# **Understanding Mortgage Fraud**:

## Early Detection and Prevention

**Research Project for Emerging Issues/Advanced Topics Course**

**Diploma in Investigative and Forensic Accounting Program**

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## INTRODUCTION AND OBJECTIVE

The objective of the paper is to understand how mortgage fraud currently is being perpetrated in Ontario and assess whether or not initiatives adopted in the United States to combat mortgage fraud may be applicable or adaptable to the situation in Ontario.

This paper discusses mortgage fraud in the residential property market focusing on Ontario. The current mortgage lending market and the parties involved in residential real estate and mortgage transactions are reviewed and the variety of ways in which residential mortgage fraud ("mortgage fraud") can and does occur in Ontario are discussed. The paper then reviews mortgage fraud in the United States, specifically the types of mortgage fraud perpetrated in the U.S., the actions that U.S. organizations are taking in their efforts to combat mortgage fraud and assesses whether such initiatives may be of benefit in Ontario. The paper concludes by discussing strategies for early prevention and detection of mortgage fraud in Ontario.

Mortgage fraud has gained prominence in the Canadian media and the mortgage industry recently. In March 2005, CTV's W5 investigative reporting program produced a documentary outlining some of the ways mortgage fraud is happening in Canada and in Ontario and Alberta in particular.[1] Since 2000, the Toronto Star newspaper has featured a number of articles discussing mortgage fraud in its weekly real estate legal column. In addition, many professional organizations whose members are involved in the mortgage

[1] CTV W5, *Stealing Home,* Aired March 21, 2005, Retrieved March 24, 2005 from, http://www.ctv.ca/servlet/ArticleNews/story/CTVNews/1111179528163_16/?hub=WFive

industry have articles and information regarding mortgage fraud on their websites to provide information to their members and the public.

So, what is mortgage fraud? Mortgage fraud is any scheme designed to obtain mortgage financing under false pretences. It can be a simple act of falsifying information in a loan application or more sophisticated schemes involving one or several parties with the intent of defrauding a financial institution and other innocent parties of money through a mortgage loan. For example, fraudster "F1" buys a rundown home for $150,000 and immediately sells it to an accomplice, fraudster "F2", on the same day or very soon after for a much higher price, say $200,000. Fraudster "F2" applies to a financial institution for a mortgage using the credit and financial information of an innocent party and obtains a mortgage for $180,000. The fraudsters pay for the house with the mortgage proceeds and may pay the mortgage for a couple of months at most. Subsequently, they default and steal the other $30,000 of mortgage proceeds. By the time the financial institution forecloses on the property, the fraudsters have disappeared and the lender is left with an outstanding mortgage that exceeds the true market value of the property.

Residential mortgage fraud is not a new type of fraud. However, it is a growing crime in both the United States and Canada. In the United States, mortgage fraud has been a concern for a number of years and has been growing since the early 1990's. The FBI has stated that mortgage fraud is "pervasive and growing".[2] In fact, the FBI has stated that if "mortgage fraud is allowed to become unrestrained, it will ultimately place financial

[2] Statement of Chris Sweeker, Assistant Director Criminal Investigative Division Federal Bureau of Investigation Before the House Financial Services Subcommittee on Housing and Community Opportunity, (October 7, 2004). Retrieved April 15, 2005 from, http://www.fbi.gov/congress/congress04/swecker100704.htm

institutions at risk and have an adverse effects on the stock market."[3] U.S. industry experts estimate that at least ten per cent of mortgage loan applications include some form of material misrepresentation although this is number is unsubstantiated.[45] The Law Society of Upper Canada (the "Law Society") has noted that in 1999 – 2000, losses from mortgage fraud in the U.S. ranged between US$5.0 billion and US$30 billion annually.[6] In these two years, mortgage loan originations totaled approximately US$2.35 trillion.[7] Because fraudulent loans usually go into default within months of funding the mortgage, it can be estimated that fraud losses represent anywhere from approximately one-half of one percent up to 2.5% of loans funded in the two-year period. These are significant losses.

In Canada, the Law Society currently is investigating 72 cases of mortgage fraud and in the spring of 2005, mortgage fraud was listed as a "Hot Topic" on the Law Society's web site.[8] The Canadian Institute of Mortgage Brokers and Lenders (CIMBL) estimated mortgage fraud to be $300 million in 2001, an increase of 400% over the 1999 estimate.[9]

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[3] Georgia Anti-Real Estate Fraud Bill Becomes Law, (2005, May 15) *Industry News,* Retrieved May 15, 2005 from http://www.alta.org/indynews/news.cfm?newsID=2771

[4] Easy Steps to Fraud Protection, ( 2005, January, Volume 3, Issue 1) *Quality Lending Review*, 3. Retrieved May 2, 2005 from, http://www.mortgagefraud.squarespace.com/the-prieston-group/

[5] Statement of Arthur J. Prieston, Chairman, The Prieston Group Before the Subcommittee of Financial Housing and Community Opportunity (October 7, 2004). Retrieved April 15, 2005 from, http://www.mortgagebankers.org/mbafightsfraud/mortgagefraud/images/files/Prieston%20Testimony.pdf

[6] The Law Society of Upper Canada (2004, March 24) *Report to Convocation*: *Mortgage Fraud,* 4. Retrieved May 15, 2005, from http://www.lsuc.on.ca/media/convmar05mortgagefraud.pdf

[7] *Freddie Mac Update* Presentation to Mortgage Bankers Association Conference May 2005, Retrieved May 2005 from, http://events.mortgagebankers.org/Secondary2005/Secondary/images/img/FMUPdate.ppt

[8] Ibid. *Report to Convocation: Mortgage Fraud* 14.

[9] Ibid. 5.

This is less than one-half of one percent of the $95.2 billion of mortgages loans funded in Canada in that year.[10] First Canadian Title, a Canadian company that insures title to property, has stated that in January 2004, the dollar value of fraud claims made to the company was 28% of the total of all such claims made since 1991, when the company entered the Canadian market.[11] Because of the increase in the number of mortgage frauds and the dollar values involved, Toronto Police Services has established a separate mortgage fraud investigation group.

Although there are many ways in which fraudsters steal mortgage money, the schemes often are relatively straightforward. What makes mortgage fraud unique and difficult to both detect and investigate, is that it frequently involves several individuals in collusion. Based on CIMBL's estimates of mortgage fraud in Canada, one may conclude that mortgage fraud is costing lenders and insurers millions of dollars annually. Accordingly, it is expected that a significant portion of the cost of these losses, if not the entire cost, eventually will be passed on to homeowners through higher loan fees, higher interest rates, and higher insurance premiums. Mortgage fraud can also target an innocent individual or small mortgage investor, resulting in significant financial costs. In some situations, the victim may incur significant costs in terms of personal time and legal fees

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[10] Canada Mortgage and Housing Corporation, *Canadian Housing Observer 2004* (n.d.) 63. Retrieved June 19, 2005, from https://www03.cmhc-schl.gc.ca/b2c/b2c/init.do?language=en&shop=Z01EN&areaID=0000000013&productID=00000000130000000006

[11] *First Canadian Title Identifies Profile of Real Estate Transactions Where Fraud is More Likely to Take Place*, News Release, (2004, February 2) First Canadian Title. Retrieved May 22, 2005 from; http://www.firstcanadiantitle.com/en/about/news_releases/Feb_2_2004.html

to rectify the fraud and is left to deal with the financial institution regarding the fraudulent loan.

From the statistics cited above, it seems likely that mortgage fraud in Canada is not of the same relative magnitude that it is in the U.S. According to the Law Society, "It is unknown how closely the Canadian experience mirrors the American situation."[12] However, the rate of increase in mortgage fraud in Canada in recent years and the dollar values involved are cause for significant concern. Therefore, as mortgage fraud has been a factor in the U.S. residential mortgage market since the early 1990's, and since U.S. organizations have taken steps to combat mortgage fraud, it is useful to review the situation in the U.S.

**DOCUMENTS REVIEWED AND RELIED ON**

As noted above, mortgage fraud has only recently become significant and therefore, information regarding mortgage fraud generally is quite recent. As such, most research materials used for this paper were obtained from information posted on web sites of organizations such as law firms, the Law Society, financial institutions, U.S. federal government departments and U.S. and Canadian government agencies, as well as websites of other organizations that are involved in real estate transactions and mortgage lending. In addition, Ontario court cases and judgments dealing with mortgage fraud were reviewed as well as one book on this topic.

[12] Supra. *Report to Convocation: Mortgage Fraud* 4.

A number of discussions regarding mortgage fraud were conducted with individuals connected to the mortgage industry and mortgage fraud investigations. However, certain individuals involved in the legal profession, law enforcement and mortgage lending wish to remain anonymous. Accordingly, their names and organizations have not been disclosed.

A detailed list of the sources, including several interviews with industry experts and documents relied on for this research paper is included at the end of this paper in the bibliography.

**SUMMARY OF FINDINGS AND CONCLUSIONS**

Mortgage fraud is a lucrative way for fraudsters to steal money. The risk versus reward profile favours the fraudster. This is due to the nature of the mortgage lending and real estate processes and the difficulties in investigating and prosecuting mortgage fraud. These factors have contributed to the increase in this form of crime in recent years.

In Ontario, the burden of proof required for a criminal conviction being 'beyond a reasonable doubt' works to the benefit of the fraudster as only cases with the strongest evidence may be prosecuted. The use of false identity and fictitious names adds to the difficulty in investigations.

The risk of sanctions against convicted fraudsters is not strong in Ontario. For example, the CTV program noted in the Introduction cited a case of one convicted mortgage fraudster who was sentenced to 30 days in jail to be served on the weekends. Another fraudster was convicted of 33 charges of fraud was sentenced to 38 months. Sanctions in the U.S. are stronger, in that the courts have ordered restitution and supervised release as well as jail time.

The real estate and mortgage lending activities involve a number of parties, any of which may collude to perpetrate a fraud. In addition, mortgage frauds often include a "mastermind" who directs the fraud and is not an industry insider. The variety of individuals that may partake in a mortgage fraud scheme, either knowingly or innocently renders these schemes difficult to detect, prevent and investigate. Generally, a lender will not know that a mortgage is fraudulent until the loan goes into default and the circumstances surrounding the default are determined. In addition, there are a number of other environmental factors that increase the risk of mortgage fraud. These include the land transfer system in Ontario, the impersonal nature of the mortgage lending process, the competitiveness of the industry, ease of access to credit information and technological advances that enable fraudsters to forge and counterfeit documents as well as enable lenders and mortgage insurers to automate certain functions in the loan approval process.

There are a number of broad categories that are useful to explain various types of mortgage fraud. However, a feature of many mortgage fraud scams is that more than one type of fraud may be involved in one overall scheme. This is similar to the experience in the U.S. and procedures to prevent and detect mortgage fraud must consider this.

When innocent homeowners are the victims of mortgage fraud, their property may be subject to mortgages for which they did not apply. If the lender obtained title insurance for the fraudulent loan or if the loan was insured against default, the lender would have recourse to those parties. However, in other situations, the homeowner may be legally responsible for the fraudulent mortgage.

Organizations in Ontario have adapted a number of individual initiatives to combat mortgage fraud. In addition, a working group consisting of industry, law enforcement and government representatives formed in 2004 to address the issue of mortgage fraud. Efforts to work co-operatively are imperative as mortgage fraud can only be stopped if all parties to real estate and mortgage transactions focus efforts on prevention and early detection. In not, fraudsters will target the part of the process with lax controls. These efforts must be ongoing as fraudsters continually devise new schemes.

Based on available information, Ontario appears to be incurring similar problems to the U.S. with respect to mortgage fraud, but perhaps, not to the same scale. Although the schemes in each country are tailored to the particular legal and business environments, the overall similarities in the schemes make it beneficial to review U.S. initiatives to combat this crime.

There may be a trade-off for lenders between improved lending practices that focus on detection of fraudulent loan applications and market pressures for fast approval. Published information indicates that lenders are concerned about mortgage fraud.[13] Accordingly, they need to be continually vigilant in the loan application review process,

[13] Canadian Bankers Association Fraud and Security, Retrieved June 2005, from http://www.cba.ca/en/viewdocument.asp?fl=3&sl=65&tl=136&docid=567&pg=1

and ensure their staff is adequately trained to recognize the red flags and risk factors of mortgage fraud.

As with all forms of fraud, the key to combating mortgage fraud lies with strong procedures that focus on prevention and early detection of potentially fraudulent transactions.

## DETAILED FINDINGS

### What is Mortgage Fraud?

As introduced above, mortgage fraud involves stealing all or a portion of mortgage proceeds. More rigorously, it can be defined as any material misstatement, misrepresentation or omission that is made with the intention that it will be relied on by a lender to underwrite, approve or fund a mortgage or by an insurer to insure a mortgage loan.

