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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

KEVIN G. DOUGHERTY,
Plaintiff,
v.
GUILD MORTGAGE COMPANY,
Defendant,
UNITED STATES OF AMERICA,
Intervenor.

Case No. 16cv2909-JAH (BLM)

**ORDER DENYING DEFENDANT’S
MOTION TO DISMISS (Doc. No. 110)
INTERVENOR’S AMENDED
COMPLAINT**

INTRODUCTION

Pending before the Court is Defendant Guild Mortgage Company’s (“Guild”) motion to dismiss Intervenor United States’ (“United States”) first amended complaint (“FAC”) (Doc. No. 107) pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure. See Doc. No. 110. The United States filed a response in opposition. The motion is fully briefed. After careful review of the pleadings, and for the reasons set forth below, Guild’s motion to dismiss the United States’ FAC is **DENIED**.

BACKGROUND

1
2 The Federal Housing Administration (“FHA”) is an entity within the United States
3 Department of Housing and Urban Development (“HUD”) that promotes American
4 homeownership through insuring home loans. Doc. No. 20 at pg. 5. Authorized by the
5 National Housing Act of 1934, the FHA agrees to protect mortgage lenders against the risk
6 of loss caused by borrowers’ default and non-payment. 12 U.S.C. § 1701. In order to
7 underwrite FHA insured mortgages on HUD’s behalf, a lender must first apply to become
8 a Direct Endorsement Lender (“DE Lender”). Id. at pg. 13. The FHA’s Direct
9 Endorsement program (“DE program”) handles these applications, and all applicants must
10 be approved by HUD. Id. Certain DE Lenders participate in the Lender Insurance (“LI”)
11 program where DE Lenders personally endorse mortgages for FHA insurance and retain
12 all documents. Id. at pgs. 13-14. Once a loan is endorsed by HUD or a DE Lender, the
13 loan is insured by the FHA. Thus, if a homeowner defaults on an FHA-insured mortgage,
14 HUD will reimburse the lender for both the outstanding balance on the loan and other costs
15 associated with the default. Id. at pgs. 12-13. This “no-loss-guarantee” incentivizes
16 lenders to grant loans to worthy applicants with low to moderate incomes and serves as an
17 alternative to conventional financing. Id.

18 There are two ways that a DE Lender can underwrite an FHA-insured loan. One, a
19 DE Lender can “manually underwrite” a loan, in accordance with HUD underwriting rules,
20 and make a decision on extending credit to the borrower. Two, a DE Lender can use a
21 HUD-approved Automated Underwriting System (“AUD”), a software system that makes
22 credit recommendations. Id. at pg. 19. Beginning in July 2008, HUD took away the ability
23 to make this choice and began requiring DE Lenders to electronically process eligible loan
24 requests through an AUD. Id. at pg. 20. The AUD connects to a proprietary HUD
25 algorithm known as Technology Open to Approved Lenders (“TOTAL”). Id. Using data
26 that the lender puts in an AUS, the TOTAL algorithm makes a credit determination and
27 either approves, subject to certain conditions, or refers the loan. Id. Approved loans are
28 only eligible for FHA’s insurance endorsement if the data entered into the AUS is true,

1 complete, and accurate. Id. When the TOTAL algorithm refers a loan, the loan goes back
2 to the lender for manual underwriting. Id.

3 For each individual mortgage loan approved for FHA insurance, the lender must
4 make a “loan-level” certification that the individual mortgage “complies with HUD rules
5 and is ‘eligible for HUD mortgage insurance under the DE program.’” Id. at pg. 26
6 (quoting Form HUD–92900–A). The certification differs depending on whether the loan
7 was manually underwritten or the lender used an AUS. Id. For each loan that was
8 underwritten using AUS, HUD requires the lender to certify to the “integrity of the data
9 supplied by the lender used to determine the quality of the loan.” Id. For a loan that
10 required manual underwriting, the lender must certify that the underwriter “personally
11 reviewed the appraisal report (if applicable), credit application, and all associated
12 documents and has used due diligence in underwriting the mortgage.” Id.

