

Mortgage Loan Fraud in Texas

Presented by

The Texas Department of Savings and Mortgage
Lending

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NOTICE

- In this presentation/Q & A, there will be opinions and positions expressed. These opinions and positions are those of the Texas Department of Savings and Mortgage Lending, its Commissioner, General Counsel, senior staff and not necessarily those of the Texas Finance Commission, its individual members or other state officials.

About the Texas Department of Savings and Mortgage Lending

- ❑ Formerly the Texas Savings and Loan Department
- ❑ Regulates all State Savings Banks in Texas with combined assets of over \$9.4 billion
- ❑ Renamed in 2005 by Texas Legislature to better depict mortgage oversight
- ❑ Mortgage Broker Licensing Act of 1999 – today 24,200 licensees
- ❑ Mortgage Banker Registration Act of 2003 – today 422 mortgage banking companies registered
- ❑ Charter state savings banks, examine banks, license and inspect mortgage brokers and their loan officers, consumer complaint investigations/resolutions, issue regulatory orders, levy fines/penalties, revocations, suspensions, issue industry prohibitions, refer criminal activity
- ❑ One of three agencies under the Texas Finance Commission
- ❑ Approve all required mortgage education providers and their coursework



SML Definition – Mortgage Fraud

- A mortgage transaction in which an intentional misrepresentation(s) or omission occurs from which one or more persons benefit or profit.

Main Players

- ❑ Borrower & Straw Borrower
- ❑ Borrower's Real Estate Agent
- ❑ Seller & Broker Owner
- ❑ Seller's Real Estate Agent
- ❑ Broker/Banker/Loan Officer/Processor/Underwriter
- ❑ Lender employee
- ❑ Title agent representative/ Fee attorney
- ❑ APPRAISER(S)
- ❑ Counterfeiter – appraisal reports “borrowed”, cut and pasted/altered
- ❑ Appraiser Impersonator – borrowed another's number and credentials
- ❑ Bank employee – deposit verifications
- ❑ Fake employer – employment verifications
- ❑ Third party service provider
- ❑ Church leaders
- ❑ Relative /friend /acquaintance

New Players/Other Facts

- ❑ Builders – new participants in fraud cases (sluggish sales or slower sales and interim construction loan meter running) AND non-occupant owner fraud representation by builder with post transaction buyback agreement or debt servicing for straw.
- ❑ Identity Thieves – information gained from trash within given neighborhoods (reason for high concentrated foreclosures), then use straw borrower with stolen ID becoming popular version, impersonators posing as “authorized” industry consultants, phishing schemes (appear to be banks, insurance companies, etc.)
- ❑ Foreclosure prevention fraud rising – Due to ARM adjustment periods occurring and reducing equities in slowing markets to some degree. Mortgagors are desperate – evade foreclosure by false purchase financing (straws).
- ❑ Fraudsters becoming more patient – buy, wait 6-8 months before flip and keep this going with multiple properties. Finance proceeds to service loan for initial period
- ❑ Investor schemes increasing – infomercials, credit card schemes, religious overtones for trust (Affinity Fraud – new tag)

Mortgage Fraud Trend

INCREASING! – YES!

- Why?
 - Significant profits
 - Commission driven compensation
 - Limited regulatory/investigative resources
 - Recruitment of accomplices is easy
 - Pizza delivery employee today – loan officer tomorrow
 - Drug criminals converting
 - Professional con-men/women learning the trade



The Complaint/Investigation Process

- ❑ Accept anonymous “tips” (with evidence)- Results in departmental complaint
- ❑ Formal Complaints lead to investigation
- ❑ Covert investigations (No Notice)
- ❑ Applicant/Shopper Operatives
- ❑ Routine inspections/examinations
- ❑ Interagency information sharing enhancements
- ❑ Interstate regulatory interaction
- ❑ Lender participation and cooperation

FBI Financial Crimes Report (5-05) Updated FBI Report (10/01/05-09/30/06) & Other Facts

- 80% of all fraud involves insiders
- Becomes much more sophisticated as it evolves
- MBA est. that in 2005, \$2.5 trillion in U.S. mortgage loan originations
 - 2005 in Texas, approx. \$59 billion from just MBs/LOs as reported from their required annual production reports
 - Mortgage Brokers reportedly produce 65-70% of all U.S. mortgage loans
- Many entities not legally required to report suspicious activity SARs with FinCEN (brokers, mort. bankers)
- Georgia Legislative Assembly – New law
- 2 FBI mortgage fraud categories: For Profit / For Housing

FBI Report (incl. other facts) – cont.

- Top 11 hot spots (S. Car., Ga., Fla., Mich., Colo., Ut., Nev., Calif., Mo., Ind., Ill.)
- 2005-annualized 1,284 cases (240% increase)
- 2004 over 2003 =246% increase, over 2001= 405% increase!
- Mortgage Fraud out-shined all other types by 200% in 2004
- SML receives 1,000 complaints/yr.
- 8-10% of those are fraud cases
- **Texas Proper Perspective** – By extrapolation, 85% of Texas brokerage licensees are compliant (21,250). Of the 15% not (3,750), around half are seriously deficient (1,875). Of that number about 26% (500) are fraud perpetrators. **2% of total licensees**
- Thus, 98% of Texas brokers DO NOT participate in fraud!

