

White Paper

The LexisNexis® 14th Annual Mortgage Fraud Report

July 2012

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Research provided by:

Jennifer Butts,
LexisNexis® Risk Solutions

Tim Coyle,
LexisNexis® Risk Solutions

Jo Prichard,
LexisNexis® Risk Solutions

Merle Sharick, CMB,
LexisNexis® Risk Solutions

Executive Summary

With still-high delinquency and foreclosure rates, little economic progress in depressed markets, and unscrupulous individuals taking advantage of the financially disenfranchised, 2011 was a bleak year for the mortgage industry. As industry insiders and economic analysts hope for noticeable recovery, 2011's mortgage loan originations were at their lowest since 2001. However, the business of home buying continues, albeit slowly and with considerable caution.

Industry participants continue to try and manage through this industry volatility, while recognizing heightened oversight and consumer uncertainty. Increased legislative and regulatory mandates like those from the Office of the Comptroller of the Currency (OCC) (a focus on 2009-10 closed loans and credentialing), the 2010 Dodd-Frank Act (overarching regulation across the financial services industry), the 2008 Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act (originator registration on National Mortgage License System & Registry (NMLS/R)), the Real Estate Settlement Procedures Act (RESPA) (new required disclosures and closing procedures), and FHA Certified Brokers (HUD transitions third party originator risk to lenders and banks) have created a tighter day-to-day reality for professionals involved in all aspects of the mortgage transaction. Such mandates, along with the newly vigilant loan industry, appear to be making a difference in one arena, as a decreased number of loan origination fraud and misrepresentation cases are being reported. However, along with these decreases are increases in potential distressed homeowner fraud and collusion schemes.

This is the LexisNexis 14th Annual Mortgage Fraud Report, formerly known as the MARI Fraud Report. These annual reports examine the current composition of residential mortgage fraud and misrepresentation involving industry professionals in the United States. (See Appendix I at the end of this report for information about the methods used to collect data on mortgage fraud.) In addition, this year we are including statistics that reveal patterns of potential mortgage industry collusion.

LexisNexis' examination of 2011 data identified that:

- According to the FBI, a total of 93,508 mortgage-related SARS were collected in FY 2011, up almost 33 percent from FY 2010.
- For loans originated in 2011, Florida ranks third on the Mortgage Fraud Index (MFI) with an MFI of 227—slightly over two times the rate of reported fraud and misrepresentation by industry professionals that would be expected based on the proportion of loans originated in Florida. However, Florida's Origination MFI is the state's lowest in the past five years.
- Five states—Florida, Michigan, California, Illinois and New York—occupy space in top ten lists for incidents of reported industry fraud and/or misrepresentation for both 2011 investigations and 2011 originations.

Mandates, along with the newly vigilant loan industry, appear to be making a difference in one arena, as a decreased number of loan origination fraud and misrepresentation cases are being reported. However, along with these decreases are increases in potential distressed homeowner fraud and collusion schemes.

- The top Metropolitan Statistical Area (MSA) for reported loans originated in 2011 is Los Angeles–Riverside–Orange County, California. Sixteen percent of all reports received included properties in this MSA.
- Reports for loans originated in 2011 have significantly fewer cases of Appraisal fraud and misrepresentation than in previous years. At 17 percent in 2011, this type of misrepresentation is down from a high of 34 percent in 2009.
- The highest categories for all reported 2011 investigations are Application and Appraisal fraud and misrepresentation. The highest categories for reported 2011 originations are Application and Verification of Deposit (and other bank-related documentation) fraud and misrepresentation.
- According to the incident data from MIDE X submissions, there is an increase in reported incidents of potential collusion involving multiple professionals.
- Six states—Alabama, New York, Kentucky, Pennsylvania, Iowa and New Jersey—rank in two different categories on the LexisNexis Collusion Indicator Index (CII) as areas with high levels of potential non-arm’s length collusion activity.

The body of this report presents the data and analysis supporting the findings cited above. The information contained in this report is meant to provide insights into current mortgage market activities.

Data and Information Sources Used in This Case Report

For over two decades, major mortgage lenders, agencies and insurers have been submitting information describing incidents of subscriber-verified fraud and material misrepresentation to an industry-contributed database, known as MIDE X (Mortgage Industry Data Exchange), in order to share adverse experiences involving professionals operating within the mortgage industry. Contributing subscribers use information services derived from the MIDE X database as a risk management tool to protect against mortgage fraud perpetrated by industry professionals. MIDE X enables subscribers to perform due diligence checks on mortgage professionals and companies as part of their business relationship credentialing process. LexisNexis utilizes MIDE X submissions to develop representative statistics on a wide range of mortgage fraud and misrepresentation characteristics. Findings from this analysis are presented in annual Case Reports to provide key insight into mortgage fraud trends, as reported by the industry.