Mortgage fraud may be prosecuted under several sections of the criminal code, depending on the nature of the alleged crime. Section 362(1) of the Criminal Code deals with obtaining credit fraudulently and states:

> 362. (1) Every one commits an offence who
>
> > (a) by a false pretence, whether directly or through the medium of a contract obtained by a false pretence, obtains anything in respect of which the offence of theft may be committed or causes it to be delivered to another person;

(b) obtains credit by a false pretence or by fraud;

(c) knowingly makes or causes to be made, directly or indirectly, a false statement in writing with intent that it should be relied on, with respect to the financial condition,….. for the purpose of procuring…

(iii) the making of a loan,

(iv) the grant or extension of credit...

Sections 365 and 465 of the Criminal Code concern conspiracy while Sections 366 through 368 concern fraud and Section 403 concerns impersonation with the intent to 'gain an advantage'. Mortgage fraudsters may be charged under several sections of the Criminal Code, including sections not mentioned, depending on the nature of the alleged crime and evidence.

The Criminal Code clearly states that obtaining funds by providing false information or by fraud is a crime. As the burden of proof for a criminal conviction is high – beyond a reasonable doubt – a number of mortgage fraud cases have not been prosecuted as Crown prosecutors and police investigators focus their efforts on cases that appear to have the evidence that will provide the strongest case against the accused. The burden of proof requirements work to the benefit of the fraudster with the result that the risk of prosecution is far outweighed by the potential "profits" from mortgage fraud. Also, criminal courts traditionally focus on proving guilt rather than providing restitution to the victim. Victims also are not likely to be successful in suing the fraudster in civil court as often the fraudsters have no easily identifiable assets to claim.

**Why is Mortgage Fraud Committed?**

Fraud of any type can occur when there is an opportunity to commit fraud with little expectation of being detected. The acronym "GONE" stands for greed, opportunity, need and expectation of being caught is low, and it is helpful in understanding the motives for fraud and can be applied to mortgage fraud. It can be helpful in understanding the who, what, when, where, why and how of fraud.[14]

***Greed***

The main motive for fraud is usually economic – the fraudster seeks to acquire cash or goods and increase his or her economic well being. Mortgage fraud can be very lucrative for the perpetrators as in the example provided in the Introduction to this paper. Fraudsters can reap thousands of dollars from one successful scam.

***Opportunity***

"Fraud is a crime of opportunity – weaknesses in the system are exploited".[15] Mortgage fraud is no exception. There are a number of parties involved in real estate and mortgage transactions – real estate agents, lawyers, mortgage brokers, appraisers, lenders and borrowers. With so many parties involved in a mortgage transaction, fraudsters can exploit weaknesses in any part of the system to commit mortgage fraud. Additionally, with collusion of industry insiders, mortgage fraud can be very difficult to detect, with the result that fraudsters have creatively found many ways to commit mortgage fraud.

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[14]Zie, (1993) *The Expert Accountant in Civil Litigation,* 98. Retrieved September 2004, from Embanet.

[15] E. Susan Elliot and Good Hawkins, (2004 V3(2)) *Is There a Crook in the Firm?*- Law Society of Upper Canada Continuing Legal Education, October 2004 4-1.

### *Need*

Need centres on the desire or requirement for funds or some other benefit. Most fraud is perpetrated for economic gain; however, some frauds such as financial statement fraud often do not result in direct financial gain to the perpetrator. For example, favourable financial results may result in a stronger stock price, which may increase the value of the fraudster's stock options. However, mortgage fraud appears to be committed for direct and immediate economic gain – the fraudsters benefit directly by stealing mortgage funds or by securing a mortgage that the fraudster does not qualify for.

### *Expectation of getting caught is low*

The risk/reward tradeoff can be viewed as being favourable to the mortgage fraudster in Ontario. To date, there have been few convictions for mortgage fraud and for those who have been convicted, the penalties have been light. In one case cited by CTV, a fraudster "stole" the home of a dentist in the Greater Toronto Area. The fraudster was convicted in 1999 "...of the offence of attempting to defraud Dr. Dehmoubed and of uttering a forged document…"[16] He was sentenced to 30 days in jail, to be served on weekends.[17] More recently, E. Tesoro was convicted of defrauding two banks of $1.5 million in connection with fraudulent mortgages in Ontario.[18] He was convicted of 33 counts of real estate fraud and was sentenced to 38 months in prison, to be served concurrently.[19] Clearly, sentences of this nature are not strong deterrents to mortgage fraud. In addition, there

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[16] Durrani v. Augier, [2000] O.J. No. 2960 (Quicklaw) (S.C.J.) para 14.

[17] Supra. CTV W5.

[18] Bob Aaron, (2005, February 9) Stolen Dreams, *Toronto Star.* Retrieved June 5, 2005, from whttp://www.aaron.ca/home.htm

[19] Ibid.

may be a time gap between funding the mortgage loan and the loan going into default. By the time the financial institution realizes that the default is due to fraud, the perpetrator may have moved to another city.

## Mortgage Fraud in Ontario

### *Who is involved in a real estate transaction or mortgage loan?*

Real estate transfers and the mortgage lending process involve a number of parties, any of whom can be involved in mortgage fraud either wittingly or unwittingly. The functions of each party in the real estate or mortgage process are described briefly below.

Purchaser or Mortgagor – In most real estate and mortgage transactions, the purchaser or mortgagor seeks to acquire mortgage financing in order to enable him or her to purchase a residence. In certain mortgage fraud scams, the purchaser and the mortgagor or both can be fraudsters.

Vendor – the seller of the property that is subject to the real estate transaction. Vendors may or may not be a party to a mortgage fraud. If the vendor agrees to accept less funds than stipulated in the contracting documents, he or she may be assisting a fraud.

Real estate agent – a real estate agent generally is involved in residential property transfers. Real estate agents by contract act for either the buyer or the seller of the property in question, although in some instances and by agreement, the agent can act for both sides of the transaction. Real estate agents draft the agreement of purchase and sale based on standard wording and often assist buyers, particularly first-time buyers, in all aspects of home acquisition, including sourcing a lawyer or mortgage broker. If real estate agents are involved in a mortgage fraud, it usually concerns false value of the property.

Mortgage Brokers – Mortgage brokers may or may not be involved in obtaining mortgage financing. Their involvement is at the discretion of the borrower. Mortgage brokers source the mortgage financing for a borrower that best meets the needs of the borrower and in the process, sources mortgage loans for lenders. Mortgage brokers act for both the borrower and the lender. In addition to sourcing the borrower for the lender, the mortgage broker can assist the applicant in completing the loan application submitted to the lender as well as collect and review the various documents needed to support the loan application. Mortgage brokers are paid a fee or commission by the lender, therefore, there is incentive to process and close as many loans as possible. The unscrupulous mortgage broker may be tempted to ignore the signs of a suspicious transaction or even falsify information submitted in the application to the lender.

Appraiser – An appraiser assesses the market value of property. If a mortgage is sought on property that has not been transferred, the lender frequently will require an appraiser to value the property so that the loan is within the lender's loan to value guidelines. Appraisers provide a written report that includes information regarding the property such as the registered owner of the property, address and legal description, assessment, property taxes and age of the home. The appraisal report may also provide information as to the neighbourhood, such as services and schools in the area. Appraisals are estimates or opinions of value, and as such, are subjective in nature. Appraisers may be party to mortgage fraud by providing inflated opinions of value in their reports, which are relied on by lenders in their mortgage lending decisions.

Lenders and mortgage insurers also conduct appraisals electronically using computer models as they don't always visit the physical site of the property.

Lawyer – A lawyer is commonly involved in conveyancing in Ontario. Financial institutions generally require lawyers to act for them to search title, conduct off-title searches, prepare and register the Charge/Mortgage of Land document on title and disburse funds in accordance with the mortgage instructions. If the lawyer finds a problem with the title or any aspect of the transaction, he / she is required to advise the lender and to obtain instructions as to how to proceed. Once funds are disbursed, the signed documents and legal opinions are delivered to the lender. In many residential mortgage transactions, the lawyer engaged by the borrower will also act for the lender as this saves the borrower money. Real estate lawyers can be involved in mortgage fraud or used by fraudsters in a number of ways, as they are knowledgeable about the land registration system.

Credit Agency – Credit agencies provide financial and other pertinent information regarding individuals that is used by lenders and other organizations that grant credit, in their assessment of creditworthiness. While credit agencies are not directly involved in mortgage fraud, credit agencies compile and maintain sensitive financial and personal data, such as date of birth, social insurance number and credit history. If a fraudster gains access to an innocent party's credit history, this may assist them in perpetrating a number of crimes of which mortgage fraud is one. Credit information is critical to the mortgage approval process.

Lender – The lender is the party that provides funds so that borrowers can acquire a home, or provides funds to re-mortgage a home. Lenders require collateral for the loan, which is the mortgage against the property. Lenders usually obtain a title opinion from the lawyer acting on the loan in respect of title to the property being mortgaged or obtain title insurance as protection against any defects before advancing funds, so that they will be able to sell the property or recover their loan in the event of default and enforcement. In many mortgage scams, lenders are financial victims. However, in Ontario, depending on the nature of the mortgage scam, the lender may not incur a loss. In such cases, either a title insurer or the innocent homeowner bears the loss.

Generally, lenders base their credit decisions on the value of the property and the applicant's ability to repay the loan. For a conventional mortgage, the mortgage must be less than 75% of the value of the property. For a non-conventional mortgage, or high ratio mortgage, lenders require the loan to be insured against default. The two main mortgage insurers are Canada Mortgage and Housing Corporation (CMHC), which is a federal government agency, and Genworth Financial Canada, a subsidiary of General Electric Company.

Title Insurer – Title insurance insures the property owner against losses arising from a defect in title in the property until such time as the owner sells the property. In Ontario, title insurance serves two functions. The first function of title insurance is that it insures against defects to the property that are present at time of purchase. The second use of title insurance is that it insures title to the property. Thus, if the property is fraudulently transferred to another person, the title insurer will reimburse the insured for legal and other costs incurred in restoring proper title.

Employees of title insurers have been involved in perpetrating mortgage fraud in the U.S., because in many states, the title insurer acts as the closing agent and transfers title in the land register.

Credit Agencies - In Canada, credit reports are prepared by two companies, Equifax and TransUnion, both of which are subsidiaries of U.S. firms that provide the same services in the United States. Credit reports contain information regarding individuals that is used by financial institutions and other organizations that grant consumer credit, such as stores and gasoline companies. Employees of credit agencies or anyone who obtains access to credit information, such as with the recently reported breach in Equifax's computer security that compromised the credit information of over 600 Canadians, are able to steal identification information in order to perpetrated mortgage fraud.[20]

***The opportunity to commit mortgage fraud: weaknesses exploited***

One of the components of GONE principle is "opportunity" – the fraudster must perceive that there is an opportunity to commit fraud. In essence, fraud happens where there is a weakness or weaknesses in a process or system, which the fraudster exploits. There are a

[20] Simon Avery, (2005, June 18), Criminals Breach Equifax Security for Second Time, *The Globe and Mail* B3.

number of characteristics of mortgage lending transactions and real estate transfers that provide fraudsters with the opportunity to commit fraud. These are discussed below.

<u>Many Parties in a Real Estate and Mortgage Transaction</u> - As described above, there are many parties that may be involved in real estate and mortgage transactions – buyer, seller, lender, real estate agent, lawyer, mortgage broker, appraiser and title insurer. This environment where any number of parties can collude makes mortgage fraud very difficult to detect and to investigate.

<u>Impersonal Nature of the Mortgage Lending Process</u> - In the past, borrowers tended to secure mortgage loans from the local branch of their financial institution. The bank would be familiar with the borrower and the borrower's financial situation. However, today mortgages can be applied for and obtained over the phone and via the internet, as well as in person. Increasingly, loans are advanced without the lender meeting the borrower "face to face". In such cases, the lender relies on the lawyer to verify the identity of the borrower.

Much of the loan approval process is computerized, such as credit checks and online appraisals. While these tools speed up the approval process, they provide opportunity for fraudulent mortgages to go undetected. In the case of computerized appraisals, which are generally done by neighbourhood or postal code, if the submitted market value of the applicant's property is within the range for the postal code or neighbourhood, the mortgage will "pass" the test.

The use of computer tools in the mortgage lending process removes human judgment from the process, which can be exploited by fraudsters as they manipulate the mortgage applications so as to meet the computerized approval criteria.

