

Extract from the CML Mortgage fraud manual

Date: August 1989

Subject: TYPES OF FRAUD

Introduction

1. Although it would be difficult to produce a comprehensive list of ways to perpetrate fraud or criminal deception in the mortgage area, the following list refers to the most prevalent types-

- (a) The mortgage applicant himself giving a false income on the mortgage application form to increase the size of the mortgage. This will enable him to buy a property which he could not otherwise afford, or to obtain a loan for which he would not otherwise qualify.
- (b) Stating that the property will be used for owner-occupation when the applicant's real intention is to let it (it is likely that some breach of the MIRAS provisions will be involved in such cases-see section D).
- (c) Falsification of personal details, particularly relating to income, by introducers on behalf of their clients to obtain mortgages which they would not otherwise be granted.
- (d) False valuation of properties by valuers to obtain, for example, a higher mortgage than is necessary to purchase the property, or where there is collusion between the valuer and purchaser to defraud the owner.
- (e) Fraud by professionals can involve introducers, solicitors, licensed conveyancers, valuers and accountants, either individually or in collusion. Mortgages may be obtained for applicants who do not exist, or on properties which do not exist. Alternatively, a number of mortgages may be obtained from different lenders on the same property at the same time.
- (f) Forged deeds-falsifying the deeds of a property could enable the fraudster to sell it to a number of different buyers at the same time.
- (g) Staff fraud-a member of staff processes the fraudulent mortgage application(s) with full knowledge and participation in the deception.

The main characteristic of each of these types of fraud are considered in the following paragraphs.

Status Fraud

2. This may be committed on the applicant's own initiative, if he is able to provide a forged reference in support of the stated income, but can also involve the deceitful collusion of his employer. In cases where a reference is forged by the individual acting alone, the applicant might not work for the employer stated or, if he does, his income would be inflated. An applicant may misrepresent his credit status, eg by not giving information on a County Court judgment against him, or that he has previously been evicted, or that he is or has been bankrupt, or that he has an existing mortgage or other loan. Assuming that the mortgage valuation is valid and a charge is validly executed on the property to protect the lender's security, the only person who may suffer is the applicant if he takes on a commitment which he subsequently finds difficult to meet. Lenders would be

unlikely to suffer a financial loss, even if mortgage arrears subsequently accrued, if the security can be realised by possession and sale of the property (depending on the accuracy of the valuation, the position of the property in the country and the state of the housing market).

Unauthorised Letting

3. The most usual method of committing the most serious type of this particular fraud is for a number of properties to be purchased by the same person with mortgage advances from different lenders. The applicant may use his own name in each case or, alternatively, adopt one or more assumed names. Obviously, the employer's reference would normally be forged but there would be no need for a dishonest solicitor or valuer to assist in the fraud if different solicitors and lenders are employed in each case. The normal practice would be for the owner to let properties purchased, typically to students or homeless persons whom the local authority is obliged to rehouse, and the rent would be used to make the monthly mortgage payments. The fraudster would pocket the difference between mortgage repayments and the rent received from the tenants (or from the local authority on their behalf) each month. If the mortgage application states that the purchaser will occupy the property as his only or main residence, and the loan has been included within MIRAS, this will amount to a breach of the MIRAS provisions (see Section D). Lenders which suspect that there has been a MIRAS fraud must notify the Inland Revenue. From lenders' financial point of view, as it is often a feature of this type of case that the mortgage repayments are made with scrupulous regularity, they may not suffer any financial loss (and if arrears did accrue, they should still be able to obtain possession of the property to realise their security). However, if a lender writes to the occupants to notify them that it is aware there has been an unauthorised letting, but fails to seek possession, a court might construe this as a waiver of any rights under the mortgage to take possession if proceedings are subsequently taken.

Introducers and Applicants acting together

4. A variation of the status fraud highlighted in paragraph 2 above can be committed where an introducer eg a mortgage broker, instigates the fraud, by encouraging the applicant to give false details on the application form, and arranges the mortgage on his behalf. The introducer may benefit by charging the applicant a substantial fee for his advice, for processing the application, or even for forging references. He may also receive commission from the mortgage lender in respect of the mortgage arranged through it, and commission on any endowment policy. The introducers are helped by the ease with which blank P60 forms and company notepaper can be obtained or falsified. The lender has been notified of cases where the introducer has encouraged an applicant to purchase a number of properties in the same way, through different lenders, and so the unauthorised letting fraud referred to in paragraph 3 may also be involved.

