

NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314

DATE: April 2008 **LETTER NO.:** 08-CU-10
TO: Federally Insured Credit Unions
SUBJ: Mortgage Loan Fraud Report

Dear Board of Directors,

The Financial Crimes Enforcement Network (FinCEN) recently released an update to its November 2006 mortgage fraud assessment. This assessment is based upon analysis of suspicious activity reports (SARs) provided by the financial industry. This updated study includes the analysis for SARs filed from March 2006 through March 2007.

In 2006, there were 37,313 mortgage fraud SARs filed. The total for mortgage fraud SARs filed in 2007 was 52,868, an increase of 42 percent. Analysis of the more recent data indicates continued trends and marked increases in certain suspicious activities. For example, reports of identity theft in conjunction with mortgage fraud SARs increased 96 percent from the previous study. According to FinCEN, the suspicious activity characterization of Mortgage Loan Fraud was the third most prevalent type of suspicious activity reported.

This report addresses several areas of interest to credit unions related to Mortgage Loan Fraud. These areas are briefly outlined below.

Vulnerabilities Identified

The review noted increases in reports of fraudulent activity by mortgage brokers and appraisers. Increased SAR filings on specified mortgage products such as cash-out refinance loans, stated income and low or no document loans, and home equity lines of credit were also noted.

Fraudulent Activities and Red Flags

A sample of depository institution SAR narratives identified commonly reported variations of mortgage fraud. Misrepresentation of income, assets, or debts was the most commonly reported fraudulent activity (43.02 percent) in the SARs reviewed. This activity involved fraudulent

misrepresentation of employment and income and failure to disclose all debts or assets. These suspected misrepresentations resulted in lower debt to income ratios resulting in the approval of loans that would otherwise be declined. Early payment defaults were reported in 5.12 percent of these narratives. Other fraudulent activities detailed include forged or fraudulent documents, occupancy fraud, and appraisal fraud. Examples of several elaborate mortgage loan fraud schemes are also included in this section.

Protective Measures

SAR filers reported various measures for detecting potential mortgage loan fraud involving particular examination procedures and red flag indicators, such as:

- Performing independent due diligence on the borrower;
- Conducting re-verification of documents;
- Reviewing income increases from year-to-year to determine reasonableness;
- Determining property described as a primary residence is outside of the member's home state, or located an unreasonable commuting distance from the stated employer; and
- Comparing signatures on all documents.

There are a variety of legitimate transactions that can raise a red flag, and the mere presence of a red flag does not automatically indicate suspicious or illicit activity.

Trends and Patterns in Total SARs Reporting Mortgage Loan Fraud

National banks filed the largest number of SARs reporting mortgage loan fraud. Credit unions filed 195 SARs reporting mortgage loan fraud for the time period April 1, 2006 through March 31, 2007. SAR filings on suspected mortgage fraud subjects increased by more than 50 percent in ten states over the previous year, and the top five states for reported mortgage fraud were California, Florida, Illinois, Georgia and Texas.

Findings Observed from Sampled Narratives

Mortgage fraud is generally divided into two broad categories: fraud for housing and fraud for profit. Fraud for housing generally involves material misrepresentation or omission of information with the intent to deceive or mislead a lender into extending credit that would likely not be offered if the true facts were known. Fraud for housing is generally committed by home buyers attempting to purchase homes for their personal use. Fraud for profit involves the same misuse of information relating to fraud for housing; however, the perpetrators of the fraud abscond with the proceeds

of the loan, with little or no intention to purchase or actually occupy the house. Both types of fraud were committed using purchase, refinance, home equity, and construction loans.

A complete copy of FinCEN's report, *Mortgage Loan Fraud, An Update of Trends based Upon an Analysis of Suspicious Activity Reports, April 2008* is located at:

<http://www.fincen.gov/MortgageLoanFraudSARAssessment.pdf>.

This review suggests that although reports of suspected mortgage loan fraud continue to grow, financial institutions appear to be initiating more stringent prevention practices. If you have any questions, please contact your regional director or state supervisory authority.

Sincerely,

JoAnn Johnson
Chairman