

# Mortgage Fraud Summit report

The Canadian Association of Accredited Mortgage Professionals (CAAMP) hosted its annual Mortgage Fraud Summit on October 8, 2010 in Vancouver. I attended the conference representing the Appraisal Institute of Canada (AIC), along with AIC President, Grant Uba.

A theme in many speaker presentations was that mortgage fraud is relatively easy to implement. The RCMP has limited resources to tackle fraud and it is difficult for them to make the case to divert funds from solving violent crime.

There are common elements in many mortgage frauds. We learned that:

- generally, fraudsters need someone on the 'inside' who can electronically file land title office documents;
- a 'straw buyer' is generally used to establish property title transfers at inflated values;

- appraisers play a key role in substantiating inflated values;
- some lenders do not report suspicion of fraud, since they do not want adverse publicity; and
- automated value models can be manipulated to produce inflated property values.

A number of speakers shared case studies in mortgage fraud. One case study, provided by Bill Edmunds of Equitable Trust, concerned its 2008 purchase of a 'book' of mortgages in Yarmouth, Nova Scotia. Equitable Trust is an 'Alt-A' or sec-



ondary lender that specializes in borrowers with a good credit history who are self-employed. In this case study, the mortgage book involved about 60 single-family and multi-family properties secured by several lenders. Unknown to the Trust, the loans had been fraudulently originated. The portfolio of properties was purchased by an elderly owner through a purchase and sale agreement at double the market value. The purchasers were involved in the sale of drugs and were laundering their proceeds. The purchasers were careful to include a small number of properties in each mortgage application to keep the level of scrutiny low. They failed to disclose in their loan application that they secured other mortgages from another borrower for similar properties.

The appraiser ensured that properties were valued using sales of other properties purchased at inflated values by the same purchasers. The fraud came to light when the borrowers were arrested by the RCMP for drug dealing and the mortgage payments stopped. An inspection of the properties by the Trust revealed that most of the properties were in very poor condition and, in most cases, were inhabited by drug dealer's clients. The Trust suffered a \$1.5 million loss, but managed to recover this amount from the lender who sold the mortgage portfolio. The interesting aspect of this case, confirmed by the RCMP, was that organized crime is frequently involved in mortgage fraud, either to launder money or as diversification into another criminal activity.

Jeff Holub of the Gowlings national law firm discussed a well-publicized fraud case in Edmonton, Alberta involving condominium conver-

sions. Known as Village on the Park, the project involved six lenders and 20 mortgages in two projects. The straw buyer (borrower) purchased a large number of units and obtained 65% financing. The buyers had put up no money in the deal and, in some cases, were relatives of the developer or others who had agreed to provide their name in exchange for a fee. The borrowers' appraiser used only sales of units within the complexes for valuation. Subsequently, the lenders retained an appraiser to review the valuations and learned that the market value was about 30% of the appraised value, after 12 months.

This fraud was uncovered when one of the straw buyers contacted the bank wondering why his 'fee' had not been paid. One important lesson from this fraud is that, contrary to generally accepted appraisal practice, the best indicators of value may not always be sales within a condo project. It is important to appraisers to test these values with sales and listings from comparable projects.

Roger Brown of the RCMP Commercial Crime Section commented that we still need human oversight for automated systems. The more complex the system, the more susceptible it is to fraud. He expressed his view that automated valuation models (AVMs) are like "building a bomb." Expert overview of AVMs and other mortgage decision making tools are essential.

Jacqueline Ogilvie, responsible for monitoring VanCity Savings Credit Union's mortgage portfolio noted that most of its mortgages are secured by AVM reports. However, VanCity also relies on credit scoring for each loan applicant


and conducts a detailed audit on 10% of all loans. VanCity currently experiences a very low level of mortgage fraud.

The counter point to this argument was offered by Michael Jenkinson, national director of appraisal services for FNF Canada, a national appraisal management company (AMC). Mr. Jenkinson noted that AMCs were embraced by the lending industry because the number one problem with appraisals is undue influence and lender coercion. He sees this problem every day and observed that there are three major ways in which appraisers fall victim to lender pressure:

- appraisers are given the sales contract and encouraged to 'hit the number,'
- appraisers restrict use of comparable evidence and use adjustments to reach predetermined results, and
- appraisers use unsubstantiated assumptions in the interest of reaching a certain number.

In his view, the industry is in denial if it believes appraisal pressure is not common in Canada. AMCs place a 'firewall' between the appraiser and lender who originates the loan.

President Uba, speaking after Mr. Jenkinson, offered the view that AMCs can also produce the same appraisal pressure. President Uba noted that members have confirmed that, when they fail to meet AMC's expectations for value levels, they receive no further work assignments. President Uba also warned mortgage brokers about the potential for fraudulent use of appraisers' signatures to create false valuations submitted electronically. Apparently, the AIC is taking steps to tighten up member use of electronic signatures with services such as Notarius.

A number of speakers touched on the widespread Calgary mortgage fraud and litigation concerning the Bank of Montreal. Due to the complexity of the investigations, it is apparent that it will be a number of years before this case comes to court. 

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