Valuation Frauds

5. The simple example of this type of fraud is where the property is over-valued to obtain a larger mortgage than would otherwise have been granted and the funds not needed to purchase the property are divided between the valuer and the fraudster.

6. A fraud may also be committed in connection with an under-valuation of the property. This would normally be arranged by an estate agent who would fix the price for the property and introduce the purchaser, who would be acting in collusion with the agent. Once the purchase was completed, the usual practice is to arrange a quick re-sale of the property at its proper valuation. A lender would not normally be adversely affected by such a fraud, if it provided a mortgage to the purchaser, as it would have the security of a charge on the property. The financial loser would be the original seller who would have sold the property at too low a price as a result of the fraud by the estate agent.

7. Another variation of the valuation fraud is where the valuation report is itself a forgery. This is designed to either benefit a vendor who is defrauding a purchaser and the lender or a purchaser/owner who is defrauding the lender. The forged report could give false details of the valuation, of the age and condition of the property, or of the occupancy, all of which would mislead a lender's assessment of the property as a mortgage security. Clearly the valuation fraud could cause considerable loss to the secured lender. It is unlikely to be detected by the solicitor.

Frauds by Professionals

8. This type of fraud, in its different guises, is particularly serious as it can lead to the highest financial losses for mortgage lenders. Where a mortgage is obtained in the name of a non-existent borrower, the lender may obtain redress eg rights of subrogation. Alternatively, if the solicitor or licensed conveyancer commits fraud or is dishonest, compensation may be obtained by making a claim against the Law Society's or the Council for Licensed Conveyancers' Compensation Funds. However, this redress is discretionary. Compensation from the Law Society's Compensation Fund is not available as of right and to succeed a claimant must always in addition to fraud or dishonesty prove 'loss or hardships' (see Section 36 of the Solicitors Act 1974). Under Rule 4 of the Council for Licensed Conveyancers Compensation Fund Rules 1987, a grant may be given out of that compensation fund for the purpose of relieving or mitigating a loss suffered in consequence of fraud or dishonesty. Where there are multiple applications and loans on the same property, involving the same solicitor or licensed conveyancer acting in all transactions, it is likely that all of the mortgage lenders involved will lose financially. It is this type of fraud which has been the main subject of press speculation and substantial police investigations.

9. A variation on the 'professionals' fraud theme can arise where a dishonest conveyancer arranges a number of completions on one day, or over a short period of time, on properties which have been properly valued but on behalf of applicants who do not exist and/or who may not have entered into a contract to purchase. In a case highlighted in the past, a solicitor who committed this type of fraud cleared the proceeds of the advance cheques through his account and left the country with the proceeds before the fraud was discovered. A further variation, which involves the collusion of estate agent, solicitor and purchaser, is to overstate the house purchase price in the mortgage application form so that the purchaser is granted a larger mortgage loan than he would otherwise obtain from the lender. The difference between the actual price of the property and the amount of the loan could be used to enable the purchaser to pay his costs in connection with the transaction or for some other purpose.

10. Other professional fraud can arise where a solicitor/licensed conveyancer acts for both the vendor and purchaser and the desire to please the vendor client leads to a lack of attention to the interests of the purchaser and/or his mortgagee. Ordinarily, to act on behalf of both vendor and purchaser could give rise to a conflict of interest and would be contrary to the Solicitors' Practice Rules. However, Rule 6(2) sets out exceptions to this general principle, and it is in respect of these cases that the possibility of fraud may arise. Fraud can also arise where a solicitor/conveyancer is allowed to act for the society if he/she is personally interested in the conveyance either as vendor or purchaser.

Forged Deeds

11. Forged deeds could cause substantial loss to lenders where a number of mortgages on the same property are obtained at the same time from different lenders. The main danger area at present is in respect of unregistered land. However, the Police are particularly concerned that this type of fraud may become more prevalent in the future for registered land if the Land Registry is opened to the public, as provided for in the Land Registration Act 1988. This Act is not yet in force, but it is proposed that it should be implemented in the next two years.

Staff Fraud

12. Each of the frauds set out in paragraphs 2 to 11 above can be more easily carried out, and can be potentially more damaging to the lenders involved in both money and public relations terms, if a member of staff is a party to the fraud and processes the fraudulent applications.