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**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS**

UNITED STATES OF AMERICA *ex rel.*
PETER BELLI,

Plaintiff,

v.

AMERICUS MORTGAGE
CORPORATION,
f/k/a/ ALLIED HOME MORTGAGE
CAPITAL CORPORATION,

Defendant.

UNITED STATES OF AMERICA,

Plaintiff-Intervenor,

v.

ALLQUEST HOME MORTGAGE
CORPORATION,
f/k/a/ ALLIED HOME MORTGAGE
CORPORATION,
AMERICUS MORTGAGE
CORPORATION,
f/k/a/ ALLIED HOME MORTGAGE
CAPITAL CORPORATION,
JIM C. HODGE, and JEANNE L. STELL,

Defendants.

12 Civ. 02676 (GCH)

**THIRD AMENDED
COMPLAINT-
IN-INTERVENTION OF THE
UNITED STATES OF AMERICA**

JURY TRIAL DEMANDED

The United States of America, by its attorney, Kenneth Magidson, United States Attorney for the Southern District of Texas, having filed a notice of intervention pursuant to 31 U.S.C. § 3730(b)(4), brings this complaint-in-intervention against Americus Mortgage Corporation, formerly known as Allied Home Mortgage Capital Corporation (“Allied Capital”), Allquest Home Mortgage Corporation, formerly known as Allied Home Mortgage Corporation, formerly known as Allied Mortgage Corporation Coast to Coast, and formerly known as Allied Mortgage Corporation (“Allied Corporation”) (collectively, the “Allied Companies”), the Allied Companies’ President and Chief Executive Officer Jim C. Hodge, and their Executive Vice President and Director of Compliance, Jeanne L. Stell, alleging upon information and belief as follows:

INTRODUCTION

1. This is a civil fraud action by the United States of America to recover treble damages and civil penalties under the False Claims Act, as amended, 31 U.S.C. §§ 3729 *et seq*, and civil penalties under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (“FIRREA”), 12 U.S.C. § 1833a, arising from fraud on the United States Department of Housing and Urban Development (“HUD”) in connection with the Allied Companies’ residential mortgage lending business. As set forth more fully below, the Allied Companies have profited for years as two of the nation’s largest FHA lenders by engaging in reckless mortgage lending, flouting the requirements of the FHA mortgage insurance program, and repeatedly lying about their compliance. In the past decade, Allied Capital and Allied Corporation have originated loans out of hundreds of branches that were never disclosed to HUD, submitted knowingly false statements to HUD concerning branch operations and accumulating sanctions, and lied to conceal their dysfunctional operations from HUD. This decade of concealed misconduct has resulted in

tens of thousands of defaulted loans, thousands of American homeowners facing eviction, and hundreds of millions of dollars in losses to the United States. Compounding the loss to taxpayers, Allied Corporation engaged in a years-long practice of recklessly underwriting thousands of loans it sponsored or originated. HUD has already paid more than \$260 million in defaulted loans underwritten by Allied Corporation, and will be faced with ever increasing as more of these loans default.

2. HUD, through its Federal Housing Administration (“FHA”), insures lenders against losses to homebuyers. FHA insures approximately one third of all new residential mortgages in the United States and is the largest mortgage insurer in the world. Under HUD’s mortgage insurance program, if a homeowner defaults on the loan and the mortgage holder forecloses on the property, HUD will pay the mortgage holder the balance of the loan and assume ownership and possession of the property. HUD incurs expenses in managing and marketing the foreclosed-upon property until it is resold.

3. By protecting lenders against defaults on mortgages, FHA mortgage insurance encourages lenders to make loans to millions of Americans who could not otherwise qualify for a mortgage. FHA mortgage insurance also makes mortgage loans valuable for sale on the secondary market.

4. The continued availability of FHA mortgage insurance requires that HUD accurately assess the risk of default on the loans it insures. To accomplish this task, HUD relies on assurances by lenders that the loans they submit for insurance comply with HUD standards and guidelines specifically designed to mitigate the risk to HUD, including, that the loan originated

from a HUD-approved lender and a HUD-approved branch office, and be properly underwritten to ensure that the borrower will be able to repay the loan.

5. Allied Capital, which once billed itself as one of the nation's largest privately-held mortgage brokers, was, until recently, an approved FHA loan correspondent. As a loan correspondent, Allied Capital had the authority to originate HUD-insured mortgage loans for sale or transfer to other qualifying mortgagees, known as "sponsor" mortgagees. Between January 1, 2001, and the end of 2010—when HUD discontinued the loan correspondent program—Allied Capital originated 112,324 home loans. Of those loans, 35,801 (or nearly 32% percent) have defaulted, resulting in more than \$834 million in insurance claims paid by HUD. Of the defaulted loans, 6,404 were early payment defaults, (*i.e.*, loans that defaulted within the first six months). In 2006 and 2007, Allied Capital's default rate climbed to a staggering 55%, and its early payment default rate exceeded 10%. The loans originated in just that two-year period resulted in \$170 million in insurance claims paid by HUD. Finally, approximately 2,500 loans are currently in default but not yet in claims status, which could result in additional insurance claims paid by HUD amounting to \$363 million.

6. Allied Corporation has been a HUD-approved mortgagee since 1991 and Direct Endorsement Lender since 1992, and, until recently, advertised itself as one of the nation's largest privately held mortgage bankers and one of the nation's largest FHA lenders. A majority of Allied Corporation's lending activity involved FHA-insured loans, and the majority of the FHA-insured loans that it underwrote were loans from its loan correspondent, Allied Capital.

7. While Allied Capital and Allied Corporation made substantial profits through their origination and sale of FHA-insured mortgages, they willfully violated the requirements that

provide protection to HUD's insurance fund and deceived HUD along the way. For instance, for years Allied Capital originated loans out of hundreds of "shadow" branches that were not approved by HUD, then submitted those loans to HUD using one of the unique branch identification numbers ("HUD IDs") assigned to a HUD-approved branch. HUD endorsed these loans for insurance based on false certifications that the loans were originated in compliance with HUD requirements, including, most fundamentally, that the loans originated from HUD-approved branches. Allied Corporation was aware that Allied Capital was continually violating HUD requirements, but rather than requiring its loan correspondent to cease its prohibited conduct, Allied Corporation instead elected to continue the practice of originating loans out of shadow branches after it acquired Allied Capital's branches in May 2010. Although several senior managers voiced concerns about this practice, it was continued under the direction of the Allied Companies' CEO, Jim Hodge.

8. Even when Allied Capital and Allied Corporation sought HUD approval for their branches, they lied to obtain that approval. Each time Allied Capital opened a new branch and applied for HUD approval, it falsely certified that the branch office met all HUD/FHA requirements and, specifically, that Allied Capital would pay all operating costs of the branch office. However, Allied Capital maintained a corporate policy of requiring branch managers to assume financial responsibility for their branches. Allied Corporation was aware of this practice and continued it after it acquired Allied Capital's branches in 2010, while falsely certifying to HUD its compliance with the applicable rules and regulations. Allied Capital, and later, Allied Corporation, thus operated their branches like franchises, collecting revenue while the branches were profitable, then closing them without notice when they were not, leaving the branch

managers liable for the branch's financial obligations. Well aware that this practice was prohibited by HUD, the Allied Companies' Executive Vice President, Jeanne Stell, instructed branch managers how to answer questions from HUD auditors, and acknowledged in an email that she instructed someone else to sign the certifications to HUD because she knew that they were false. More recently, after the Government's original complaint was filed, Hodge spent the salary and commissions owed to his branch managers, using that money to fund loans after Allied Corporation's warehouse lines of credit were frozen, then summarily closed the remaining branches, leaving the branch managers both on the hook for financial obligations and without any money to pay them.

9. Allied Capital and Allied Corporation—which shared a quality control department—also failed to implement an internal quality control plan, effectively allowing their shadow branches to operate independently of any scrutiny whatsoever. Allied Capital utterly failed to conduct audits of its branches or review its early payment defaults as it was required to do by HUD. Indeed, neither of the Allied Companies ever hired an adequate or trained staff to conduct quality control. Even while operating 600 or more branches at a time, the Allied Companies maintained only two quality control employees in their corporate office.

10. The Allied Companies maintained a handful of additional quality control staff members in St. Croix, in the U.S. Virgin Islands, but their offshore employees had no mortgage experience and, according to multiple witnesses, did not even know what a mortgage was. The Allied Companies nonetheless falsely certified to HUD their compliance with HUD's quality control requirements.

11. The Allied Companies even went so far as to submit falsified quality control reports to HUD. For example, when HUD asked Allied Capital to provide up-to-date quality control reports in early 2009, Allied Capital simply could not comply. Nevertheless, at the direction of Hodge, Allied Capital concealed its failure by preparing reports without conducting the requisite loan file review and then submitted fraudulent quality control reports to HUD. Allied Corporation likewise submitted false quality control reports to HUD around the same time, falsely indicating that it had timely completed loan file reviews or had conducted proper quality assurance reviews.

12. Finally, Allied Capital concealed from HUD information it was obligated to disclose, including information about sanctions by state regulators and felony convictions of employees. Such information would have alerted HUD to Allied Capital's lack of internal controls and habitual disregard of regulations. Allied Capital faced sanctions by one or more states every year for many years, yet repeatedly certified to HUD that it had not been sanctioned by any state in which it operated. Here too, Allied Corporation was aware of this improper conduct on the part of its loan correspondent, yet did nothing to stop it.

13. Allied Capital and Allied Corporation operated with impunity for many years due to a culture of corruption created by Hodge, who eliminated the position of chief financial officer and other senior management positions at Allied Capital, intimidated employees by spontaneous terminations and aggressive email monitoring, and silenced former employees by actual and threatened litigation against them. As a result, the Allied Companies were able to conceal their dysfunctional operations and maintain their profitable position in the mortgage industry.

14. In addition to its culture of corruption, Allied Corporation was plagued by a pattern of recklessness that infected every aspect of its loan underwriting process. As a result, approximately 10% of loans underwritten by Allied Corporation have already resulted in FHA insurance claims, with countless more to come.

15. The United States seeks the maximum amount of damages and the maximum amount of civil penalties allowed by law. Specifically, the United States seeks treble damages under the False Claims Act and compensatory damages under the common law theory of indemnification for each of the Allied Companies' defaulted loans. The United States also seeks to recover damages and civil penalties under FIRREA for each of the hundreds of false certifications and other false statements submitted to HUD.

JURISDICTION AND VENUE

16. This Court has jurisdiction pursuant to 31 U.S.C. § 3730(a), 28 U.S.C. §§ 1331 and 1345, and the Court's general equitable jurisdiction.

17. Venue is proper in this judicial district pursuant to 28 U.S.C. §§ 1391(b)(1) and (c) and 31 U.S.C. § 3732(a) because the defendants can be found and/or transact business in this judicial district, and/or because an act proscribed by 31 U.S.C. § 3729 occurred in this judicial district.

PARTIES

18. Plaintiff is the United States of America.

19. Relator Peter Belli, deceased as of February 20, 2012, was an individual domiciled in Massachusetts and a former branch manager for Allied Capital.

20. Defendant Allied Capital is a Texas corporation with its principal place of business located in Houston, Texas. Until recently Allied Capital billed itself as one of the nation's largest privately held mortgage brokers and was approved by HUD to be an FHA loan correspondent, meaning it had the authority to originate HUD-insured mortgage loans for sale or transfer to other qualifying mortgagees, known as "sponsor" mortgagees for underwriting and closing. Allied Capital was an approved loan correspondent from approximately September 26, 1991 until December 31, 2010, when HUD discontinued the loan correspondent program. Allied Capital is owned 49.5% by Jim Hodge, 49.5% by Jim Hodge's wife, Kathy Hodge, and 1% by Jim Hodge's son, Jamey Hodge. On or about January 23, 2012, Allied Capital changed its name with the Secretary of State of Texas to "Americus Mortgage Corporation."

