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Cleaning the Augean stables: obstacles to fighting loan fraud

Part 3 of 5: Inside real estate's fraud crisis

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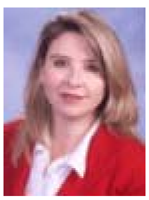
Inman News

Editor's note: In this five-part series, Inman News examines the rising tide of mortgage fraud in the U.S., giving an overview of the problem, describing how it works, explaining obstacles to fighting it and describing technologies that combat it and legislation that aims to defeat it. To read the entire five-part report, "Inside real estate's fraud crisis," with two bonus stories, subscribe to Inman News*.*


Rachel Dollar, The Dollar Law Firm

A Realtor from a small rural town in Indiana stood before the microphone in the convention hall, his palms pressed together in front of him as if in prayer. "I've been to the D.A. I've called the FBI and they told me they couldn't help me. What can I do?" he asked.

The speaker was an attendee at a mortgage fraud presentation in San Francisco at a National Association of Realtors convention in October 2005.

"Because we're small potatoes, I can't get the FBI. But this (mortgage fraud) is having a big impact on our community," the man said. "When we talk to the FBI, they are only concerned about Indianapolis."

He was standing directly across from James "Chip" Burrus, deputy assistant director of criminal investigations for the FBI and speaker at the presentation. Burrus didn't flinch.

"If it's a single buyer on a $200,000 house, we can't get involved. The threshold is $500,000," Burrus said. The director said the FBI currently has only 100 agents dealing with financial fraud.

Residential real estate loan fraud is a national epidemic, costing communities nationwide an estimated $1 billion in 2005, compared to $429 million in 2004, according to the Federal Bureau of Investigation. In this five-part series, *Inman News* examines the rising tide of mortgage fraud in the U.S. This part focuses on the obstacles to fighting it.

The fact that the FBI has only 100 agents dealing with a $1 billion crime speaks volumes about the obstacles to fighting the problem.

The number of suspicious activity reports to the FBI in 2004 almost tripled those in 2003, according to a report released last May. "Mortgage fraud is a crisis in the making," Burris told the appraisers and Realtors that made up most of the crowd at the NAR convention.

Beleaguered district attorneys and attorneys general have small staffs and limited resources to begin with. These officials are struggling to arrest and prosecute violent criminals, break up meth labs and deal with loss to life and limb, and often don't have time or staff to cope with mortgage fraud.

"The authorities *should* be more concerned with crimes against people," said mortgage banking attorney Rachel Dollar, who represents lenders in mortgage-fraud cases. "Although we need more resources (for fighting mortgage fraud), this should not be at the expense of putting violent criminals behind bars."

According to Dollar, "Generally the attorneys general deal with the consumer issues and the FBI deals with the banking issues. A lot of time it's tough to get to thresholds and the Feds don't always have jurisdiction in cases where there is only consumer damage."

Even if law enforcement officials have time and manpower to look at mortgage fraud, it isn't an easy crime to understand, much less prosecute, according to Becky White, president of the Georgia Real Estate Fraud Prevention Awareness Coalition.

"These cases are very labor-intensive to prosecute because of the ins and outs, getting to understand specifically what the fraud was, trying to trace the money," White said. "Those mortgage fraud rings create a complicated situation.

"When you have a stolen identity used, or straw borrowers used, for those types of loans there wasn't anything verified other than that credit score and having an appraisal that shows a good piece of collateral," White said.

"So it's very easy in that type of a loan program for a fraudster to get away with the crime. And it makes it very hard to prove, with the exception of the bad appraisal," White said.

White was referring to the fact that mortgage fraudsters often use "straw borrowers" – phony borrowers who were recruited for the transaction and who allow their names and credit to be used without intending to take possession of the property. Another gambit is to steal an individual's identity and use the stolen identity to obtain the loan.

In addition to constraints on law enforcement, more sophisticated technology makes it harder to detect mortgage fraud. For example, it's possible to scan in a document and then change such elements as the price at which a house is appraised using the typeface that appeared in the original document. Such alterations are nearly impossible to catch.


Bill Matthews, Conference of State Bank Supervisors

According to Bill Matthews, senior vice president, Mortgage Project, at the Conference of State Bank Supervisors, depersonalization in the mortgage lending industry is another reason it's so hard to detect mortgage fraud.

"Before the massive savings and loan failures in the 1980s, savings and loans made mortgage loans in their communities," Matthews said. Under those circumstances, it would be hard to lie on an application. Loan officers worked in the same town as borrowers and could, if they chose, drive past the properties for which loans were sought.

Under those circumstances, it would be difficult to get away with an inflated appraisal or use a straw buyer.

But in today's lending industry, where loan officers don't know applicants and often don't live in the same town as the property, it can be much harder to realize one is dealing with fraudulent material, Matthews said.

Pressure on loan officials to make money is another factor, according to Matthews. Loan officials work on commission. Now that the refinance boom is over and money is getting tighter, people who made $200,000 a year are watching their income slide into the $80,000 range. The decline makes them more susceptible to the temptation to overlook fraud.

The pressure sometimes comes from other sources, Matthews said.

"I was at a broker conference doing a mortgage fraud panel and at the end we had a question-and-answer session. One of the brokers asked, 'Is it inappropriate for us to take a borrower who doesn't qualify for a conventional loan, convert them to a stated income loan and increase their income so they will now qualify for the loan?'" Matthews said.

"Three panelists jumped out of their seats and almost wrung that lady's neck. We all said, 'It's unethical." And she said, 'What if the wholesale account rep is telling us that's what we should do?'"

Editor's Note: If you suspect mortgage fraud, the FBI suggests reporting it to your local FBI Division; a list of contact numbers appears at http://www.fbi.gov/contact/fo/fo.htm. The FBI has a mortgage fraud education page online that explains various types of schemes. The agency also accepts fraud tips at its Web site: https://tips.fbi.gov/. Mortgage industry watchdogs recommend contacting your state's regulator or attorney general.

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