

## SETTLEMENT AGREEMENT

This Settlement Agreement ("Agreement") is entered into among the United States of America, acting through the United States Department of Justice and on behalf of the Department of Housing and Urban Development ("HUD") and the Department of Housing and Urban Development Office of Inspector General (collectively the "United States") and First Tennessee Bank National Association, a wholly-owned subsidiary of First Horizon Financial Corporation ("First Tennessee") (hereafter collectively referred to as "the Parties"), through their authorized representatives.

### RECITALS

A. Between January 2006 and December 2008, First Tennessee, through its wholly-owned subsidiary First Horizon Home Loans Corporation, was a Direct Endorsement Lender approved by the Federal Housing Administration ("FHA"). First Tennessee has its principal place of business in Memphis, Tennessee.

B. First Tennessee agrees that it engaged in the conduct set forth in Attachment A in connection with its origination, underwriting, and quality control of single-family residential mortgage loans, excluding origination or underwriting of Home Equity Conversion Mortgages under 12 U.S.C. § 1715z-20 or Streamlined Refinances under 12 U.S.C. § 1715n(a)(7), insured by the FHA on or after January 1, 2006 and that resulted in claims submitted to HUD on or before April 2, 2015 (hereafter referred to as the "Covered Conduct"). The United States contends that it has certain civil claims against First Tennessee based upon the Covered Conduct.

C. First Tennessee denies that the United States has any cognizable claims arising out of the Covered Conduct. This Settlement Agreement is neither an admission

of liability by First Tennessee nor a concession by the United States that its claims are not well founded

To avoid the delay, uncertainty, inconvenience, and expense of protracted litigation of the above claims, and in consideration of the mutual promises and obligations of this Agreement, the Parties agree and covenant as follows:

#### TERMS AND CONDITIONS

1. First Tennessee shall pay to the United States \$212,500,000 (the "Settlement Amount") by electronic funds transfer pursuant to written instructions to be provided on the Effective Date by the Civil Division of the Department of Justice. Payment of the Settlement Amount shall be no later than 7 days after the Effective Date of this Agreement.

2. Subject to the exceptions in Paragraph 3 (concerning excluded claims) below, and conditioned upon First Tennessee's full payment of the Settlement Amount, the United States releases First Tennessee, together with all of its current and former parent corporations, predecessor and successor corporations, divisions, affiliates, direct and indirect subsidiaries, and attorneys and assigns from any civil or administrative monetary claim the United States has for the Covered Conduct under the False Claims Act, 31 U.S.C. §§ 3729-3733; the Financial Institutions Reform, Recovery, and Enforcement Act; the Program Fraud Civil Remedies Act, 31 U.S.C. §§ 3801-3812 & 24 C.F.R. §§ 28.1-28.45; or common law theories of negligence, breach of fiduciary duty, misrepresentation, deceit, breach of contract, payment by mistake, unjust enrichment, and fraud; or that the Civil Division of the United States Department of Justice has actual and

present authority to assert and compromise pursuant to 28 C.F.R. §0.45(d) in connection with the Covered Conduct.

3. Notwithstanding the release given in paragraph 2 of this Agreement, or any other term of this Agreement, the following claims of the United States are specifically reserved and are not released:

- a. Any liability arising under Title 26, U.S. Code (Internal Revenue Code);
- b. Any criminal liability;
- c. Except as explicitly stated in this Agreement, any administrative liability, including the suspension and debarment rights of any federal agency;
- d. Any liability based upon obligations created by this Agreement; or
- e. Any liability of individuals.

4. First Tennessee waives and shall not assert any defenses First Tennessee may have to any criminal prosecution or administrative action relating to the Covered Conduct that may be based in whole or in part on a contention that, under the Double Jeopardy Clause in the Fifth Amendment of the Constitution, or under the Excessive Fines Clause in the Eighth Amendment of the Constitution, this Agreement bars a remedy sought in such criminal prosecution or administrative action. Nothing in this paragraph or any other provision of this Agreement constitutes an agreement by the United States concerning the characterization of the Settlement Amount for purposes of the Internal Revenue laws, Title 26 of the United States Code.