Land Transfer System - Ontario is the first jurisdiction in the world to operate an electronic land registration system. The land transfer system provides information regarding the property, such as legal description, registered owner(s) and any encumbrances against the land. The electronic system is operated and maintained by a private company called Teranet Inc. (Teranet). While fraudulent property transfers occurred prior to the conversion to an electronic system, with access to the electronic system, a fraudster can discharge charges and transfer title with ease and "invisibly". All a fraudster requires to fraudulently change title records is an understanding of the conveyancing system in Ontario and a specially encrypted diskette and pass phrase, which are necessary to access the system. Real estate lawyers and their staff and financial institutions are the main users of Teranet and access is also available to those in the real estate industry such as real estate agents, appraisers and surveyors. That said, access is available to any individual who applies to Teranet, meets Teranet's security screening and pays the fee to access the system. Once approved, Teranet provides access to the system via a special encrypted diskette. The diskette contains a tracking feature that allows all transactions undertaken with the diskette to leave an electronic trail on Teranet's server. This is an improvement from the paper system, where anyone fraudulently transferring title was untraceable. While individuals wishing to obtain access to the Teranet system must have their identity validated, anyone with access to a diskette and pass phrase can transfer properties and register and de-register charges of land. Fraudsters can obtain access to the Teranet system either "validly" by applying to Teranet, or by using someone else's diskette and pass phrase. This system allows land transfers to occur without any face to face contact with the staff of the registry office, which is of benefit to fraudsters. Searches to determine ownership of properties and charges against properties can be done very quickly and in the fraudster's "home base".

Competitive Environment - The current residential mortgage industry is very competitive.[21] There are many lenders in the marketplace – "big 5" banks, internet banks, such as ING Direct and President's Choice Financial, mortgage companies, credit unions, trust companies, and individual lenders. Some institutions do not require the borrower to come into the branch to arrange a mortgage as many institutions accept mortgage applications over the phone and via the internet. With so many institutions chasing mortgage money, the market is very competitive, not only in terms of financial options available to the borrower, such as term, interest rate, open versus closed mortgage, but also in terms of approval time. However, quick approval turnaround lessens the time available to scrutinize loan applications for indicators of fraud.

Buoyant Residential Real Estate Market - The real estate market in Ontario has been very active for the past few years. The value of real estate transactions has been increasing with the result that the value of mortgage loans is increasing. This is evidenced by statistics from CMHC that show residential housing prices in Ontario increased by 25% over the four-year period 2000 – 2003 and price increases in Toronto were higher, at

[21] Shecter, (2005, June 2) Analysts Puzzle Over RBC Numbers – Explanations Insufficient, *National P*ost FP1.

36%. Total mortgage loans outstanding in Canada during that period increased by 21%, from \$429.5 billion to \$518.9 billion.[22]

<u>Access to Credit Information</u> - Credit reports provide valuable information to lenders to assist them in evaluating an applicant's credit worthiness. The information provided by credit reports is below.

- *Basic personal information* – name, address, date of birth, social insurance number
- *Financial information*:
    - *Credit cards* – a list of all credit cards issued to the individual and for each credit card, the date of issue, credit limit, payments history, current balance, past due balances
    - *Loans* – term of loan, date issued, due date, payment history
    - *Public records and other information* – bankruptcies, judgments, voluntary repayment programs and secured loans
    - *Collections* – list of any accounts that have been turned over to a collection agency
    - *Credit inquiries* - list of all organizations that have requested a credit report and the date of the request

Individuals can obtain their own credit reports either by submitting a request to the credit agency in writing or via the internet. Through either method, the party requesting credit information must provide proof of identity. In fact, to obtain a credit report online

[22] Supra. *Canadian Housing Observer 2004* 62.

through TransUnion, only the individual's name, date of birth, current address and valid credit card number are needed. The relative ease with which credit information can be obtained can provide the fraudster with access to sensitive personal credit information.

Technological Advances: Acceptance of Copied or Electronic Information and Speed of Loan Approval - Mortgage loan applications require personal and financial information to be provided so financial institutions can obtain information regarding the applicant necessary for lenders to assess the creditworthiness of the applicant. In addition, it has become standard practice in Ontario for lawyers to verify the identity of the parties signing documents in real estate and mortgage transactions. This practice was referred to in a 1996 court judgment, Yamada v. Mock.[23] In this case, a lawyer, Gerald Miller, acted for both the lender, Mock, and the borrowers, Yamada and her husband. Miller was held partly responsible for a fraudulent mortgage taken out by the husband and a woman impersonating Yamada. Because Miller had had prior business dealings with the husband and the imposter, he did not request identification from the imposter even though Yamada's signature on title was different from the signature in the loan documents. Two members of the Ontario bar provided evidence in this case, and both opined that lawyers should check the identity of clients. The judge determined "that the failure to ask for identification is below the standard of care of solicitors in this situation."[24]

[23] Yamada v. Mock, [1996] O.J. No. 2045 (Quicklaw) (Ontario Court (General Division))

[24] Ibid. 3.

Fraudsters can acquire the needed identification either by purchasing documents such as passports, driver's licences and social insurance numbers on the "black market" or by having such documents fabricated. With desktop publishing, scanners and colour printers, fraudsters are able to create fraudulent company letterhead, pay stubs, T4 slips, Canada Revenue Agency Notices of Assessment and other documents relied on by lenders to verify the borrower's ability to repay the loan as well as produce phony appraisals, which are relied on by lenders in re-financings. In a recent article on identity theft, lawyer Bob Aaron emphasized this fact. His dog "ordered a "novelty" (translation: counterfeit) Ontario driver's licence for himself."[25]

Technology has also resulted in decreasing the time lenders take to review and approve mortgages. Loan applications are available on web sites of financial institutions and mortgage brokers. Applications can be submitted online and financial institutions can perform information checks electronically. In order to speed up and standardize the approval process, financial institutions have developed formulas as guidelines in their credit decision. If the mortgage meets certain debt service and loan to value thresholds and credit scores, the mortgage application may be approved quickly. While these are not new features of the lending process, with emphasis on speed of loan approvals, the lenders may just consider the numerical indicators that are obtained electronically rather than review the detailed information behind the numbers. Fraudsters are aware of these numerical thresholds and therefore in some cases they may apply for a mortgage well within the thresholds, so that mortgages may be approved more readily.

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[25] Bob Aaron, (2005, June 4), It's Difficult to Detect Bogus ID, *Toronto Sta*r. Retrieved June 6, 2005 from, http://www.aaron.ca/home.htm

For high ratio mortgages, CMHC, the major mortgage insurer in Canada, does not independently appraise the value of the property. Rather, CMHC conducts electronic appraisals by postal code. If the applicant's home value is within the values in the neighbourhood, it will "pass" CMHC's property value review process.

***Ways in which mortgage fraud is perpetrated in Ontario***

There are two general motives for mortgage fraud, fraud for credit and fraud for profit, which includes identification fraud, theft of title and value fraud. With fraud for profit the motive is just that – the fraudster obtains mortgage financing and steals some or all of the funds. With credit fraud, the fraudster is an individual who wants to obtain financing for a property for which he or she would not qualify. Each of these is described in detail below.

Identification Mortgage Fraud - Identification fraud involves two general types of scam: mortgage fraud perpetrated by stealing an innocent person's identity and scams whereby the fraudster "borrows" the identity of a willing party.

> *Identity theft* - Identity theft is a major problem globally and is a dominant form of white-collar crime. It involves the theft of personal identification information such as social insurance number, date of birth, employment history, etc., which fraudsters use to commit other crimes such as credit card fraud and mortgage fraud. Some important identification such as driver's licenses and social insurance numbers are very easy to counterfeit or forge with current computer

technology.[26] With false documents, fraudsters are able to provide identification that looks valid when applying for a mortgage.

Mortgage fraud committed through theft of identity can occur in a number of ways. For example, fraudster "F" steals the personal and financial identification information of an innocent party "P" who has a good credit rating and is mortgage free. F counterfeits a driver's licence and social insurance card using P's information but substitutes the picture with that of himself or of an accomplice. With the forged and counterfeit identification and P's good credit history, F purchases property and obtains mortgage financing in P's name. The lawyer, according to standard practice in Ontario, checks F's identification, in which he is calling himself "P", and finds that it is in order and that P is registered as the owner of the property. Of course, F has instructed the lawyer acting in the transaction to direct the mortgage proceeds to himself, thus stealing the cash and then defaulting on the mortgage. As P is on record as the mortgagor, he is the first victim of the fraud. P will find out about the fraud when the mortgagee follows up on the overdue mortgage payments and eventually tracks down P. A fraud with similar facts was perpetrated against Jennifer Fiddian-Green, a Toronto-based CA•IFA. This fraud was highlighted in one of the segments of the CTV program on mortgage fraud referenced earlier in this paper. Although P is an innocent victim, P may be responsible for the fraudulent mortgage placed on his or her property, depending on the nature of the fraud and whether or not the

[26] A Page From CLE. Excerpt from a Presentation by B. Hengeveld, (April 6-7, 2005) Retrieved May 21, 2005 from, http://www.lsuc.on.ca/resources-for-lawyers/a/professional-development-resources/a-page-from-cle/april-2005/

lender insured the loan. In any case, P will have to prove that he or she is an innocent victim of the fraud. In addition, once P is proven innocent, it may take him or her months to get his or her credit history corrected by the credit agencies, which in the meantime can hamper P from acquiring credit that P legitimately needs.

False identity was also used in an Ontario case tried in 2003, Chornley v. Chornley.[27] In this case, the defendant husband obtained a mortgage against the matrimonial home without his wife's knowledge by arranging for an imposter posing as his wife to accompany him to the bank to obtain a mortgage. The imposter had the wife's pay documents, which the bank confirmed with the employer.

Theft of the identity of practicing lawyers has also occurred in Ontario. With theft of a lawyer's identity, fraudsters are able to transfer property and register and de-register encumbrances to land. In these frauds, the fraudsters arrange mortgage financing and use the false lawyer to close the transaction, thus misappropriating the mortgage proceeds.[28]

Mortgage fraud committed using false identity currently is a common form of fraud, and in a number of recent cases, it has accompanied value fraud and title fraud.

[27] Chornley v. Chornley, [2003] O.J. No. 3438 (Quicklaw) (S.C.J.)

[28] Personal communication, June 13, 2005.

*Straw buyers* – Straw buyers are phony buyers and are used in a variety of ways to perpetrate mortgage fraud. They are used by fraudsters to purchase property and obtain a mortgage to conceal the fraudster's identity. In this way, the fraudster "borrows" the credit history and personal identification of the straw buyer. The straw buyer generally is paid a fee for loaning his or her identity for the home purchase and mortgage and often does not realize that his or her credit information is being used to perpetrate a fraud. The fraudster instructs that the mortgage proceeds be directed to him or her with the "promise" that the fraudster will buy the property from the straw borrower. However, the fraudster does not honour the commitment and the straw buyer ultimately defaults on the property.

A fraud involving a straw buyer could operate as follows. The fraudster buys a property that is the lowest value for the neighbourhood, for example $150,000. He or she will make cosmetic changes to the house but claim that the house has been renovated and then list the house for sale. The fraudster will recruit a straw buyer to purchase the house for a much higher value, say $300,000. The fraudster pays the straw buyer several thousand dollars for completing this transaction. The fraudster will provide the lender with phony employment letter and income documents for the straw buyer, a phony agreement of purchase and sale and will work with a less than reputable mortgage broker to obtain mortgage financing. So that no appraisal is done on the property, the fraudster will have the straw buyer apply for a conventional mortgage of $195,000, which is within the lender's loan to value thresholds. The fraudster then uses the mortgage proceeds to pay for the original home price of $150,000 and then steals the excess of $45,000 less expenses such as land transfer tax, the fee to the straw buyer and perhaps several months of mortgage payments. Alternately, the fraudster and mortgage broker may direct the straw buyer to apply for a high ratio mortgage that will be insured by CMHC. As noted above, CMHC does not conduct physical appraisals, only electronic appraisals by postal code. As long as the value of the property stated in the loan application is within the range in the postal code, the loan will "pass" the value checks. Under either scenario, the fraudster and straw buyer often use different lawyers in the transaction, so if a reputable lawyer is used, the transaction will appear to be bona fide. Eventually the fraudster stops paying mortgage payments and the property goes into default. The straw buyer, whose identification was used to acquire the mortgage, is left with a mortgage that they cannot service. In such case, the straw buyers usually are of low economic means and not familiar with real estate and mortgage transactions and are duped by the fraudster.

<u>Theft of Title</u> - Although there are no statistics concerning the volume and types of mortgage fraud in Ontario, mortgage fraud committed by theft of title is prevalent. Fraudsters that are familiar with the system of conveyancing in Ontario have been able to "steal" the title to property. The frauds involve two general methods. With one scam, the fraudster registers a fraudulent charge against an innocent party's property and then forecloses on the fraudulent charge and becomes the registered owner. The fraudster profits by selling the property or mortgaging it. A mortgage fraud case that went to court

in 2000 involved this type of scheme.[29] With the second scheme, the fraudster transfers title to an innocent person's property into his or her own name or that of an accomplice or even a fictitious person and discharges any liens against an innocent party's property. Under both scams, the fraudster acquires registered title to the property. With registration as the owner on title, the fraudster can then mortgage the property. There are several title theft mortgage fraud cases in Ontario that have gone to court. The main cases are summarized later in this paper together with the legal decisions of such frauds to the innocent property owner or mortgagee.