FBI – Update 10/01/05-09/30/06

- All mortgage fraud programs consolidated within Financial Institution Fraud Unit (including non-financial institutions)
- MBA est. \$2.37 trillion in loans 2006
- Significant portion of industry not required to report SARs; total picture not known.
- FBI is working to establish reporting requirements for all lenders
- 2006 West Region of U.S. led with SARs with 35.9%; Central, SE & NE with 24.7%-22.6%-16.9%
- Central had 33.3% of all pending cases with West, SE and NE with 26.7%-27.2%-12.8%
- Depending on which source one uses, Texas ranks much differently.
- 818 FBI cases in fiscal 2006, 263 indictments and 204 convictions

Red Flags

- ❑ Inflated appraisals - *#1 by far!*
- ❑ Bonuses to brokers or fee-based providers POC or at closing
- ❑ Higher than customary fees
- ❑ Falsifications of income, deposits, rents, etc. (sometimes instructed as to how by broker)
- ❑ Fake supporting documentation
- ❑ Requesting documents be signed in blank
- ❑ Purchase loans disguised as refis w/cash outs
- ❑ Multi – sales – active title history
- ❑ Investment opportunities and guarantees
- ❑ Terms too good to be true

Red Flags – cont.

- ❑ High pressure tactics employed
- ❑ Unexplained excessive fees/costs
- ❑ Requiring “prepayment” of certain disallowed fees
- ❑ Investment opportunities outside of the transaction but in connection with
- ❑ Multi-level services offers
- ❑ Does not have/advertise a physical business address
- ❑ Does not disclose license number
- ❑ Bait and switch advertising

Common Types of Mortgage Fraud

- ❑ Flipping (with inflated values)
- ❑ Silent 2nds (forgivables)- VERY ILLEGAL!
- ❑ Straw Borrower(s)
- ❑ Stolen or “Leased” Identities
- ❑ INFLATED APPRAISALS
- ❑ Foreclosure Schemes- Elderly, uneducated
- ❑ Equity Skimming (normally requires a straw)
- ❑ Air Loans

NOTE: Fraud conducted within “same” ethnic groups

Fraud – Example – cont.

- Investment Opportunity – Income Property
 - Find Straw Borrower (conspirator or unwitting)
 - Inflate appraisal, listing price, sales contract
 - Inducement of “cash” from purchase closing
 - No down payment (100%+ financing)
 - Arrangements with seller – rehab lien scheme
 - Broker produce lease agreement exceeding mortgage payment
 - Broker propose to collect rents, secure leases, manage property for modest fees
 - Repeats transaction with same/other straw until first foreclosure imminent – may attempt to refi prior to default or multi-quick purchases and/or finance debt service for several months to clear early default watch

Fraud Investigative Priorities (Basic)

- ❑ Dissect/Analyze appraisal reports IN DETAIL
- ❑ Check for Internal Controls/Safeguards
- ❑ Closing disbursements analysis
- ❑ Subpoena and analyze personal and business bank statements of ALL parties involved, phone records, email, etc.
- ❑ Complaint history analysis (trends)
- ❑ Analyze sales contracts/agreements
- ❑ Collaborate with other licensing entities
- ❑ Question all parties, associates, neighbors, employees (past/present), employers, customers
- ❑ Check for associations/ties with other known perpetrators
- ❑ Computer forensics available through other state agencies

Possible 2007 Legislative Expectations

Fraud and Other

- ❑ Georgia Law version of culpability - Texas Bill HB 716 by Solomons
- ❑ Identity Theft bills
- ❑ Possible changes in disclosure requirements
- ❑ Mortgage Broker represents which party ?
- ❑ Fraud prevention/additional enforcement
- ❑ Predatory lending prohibitions bills
- ❑ Company licensing for mortgage brokers
- ❑ ABA restrictions
- ❑ Builder owned mortgage companies – incentive packages
- ❑ Contract for deed/lease purchase regulations/licensing
- ❑ More detailed disclosures
- ❑ Licensing agencies consolidation
- ❑ Increased net worth/bond license qualifier for brokers
- ❑ Migration enforcement from broker jurisdiction by licensees or ex-licensees

What can you do to fight mortgage fraud? (Industry primarily)

- ❑ REPORT IT, REPORT IT, REPORT IT, REPORT IT, REPORT IT
- ❑ Check the appraisal - learn the review process!
- ❑ Compare property and all comps' value with County Tax Assessors files/database (if appraisal is 15-20% above county value – RED FLAG!)
- ❑ Closely check title runs and reports/analyze title history
- ❑ Get educated! Get trained! Continue to do so!
- ❑ Get legal or expert advice if in doubt
- ❑ See the property, kick it, feel it, know it!
- ❑ Be proactive and get involved in the fraud cleanup
- ❑ PAY ATTENTION TO DETAIL!
- ❑ Trust your instincts – first impression normally correct
- ❑ If in ANY doubt, DO NOT PROCEED...you need the sleep
- ❑ Know or check out (with us) who you're doing business with or hiring
- ❑ Attend the SML “BEST PRACTICES” seminars to be scheduled across the state

Entertainment Segment Anecdotes

- ❑ Deljavan Case
- ❑ Counterfeit cashier's checks for restitution (11/06)
- ❑ 2 Murder Convictions
- ❑ Stress relief exposure
- ❑ Incarcerated appeal continuance request
- ❑ Confession of a fraudster
 - Thrill
 - Beat the system
 - Smarter than anyone else
 - Because I can
 - Money is good

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