13 Guild is a California corporation that originates and underwrites residential
14 mortgage loans for properties throughout the United States. Id. at pg. 9. Guild has been
15 participating in the DE Lender program since 1984 and in the LI program since 2007. As
16 of May 2016, HUD paid claims totaling almost \$300 million on at least 1,691 mortgages
17 endorsed by Guild. Id. at pg. 29.

18 Plaintiff Kevin Dougherty (“Dougherty”) began working for Guild as its Quality
19 Assurance (“QA”) manager in 2010. Doc. No. 27 at pg. 2. Dougherty learned that between
20 2006 and 2012, Guild had failed to report loans to HUD that presented material risk and
21 “[f]indings of fraud or other serious violations” discovered during the “normal course of
22 business and by quality control staff during reviews/audits of FHA loans.” Id. at pgs. 3-4.
23 Such reporting is required by HUD guidelines within 60 days of discovery. Id. (quoting
24 HUD Handbook 4060.1, REV-2, ch. 7-3.J, 7-4.D; HUD Handbook 4060.1, REV-2, ch. 2-
25 23). Dougherty brought these defective loans to the attention of senior management at a
26 bi-monthly Audit Committee meeting and was specifically told not to report any defective
27 loans to HUD without senior management approval. Id. at pg. 4. Dougherty became
28 increasingly concerned about Guild’s failure to report defective loans to HUD and

1 management's refusal to change Guild's faulty loan origination and underwriting practices.
2 Id. at pgs. 4-5.

3 On December 3, 2013, Dougherty filed a complaint against Guild. Id. After filing
4 this initial complaint, the Department of Justice, along with HUD and its Office of
5 Inspector General, commenced an investigation into Guild's origination and underwriting
6 of single family residential mortgages insured by the FHA. Doc. 40 at pg. 11. In January
7 2014, Guild received a subpoena from the United States Department of Justice. Doc. No.
8 27 at pg. 5. Lisa Klika ("Klika"), Guild's Senior Vice President of Compliance and Quality
9 Assurance, made comments that led Dougherty to believe that Klika suspected Dougherty
10 was responsible for the subpoena. Id. at pg. 5. Following Klika's comments, Dougherty
11 received decreased marks on his performance review despite Dougherty's steady,
12 unchanging performance. Id. at pgs. 5-6. On April 9, 2014, Dougherty filed a first
13 amended complaint See Doc. No. 5.

14 In August 2014, Dougherty was given a project relating to Guild's response to the
15 government investigation. Id. at pgs. 6-7. Shortly after the project was completed, Klika
16 determined the project was done incorrectly, and another employee, McIntosh, took
17 responsibility for the mistake. Id. A few days later, on August 19, 2014, Klika terminated
18 Dougherty, effective immediately. Id. at pg. 7. Klika justified Dougherty's termination by
19 asserting that the mistake in the project and Dougherty's purported lack of responsibility
20 had led to an erosion of confidence in Dougherty's management abilities. Id. Dougherty
21 asserts he was terminated because he engaged in protected activity under 31 U.S.C. § 3730
22 (h)(1) and not because his performance. Id. On September 8, 2014, Dougherty filed a
23 second amended complaint. See Doc. No. 8.

24 On May 18, 2016, the United States filed a complaint in intervention against Guild.
25 See Doc. No. 20. On May 26, 2016, Dougherty filed his third amended complaint (TAC)
26 alleging retaliation in violation of the FCA. Doc. No. 27 at pgs. 7-8. On November 29,
27 2016, Guild's motion to transfer venue (Doc. No. 32) was granted, and the case was
28 transferred to the Southern District of California. On June 8, 2017, this Court took the

1 pending Motion to Dismiss under submission pursuant to Civil Local Rule 7.1.d.1. See
2 Doc. No. 89. On March 4, 2019, the United States filed a first amended complaint (FAC).
3 See Doc. No. 107. Guild filed a motion to dismiss the United States’ FAC on March 22,
4 2019. See Doc. No. 110. On April 12, 2019 the United States filed a response in opposition
5 to Guild’s motion. See Doc. No. 113. Guild filed a reply to the United States’ response
6 on April 24, 2019. See Doc. No. 116.