5. First Tennessee fully and finally releases the United States, its agencies, officers, agents, employees, and servants, from any claims (including attorney's fees, costs, and expenses of every kind and however denominated) that First Tennessee has asserted, could have asserted, or may assert in the future against the United States, its agencies, officers, agents, employees, and servants, related to the Covered Conduct and the United States' investigation and prosecution thereof.

6. a. Unallowable Costs Defined: All costs (as defined in the Federal Acquisition Regulation, 48 C.F.R. § 31.205-47) incurred by or on behalf of First Tennessee in connection with:

- (1) the matters covered by this Agreement;
- (2) the United States' audit(s) and civil investigation(s) of the matters covered by this Agreement;
- (3) First Tennessee's investigation, defense, and corrective actions undertaken in response to the United States' audit(s) and civil and any criminal investigation(s) in connection with the matters covered by this Agreement (including attorney's fees);
- (4) the negotiation and performance of this Agreement; and
- (5) the payment First Tennessee makes to the United States pursuant to this Agreement,

are unallowable costs for government contracting purposes (hereinafter referred to as "Unallowable Costs").

b. Future Treatment of Unallowable Costs: Unallowable Costs will be separately determined and accounted for by First Tennessee, and First Tennessee shall not charge such Unallowable Costs directly or indirectly to any contract with the United States.

c. Treatment of Unallowable Costs Previously Submitted for Payment: Within 90 days of the Effective Date of this Agreement, First Tennessee shall identify and repay by adjustment to future claims for payment or otherwise any Unallowable Costs included in payments previously sought by First Tennessee or any of its subsidiaries or affiliates from the United States. First Tennessee agrees that the United States, at a minimum, shall be entitled to recoup from First Tennessee any overpayment plus applicable interest and penalties as a result of the inclusion of such Unallowable Costs on previously-submitted requests for payment. The United States, including the Department of Justice and/or the affected agencies, reserves its rights to audit, examine, or re-examine First Tennessee's books and records and to disagree with any calculations submitted by First Tennessee or any of its subsidiaries or affiliates regarding any Unallowable Costs included in payments previously sought by First Tennessee, or the effect of any such Unallowable Costs on the amount of such payments.

7. First Tennessee agrees to cooperate fully and truthfully with the United States' investigation of individuals and entities not released in this Agreement. Upon reasonable notice, First Tennessee shall encourage, and agrees not to impair, the cooperation of its directors, officers, and employees, and shall use reasonable efforts to make available, and encourage, the cooperation of former directors, officers, and

employees for interviews and testimony, consistent with the rights and privileges of such individuals.

8. This Agreement is intended to be for the benefit of the Parties only.

9. Each party shall bear its own legal and other costs incurred in connection with this matter, including the preparation and performance of this Agreement.

10. Each party and signatory to this Agreement represents that it freely and voluntarily enters in to this Agreement without any degree of duress or compulsion.

11. This Agreement is governed by the laws of the United States. The exclusive jurisdiction and venue for any dispute relating to this Agreement is the United States District Court for the Northern District of Georgia. For purposes of construing this Agreement, this Agreement shall be deemed to have been drafted by all Parties to this Agreement and shall not, therefore, be construed against any Party for that reason in any subsequent dispute.

12. This Agreement constitutes the complete agreement between the Parties. This Agreement may not be amended except by written consent of the Parties.

13. The undersigned counsel represent and warrant that they are fully authorized to execute this Agreement on behalf of the persons and entities indicated below.

14. This Agreement may be executed in counterparts, each of which constitutes an original and all of which constitute one and the same Agreement.

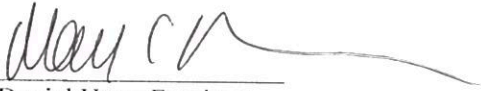
15. This Agreement is binding on First Tennessee and the First Tennessee Released Parties' successors, transferees, heirs, and assigns.

16. All parties consent to the United States' disclosure of this Agreement, and information about this Agreement, to the public.

17. This Agreement is effective on the date of signature of the last signatory to the Agreement ("Effective Date of this Agreement"). Facsimiles of signatures shall constitute acceptable, binding signatures for purposes of this Agreement.

