

## ATTACHMENT A

1. Since at least January 2006, Manufacturers and Traders Trust Company a/k/a M&T Bank, successor by merger to M&T Mortgage Corporation (“M&T”) has been 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, M&T is authorized by HUD to originate and underwrite mortgage loans on HUD’s behalf, including determining a borrower’s creditworthiness and whether the proposed loan met all applicable HUD requirements. M&T obtained Lender Insurance status in February 2006. As a Direct Endorsement lender with Lender Insurance status, M&T is authorized to endorse mortgage loans for HUD insurance without any pre-endorsement review of the mortgage application by HUD. Prior to obtaining Lender Insurance status, HUD performed a limited review of loans M&T submitted for FHA insurance pursuant to the requirements of 24 C.F.R. § 203.255(c).

2. HUD required Direct Endorsement lenders, such as M&T, 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 Mortgagee Letters.<sup>1</sup>

3. HUD required Direct Endorsement lenders, such as M&T, 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 User Guide, TOTAL evaluated the overall creditworthiness of the applicants based on a number of

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<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 Mortgagee Letters.

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. M&T 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 M&T, 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 M&T, to review a sample of loans based on 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 M&T, 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 M&T, in performing these quality control reviews, to review the mortgage loan file, re-verify certain information, review the soundness of underwriting judgments, document the 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 M&T, 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 M&T, 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 M&T, 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, [M&T] 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 M&T, to submit an Annual Certification stating:

I know, or am in a position to know, whether the operations of [M&T] conform to HUD-FHA regulations, handbooks, and policies. I certify that to the best of my knowledge, [M&T] conforms to all HUD-FHA regulations necessary to maintain its HUD-FHA approval, and that [M&T] 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 M&T, to submit a statement to HUD that it was unable to so certify and to explain why it could not execute the certification.

8. To qualify as a Direct Endorsement underwriter an underwriter must satisfy several requirements. The Direct Endorsement underwriter “must have a minimum of three years full-time recent experience (or equivalent experience) reviewing both credit applications and property appraisals.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.A.3; *see also* HUD Handbook 4155.2 ch. 2.A.4.a. The underwriter must

also be a “reliable and responsible professional skilled in mortgage evaluation” and “must be able to demonstrate his or her knowledge and experience regarding the principles of mortgage underwriting.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.A.1; *see also* HUD Handbook 4155.2 ch. 2.A.4.a.

9. HUD considers the Direct Endorsement underwriter to be “the focal point of the Direct Endorsement program.” HUD Handbook 4000.4, REV-1, CHG-2, ch. 2-4.C. The Direct Endorsement underwriter must assume the following responsibilities: (1) compliance with HUD instructions, the coordination of all phases of underwriting, and the quality of decisions made under the program; (2) the review of appraisal reports, compliance inspections and credit analyses performed by fee and staff personnel to ensure reasonable conclusions, sound reports and compliance with HUD requirements; (3) the decisions relating to the acceptability of the appraisal, the inspections, the buyer’s capacity to repay the mortgage, and the overall acceptability of the mortgage loan for HUD insurance; (4) the monitoring and evaluation of the performance of fee and staff personnel used for the Direct Endorsement program; and (5) awareness of the warning signs that may indicate irregularities, and an ability to detect fraud, as well as the responsibility that underwriting decisions are performed with due diligence in a prudent manner.

10. With respect to each mortgage loan submitted or endorsed by M&T for FHA insurance, either an M&T mortgagee representative or an M&T 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, an M&T mortgagee representative was required to certify to the “integrity of the data supplied by [M&T] used to determine the quality of the loan [and] that a Direct

Endorsement Underwriter reviewed the appraisal.” For each FHA loan that M&T approved using manual underwriting, an M&T 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 the[e] mortgage.”

11. For every mortgage loan approved by M&T, whether through AUS or manual underwriting, an M&T employee was required to certify that:

I, the undersigned, as authorized representative of M&T 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.

12. When a borrower defaults on an FHA-insured loan underwritten and endorsed by a Direct Endorsement lender, such as M&T, 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.

13. The Department of Justice has investigated M&T with regard to its origination, underwriting, property appraisal, quality control, and endorsement practices, as well as its submissions of certifications, related to FHA-insured single-family residential mortgage loans originated between January 1, 2006 and December 31, 2011, and for which claims for FHA insurance benefits were submitted by July 15, 2015 (the “Released Loans”). The following statements apply to the Released Loans only.