In addition to MIDE X incident data, the report utilizes Home Mortgage Disclosure Act (HMDA) data sourced by the Mortgage Bankers Association (MBA), a key component used for calculating a state’s Mortgage Fraud Index (MFI) value. Please refer to Appendix II for information on the MFI and its computation.

According to the incident data from MIDE X submissions, there is an increase in reported incidents of potential collusion involving multiple professionals.

Using proprietary algorithms, LexisNexis public record data is used to calculate the LexisNexis Collusion Indicator Index (CII) to determine potential collusion activity within a state. Please refer to Appendix III for information on the CII and its computation.

The LexisNexis Mortgage Fraud Reports and SAR Filing Trends

The Federal Bureau of Investigation (FBI) collects Suspicious Activity Reports (SARs) from all federally-insured financial institutions. Figure 1 shows the increase in mortgage fraud SAR submissions over the past several years. A total of 93,508 SARs were collected in FY 2011, up almost 33 percent from FY 2010. However, it would appear that a significant number of these SARs no longer involve loan origination fraud. Per the FBI's *Financial Crimes Report to the Public for FY 2010-2011*, "for the first time in recent history, distressed homeowner fraud has displaced loan origination fraud as the number one mortgage fraud threat in many offices." In Figure 2, the FBI reports that there was a decrease in pending cases in 2011. However, FBI mortgage fraud investigations resulted in 1,223 criminal indictments and informations and 1,082 convictions in FY 2011 alone.

Figure 1

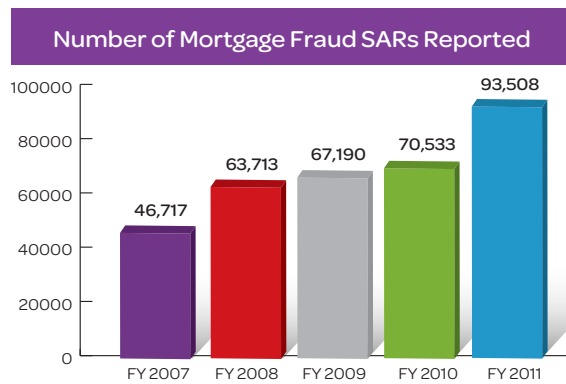
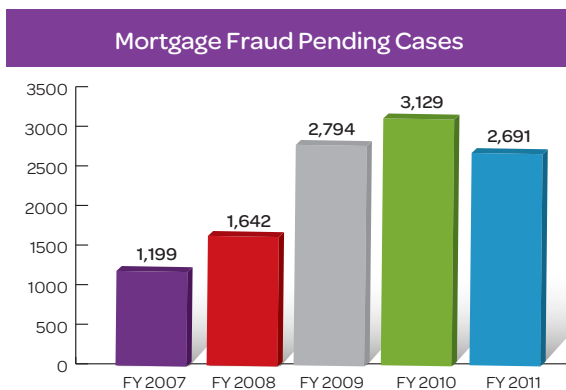


Figure 2



Source: FBI's *Financial Crimes Report to the Public for FY 2010-2011*

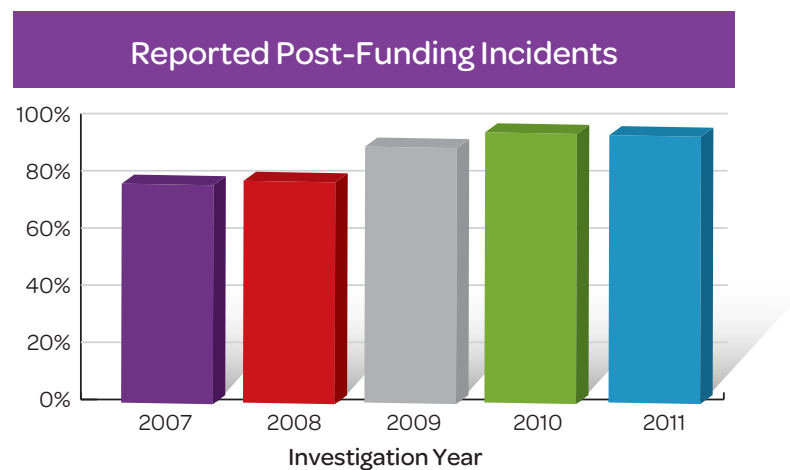
Per the FBI, "for the first time in recent history, distressed homeowner fraud has displaced loan origination fraud as the number one mortgage fraud threat in many offices."