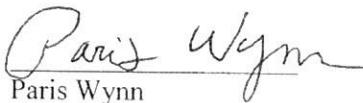
THE UNITED STATES OF AMERICA

DATED: 6/1/2015

BY: 

Daniel Hugo Fruchter  
Mary Chris Dobbie  
Trial Attorneys  
Commercial Litigation Branch  
Civil Division  
United States Department of Justice

DATED: June 1, 2015

BY: 

Paris Wynn  
Assistant United States Attorney  
United States Attorney's Office  
Northern District of Georgia



First Tennessee Bank National Association

DATED: June, 2015

BY: Charles T. Tuggle, Jr.  
Charles T. Tuggle, Jr  
Executive Vice President and General  
Counsel  
First Tennessee Bank National Association

DATED: 6/1/15

BY: John H. Culver III  
John H. Culver III  
K&L Gates LLP  
Counsel for First Tennessee Bank National  
Association

## ATTACHMENT A

1. Between January 2006 and December 2008, First Tennessee Bank National Association (“First Tennessee”), a wholly-owned subsidiary of First Horizon Financial Corporation, was a Direct Endorsement lender approved by the Federal Housing Administration (“FHA”) and U.S. Department of Housing and Urban Development (“HUD”). As a Direct Endorsement lender with Lender Insurance status, First Tennessee was authorized by HUD to originate, underwrite, and endorse mortgage loans on HUD’s behalf, including determining a borrower’s creditworthiness and whether a proposed loan satisfies applicable HUD requirements, and to collect allowed fees and charges from a borrower. As a Direct Endorsement lender with Lender Insurance status, First Tennessee was authorized to provide the service of endorsing mortgage loans for HUD insurance without any pre-endorsement review of the mortgage application by HUD.

2. HUD required Direct Endorsement lenders, such as First Tennessee, to follow applicable HUD regulations and underwriting requirements in originating and underwriting mortgage loans for FHA insurance, including those requirements set out in HUD’s Handbooks and Mortgage Letters.<sup>1</sup>

3. HUD required Direct Endorsement lenders, such as First Tennessee to submit certain proposed FHA originations through a HUD-approved Automated Underwriting System (“AUS”) in conjunction with a tool known as Technology Open to Approved Lenders (“TOTAL”). According to the FHA’s TOTAL Mortgage Scorecard

---

<sup>1</sup> The requirements referenced in paragraphs two through eleven of this document reflect standard HUD-FHA program requirements for Direct Endorsement lenders as provided in HUD’s Handbooks and Mortgage Letters.

User Guide, TOTAL evaluated the overall creditworthiness of the applicants based on a number of credit variables. After a proposed loan was submitted, TOTAL would either: (1) approve the mortgage subject to certain eligibility criteria or other conditions, including conditions that the lender validate the information that formed the basis for TOTAL's determination; or (2) refer the mortgage application for manual underwriting by the lender in accordance with HUD requirements. First Tennessee understood that TOTAL's determination was based on the integrity of the data supplied by the lender. HUD has promulgated requirements for calculating data used by TOTAL.

4. HUD required Direct Endorsement lenders such as First Tennessee to implement and maintain a quality control program in accordance with HUD Handbook requirements for FHA loans in order to maintain Direct Endorsement lender status. HUD required the FHA quality control function to be independent of FHA mortgage origination and underwriting functions. HUD required Direct Endorsement lenders such as First Tennessee to review a sample of loans based upon the number of FHA loans originated and/or underwritten per year. HUD Handbook 4060.1 REV-2, § 7-6.C. Direct Endorsement lenders, such as First Tennessee, were also required to review each FHA mortgage loan that became 60 days delinquent within the first six payments, which HUD defined as "early payment defaults" or EPDs. *Id.* HUD required Direct Endorsement lenders such as First Tennessee, in performing these quality control reviews, to review the mortgage loan file, re-verify certain information, review the soundness of underwriting judgments, document its review and any findings in a quality control report, and report the findings to senior management within one month.