Several aspects of the mortgage lending and title registration systems in Ontario provide fraudsters with the ability to commit mortgage fraud through forms of title theft. As noted earlier, anyone with knowledge of and access to the conveyancing system in the province and criminal intent can commit title theft. Although title theft occurred with the paper system, the electronic land registration system provides an invisible and fast way to search title, transfer title and register and discharge charges of land. Although the Teranet system provides security features to guard against inappropriate use, the knowledgeable fraudster will be able to overcome these. While the system tracks which diskette performed each transaction, it is not designed to prevent the fraud in the first place. Often the victim homeowner will not find that title to their home has been changed until the lender contacts them regarding non-payment of a mortgage that they are not aware of.

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[29] Supra. Durrani v. Augier.

Value Fraud - Value fraud includes a number of frauds that result in the market value of the property being falsely inflated. Lenders can incur substantial losses through value fraud as the mortgages granted usually exceed the property's true market value.

*False Purchase Price* – There are several ways in which fraudsters have inflated purchase prices. One way is to falsify the agreement of purchase and sale or other document that is provided to the lender to support the mortgage value requested by the applicant. This is as straightforward as changing the purchase price of the property. A 1991 discipline case before the Law Society of Upper Canada dealt with this issue. [30] The lawyer under review was found "to have breached her duty to her client Home Savings & Loan Corporation by allowing it to advance $205,000 to Tom Reid on a first mortgage…on the basis of its belief that the consideration for the purchase was $290,000 as stated in an agreement of purchase and sale...when she knew that the consideration was in fact only $215,000."[31]

The second way in which purchase prices are inflated is a bit more involved, but still quite easy to do. The purchaser, who is the fraudster, agrees to pay a price, for example $250,000, for the property on the proviso that the vendor rebates a portion of the purchase price on closing under a second agreement, which is effected at the same time as the closing. The second agreement provides for a rebate of $50,000 from the selling price of $250,000. Thus, the actual price of the property deal is $200,000. The fraudster then applies for a mortgage of $235,000

[30] Law Society of Upper Canada v. Gower [1992] L.S.D.D. No 34

[31] Ibid. 2.

using the agreement of purchase and sale, which has an inflated purchase price of $250,000. Eventually the fraudster defaults on the mortgage and the lender is left with a mortgage that often exceeds the true value of the property, in this case, by $35,000.

*Property flips* – Property flips or "Oklahoma Flips" involve purchasing a property and then re-selling the property within a relatively short period of time at a higher price. What differentiates a flip scheme from a bona fide real estate purchase and sale is that flip schemes result in overvalued properties. Property flips can involve either a bona fide seller or a fictitious seller of property and a fraudulent purchaser who resells the property within a very short period of time for an inflated value. In some cases, the property will be purchased and sold several times through related parties, each with a higher purchase price based on fraudulent appraisals. Alternately, the fraudster may use a straw borrower to buy the property. The purpose of a flip scheme is to artificially inflate the value of property and then obtain a mortgage based on the inflated property value. Another form of property flip does not involve mortgage fraud, but is very similar. Fraudsters artificially inflate the value of property through flips and then sell the property to an innocent third party, who has overpaid for the property. The fraudster benefits with an ultimate sale to a third party by the difference between the ultimate sale proceeds and the original purchase price.

There have been several recent cases involving property flips where the lawyer involved in the real estate and mortgage transactions were subject to discipline hearings of the Law Society. In one 2003 hearing, V. Poonai was charged with being involved in 23 real estate flips in the Toronto area between 1997 and 2003 and in each of the 23 property transactions investigated, the Law Society found that the property involved had been purchased and resold within a very short period of time.[32] In each case, the higher sales price was presented to the lending institution as the purchase price for the purpose of obtaining mortgage financing.[33] In most cases, the purchaser defaulted on the mortgages with the result that the lenders were left with mortgages in excess of the property value. In one instance, "…a property on Ashley St. was sold for $80,000 and again for $288,000 on the same day. Another property on Clyde St. was sold for $115,000 and flipped for $493,000…" on the same day.[34] In total, the frauds reaped $5.6 million in profits.[35] Poonai was charged under Criminal Code sections 380(1)(a), defrauding the public, and 465(1)(c), conspiracy to defraud the public, in connection with his involvement in these transactions.[36]

Value fraud exploits the impersonal nature of the current lending environment and the fact that there are a number of parties involved in mortgage and purchase and sale transactions. If several individuals are involved in a scam, it is more

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[32] Bob Aaron, (2003, October 4) Property 'Flips' Land Lawyer in Hot Water, *Toronto Star,* Retrieved June 4, 2005 from, http://www.aaron.ca

[33] Ibid.

[34] Ibid.

[35] Ibid. .

[36] Law Society of Upper Canada. Discipline Decisions, (n.d.) Retrieved June 4, 2005 from, http://www.lsuc.on.ca/regulation/a/discipline/m/

difficult to investigate the case. Fraudsters ensure that the values of the flipped properties are not in excess of other properties in the neighbourhood so that the property value is not flagged by the automated value checks used by lenders and CMHC. In the example above, property values in the same postal code as the Ashley St. property may have ranged in value from $75,000 - $300,000. The flipped property value was $288,000, which was at the high end of values for that particular area, but still within the acceptable range for the neighbourhood. So, the application would “pass” the electronic value check. In such cases, a “drive by” appraisal might well have uncovered the fraudulent property value in the loan application.

Value fraud involving property flips has been cited by the Real Estate Council of Ontario as a potential contributor to the increase in value of real estate recently. [37] In a buoyant and escalating real estate market such as has existed in Toronto over the past few years, value fraud may be difficult to detect as real estate values are increasing rapidly. However, with any form of value fraud, if the mortgagor is unable to service the mortgage, the lender is left with a mortgage in default. In a buoyant real estate market, and depending on the loan to value ratio of the mortgage, the lender may not incur a loss as a result of the value fraud. However, in the case of high ratio mortgages or in a declining real estate market, the loan value could exceed the market value of the property, thus resulting in a loss to the lender.

[37] *Mortgage Fraud: Targeting a Growing Epidemic*. (n.d.) Retrieved May 22, 2005 from, http://www.reco.on.ca/site.asp?WCE=C=47|K=2235709

Credit Fraud - Credit fraud is perpetrated by the borrower. The borrower knowingly provides false information in the mortgage application, which is used by the lender in the credit assessment. Information that could be falsified includes source of down payment, place of employment, and personal and financial information such as annual income, net worth, social insurance number, driver's licence, citizenship cards and passports. The intent of individuals to commit credit fraud is to obtain a mortgage that is larger than their financial situation would justify. Generally, these individuals would not qualify for a mortgage due to poor credit risk or inability to service the debt. In cases of credit fraud, the borrower usually intends to repay the mortgage.

In one case cited by an anonymous lender, the borrower filed for bankruptcy shortly after the loan was funded. In working with the trustee in bankruptcy, it became apparent that the information provided in the loan application regarding the borrower's assets and liabilities did not agree with the amounts filed in the bankruptcy statement. The investigation into the case found that the mortgage broker had filled out the financial information in the loan application and the borrower had not verified the information before signing.

As in this situation, in cases of credit fraud, due to the borrower's actual financial situation, there is a risk that the borrower will default. Accordingly, credit fraud presents an unknown risk to the lender.

***Who are the victims of mortgage fraud?***

It is expected that the cost of mortgage fraud eventually will be passed on to consumers through higher interest rates or loan origination fees or higher mortgage insurance premiums or any combination thereof. In cases of title theft that are compensable through Ontario's Land Titles Assurance Fund, it is taxpayers that bear the cost.

However, it is useful to review the possible victims of mortgage fraud at a finer level. Due to the multitude of ways in which mortgage fraud can be perpetrated, there are several possible victims of mortgage fraud. In frauds where the fraud is committed using false identification, the lender, mortgage insurer and person whose identity was stolen can all be victims. The individual whose identity is stolen is a victim in a number of ways. First, the individual may be registered on title as the mortgagor and until they are successful in getting the land register changed, they could have difficulty securing a valid mortgage. Secondly, the individual's credit rating will show the number of credit checks obtained by lenders, thus ruining his or her credit rating. It can take months before the individual's credit history is corrected by the credit rating agencies.

In cases of value fraud, the lender usually is the victim, as the lender can be left with a mortgage that exceeds the true value of the property. In addition, the lender bears the cost of enforcement of its security. With flips that involve a sale to an innocent third party, the innocent buyer is also a victim, as he or she has purchased a property that is overvalued.

With credit fraud, there may not be a victim. If the mortgagor is able to pay the monthly mortgage payments, there is no loss to the lender.

With frauds on title that are committed in order to obtain a fraudulent mortgage, victims include lenders and in some situations, innocent homeowners as well as innocent persons whose identity may have been stolen.

***Laws governing real property transactions in Ontario***

In Ontario, the Registry Act and the Land Titles Act govern land registration in Ontario and all property in the province falls under one of the two acts. Ontario has been moving properties from the registry system into the land titles system over the past few years. Currently, the majority of titles in Ontario are under the Land Titles Act.

<u>Registry Act</u> - The government provides a registry office where individuals can register their interests in land. The government does not guarantee the accuracy of the information contained in the registry office. Therefore, when property is being purchased, a search of the documents that have been registered in respect of the property is necessary to determine whether the vendor has good title to the property and to determine whether there are any liens on the property. If there was a fraud on title in the past, the current owner could be deprived of his interest in land if the fraud was discovered and proved. In Ontario, the chain of ownership to a registered property generally is searched for 40 years prior to the current transaction. In addition, at common law, if a fraudulent or forged document is registered in the registry office, it will be rendered void once the fraud or forgery has been uncovered and proven.

Land Titles Act - The Land Titles Act is effectively a modified Torrens system for registering titles as opposed to interests. The Torrens system was developed in Australia in the 1800's in response to the disarray in the registry system. Under a Torrens land registration system, title to land and the encumbrances affecting that particular title are recorded in a government register. Generally speaking, any interests in land that are not registered on the title to the property (or listed in Section 44 of the Land Titles Act) are void against third parties without notice of the interest and who are relying on the register. The province guarantees that the register is accurate with respect to registered ownership of property and registered charges against the property.

A Torrens system and The Land Titles Act in Ontario are said to operate under the following three principles, the Mirror Principle, the Curtain Principle and the Insurance Principle. These principles are not stated in the Land Titles Act. Rather they have been developed by practitioners to explain how a Torrens system and the Ontario Land Titles Act operate.

*Mirror Principle* - The Mirror Principle provides that the land registration system accurately reflects the true ownership of land and charges against land. In this way, the land titles system "mirrors" the true state of the title.

*Curtain Principle* - The Curtain Principle provides that anyone searching title does not have to have any regard for prior registered owners of the property.

*Insurance Principle* - Because the government guarantees the accuracy of title and interests in property, the government provides a fund to compensate those

> who have been deprived of their interest in land due to errors in the registration system. In Ontario, the Land Titles Assurance Fund will compensate a person that is wrongfully deprived of his or her interest in land due to an error in the land titles register. The Fund is a fund of last resort. Individuals must first try to recover their loss from the party who is responsible for the error and prove that there was an error on title.

"These principles form the doctrine of indefeasibility of title and is the essence of the land titles system…"[38] The doctrine of indefeasibility of title holds that the person registered on title has a valid title to the land even if the title was acquired fraudulently. The argument is that the fraud happened prior to the registration on title.[39] While the province guarantees title to property, it does so only to bona fide registrants. It does not guarantee title that has been obtained fraudulently. Rather, if there has been a fraud on title, the courts will correct the register. Anyone who relied on the "error" in title however, may apply for compensation for the loss incurred as a result of his or her reliance on the incorrect title from the Land Titles Assurance Fund. This forms the principle of "deferred indefeasibility" as how decisions rendered by the Director of Titles of the land registration system has interpreted the Act in cases of claims for compensation from the Fund.

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[38] Supra. Durrani v Augier at para 42a.

[39] Brian Bucknall. *Fraud & Forgery Under the Land Titles Ac* (n.d.). Retrieved April 2005 from, www.firstcdntitle.com.au/Brian-Bucknall-Fraud-and-Forg-s.pdf.

