

Money Laundering: Not So Clean

With the exponential rise in mortgage fraud, know what to watch out for and how to protect yourself

By **Ivan A. Garces**, director of forensic services, Kaufman, Rossin & Co.

EXCEPTIONAL GROWTH IN THE REAL estate market in the past few years made mortgage financing an attractive opportunity for fraudsters. Add to that the development of innovative loan products that made qualifying for home financing easier — plus the increase in automated, Internet-based loan processing — and an increase in mortgage fraud was inevitable.

The Financial Crimes Enforcement Network (FinCEN) reported that between April 1, 1996, and March 31, 2006, 82,851 suspicious-activity reports were filed related to mortgage fraud. FinCEN also found that mortgage fraud increased by 1,411 percent between 1997 and 2005, and the pace continued in 2006.

Despite the uncertainty in the current environment, the use of mortgage transactions for illicit purposes such as money laundering continues to flourish. Learn how to spot it and how to shield yourself, your company and your clients.

The laundering process

Money launderers have used real estate and mortgage loans to place illicit proceeds into the financial system, to layer the funds to disguise their true origin and to integrate the now-disguised illicit proceeds back into the economy.

For such fraudsters with a substantial amount of “dirty money,” real estate is a viable means for laundering. They may purchase a property partly in cash and borrow the remainder through a mortgage using a “straw buyer.” This is someone who often is paid to lend a name and information but who has no intention to occupy the property. The buyers may then flip the property

immediately for the same price or even for less. Making a gain would be gravy, and the funds now appear clean.

When real estate and mortgages are used for money laundering, fraudsters may structure deposits to avoid having to file a currency transaction report. These reports must be filed for cash transactions of more than \$10,000. For example, fraudsters may purchase multiple cashier’s checks in amounts of less than \$10,000, possibly from different banks, that are payable to the title company or escrow agent. Or they’ll deposit funds from unrelated or unknown third parties.

Although significant down payments don’t necessarily mean money laundering is occurring, you should look more closely when buyers bring substantial cash to the table.

respondent mortgage lender, of any person who has engaged in a pattern of misconduct while an associate of a mortgage brokerage business or an employee of a mortgage lender or correspondent lender.”

The potential penalties at the federal level can be even more severe. With respect to money laundering, the penalties can include a fine of as much as \$500,000, imprisonment for as many as 20 years and restitution to the victimized bank. If the fraud is classified as bank fraud, the penalties are even worse — as much as \$1 million in fines and as many as 30 years in prison.

Protect yourself

A mortgage company’s management should be explicit about its views on fraud through a written anti-fraud policy and code of conduct that

Executive Summary: Red Flags

When working with new clients, ask yourself the following questions to be on the lookout for money laundering or another type of mortgage fraud.

- Does the information borrowers provide make sense?
- If borrowers have a large down payment, what’s the source?
- Are the buyers seeking a first and a second mortgage?
- Have the borrowers made unusually large deposits to their account in round dollar amounts?
- Do the buyers want to take a significant amount of cash out at closing?

Serious penalties

Several states are taking steps to combat mortgage fraud. For instance, in Florida, which leads the nation in mortgage fraud, the state Legislature sent a bill to the governor this past May that would make fraud a third-degree felony punishable with a five-year state-prison sentence. If more than one property is involved, it would be a second-degree felony that would involve higher penalties. If the governor signs the law, it will take effect in October.

The bill also would authorize the state’s Office of Financial Regulation to “prohibit the association by a mortgage broker business, or the employment by a mortgage lender of cor-

is communicated to employees. Senior management should use proactive employment practices, such as comprehensive background checks and ongoing monitoring.

Management oversight is an important element. Senior management should regularly review unusual, significant and highly complex deals to see if they are reasonable.

Also, protect yourself by getting to know your buyers. The advent of Internet-based lending makes this more difficult; face-to-face contact is no longer required. Perform due diligence to gain a level of confidence that the buyers’ statements and documents are legitimate.

Continued ...



Ivan A. Garces, CPA, CFE, CAMS, is the director of forensic services for Kaufman, Rossin & Co., one of the largest independent accounting firms in Florida, with clients throughout the state and in more than two dozen

countries. Garces can be reached at igarces@kaufmanrossin.com.

REPRINTED FROM *SCOTSMAN GUIDE RESIDENTIAL EDITION* AND SCOTSMANGUIDE.COM, JULY 2007

All rights reserved. Third-party reproduction for redistribution is prohibited without contractual consent from Scotsman Publishing Inc.

Money Laundering: Not So Clean

... Continued

Check employer references, research the source of funds and confirm borrowers' identities.

If third-party checks are involved, find out who the parties are and why they are involved. Ask all the questions you can think of, and then ask some more. This is more important now than ever.

Go a few steps further by getting to know anyone else involved in the transactions, including real estate agents and appraisers. If buyers specifically request an appraiser you don't know, a red flag should go up. Appraisers should be independent.

Here are some other red flags to watch for:

- **Does the information borrowers provide make sense?** Do their occupation and age look right? Do they match the stated income, debt, assets and down payments? Trust your instincts — a mismatch could indicate money laundering or another type of mortgage fraud.
- **If borrowers have a large down payment, what's the source?** Does the source make sense? Can you verify it? Keep an eye out for large escrows in sales contracts, which also could be a red flag.
- **Are the buyers seeking a first and a second mortgage?** Or do they apply for a second mortgage immediately after closing on the first? Does the reason for doing so sound legitimate? Again, verify and ask many questions.
- **Have the borrowers made unusually large deposits to their account** — especially in round dollar amounts? Again, consider whether the deal is being used to launder funds.
- **Do the buyers want to take a significant amount of cash out at closing?** This could be a big red flag for money laundering and should immediately trigger additional due diligence.

These ideas are not exhaustive, but they are steps you may want to consider to help mitigate the risk that you and your company are used to further illicit activities.

Implementing these precautions is no guarantee that you won't be defrauded; every situation is different. You may wish to consult professionals who specialize in fraud prevention and investigation to assess your operation and recommend specific safeguards.

For mortgage brokers, the federal penalties for money laundering and bank fraud are already harsh, and with states beginning to add their own statutes, now is the time to increase vigilance.

In today's environment, where transactions require less face-to-face interaction, it's more important than ever to make sure you know

your clients. The rising tide of the real estate market may have lifted all boats, but as the tide goes out, we may see some nasty things lurking at the bottom. **!!!**