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First Magnus violated federal law, HUD says

Brokers' incentives typical, mortgage lenders point out

By Christie Smythe

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Defunct mortgage lender First Magnus Financial Corp. broke a federal law by paying certain incentives to mortgage brokers, according to a report by the Department of Housing and Urban Development.

The report, issued by HUD's Office of Inspector General on July 14, states that First Magnus violated the Real Estate Settlement Procedures Act by providing "volume-based" and "quality" incentives for Federal Housing Administration-insured loans.

A former First Magnus executive said the loan program involved represented a fraction of the company's business and First Magnus did not believe any laws were violated.

HUD found that First Magnus paid \$58,571 in incentives from 2003 to 2006 to seven brokers for 169 FHA-insured mortgages totaling more than \$24 million, according to the report.

The report recommended that HUD "pursue administrative actions" against First Magnus owners and management in addition to other sanctions.

The law, known as RESPA, was designed to protect consumers from undisclosed costs in real estate transactions, said Lawrence H. Jacobson, a Beverly Hills attorney and national expert on real estate law.

Under the act, it is illegal for any mortgage lender to give or accept any "fee, kickback or thing of value" to real estate agents, mortgage brokers or other parties involved in a real estate settlement.

"In a perfect world, (mortgage lenders) would like a quid pro quo — 'If you refer a loan to me, I will cut you a check,' "Jacobson said.

In the past, the cost of paying referral fees has been passed to consumers by some mortgage lenders, Jacobson said.

HUD is generally the agency that enforces the law, he said.

The agency can pursue fines, cease and desist orders and other penalties against both businesses and individuals for violations. Criminal charges are also possible, Jacobson said.

Although RESPA covers most home loans, HUD sometimes focuses on violations involving federally insured loans, he said.

The report noted that First Magnus paid an additional \$44,269 in similar incentives for non-FHA loans. HUD representatives did not return calls for comment.

HUD's findings come as former executives of First Magnus are launching a new lender, StoneWater Mortgage in the previous company's headquarters, 603 N. Wilmot Road

Karl F.W. Young, president of StoneWater and former chief operating officer of First Magnus, said in an e-mail the report pertains to only a small fraction of First Magnus' business.

The company funded more than 300,000 loans during that time, he said.

"Nevertheless, First Magnus did not believe the program to be a violation of RESPA," Young said.

Other Arizona mortgage lending representatives were surprised by HUD's report. The fees described in it are fairly common in the industry, they said.

Mortgage "wholesalers," which provide funding for loans, often give extra fees to brokers for sending large volumes of business or loans that are well-handled, said Jill Hoogendyk, president-elect of the Arizona Mortgage Lenders Association.

Those fees are described as volume and quality incentives, she said.

"Far be it from me to second-guess HUD," she said. "If they saw it as a violation, they saw it as a violation. I'm not sure if in any way, shape or form that it hurt the consumer."

Violations of the Real Estate Settlement Procedures Act are taken seriously in the industry, though, said Tom Heath, vice president of advocacy for the Southern Arizona Mortgage Lenders.

"HUD is a pretty powerful entity in the lending business, and if they've got issues, certainly it would raise some eyebrows," Heath said.

First Magnus, which had a national presence, suddenly collapsed and filed for bankruptcy last August, leaving about 5,500 employees without final paychecks and numerous other creditors unpaid.

The major mortgage lender is in the process of being liquidated.

StoneWater began funding loans outside Arizona this month and like First Magnus is aiming for a national reach.

How it happened: Read the Star's coverage of the **First Magnus collapse**.

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