acting as responsible contractors and in good faith as they attempted to correct the deficiencies caused by their subcontractors, *First Capital Home Improvements*, HUDBCA No. 99-D-108-D7 (Nov. 24, 1999).

Although Respondent's actions here do not involve bad faith or fraudulent conduct as in the cases above, the Government has established that Respondent clearly violated a number of HUD guidelines, and demonstrated a lack of understanding of said guidelines. As an experienced underwriter of some 20+ years, who holds the designation of Direct Endorsement Underwriter, Respondent's conduct raises serious concerns that hold significant implications for the public interest. I, therefore, find that the Government has established a clear basis for the imposition of a debarment in this case.

B. Mitigating and Aggravating Factors, and Other Considerations

In deciding the length of a debarment, the debarring official must consider the length of any preceding suspension. 2 C.F.R § 180.865(b). Alaso, a debarring official may choose not to impose a debarment even if cause for the debarment exists. 2 C.F.R. § 180.845(a). In making the decision the official may consider mitigating or aggravating factors, pursuant to 2 C.F.R. § 180.860. The existence or nonexistence of any single factor is not determinative. *Id.*

The Government argues that a number of aggravating factors exist in this case, namely, subsections (a), (g), (k), and (s) of 2 C.F.R. § 180.860.[8] Subsection (a) of 2 C.F.R. § 180.860 states that the debarring official may consider "the actual or potential harm or impact that results or may result from the wrongdoing." 2 C.F.R. § 180.860(a). The Government argues that "the potential harm is equivalent to the dollar amount of each of the loans identified above." (Gov't Post-Hr'g Br. 29.) Indeed, each loan had the potential for being defaulted on from the onset, resulting in HUD potentially indemnifying the lenders for the full dollar amount of the loan. However, the fact that the Government did not present evidence at the hearing of any actual harm (i.e., actual defaulted loans or money paid by HUD to indemnify lenders for the loans) is also taken into account.

The Government also highlights, as an aggravating factor under 2 C.F.R. § 180.860(g), the fact that "Respondent has failed to accept responsibility for the wrongdoing and, instead has

[8] The Government mistakenly cited the regulation as 2 C.F.R. § 180.960.

provided excuses for approving loans to borrowers who simply were not credit worthy. Respondent has also failed to recognize the seriousness of her actions." (*Id.*)

Throughout the hearing, Respondent repeatedly argued that she underwrote the loans to the best of her ability and that her actions were not unreasonable. A review of the record of this proceeding demonstrated that although some of Respondent's acts and omissions were relatively minor in scope, Respondent failed to comply in large measure with a number of the underwriting guidelines set forth by HUD.

Respondent's failure to admit or understand that her underwriting for these loans did not meet HUD standards is particularly troubling in this case. Respondent either does not have sufficient knowledge of HUD's underwriting guidelines or refuses to appreciate her responsibility to comply with them. In addition, Respondent's actions appear to reflect a lack of understanding of — or a lack of respect for — the underlying rationale for HUD's guidelines. In the Crump, Herard, O'Neal, and Santiago loans, for example, Respondent ignored major "red flags" in the borrowers' credit reports that should have triggered further investigation on her part. Instead, she chose to simply accept the borrowers' explanations at face value, and in direct contravention of the applicable guidelines.

Respondent's position as a Direct Endorsement underwriter requires that she endeavor to minimize HUD's exposure to indemnification for homeowner defaults on each and every loan she is charged with underwriting. A thorough analysis of the borrower's credit reports is fundamental to this purpose. The guidelines expressly state that an underwriter must analyze and explain why she chose to approve a loan when the credit report reveals derogatory information. HUD Handbook 4155.1 REV-5, ch. 2, sec. 1, subsec. 2-3, at 2-5. Respondent's failure to perform and document this analysis lies at the heart of most of the Government's allegations. Indeed, Respondent's omission of any analysis of the Santiago loan, in particular, is strong evidence that the Government's concerns are well-founded. Despite a particularly derogatory credit report, Respondent accepted the borrower's explanation, wholesale, and failed to perform the required analysis, stating she "did not feel it was necessary."

