

**White Paper**

# **Mortgage Asset Research Institute Quarterly Fraud Report—Volume IV**

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**Mortgage Asset Research Institute**  
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The LexisNexis® Mortgage Asset Research Institute provides valuable industry insight derived from reported incidents of fraud and verified misrepresentation submitted by leading mortgage industry participants to the Mortgage Industry Data Exchange (MIDEX®).<sup>1</sup> Mortgage Asset Research Institute analyzes this data and helps the industry depict a national composition of residential mortgage fraud and misrepresentation to support efforts to combat mortgage fraud.

Like Mortgage Asset Research Institute's annual *Mortgage Fraud Case Reports to the Mortgage Bankers Association*, the *Mortgage Asset Research Institute Quarterly Fraud Report* is intended to provide industry insight into current and emerging fraud trends, as well as enable awareness of pending mortgage fraud risk. Our quarterly analyses provide more in-depth discussions of fraud types and trends over a shorter period of time. In this analysis of loans originated during the fourth quarter of 2008, we will show that the mortgage fraud landscape is beginning to change as a result of increased industry awareness of and attention to fraud.

Prior 2008 *Mortgage Asset Research Institute Quarterly Fraud Reports* have documented a dramatic increase in finding and reporting mortgage fraud to Mortgage Asset Research Institute—an increase which began during the third quarter of 2007 and continued to rise through the third quarter of 2008. For the fourth quarter of 2008, reporting is almost equal to levels at the end of 2007. Fraud reporting increased by one percent for loans originated during the fourth quarter of 2008, versus those originated during the fourth quarter of 2007. This 1 percent increase for the fourth quarter indicates that fraud reporting remained consistent with what was reported for the same time period in 2007, which was 20 percent higher than submissions received for the fourth quarter of 2006.

## Report Highlights and Trends

- Reported General Application Misrepresentation and Income Misrepresentation on the Application were not as prevalent for fourth quarter originations as they have been in previous quarters.
- Appraisal Misrepresentation rose during the fourth quarter.
- The top three states for the highest reported incidents of mortgage fraud and/or misrepresentation in the fourth quarter of 2008 are:
  - Number 1: California
  - Number 2: Florida
  - Number 3: New York

## Quarter versus Quarter Mortgage Fraud Analysis

As evidenced in Table 1 on the next page, an analysis of loans with misrepresentation and/or fraud originated nationwide during the fourth quarter of 2008 reveals that certain types of misrepresentation that have traditionally been highly ranked in Mortgage Asset Research Institute's fraud studies—General Application Misrepresentation and Income Misrepresentation on the Application, for example—were not as prevalent during the last part of the year. Application Misrepresentation, historically trending in the 60th percentile, occurred in 47 percent of reported loans with misrepresentation. Similarly, Income Misrepresentation, which in the first three quarters of 2008 occurred in 31, 36, and 38 percent of misrepresented loans, fell to 12 percent for the fourth quarter. Other fraud types related to borrowers' financial profiles also experienced drops in reported percentages: Asset and/or Debt Misrepresentation fell to 15 percent; Verification of Employment (VOE) Misrepresentation fell to 8 percent; and Tax Return and/or Financial Statement Misrepresentation fell to 22 percent.

These downward trends have several possible causes. First, the industry's shift to funding loans through conforming loan products facilitated the removal of the ubiquitous income inflation and debt erasure associated with non-conforming loan programs. Historically, some of these non-conforming "liars' loans" have proven to be riddled with unverified, inaccurate information associated with the borrower's financial worthiness. Second, the industry at-large has refocused its efforts on authenticating and reverifying loan profile information—and they are doing this on greater percentages of their loan pipelines. Of course, this is good news for the mortgage industry and the national economy; however, as Table 1 indicates, other types of mortgage fraud increased during the fourth quarter.

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The fourth quarter saw the largest increase in misrepresentation and/or fraud on the appraisal. For fourth quarter originations, 34 percent of loans with reported misrepresentation included some type of fraud associated with the appraisal. This is an increase from 19 percent in the third quarter. Nationwide, 52 percent of loans reported with Appraisal Misrepresentation included false or incorrect use of comparables; 33 percent had inflated property values between 15 and 30 percent; and 26 percent had inflated property values over 30 percent. This increase in appraisal fraud is likely due to the decline in property values nationwide.