***How fraudsters have exploited the land titles system to perpetrate mortgage fraud***

Typically, when a person wants to purchase a property, his or her lawyer will check to ensure that the vendor has title to the property. The purchaser will also want to know if there are any outstanding encumbrances on the property. Generally speaking, under the land titles system, the lawyer only needs to check the title and encumbrances registered on the title and address the exceptions as set out in Section 44 of the Land Titles Act and off-title searches as the government ensures that the land titles register is correct.

Anyone that has knowledge of conveyancing in Ontario can change records registered under both under both the Land Titles Act and the Registry Act. Fraudsters have exploited both systems by fraudulently discharging existing charges of land and transferring title. Where the land is in a county designated for electronic registration, the fraudster must have access to an activated Teranet diskette and pass phrase, which as noted above, is not restricted to real estate lawyers or others involved in real estate and mortgage transactions. Thus, a property could be subject to two mortgages, one legitimate and one fraudulently registered. Also, the true owner of the property can lose his or her registered interest in land.

With theft of title, there are two possible victims, the true owner of the property and the financial institution that provided mortgage financing on the fraudulently registered property. A key provision the Land Titles Act is that only the person registered under the Act as the owner of property can transfer or encumber land. This feature of the Act has resulted in innocent parties to mortgage transactions incurring a loss due to fraud.

However, the Act provides that in cases where a landowner has been deprived of his or her interest in land due to an error in title in the land register, the province provides a fund to compensate such victims. This is the insurance principle underlying the Act. A review of case law provides guidance as to how the courts have treated frauds on title.

<u>Risman - Application for Compensation from the Land Titles Assurance Fund</u>[40] - In this case, in 1995, the applicant, Lorrie Risman, invested in a second mortgage in property owned by James Gilbert. However, unbeknownst to Risman and Risman's lawyer, they were really dealing with Ted Danek, who was posing as Gilbert. Risman's lawyer advanced the funds to Danek's lawyer and the mortgage was registered on title. Danek defaulted on the mortgage on Gilbert's property. Subsequently, Danek pleaded guilty to defrauding Gilbert and Risman. However, Risman was unable to recover her loss from Danek and applied to the Land Titles Assurance Fund for compensation. The Director of Titles found that Risman's loss, while unfortunate, was not compensable by the Fund as Risman did not deal with the registered owner of the property. Rather, Risman dealt with an imposter and the Act specifies that only registered owners can deal with land.

<u>Durrani v. Augier</u>[41] - This case was tried in 2000 and the court's decision has been relied on in subsequent cases concerning the same issue. In 1995, the defendant Augier forged a loan agreement for US$158,000 collateralized by the Durranis home in Scarborough

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[40] Bob Aaron, (2002, March 9) Title fraud Costs Taxpayers, *Toronto Star* Retrieved June 4, 2005 from, http://www.aaron.ca

[41] Supra. Durrani v. Augier.

Ontario. Augier then arranged for the forged loan agreement to be registered under the Land Titles Act. A few months later, Augier commenced an action for foreclosure and obtained a default judgment whereby he obtained ownership of the property and registered it against title in the Land Titles Office. The Durranis learned of the fraudulent loan agreement and their lawyer notified Augier's lawyer that the Durranis were trying to have the default foreclosure set aside and that no steps should be taken to sell the property. In spite of this notice, Augier listed the house with a real estate agent who subsequently sold the house to her two teen-aged daughters. The agent paid a deposit on the property and secured a mortgage from Royal Bank of Canada for the balance of the purchase price. Royal Bank registered the mortgage against the house, which then showed the real estate agent's daughters as owners.

The court determined that the document Augier registered was fraudulent and therefore, Augier did not obtain a valid interest in the Durranis home. The judge further determined that the real estate agent's daughters also did not acquire a valid interest in the property. The real estate agent was aware that Augier's claim of ownership was not legitimate and therefore should not have closed the sale. The judge ordered title of the property to be rectified to show the Durranis as the registered owners. The last party with an interest in the Durranis' property was Royal Bank. The judge did not find any evidence that Royal Bank was aware that the daughters did not hold valid title to the property. Accordingly, the judge determined that Royal Bank held a valid charge against the Durranis' home.

The judge stated:

> "Through the doctrine of deferred indefeasibility, the land titles registration system reflects a policy choice to protect the security of title of those who are innocent parties who rely on title."[42]

The judge noted that there was a "conundrum" with this outcome. The Durranis had owned their home and were mortgage free. Therefore, it should not be encumbered with a mortgage that they did not apply for. The Royal Bank however, was an innocent party as well, as it funded a mortgage based on the understanding, based on the land titles register, that the agent's daughters had a valid title to the property. Under the Land Titles Act, only the registered owner can transfer or encumber land.

The doctrine of deferred indefeasibility holds that an innocent person who relies on title as recorded in the land titles register will have a valid interest in land even if the register is incorrect. Thus, in Durrani v Augier, Royal Bank relied on the land titles register, which showed the daughters as the registered owners and funded a mortgage on that understanding.

This was a situation in which the "insurance principle" of the Land Titles Act was applicable. While the judge ruled that the bank had a valid mortgage against the Durranis' home, he stated that the Durranis could apply to the Land Titles Assurance Fund for compensation for the mortgage in favour of Royal Bank.

[42] Supra. Durrani v Augier at para 78.

TD Bank v. Jiang[43] - The doctrine of deferred indefeasibility was discussed and relied on in a case heard in 2003, Toronto-Dominion Bank v Jiang. In this case, the defendant Jiang fraudulently transferred title to the home of the true owners, the Shins, to himself and then obtained a $200,000 mortgage from Toronto-Dominion Bank. The judge ordered that title to the property be corrected to show the Shins as owners. The judge also found that the Toronto-Dominion Bank had a valid mortgage as it relied on the register, which showed Jiang as owner. In this situation, the Shins also had a valid claim against the Land Titles Assurance Fund.

CIBC Mortgages v Chan[44] - A more recent case, CIBC Mortgages v. Chan, which was tried in 2004, concerned a fraudulent power of attorney that was registered on title and relied upon by two lenders, CIBC Mortgages Inc. and Household Realty Corporation Limited. In this case, S. Chan forged her husband's signature on a power of attorney that granted her authority to sell or mortgage the home she owned jointly with her husband, L. Liu. She had the fraudulent power of attorney registered on title. Her husband lived in Hong Kong and was unaware of the forged power of attorney and that Chan had obtained two mortgages on their home. In their credit reviews, the financial institutions relied on the power of attorney that Chan provided as they had no reason to believe it was fraudulent.

The position of Liu, the defendant husband, was that since the power of attorney was forged, it could not be relied on by the lenders. Title to the property had not been

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[43] Toronto-Dominion Bank v. Jiang, [2003] O.J. No. 995 (Quicklaw) (S.C.J.)

[44] CIBC Mortgages Inc. v. Chan, 20 R.P.R. (4th) at p. 151 (S.C.J.)

changed and it was correct as it showed both husband and wife as owners. He argued that the power of attorney, even though it was registered on title, it was not a document that could transfer or encumber land. Therefore, since the power of attorney used to obtain the mortgages was a forgery, the lenders did not obtain an indefeasible interest in the property and therefore, the mortgages should be void. The court determined that the financial institutions met the standard of care in relying on the power of attorney as they were not aware it was a forgery and enforced the mortgages.

In the Ontario Real Property Reports, Sidney Troister, a prominent Ontario real estate lawyer, has argued that the CIBC Mortgages v. Chan decision in reality applied the theory of immediate indefeasibility rather than deferred indefeasibility.[45] In this case, the court determined that the financial institution held a valid mortgage against Chan's property even though title had not been fraudulently transferred. The appeal of this case was heard on May 30, 2005 and judgment has been reserved. The basis of the appeal was that the mortgages were unenforceable as they were signed pursuant to a fraudulent power of attorney. Both sides presented arguments to the court based on the Durrani case.[46] As of June 16, 2005, the Court or Appeal has not rendered its decision. The decision will be important for the mortgage industry in terms of whether the appeal will reaffirm the validity of the mortgages or will apply the principle of deferred indefeasibility, which would result in the mortgages not being enforceable.

[45] Supra. CIBC Mortgages Inc. v. Chan.

[46] personal email from legal source received June 16, 2005.

In frauds on title, the Fund will only compensate victims for a very narrow form of loss due to fraudulent title, specifically, if there was an error in the title register and that someone relied on that "error" and suffered a loss as a result of the error. This is the principle of 'deferred indefeasibility' of the Act. If the loss cannot be proved to be attributable to the error, the Fund will not compensate victims.[47] Similarly, if the fraudster registered title in the name of an imposter or a fictitious person or a cohort, the Fund will not compensate the victim. The Land Titles Act specifies that only the registered owner can charge land, and therefore, only in cases where the lender or other victim suffered a loss as a result of reliance on the "error" in title, will the Fund compensate victims. Clearly, from the cases discussed above, The Land Titles Assurance Fund applies to a very narrow class of persons who are innocent victims of mortgage fraud.

***Detection of mortgage fraud***

Detection of mortgage fraud is extremely difficult between the time the loan is funded and the time the loan goes into default, particularly because in many cases, the time between funding and default is short. In cases where a straw buyer is used, the straw buyer often is reluctant to disclose the fraud, even if they become a victim, due to their involvement. Efforts to detect suspicious and fraudulent transaction therefore must be concentrated prior to funding the loan. Because fraudsters will target the "weak link" in the process, detection of suspicious and fraudulent transaction requires the diligence of

[47] Kerr v. Ontario (Land Titles Assurance Fund), [2001] O.J. No. 1215 (Quicklaw) (S.C.J.)

all of the parties to such transactions. Detection tools therefore overlap with prevention tools and are discussed in the conclusion to the paper.

### ***Red flags and risk factors of mortgage fraud***

A red flag is a warning signal. Fraud investigators look for the presence of red flags as these may indicate suspicious or fraudulent activity. Red flags in isolation are not necessarily indicators of fraud. However, if several red flags are present in the same activity or series of activities or there is a pattern of activity or parties to transactions, further investigation or consideration is warranted. Risk factors concern environmental factors that increase the probability of fraud. Understanding the red flags and risk factors of real estate and mortgage loan transactions is necessary in order to manage the risk of fraud and detect fraudulent transactions before the loan is funded. Industry experts have identified a number of red flags and risk factors associated with fraudulent real estate and mortgage transactions. A sample of these is provided in Appendix II together with follow up practices.

### ***Measures adopted in Ontario to combat mortgage fraud***

There have been a number of initiatives in Ontario to increase awareness by the industry and the public regarding mortgage fraud. These are explained below.

<u>The Law Society of Upper Canada</u> - The Law Society has been very proactive in heightening awareness of mortgage fraud. While the focus is on their members, in providing both information and training to lawyers regarding mortgage fraud scams and the indicators of mortgage fraud and how to avoid it, it has also been active in

investigating complaints against lawyers concerning mortgage fraud. As noted above, the Law Society is conducting 72 investigations into lawyers' conduct in connection with alleged mortgage fraud. In order to focus on this effort, a special team has been established within the investigations group to concentrate on investigating potential mortgage fraud.[48]

CIMBL – CIMBL has been proactive in educating members and the public about mortgage fraud. In addition, CIMBL has implemented an accreditation for mortgage brokers, the Accredited Mortgage Professional or "AMP" designation. Among the required courses for this certification is an ethics course. Recently, CIMBL has placed advertisements in the media to encourage consumers to work only with an accredited mortgage professional. In addition, in April 2005 CIMBL issued a document entitled "Origination Standards for Fraud Avoidance", which is available on the CIMBL web site.[49]

The Real Estate Council of Ontario (RECO) - RECO provides information to members through education initiatives. RECO's web site also includes information for real estate agents and consumers regarding mortgage fraud. In addition, similar to other professional organizations, RECO can revoke the real estate licence of agents found to have knowingly participated in mortgage fraud.[50]

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[48] Supra *Report to Convocation: Mortgage Fraud* 15.

[49] CIMBL, *Origination Standards for Fraud Avoidance*, (2005, April). Retrieved May 21, 2005 from, http://www.cimbl.ca/download_docs/Origination_Standards_April2005.pdf

[50] RECO website http://www.reco.on.ca

Law Enforcement Units - Law enforcement units are actively investigating mortgage fraud.  Recently the Toronto Police Services established a dedicated mortgage fraud team.  This will be a beneficial move as these individuals will become experts in this form of crime and therefore, better able to investigate cases.

Multi-Disciplinary Group Formed - In 2004, a group of organizations involved in real estate and mortgage transactions, including law enforcement bodies, government agencies, lawyers and private industry formed to focus on various aspects of mortgage fraud and its impact.  The group is considering a number of issues, including reporting mortgage fraud, sharing of information and education of industry participants.