The appropriate reaction when confronted with an applicant's derogatory credit account is to be wary of it and thus require an analysis of the report. The purpose of the underwriter's documented, reasoned analysis is to alleviate this wariness. If Respondent does not appreciate why such documentation is necessary, she calls into question her suitability for being trusted with the responsibilities of a Direct Endorsement underwriter.

I therefore find that Respondent's failure to accept responsibility for her deficient underwriting, and the nature and seriousness of Respondent's violations of HUD guidelines, are aggravating factors under the regulation.

The Government also argues that "[a]s the underwriter of the loans, Respondent was the focal point of the Direct Endorsement program. HUD relied on Respondent to make sound decisions in determining whether to approve or reject the loans." (*Id.*) This fact, the Government claims, is an aggravating factor under 2 C.F.R. § 180.860(k), which considers "[t]he kind of positions held by the individuals involved in the wrongdoing." 2 C.F.R. § 180.860(k).

Due to the unique nature of the Direct Endorsement program, where it is the mortgagee that "determines [whether] the proposed mortgage is eligible for insurance under the applicable program regulations," the role of the mortgagee's underwriter is of paramount importance. Under the Direct Endorsement program, it is the underwriter who ultimately decides if the borrower is creditworthy and meets HUD's FHA eligibility requirements. 24 C.F.R. § 203.5(a); HUD, Handbook 4000.4 REV-1 CHG-2 ch. 3-16. Therefore, Respondent's position as an underwriter placed her in a position of trust in which she was expected to meet the minimum standard of due diligence in underwriting mortgages by complying with the underwriting guidelines set forth by HUD. 24 C.F.R. § 203.5(c). Accordingly, I consider Respondent's special status as a Direct Endorsement Underwriter to be an aggravating factor that offers little tolerance for the sorts of mistakes and oversights such as those made by Respondent in this case.

Lastly, the Government asks this Court to consider, as an aggravating factor under 2 C.F.R. § 180.860(s), which allows consideration of "other factors that are appropriate to the circumstances of a particular case," Respondent's "interest in approving loans because each loan she approved brought her closer to meeting her goals and earning a bonus." (Gov't Post-Hr'g Br. 30.) To consider this as an aggravating factor would require this Court to infer that Respondent intended to approve loans that she knew did not meet FHA requirements in order to reap a benefit. The record of this proceeding does not reflect any such improper intent on the part of Respondent. At most, the evidence paints a picture of an underwriter who seemed to be too often willing to look past her responsibilities as an underwriter in a misguided effort to "help" borrowers who should not have been approved, or perhaps because she was just not performing her work in a careful manner. In any case, in the absence of additional evidence, I find that the Government has not substantiated this allegation as an aggravating factor.

Along with the aggravating factors alleged by the Government, I have considered all other mitigating and aggravating factors set forth in 2 C.F.R. § 180.860, including Respondent's relatively long history of good service with HUD and FHA loans. The Government introduced no evidence that Respondent had been previously sanctioned by the Department or subject to disciplinary action of any sort. I also considered the fact that the Government did not introduce evidence that Respondent had been given an opportunity to correct her behavior prior to receiving the Notice of Suspension. I find that 2 C.F.R. § 180.860(b-e), (h-j), and (l-r), are either inapplicable, or do not reach the level of qualifying as either mitigating or aggravating factors in this case.

However, I find that consideration of 2 C.F.R. § 180.860(f), "[w]hether and to what extent [Respondent] planned, initiated, or carried out the wrongdoing," bears discussion. Although Respondent's actions as an underwriter indicate a lack of appreciation for the importance of several of HUD's guidelines and requirements, from the evidence of record, I find that none of Respondent's actions rise to the level of intentional misconduct. Since evidence of fraud or intentional misconduct requires and generally results in more severe sanctions, as indicated in the cases cited above, I find the lack of such conduct here to be a mitigating factor in this case.

C. Present Responsibility

After establishing that a cause for debarment exists, the burden shifts to Respondent, who must demonstrate "to the satisfaction of the debarring official that [Respondent is] presently responsible and that debarment is not necessary." 2 C.F.R. § 180.855(b). In determining whether debarment is an appropriate sanction, "[t]he debarring official bases the decision on all information contained in the official record. The record includes ... [a]ny further information and argument presented in support of, or in opposition to, the proposed debarment."[9] 2 C.F.R. § 180.845(b)-(b)(1).