21. Defendant Allied Corporation is also a Texas corporation with its principal place of business in Houston, Texas. Until recently Allied Corporation billed itself as one of the nation's largest privately held mortgage bankers and one of the nation's largest FHA lenders. Allied Corporation has been approved by HUD since 1992 to be a Direct Endorsement Lender and thus had the ability to "sponsor" loans originated by Allied Capital by underwriting and endorsing those loans for HUD insurance.

22. In May 2010, Allied Capital sold substantially all of its assets to Allied Corporation, and throughout late 2010 and early 2011, Allied Capital terminated nearly all of its branch offices and reopened them as branches of Allied Corporation. According to numerous witnesses, apart from changes in signage, the conversion of branches from the ownership of Allied Capital to Allied Corporation resulted in no changes to branch operations. Allied Corporation continued the business of Allied Capital, operated nearly all of the same branches, and employed

nearly all of the same senior managers. Specifically, Hodge and Stell maintained the same roles at both companies and the two companies maintained the same general counsel, chief financial officer (although this position has remained empty for years), secretary, corporate comptroller, accounting department, information technology department, and quality control department. Allied Capital and Allied Corporation also have the same address and the same ownership structure. On or about January 10, 2012, Allied Corporation changed its name with the Secretary of State of Texas to “Allquest Home Mortgage Corporation.”

23. Defendant Jim Hodge is the founder, President and Chief Executive Officer of both Allied Capital and Allied Corporation, the sole director of both companies, and an individual with domiciles in Texas, St. Croix, Colorado, and South Dakota. According to witnesses, Hodge is heavily involved in the management and operations of his companies, and “approves every major decision.” In addition to owning Allied Capital and Allied Corporation, Hodge owns dozens of companies in the United States, the U.S. Virgin Islands, and the Cook Islands.

24. Defendant Jeanne Stell is a Texas resident and was the Executive Vice President and Director of Compliance of both Allied Capital and Allied Corporation. Stell has held a senior management position and served as the Director of Compliance for both Allied Capital and Allied Corporation since approximately 2001, with the exception of a temporary absence between November 2007 and early 2010. During the aforementioned period, when Stell was not in a senior management position, she worked at times, for other Hodge-owned companies, including in 2009 for the Hodge-owned quality control company that supposedly performed quality control work for both of the Allied Companies.

CIVIL STATUTES TO COMBAT MORTGAGE FRAUD

25. The False Claims Act provides liability for any person (i) who “knowingly presents, or causes to be presented, a false or fraudulent claim for payment or approval;” or (ii) who “knowingly makes, uses, or causes to be made or used, a false record or statement material to a false or fraudulent claim.” 31 U.S.C. § 3729(a)(1)(A) (as amended), 31 U.S.C. § 3729(a)(1) (2006), and 31 U.S.C. § 3729(a)(1)(B) (as amended), 31 U.S.C. § 3729(a)(2) (2006).

26. The False Claims Act further provides that for persons who violate the Act: “[such person] is liable to the United States Government for a civil penalty of not less than [\$5,500] and not more than [\$11,000] . . . , plus 3 times the amount of damages which the Government sustains because of the act of that person” 31 U.S.C. § 3729(a); 28 U.S.C. § 2461 note; Pub. L. No. 104-410 (raising the penalty range for violations of the FCA).

27. Congress enacted FIRREA in 1989 to reform the federal banking system. Toward that end, FIRREA authorizes civil enforcement of enumerated criminal predicate offenses—as established by a preponderance of the evidence—that affect financial institutions and certain government agencies. *See* 12 U.S.C. § 1833a(e). Two of the predicate offenses that can form the basis of liability under FIRREA are relevant here. First, 18 U.S.C. § 1006 prohibits any person, who is “connected in any capacity with [HUD]” from “mak[ing] any false entry in any book, report or statement of or to [HUD]” with the “intent to . . . deceive any officer, auditor, examiner, or agent . . . of [a] department or agency of the United States.” Second, 18 U.S.C. § 1014 (as amended on July 30, 2008) prohibits any person from “knowingly mak[ing] any false statement or report . . . for the purpose of influencing in any way the action of [FHA].” *Id.*

28. FIRREA provides that the United States may recover civil penalties of up to \$1 million per violation, or, for a continuing violation, up to \$5 million or \$1 million per day, whichever is less. The statute further provides that the United States can recover the amount of any gain to the person committing the violation, or the amount of the loss to a person other than the violator stemming from such conduct, up to the amount of the gain or loss.

FACTUAL BACKGROUND

A. The FHA Mortgage Insurance Program

29. Pursuant to the National Housing Act of 1934, the FHA offers various mortgage insurance programs. Through these programs, FHA insures approved lenders (“mortgagees”) against losses on mortgage loans made to buyers of single-family housing. The program helps low-income and moderate-income families become homeowners by lowering some of the costs of their mortgage loans. FHA mortgage insurance encourages lenders to make loans to creditworthy borrowers who nevertheless might not meet conventional underwriting requirements. In the mortgage industry, HUD-insured loans are highly marketable for resale to investors both because such loans are expected to have met HUD requirements and because they are backed by the full faith and credit of the United States.

30. In the event that a borrower defaults on an FHA-insured mortgage, the holder of the loan submits a claim to HUD for the costs associated with the defaulted mortgage and the sale of the property. HUD then pays off the balance of the mortgage and other related costs, and may assume ownership of the property. If a homeowner defaults on a loan and the mortgage holder forecloses on the property, HUD will pay the mortgage holder the balance of the loan and assume ownership and possession of the property.

31. A fundamental rule of the HUD insurance program is that a lender must be approved by HUD to originate, purchase, hold, or sell HUD/FHA-insured mortgages. Accordingly, to participate in the HUD insurance program, lenders were required to submit an application to HUD. Allied Corporation submitted its application to become a mortgagee in December 1990.¹ In its application, Allied Corporation agreed (among other things) that, if approved by HUD, “[i]t will comply with the provisions of the HUD Regulations and other requirements of the Secretary of HUD.” Allied Corporation was approved as a mortgagee in March 1991. Allied Corporation subsequently applied for approval as a Direct Endorsement Lender, making similar representations, and was approved as a Direct Endorsement Lender in February 1992.

32. By obtaining approval as a mortgagee and Direct Endorsement Lender, Allied Corporation was able to certify loans for FHA insurance, meaning that the loans were insured from all loss. Allied Corporation could then sell these FHA-insured loans at a substantially higher premium than a traditional loan. In addition, FHA-approval allowed Allied Corporation to market itself as an FHA-approved lender. A HUD-approved Direct Endorsement Lender, such as Allied Corporation, is authorized to underwrite mortgage loans, decide whether the borrower represents an acceptable credit risk for HUD, and certify loans for FHA mortgage insurance without prior HUD review or approval.

33. Allied Capital submitted an application to HUD seeking approval as a loan correspondent, which application was approved by HUD in September 1991.

¹ At the time of its application, Allied Home Mortgage Corporation was doing business as Allied Mortgage Corporation.

34. A HUD-approved loan correspondent, such as Allied Capital, can originate loans, but is required to send them to a HUD-approved Direct Endorsement Lender, such as Allied Corporation, for underwriting approval prior to loan closing and securing an insurance endorsement from HUD. Based on the information gathered by the loan correspondent, the sponsor mortgagee underwrites the loan and decides whether the borrower represents an acceptable credit risk for HUD.

35. For a loan correspondent, such as Allied Capital, HUD requires not only that the lender be approved generally but also that the lender obtain HUD approval for each branch office from which the lender intends to originate HUD-insured loans.

36. To obtain HUD approval to originate FHA loans from a specific branch office, the loan correspondent must submit a form (HUD Form 92001-B) to HUD containing basic information about the branch, a general certification that the branch “meets all HUD/FHA requirements,” and a specific certification that the lender “will pay all operating costs of the branch office”

37. The purpose of requiring the lender to pay operating costs of its branch office is to prevent the lender from operating “net branch” or “franchise” offices that provide a potential revenue stream at little cost to the lender. Although lenders are permitted to pay branch managers the commission resulting from branch revenue minus branch expenses, they must remain the financially responsible party and be the ultimate guarantor on branch contractual obligations. If a lender is permitted to operate “no cost” branches by paying its branch managers purely on commission and assuming no ultimate financial responsibility for the branch, it will have an incentive to add far more branches than it can effectively supervise and control.

38. After submitting the certification, the loan correspondent receives a HUD ID that permits the branch to originate FHA loans. To monitor lender default rates on a branch-by-branch basis, HUD requires lenders to enter the specific HUD ID for the originating branch in every loan file submitted to HUD.

39. If a branch's default rate exceeds 200% of the regional average for HUD approved lenders, HUD issues a "Credit Watch Termination" that revokes the lender's approval to originate FHA loans at that branch and suspends approval of any new branches within a specified area. This area, roughly the size of a state, is formally referred to as a "HUD field office jurisdiction."

40. To maintain HUD-approved status, loan correspondents and Direct Endorsement Lenders must also submit annual certifications to HUD. The annual certifications contain four distinct representations, set forth below:

I certify that none of the principals, owners, officers, directors, and/or employees of the above-named lender is currently involved in a proceeding and/or investigation that could result, or has resulted in a criminal conviction, debarment, limited denial of participation, suspension, or civil money penalty by a federal, state, or local government.

I certify that the above named lender has not been refused a license and has not been sanctioned by any state(s) in which it originates and/or services HUD-FHA insured loans.

I know, or am in the position to know, whether the operations of the above named lender conform to HUD-FHA regulations, handbooks, and policies.

I certify that to the best of my knowledge, the above named lender conforms to all HUD-FHA regulations necessary to maintain its HUD-FHA approval, and that the above named lender is fully responsible for all actions of its employees including those of its HUD-FHA approved branch offices.

41. Among the requirements for both loan correspondents and Direct Endorsement Lenders to maintain HUD-FHA approval is that they implement a quality control program, which,

among other things, ensures compliance with certain key HUD requirements. *See* HUD Handbook 4060.1, REV-2, paragraph 7-1; 24 C.F.R. § 202.5(h). A proper quality control program must meet the following goals: (1) assure compliance with FHA's and the mortgagee's own origination or servicing requirements throughout its operations; (2) protect the mortgagee and FHA from unacceptable risk; (3) guard against errors, omissions and fraud; and (4) assure swift and appropriate corrective action. *See* HUD Handbook 4060.1, REV-2, paragraph 7-2; *see also* 24 C.F.R. § 202.5(b) (lender "shall employ competent personnel trained to perform their assigned responsibilities").

42. As part of its quality control program, a mortgagee must (a) employ qualified staff, (b) conduct an on-site audit of all branch offices within 90 days of opening and annually thereafter; (c) review 10% of all closed loan files to ensure they were underwritten in accordance with HUD guidelines; and (d) review all early payment defaults (*i.e.*, those that default within the first six months). *See* HUD Handbook 4060.1, REV-2, paragraph 7-3. Review of early payment defaults is particularly important because such defaults are indicative of mortgage fraud.

43. In addition, HUD regulations provide that each Direct Endorsement Lender is responsible for the actions of its loan correspondents in originating loans or mortgages. *See* 24 C.F.R. § 202.8(b)(7) (2002-2010); *see also* HUD Handbook 4060.1, paragraph 7-3(H). The Direct Endorsement Lender is required to supervise its loan correspondents and ensure that they operate in compliance with FHA requirements, including, but not limited to, HUD's branch office origination requirements and HUD's quality control requirements. *See* HUD Handbook 4060.1, paragraphs 2-19, 5-8, and 7-3.