**Table 1**

<b>Mortgage Fraud Types – All States</b>				
<b>Fraud Classification</b>	<b>Analysis of Quarter Vs. Quarter Findings</b>			
	<b>1Q 2008</b>	<b>2Q 2008</b>	<b>3Q 2008</b>	<b>4Q 2008</b>
<b>General Application Misrepresentation<sup>2</sup></b>	64%	<b>65%</b>	64%	<b>47%</b>
<b>Income Misrepresentation on the Application</b>	31%	<b>36%</b>	38%	<b>12%</b>
<b>Employment Misrepresentation on the Application</b>	21%	<b>20%</b>	17%	<b>21%</b>
<b>Asset and/or Debt Misrepresentation on the Application</b>	21%	<b>28%</b>	20%	<b>15%</b>
<b>Occupancy Misrepresentation on the Application</b>	14%	<b>6%</b>	8%	<b>13%</b>
<b>ID Theft</b>	1%	<b>1%</b>	1%	<b>1%</b>
<b>Verification of Employment Misrepresentation</b>	18%	<b>16%</b>	11%	<b>8%</b>
<b>Verification of Deposit and/or Bank Statement Misrepresentation</b>	18%	<b>21%</b>	22%	<b>23%</b>
<b>Tax Return and/or Financial Statement Misrepresentation</b>	24%	<b>28%</b>	35%	<b>22%</b>
<b>Undisclosed Non-Arm's-Length Transactions</b>	6%	<b>6%</b>	4%	<b>6%</b>
<b>Appraisal Misrepresentation</b>	15%	<b>21%</b>	19%	<b>34%</b>
<b>Credit History Documentation Misrepresentation</b>	6%	<b>3%</b>	3%	<b>2%</b>
<b>Escrow and/or Closing Document Misrepresentation</b>	3%	<b>4%</b>	3%	<b>10%</b>

Other types of mortgage fraud, such as Identity Theft and Undisclosed Non-Arm's-Length Transactions, remained constant throughout all four quarters of 2008.

## Fourth Quarter 2008 State Rankings

The top states for fraudulent mortgage activity for loans originated during the fourth quarter of 2008 are shown in Table 2 below.

**Table 2**

4Q 2008 Mortgage Fraud Rankings <sup>3</sup>		
1	California	22%
2	Florida	15%
3	New York	10%

For the first time in 2008, California topped Florida as the first-ranking state for reported mortgage fraud with 22 percent of all submissions for loans with misrepresentation originated during the fourth quarter. Florida is second, with 15 percent of fourth quarter reports. New York ranks third with 10 percent of all reported loans with fraudulent activity.

Within the state of California, 62 percent of the fourth quarter reported misrepresentation occurred in the Los Angeles Metropolitan Statistical Area (MSA). The Los Angeles MSA's primary mortgage fraud problems are: fictitious bank statements; incorrect assets listed on the loan application; incorrect employment history listed on the loan application; and altered tax documents and/or W-2s.

The Miami-Ft. Lauderdale MSA has more reported cases of mortgage fraud than any other MSA in the state—38 percent of cases for properties in Florida occurred here. Within this MSA, the most reported type of fraud is inflated appraisal value of over 30 percent. Other prevalent types of misrepresentation for this MSA include: incorrect income, employment, assets, and debts/liens on the loan application; fictitious bank statements; and altered tax documents and/or W-2s.

Eighty-nine percent of reported loans with misrepresentation in the state of New York are for properties in the New York City MSA. The top issues for this MSA are: material omissions of information on the appraisal that affect value; fictitious bank statements; and altered tax documents and/or W-2s.

A detailed breakdown of fraud types across the top three states can be found in the next section.

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## Fraud Types

Table 3 presents percentages for specific mortgage fraud types in each of the top three states for the third and fourth quarters of 2008.