5. HUD required Direct Endorsement lenders, such as First Tennessee, to self-report to HUD all findings related to FHA mortgage loans that constituted “material violations of FHA or mortgagee requirements and represent an unacceptable level of risk” and all findings of “fraud or other serious violations.” HUD Handbook 4060.1 REV-2, §§ 7-3.J & 7-4.D. Direct Endorsement lenders such as First Tennessee were also required to take “prompt action to deal appropriately with any material findings.” *Id.* § 7-3.I.

6. In order to obtain Direct Endorsement status, HUD required Direct Endorsement lenders such as First Tennessee to certify as follows:

I certify that, upon the submission of this application, and with its submission of each loan for insurance or request for insurance benefits, [First Tennessee] has and will comply with the requirements of the Secretary of Housing and Urban Development, which include, but are not limited to, the National Housing Act (12 U.S.C. § 1702 *et seq.*) and HUD’s regulations, FHA handbooks, mortgagee letters, and Title I letters and policies with regard to using and maintaining its FHA lender approval.

7. Additionally, HUD required a Direct Endorsement lender, such as First Tennessee, to submit an Annual Certification stating:

I know, or am in a position to know, whether the operations of [First Tennessee] conform to HUD-FHA regulations, handbooks, and policies. I certify that to the best of my knowledge, [First Tennessee] conforms to all HUD-FHA regulations necessary to maintain its HUD-FHA approval, and that [First Tennessee] is fully responsible for all actions of its employees including those of its HUD-FHA approved branch offices.

Alternatively, HUD required a Direct Endorsement lender, such as First Tennessee, to submit a statement to HUD that it was unable to so certify and to explain why it could not execute the certification.

8. With respect to each mortgage loan submitted or endorsed by First Tennessee for FHA insurance, either a First Tennessee mortgagee representative or a First Tennessee direct endorsement underwriter was required to certify that the mortgage “is eligible for HUD mortgage insurance under the Direct Endorsement program.” For each loan that was approved using AUS, a First Tennessee mortgagee representative was required to certify to “the integrity of the data supplied by [First Tennessee] used to determine the quality of the loan [and] that a Direct Endorsement Underwriter reviewed the appraisal.” For each FHA loan that First Tennessee approved using manual underwriting, a First Tennessee direct endorsement underwriter was required to certify that he or she “personally reviewed the appraisal report (if applicable), credit application, and all associated documents and ha[s] used due diligence in underwriting th[e] mortgage.”

9. For every mortgage loan approved by First Tennessee, whether through manual underwriting or the use of an AUS, a First Tennessee direct endorsement underwriter was required to certify that:

“I, the undersigned, as authorized representative of [First Tennessee] at this time of closing of this mortgage loan, certify that I have personally reviewed the mortgage loan documents, closing statements, application for insurance endorsement, and all accompanying documents. I hereby make all certifications required for this mortgage as set forth in HUD Handbook 4000.4.”

10. Additionally, for each mortgage loan approved by First Tennessee, a First Tennessee direct endorsement underwriter was required to certify, to the best of his or her knowledge, that the information in the loan application was true and correct, that the loan conditions were satisfied, and that the proposed loan met the applicable HUD requirements.

11. When a borrower defaults on an FHA-insured loan underwritten and endorsed by a Direct Endorsement lender, such as First Tennessee, the lender, or if the mortgage or servicing rights were transferred after closing, the mortgage holder or servicer, has the option of submitting a claim to HUD to compensate the lender for any loss sustained as a result of the default. As such, once a mortgage loan is endorsed for FHA insurance, HUD insures the risk of the borrower defaulting on that mortgage, which is realized if an insurance claim is submitted.

12. The Department of Justice has investigated First Tennessee with regard to its origination, underwriting, quality control, and endorsement practices, as well as its submission of certifications, related to certain FHA-insured single-family residential mortgage loans originated between January 1, 2006 and December 31, 2008, and for which claims for FHA insurance benefits were submitted by April 2, 2015 (the “Released Loans”). The following statements apply to the Released Loans only.

13. Between January 1, 2006 and December 31, 2008, First Tennessee certified for FHA mortgage insurance pursuant to the Direct Endorsement Program certain Released Loans that did not meet certain HUD requirements and therefore were not eligible for FHA mortgage insurance under the Direct Endorsement Program.

