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Inside Real Estate

Mortgage Scams Rising Along With Home Prices

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It was a scam undone by bad credit reports. Lenders refused home loans to several Florida A&M University graduates because foreclosures had killed their credit scores. Just one problem: None of the applicants had ever seen or owned any of the foreclosed homes.

The FBI and U.S. Attorney's office traced the properties to a lawyer/mortgage broker, Chalana McFarland, in Stone Mountain, Ga. McFarland had purchased the students' Social Security numbers from a classmate, then used them to dupe lenders into 169 loans worth more than \$20 million.

The swindle was far beyond the garden-variety scams typically labeled mortgage fraud. It is just one example of what some in the industry say is a renaissance of fraud underwritten by recent, record-setting real estate markets.

According to the FBI, mortgage fraud has surged fourfold in recent years, climbing from 4,225 cases in 2001 to 17,127 last year.

"The types of fraud occurring are moving away from the fraud for home ownership, the little-white-lie kind of fraud, to the fraud for profit, where people are just flat out looking to take money from the banks and fly," said Nick Larson, with the Mortgage Asset Research Institute.

Mortgage lenders will dole out an estimated \$2.8 trillion in loans this year, down 30% from the record \$4 trillion in 2003. But even as markets cool and the borrowing frenzy eases, many industry observers see mortgage fraud on the rise.

Among those observers: the FBI, which investigates potential fraud cases for mortgage lenders Fannie Mae, Freddie Mac and other federally involved entities.

While fraud losses among mortgage companies are on the rise, industry researchers say more specific figures on losses from fraud are hard to come by largely because lenders are reluctant to reveal such potentially embarrassing figures.

"You are not going to find them," said Rachel Dollar, a Santa Rosa, Calif.-based real estate attorney who also publishes mortgagefraudblog.com.

The FBI tracks fraud trends via suspicious activity reports, or SARs, filed by federally insured financial institutions. It reported receiving 300% more SARs last year than in 2001. The agency this year identified 26 states as having "significant mortgage fraud problems."

U.S. attorney David Nahmias, with Georgia's northern district office, says Georgia's problems revolve around Atlanta, where growing real estate schemers find safety in all kinds of numbers.

"You have a lot of inflating prices for housing and a lot of legitimate speculation," Nahmias said. "That allows the fraudsters to hide more of their transactions among a sea of legitimate ones."

In many states, the high tide of home appreciation has drawn a growing number of equity skimming swindles. Scott Bice, commissioner of Nevada's Mortgage Lending Division, says many homeowners with poor credit have found themselves

suddenly equity rich. The combination makes for susceptible targets.

One recently cracked scheme pitched homeowners an equity loan with no payments for three months. Equity would cover the payments and repair the homeowner's credit, the spiel promised. The agent would refinance the homeowner into a low interest loan. Easy as pie.

The fine print of the contract, however, stated the total loan amount was due in 120 days. After 90 days of no payments, the fraudsters filed delinquency papers.

"In the fourth month they foreclosed, sold the property and took the equity," Bice said.

Naive investors or nouveau riche homeowners aid mortgage crime in some markets. Nahmias says the real estate crime culture around Atlanta has evolved into a professionalized network.

"We've seen quite a bit of fraudsters training fraudsters," he said. "Somebody who operates as a recruiter or straw purchaser in one fraud ring then sets off to start their own scheme."

Mortgage fraud is defined in different ways. The FBI draws a clear line between mortgage fraud, where lenders suffer the loss, and predatory lending, which targets consumers. Others, like the Mortgage Bankers Association, differentiate fraud for ownership from fraud for profit.

The "white lie" strain of mortgage fraud can be what some call a victimless crime. Tom Pool, assistant commissioner of the California Department of Real Estate, says that in many cases, the state's vaulting real estate values have eased the usual impact of some crimes.

"Because of the hyperappreciation we've had, there are cases where frauds have been perpetrated on lenders, but there is enough appreciation and value in the property that there is no damage," Pool said.

Other schemes, particularly flipping, in which properties are resold fast at inflated prices, can drive up community tax assessments while driving down real property values.

Will the level of fraud fall as real estate markets downshift? Nahmias, in Atlanta, says yes and no.

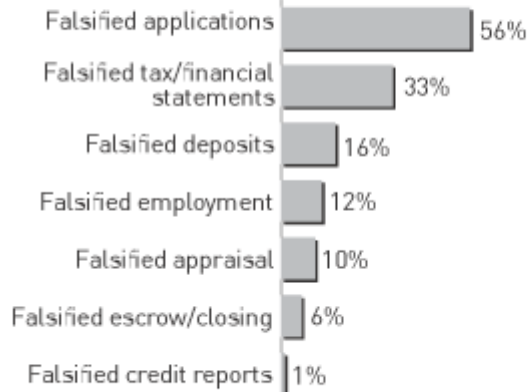
Less property appreciation will likely lead to less real estate speculation, making it more difficult to hide the illegitimate deals. The flip side is fraudsters will become more ingenious and aggressive as they struggle to maintain their incomes.

"We don't see the trouble going away because of market changes any time soon," Nahmias said.

Hot Property

The thriving real estate market has cloaked a growth industry in real estate fraud. Experts say that as the market cools, scamsters will grow more desperate and bold

How borrowers are defrauding lenders



States with highest fraud percentages

1. Georgia
2. Florida
3. Utah
4. N.C.
5. Missouri
6. Nevada
7. Illinois
8. Michigan
9. Colorado
10. California

Sources: FBI, Mortgage Asset Research Institute

[Return to top of page](#)

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