**Table 3**

Fraud Classification	Analysis of 2008 State-Specific Findings, Third Quarter vs. Fourth Quarter <sup>4</sup>					
	California 3Q	California 4Q	Florida 3Q	Florida 4Q	New York 3Q	New York 4Q
General Application Misrepresentation	72%	<b>64%</b>	63%	<b>45%</b>	91%	<b>42%</b>
Income Misrepresentation on the Application	38%	<b>5%</b>	48%	<b>17%</b>	61%	<b>5%</b>
Employment Misrepresentation on the Application	21%	<b>21%</b>	15%	<b>26%</b>	4%	<b>16%</b>
Asset and/or Debt Misrepresentation on the Application	24%	<b>24%</b>	19%	<b>14%</b>	22%	<b>16%</b>
Occupancy Misrepresentation on the Application	7%	<b>21%</b>	2%	<b>14%</b>	22%	<b>11%</b>
Verification of Employment Misrepresentation	24%	<b>7%</b>	15%	<b>10%</b>	17%	<b>0%</b>
Verification of Deposit and/or Bank Statement Misrepresentation	38%	<b>40%</b>	13%	<b>31%</b>	35%	<b>21%</b>
Tax Return and/or Financial Statement Misrepresentation	31%	<b>19%</b>	33%	<b>17%</b>	57%	<b>32%</b>
Undisclosed Non-Arm's-Length Transactions	0%	<b>7%</b>	6%	<b>3%</b>	4%	<b>0%</b>
Appraisal Misrepresentation	7%	<b>12%</b>	15%	<b>34%</b>	13%	<b>26%</b>
Credit History Documentation Misrepresentation	0%	<b>2%</b>	2%	<b>0%</b>	9%	<b>16%</b>
Escrow and/or Closing Document Misrepresentation	3%	<b>10%</b>	0%	<b>7%</b>	4%	<b>11%</b>

The data presents a number of interesting trends:

- Trending for General Application Misrepresentation and Income Misrepresentation on the Application for the top three states mirrors the national statistics presented in Table 1. California saw decreases to 64 percent and 5 percent on Application and Income Misrepresentation, respectively. In Florida, Application Misrepresentation fell to 45 percent and Income Misrepresentation fell to 17 percent. The most dramatic drops in these categories appear in New York—Application Misrepresentation is down to 42 percent from 91 percent; and Income Misrepresentation is down to 5 percent from 61 percent. Reasoning for these decreases appear in the discussion of Table 1.
- Similarly, all three states saw significant decreases in reported misrepresentations on the VOE and Tax Returns and/or Financial Statements.
- Although reported Income Misrepresentation decreased in the fourth quarter, Employment Misrepresentation on the Application in Florida and New York increased to 26 and 16 percent, respectively.
- California and Florida saw increases in Occupancy Misrepresentation, while New York saw a decrease.
- Reported Appraisal Misrepresentation increased in the fourth quarter in all three states—it increased to 12 percent in California, 34 percent in Florida, and 26 percent in New York. Again, this trend mirrors the nationwide data presented in Table 1.
- At 16 percent, New York had the highest percentage of reported misrepresentation associated with the borrower's Credit History.

## Conclusions

It is clear from the data in this report that awareness and subsequent action from the mortgage industry can make a difference. Regulators and industry participants have focused on verifying (and reverifying) income and other pertinent personal information associated with loan applications, and these types of reported fraud have decreased in the fourth quarter. As non-conforming loan products became virtually nonexistent, so followed decreases in these programs' most significant problem areas. However, although reported mortgage fraud is still as prevalent as it has been over the last 15 months, the most prevalent fraud types are changing with the industry.

*For more information, visit [risk.lexisnexis.com/mari](http://risk.lexisnexis.com/mari)  
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## End Notes

- <sup>1</sup> These submissions contain accounts of subscriber-verified material misrepresentation and/or fraud.
- <sup>2</sup> General Application Misrepresentation includes, but is not limited to the following categories of fraud on the loan application: incorrect name(s) used for the borrower(s); occupancy, income, employment, debt, and asset misrepresentation; different signatures for the same name(s); invalid Social Security Number(s); misrepresented citizen/alien status; incorrect address(es) and/or address history; and incorrect transaction type.
- <sup>3</sup> Ranking is based on total numbers of investigations submitted to Mortgage Asset Research Institute by its subscribers for loans originated during the fourth quarter of 2008. This is not a Mortgage Asset Research Institute Fraud Index (MFI) ranking, and the rankings presented in this report should not be compared to Mortgage Asset Research Institute's annual Mortgage Fraud Case Reports to the MBA because of this difference in methodology. Each series of reports presents a different view of mortgage fraud statistics.
- <sup>4</sup> It should be noted that the percentage for each state exceeds 100 percent, as most incidents contain more than one type of fraud.

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