Provincial Government Ministry of Consumer and Business Affairs – This ministry administers the land titles system.  The Land Titles office will register a "No Dealings Indicator" in the land titles register if an individual alleges that they have been a victim of mortgage fraud.  And, as noted above, the individual may qualify for compensation for losses incurred from the Land Titles Assurance Fund.[51]

Teranet- Teranet has a module available that provides information regarding "disciplinary enforcement and certain legal actions taken by regulators..."[52] that subscribers can access to check on individuals and companies with whom they may do business.

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[51] Supra. *Report to Convocation: Mortgage Fraud* 18.

[52] Ibid. 18.

Media - The media has been helpful in bringing the issue of mortgage fraud to the general public. This is an important initiative as it has brought widespread awareness of this issue to Canadians, particularly through the format of the investigative report produced by CTV.

**Mortgage Fraud in the United States**

Mortgage fraud in the United States has been a significant and growing problem for a number of years, whereas in Canada, mortgage fraud has only become a significant problem in the past couple of years. Thus, it is instructive to review the U.S. situation and particularly the measures that are being taken to combat mortgage fraud and to consider whether these measures would be of benefit in Canada, and in Ontario in particular.

***Current mortgage fraud situation and mortgage lending environment***

In May 2005, the FBI stated that it had 642 mortgage fraud investigations in progress, compared with 436 cases in 2003 and 102 cases in 2001.[53][54] Although there is no system for compiling mortgage fraud statistics in the U.S., as noted in the Introduction, the industry generally accepts that approximately ten per cent of mortgage loan applications are fraudulent.[55] As a result of the devastating effect mortgage fraud has had in the U.S.,

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[53] Issue Paper *Mortgage Fraud Perpetrated Against Residential Lenders,* The Mortgage Bankers Association May 2005. Retrieved June 18, 2005 from, http://www.mortgagebankers.org/library/isp/2005_5/Mortgage%20Fraud%20Perpetrated%20Against%20Residential%20Lenders.pdf

[54] Derus (2005, April 15), Fraudulent Mortgage Cases are Mounting, *The Milwaukee Journal Sentinel*. Retrieved May 30, 2005 from, http://www.sunherald.com/mld/sunherald/business/11398761.htm.

[55] Supra. Easy Steps to Fraud Protection.

in 2000 a U.S. Senate subcommittee held two days of hearings into flipping schemes in order to understand the schemes and determine measures Congress and the U.S. Department of Housing and Urban Development (HUD) could take to prevent these frauds.[56] In October 2004, a subcommittee of Congress held hearings entitled, "Fraud in Our Nation's Mortgage Industry." Industry leaders, government officials and the FBI testified at these hearings. In these hearings, speakers discussed the nature of mortgage fraud in the U.S. and its impact to lenders and the lending system.

In the U.S. "based on existing investigations and mortgage fraud reporting, 80% of reported fraud losses involve collusion by industry insiders."[57] These individuals are familiar with the real estate and mortgage finance system and the weaknesses therein. Such collusion may involve small groups of fraudsters or large, organized fraud rings. The fraud rings may also involve collusion with individuals who are not involved in the real estate and mortgage industry. With property flips, the collusion usually is between mortgage brokers, real estate appraisers and settlement agents.[58] Large flipping frauds that involve multiple homes in an area in some cases have had severe adverse effects on neighbourhoods as evidenced by the following statement:

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[56] Arthur Prieston & Jacqueline Dreyer (2001), *Mortgage Fraud: The Impact on Your Company's Bottom Line,* (American Bankers Association, Washington D.C.), xviii.

[57] *Financial Crimes Report to the Public- Mortgage Fraud*, (2005, May 4), U.S. Department of Justice Federal Bureau of Investigation Financial Crimes Section Criminal Investigative Division. Retrieved May 15, 2005 from, http://www.fbi.gov/publications/financial/fcs_report052005/fcs_report052005.htm#d1

[58] In the United States, settlement agents frequently are real estate agents or title insurers.

> "It leaves a trail of deteriorating neighborhoods, destroyed personal credit histories and artificially inflated home values on the public record.[59]

In the U.S., many residential mortgages are sold by the lenders to the secondary mortgage market. The secondary mortgage market includes U.S. government sponsored enterprises (GSEs) and private investment companies. These organizations either hold the mortgages in their portfolios, sell the mortgages to third party investors or securitize them into mortgage-backed securities, which are sold to investors. As a result of mortgage fraud, the GSEs that operate in the secondary market now require lenders to repurchase the loans in the event the loan goes into default due to fraud. Thus, the risk of fraud is placed back with the loan originator, who is in the best position to detect potentially fraudulent applications at the outset.

Federally regulated financial institutions are required to report incidents of suspicious activity whenever they suspect or know of criminal activity. The suspicious activity must be reported to the Financial Crimes Enforcement Network (FinCEN) of the Department of the Treasury through Suspicious Activity (SAR) Reports. FinCEN then relays the reports to law enforcement agencies for investigation. Incidents of mortgage fraud or suspicious mortgage transactions are included in the SAR reports. An indication of the growth of suspicious mortgage transactions can be inferred from SARs filings. In 2004, the FBI received 17,137 SARs filings for mortgage fraud compared with 6,935 in 2003.[60] However, much mortgage fraud in the United States is not reported as many mortgage

[59] High time to Clean up Mortgage Fraud, (2003, June 27) [Editorial] *Inman News*.

[60] Supra. Statement of Chris Sweeker

lending institutions are not subject to the legislation under which SARs reporting is prescribed. In addition, the secondary market is not required to report fraudulent mortgages. Accordingly, there is "no central clearing house for reporting mortgage fraud"[61] so the actual amount of mortgage fraud in the U.S. is unknown.

To the lending industry, mortgage fraud results in higher defaults, which in turn, may result in higher fees and interest rates charged to borrowers. Fraudsters have taken advantage of the increasing market for loan originations in the U.S. and the fast turnaround for approving mortgages.

***Legal framework***

Mortgage fraud is not a specific crime in the United States except in the State of Georgia, which passed a law on May 5, 2005 making mortgage fraud a criminal offence in the State.[62] Therefore, in other jurisdictions, law enforcement agencies must prosecute mortgage fraud perpetrators under a related crime, such a bank fraud or wire fraud. The lack of a specific federal crime of mortgage fraud and lack of civil statutes regarding mortgage fraud may result in inconsistent treatment of such frauds by the courts.

***Common ways in which mortgage fraud is perpetrated in the United States***

There are three main categories of mortgage fraud in the United States: fraud for profit, credit fraud and predatory lending. Predatory lending usually is directed at first time buyers, senior citizens, low income families and individuals with poor credit history.

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[61] Technology and Mortgage Fraud, (2005, February) Volume 3, Issue 2) Quality Lending Review 3. Retrieved May 2, 2005 from, http://www.mortgagefraud.squarespace.com/the-prieston-group/

[62] Supra. Prieston & Dreyer 47.

Predatory lending involves unfair lending practices and is a fraud perpetrated by the lender. All predatory lending practices involve the granting of mortgages with sub prime or higher interest rates and often involve high loan origination fees and unreasonable fees for servicing the mortgage. Borrowers frequently default and the lender forecloses on the property. Predatory lending is fraud perpetrated by the lender and is not comparable to fraud perpetrated on lenders, borrowers and homeowners. Although it is often grouped with frauds on lenders, it really is a distinct form of fraud and not comparable to mortgage fraud as discussed in this paper.

While there is a multitude of mortgage fraud schemes in the U.S., the FBI has identified the most common forms of fraud for profit and has categorized them accordingly; mortgage fraud involving identity theft, value fraud, scams involving the use of straw buyers and straw sellers, foreclosure schemes and air loans. Similar to Canada, credit fraud results when a borrower falsifies information on the loan application in an effort to secure mortgage financing for which he or she would otherwise not qualify. In the U.S., credit fraud is not a significant problem and does not result in large losses to lenders.[63] The common forms of fraud for profit are explained below.

Identity Theft Mortgage Fraud – In the U.S., more than ten per cent of recent mortgage fraud charges have involved theft of identity.[64] Its use in the U.S. to perpetrate mortgage

[63] Testimony of William Matthew, Mortgage Asset Research Institute, Inc. Before the Unites States House of Representatives Subcommittee on Housing and Community Opportunity (October 4, 2004). Retrieved April 2005 from, http//www.financialservices.house.gov/mediafdp/100704wm.pdf.

[64] Fraud Files: New Trends in an Old Crime, (2005, January, Volume 3, Issue 1), *Quality Lending Review,* 14. Retrieved May 2, 2005 from, http://www.mortgagefraud.squarespace.com/the-prieston-group

fraud is similar to that in Ontario.

Value Fraud – In the U.S., property flips often involve kickbacks to parties that participate in the scam, typically mortgage brokers, employees of title insurers, appraisers and phony buyers. Under any value fraud scheme, the fraudster or innocent buyer ultimately defaults on the loan leaving the lender with a property that often is only worth 50% or less of the original value.[65]

Recently a new form of a land flip scheme called "chunking" has emerged. These schemes start with seminars that teach attendees how to make money by investing in real estate with no up front investment. However, often the real estate agent, appraiser and mortgage broker involved in the "investment" are parties to the scam. The attendees are contacted by someone connected with the seminar company to encourage the attendee to invest. With these frauds, the "investor" is not required to invest funds up front but he or she is required to provide financial and credit information as the properties are purchased and mortgaged in the "investor's" name. The fraudsters acquire properties and inflate the true value with false appraisals, which are then used to mortgage the properties. The fraudsters direct the settlement agent to disburse the proceeds to the fraudsters, leaving the investors with mortgages that exceed the market value of the properties.

Use of Straw Buyers and Straw Sellers – Similar to Ontario, a number of mortgage frauds involve the use of phony purchasers. In some frauds, phony sellers are also used to pose

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[65] *Mortgage Fraud* U.S. Department of Justice Federal Bureau of Investigation, Financial Crimes Section (May 4, 2005). Retrieved May 15, 2005 from, http://www.fbi.gov/publications/financial/fcs_report052005/fcs_report052005.htm#d1

as the current owner of the property.[66] The straw sellers then sell the properties to straw buyers, usually at inflated prices. The straw borrowers are then used to obtain fraudulent mortgages based on inflated property values. The fraudster pays the straw borrower or straw seller a fee for their "services" and use of identity and eventually the loan goes into default.

<u>Foreclosure Schemes</u> – These scams target homeowners whose homes are in foreclosure or are at risk of defaulting on their mortgage. The fraudster approaches the homeowner under the guise of helping them retain their homes in exchange for up-front fees and transfer of the deed. The fraudster pockets the fees and re-mortgages the home.

<u>Air Loans</u> – Air loans are loans collateralized by a non-existent property. Often the fraudster will set up a completely fictitious file and books, including bank accounts and fictitious buyers.

***Opportunity to commit mortgage fraud***

The U.S. mortgage lending environment is very similar to Ontario. The industry is highly competitive with many lenders – national banks, regional banks, mortgage banks, and other financial institutions as well as private lenders. And, similar to Ontario, there is competition in terms of rates, terms and turnaround time. The loan origination system is very similar in terms of the impersonal nature of the lending system and the ability to apply for mortgages electronically. The system of conveyancing in many states differs from that in Ontario - in many states settlement agents and title insurers are able to close

[66] Press Release U.S. Attorney's Office, *Indictment Handed Down in $20 Million Mortgage Fraud,* (May 13, 2004). Retrieved June 16, 2005 from, http://www.usdoj.gov/usao/gan/press/05-13-04.html

real estate transactions and register title to property – and many fraud schemes have relied on settlement agents not informing the lender of questionable transactions, such as property flips.

## U.S. Initiatives to Combat Mortgage Fraud

Initiatives that have been taken and are in consideration may be grouped into two categories: government, regulatory and law enforcement initiatives, and industry initiatives.

### *Government, regulatory and law enforcement initiatives*

U.S. law enforcement agencies, such as the FBI and the U.S. Attorney's office vigorously investigate and prosecute individuals that are alleged to have committed mortgage fraud against federally regulated financial institutions. This is evidenced by the numerous indictments and sentences for mortgage fraud listed in the Department of Justice website. In 2001, the FBI investigated mortgage fraud cases where losses exceeded US$100,000.[67] Mortgage frauds against lenders that are not federally regulated generally are investigated and prosecuted by state agents and prosecutors.[68] As noted below, the U.S. has implemented measures to combine the efforts of various agencies in investigations under certain circumstances.

The FBI has implemented procedures to detect and combat mortgage fraud. To assist in identifying potential property flipping scams, the FBI developed an analytical computer

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[67] Supra. Prieston & Dreyer 68.