14. Between January 2006 and April 2007, First Tennessee retained an outside firm to conduct certain aspects of its quality control reviews on FHA mortgages. The outside vendor graded its findings either “ARN” (no finding), “AWE” (a deficiency was noted but the loan did not demonstrate unacceptable risk), or “UR” (a significant finding causing the loan to exhibit unacceptable risk). The outside vendor’s quality control findings between January 2006 and April 2007 rated 42 percent of First Tennessee’s

FHA mortgages as “UR”. The outside vendor’s monthly findings of First Tennessee’s “UR” FHA mortgages ranged from 27 percent to 62 percent.

15. In mid-2007, First Tennessee terminated its relationship with the outside vendor and retained another firm, based in India, to conduct quality control reviews. The India-based firm also documented high levels of significant findings in First Tennessee’s originations.

16. Beginning in late 2007, First Tennessee significantly increased its FHA originations. This increased volume of FHA originations resulted in a decline in the quality of First Tennessee’s underwriting beginning in late 2007. For example, a May 2008 email distributed to First Tennessee management set forth that the January 2008 quality control review had initially determined that 161 of the 202 mortgages reviewed that month contained significant findings. The email further explained that “the overall error rate will be 37.62%” even if “QC overturns 100% of the rebutted findings” based on additional information received from the First Tennessee underwriters responsible for the loans in question.

17. With respect to EPDs, First Tennessee’s significant findings percentage increased from 7.7% in March 2007 to 47% by February 2008. These and other findings were routinely distributed to First Tennessee management.

18. Some of First Tennessee’s FHA underwriters were unable to keep up with the increasing FHA volume or the expectations of First Tennessee management regarding the volume of FHA mortgages that the underwriters were expected to underwrite per day. For example, an April 2008 email from a First Tennessee Senior Vice President and Regional Underwriting Manager to First Tennessee’s National Underwriting Manager

explained that “FHA submissions have increased from [less than] 10% of volume to 40-50% of volume. Our employee underwriters are buried with FHA loans[.]”

19. First Tennessee’s FHA underwriters and underwriting managers explained that part of the problem was the increased quantity and poor quality of the FHA mortgage files submitted to underwriting. In particular, the volume and condition of the “wholesale” loans submitted by mortgage brokers to First Tennessee for underwriting were particularly problematic. For example, in April 2008 a First Tennessee Pacific region underwriting manager emailed her supervisor that “quite honestly the FHA loans coming through the region have been put together pretty poorly.” Another April 2008 email from a different First Tennessee Regional Underwriting Manager for the mid-Atlantic region explained to First Tennessee’s National Underwriting Manager that “[w]e have sponsored brokers who know nothing about FHA. Some of these brokers were subprime brokers.” However, suggestions from these underwriting managers to address the quality of the FHA mortgage files submitted to First Tennessee’s underwriting department by third party brokers were not implemented.

20. First Tennessee also failed to comply with its obligation to self-report materially deficient FHA mortgages to HUD. Between January 2006 and December 2008, First Tennessee became aware of hundreds of materially deficient FHA mortgages through its quality control process. However, First Tennessee failed to self-report any of these mortgages to HUD.

21. First Tennessee also failed to comply with its obligation to perform a quality control review on each FHA mortgage that resulted in an Early Payment Default. While First Tennessee’s quality control plan stated that each Early Payment Default



would be reviewed, First Tennessee failed to comply with this requirement in 2008 when First Tennessee encountered increasing and substantial Early Payment Defaults. As First Tennessee internally acknowledged in July 2008, its quality control department lacked the resources to properly review each EPD.

22. As a result of First Tennessee's conduct and omissions, HUD insured hundreds of loans approved by First Tennessee that were not eligible for FHA mortgage insurance under the Direct Endorsement Program, and that HUD would not otherwise have insured. HUD subsequently incurred substantial losses when it paid insurance claims on those Released Loans.

23. The statements herein apply only to certain mortgages which are the subject of the release in this Agreement. This document is not an admission as to any conduct related to any mortgage not released in this Agreement, nor is it an admission of any legal liability. First Tennessee reserves the right to contest the use or application of this document in any future litigation.