As we reported in last year's report, the year-over-year increases in SAR submissions represented on the previous page are not likely to be entirely reflective of mortgage fraud activity. SAR submissions are currently only required of federally-insured financial institutions and their affiliates, though this will change this year as the Financial Crimes Enforcement Network (FinCEN) implements mandatory reporting for non-depository institutions including mortgage brokers and lenders. Therefore, fraud experiences of independent mortgage entities are currently not likely to be reflected in Figure 1. These independent mortgage companies, however, comprise a portion of MIDEX subscribers, and therefore, their reported incidents of fraud and misrepresentation are represented in the MIDEX data.

Furthermore, incident reports submitted must be verified, material misrepresentations involving industry professionals. In 2011, LexisNexis experienced a decrease in reported instances of material fraud and misrepresentation. From 2010 to 2011, 35 percent fewer reports of verified, material misrepresentation involving industry professionals were received. This is to be expected, as the FBI noted above, fewer mortgage fraud schemes involve loan origination fraud and misrepresentation. Additionally, according to FinCEN's April 2012 *Mortgage Loan Fraud Update*, close to 80 percent of 2011 SARs in a sample study involved Fraud for Housing, or fraud and misrepresentation most often perpetrated by borrowers in order to qualify for a home. The majority of MIDEX incidents involve Fraud for Profit, or fraud or misrepresentation involving industry professionals.

Among these instances of Fraud for Profit, there is often a marked time lapse between loan origination and submission of a post investigation report to MIDEX.

Figure 3

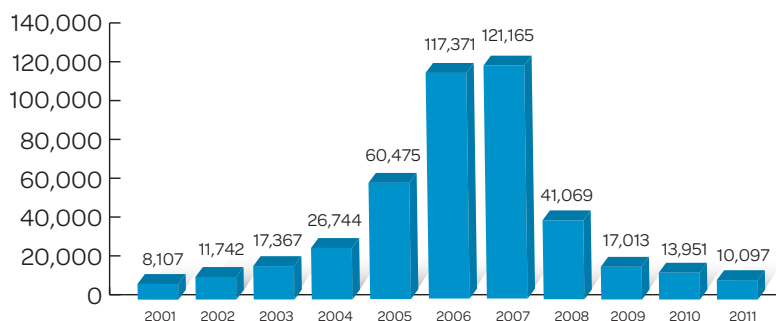


As Figure 3 indicates, in 2007, 77 percent of loans investigated and submitted to LexisNexis were for loans originated in prior years, and 23 percent of investigations submitted in 2007 involved loans originated during that year. In 2010 and 2011, we have seen a marked increase in submissions for years older than the investigation year.

Close to 80 percent of 2011 SARs in a sample study involved Fraud for Housing or fraud and misrepresentation most often perpetrated by borrowers in order to qualify for a home. The majority of MIDEX incidents involve Fraud for Profit, or fraud or misrepresentation involving industry professionals.

Ninety-four percent of all incidents reported to MIDEX in 2011 were for loans originated prior to 2011. According to FinCEN, the increased number of SARS received in 2011 is related to the mortgage repurchase demands made on banks. As loans are repurchased, older loans are (re) investigated, resulting in more SARs for loans originated in prior years. Figure 4 shows this trend in detail:

Figure 4



Source: FinCEN, April 2012 Mortgage Loan Fraud Update

A detailed accounting of mortgage loan fraud SAR filings by activity starting date, Figures 3 and 4 seem to demonstrate the plethora of older loans being investigated as a direct result of both decreased new origination volumes and increased delinquency rates and repurchase demands.

Geographic Distribution of Mortgage Fraud

Tables 1 and 2 and Figure 5 on the next few pages present the states with the highest mortgage fraud indices (MFIs) based on incident reports submitted to LexisNexis. The first three columns of Table 1 show the rankings of states with the most serious mortgage fraud problems in loans investigated during 2011 (Investigation MFI). The remaining columns of the table show the rankings and a numerical measure for the same 10 states in preceding years, back to 2007.

Table 2 provides a different view of states with high volumes of reported fraud and/or misrepresentation. This table examines the rankings of states with the most serious reported mortgage fraud problems in loans originated during 2011 (Origination MFI). A subset of Table 1 above, the remaining columns of the table show the rankings and a numerical measure of the same ten states in prior years, dating back to 2007.

