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Understanding the Scale of Mortgage Fraud

How much does mortgage-related fraud really cost the sector?

There is no denying that the number of mortgage fraud incidents being unearthed is on the increase. Industry organisations, gurus and analysts are all quoted in the press saying that the numbers of identified fraud-related cases have increased over the past 12-18 months, and will continue to do so going forward.

Much of this is being blamed on the current economy, as uncertain times unfortunately go hand in hand with an increasing number of people resorting to 'creative' ways of accessing additional funds to maintain or increase their current standard of living or lifestyle – whether this is falsifying a mortgage application or by a wide range of other means.

Aside from individuals who are chancing their arms through one-off acts of fraudulent activity, there are also the organised groups to take into consideration. It is these that are typically generating the larger scale frauds that are costing the mortgage sector the most, with multi-million pound losses that could create potentially longer-term harmful consequences to the market.

When it comes to assessing the full scale and financial cost of fraud however, and in particular I am referring solely to mortgage-related incidents, it all becomes a little cloudy and difficult to quantify. There are a vast amount of stats and figures available on the topic, although they vary greatly in scale based on how the analysing organisation has generated the calculation.

From reading reports into the financial-related crimes, it is however unclear as to whether the actual volume of incidents has increased or whether in fact greater regulation, tighter lending criteria and improved technologies to analyse mortgage fraud have simply highlighted cases that would have previously gone 'under the radar', or even potentially written off as bad debts by the lender?

In the US, the FBI publishes an annual report on mortgage fraud. The latest report identified that the cost to the US lending industry was more than one billion dollars last year and is on track to increase in 2009. It also found that suspicious activity reports filed by financial institutions in

2008 for mortgage fraud showed losses of more than 1.4 billion dollars, which was a substantial increase of 83.4 per cent compared to 2007.

However, a large proportion of the US mortgage industry does not instil mandatory, centralised fraud reporting to capture incidents of attempted and successful crimes. In addition, the FBI reports that as initial mortgage products are repackaged and sold to secondary markets, it conceals or distorts the fraud meaning it is not reported to the authorities. This means the true scale of mortgage fraud in the US is largely unknown.

How does the UK compare? Here too, there is no centrally managed database or organisation that logs all incidents of attempted and successful mortgage fraud here in the UK. There are however organisations analysing cases that have gone through the high courts, those that assess reported cases where the crime value exceeds £50,000 and various other calculations made by individual groups, which provide a glimpse into the shape of the market.

For example, if we look at the latest figures released from KPMG's Fraud Barometer, (which takes into consideration major fraud cases that were presented in UK courts and where the charges exceeded £100,000,) the report identified that the total value of fraud cases during the first half of this year had a total value of £636m. The number of court cases related specifically to mortgage fraud had a combined value of £24m, which compares to the reported £36m for the whole of 2008.

In July this year, BDO Stoy Hayward released its FraudTrack report, which is developed using data from publicly available sources including the UK's national, regional and local press and analyses fraud cases that were reported to be over £50,000. This confirmed that the total of all fraud cases in the UK during the first six months of the year are to have cost the country £960m. Specific fraud related to property came in at £97m, which is just over 10 per cent of the total sum. Simon Bevan, head of BDO Stoy Hayward's fraud services team was reported to say he was surprised by what he felt was a particularly low total for mortgage-related crime, however 'banks, property companies, housing associations that are hit by property frauds are very unlikely to go to the criminal courts.'

As you will see, the difference between the figures quoted in these two reports alone represents a gap of £73 million between the lowest and highest quoted total for mortgage fraud in the first half of this year.

We believe, however, that these figures are the tip of an iceberg, particularly when you take into consideration that these statistics are based purely on incidents that have been taken through the judicial system or reported in the media. They don't take into account the other cases that have gone undetected or unreported, and, as there is currently no central resource for recording all attempted and successful incidents of fraud, a clear-cut figure regarding the scale of fraud is difficult to come by.

According to a progress report published by the National Fraud Strategic Authority (NFSA), it stated that industry opinions greatly differ as to the full scale of mortgage fraud losses, however estimates are said to be in the hundreds of millions of pounds and that 'fraud for profit', i.e. where a mortgage has been obtained and the funds are then stolen poses a more significant and organised threat over 'fraud for property', which is where an individual inflates their salaried income in order to get the property they want.