Respondent notes that she has been an underwriter for twenty years, in which time she has underwritten "in the vicinity of 10,000" loans. (Tr. 150:16, 151:19-22.) She has been an FHA underwriter since 1992 (Tr. 152:15.) and has never before been the subject of any inquiries into violations of HUD guidelines (Tr. 151:6-16.)

Respondent argues that debarment is an inappropriate sanction because, "[a]ll of the deficiencies identified by HUD with respect to the Six Loans are no more than level one deficiencies." (Resp't Post-Hr'g Br. ¶ 19.) In support of her argument, Respondent cites HUD Handbook 4000.4 REV-1 CHG-2, which defines a "level one deficiency" as "any minor underwriting deficiency which does not change the eligibility determination of the property, the mortgagor, the mortgage amount or term." HUD, Handbook 4000.4 REV-1 CHG-2 ch. 5, sec. 5-3(A)(1).

Although HUD Handbook 4000.4 REV-1 CHG-2 was incorporated into HUD Handbook 4155.1 and therefore did not specifically govern Respondent's underwriting obligations to HUD during the relevant time period, it serves as a helpful guide for determining the severity of Respondent's acts and omissions. While this Court does not agree that all the deficiencies stated in the Notice of Proposed Debarment were "level one" deficiencies, it appears that some of Respondent's violations were, as the HUD Handbook describes, relatively minor.

For several of the violations, documentation within the FHA binders suggests that Respondent attempted to comply with HUD guidelines that required supporting documentation and analysis for her underwriting decisions, but failed to do so because the additional documentation did not clearly support Respondent's decision to approve the loan. The Court agrees that debarment is generally, not warranted in instances where Respondent merely neglects to include explanations of her analysis to support and/or clarify her decision to approve the loans. However, where such deficiencies serve to mask significant information necessary to evaluate loan eligibility criteria, debarment may well be warranted.

In much of the loan data in this case, e.g., the O'Neal Loan, where Respondent failed to produce documentation explaining the borrower's other delinquent debts and numerous NSF fees and failed to obtain a gift letter for a $2,500 gift; the Santiago Loan, where the only explanation

[9] A United States District Court has interpreted this to impose an affirmative duty on the hearing official to consider mitigating factors contained in the official record. *See Feinerman v. Bernardi*, 558 F. Supp. 2d 36, 50 (D.D.C. 2008) ("[T]he Debarring Official acted in an arbitrary and capricious manner by failing to explain why he did not find the mitigating evidence presented by the plaintiffs persuasive.").

letter from the borrower included in the FHA binder referenced the borrower's derogatory credit in general and did not explain each of the numerous collection accounts; and the Herard Loan, where the only compensating factor cited by Respondent was not supported by documentation, and where Respondent failed to obtain credible documentation of the borrower's rental income — the alleged violations were the result of the omission of requisite documents from Respondent's analysis itself, as well as the FHA binder. There was no evidence of Respondent's efforts to obtain these documents, which would have demonstrated Respondent's good faith attempts to comply with HUD guidelines. Respondent's violations in these cases presented an unacceptable risk to HUD and the FHA program, and may well have resulted in a denial of loan eligibility by Respondent or other Direct Endorsement underwriters.

A more egregious example is provided by the Crump Loan, where the borrower was clearly ineligible for an FHA-insured loan under HUD guidelines because he failed to make his mortgage payments in a timely manner during the 12 months prior to the loan closing. This was a requirement clearly stated in Mortgagee Letter 05-43. However, instead of accepting responsibility for this violation, which could be considered a mitigating factor under 2 C.F.R. § 180.860, Respondent denied that this mortgagee letter was applicable. Respondent's denial is further evidence that she lacks sufficient knowledge of HUD's eligibility requirements for FHA loans or she does not feel she is obligated to conform to them. Either condition renders Respondent not presently responsible to underwrite FHA insured loans. *See Benjamin J. Roscoe*, HUDALJ 93-2007-DB (June 26, 1995)("'Present responsibility' includes not only financial responsibility but also the capacity and willingness to comply with governmental rules and regulations.")