44. Finally, each loan file submitted for HUD insurance contains a loan-specific certification –HUD Form 92900-A– in which a lender certifies that the information contained in the application is “true to the best of the lender’s knowledge and belief.” If, when the loan “is submitted [to HUD] for endorsement, HUD has evidence that there is fraud or misrepresentation on the part of the originating mortgagee, HUD will consider the certifications as fraudulent and will not endorse the mortgage for insurance.” HUD Handbook 4000.4, paragraph 1-3.

B. The FHA’s Direct Endorsement Program

45. To qualify for FHA mortgage insurance, a mortgage must meet all of the applicable HUD requirements (e.g., income, credit history, valuation of property, etc.). Under the Direct Endorsement process, HUD does not itself conduct a detailed review of applications for mortgage insurance before an FHA-insured mortgage closes. Rather, approved Direct Endorsement Lenders are responsible for all aspects of the mortgage application, the property analysis, and the underwriting of the mortgage and must determine whether the proposed mortgage is eligible for FHA insurance under the applicable program regulations. A Direct Endorsement Lender underwrites and closes mortgages without prior HUD review or approval. Direct Endorsement Lenders submit documentation (the Case Binder) produced in connection with the underwritten loans after the mortgage has closed, and certify that the endorsed mortgage complies with HUD rules. If a lender has been approved under HUD’s Lender Insurance program, the lender endorses the mortgage on HUD’s behalf and the Case Binders are held the lender. The lender sends the Case Binder to HUD only upon request.

46. Under HUD’s Direct Endorsement Program, the Direct Endorsement Lender originates a proposed loan, or in some instances, acts as a sponsoring lender by underwriting and

funding proposed mortgages originated by loan correspondents. In either case, the Direct Endorsement Lender ultimately reviews the proposed mortgage. The borrower, along with the Direct Endorsement Lender representative, completes the loan application. A loan officer collects all supporting documentation from the borrower and submits the application and documentation to the Direct Endorsement Lender. The Direct Endorsement Lender obtains an appraisal. A professional underwriter employed by the Direct Endorsement Lender performs a mortgage credit analysis to determine the borrower's ability and willingness to repay the mortgage debt in accordance with HUD rules. The Direct Endorsement Lender underwriter makes the underwriting decision as to whether the mortgage may be approved for FHA insurance or not, according to HUD rules. If the underwriter decides that the mortgage may be approved for FHA insurance in accordance with HUD rules, the Direct Endorsement Lender closes the loan with the borrower. Thereafter, the Direct Endorsement Lender certifies that the mortgage qualifies for FHA insurance (a "loan level certification"). FHA endorses the loan on the basis of the Direct Endorsement Lender certification and provides the Direct Endorsement Lender with a mortgage insurance certificate.

47. The underwriter's responsibilities are critical elements of the Direct Endorsement Program. An underwriter must be a full time employee of the mortgage lender and must either be a corporate officer with signatory authority or otherwise be authorized to bind the mortgage lender in matters involving origination of mortgage loans. An underwriter must also be a reliable and responsible professional who is skilled in mortgage evaluation and able to demonstrate knowledge and experience regarding principles of mortgage underwriting, including detecting warning signs that may indicate irregularities, as well as detecting fraud. HUD Handbook 4000.4 REV-1, ¶

2-4(C)(5); see also HUD Handbook 4155.2 ¶ 2.A.4.b. The lender must also maintain a compliant compensation system for its staff, an essential element of which is the prohibition on paying commissions to underwriters. HUD Handbook 4060.1 REV-2, ¶ 2-9(A). A Direct Endorsement Lender must certify that its underwriters meet FHA qualifications.

48. The underwriter must “evaluate [each] mortgagor’s credit characteristics, adequacy and stability of income to meet the periodic payments under the mortgage and all other obligations, and the adequacy of the mortgagor’s available assets to close the transaction, and render an underwriting decision in accordance with applicable regulations, policies and procedures.” 24 C.F.R. § 203.5(d). In the event a loan scores an Accept rating through a HUD approved automated underwriting system, the underwriter does not certify to the evaluation of the borrower credit, but instead, certifies that the data utilized in obtaining the “Accept” rating has integrity. In addition, the underwriter must “have [each] property appraised in accordance with [the] standards and requirements” prescribed by HUD. 24 C.F.R. § 203.5(e).

49. The loan level certification from the lender for each loan contains specific representations by the underwriter that the “mortgage is eligible for HUD mortgage insurance under the Direct Endorsement program,” including HUD Handbook 4004.4.

50. Absent a truthful loan level certification, a Direct Endorsement Lender is not entitled to endorse a particular loan for FHA insurance.

C. The Allied Companies' Deception of HUD

1. The Allied Companies Originate Loans Out of Unapproved "Shadow" Branches

51. For years, Allied Capital originated thousands of FHA loans out of branches that were not HUD approved. Allied Capital originated these loans by "marrying" an unapproved branch to an approved branch and entering the HUD ID of an approved branch on all loans originated from the "shadow" branch. In the last decade, Allied Capital has operated hundreds of shadow branches, including in regions where HUD terminated Allied Capital's approval to originate FHA loans.

52. In operating its shadow branches, Allied Capital was well aware that it was flouting HUD's requirements. In 2000, a HUD audit of two branch offices in Arizona found that Allied Capital was operating thirteen unapproved "satellite" offices, one of which originated 221 loans in 24 months, "more than [Allied's] registered branch offices and satellite offices combined."

53. Although in 2000 HUD permitted the use of unapproved "satellite offices" for certain limited activities, satellite offices could not originate FHA loans.

54. In 2002, HUD revisited the branch offices in Arizona and again found Allied Capital to be originating FHA-insured loans out of satellite offices. HUD requested indemnification for the loans originated from the non-approved offices and reminded Allied that any "office that originates and processes FHA-insured mortgages must be approved by HUD."

55. Finally, a June, 2005 review of a branch in Fresno, California revealed that "Allied failed to seek HUD's approval for several branch locations where FHA insured loans are

originated and processed. This practice violates the certifications made on HUD Form 92900A [the individual loan certification].”

56. By 2006, HUD no longer permitted even limited-use satellite offices and required that every office that originated or processed FHA loans in any way had to be approved by HUD, thereby creating a bright-line rule for enforcement. Allied Capital’s Executive Vice President, Jeanne Stell, thereafter sent a memo to all branch managers, notifying them that the revised HUD Handbook required that “FHA loans must be originated and processed from a ‘HUD/FHA registered/approved’ location.”

57. Even while reminding branch managers of HUD’s requirement, however, Allied Capital continued to violate it, operating newly-opened shadow branches in regions where HUD terminated its approval to originate FHA loans.

58. In March of 2006, HUD issued a Credit Watch Termination of Allied Capital’s origination authority within the Greensboro, North Carolina HUD field office jurisdiction, thereby barring Allied Capital from originating FHA loans from the branch that prompted the termination as well as from newly-opened branches throughout North Carolina.

59. Notwithstanding its termination, Allied Capital continued to open new branches in that area, approximately one or two per month, and nearly all of those branches secretly originated FHA loans. Allied Capital achieved this deception by submitting the loans to HUD under the HUD ID numbers of other, still-approved branches.

60. Several senior managers raised their concerns about Allied Capital’s practice with Hodge. The practice persisted, however; the decision to do so, according to witnesses, was “mainly Jim’s decision.”

61. Although Allied Capital sought HUD approval for a total of eight branches in North Carolina, it originated FHA loans out of more than *seventy* shadow branches in that state without HUD's knowledge or approval.

62. Allied Capital's default rates should have prompted earlier and additional Credit Watch Terminations, but Allied Capital manipulated the HUD ID system to conceal its true default rates. Specifically, Stell monitored the default rate of each branch and applied for a new HUD ID for any branch whose default rate approached 200%. When applying for a new HUD ID, Stell changed the address of the branch superficially (*e.g.*, adding a Suite number, or changing "Street" to "St."), so that the automated FHA system could not detect that the ID was sought for an existing branch. The new ID provided a brand new default rate, clearing the past rate.

63. When HUD updated its system to prevent such manipulation, Allied Capital found a new way to conceal its default rates. In late 2010 and early 2011, Allied Capital switched all of its remaining, approved branches from the ownership of Allied Capital to Allied Corporation, thereby obtaining a new ID for each branch, and thus again achieving a clean slate on its default rates.

64. Allied Capital's use of shadow branches was not limited to North Carolina. In Michigan, Allied operated approximately fifty shadow branches, and in other states, as many as twenty shadow branches operated under a single HUD ID.

65. According to witnesses, Allied Capital operated shadow branches through 2010. One former employee tasked with obtaining FHA case numbers for FHA loans was instructed that for any branch that did not have a HUD ID, she should use the HUD ID of a nearby, approved branch. Another former employee instructed to supply HUD IDs to shadow branches raised her

concerns with Stell's assistant, who assured her that they were acting on Hodge's instruction and showed her a printed-out email from Hodge endorsing the practice.

66. Allied Corporation was well aware that its loan correspondent, Allied Capital, improperly originated loans from shadow branches. Allied Corporation and Allied Capital have the same ownership structure and the same management, share employees, and are located in the same building. There is no clear and effective separation of their respective operations.² In addition, Hodge, as the CEO and owner of both companies, micromanaged both of the Allied Companies and "approved every major decision." Allied Corporation, under the direction of Hodge, took no steps to halt the improper practices of its loan correspondent. To the contrary, at Hodge's direction, Allied Capital continued this practice despite the fact that employees raised concerns.

67. Unsurprisingly, given the common management of both companies, Allied Corporation continued the practice of originating loans out of unapproved shadow branches while using the branch ID of an approved branch office after it acquired Allied Capital's branches in 2010. For instance, in 2011, Allied Corporation originated loans out of unapproved shadow branches in Maryland and West Virginia. Upon information and belief, these were not isolated incidents, but rather were part of a systemic practice continued by Allied Corporation under the direction and control of Hodge.

68. In sum, the Allied Companies operated hundreds of shadow branches at the direction of Hodge, in order to evade HUD oversight scrutiny. As explained more fully below, the Allied Companies could not and did not audit and supervise all of their hundreds of branches,

² In fact, Allied Corporation is the registered owner of the trademark Allied Home Mortgage Capital Corporation. See U.S. Patent & Trademark Office Registration No. 3084646.

and, as long as they concealed these branches, HUD could not audit them either. The Allied Companies nevertheless profited from these shadow branches and obtained FHA mortgage insurance for loans originated out of them by knowingly creating false records and certifications and submitting them to HUD.

69. The Government estimates that Allied Capital's shadow branches alone are responsible for defaulted loans resulting in at least \$150 million in insurance claims paid by HUD.

2. The Allied Companies Deceive HUD about Their Branch Operations

70. Allied Capital, and later Allied Corporation, were equally deceptive about their practices at approved branches. Each time Allied Capital or Allied Corporation sought approval for a branch office, the company certified that it complied with HUD requirements and that it "paid the operating costs of the branch office." These certifications were knowingly false. The Allied Companies instead maximized their profits by opening and collecting revenue from more than 2000 branches, while failing to supervise and assume financial responsibility for them.

71. In 2000, Allied Capital's employment agreements with branch managers provided that (i) branch managers indemnify Allied Capital from any and all claims, losses, damages, fines, and "liability of every kind;" (ii) branch managers be charged for core expenses, including "office space, telephones, facsimile machines, equipment, supplies, advertising, payroll expenses, and insurance;" and (iii) Allied Capital could "require that a portion of the compensation, although earned by [the branch manager], be held in a reserve account for future possible losses or expenses incurred by [the branch manager]."

72. When HUD audited Allied Capital in early 2001, it found that its employment agreement violated HUD requirements and, on April 23, 2001, notified Allied Capital that it intended to seek civil penalties.