7 DISCUSSION

8 **I. Legal Standard**

9 **a. Federal Rule of Civil Procedure 12(b)(6)**

10 A motion to dismiss under Rule 12(b)(6) tests the sufficiency of the complaint.
11 Navarro v. Block, 250 F.3d 729, 732 (9th Cir. 2001). Dismissal is warranted under Rule
12 12(b)(6) where the complaint lacks a cognizable legal theory or fails to allege sufficient
13 facts to support a cognizable legal theory. Li v. Kerry, 710 F.3d 995, 999 (9th Cir. 2013).
14 “To survive a motion to dismiss, a complaint must contain sufficient factual matter,
15 accepted as true, to ‘state a claim to relief that is plausible on its face.’” Ashcroft v. Iqbal,
16 556 U.S. 662, 678 (2009) (citing Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570
17 (2007)). A claim is facially plausible when the factual allegations permit “the court to draw
18 the reasonable inference that the Guild is liable for the misconduct alleged.” Iqbal, 556
19 U.S. at 678. In other words, “the non-conclusory ‘factual content,’ and reasonable
20 inferences from that content, must be plausibly suggestive of a claim entitling the
21 Dougherty to relief.” Moss v. U.S. Secret Serv., 572 F.3d 962, 969 (9th Cir. 2009) (citing
22 Iqbal, 556 U.S. at 678). “Determining whether a complaint states a plausible claim for
23 relief will...be a context-specific task that requires the reviewing court to draw on its
24 judicial experience and common sense.” Iqbal, 556 U.S. at 679.

25 In reviewing a motion to dismiss under Rule 12(b)(6), a court must assume the truth
26 of all factual allegations and construe the factual allegations in the light most favorable to
27 the nonmoving party. Cahil v. Liberty Mut. Ins. Co., 80 F.3d 336, 337-38 (9th Cir. 1996).
28 However, legal conclusions need not be taken as true merely because they are “cast in the

1 form of factual allegations.” Ileto v. Glock Inc., 349 F.3d 1191, 1200 (9th Cir. 2003). “Nor
2 does a complaint suffice if it tenders ‘naked assertion[s]’ devoid of ‘further factual
3 enhancement.’” Iqbal, 556 U.S. at 678 (citing Twombly, 550 U.S. at 557). The court may
4 consider facts alleged in the complaint, documents attached to the complaint, documents
5 relied upon but not attached to the complaint when authenticity is not contested, and
6 matters of which the court takes judicial notice. Lee v. City of Los Angeles, 250 F.3d 668,
7 688-89 (9th Cir. 2001). If a court determines that a complaint fails to state a claim, the court
8 should grant leave to amend unless it determines that the pleading could not possibly be
9 cured by the allegation of other facts. Doe v. United States, 58 F.3d 494, 497 (9th Cir.
10 1995).

11 **b. Federal Rules of Civil Procedure 8**

12 Rule 8 of the Federal Rules of Civil Procedure provides that in order to state a claim
13 for relief in a pleading it must contain “a short and plain statement of the grounds for the
14 court’s jurisdiction” and “a short and plain statement of the claim showing that the pleader
15 is entitled to relief.” Fed.R.Civ.P 8(a)(1)&(2). “The pleading standard Rule 8 announces
16 does not require ‘detailed factual allegations,’ but it demands more than an unadorned, the
17 Guild-unlawfully-harmed me accusation.” Iqbal, 556 U.S. at 678 (quoting Twombly, 550
18 U.S. at 555).