[68] Ibid. 68.

program that searches for patterns of companies and individuals that are flipping properties. This tool has been successful in identifying fraudulent mortgage flips and inflated property values and is used throughout the country.[69] The FBI's investigative efforts have concentrated on industry insiders as such schemes have been extensive. For example, in 2002, the FBI identified a large mortgage fraud ring of industry insiders that engaged in flipping properties in the Cleveland Ohio area. The FBI indicted 94 individuals in connection with this scheme, including mortgage brokers, appraisers, loan underwriters and employees of title insurers.[70]

In an effort to obtain information regarding all suspicious mortgage fraud transactions, the FBI is considering implementing a Suspicious Mortgage Activity Report, or SMARt report, which would be filed by all lending institutions that do not file SAR reports.[71]

U.S. federal, state and local governments and agencies, including the FBI and private industry, are working together to combat mortgage fraud.[72] The effectiveness of this initiative was cited in a press release issued May 13, 2004 by the U.S. Attorney's office announcing indictments in a US$20 million mortgage fraud ring.[73] In addition, in August 2004, the FBI implemented "Operation Continuous Action". This initiative, which focuses on frauds against financial institutions, including mortgage fraud, is comprised of

[69] Supra. Statement of Chris Sweeker.

[70] Ibid.

[71] Ibid.

[72] Ibid.

[73] Supra. Press Release May 13, 2004.

law enforcement agencies at the local, state and federal levels as well as the regulatory agencies for financial institutions. One month after the formation of this group, the FBI announced that it had "taken action against 205 individuals" in connection with financial institution fraud.[74]

As noted above, concern for the level of mortgage fraud has reached the U.S. Congress, which has held hearings into this significant problem. Although mortgage fraud is not a separately defined crime in the U.S., with the exception of the State of Georgia, in 1998 Congress passed legislation making identity theft a federal crime.[75] Since identity theft is a relatively common way in which to perpetrate mortgage fraud, this law is an important measure for successful prosecutions for the criminal use of stolen identity.

In February 2005, the U.S. Department of Housing and Urban Development Office of Federal Housing Enterprise Oversight (OFHEO) issued a proposed regulation regarding mortgage fraud and Fannie Mae and Freddie Mac, the GSEs that operate in the secondary mortgage market. The proposal defines the mortgage fraud as "...a material misstatement, misrepresentation, or omission relied upon by a [GSE] to fund or purchase – or not to fund or purchase – a mortgage, mortgage-backed security, or similar financial instrument…" The proposal also defines "possible mortgage fraud" as anything that would lead the GSEs to believe that mortgage fraud is occurring or has occurred. The proposal also prohibits Fannie Mae and Freddie Mac from purchasing or requiring the

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[74] Press Release U.S. D.O.J. *FBI Announces Operation Continuous Action Targeting Financial Institution Fraud, (*September 17, 2004). Retrieved May 30, 2005 from, http://fbi.gov/pressrel/pressre104/contaction091704.htm

[75] Supra. Prieston and Dreyer 74.

loan originator to repurchase a mortgage if they are aware of a fraudulent mortgage or potentially fraudulent mortgage until they report such frauds to the Director of OFHEO. In addition, the proposal requires Fannie Mae and Freddie Mac to establish internal controls and procedures and training programs to detect and prevent mortgage fraud.[76] The proposal, if adopted, should help to identify additional suspicious schemes for investigation by law enforcement bodies and help quantify the economic impact of mortgage fraud. A number of industry organizations have submitted comments on the proposed rules to OFHEO but final rules have not yet been released.

In 2003, HUD implemented rules aimed at reducing the amount of fraudulent property flips. One rule "…makes properties that have been bought and resold within 90 days ineligible for Federal Housing Administration-insured (FHA) loans."[77] In addition, for any property that has been resold between 91 and 180 days and the selling price is at least double the seller's purchase price, FHA requires a second appraisal.[78] These are positive measures but since these rules only apply to FHA-insured loans, much of the industry is not subject to this rule.

[76] U.S Department of Housing and Urban Development Office of the Federal Housing Enterprise Oversight 12 CFR Part 1731 *Mortgage Fraud,* Retrieved May 7, 2005 from, http://www.ofheo.gov/media/pdf/mortfraudextensionperiod.pdf

[77] Mortgage Fraud: Crooks Buy Cheap, Sell High, Real Estate Fraud: The Housing Industry's White Collar Epidemic. (2003, June 25), *Inman News,* Retrieved May 30, 2005 from, www.inman.com/Member/reports/fraud/mort6841n11.pdf

[78] Mortgage Bankers Association. Issue Paper: *FHA's Prohibition of Property Flipping Regulations* (n.d.), Retrieved June 2005 from, http://www.mortgagebankers.org/library/isp/2005_5/FHA%20Prohibition%20of%20Property%20Flipping%20Regulations.pdf

Individuals convicted of crimes associated with mortgage fraud, such as wire fraud or bank fraud, face up of to 30 years in jail. In addition, the courts may order the criminal to pay restitution. Although several recent convictions indicate that the courts may not enforce the maximum penalties, prison terms ranged from 15 months to several years followed by several years of supervised release. In addition, the courts ordered the convicted fraudsters to pay restitution, which ranged from US$140,000 to US$2.9 million dollars.

***Industry initiatives***

The mortgage lending industry in the U.S. has undertaken many initiatives to combat mortgage fraud. The Mortgage Bankers Association, an umbrella organization for U.S. mortgage bankers, has established a comprehensive web site dealing with mortgage fraud issues. This site includes information on recent fraud frauds that have been reported by law enforcement agencies, legislative initiatives and reports by industry insiders. The web site is continually updated, thus providing a very important and useful source of information on this topic to the industry and the general public.

Freddie Mac has implemented quality control and credit risk procedures in their lending reviews to detect potentially fraudulent mortgages.[79] It also has published a booklet

[79] Statement of Donald J. Bisenius, Senior Vice President Credit Policy and Portfolio Management, Freddie Mac Before the Subcommittee of Capital Markets, Insurance and Government Sponsored Enterprises of the House of Representatives (May 30, 2004). Retrieved May 30, 2004 from, http://financialservices.house.gov/media/pdf/061404db.pdf

entitled "Fraud Prevention Best Practices" on its website, which is of benefit to loan originators and the general public.[80]

Also, in the U.S. there are several software products available to the mortgage lending industry that are designed to detect suspicious information contained in loan applications, including personal information, employment information and information regarding the property to be mortgaged. These tools detect inconsistencies in personal and employment information, property values as well as patterns of individuals applying for mortgage loans. Necessarily, such tools may generate "false positives" and therefore, are useful tools when used in conjunction with other detection and verification procedures.

The Prieston Group, a consulting firm to the mortgage lending industry, provides training to lenders to strengthen their loan approval processes with the objective of identifying risky and fraudulent loan applications. This training has been used by numerous lenders in an effort to reduce their exposure to fraudulent mortgages. In the U.S., seminars and conferences dealing with mortgage fraud are also an important means whereby the industry is educated and updated on current issues.

**Applicability and Adaptability of U.S. Initiatives to the Situation in Ontario**

***Government, regulatory and law enforcement initiatives***

<u>Resources and Partnerships</u> - U.S. law enforcement agencies generally have more resources available to investigate and prosecute mortgage fraud than Ontario. However, similar to U.S. initiatives, Ontario law enforcement agencies could benefit from

[80] Booklet available at www.freddicmac.com/singlefamily

partnerships with other government agencies and other organizations on an ongoing basis. For example, it may be beneficial for law enforcement to work in partnership with CMHC and the Law Society in investigating mortgage fraud. Such partnerships may help to identify the latest schemes, patterns of behaviour of individuals and geographic regions where flip schemes have occurred and to analyze why. In addition, an initiative similar to "Operation Continuous Action" that involves all levels of law enforcement and regulatory agencies in an ongoing relationship may prove to be beneficial in the Ontario situations.

Analytical Computer Tools - The use of an analytical computer programs similar to that developed by the FBI, that would search for patterns of behaviour to identify large-scale flipping schemes also could be of benefit in Ontario and Canada as a whole. However, due to the smaller Canadian economy, the costs to develop such software would need to be carefully considered in reference to the potential benefits as well as the cost to uncover such activity through other means.

Mandatory Reporting of Mortgage Fraud, Including Suspicious Transactions - The development and implementation of a mandatory reporting tool for all lenders, whether they be federally regulated, provincially regulated or unregulated, would be of significant benefit in Ontario. The U.S. experience with SARs reporting, although it does not apply to all institutions, has provided information regarding suspicious mortgage transactions that is provided to the FBI for investigation.

Identity Theft - Similar to the U.S., identity theft should be clearly defined in the Criminal Code, including a provision stating that it is an offence to possess multiple pieces of identification.[81] This measure would assist in prosecutions of mortgage fraud where identity theft was used to perpetrate the fraud.

Anti-flipping Regulations - Fraudsters do not want to hold onto the properties they deal with, as this ties up their "capital". Therefore, anti-flipping regulations similar to the U.S. regarding would be of benefit in Ontario, particularly in preventing inflated values from penetrating a particular neighbourhood. There is a risk that legitimate transactions could be caught under such rules, but this risk is minimal in comparison with the potential benefit.

Penalties for Convicted Fraudsters - Stricter penalties for convictions of mortgage fraud, as in the U.S., may provide a stronger deterrent to mortgage fraudsters in Ontario. The light sentences imposed by the Ontario courts are not a significant deterrent as there are instances where fraudsters have perpetrated frauds multiple times. For example, investigative reporters for CTV found that one convicted fraudster, Gideon Augier "has a 20-year criminal record, with no fewer than eight convictions for fraud, mostly related to mortgages. Yet he has served mere days in jail, and to this day is a free man."[82] This is the same individual that was the defendant in a case discussed above, "Durrani v.

[81] Canadian Bankers Association, *Fraud and Security*: *Identity Theft,* Retrieved April 30, 2005 from, http://www.cba.ca/en/section.asp?fl=4&sl=268&tl=276&docid

[82]Supra. CTV W5

Augier". U.S. mortgage fraudsters face stiffer penalties, including restitution, which should provide a stronger deterrent to this form of white-collar crime.

***Industry Initiatives***

Co-operative Industry Efforts - Industry efforts to work together must continue as in the United States. Combined efforts are needed not only to identify swindles and patterns of behaviour but also to seek solutions. As noted earlier in this paper, a working group consisting of industry participants as well as provincial government representatives and the police was formed in 2004. In addition, on their website, the Canadian Bankers Association (CBA) states that the banks and the CBA are members of task forces and working groups throughout Canada.[83] These are beneficial initiatives. This group must continue to work cooperatively by sharing information regarding experiences and trends and developing procedures to prevent and detect mortgage fraud.

Conferences and Seminars - In addition, industry conferences that include mortgage fraud on the agendas, or even separate conferences specific to this issue would be of benefit. Such events would provide a forum for sharing information regarding, experiences, trends, and 'best practices' in prevention and detection from many parties from across the country or region.

Analytical computerized tools that are designed to detect inconsistencies and risk factors in loan applications would be of benefit to all lenders. While the large banks may have

[83] Canadian Bankers Association *Consumer Protection Fraud and Security Real Estate Fraud 2005*. Retrieved June 19, 2005 from, http://www.cba.ca/en/viewdocument.asp?fl=3&sl=65&tl=136&docid=567&pg=1

the resources to develop such software applications in-house, the development cost may be too high for smaller institutions. In such cases, consideration may be given to adapting commercial U.S. systems to the Canadian marketplace.

Training - U.S. loan originators that have engaged consultants to train loan staff to identify the red flags and risk factors that may indicate a fraudulent loan application have benefited through lower losses from defaults.[84] Such training in certain cases has been adapted to the specific of individual lenders. The benefit of this measure is that staff at every phase of the loan application process would be trained to identify the red flags and risk factors. This training could be developed in-house using a review of loan files that are known to be fraudulent. This initiative is key to early detection and prevention of mortgage fraud.

**Conclusion: Early Detection and Prevention**

Prevention of mortgage fraud requires the combined efforts of all parties to real estate and mortgage transactions because, as stated above, fraudsters will target the stage in the process or parties to the process where controls are lax. In addition, industry, government, regulatory and law enforcement efforts must recognize that mortgage fraud results in significant negative consequences for all victims, whether they be deep-pocketed financial institutions or innocent individuals. Society as a whole pays for mortgage fraud.

[84] Supra. Easy Steps to Fraud Protection 3.

Lenders must implement strategies and programs for employees in loan origination, credit review and loan administration functions so that these individuals are trained to detect the red flags and risk factors of fraudulent applications and loan files. A system of red flags and risk factors review, whereby if red flags or risk factors are present, the loan is subject to additional reviews and verifications, or ultimately, is rejected. For example, if two red flags are present, the loan originator would follow up by requesting additional information and performing additional verification checks. If more than four red flags or risk factors are present, the loan application would need to be reviewed at a more senior level in the organization. After some threshold of red flags and risk factors, the loan ultimately would be rejected. This system can also incorporate the relative significance of various red flags and risk factors, as some are of more concern than others.[85] If we are to successfully fight mortgage fraud, lenders must not consider mortgage fraud to be a normal cost of doing business. Mortgage defaults due to legitimate reasons, such as a job loss or disability, for example, are a normal cost of doing business, but not fraud.