73. Just one week later, on April 30, 2001, Allied Capital issued an update to its operating manual to all branch managers, referencing HUD Mortgagee Letter 00-15 and stating that “[i]t is important that everyone understand that . . . [Allied] pays all of the operating expenses for each branch including . . . rent, equipment leases, phone bills, payroll and any other expenses incurred by the branch. [Allied] is also the lessee of the space occurred by the [Allied] branches.”

74. Shortly thereafter, Allied Capital prepared an updated chapter on “Examination/Audit Procedure” to its manual, dated August 29, 2001, which provides instructions on steps to follow if a government auditor shows up at a branch, including the following:

- Select ONE PERSON, and one person ONLY in your office to interface and converse with the examiner/auditor . . . No one else in the office should have any conversation with the examiner/auditor prior to, during or after the examination/audit. The only corporate personnel who should converse with the examiner/auditor prior to, during or after the exam/audit should be Jeanne Stell or Jim Hodge. It is important to keep the number of people in contact with the examiner/auditor very limited.”
- You, and any employee working in your branch, are W-2 employees of Allied. Frequently, examiners/auditors view us as a franchise. WE ARE NOT A FRANCHISE. Along those same lines, Allied pays all the bills incurred by the branch. **Both of these statements are true and that is the only way those questions are to be answered, *no deviations!*** (bold and italics in original.)

75. Such a directive itself fails to comply with the HUD Handbook, which requires that a lender “fully cooperate with any investigations brought by HUD[,] . . . make all officers and employees available for interviews and [] promptly provide . . . information and documents requested by HUD.” 4060.1, REV-2, paragraph 2-16 (B).

76. On August 5, 2003, Allied Capital entered into a consent decree with HUD, promising to comply with HUD's requirement that it pay operating costs of Allied Capital's branch offices and paying a civil penalty of \$50,000. Again, that promise was false.

77. Shortly thereafter, in January 2004, Allied Capital applied to the State of New York Banking Department for a mortgage banker's license. Because the State of New York has a similar prohibition against "net branching," Allied Capital's application stated that "Allied has decided to cease using the term 'net branch' to describe its branch operations" and that "although the future compensation of the branch managers is [a]ffected by losses experienced by the branch, the branch manager has absolutely no liability to any third party associated with these losses." That representation was false.

78. Allied Capital added that, should its application be accepted, it planned "to install a state manager in New York to monitor the company's growth and expansion in the State and to further ensure strict compliance with all State and federal regulations . . ." The company further represented that its "nationwide operations are in compliance with all aspects of HUD's requirements for branch offices of HUD/FHA approved mortgagees" (citing HUD Mortgagee Letter 00-15). Despite its representations to HUD and the New York Banking Department, Allied Capital never changed its practices.

79. Allied Capital opened hundreds of branches in the years that followed, viewing the proliferation of branches as a "bragging point" and touting that it had "seven hundred plus branches" or was "on [its] way to a thousand branches." Allied Capital achieved such dramatic growth by recruiting branch managers with the promise that they could exercise greater control

over their offices than they could as branch managers for competing lenders. Allied Capital's on-line advertising and website even prominently displayed the motto "Better Than a Net Branch."

80. Allied Capital's proliferation of branches came at little cost to the company. Allied Capital paid its branch managers pure commission, required them to set aside a "reserve" of at least a thousand dollars, failed to pay operating costs when branches were unprofitable, and continued to limit its financial obligation to its branches to month-to-month subleases.

81. Allied Capital supervised little more than the revenue of its branches. Some branch managers operated for years without ever being audited by the corporate office. And by early 2009, Allied Capital discontinued on-site branch audits entirely.

82. Where senior managers were able to identify problems at branches, and either sought to—or actually did—close them, they frequently encountered resistance from Hodge. For instance, senior managers repeatedly closed down a branch in Texas where they suspected the branch manager—Richard Bell—was committing fraud, only to find that Hodge repeatedly reopened the branch. The branch manager was indicted in 2007 for bank fraud, pled guilty, and was sentenced to ten years in prison for misconduct committed while he remained a branch manager at Allied Capital.

83. When Hodge did decide to close a branch, he ordered it shut down immediately, leaving the branch manager liable for long-term contractual commitments. Allied Capital even required branch managers to pay legal judgments against the company when a lawsuit implicated conduct at their branch.

84. For example, in 2006 a borrower sued Allied Capital over the conduct of a loan officer at an Ohio branch. Allied Capital informed the branch manager that its legal department

would handle the lawsuit. But after Allied Capital was found to be liable, it settled the suit for \$40,000 and sent the branch manager the bill for the settlement amount. When the manager asked why she was required to pay when “we had insurance for this type of thing,” Allied’s corporate office replied, “I do not believe there has ever been an actual judgment of money damages that was not assessed against branch revenue . . . [I]f the case goes to trial and a judgment is entered . . . it is considered a branch operating expense.”

85. In 2007, Allied Capital shut down a branch in Massachusetts, leaving the manager liable for more than a hundred thousand dollars on a multi-year commercial lease. When the landlord demanded that Allied Capital pay the rent, the company refused, stating that “[w]hile Allied made rent payments . . . for several years, those payments were made on behalf of [the branch manager] in order to allow him to meet *his* obligations to you under his lease(s) with you” (italics in original).

86. In 2008, acting on a HUD hotline tip from a former Allied Capital employee, HUD conducted a second audit of five branch offices to determine whether Allied Capital was engaging in prohibited branch operations. HUD issued its audit report as to these branches on February 10, 2009, finding that Allied Capital violated HUD guidelines on branch operations and recommending action by the Mortgagee Review Board. Specifically, HUD found that:

[n]one of the office space lease agreements for the five branches reviewed were in Allied’s name. Instead, the branch managers personally entered into and signed the lease agreements. Four of the five branch managers had signed month-to-month subleases with Allied . . . However, ultimate responsibility for the lease payments continued to rest with the branch manager if Allied canceled the sublease . . . By not directly entering into leases, Allied apparently attempted to main a separation between itself and its branch offices which was inconsistent with the close supervisory control and oversight of its branches required by HUD (citing HUD Mortgagee Approval Handbook 4060.1, REV-2, paragraphs 2-9 A and D).

87. Just days after the 2009 audit report was issued, Stell (who had left Allied temporarily in November of 2008) emailed a link to the audit report to another former employee, who replied that HUD's order requiring "Allied to . . . directly enter into leases and/or agreements and implement the necessary policies, systems, and controls to ensure that it pays all required branch operating costs" was "going to be a big one to comply with."

88. In response, Stell wrote: "What do you think about the part that they want the [HUD] to go after not just Allied but the people responsible for non-compliance. I had [another senior manager] sign the 'add a branch' form for years for HUD as I knew this would eventually happen. It required that you swear the branches meet and will continue to meet HUD's regulations. Jim [Hodge] has to be the biggest target personally for his disregard for the regulations. Serves him right never listening and thinking he didn't have to play by the rules."

89. Allied Capital refused to change its practices even after the 2009 HUD audit report issued. In May of 2009, when the landlord of a recently-closed Missouri branch office sued both Allied Capital and the branch manager for rent due on a five-year commercial lease, Allied Capital filed a cross-claim against the branch manager, alleging that "[b]ecause [the manager], rather than Allied, is liable on the Lease . . . , [he] would be liable to Allied for all such liability, and Allied is entitled to indemnification for all such liability."

90. In responding to HUD, Allied Capital's attorneys presented a different picture. Specifically, Allied Capital's attorneys represented that "Allied did pay the core expenses for the five branch offices reviewed 95% of the time and we are confident with the new operations changes as of today we are 100% compliant and will maintain that level on an ongoing basis."

91. Hodge and other senior management of Allied Corporation were aware that Allied Capital was falsely certifying that it paid the operating expenses of its branches. Yet Allied Corporation took no steps to halt this fraudulent practice of its loan correspondent.

92. To the contrary, when Allied Corporation acquired Allied Capital's assets and converted nearly all of Allied Capital's branches to branches of Allied Corporation in late 2010 and early 2011, Allied Corporation made similar misrepresentations to HUD. Allied Corporation submitted branch certifications (HUD Form 92001-B) to HUD for each branch that it acquired and converted, in which Allied Corporation certified that it would comply with HUD/FHA requirements and would pay the operating expenses of its branch offices. These certifications were false, however, as Allied Corporation had adopted the same net branching practices as Allied Capital. Indeed, Stell emailed a new sublease to almost every branch manager to execute with Allied Corporation, leaving the branch manager as the responsible party on the primary lease.

93. On January 26, 2011, an Iowa branch manager was informed that her branch would be closed that day and that she would be transferred to an office in Illinois as a loan officer (even though she had no Illinois license). As the signatory on all branch contracts, the manager asked the corporate office what Allied Corporation planned to do "about these leases or am I going to be left holding the bag?" In response, Hodge emailed, "Allied corp policy is only a month to month lease we have no control over what you sign or do." Later that day, the branch manager received a call from Hodge's assistant informing her that she would be terminated.

94. Similarly, in November and December 2011, Allied Corporation refused to pay the rent for a branch in New Jersey, and likewise failed to pay the other operating expenses, such as gas, electric, phone, and advertising costs, for this branch.

95. When Allied Corporation closed its remaining branches on November 29, 2011, branch managers across the country found themselves responsible for the branch's continuing financial obligations but without the funds to meet those obligations. Although branch managers had retained salary and commissions, along with a mandatory "reserve" in their branch accounts, as of November 2, 2011, they were unable to withdraw any of the funds owed to them. At the same time, the branch managers were told multiple lies by Hodge as to why their funds were unavailable.

96. At first, Hodge—through his assistant—falsely informed his employees that the Department of Justice had frozen the company's bank accounts. When employees began to raise questions about this, Hodge emailed all employees falsely informing them that "the banks" had frozen the company's accounts, preventing the branch managers from withdrawing their money.

97. Hodge only later admitted that the commissions and other earnings the branch managers had accrued were simply gone. Hodge in fact had used the branch managers' money to fund loans after his warehouse lines of credit were frozen on or about November 2, 2011, then attempted to conceal this fact by lying to his employees about the reason their funds were unavailable for withdrawal.

98. As a result of Hodge's actions, branch managers across the country have faced serious financial harm, which is compounded by the fact that many of them remain personally responsible for outstanding invoices pertaining to branch expenses.

99. In sum, Allied Capital willfully flouted HUD's requirement since at least 2000, and attempted to conceal its practices by submitting false branch certifications to HUD, misrepresenting Allied Capital's practices in responding to HUD audits, and instructing its

employees how to (untruthfully) answer questions from HUD and other auditors. Hodge and other senior management of Allied Corporation were not only aware of Allied Capital's fraudulent conduct, Allied Corporation actually continued this practice after it acquired Allied Capital's branches in 2010. Thus, the Allied Companies' "net branch" system enabled them to reap enormous profits while it left its branch managers unsupervised, uncontrolled, and ultimately liable for costs at its branches.

3. The Allied Companies Fail to Implement a Quality Control Program

100. Given that Allied Capital and Allied Corporation were operating hundreds of branches under the regulatory radar, they alone were responsible for monitoring these branches and their loans. And as HUD-approved lenders, Allied Capital and Allied Corporation were required to maintain quality control plans that included: (a) conducting audits on all early payment defaults; (b) reviewing 10% of all closed-loan files; and (c) conducting on-site branch office reviews within 90 days of opening and once per year thereafter. Allied Capital and Allied Corporation's shared quality control program, however, was either dysfunctional or entirely nonexistent during most of the last decade.

101. Allied Capital conducted on-site branch office audits only sporadically, at best. Although Allied Capital operated between 400 and 650 branches at any given time between 2003 and early 2009, it typically maintained only three branch auditors, and those three auditors had other responsibilities in addition to conducting branch audits. As stated above, some long-time branch managers were never visited by the corporate office, and by 2009, Allied Capital discontinued branch audits entirely.