Respondent also argues that the Government's purpose in bringing this debarment action is punitive, as evidenced by the fact that (1) HUD did not issue the Notice of Suspension and Proposed Debarment until eight months after the QAD's review (Resp't Post-Hr'g Br. ¶ 12); and that (2) "the timing of the October 20 Letter ... was contemporaneous with both a letter delivered to her employer by the HUD Mortgagee Review Boards, and a civil action filed against her employer by the Government. (*Id.* ¶ 90). While HUD's timing in this case might raise questions, Respondent failed to show that her suspension and proposed debarment under the circumstances of this case "[do] not reflect the Government's desire to protect the public interest pursuant to 24 C.F.R. § 24.115(a) or that its imposition reflects an abuse of agency discretion. *William Johnson and Linear Non-Profit Hous. Corp.*, 06-1 BCA P 33132, HUDBCA No. 03-D-104-D5 (July 2, 2004). I find that the Notice of Suspension was not imposed for the purpose of punishing Respondent.

Lastly, Respondent argues she is presently responsible and that:

> [n]one of the allegations in the October 20 Letter are reasonably relevant to [her] present responsibility. All of the allegations of the October 20 Letter are exceedingly remote; the Letter concerns underwriting actions that took place more than 2½ years ago, and most of the underwriting actions took place more than 3 years ago.

(Resp't Post-Hr'g Br. ¶ 89.)

Indeed, it has been held that the "passage of time diminishes the probative value of acts showing lack of present responsibility." *Gary M. Wasson*, HUDALJ 04-030-DB (Aug. 5, 2004) (citing *Lynne Borrell and Lynne Borrell and Assocs.*, HUDBCA No. 91-5907-D52 (Sept. 20, 1991)).

In *Gary M. Wasson*, the administrative law judge stated that, "to be sure, a respondent may be found to lack present responsibility based on past acts; but the staler the evidence, the weaker the proof" and held that "HUD's delay in bringing a case against Respondent undermined the cause for debarment to the point that he cannot now be found to lack 'present responsibility' on the basis of events that occurred from six years, 10 months to nearly eight years ago." *Gary M. Wasson*, HUDALJ 04-030-DB; *see also Roberto Soto Carreras*, HUDALJ-88-1234-DB(TDP) (June 22, 1988) (finding that three years was an inordinate amount of time to delay bringing charges against a Respondent based on events occurring almost seven years prior to the initiation of a temporary denial of participation). However, this debarment action differs from *Gary M. Wasson* because, in that case, the Government knew of the respondent's violation within days of its occurrence but did not take action against the respondent for six and a half years. *Id.* In the present case, HUD's decision to wait eight months before issuing the Notice of Suspension was entirely reasonable.

In *Uzelmeier v. United States Department of Health and Human Services*, the district court upheld an administrative law judge's decision to debar a participant even though the Department of Health and Human Services waited seven years before initiating debarment proceedings. 541 F. Supp. 2d 241, 247-48 (D.D.C. 2008). The court in *Uzelmeier* cited another district court case where "the length of time between the underlying events and the debarment ... was just one factor that the court considered, but there was no indication that it was the dispositive factor or even the primary one." *Uzelmeier*, 541 F. Supp. 2d at 249 (discussing *Roemer v. Hoffmann*, 419 F. Supp. 130 (D.D.C. 1976)). The court distinguished *Uzelmeier* from *Roemer* by noting that, "in this case plaintiff has admitted no past wrongdoing and has not demonstrated that her present responsibility has changed or improved since the underlying incidents." *Id.* at 248. Like the plaintiff in *Uzelmeier*, Respondent has not acknowledged her failure to comply with HUD guidelines. Instead, Respondent has continued to argue that she "acted in a reasonable manner" when she underwrote the loans. (Resp't Post-Hr'g Br. ¶¶ 40, 57, 72, 85.) I find this fact to weigh more heavily than the length of time HUD waited before initiating debarment proceedings.