19 **c. Federal Rules of Civil Procedure 9(b)**

20 Under Rule 9(b) of the Federal Rules of Civil Procedure, “[i]n alleging fraud or
21 mistake, a party must state with particularity the circumstances constituting fraud or
22 mistake.” Under Ninth Circuit case law, Rule 9(b) imposes two distinct requirements on
23 complaints alleging fraud. First, the basic notice requirements of Rule 9(b) require
24 complaints pleading fraud to “state precisely the time, place, and nature of the misleading
25 statements, misrepresentations, and specific acts of fraud.” Kaplan v. Rose, 49 F.3d 1363,
26 1370 (9th Cir. 1994); see also Vess v. Ciba-Geigy Corp., U.S.A., 317 F.3d 1097, 1106 (9th
27 Cir. 2003) (citation omitted) (stating that a plaintiff must set forth the “who, what, when,
28 where and how” of the alleged misconduct). Second, Rule 9(b) requires that the complaint

1 “set forth an explanation as to why the statement or omission complained of was false or
2 misleading.” Yourish v. California Amplifier, 191 F.3d 983, 993 (9th Cir. 1999) (citation
3 and quotation omitted).

4 **II. Analysis**

5 The United States’ FAC asserts four causes of action for violations of: (1) The False
6 Claims Act (31 U.S.C. §3729(A)(1) (2006) and 31 U.S.C. §3729(A)(1)(A) (2010)); (2) The
7 False Claims Act (31 U.S.C. §3729(A)(1)(B) (2010) (formerly 31 U.S.C. §3729(A)(2)
8 (2006)); (3) breach of fiduciary duty; and (4) breach of contract. See Doc. No. 107.

9 **a. False Claims Act Causes of Action**

10 Guild argues that the United States has not properly alleged a scheme to submit false
11 claims. Doc. No. 110-1 at pg. 12. Specifically, Guild contends that the United States “fails
12 to provide any particulars about the scope and implementation of the scheme or identify
13 the specific FHA requirements the scheme was designed to flout.” Id. Guild asserts that
14 the United States is only able to allege that Guild’s work, in hindsight, was “imperfect,”
15 but does not establish falsity. Id. at pgs. 12-13. Guild argues that the United States’
16 allegations “do not provide the level of detail required for Guild to be on notice of how
17 FCA liability may attach to an individual FHA-insured loan or be able to identify the FHA
18 loans subject to the Amended Complaint.” Id. at pg. 13. Guild contends that the United
19 States fails to reference any requirements for an actual claim for insurance proceeds made
20 to HUD and doesn’t identify any specific statements from the claim form. Id. at pgs. 16-
21 17. Guild argues that the United States fails to properly plead the elements required to
22 establish promissory fraud or implied false certification. Id. at pgs. 19-20. Specifically,
23 Guild asserts that the United States needed to plead that Guild acted with a specific intent
24 to perpetuate knowing, willful fraud. Id. at pg. 20. Guild argues that the United States
25 fails to allege materiality because “the Government fails to allege which specific statutory,
26 regulatory, or contractual requirements were violated.” Id. at pg. 25. Guild also argues
27 that the requirements implicated by the United States are not material “because HUD not
28 only consistently pays claims where it knows there is or may be a violation of its

1 regulations, but it allows companies it knows have violated regulations to continue
2 originating FHA-insured loans.” Id. at pg. 34. Guild asserts that the United States doesn’t
3 present facts to meet the FCA’s scienter element nor does the United States show that Guild
4 acted recklessly. Id. at pg. 37. Guild argues that proving “[c]ollective knowledge, wherein
5 the states of mind of multiple individuals is aggregated to infer corporate intent, is not
6 sufficient.” Id. at pg. 38. Guild contends that the United States does not allege that Guild
7 was aware of any regulatory violations on any loan before certification on the loan-level
8 application for insurance. Id.