102. Allied Capital's review of early payment defaults was equally deficient. When Allied Capital hired a new quality control manager in August of 2004, she discovered that the company was not reviewing early payment defaults and was informed by Stell (incorrectly) that the company was not required to conduct such reviews. Similarly, a HUD audit of Allied Capital's quality control department in late 2004 concluded that it "was not doing EPD reviews" and that the only two quality control reports Allied Capital produced to HUD "contain[ed] no information of use." Allied Capital did not even begin conducting reviews of early payment defaults until late 2005 or early 2006.

103. When Allied Capital eventually began conducting reviews of early payment defaults, it was plagued by inadequate and unqualified staffing. Between 2004 and 2008, Allied Capital was originating loans out of several hundred branches, yet had a quality control staff of just *two* in its corporate office to conduct reviews of all early payment defaults. Allied Capital and Allied Corporation maintained 2-5 additional members of their shared quality control department in St. Croix, in the U.S. Virgin Islands. When the quality control manager visited her staff in St. Croix, however, she discovered that they did not know "what HUD was," or even "what a mortgage was."

104. Despite their lack of qualifications, the St. Croix-based employees were hired to work for another Hodge-owned entity called "Allquest Mortgage Capital Corporation," an economic development corporation. As an economic development corporation, Allquest was entitled to receive a 90% reduction in income taxes. In exchange for providing nominal quality control services to Allied Capital and Allied Corporation, Allquest received millions of dollars in management fees that the Allied Companies then deducted as business expenses.

105. When HUD conducted a limited audit of Allied Capital in 2007, it again found that Allied Capital “has not implemented a Quality Control (QC) Plan and is not conducting Quality Control reviews in accordance with HUD criteria.”

106. In October 2008, Allied Capital abruptly fired its quality control manager, informing her that her position was being “eliminated.” Shortly thereafter, however, Allied Capital was asked to provide up-to-date quality control reports to HUD as it was concluding its audit. Allied Capital did not have the reports available, as it was months behind in reviews of early payment defaults.

107. Allied Capital initially attempted to prepare the reports by assigning a few underwriting assistants from Allied Corporation to assist with the reports. The assistants were provided no training but simply handed a checklist of questions to answer as they reviewed each file. One of the assistants complained that she did not know what she was looking for in the loan file, but was told just to work from the checklist.

108. Another member of the quality control department, who later became the quality control manager, reported to Hodge that even with the help from underwriting assistants, the department could not complete the quality control reports on time. Hodge instructed her to make the reports appear complete by indicating that verifications of income, employment, and deposit had been conducted. The employees followed Hodge’s instructions and prepared fraudulent quality control reports, which were then submitted to HUD and other third parties.

109. Allied Corporation, which shared its senior management, including Hodge and Stell, with Allied Capital, was aware that Allied Capital failed to implement or maintain a quality

control program and falsified quality control reports, yet took no steps to bring Allied Capital into compliance with HUD regulations.

110. From a period beginning at least in 2008 (if not earlier), Allied Corporation maintained a corporate policy and practice of knowingly and deliberately flouting HUD's quality control requirements in order to maximize its own profit at the expense of the ensuring the quality of the loans being insured by the HUD/FHA program. For example, even though Allied Corporation was required to ensure that independent, trained, and competent quality control staff performed quality and compliance reviews, *see* 24 C.F.R. § 202.5(b); HUD Handbook 4060.1, REV-2, paragraph 7-3(C), Allied Corporation failed to do so. In 2009, Allied Corporation directed underwriting coordinators with no quality control review experience to perform quality control reviews. Allied Corporation failed to provide its unqualified staff with any training with respect to their assigned quality control functions. In addition, the individuals tasked with conducting the quality control reviews were not independent, but rather were involved in Allied Corporation's day-to-day loan origination business. Upon information and belief, this was not an isolated incident, but rather was a part of Allied Corporation's knowing and ongoing pattern of ignoring HUD's quality control requirements.

111. Similarly, Allied Corporation failed to perform quality control reviews in a timely fashion (*i.e.* within 90 days after the relevant loan closed). *See* HUD Handbook 4060.1, REV-2, paragraph 7-6(A). For example, Allied Corporation failed to timely perform the quality controls reviews for hundreds of loans that closed in 2008 and 2009. Allied Corporation submitted Quality Assurance Division ("QAD") reports to HUD that appeared to show Allied Corporation's compliance with the quality control requirements. However, with respect to at least 145

FHA-insured loans, quality control reports were not performed within the 90-day period prescribed by HUD regulations.

112. Allied Corporation also maintained a corporate policy and practice of failing to properly review and verify loan documents, which is a fundamental part of the quality control process and is required by HUD. *See* HUD Handbook 4060.1, REV-2, paragraph 7-6(E). This process includes, *inter alia*, obtaining credit reports and re-verifying certain information, including employment, income, deposits, alternate credit sources. *See id.* Allied Corporation did not comply with these requirements. For example, one employee was instructed by Stell to skip the reverification questions in Allied Corporation's automated system to make the loan files appear complete. Another former employee was told in 2009, on Jim Hodge's instruction, to skip certain reverification requirements and to make it appear that the quality control review had been completed. In fact, when a former quality control manager became aware that quality control employees were skipping verification steps and informed Hodge, Hodge replied that "it would be fine" to skip these quality control measures. And when another quality control employee raised quality control concerns with Stell, she was fired the next day.

4. Allied Capital Conceals Sanctions and Convictions from HUD

113. In addition to concealing its branch operations and lack of quality control from HUD, Allied Capital concealed prior sanctions and convictions that could have alerted HUD to the risk that the company posed to its insurance fund.

114. To maintain its HUD-approved status, Allied Capital was required to certify each year not only that it complied with all HUD/FHA requirements, but also that it satisfied two more specific conditions. First, Allied Capital was required to certify that: "none of the . . . employees

of the above-named lender is currently involved in a proceeding and/or investigation that could result, or has resulted in a criminal conviction . . . limited denial of participation, [or] suspension . . . by a federal, state, or local government.” Second, Allied Capital was required to certify that it “has not been refused a license and has not been sanctioned by any state(s)” in which it originates loans.

115. The HUD Handbook provides that mortgagees are “ineligible” for approval by HUD if, among other things, any officer, partner, director, principal, or employee of the lender is “[u]nder indictment for, or has been convicted of, an offense that reflects adversely upon the applicant’s integrity, competence, or fitness to meet the responsibilities of an approved mortgagee [or] [s]ubject to unresolved findings contained in a HUD or other governmental audit, investigation . . .” 4060.1, REV-2, paragraph 2-10. *See also* 24 C.F.R. 202.5.

116. Further, a lender that has been subject to a sanction or action against its state license “must submit documentation concerning the action.” HUD Handbook 4060.1, REV-2, paragraph 2-3. Information about sanctions and other government actions is useful to HUD to ensure that its approved lenders are properly supervising their branches and screening the employees they hire.

117. Allied Capital, at the direction of Hodge and over the objections of its human resources manager, repeatedly hired employees whose background checks revealed they were convicted felons. Allied Capital also concealed these convictions as well as numerous state sanctions from HUD. Just a few examples are set forth below.

118. In June 2004, Allied Capital entered into a consent agreement with the Rhode Island Department of Business Regulation, paying \$50,000 and acknowledging that an Allied

Capital branch manager was using his Rhode Island license to operate an unlicensed branch across state lines in Milford, Massachusetts.

119. In December 2005, the South Carolina Department of Consumer Affairs denied a license to a former branch manager in Goose Creek, South Carolina, based on its finding that she had “been convicted of several offenses within the last ten years.” The Goose Creek branch also operated as a shadow branch.

120. In February 2006, the State of Washington Department of Financial Institutions banned Allied Capital’s former branch manager in Spokane, Washington, from working as a mortgage broker after he was convicted of stealing client’s money and laundering it. The Spokane branch also operated as a shadow branch.

121. In May 2006, Allied Capital filed an annual report with the New York State Banking Department, which required it to answer whether any convicted felon served as an employee “during the reported year or any time since.” In response, Allied Capital identified fifteen employees with felony convictions that it had hired (and terminated) in just the 12-month reporting cycle. It added, however, that it “conducts criminal background investigations on all new employees,” that “no person convicted of a felony may be hired in any capacity,” and that “[n]o current company employees have felony convictions.”

122. In July 2006, the Arizona Department of Financial Institutions denied a mortgage broker license to a separate firm owned by Allied Capital’s branch manager in Tucson, Arizona, because the branch manager had been previously convicted of stealing money while working as a bank teller for Bank of America. The Tucson branch also operated as a shadow branch.

123. In November 2007, Allied Capital paid \$30,000 and entered into a second consent agreement with the Rhode Island Department of Business Regulation, resulting from an examination that found six separate violations of Rhode Island law, four of which were recurring violations.

124. In December 2007, Allied Capital's compliance department shut down a shadow branch in Conyers, Georgia, after verifying a tip that the branch manager was a convicted felon running the branch under a fraudulently-obtained identity.

125. In September 2009, when Allied Capital applied for a New York State mortgage broker license, it named as its proposed state manager (the individual tasked with ensuring compliance with all state and federal regulations) a convicted felon who had been sentenced to 60 months in prison for distributing methamphetamines. The employee worked for Allied Capital since 1998 and had been the state manager for New Jersey since 2007, where he was responsible for overseeing fifty-six branches. Despite the employee's long tenure with Allied Capital, he was not identified on its list of employees with felony convictions provided to the state banking department, nor were any of the other individuals referred to above.

126. Allied Capital avoided additional state sanctions by deceiving state regulators about its compliance. Among other things, Allied Capital sought to save money on state-required surety bonds by having them issued from another Hodge-owned entity in the Cook Islands, Mercantile Insurance & Fidelity Company ("Mercantile"). The purpose of such bonds is to assure the recovery of penalties imposed by state regulators for non-compliance with regulations.

127. Mercantile was never licensed to do business in any state and was little more than a shell company. Nevertheless, Mercantile issued bonds in numerous states between 2003 and

2010. Allied Capital's licensing department, aware that Mercantile was another Hodge-owned entity not licensed to issue bonds in any state, was "told to write bonds in all states until 'something happened'." As of early 2010, Mercantile had issued bonds as part of Allied Capital's state licensing requirements in twelve different states, for a total bond amount in excess of \$2 million.

128. As the senior compliance officer for Allied Capital, Stell had knowledge of all of the above sanctions. In addition, Hodge was told "as a matter of course" anytime Allied Capital was sanctioned by a regulatory agency. Stell and Hodge were likewise aware that Allied Capital did not conform to all HUD/FHA regulations necessary to maintain its HUD/FHA approval, including HUD's quality control requirements. Allied Capital nonetheless submitted unqualified annual certifications for the fiscal years ending June 30, 2004, June 30, 2006 and June 30, 2007, each of which was signed by Stell, and an unqualified annual certification for the fiscal year ending June 30, 2008, which was signed by Hodge. The annual certifications submitted to HUD were therefore knowingly false.

129. Allied Capital's concealed corruption continued in part because Hodge persistently monitored and intimidated senior managers and other employees. For instance, Hodge provided his assistant with full access (including the ability to delete emails) to the email accounts of several key employees, including Allied Capital's general counsel, senior compliance officers, quality control managers, and others.

130. Hodge also required employees to sign extremely broad confidentiality agreements and has sued numerous former employees for the slightest perceived breach, including a former tax manager for speaking to the IRS. In one recent such action, when Stell was asked what a

former employee of Allied Capital could say that was *not* confidential, she responded: “just what a good company it is.”

131. Hodge and other senior management of Allied Corporation were aware that Allied Capital routinely concealed prior sanctions and convictions that could have alerted HUD to the risk that the company posed to its insurance fund, yet Allied Corporation took no actions to halt the fraudulent practices of its loan correspondent.