The numerical measure of each state's fraud problem is represented by the Mortgage Fraud Index (MFI). An MFI of 0 would indicate no reported fraud to MIDEX for a state. An MFI of 100 would indicate that the reported fraud for a state is level with expectations specific to fraud rates, given the number of loan originations for that state. That is, a state that has five percent of the incident reports submitted to MIDEX for 2011 and also has five percent of the country's loan originations in the same year would have an MFI of 100. Appendix II at the end of this report explains in detail how the MFI is calculated.

Based on incident reports submitted to LexisNexis through the first quarter of 2012, Florida's MFI ranked first in the nation for loans investigated in 2011.

Tables 1 and 2 detail how states rank against others for reported fraud and misrepresentation in the past five years. Based on incident reports submitted to LexisNexis through the first quarter of 2012, Florida's MFI ranked first in the nation for loans investigated in 2011. The reported fraud rate was over six times (MFI FL/2011 = 766) that of California for investigated loans. This is a slight increase from its updated fraud rate for loans investigated in 2010 (MFI FL/2010 = 732) and 2009 (MFI FL/2009 = 714). It is significant that Florida's Investigation MFI is in the 700s—that is over seven times the expected rate of fraud for the state, based on its origination volume. Compare this to Florida's Origination MFI, which is considerably lower: for loans originated in 2011, Florida ranks third with an MFI of 227—slightly over two times the expected rate of fraud and misrepresentation. This year's Origination MFI is the state's lowest in the five-year period detailed below.

Table 1

Mortgage Fraud Index (MFI) By State (2007-2011 All Forensic Investigations)										
State	2011		2010		2009		2008		2007	
	Rank	MFI	Rank	MFI	Rank	MFI	Rank	MFI	Rank	MFI
Florida	1	766	1	732	1	714	1	426	1	225
Nevada	2	290	3	225	3	219	6	165	3	202
Arizona	3	214	2	231	4	196	9	108	15	76
Michigan	4	188	5	178	2	254	2	191	2	220
Rhode Island	5	182	11	68	9	116	3	189	14	78
Georgia	6	145	4	185	5	150	5	167	6	162
California	7	124	6	141	6	130	4	187	4	185
Illinois	8	96	7	119	10	115	7	143	8	124
New Jersey	9	87	12	66	13	70	14	73	19	65
New York	10	82	14	63	8	120	12	83	11	95

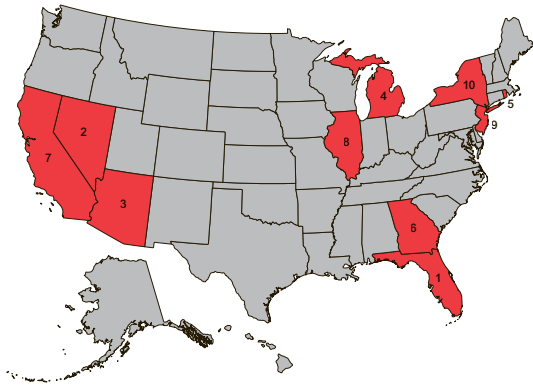
A subset of all investigations conducted in 2011 is that which involves loans also originated in 2011. The following listing ranks states based solely on these 2011 originations:

Table 2

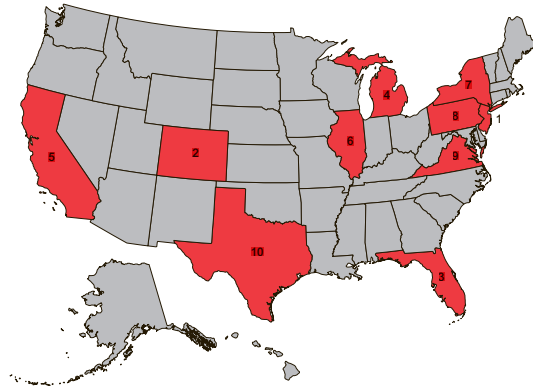
Mortgage Fraud Index (MFI) By State (2007-2011 All Originations)										
State	2011		2010		2009		2008		2007	
	Rank	MFI	Rank	MFI	Rank	MFI	Rank	MFI	Rank	MFI
New Jersey	1	293	9	145	8	161	11	105	20	57
Colorado	2	248	15	103	29	64	18	56	15	63
Florida	3	227	2	305	1	359	1	470	1	380
Michigan	4	223	13	112	7	163	4	173	3	180
California	5	178	5	215	12	125	5	159	4	150
Illinois	6	138	20	80	11	127	9	148	7	131
New York	7	125	1	331	3	262	7	154	23	51
Pennsylvania	8	124	35	14	34	44	37	25	38	27
Virginia	9	117	11	129	23	75	21	55	12	69
Texas	10	80	24	59	18	91	20	55	17	62