D. Length of Debarment

Generally, debarment should not exceed three years. 2 C.F.R. § 180.865(a). However, the debarring official may impose a longer debarment if circumstances warrant. *Id.* In determining an appropriate period of debarment to be imposed in this case, I look to precedent established in previous HUD debarment cases, including those decided by the former HUD Board of Contract Appeals and the Office of Administrative Law Judges. In those cases, we have held that the period of debarment imposed should be decided according to the severity of Respondent's actions in failing to comply with departmental regulations and applicable standards of conduct. *See Walter C. Johnston*, HUDALJ 90-1499-DB (Sept. 26, 1990) ("[T]he period of

debarment must be for a period commensurate with the seriousness of the cause(s)." (quoting 24 C.F.R. § 24.320(a)) (internal quotation marks omitted)); *see also Howard Burgess*, HUDALJ 95-5023-DB (May 10, 1995) ("[T]he seriousness of the person's acts or omissions and any mitigating factors shall be considered in making any debarment decisions.").

We have reserved our most severe administrative sanctions for cases where respondents have committed deliberate misconduct, acted with scienter, or acted with reckless disregard of applicable standards. *See, e.g., John E. Signorelli*, HUDBCA No. 94-C-I44-D1 (Sept. 21, 1995) (imposing a debarment period of five years based on Respondent's actions in defrauding the public of 17 million dollars through deliberately misleading solicitations). We have also held that debarment is not a "punishment," but is rather an administrative action designed to protect the public interest. *See, e.g., Marilee Jackson*, HUDBCA No. 05-K-112-D7, at *21 (Oct. 13, 2005) (citing 24 C.F.R. § 24.110(C) (2004)). The focus of our inquiry must be on whether Respondent is "presently responsible." 2 C.F.R. § 180.855(b) (2010).

A three-year period of debarment is generally imposed in cases involving fraud. In *Walter C. Johnston*, the Court imposed such a debarment on the Respondent after finding that he knowingly and willfully represented to HUD that cash payments had been made by the borrowers in order to accomplish the sale of properties with mortgages insured by FHA. HUDALJ 90-1499-DB, at *14 (Sept. 26, 1990). The Court found that the respondent's "willful falsification" of terms and conditions placed public funds at risk and prevented HUD from relying on his statements in making eligibility determinations. *Id.* at *23, *25; *see also James Myers & Tammy Myers*, HUDBCA No. 96-A-105-D2 (Sept. 12, 1996); *Howard Burgess*, HUDALJ No. 95-5023-DB (May 10, 1995). *But see John E. Signorelli*, HUDBCA No. 86-1517-D8 (Sept. 30, 1986) (imposing a two-year period of debarment based on respondent's publication of false financial statements).

While the Respondent's intent to defraud HUD was clear in *Johnston*, a debarring official may still impose a three-year debarment period even if the Government cannot prove a respondent was complicit in fraudulent acts, as long as the respondent's conduct was so glaring and irresponsible as to create an environment conducive to fraud. *See Kay Yarbrough*, HUDBCA No. 92-C-7513-D33, at *37-41 (Oct. 28, 1992) (holding that even though the Government could not prove that the respondent engaged in fraud, her "absolutely appalling, lazy, and ultimately dishonest abdication of her responsibilities ... set in motion a chain of events ... where fraudulent schemes could gain a firm foothold").

In contrast, if no fraud is alleged and the respondent demonstrates an awareness of her deficiencies, officials have generally imposed a debarment period of less than three years. In *Renee Divins*, the Respondent's acknowledgment of her loan processing errors led to a debarment period of 18 months, rather than the Government's proposed five-year debarment. HUDBCA No. 92-C-7511-D30 (June 4, 1992). Since the Court found that the nature of the respondent's errors reflected "technical falsehoods" rather than fraud and that the Respondent had "become more aware, more careful," the Court determined that a shorter debarment period was warranted. *Id.* at *41, *43. Similarly, although the respondent in *Mayer Co., Inc. & Carl A. Mayer, Jr.* failed to obtain liability insurance on certain apartments and failed to make timely mortgage payments on properties owned, insured, or subsidized by HUD, the Court nevertheless

noted that the Respondent became "cognizant of the deficiencies of his performance.... His growing awareness of what he should have done to avoid the contract performance problems ... mitigates somewhat the more troubling aspects of this case." HUDBCA No. 81-544-D1, at *3-7, *14-15 (Dec. 1, 1981). Accordingly, a one-year period of debarment was imposed. *Id.* at *15.