132. Under the direction of Hodge, Allied Capital, with the full knowledge of Allied Corporation, has therefore engaged in a pattern of deception for at least a decade, attempting to evade regulatory scrutiny, and, when confronted, lying to protect its profitable position in the FHA mortgage market.

5. Allied Corporation Submits False Annual Certifications to HUD

133. To maintain its HUD-approved status, Allied Corporation was required to certify each year that it complied with all HUD/FHA regulations necessary to maintain its HUD/FHA approval. Allied Corporation submitted such annual certifications for the years ending December 31, 2003, December 31, 2006, December 31, 2007, December 31, 2008, and December 31, 2010. These annual certifications were false, as between 2003 and 2010 Allied Corporation was not operating in compliance with the requisite HUD regulations, including HUD’s quality control requirements and HUD regulations requiring supervision of loan correspondents.

134. Hodge was aware that Allied Corporation was not in compliance with these HUD regulations at the time Allied Corporation submitted its annual certifications. Hodge was also aware of HUD’s annual certification requirement by at least September 2008 (if not earlier). Hodge nonetheless permitted his employees to submit false annual certifications on behalf of

Allied Corporation. Stell executed the false 2003 annual certification on behalf of Allied Corporation, even though she was aware that Allied Corporation was not in compliance with HUD regulations at the time she made this certification.

D. Allied Corporation's Underwriting Violations

135. Allied Corporation abused its Direct Endorsement Lender status through its false statements regarding individual loans. In particular, Allied Corporation regularly violated HUD rules and requirements, prudent underwriting practices, and its duties to HUD, by failing to conduct due diligence on mortgages that it underwrote and approved for FHA insurance. Specifically, Allied Corporation, through its underwriters, falsely certified, on a loan-by-loan basis, that it had complied with HUD rules and requirements, and that the mortgages it endorsed were eligible for FHA insurance under HUD rules.

136. Allied Corporation engaged in a pattern of failing to conduct due diligence in accordance with HUD rules and requirements, and with sound and prudent underwriting principles, contrary to the certifications appearing on each mortgage that it endorsed.

137. Violations of HUD's underwriting and due-diligence requirements included, but are not limited to, a failure to ensure that the borrower of property was eligible for an FHA-insured loan, a failure to ensure that the borrower is creditworthy, the approval of loans with unacceptable debt-to-income ratios, a failure to verify or document a borrower's employment or income, a failure to resolve inconsistencies or irregularities prior to approving a loan, submission of information into the automated underwriting system ("AUS") information that lacked integrity, a failure to manually downgrade a loan in AUS to "Refer" when required to do so, and refinancing loans where the borrower was not current on the loan being refinanced. This pattern of false

certifications is illustrated by the examples below. These examples were not isolated events, but rather provide a representative sample of Allied Corporation's fraudulent practices.

Cherry Street Property

138. FHA case number 412-5602712 involves a mortgage for a property on Cherry Street in Perrysburg, Ohio (the "Cherry Street Property"). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about July 26, 2007.

139. Allied Corporation approved a purchase money loan despite the fact that it had failed to obtain borrower's explanations for the following items on the borrowers' joint credit report: the borrower's Chapter 7 bankruptcy that was discharged five years, eight months prior to closing, the 20 collection accounts, the fourteen 30-day late payments, the ten 60-day late payments, and the sixty-one 90-day late payments. *See* HUD Handbook 4155.1, REV-5, paragraph 2-3. Allied Corporation also failed to obtain explanations for the borrowers' two bank overdraft fees that were incurred two months before closing. *Id.*

140. Allied Corporation's false certification on the application for the Cherry Street Property was material and bore upon the likelihood that the borrower would make mortgage payments.

141. The loan was reported in default in February 2008.

142. As a result, HUD paid a loss mitigation on or about May 16, 2008, of \$200, and an additional FHA insurance claim on or about June 27, 2013, of \$132,363.65. The claims paid total \$132,563.65.

White Oak Property

143. FHA case number 495-8133639 involves a mortgage for a property on White Oak Loop in Round Rock, Texas (the “White Oak Property”). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about December 19, 2008.

144. For this loan, Allied Corporation failed to ensure the integrity of the documents supporting the decision of the AUS to approve the loan. The HUD-1 (which is the closing statement that reflects all payments in and out of escrow) reflected that a second mortgage was paid off to an individual servicing mortgagee. The HUD-1 also reflected the existing first mortgage serviced by Wells Fargo was paid off at closing. However, the sole payoff statement³ in the file, which was supported by the servicing mortgagee’s cash receipts records for the mortgage, showed that the holding and servicing mortgagee for the only existing mortgage was Market Properties, L.P. The payoff statement did not include either of the other loans. Allied Corporation failed to resolve this inconsistency, and thereby failed to ensure that the loan closed in such a way as to preserve the first-lien position of the new FHA loan. *See* HUD Handbook 4155.1, REV-5, chapter 3; HUD Handbook 4000.4, REV-1, paragraph 2-4(c)(5); Mortgagee Letter 92-5.

145. Allied Corporation also included the borrowers’ claimed monthly self-employment income of \$1,874.25, which was derived from “web-based sales,” despite the fact that Allied Corporation failed to adequately document the income. Allied Corporation failed to obtain the required year-to-date profit-and-loss statement and balance sheet pertaining to this income stream.

³ A payoff statement shows the amount due to a lender by a date certain in order to pay off a mortgage lien. This document is provided by the servicing mortgagee to the underwriter.

See HUD Handbook 4155.1, REV-5, paragraph 2-9(B)(3); and FHA TOTAL Mortgage Scorecard User Guide (December 2004 Edition).

146. Allied Corporation's false certification on the application for the White Oak Property was material and bore upon the likelihood that the borrower would make mortgage payments.

147. The loan was reported in default in June 2009.

148. As a result, HUD paid an FHA insurance claim on or about September 24, 2010, of \$175,840.37, a second claim on or about December 12, 2011, of \$7,197.24, and a third claim on or about May 24, 2013, of \$512.28. The claims paid total \$183,549.89.

Oso Parkway Property

149. FHA case number 495-7958467 involves a mortgage for a property on Oso Parkway in Corpus Christi, Texas (the "Oso Parkway Property"). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about July 28, 2008.

150. Allied Corporation improperly included in the AUS ratio calculations the borrower's \$472 per month in former child support income that, per a court document in the file, had been nullified by the local family court when the borrower reconciled with her husband, who was the father of her children. The borrower's income was therefore overstated by \$472 per month, and the actual total debt-to-income ratio was 56.6%, 13.6 percentage points above the maximum allowed by Mortgage Letter 2005-16.

151. Further, Allied Corporation failed to resolve the discrepancy between the borrower's statement on the uniform residential loan application ("URLA") that the borrower

earned \$752.00 per month in child support and the court document stating that the \$472-per-month child support order against her husband was nullified when the couple reconciled. *See* HUD Handbook 4155.1, REV-5, chapter 3; HUD Handbook 4000.4, REV-1, paragraph 2-4(C)(5); Mortgagee Letter 92-5.

152. Allied Corporation's false certification on the application for the Oso Parkway Property was material and bore upon the likelihood that the borrower would make mortgage payments.

153. The loan was reported in default in December 2008.

154. As a result, HUD paid an FHA insurance claim on or about December 14, 2009, of \$171,117.16, and a second claim on March 21, 2010, of \$9,948.72. The claims paid total \$181,065.88.

Campbell Avenue Property

155. FHA case number 137-6320410 involves a mortgage for a property on Campbell Avenue in Chicago, Illinois (the 'Campbell Avenue Property'). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about June 9, 2011.

156. Allied Corporation approved the loan even though the borrower's asset information contained irregularities and lacked proper documentation. The bank statements in the file showed that, subsequent to the borrower's receipt of gift funds from his mother (which were necessary to fund the settlement), the borrower made several unexplained cash withdrawals from his bank account that exceeded the total of the gifts. The borrower also opened a second bank account 45 days prior to settlement with an undeterminable opening deposit. The first transaction that was

listed on the new account's history report in the file was a \$280 withdrawal 35 days prior to settlement that resulted in an account balance of \$4,370.92. Subsequently, from the new account, a certified check for \$3,200 was issued to the borrower 23 days prior to settlement, and the borrower wrote a check to himself for \$1,200 twenty-two days prior to settlement. There is no documentation in the file showing the source of the \$4,370.92 balance 35 days prior to settlement (which consisted of funds deposited into the new checking account during the period between 45 and 35 days prior to settlement). Nor is there documentation of the source of the \$3,991.05 that the borrower tendered at the settlement table. *See* HUD Handbook 4155.1, chapter 5, Section B; FHA TOTAL Mortgage Scorecard User Guide (December 2004 Edition); HUD Handbook 4155.2, paragraph 2.A.4.b; Mortgagee Letter 92-5.

157. Allied Corporation's false certification on the application for the Campbell Avenue Property was material and bore upon the likelihood that the borrower would make mortgage payments.

158. The loan was reported in default in November 2011.

159. As a result, HUD paid loss mitigation on or about September 21, 2013, of \$10,810.57.

118th Street Property

160. FHA case number 412-5669606 involves a mortgage for a property on 118th Street in Toledo, Ohio (the "118th Street Property"). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about January 24, 2008.

161. Allied Corporation approved this refinance transaction without obtaining any explanation for derogatory credit, improperly including delinquent tax debt and uncollected mortgage late charges in the new loan amount, failing to resolve conflicting or inconsistent mortgage payment history information, failing to fully analyze borrowers' overall credit picture, and failing to document acceptable compensating factors justifying loan approval with a total debt-to-income ratio far in excess of the maximum allowable.

162. HUD requires that lenders obtain written explanations of all derogatory credit report entries within the previous two years. *See* HUD Handbook 4155.1, REV-5, paragraph 2-3. Yet Allied Corporation failed to obtain any explanation from the borrower concerning delinquent property tax obligations.

163. Relatedly, Allied Corporation failed to analyze the overall credit-worthiness of the borrowers, who had unpaid delinquent taxes listed on the HUD-1, as well as a long pattern of untimely mortgage payments reflected by the large amount of uncollected late charges. *See* HUD Handbook 4155.1, REV-5, paragraph 2-3. And although Allied Corporation cited no derogatory credit in the past 18 months as a strong compensating factor, Allied Corporation failed to include the analysis required to be provided by HUD Handbook 4155.1, REV-5, paragraph 2-3.

164. Allied Corporation also ignored Mortgagee Letter 05-16 and HUD Handbook 4155.1, REV-5, paragraph 2-13, and approved the loan despite having failed to document acceptable compensating factors justifying approval with a total debt-to-income ratio of 52.9%, which is 9.9% above the allowable maximum of 43%.

165. Allied Corporation's false certification on the application for the 118th Street Property was material and bore upon the likelihood that the borrower would make mortgage payments.

166. The loan was reported in default in November 2008.

167. As a result, HUD paid an FHA insurance claim on or about June 16, 2011, of \$83,080.01.

Makakoa Loop Property

168. FHA case number 141-1451949 involves a mortgage for a property on Makakoa Loop in Waipahu, Hawaii (the "Makakoa Loop Property"). Allied Corporation underwrote the mortgage, reviewed and approved it for FHA insurance, and falsely certified that the loan complied with HUD requirements. The loan closed on or about July 31, 2008.

169. Allied Corporation failed to analyze the borrower's creditworthiness pursuant to HUD requirements. Specifically, it failed to obtain the borrower's explanation for a credit card payment to Capital One that was 30-days late only four months prior to the closing. *See* HUD Handbook 4155.1, REV-5, paragraph 2-3.

170. Allied Corporation also improperly approved a refinancing loan even though the borrower was not current on the existing mortgage. Under HUD regulations, borrowers must either make the outstanding payments or bring the mortgage payments due to the closing. *See* HUD Handbook 4155.1, REV-5, paragraph 1-10, and Mortgagee Letter 05-43. In this loan transaction, Allied Corporation approved the refinancing loan even though the existing first mortgage was 30 days delinquent on the date of closing and the borrower did not bring the balance due to the closing.