9 In response, the United States argues that it has sufficiently pled Guild’s violation
10 of the FCA by pleading the “who,” “what,” “when,” “where,” and “how” necessary to state
11 a claim for fraud. Doc. No. 113 at pgs. 16-20. The United States asserts that Guild’s
12 falsities are actionable both under an implied certification theory and promissory fraud
13 theory. Id. at pgs. 21-28. The United States contends that “Guild being a DE lender knew,
14 or should have known, that the certifications of compliance it made at the time of
15 endorsement were false because the falsities were facially apparent from the loan files that
16 it was required to underwrite in accordance with HUD’s requirements. Id. at pg. 27. The
17 United States argues that it has sufficiently pled the materiality of Guild’s fraud. Id. at pg.
18 30. The United States contends that its amended complaint “sets forth the rationale for the
19 requirements and how they are critically important to FHA lending.” Id. at pg. 31. The
20 United States specifically alleges that “[t]he entire scheme of FHA mortgage guaranties
21 presupposes an honest mortgagee performing the initial credit investigation with due
22 diligence and making the initial judgment to lend in good faith after due consideration of
23 the facts found.” Id. The United States argues that it sufficiently pled Guild’s knowledge
24 of the violation of the FHA requirements Guild certified. Id. at pg. 37. The United States
25 contends that the complaint makes plausible allegations of Guild’s scienter because the
26 detailed allegations of Guild’s knowledge and recklessness satisfy the standard. Id. at pgs.
27 37-38. The United States alleges that “the Complaint details Guild’s practice of falsely
28 certifying compliance with material FHA requirements and causing false claims to be

1 submitted to, and paid by, HUD when Guild’s improperly-underwritten mortgages
2 defaulted. Id. at pg. 39.

3 The Court finds that the United States sufficiently alleges the “who, what, where,
4 how, and why” of Guild’s misconduct. The pleadings allege with specificity how Guild
5 “knew, or should have known, that the certifications of compliance it made at the time of
6 endorsement were false because the falsities were facially apparent from the loan files that
7 it was required to underwrite in accordance with HUD’s requirements.” Id. at pg. 27. The
8 United States sets forth which requirements are critically important to FHA lending and
9 demonstrates how Guild’s scheme knowingly violated the requirements. Id. at pgs. 31-37.
10 The United States also shows, through detailed allegations of Guild’s knowledge and
11 recklessness, that its Amended Complaint satisfies the scienter standard. Id. at pgs. 37-38.
12 Thus, the Court finds that the United States’ Amended Complaint demonstrates that the
13 United States has plead with particularity sufficient to meet the 9(b) heightened standard.

14 **b. Breach of Fiduciary Duty**

15 Guild argues that the United States’ fiduciary claim fails because Congress has
16 already provided guidance through extensive statutory and regulatory framework for
17 enforcing the obligations of FHA-approved lenders. Doc. No. 110-1 at pg. 42. Guild
18 contends that because of HUD’s “administrative enforcement regime to ensure compliance
19 with program requirements and the general presumption against federal common law, the
20 Government must show any ‘few and restricted instances’ where common law is necessary
21 in this case – which it cannot.” Id.

22 In response, the United States asserts that Guild is incorrect in claiming that common
23 law is unnecessary to show a breach of fiduciary duty. Doc. No. 113 at pg. 42. The United
24 States contends that although Guild asserts that the fiduciary claim is preempted by HUD’s
25 regulatory regime, Guild does not identify any statute that would have such a preclusive
26 effect. Id. at pgs. 42-43.

27 The Court finds that Guild fails to address whether the United States’ allegations in
28 its Amended Complaint state a facially plausible claim. See Iqbal, 556 U.S. at 678.

1 Although Guild asserts that such a breach of fiduciary duty claim is preempted, Guild does
2 not identify a federal statute that preempts the United States' claim. The United States, in
3 support of its assertion that federal common law recognizes a breach of fiduciary duty
4 claim, cites to numerous federal court cases. Doc. No. 113 at pg. 42. The Court finds that
5 the United States demonstrates that here, this is one of the "few and restricted instances"
6 where federal common law is necessary. Thus, the Court finds that the United States has
7 sufficiently pled its breach of fiduciary claim.