If a Respondent fails to understand the seriousness of her violations, however, an official may decide to impose a two-year debarment period. For instance, the Court in *Joan Galati* imposed a two-year debarment on the Respondent after determining that "[s]he [was] still trying to explain away and dodge from serious irregularities in her conduct," including failure to verify information provided by borrowers. HUDBCA No. 88-3455-D64, at *11, *20 (March 9, 1989; *see also Stephen J. Ferry & Beth Ann Ferry*, HUDBCA No. 90-5228-D17, at *17 (Oct. 31, 1990) (noting particularly the Respondents' attitudes during the hearing, stating that "[t]hey profess ignorance of HUD rules and regulations, quibble with them, and were generally defiant").

Likewise, even if a Respondent genuinely regrets his actions, the official must be persuaded that the Respondent actually understands *why* his conduct was improper. *See Michael E. Ipavec*, HUDBCA No. 95-A-128-D19 (Feb. 21, 1996) (imposing a two-year period of debarment based on Respondent's failure to grasp the seriousness of his violation, despite expressions of regret).

On this record, I have not found conduct that could be considered as having emanated from any fraudulent scheme or scienter on the part of Respondent. Rather, I find that Respondent's deficiencies were a result of her lack of knowledge or understanding of the HUD guidelines, and her negligence in properly documenting her analysis of certain aspects of the loan applications and approvals in question. Therefore, in determining the appropriate period of debarment, I have considered whether Respondent has demonstrated an awareness of her deficiencies, warranting a one-year period of debarment, or whether she continues to excuse her deficiencies, warranting a two-year period of debarment.

I find that Respondent's hearing testimony evidenced a lingering refusal to accept responsibility for her serious underwriting infractions. Respondent continually sought to justify her actions in the face of clear contravening HUD requirements. For instance, despite the language contained in Mortgagee Letter 05-43 regarding eligibility requirements for FHA loans, Respondent claimed that the letter was inapplicable to the Crump loan. While Respondent came close to admitting her shortcomings regarding the Herard loan, stating that "[u]ltimately, I should have questioned [the 401k statement], she nevertheless maintains that her actions were reasonable. (Tr. 197:17-18; Resp't Post-Hr'g Br. ¶ 50.) That Respondent does not comprehend that the standard to be met as an underwriter is not one of "reasonable" actions, but one of compliance with HUD guidelines, is problematic. This is especially so, since she evinced these attitudes at the hearing, well after having received the Notice of Suspension.

Unlike the Respondents in *Renee Divins* and *Carl A. Mayer*, Respondent refuses to admit, or fails to comprehend, her culpability in the documented violations. Respondent's attitude instead parallels that of the respondent in *Joan Galati*, where the debarring official imposed a debarment period of two years. As this administrative body has previously stated, "[i]t is not the quantity of transactions so flawed, but the nature of the act and the *recognition* of them." *Joan*

Galati, HUDBCA No. 88-3455-D64, at *20 (March 9, 1989) (emphasis added); *see also*, *Howard Burgess*, HUDALJ No. 95-5023-DB (May 10, 1995)("Respondent's explanation demonstrates that he has yet to accept responsibility for his unlawful conduct, and, therefore, that there remains a likelihood that he will repeat such acts in the future.") Without express recognition of her errors in judgment, I have no basis to believe that Respondent will not repeat these same errors in the future or that she not will continue to pose an unacceptable risk to HUD.

I further find that Respondent's failure to acknowledge her wrong-doing outweighs any mitigating impact that may be gleaned from any lack of opportunity to correct her actions before being served with the Notice of Suspension. Moreover, after considering all of the factors that militated in Respondent's favor, as set forth in 2 C.F.R. §180.860, I find that these factors do not outweigh the Department's compelling interest in protecting the public fisc from potentially significant financial losses.

Although I find Respondent's attitude parallels that of the respondent in *Joan Galati*, and that a two year debarment period is appropriate to her actions, I must also consider the time during which Respondent has already been suspended pending the outcome of this proceeding. 2 C. F.R. § 180.865. I note that Respondent has been suspended since October 20, 2009, or just over two years to date, and thus find that a two-year period of debarment is appropriate and necessary in this case.

RECOMMENDED ORDER

Considering the seriousness of Respondent's acts and omissions weighed against the fact that Respondent has been suspended since October 20, 2009, I recommend that a period of debarment be ordered for two years, beginning from the date of the Notice of Suspension.

H. Alexander Manuel
Administrative Judge

November 3, 2011