The NFSA is working closely with the industry on a number of initiatives that we are interested in monitoring over the coming months. In particular, 'intelligence sharing' is a key initiative that will help the industry stay ahead of the constantly evolving fraudster. It is also focused on improving lenders access to check the validity of documentation used in the mortgage process and finally the implementation of safeguards and controls via an increased use of fraud prevention tools and techniques has also been highlighted as a key consideration.

At Quest, we see there are great advantages of the industry working closer together to intelligently scrutinise mortgage applications from every angle. As they say, knowledge is power and so by working together we will be able to analyse a greater amount of detail to help combat this increasing threat.

As technologies continue to advance across the UK's lending community, security will become even tighter. Analysis of real-time and historic data from multiple lenders will report suspicious characteristics and therefore help combat the increasing number of cases.

When it comes to mortgage-related fraud, the real challenge for lenders is to not only catch up with criminals' constantly evolving fraudulent activities, but to overtake them. It is therefore essential that the next generation of fraud related technology also continues to evolve. Eventually the technology must become as much a deterrent as a detective, to force the fraudsters to go elsewhere.

At Quest, we have developed a new tool that adds an additional layer of security to the entire process. Q-Guard was beta-launched 18 months ago and has been designed to analyse for areas of risk at the point of valuation. It was the first product of its kind to market and works by detecting suspicious characteristics, which are automatically sent to the lender as an alert. This provides them with the opportunity to investigate the application more thoroughly before it is processed.

During the past 18 months, we have witnessed an increase of 132% in the number of Risk Alerts that are being issued to lenders by Q-Guard. And already this year, Q-Guard has highlighted over 10,000 suspicious transactions and has been successfully used to track fraudsters who make multiple applications across several lenders, which Quest is uniquely positioned to do.

Understanding the true scale of mortgage fraud isn't a simple calculation, and unfortunately as technologies become even more advanced, the industry works closer together on new initiatives and regulation is tightened further still, the figures are likely to rise further still as new cases are unearthed. However in the long term, we believe the number of individuals or groups operating fraud scams will start to reduce as they become more acutely aware of the steps being taken to stamp out such activities and the stricter penalties that are being dealt as a result.

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Bernard Herdan, CEO of the National Fraud Authority (NFA):

"Estimates suggest that mortgage fraud costs the UK economy hundreds of millions each year. However, it's not just the financial impact of this crime that is so worrying but also the devastating effect it can have on innocent homeowners and businesses.

Fighting this crime has been a top priority for the NFA since its inception. In the last 18 months our work in this sector has been unprecedented. By bringing together all the groups involved in the mortgage process, the NFA has provided a structured approach for people to identify the causes - and most importantly - develop and own solutions to shut down opportunities for fraudsters to exploit the buying process.

Working together we have already made major gains. A pilot between HMRC and lenders has prevented over £16 million worth of fraudulent transactions and the re-launch of the FSA's 'Information of Lenders' scheme has led to a 25 percent jump in reports of suspicious brokers with 24 suspensions and £300,000 in fines.

Currently the NFA is looking at further ways to curtail the activities of corrupt professionals. Removing these links in the chain can have a massive impact on this organised criminal activity."

Sarah Robson, spokesperson, Council of Mortgage Lenders

"There is very little data which makes it difficult to quantify the true extent of the volume and value of mortgage fraud.

Lenders have to be constantly vigilant against fraud as the difficult market conditions are leading criminals to target lenders in different ways. Sharing information remains crucial in combating their activities.

Individual lenders have their own measures for detecting and combating fraud and we continue to work to improve the flow of information between lenders, police, the Financial Services Authority (FSA) and other industry professionals, including conveyancers, surveyors, solicitors and accountants.

Last year, we helped the FSA to re-launch the 'information from lenders' initiative, targeting suspected fraud by intermediaries. We are encouraging more firms to contribute to the scheme, which provides a highly effective channel through which lenders can report their concerns about potentially fraudulent mortgage applications coming from brokers. By looking at information from a variety of sources, the FSA has been able to take decisive action against the relatively small number of fraudulent brokers. Since it was re-launched last summer, more lenders are contributing to the scheme and there has been a 25% increase in the overall number of reports to the FSA."

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