171. Allied Corporation's false certification on the application for the Makakoa Loop Property was material and bore upon the likelihood that the borrower would make mortgage payments.

172. The loan was reported in default in July 2009.

173. As a result, HUD paid an FHA insurance claim on or about July 4, 2011, of \$139,416.37.

* * * * *

174. The examples above are merely illustrative of an ongoing pattern of flawed underwriting by Allied Corporation. For instance, Allied Corporation has originated or sponsored approximately 900 loans since September 1, 2011. Of those, more than 50 are already in default, which is 5 times the national average. Moreover, one-third of those 900 loans have been delinquent at some point, and thus pose an increased risk of default and loss.

175. Moreover, since January 1, 2001, Allied Corporation has originated or sponsored approximately 18,000 loans. Of these, approximately 1,850 have gone into claim status, representing approximately 10% of the loans originated or sponsored by Allied Corporation (a percentage which is significantly higher than the national average). Attached hereto as Exhibit A is a list of loans sponsored or originated by Allied Corporation since January 1, 2001, which are in claim status. The Government estimates that HUD has paid in excess of \$230 million in FHA insurance claims for those 1,851 loans listed in Exhibit A. This figure does not include the numerous loans that are in default but where no claim has yet been made, or those which are likely to default and result in a claim.

FIRST CLAIM

**Violations of the False Claims Act by Allied Capital
(31 U.S.C. § 3729(a)(1)(B) (as amended), 31 U.S.C. § 3729(a)(2) (2006))
Use of False Statements—False Loan Certifications to HUD**

176. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

177. By virtue of its use of borrowed HUD IDs to originate loans from its shadow branches, as described above, and in violation of 31 U.S.C. § 3729(a)(1)(B) (as amended) and 31 U.S.C. § 3729(a)(2) (2006), for each of the loans originated from its shadow branches and submitted to HUD for FHA mortgage insurance, Allied Capital knowingly made, used, or caused to be made or used, false records or statements material to a false or fraudulent claim for payment or approval by the United States.

178. The Government paid insurance claims, and incurred losses, relating to FHA-insured mortgages based on the misrepresentation that the mortgage was originated in accordance with HUD requirements, including that it was originated by a HUD-approved branch.

179. Pursuant to the False Claims Act, 31 U.S.C. § 3729(a)(1)(B) (as amended) and 31 U.S.C. § 3729(a)(2) (2006), Allied Capital is liable to the United States under the treble damage and civil penalty provisions for a civil penalty of not less than \$5,500 and not more than \$11,000 for each of the false or fraudulent claims described herein, plus three (3) times the amount of damages which the United States has sustained because of Allied Capital's actions.

SECOND CLAIM

**Violations of the False Claims Act by Allied Corporation
(31 U.S.C. § 3729(a)(2) (2006))
Use of False Statements—False Loan Certifications to HUD**

180. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

181. By virtue of its use of borrowed HUD IDs to originate loans from shadow branches, as described above, and in violation of 31 U.S.C. § 3729(a)(2) (2006), for each of the loans originated from its shadow branches and submitted to HUD for FHA mortgage insurance, Allied Corporation knowingly made, used, or caused to be made or used, false records or statements material to a false or fraudulent claim for payment or approval by the United States.

182. The Government paid insurance claims, and incurred losses, relating to FHA-insured mortgages based on the misrepresentation that the mortgage was originated in accordance with HUD requirements, including that it was originated by a HUD-approved branch.

183. Pursuant to the False Claims Act, 31 U.S.C. § 3729(a)(2) (2006), Allied Corporation is liable to the United States under the treble damage and civil penalty provisions for a civil penalty of not less than \$5,500 and not more than \$11,000 for each of the false or fraudulent claims described herein, plus three (3) times the amount of damages which the United States has sustained because of Allied Corporation's actions.

THIRD CLAIM

**Violations of the False Claims Act by James Hodge
(31 U.S.C. § 3729(a)(1)(B) (as amended), 31 U.S.C. § 3729(a)(2) (2006))
Use of False Statements—False Loan Certifications to HUD**

184. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

185. By directing the use of borrowed HUD IDs to originate loans from shadow branches, as described above, and in violation of 31 U.S.C. § 3729(a)(1)(B) (as amended) and 31 U.S.C. § 3729(a)(2) (2006), for each of the loans originated from Allied Capital's and Allied Corporation's shadow branches and submitted to HUD for FHA mortgage insurance, Hodge knowingly made, used, or caused to be made or used, false records or statements material to a false or fraudulent claim for payment or approval by the United States.

186. The Government paid insurance claims, and incurred losses, relating to FHA-insured mortgages based on the misrepresentation that the mortgage was originated in accordance with HUD requirements, including that it was originated by a HUD-approved branch.

187. Pursuant to the False Claims Act, 31 U.S.C. § 3729(a)(1)(B) (as amended) and 31 U.S.C. § 3729(a)(2) (2006), Hodge is liable to the United States under the treble damage and civil penalty provisions for a civil penalty of not less than \$5,500 and not more than \$11,000 for each of the false or fraudulent claims described herein, plus three (3) times the amount of damages which the United States has sustained because of Hodge's actions.

FOURTH CLAIM

**Indemnification Claim Against Allied Capital
False Loan Certifications to HUD**

188. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

189. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD mortgage insurance, for each of the loans originated from its shadow branches that is currently in default, but for which no insurance claim has been submitted to HUD, Allied Capital knowingly made, used, or caused to be made or used, false and fraudulent records, statements, or certifications and submitted such false and fraudulent records, statements, and certifications to HUD.

190. As a result of the false or fraudulent records, statements, or certifications submitted to HUD on each of the loans originated out of a shadow branch, the Government will pay future insurance claims, and incur future losses, relating to FHA-insured mortgages originated by Allied Capital.

191. Accordingly, the Government is entitled to indemnification of the losses described herein from Allied Capital.

FIFTH CLAIM

**Indemnification Claim Against Allied Corporation
False Loan Certifications to HUD**

192. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

193. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD mortgage insurance, for each of the loans originated from its shadow branches that is currently in default, but for which no insurance claim has been submitted to HUD, Allied Corporation knowingly made, used, or caused to be made or used, false and fraudulent records, statements, or certifications and submitted such false and fraudulent records, statements, and certifications to HUD.

194. As a result of the false or fraudulent records, statements, or certifications submitted to HUD on each of the loans originated out of a shadow branch, the Government will pay future insurance claims, and incur future losses, relating to FHA-insured mortgages originated by Allied Corporation.

195. Accordingly, the Government is entitled to indemnification of the losses described herein from Allied Corporation.

SIXTH CLAIM

Indemnification Claim Against Hodge False Loan Certifications to HUD

196. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

197. By directing the use of borrowed HUD IDs to originate loans from shadow branches, and for the purpose of fraudulently obtaining HUD mortgage insurance, for each of the loans originated from Allied Capital's and Allied Corporation's shadow branches that is currently in default, but for which no insurance claim has been submitted to HUD, Hodge knowingly caused

to be made or used, false records or statements material to a false or fraudulent claim for payment or approval by the United States.

198. As a result of the false or fraudulent records, statements, or certifications submitted to HUD on each of the loans originated out of a shadow branch, the Government will pay future insurance claims, and incur future losses, relating to FHA-insured mortgages originated by Allied Capital and Allied Corporation.

199. Accordingly, the Government is entitled to indemnification of the losses described herein from Hodge.

SEVENTH CLAIM

**Violations of FIRREA by Allied Capital
(12 U.S.C. § 1833a)
False Loan Certifications to HUD**

200. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

201. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD mortgage insurance in violation of 12 U.S.C. § 1833a, for each of the loans originated from its shadow branches that is currently in default, but for which no insurance claim has been submitted to HUD, Allied Capital knowingly made, used, or caused to be made or used, false and fraudulent records, statements, or certifications and submitted such false and fraudulent records, statements, and certifications to HUD/FHA in violation of 18 U.S.C. § § 1006 and 1014 (as amended).

202. Defendant Allied Capital (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into providing mortgage insurance (18 U.S.C. § 1006); and (b)

knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

203. Accordingly, for each of the loans originated out of its shadow branches that is in default but on which no claim has been made, Allied Capital is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

EIGHTH CLAIM

Violations of FIRREA by Allied Corporation (12 U.S.C. § 1833a) False Loan Certifications to HUD

204. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

205. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD mortgage insurance in violation of 12 U.S.C. § 1833a, for each of the loans originated from its shadow branches that is currently in default, but for which no insurance claim has been submitted to HUD, Allied Corporation knowingly made, used, or caused to be made or used, false and fraudulent records, statements, or certifications and submitted such false and fraudulent records, statements, and certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014 (as amended).

206. Defendant Allied Corporation (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into providing mortgage insurance (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

207. Accordingly, for each of the loans originated out of its shadow branches that is in default but on which no claim has been made, Allied Corporation is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

NINTH CLAIM

**Violations of FIRREA by Hodge
(12 U.S.C. § 1833a)
False Loan Certifications to HUD**

208. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

209. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD mortgage insurance in violation of 12 U.S.C. § 1833a, for each of the loans originated from an Allied Capital or Allied Corporation shadow branch that is currently in default, but for which no insurance claim has been submitted to HUD, Hodge knowingly made, used, or caused to be made or used, false and fraudulent records, statements, or certifications and submitted such false and fraudulent records, statements, and certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014 (as amended).

210. Defendant Hodge, as an officer and agent of a mortgage corporation, (a) caused statements to be made to HUD/FHA with the intent to defraud or deceive HUD/FHA into providing mortgage insurance (18 U.S.C. § 1006); and (b) knowingly caused false statements to be made for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

211. Accordingly, for each of the loans originated out of an Allied Capital or Allied Corporation shadow branch that is in default but on which no claim has been made, Hodge is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

TENTH CLAIM

**Violations of FIRREA by Allied Capital
(12 U.S.C. § 1833a)
False Branch Certifications to HUD**

212. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

213. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD approval for its branches, Allied Capital knowingly made, used, or caused to be made or used, false certifications and submitted such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

214. Defendant Allied Capital (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into approving branches for the origination of FHA loans (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

215. Accordingly, for each of the false branch certifications it submitted to HUD, Allied Capital is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

ELEVENTH CLAIM

**Violations of FIRREA by Allied Corporation
(12 U.S.C. § 1833a)
False Branch Certifications to HUD**

216. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

217. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD approval for its branches, Allied Corporation knowingly made, used, or caused to be made or

used, false certifications and submitted such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

218. Defendant Allied Corporation (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into approving branches for the origination of FHA loans (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

219. Accordingly, for each of the false branch certifications it submitted to HUD, Allied Corporation is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

TWELTH CLAIM

Violations of FIRREA by Stell (12 U.S.C. § 1833a) False Branch Certifications to HUD

220. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

221. By virtue of the acts described above, and for the purpose of fraudulently obtaining HUD approval for Allied Capital's and Allied Corporation's branches, Stell knowingly made, used, or caused to be made or used, false certifications, and submitted or caused to be submitted such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

222. Defendant Stell, as an officer and agent of a mortgage corporation, (a) made and caused to be made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into approving branches for the origination of FHA loans (18 U.S.C. § 1006); and (b) knowingly made

and caused to be made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

223. Accordingly, for each of the false branch certifications Allied Capital or Allied Corporation submitted to HUD, Stell is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

THIRTEENTH CLAIM

Violations of FIRREA by Allied Capital (12 U.S.C. § 1833a) False Annual Certifications to HUD

224. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

225. By virtue of the acts described above, and for the purpose of fraudulently maintaining HUD approval in the loan correspondent program, Allied Capital knowingly made, used, or caused to be made or used, false annual certifications stating that Allied Capital had complied with all HUD/FHA requirements, when in fact it had not. Further, Allied Capital submitted false annual certifications stating that none of Allied Capital's employees had a criminal conviction, and that Allied Capital had not been subject to sanctions in any state in which it operated. Allied Capital submitted such false certifications to HUD in violation of 18 U.S.C. § 1006.