Similarly, mortgage brokers must be diligent in reviewing identification and the financial information presented by loan applicants. As noted earlier in this paper, CIMBL has recognized the importance of these activities by publishing a booklet that details "…the minimum standards of care and due diligence required for the acceptance, completion and submission of mortgage loan applications."[86] Additionally, lenders and mortgage brokers in Ontario have an opportunity to review the compensation arrangements with

[85] Jennifer Fiddian-Green discussed a red flag and fraud scoring system in her Embanet presentation to DIFA 2005 May 4, 2005.

[86] Booklet is available at http://www.cimbl.ca/download_docs/Origination_Standards_April2005.pdf

mortgage brokers as the incentive-based system could entice a less than ethical broker to 'look the other way' if presented with a questionable loan application.

Real estate lawyers are required to exercise due diligence in every real estate and mortgage transaction. It is imperative that they have good processes to verify the identification of their clients for a couple of reasons. Firstly, because clients generally engage in real estate purchases infrequently and therefore, it may be difficult to "know your client". Secondly, due to the availability of mortgages over the phone and internet, the lawyer may be the only party to the transaction to meet the borrower in person. Thus, the lawyer has the last opportunity in the process to detect fraudulent identification. Additionally, to detect potentially fraudulent transactions, particularly property flips and title theft, lawyers need to review their title searches of the subject property thoroughly. This may reveal information that could identify whether there have been any recent property transfers and significant value increases that might indicate a fraudulent transaction. Follow up by lawyers on suspicious transactions could lead to reduced incidents of mortgage fraud.

Real estate agents also need to be cognizant of potentially fraudulent real estate deals and to disassociate themselves from any deals where purchase prices are effectively amended, whether through a side agreement that is not presented to the lender or misrepresentation in the agreement of purchase and sale. As noted above, RECO provides information to members through education. In addition, similar to other professional organizations, RECO can revoke the real estate licence of agents found to have knowingly participated in mortgage fraud.[87]

As suggested by the Law Society in its "Report to Convocation: Mortgage Fraud" of March 2005, limiting distribution of Teranet licences to lawyers and government officials will help prevent fraudulent title transfers.[88] This will make the tracking feature of the Teranet system a more effective investigative tool as the pool of available parties would be restricted and known to Teranet. With the current system, the fraudster may be long gone by the time the fraud is uncovered and, if the licence was acquired through use of false identity documents, tracking the fraudster would be much more difficult.

To the extent that financial institutions continue to view fraud as a cost of doing business, this is a potential advantage to fraudsters. Specifically, procedures to detect fraud at the loan origination stage may be lax due to a focus on fast turnaround of loan approvals and higher volume of loans funded. Such lenders may assume that their fraud losses will be compensated by high volume. There is a cost to additional procedures and an internal focus on risk factors and the red flags of real estate and mortgage transactions to detect and therefore, prevent mortgage fraud. Financial institutions must weigh the cost and benefit of such measures. However, if mortgage fraud continues to rise in Ontario, as has been the U.S. experience, the business case for such measures will become clearer.

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[87] RECO website http://www.reco.on.ca

[88] Supra. *Report to Convocation: Mortgage Fraud* 23.

In the book "Mortgage Fraud: The Impact of Fraudulent Loan Practices on Your Company's Bottom Line"[89], the authors liken mortgage fraud to a computer virus as they both are continually changing and evolving and reacting to the responses of the industry. As the authors state, review of detection and prevention tools must be ongoing, in order to keep abreast of the latest scams. Clearly, our opportunity to deter mortgage fraud in Ontario must be an ongoing and diligent effort. It is helpful to understand certain of the measures undertaken in the U.S., and consider their application to the situation in Ontario. Regulatory initiatives aimed at stopping flipping schemes and efforts to require reporting of fraud or suspicious transaction by all loan originators and the secondary mortgage market are initiatives that Ontario regulatory agencies could adapt to the Ontario environment. Industry efforts that focus on staff training staff to prevent and detect suspicious loan applications and industry groups and conferences are also measures that are applicable to Ontario. Lastly, legislative changes to the Criminal Code to clearly define identity theft as in the U.S. may be of benefit to other crimes that are perpetrated with false identification as well as mortgage fraud. And, we particularly require diligent and continuing effort in the fight against mortgage fraud from all industry, government and professional organizations involved. To the extent that these groups work together to communicate and educate one another regarding the nature of mortgage fraud, parties and individuals involved, and detection and prevention efforts, we have a significant opportunity to significantly reduce this fraudulent activity.

[89] Supra. Prieston & Dreyer xx.

## Appendix I
## Glossary of Terms

**Off-title Search –** Includes such checks as ensuring property taxes and municipal utility bills are up-to-date, compliance with zoning by-laws and unregistered easements.

**Charge/Mortgage of Land** – In order to register a charge on title in Ontario, it must be in the prescribed document form, which is the "Charge/Mortgage of Land" form.

**Conventional Mortgage –** A conventional mortgage is a mortgage granted without the borrower providing the lender with insurance in the event of default. In Canada, financial institutions will grant conventional mortgages to borrowers that have at least a 25% down payment and favourable financial status. A conventional mortgage is granted based on the credit-worthiness of the borrower and value of the property. The borrower must have job stability and sufficient income, excellent credit history and low debt in total.

**High Ratio Mortgage**– High ratio mortgages are mortgages where the mortgage loan exceeds 75% of the house value as determined either by an appraisal or by the purchase price of the home. Lenders require that borrowers obtain mortgage insurance for high ratio mortgages, to protect the lender in the event of default. The borrower pays the premium, which is a percentage of the loan value and the beneficiary of the policy is the lender. In Canada, the insurers usually are Canada Mortgage and Housing Corporation or Genworth Financial Canada.

**Secondary Mortgage Market –** The secondary mortgage market does not originate mortgage loans. Rather, organizations that operate in the secondary mortgage market buy mortgages from loan originators and either hold the mortgages in their portfolios or sell them to other secondary market organizations or securitize the mortgages as mortgage-backed securities. Fannie Mae and Freddie Mac operate in the secondary mortgage market.

**Federal Housing Administration (FHA) Loans –** FHA loans are insured by the U.S. government. FHA insures 100% of the mortgage loan for qualified borrowers. FHA requires a down payment of 3% of the home value, but closing costs may be paid out of the loan. Borrowers pay a premium of 1.5% of the loan value for the insurance.

**Fannie Mae (FNMA) -** formerly Federal National Mortgage Association – Fannie Mae was formed by the U.S. federal government in 1938 to purchase FHA-insured mortgages. Since the 1970's FNMA has been conventional mortgages as well as insured mortgages. Fannie Mae does not originate loans. Rather, it buys mortgages granted by lenders and either keeps the mortgages in its portfolio, sells them to another institution or packages them as mortgage-backed securities and sells them to investors.

**Freddie Mac (FHLMC) -** formerly Federal Home Loan Mortgage Corporation - Freddie Mac is a stockholder-owned corporation chartered by Congress in 1970 to keep money flowing to mortgage lenders in support of homeownership and rental housing. Freddie

Mac purchases single-family and multifamily residential mortgages and mortgage-related securities, which it finances primarily by issuing mortgage pass through securities and debt instruments in the capital markets. Retrieved May 30, 2005 from http://www.freddiemac.com/corporate/whoweare/

**Summary Judgment** – Summary judgment arises when the defendant does not file a Statement of Defence in response to the Pleadings filed by the plaintiff. The courts then decide in favour of the plaintiff as there is no rebuttal of facts or issues.

**Title Insurance -** Title insurance protects the insured (homebuyer and lender) against loss resulting from title defects and defects that would have been revealed by an up-to-date survey or real property report.[90] Some of the matters over which a title insurance policy provides coverage include survey irregularities, zoning problems, title defects, liens, easements and unmarketability of title. Title insurance also protects policyholders in the event that there is a forgery or fraud relating to title.[91]

**Suspicious Activity Reports (SAR Reports)**
Financial institutions that are regulated by a federal supervisory agency are required to file reports of suspicious financial activity with the Financial Crimes Enforcement Network (FINCen) of the U.S. Department of the Treasury. SAR reports report known or suspected criminal offenses, at specified thresholds, or transactions over $5,000 that they suspect involve money laundering or violate the U.S. Bank Secrecy Act. Retrieve June 16, 2005 from http://www.occ.treas.gov/sar.htm and from http://www.occ.treas.gov/ftp/release/2000-45.txt

**Loan to Value Ratio**
Loan to value is the ratio of the mortgage loan to the value of the property. If the loan to value ratio is within certain targets, the loan generally will be approved. Lenders will either use the appraised value or the purchase value.

**Credit Scores**
A credit score is a numerical value calculated using information in an individual's credit report and loan application. Lenders use the credit score as a measure of credit-worthiness. Extracted June 17, 2005 from https://www.econsumer.equifax.ca/ca/main?forward=/view/common/template.jsp&body=/view/education/credit_ed.jsp&show=score_basics_llaanngg.jsp#5

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[90] First Canadian Title *Title Insurance* http://www.firstcanadiantitle.com/en/products_services/index.html

[91] Lorne Shuman. *Title Insurance: A Modern Tool for Real Estate Lawyers*. Retrieved June 13, 2005 from http://www.firstcanadiantitle.com/en/about/media_centre/articles/general/Article%20Shuman%20Eastern.pdf

## Appendix II – Red Flags and Risk Factors of Mortgage Fraud

| Item | Red Flag and Risk Factors | Follow Up | Red Flag<br><br>Y/N – If N add score |
|---|---|---|---|
| **General Information** | | | |
| 1 | A new mortgage that isn't being used either to purchase a property or replace an existing first mortgage. | Follow up as to intended us of proceeds. | |
| 2 | The borrower is not known to either the lender or lawyer. | Scrutiny of all identification documents. | |
| 3 | The buyer of the property is a corporation. | Verify business of company by checking address & phone #. | |
| 4 | Property being mortgaged was acquired through a private sale. | | |
| 5 | Property being mortgaged is significantly more expensive than the property being sold. | | |
| 6 | Applicant only has a cell phone for contact. In the case of young applicant's (those in their 20's and early 30's) the only phone number they have may be a cell phone, so this risk factor must be considered in reference to others. | Verify reason for cell phone. | |
| **Loan Application Information** | | | |
| 7 | Information in loan application seems altered – change in font, white-out, etc. | Verify altered terms with other party to the transaction. | |
| 8 | Employment information is inconsistent with job function. For example, retail clerk with stated income of $100k. | Verify salary or job function with employer. | |
| 9 | Sequential pre-printed forms are submitted from different applicants – such as pay stubs, T4's, etc. | | |

## Appendix II – Red Flags and Risk Factors of Mortgage Fraud

| Item | Red Flag and Risk Factors | Follow Up | Red Flag<br><br>Y/N – If N add score |
|---|---|---|---|
| 10 | Verification of employment information is not provided on corporate letterhead or address is a P.O. box only. | Verify employer by phoning and request physical address.<br>Verify the phone number in phone book or Canada 411 with letterhead. | |
| 11 | Income information is hand-written, such as T4's, pay stubs, etc. | | |
| 12 | Similar letters of employment from different applicants. | Verify employment of applicants with employer. | |
| 13 | Annual income is in exact dollars and cents. | | |
| 14 | Applicant's representation as to source of deposit is not verifiable. | If first time buyer, applicant should have enough funds for deposit in a bank account for 60 days prior or proof of gift. | |
| 15 | Driver's licence and / or social insurance number are not valid numbers or documents. | Enquire of applicant as to source of the documents. | |
| 16 | Source of down payment – if it has not been in the borrower's possession for at least 90 days, and does not come from sale of existing property. | | |
| 17 | Borrower contends that down payment is a gift. | Obtain confirmation from giftee as to amount of gift and use. | |
| 18 | Numerous credit inquiries on credit report. | Enquire of applicant the nature of the inquiries. Perhaps applicant has applied to other lenders for the same loan. | |

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Yamada v. Mock, [1996] O.J. No. 2045 (Quicklaw) (Ontario Court (General Division))

**Interviews Conducted**

C. Burgess, real estate agent

B. Durkin, mortgage broker

A number of interviews were conducted with lenders, lawyers, law enforcement officers and other individuals involved in the real estate and mortgage lending industry. Many of these individuals wish to remain anonymous.

**Confidential Document**

A confidential document was provided to the writer of this paper, which is not disclosed in the bibliography.

**Statutes**

Criminal Code – selected sections
Land Titles Act – selected sections