14. Between January 1, 2006 and December 31, 2011, M&T 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.

15. Between January 1, 2006 and December 31, 2011, M&T did not maintain a Quality Control (QC) program that fully complied with the QC requirements established by HUD.

- a. M&T's QC Department did not consistently review an adequate sample of FHA insured loans. Specifically, HUD requires a DE lender to review either 10 percent of the FHA loans it originates, or a "statistical random sampling that provides a 95 percent confidence level with 2 percent precision." HUD Handbook 4060.1, Rev-2, Section 7-3(C). M&T chose to perform the latter, but did not adhere to HUD's 2 percent precision requirement. M&T used a statistical formula to determine the number of loans it needed to review in order to adhere to HUD's statistical sampling requirements. One input into that formula was an 'Expected Exception Level,' which corresponded to the percentage of loans underwritten by M&T that contained material underwriting defects. Under the formula used by M&T, the higher the 'Expected Exception Level', the more loans M&T would need to review in order to adhere to HUD's 2 percent precision requirement. M&T's QC plan stated that M&T would use an 'Expected Exception Level' of 5 percent, a percentage that would be "periodically validated." M&T did not validate, update, or calculate an 'Expected Exception Level.' As a result, M&T's statistical sample had a precision rate that often exceeded HUD's 2 percent threshold.

- b. M&T conducted a monthly quality control review of a statistical sampling of all mortgage loans originated by M&T, including but not limited to FHA-insured loans. As a result, during certain time periods M&T reviewed fewer FHA-insured loans than if it had reviewed 10% of its FHA loans or a statistical sampling of its FHA-insured loans that provided a 95% confidence level with 2% precision. In addition, the quality control reports that M&T prepared on a monthly basis covered all of M&T's retail mortgage originations and did not separately break out its FHA loans.
- c. Prior to 2010, M&T did not review all FHA insured loans it underwrote that became EPD loans. Between 2006 and 2009, M&T only reviewed a portion of the EPD loans it endorsed for FHA mortgage insurance because M&T only reviewed those loans that M&T serviced. M&T did not service approximately 50 percent of the loans it originated. After HUD notified M&T in 2010 that it was obliged to review service-released EPD loans, M&T: (1) enhanced its QC procedures to ensure that it reviewed all EPD loans it had underwritten, and (2) conducted a QC review of service-released EPD loans that it had not previously reviewed.
- d. M&T created a QC system that reviewed M&T's underwriting quality by calculating an error rate based on the number of major errors preliminarily identified by the QC Department in the loans it reviewed in a given review period divided by the number of possible major errors in the reviewed loans. Thus, M&T's QC Department issued reports to management that identified preliminary major error rates routinely below 1 percent (for example, 00.46 percent in September, 2009). The preliminary major error rate would have been significantly

higher had M&T calculated its preliminary error rate by dividing the number of loans with major errors by all loans reviewed, in order to determine what percentage of M&T loans contained a preliminary major error. Many of these preliminary major errors did not concern FHA underwriting requirements, and after further review and obtaining additional documentation, the QC Department was able to cure many of the preliminarily identified major errors. M&T's QC Department did not publish a final major error rate that took into account its cure of preliminary findings. M&T used these preliminary major error rates to track underwriter and loan production office performance over time.

16. M&T did not fully adhere to HUD's self-reporting requirements even though M&T's QC plan consistently recognized its duty to make such self-reports. During the period between January 1, 2006 and December 31, 2011, the HUD handbook required lenders to report "findings of fraud" or "other serious violations" or "serious material deficiencies" to HUD. M&T's general practice during this time period was to report loans for which there was documented evidence of fraud. During this time period M&T's monthly QC reviews preliminarily identified numerous FHA-insured loans that contained 'Major' errors. M&T defined a "Major" error as an error that "seriously impacts loan quality, may not meet M&T and/or investor guidelines or credit standards; error may or may not be correctable." Because a "Major" error included violations of M&T's guidelines that in some instances were more stringent than FHA requirements, only some "Major" errors were required to be self-reported. Even though M&T identified numerous FHA-insured loans that contained a "Major" error, M&T did not self-report a single loan to HUD until 2008, and thereafter self-reported only 7 loans that M&T



underwrote and endorsed during the foregoing time period, significantly less than the number of “Major” errors identified.

17. As a result of M&T’s conduct and omissions, HUD insured hundreds of loans approved by M&T 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.

18. 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. M&T reserves the right to contest the use or application of this document in any future litigation.