226. Defendant Allied Capital made statements to HUD/FHA with the intent to defraud or deceive HUD into maintaining Allied Capital's approval (18 U.S.C. § 1006).

227. The false annual certifications submitted on behalf of Allied Capital for 2004 and 2006 through 2008 deceived HUD into maintaining Allied Capital as an approved HUD loan

correspondent and resulted in HUD paying insurance claims in excess of \$170 million on loans originated in those four years.

228. Accordingly, for the 2004, 2006, 2007 and 2008 false annual certifications submitted to HUD on behalf of Allied Capital, Allied Capital is liable for the losses to HUD as authorized under 12 U.S.C. § 1833a.

FOURTEENTH CLAIM

Violations of FIRREA by Allied Corporation (12 U.S.C. § 1833a) False Annual Certifications to HUD

229. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

230. By virtue of the acts described above, and for the purpose of fraudulently maintaining HUD approval as an FHA mortgagee and Direct Endorsement Lender, Allied Corporation knowingly made, used, or caused to be made or used, false annual certifications stating that Allied Corporation had complied with all HUD/FHA requirements, when in fact it had not. Allied Corporation submitted such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

231. Defendant Allied Corporation (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into maintaining Allied Corporation's approval (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

232. The false annual certifications submitted on behalf of Allied Corporation between 2003 through 2010 deceived HUD into maintaining Allied Corporation as a HUD- approved

mortgagee and Direct Endorsement Lender, and resulted in HUD paying insurance claims in excess of \$100 million on loans originated or sponsored in those years.

233. Accordingly, for the false annual certifications submitted to HUD on behalf of Allied Corporation for the years 2003 through 2010, Allied Corporation is liable for the losses to HUD as authorized under 12 U.S.C. § 1833a.

FIFTEENTH CLAIM

Violations of FIRREA by Hodge (12 U.S.C. § 1833a) False Annual Certifications to HUD

234. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

235. By virtue of the acts described above, and for the purpose of fraudulently maintaining HUD approval of Allied Capital as an FHA loan correspondent, and Allied Corporation as an FHA mortgagee and Direct Endorsement Lender, Hodge knowingly made, used, or caused to be made or used, false annual certifications on behalf of Allied Capital and Allied Corporation. Hodge submitted, or caused to be submitted, such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

236. Defendant Hodge, as an officer and agent of a mortgage corporation, (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into maintaining its approval (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

237. The false annual certifications submitted on behalf of Allied Capital for 2004 and 2006 through 2008 deceived HUD into maintaining Allied Capital as an approved HUD loan

correspondent, and resulted in HUD paying insurance claims excess of \$170 million on loans originated in those four years. The false annual certifications submitted on behalf of Allied Corporation between 2003 through 2010 deceived HUD into maintaining Allied Corporation as a HUD-approved mortgagee and Direct Endorsement Lender, and resulted in HUD paying insurance claims in excess of \$100 million on loans originated or sponsored in those years.

238. Accordingly, for the false annual certifications submitted to HUD on behalf of Allied Corporation and Allied Capital, Hodge is liable for the losses to HUD as authorized under 12 U.S.C. § 1833a.

SIXTEENTH CLAIM

Violations of FIRREA by Stell (12 U.S.C. § 1833a) False Annual Certifications to HUD

239. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

240. By virtue of the acts described above, and for the purpose of fraudulently maintaining HUD approval of Allied Capital as an FHA loan correspondent, and Allied Corporation as an FHA mortgagee and Direct Endorsement Lender, Stell knowingly made, used, or caused to be made or used, false annual certifications on behalf of Allied Capital and Allied Corporation. Stell submitted such false certifications to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

241. Defendant Stell, as an officer and agent of a mortgage corporation, (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA into maintaining its

approval (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

242. The false annual certifications submitted on behalf of Allied Capital for 2004 and 2006 through 2007 deceived HUD into maintaining Allied Capital as an approved HUD loan correspondent, resulting in HUD paying insurance claims in excess of \$170 million on loans originated in those three years. The false annual certification submitted on behalf of Allied Corporation for 2003 deceived HUD into maintaining Allied Corporation as a HUD-approved mortgagee and Direct Endorsement Lender, and resulted in HUD paying insurance claims on loans originated or sponsored in that year.

243. Accordingly, for the false annual certifications described herein, Stell is liable for the losses to HUD as authorized under 12 U.S.C. § 1833a.

SEVENTEENTH CLAIM

Violations of FIRREA by Allied Capital (12 U.S.C. § 1833a) False Statements to HUD

244. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

245. By virtue of the acts described above, and for the purpose of fraudulently concealing from HUD Allied Capital's lack of quality control, Allied Capital knowingly made, used, or caused to be made false statements to HUD/FHA and made, used, or caused to be made false and fraudulent records and submitted such false and fraudulent records to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

246. Defendant Allied Capital (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA concerning Allied Capital's maintenance of a quality control plan (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

247. Accordingly, for each of the false statements and records it submitted or caused to be submitted to HUD, Allied Capital is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

EIGHTEENTH CLAIM

**Violations of FIRREA by Allied Corporation
(12 U.S.C. § 1833a)
False Statements to HUD**

248. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

249. By virtue of the acts described above, and for the purpose of fraudulently concealing from HUD Allied Corporation's lack of quality control, Allied Corporation knowingly made, used, or caused to be made false statements to HUD/FHA and made, used, or caused to be made false and fraudulent records and submitted such false and fraudulent records to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

250. Defendant Allied Corporation (a) made statements to HUD/FHA with the intent to defraud or deceive HUD/FHA concerning Allied Corporation's maintenance of a quality control plan (18 U.S.C. § 1006); and (b) knowingly made false statements for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

251. Accordingly, for each of the false statements and records it submitted or caused to be submitted to HUD, Allied Corporation is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

NINETEENTH CLAIM

**Violations of FIRREA by Hodge
(12 U.S.C. § 1833a)
False Statements to HUD**

252. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

253. By virtue of the acts described above, and for the purpose of fraudulently concealing from HUD Allied Capital's and Allied Corporation's lack of quality control, Hodge knowingly made, used, or caused to be made false statements to HUD/FHA and made, used, or caused to be made false and fraudulent records and submitted such false and fraudulent records to HUD/FHA in violation of 18 U.S.C. §§ 1006 and 1014.

254. Defendant Hodge, as an officer and agent of a mortgage corporation, (a) caused statements to be made to HUD/FHA with the intent to defraud or deceive HUD concerning the Allied Companies' maintenance of a quality control plan (18 U.S.C. § 1006); and (b) knowingly caused false statements to be made for the purpose of influencing the FHA (18 U.S.C. § 1014, as amended).

255. Accordingly, for each of the false statements and records he submitted or caused to be submitted to HUD, Hodge is liable for civil penalties to the maximum amount authorized under 12 U.S.C. § 1833a.

TWENTIETH CLAIM

**Violations of the False Claims Act by Allied Corporation
(31 U.S.C. § 3729(a)(1) (2006), and as amended, 31 U.S.C. § 3729(a)(1)(A))
Causing False Claims (Reckless Underwriting)**

256. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

257. The Government seeks relief against Allied Corporation under Section 3729(a)(1) of the False Claims Act, 31 U.S.C. § 3729(a)(1) (2006), and, as amended, Section 3729(a)(1)(A) of the False Claims Act, 31 U.S.C. § 3729(a)(1)(A).

258. As set forth above, Allied Corporation knowingly, or acting with deliberate ignorance and/or with reckless disregard for the truth, presented and/or caused to be presented, to an officer or employee of the Government, false and fraudulent claims for payment or approval in connection with its endorsement of FHA-insured mortgages, by:

- a. Submitting false annual certifications and making false representations to HUD with respect to Allied Corporation's qualifications for Direct Endorsement Lender status; and/or
- b. Submitting false loan-level certifications to HUD in endorsing mortgages for FHA insurance

259. The Government paid insurance claims, and incurred losses, relating to FHA-insured mortgages wrongfully endorsed by Allied Corporation.

260. By reason of the false claims of Allied Corporation, the Government has been damaged in a substantial amount to be determined at trial, and is entitled to a civil penalty as required by law for each violation.

TWENTY-FIRST CLAIM

**Violations of the False Claims Act by Allied Corporation
(31 U.S.C. § 3729(a)(2), and, as amended, 31 U.S.C. § 3729(a)(1)(B))
Use of False Statements (Reckless Underwriting)**

261. The Government incorporates by reference each of the preceding paragraphs as if fully set forth in this paragraph.

262. The Government seeks relief against Allied Corporation under Section 3729(a)(2) of the False Claims Act, 31 U.S.C. § 3729(a)(2) (2006), and, as amended, Section 3729(a)(1)(B) of the False Claims Act, 31 U.S.C. § 3729(a)(1)(B).

263. As set forth above, Allied Corporation knowingly, or acting in deliberate ignorance and/or with reckless disregard of the truth, made, used, or caused to be made or used, false records and/or statements material to false or fraudulent claims in connection with Allied Corporation's maintenance of its Direct Endorsement Lender status and/or its endorsement of FHA-insured mortgages.

264. The Government paid insurance claims, and incurred losses, relating to FHA-insured mortgages wrongfully endorsed by Allied Corporation.

265. By reason of the false claims of Allied Corporation, the Government has been damaged in a substantial amount to be determined at trial, and is entitled to a civil penalty as required by law for each violation.

WHEREFORE, the Government respectfully requests that judgment be entered in its favor and against Allied Capital, Allied Corporation, Hodge, and Stell as follows:

a. On Counts One through Three (FCA), judgment for the Government against Allied Capital, Allied Corporation, and Hodge, treble the Government's damages from defaulted loans from shadow branches that have resulted in claims paid by the Government, and civil penalties for the maximum amount allowed by law;

b. On Count Four through Six (Indemnification), judgment for the Government against Allied Capital, Allied Corporation, and Hodge, and indemnification for the Government's losses on loans from shadow branches that are in default but on which no claim has been paid;

c. On Count Seven through Nine (FIRREA), judgment for the Government against Allied Capital, Allied Corporation, and Hodge, civil penalties up to the maximum amount of \$1,000,000, or the amount of gain to the defendants, or, if greater, the amount of the loss to HUD stemming from such conduct;

d. On Counts Ten through Twelve (FIRREA), judgment for the Government against Allied Capital, Allied Corporation, and Stell, civil penalties under each claim up to the maximum amount of \$1,000,000, or the amount of gain to the defendants, or, if greater, the amount of the loss to HUD stemming from such conduct;

e. On Counts Thirteen through Sixteen (FIRREA), judgment for the Government against Allied Capital, Allied Corporation, Hodge and Stell, civil penalties under each claim up to the maximum amount of \$1,000,000, or the amount of gain to the defendants, or, if greater, the amount of the loss to HUD stemming from such conduct;

f. On Counts Seventeen through Nineteen (FIRREA), judgment for the Government against Allied Capital, Allied Corporation, and Hodge, civil penalties up to the maximum amount

of \$1,000,000, or the amount of gain to the defendants, or, if greater, the amount of the loss to HUD stemming from such conduct;

g. On Count Twenty and Twenty-One (FCA), judgment for the Government against Allied Corporation, treble the Government's damages and civil penalties for the maximum amount allowed by law.

h. For an award of costs pursuant to 31 U.S.C. § 3729(a); and

i. For an award of any such further relief as is proper.

Dated: New York, New York
October 24, 2013

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