8 **c. Breach of Contract**

9 Guild argues that the United States "fails to allege which contract or contracts it
10 thinks were violated," and also "fails to identify any specific provision or how Guild
11 breached it." Doc. No. 110-1 at pg. 43. Guild asserts that the United States' pleadings as
12 to causation are "too vague and speculative." *Id.* Guild argues that the United States does
13 not sufficiently allege that Guild caused the defaults, and based upon the pleadings, it is
14 impossible to discern how Guild breached the FHA requirements. *Id.* at pgs. 42-43.

15 In response, the United States asserts that a claim can be false under numerous
16 theories, including "when [a claim] is submitted on a contract induced by falsities or
17 fraud...." Doc. No. 113 at pg. 17. The United States argues that liability for claims
18 submitted under a contract will attach "when the contract of extension of government
19 benefit was originally obtained through false statements or fraudulent conduct." *Id.* at pg.
20 25 (quoting United States ex rel. Hendow v. Univ. of Phoenix, 461 F.3d 1166, 1170 (9th
21 Cir. 2006)).

22 The Court finds that the United States sufficiently pled its breach of contract claim.
23 The United States asserts that "Guild entered into a contract with HUD for each loan that
24 it endorsed for FHA mortgage insurance" and "[u]nder the terms of that contract, in
25 committing FHA insurance to the loan Guild represented it complied with, and obligated
26 it itself to comply with FHA origination, underwriting, endorsement, and other insurance
27 requirements." Doc. No. 107 at pg. 99. The United States contends that Guild breached
28 this contractual obligation by not complying with FHA requirements during the Lending

1 Time Period. Id. The United States argues that as a result of these actions, “HUD has paid
2 insurance claims, and incurred losses, relating to hundreds of FHA-insured loans
3 wrongfully endorsed by Guild.” Id. The court may consider facts alleged in the complaint,
4 documents attached to the complaint, documents relied upon but not attached to the
5 complaint when authenticity is not contested, and matters of which the court takes judicial
6 notice. Lee, 250 F.3d at 688-89. In viewing the totality of the facts in the light most
7 favorable to the United States, the Court finds that Guild breached its contractual
8 obligations and HUD suffered damages as a result of Guild’s breach.

9 **d. Time Bar**

10 Guild asserts that the United States’ breach of fiduciary duty claims arising prior to
11 December 3, 2010, breach of contract claims arising prior to December 3, 2007, and FCA
12 claims arising prior to December 3, 2007 are all time-barred. Doc. No. 110-1 at pg. 44.

13 In response, the United States argues that its claims are timely. Doc. No. 113 at pg.
14 43. The United States contends that Guild has failed to meet its burden of conclusively
15 showing that the United States’ actions are “conclusively time-barred”. Id. at pg. 43. The
16 United States contends that Guild “does not identify the date that the responsible
17 Government official(s) knew or should have known the facts material to the Government’s
18 claims.” Id. at pg. 44. The United States asserts that the statute of limitations began to run
19 when a false claim was submitted on an improperly underwritten loan, and not when Guild
20 underwrote that loan.” Id.


21 There is limited case law on this topic within the Ninth Circuit. In situations where
22 the Ninth Circuit and Supreme Court have not given instruction, the Court will look to case
23 law from other district courts. Other courts have concluded “that the statute of limitations
24 starts to run when a case claim is submitted to the government.” United States ex rel.
25 Durkin v. County of San Diego, 2017 WL 3315784 (S.D. Cal. 2017). Following that
26 standard, the Court finds that the United States’ period began to run when the false claim
27 was submitted and not when Guild improperly underwrote the loan. The Court finds that
28 the United States’ claims are not time-barred.

CONCLUSION

Based on the foregoing reasons, **IT IS HEREBY ORDERED** that Defendant Guild's Motion to Dismiss (Doc. No. 110) is **DENIED**.

IT IS SO ORDERED.

DATED: September 11, 2019



JOHN A. HOUSTON
United States District Judge

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