Mortgage Fraud: The Basics

In monitoring fraud activity across the United States, it has been no surprise to see so much attention to and interest in mortgage related frauds. Among the myriad of mortgage fraud schemes that exist, they generally fall into one of two categories, depending on their intended purpose: for property (i.e. housing) or for profit.

Fraud for property involves schemes whereby those wishing to become homeowners or purchase property lie or employ deception in order to qualify for a mortgage. They may do so because they cannot afford the property ("dream-house") or because they know they will not otherwise qualify for a loan without lying. This is most often done by falsifying information on a loan application, sometimes to include moderate "back-stopping" (a tradecraft term whereby which resources are employed to give the appearance that information is accurate if checked).

These are not the frauds which cause significant individual financial impact, as the borrower generally intends to pay the mortgage and use the property, often as a primary residence. In recent years, speculators have caused this type of fraud to have a greater impact because of the negative turn in housing values and demand. In those cases, property that was mortgaged based upon fraudulent loan applications by borrowers intending to make payments until such time as the property could be fixed-up and sold, could not be sold and went into foreclosure.

Most fraud for property attempts can be easily detected and prevented in the loan processing and underwriting process. Though there are many controls that can be employed to prevent fraud for property, some basic training of loan processors on red flags to look for, along with incentivation to prevent fraud, goes a long way. Combine this with verification of key information on the loan application (i.e. employment, income, credit, savings, etc…) and the risk for this type of fraud is significantly mitigated.

Unfortunately, in many recent cases, otherwise honest homebuyers were coached by unscrupulous mortgage brokers and lenders to enter false information into their loan application (in some instances, loan application information was altered without the homebuyer's knowledge or consent), being told that doing so was not illegal or common practice. That's a lie. Though this type of fraud may better fit into the next category, a lie on a loan application is a federal offense with a long statute of limitations and big penalties, including prison time.

The other category of mortgage fraud involves those committing fraud for monetary gain. These are the really financially damaging frauds with broad impact, usually involving multiple parties conspiring and working together to deceive lending institutions and homeowners or prospective buyers. As was described earlier regarding the entering or altering of false information on loan applications, numerous instances have been uncovered over the last few years where this was done on a grand scale, particularly by mortgage brokers. Their ability to do so was made easier with the acceptability of "stated income" or "no document" loans, which accepted the information on the loan application without question, much less support.

Following are descriptions of some of the more common fraud for profit schemes:

Property Flipping:

Equity skimming:

Straw buyers:

FROM FREDDIE MAC SITE:

Mortgage Fraud Schemes

Mortgage fraud is becoming more common. To protect your home and your home equity it is important to understand and recognize the signs of mortgage fraud. It's also important to know how to report fraud to state and federal authorities so they can stop scam artists from preying on innocent borrowers.

Scam artists will often target homeowners already struggling to meet their mortgage commitments or anxious to sell their homes. There is help available when facing financial problems or foreclosure, but make sure you are dealing with a reputable organization before getting involved. Fraud schemes may sound good, but ultimately the goal is to take your home – not help you keep it.

Here are several common frauds being reported today:

Foreclosure Rescue Scheme

If you have fallen behind on your mortgage payments, this may seem like an attractive solution – but beware. A foreclosure rescue scheme often begins with a scam artist offering a promise to pay off your delinquent mortgage, allowing you to stay in the home as a renter with the option to purchase the home back when your financial situation improves.

But what really happens is a series of steps designed to cash out the equity in the home and disappear:

- *As part of the "rescue," the homeowner will be required to deed the property to a new borrower who is often "investing" in a rental property, but who is really part of the scam.*
- *The proceeds of the sale pay off the delinquent loan and the new borrower removes all the equity in the house, never to be seen again.*
- *The distressed homeowner is now merely a renter in a home they no longer own, unaware that the new borrower is not making payments.*
- *When the new borrower defaults on the loan, the homeowner is evicted from the home.*

Scam artists are very crafty and will often vary the scheme depending on the homeowner they are talking to, so be cautious. Some warning signs that a scam artist may be trying to set you up as a victim of a foreclosure rescue scheme include:

- *Being approached by a stranger with an unsolicited "rescue" offer.*
- *Receiving an unsolicited call, mail or flyer about "foreclosure rescue" or saving your home.*
- *Participating in a complicated deal that you don't fully understand.*
- *Signing documents that have blanks or false statements. Regardless of what you are told, this is never okay.*

Protect yourself from fraud. Scam artists are often very charming but beware of unsolicited offers of help. The best solution when you face financial difficulties that may endanger your home is always to talk to your lender or a reputable housing counselor.

Illegal Flipping

Flipping is a legitimate practice where an investor purchases a property in need of repairs or upgrades, makes the necessary changes to the property in a very short amount of time and sells the home for a profit.

We've all seen the TV shows about flipping and they're fun to watch. But there are scam artists who use flipping to make money illegally.

