

What are the causes of mortgage fraud

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What are the Causes of Mortgage Fraud?

Loan fraud refers to the practice of misrepresenting material information, to make it possible for a borrower who does not qualify for a loan to get one, or to make it possible to grant borrowers more loan than they qualify for. There are various causes of mortgage fraud, which have led to the mortgage crisis that was experienced in 2007. These causes include:

Lack of disciplined underwriting

The consistent failure to apply underwriting policies, in the process of assessing the suitability of borrowers to qualify for a loan is the major cause of mortgage fraud (USRMR, 3). Therefore, when the lenders fail to adhere to the outlined underwriting guidelines, they increase the chances of risks involved in granting loans to individuals who are not capable of repaying the loans accordingly. Failure to apply the necessary underwriting guidelines comes in the form of deliberately refusing to apply the required mortgage control procedures, which in turn lead to the misrepresentation of facts regarding the ability of the borrower to repay the mortgage. Therefore, inadequate appraisal of the borrower has highly contributed to mortgage fraud, since if it is not done accurately at the initial stages of evaluation, the risks associated may not be identified, until it is too late, and the borrower has already started defaulting on the mortgage repayment (USRMR, 10). Thus, the major problem underlying mortgage fraud is not the provision of inaccurate records by the borrower. Instead, the major contributors to mortgage fraud are inadequate quality control application, poor underwriting practices and poor valuation of borrower's assets (USRMR, 4).

Decline in mortgage underwriting standards

The regulators and specialists applied lenient measures in the mortgage

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underwriting standards in the name of innovation, seeking to make the process of acquiring mortgage loans easier and convenient for low income households (Liebowitz, 7). However, these innovations declined the mortgage underwriting standards and weakened the control policies. This served the purpose of making mortgage underwriting easier for small income earners, increasing home ownership and raising the prices of houses (Liebowitz, 15). Therefore, speculators purchased and sold houses under minimal underwriting control, increasing their profits by a greater margin and then running away from the market when the crisis became eminent. This left the mortgage business with large debts owed by home owners who could not manage to repay the loans, thus causing the acceleration of the mortgage crisis (Liebowitz, 24).

Inadequate accounting techniques/control fraud

The application of inadequate accounting techniques while valuing the borrower's ability to repay a loan is another major cause of mortgage fraud. Lack of supervision and failure to review loan files increases the chances of fraud, as the lenders overlook the borrower's ability to cover the loans, so they can increase the loans disbursed and thus increase their profits (Black, n. p.). The inadequate accounting techniques include the failure to review loan files for nonprime loans and the failure to require the lenders to provide loan tapes (Black, n. p.). The accounting vice was borrowed from the lenders by the rating agencies, who failed to review the loan files and instead opted to rate nonprime loans highly, so they could increase their profits. This saw borrowers qualify for highly rated loans, which they could otherwise have not qualified, if accounting vigilance was applied (Black, n. p.). This contributed to high mortgage fraud.

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