Often times, the scam artist will offer much more than the asking price of a home with a stipulation that the "surplus" amount over the asking price is given back to the borrower at closing.

At closing, the inflated value of the home will be attributed to home improvements that were never made. The scam artist will pocket that surplus money and default on the loan.

As a homeowner, especially one whose house has been on the market a long time, this may seem like an attractive deal but remember – falsifying documents is fraud.

FBI:

COMMON MORTGAGE FRAUD SCHEMES

Property Flipping - Property is purchased, falsely appraised at a higher value, and then quickly sold. What makes property illegal is that the appraisal information is fraudulent. The schemes typically involve one or more of the following: fraudulent appraisals, doctored loan documentation, inflating buyer income, etc. Kickbacks to buyers, investors, property/loan brokers, appraisers, title company employees are common in this scheme. A home worth $20,000 may be appraised for $80,000 or higher in this type of scheme.

Silent Second - The buyer of a property borrows the down payment from the seller through the issuance of a non-disclosed second mortgage. The primary lender believes the borrower has invested his own money in the down payment, when in fact, it is borrowed. The second mortgage may not be recorded to further conceal its status from the primary lender.

Nominee Loans/Straw Buyers - The identity of the borrower is concealed through the use of a nominee who allows the borrower to use the nominee's name and credit history to apply for a loan.

Fictitious/Stolen Identity - A fictitious/stolen identity may be used on the loan application. The applicant may be involved in an identity theft scheme: the applicant's name, personal identifying information and credit history are used without the true person's knowledge.

Inflated Appraisals - An appraiser acts in collusion with a borrower and provides a misleading appraisal report to the lender. The report inaccurately states an inflated property value.

Foreclosure Schemes - The perpetrator identifies homeowners who are at risk of defaulting on loans or whose houses are already in foreclosure. Perpetrators mislead the homeowners into believing that they can save their homes in exchange for a transfer of the deed and up-front fees. The perpetrator profits from these schemes by remortgaging the property or pocketing fees paid by the homeowner.

Equity Skimming - An investor may use a straw buyer, false income documents, and false credit reports, to obtain a mortgage loan in the straw buyer's name. Subsequent to closing, the straw buyer signs the property over to the investor in a quit claim deed which relinquishes all rights to the property and provides no guaranty to title. The investor does not make any mortgage payments and rents the property until foreclosure takes place several months later.

Air Loans - This is a non-existent property loan where there is usually no collateral. An example of an air loan would be where a broker invents borrowers and properties, establishes accounts for payments, and maintains custodial accounts for escrows. They may set up an office with a bank of telephones, each one used as the employer, appraiser, credit agency, etc., for verification purposes.

Mortgage Fraud Prevention Measures

General Fraud Tips

Mortgage Fraud is a growing problem throughout the United States. People want to believe their homes are worth more than they are, and with housing booms going on throughout the U.S., there are people who try to capitalize on the situation and make an easy profit.

Tips to protect you from becoming a victim of Mortgage Fraud

• Get referral for real estate and mortgage professionals. Check the licenses of the industry professionals with state, county, or city regulatory agencies.
• If it sounds too good to be true, it probably is. An outrageous promise of extraordinary profit in a short period of time signals a problem.
• Be wary of strangers and unsolicited contacts, as well as high-pressure sales techniques.
• Look at written information to include recent comparable sales in the area, and other documents such as tax assessments to verify the value of the property.
• Understand what you are signing and agreeing to--If you do not understand, re-read the documents, or seek assistance from an attorney.
• Make sure the name on your application matches the name on your identification.
• Review the title history to determine if the property has been sold multiple times within a short period--It could mean that this property has been "flipped" and the value falsely inflated.
• Know and understand the terms of your mortgage--Check your information against the information in the loan documents to ensure they are accurate and complete.
• Never sign any loan documents that contain blanks--This leaves you vulnerable to fraud.
• Check out the tips on the Mortgage Bankers Association's (MBA) website at http://www.StopMortgageFraud.com for additional advice on avoiding mortgage fraud.

Mortgage Debt Elimination Schemes

• Be aware of e-mails or web-based advertisements that promote the elimination of mortgage loans, credit card and other debts while requesting an up-front fee to prepare documents to satisfy the debt. The documents are typically entitled Declaration of Voidance, Bond for Discharge of Debt, Bill of Exchange, Due Bill, Redemption Certificate, or other similar variations. These documents do not achieve what they purport.
• There is no magic cure-all to relieve you of debts you incurred.
• Borrowers may end up paying thousands of dollars in fees without the elimination or reduction of any debt.

Foreclosure Fraud Schemes

Perpetrators mislead the homeowners into believing that they can save their homes in exchange for a transfer of the deed, usually in the form of a Quit-Claim Deed, and up-front fees. The perpetrator profits from these schemes by remortgaging the property or pocketing fees paid by the homeowner without preventing the foreclosure. The victim suffers the loss of the property as well as the up-front fees.

• Be aware of offers to "save" homeowners who are at risk of defaulting on loans or whose houses are already in foreclosure.
• Seek a qualified Credit Counselor or attorney to assist.
Predatory Lending Schemes

• Before purchasing a home, research information about prices of homes in the neighborhood.
• Shop for a lender and compare costs. Beware of lenders who tell you that they are your only chance of getting a loan or owning your own home.

• Beware of "No Money Down" loans--This is a gimmick used to entice consumers to purchase property that they likely cannot afford or are not qualified to purchase. Be wary of mortgage professional who falsely alter information to qualify the consumer for the loan.
• Do not let anyone convince you to borrow more money than you can afford to repay.
• Do not let anyone persuade you into making a false statement such as overstating your income, the source of your down payment, or the nature and length of your employment.
• Never sign a blank document or a document containing blanks.
• Read and carefully review all loan documents signed at closing or prior to closing for accuracy, completeness and omissions.
• Be aware of cost or loan terms at closing that are not what you have agreed to.
• Do not sign anything you do not understand.
• Be suspicious if the cost of a home improvement goes up if you accept the contractor's financing.
• If it sounds too good to be true--it probably is!

REAL ESTATE BLOG:

*1. **AIR LOANS**: A swindler invents borrowers and properties to obtain loans. The perpetrator may set up phones and pose as borrower, employer, appraiser and credit agency when the lender calls to verify employment, income and credit.*

RED FLAGS:

1. Application completed or forwarded by someone other than the borrower.

2. Employment and address discrepancies between credit report and app lication.

4. Applicant requests to use their own appraiser

*2. **SELLER BAILOUT:** A very common scheme in weak markets (values are soft or declining) where sellers (primarily builders and developers) are finding it difficult to sell their properties at the cost of construction or to obtain their expected equity. Appraisers are recruited to over-appraise properties using older comps, etc. Buyers are recruited to purchase properties at a higher sales price with significant cash kickbacks at closing to buyers. These kickbacks may or may not be disclosed on the HUD I.*

RED FLAGS

1. Buyers are not "typical" real estate investors and are not well informed on the details of the investment property they are purchasing.

2. Appraiser appears to be well connected to seller.

3. Documentation for loan may be atypical for a purchase transaction.

4. Financing denied by another lender and reason appears suspect.

5. Source of down payment may be not appropriately documented.

6. Unusual Inquiries to loan officers asking about policies on seller credits.

*3. **CHUNKING**: A swindler holds a seminar promising to show investors how to get rich buying property with no money down. Using the investors' personal information, the swindler submits multiple mortgage applications, pocketing the loan proceeds.*

RED FLAGS:

1. *Requests for fast closings on multiple loans.*
2. *Income appears inflated on stated income*
3. *Person other than borrower heavily involved in application process*
4. *Stated Assets or VODs used from one bank on multiple loans*

*4. **DOUBLE SALES**: A swindler can record a deed, arrange a loan, and before those transactions show up in the computer, file another deed and arrange another loan. Weeks can pass between the filing of a property record and its appearance in computerized registries used by title-search companies.*

RED FLAGS

1. *Multiple new mortgage loans on credit report*

2. *Request for rush closing.*

3. *Unusual concern by borrower in details of mortgage process.*

***5. HOME IMPROVEMENT CONS:** A contractor talks the homeowner into making costly or unnecessary repairs. The contractor loans the homeowner money for the job or steers him to a mortgage lender, then has the loan proceeds sent directly to the contractor. When the loan forecloses, the contractor can end up taking the house or part of the sale proceeds from it.*

RED FLAGS

1. Cash out proceeds where title company is directed by another entity to pay proceeds of loan to someone other than the borrower.

2. Borrower does not appear well informed on reason for applying for loan. May be elderly person with considerable equity in property.

*6. **STRAW BUYER:** The swindler pays a person, often a friend or relative, for the use of his name and credit history to use in applying for a loan. This is similar to an AIR LOAN but typically involves the borrower getting paid for the use of his/her name and credit history.*

RED FLAGS

1. *Borrowers who appear to be "steered" by seller or realtor or another entity on all details of transaction.*
2. *Borrowers who appear to not ask typical questions or refer your questions to another party in the transaction.*
3. *Purpose for purchasing home appears to be atypical (not in borrower's area for investment purposes or in borrower's price range).*

As elaborate as they may appear, most of these schemes become readily apparent when the Loan Officer asks the right questions during the interview process and follows up with the right questions when something does not appear legitimate.

The challenge is identifying a conspiracy scheme when more than one person is involved particularly when they are industry professionals. The best fraud artist is an industry player because they know how to manipulate the system.

Everybody involved in a real estate transaction, professionals and consumers alike, should be mindful of these schemes and work to prevent fraud and protect the system.