Figure 5

2011 Investigations – Top 10 States



2011 Originations – Top 10 States



It should be noted that the 2007 through 2010 MFI values for all states listed in Tables 1 and 2 differ somewhat from those shown in the same tables of last year’s Case Report. This is due to the fact that this year’s tables are based on an additional year of submissions, some of which were reported on loans investigated and originated in years 2007 through 2010.

Further analysis of Tables 1 and 2 and the maps in Figure 5 demonstrate that:

- Five states—Florida, Michigan, California, Illinois and New York—occupy space on both the Investigation and Origination Mortgage Fraud Indices.
- Georgia’s 2011 Investigation MFI fell to 145 from 185 in 2010. The state is not ranked in the top 10 for loans originated in 2011.
- Illinois’ 2011 Investigation MFI is 96; however, its 2011 Origination MFI is 138.
- Both New Jersey (293) and Colorado (248) had significantly higher Origination MFIs for 2011 loans than in previous years.
- New York’s Investigation MFI in 2011, at 82, is lower than what is expected based on the state’s loan volume. Its 2011 Origination MFI, 125, is a significant decrease from 2010’s 331.
- Prior to 2011, Pennsylvania scored low Origination MFIs, with numbers falling below expected amounts of reported fraud and misrepresentation. Its 2011 Origination MFI, 124, indicates that the state had 1.24 times the expected rate based on its volume of originations.

Closer analysis of the loan origination locations appearing most commonly on MIDEX reports for loans originated in 2011 yields five Metropolitan Statistical Areas (MSAs) that, combined, represent 46 percent of all reports received.

Table 3

Top National MSAs	Percentage of All Reports Received
Los Angeles-Riverside-Orange County, CA	16%
New York-Northern New Jersey-Long Island, NJ-NY	11%
Miami-Fort Lauderdale, FL	7%
Chicago-Gary-Kenosha, IL-IN-WI	6%
Denver-Boulder-Greeley, CO	6%

In first place for reported loans originated in 2011 is Los Angeles-Riverside-Orange County, CA. Sixteen percent of all MIDEX submissions included properties in this MSA. The New York-Northern New Jersey-Long Island MSA ranks in second place, with 11 percent of all reports submitted to MIDEX. In third place with seven percent is the Miami-Fort Lauderdale, FL MSA. The Chicago-Gary-Kenosha, IL-IN-WI and Denver-Boulder-Greeley, CO MSAs are tied for fourth place, with six percent each.

Types of Fraud Reported

The LexisNexis MIDEX system classifies the types of subscriber verified fraud and misrepresentation involved in each incident reported by its cooperating subscribers. These classifications are shown in Figures 6 and 7 for loans originated in the five-year period from 2007 through 2011. It should be noted that fraud perpetrated in 2011 will continue to surface and be reported for another three years or more.

Figure 6

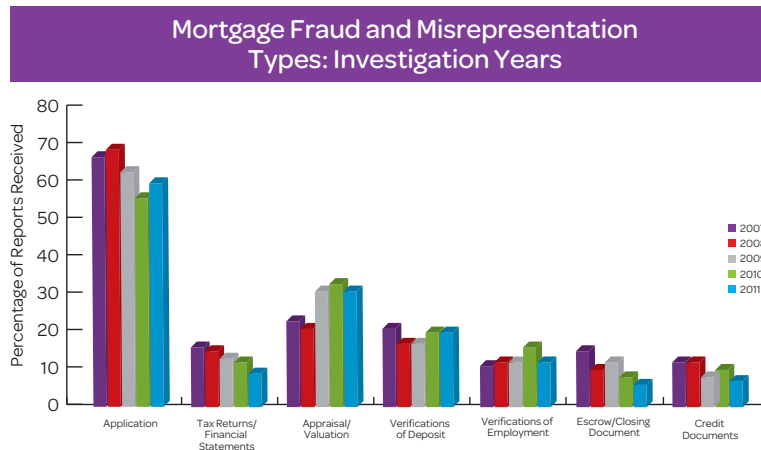
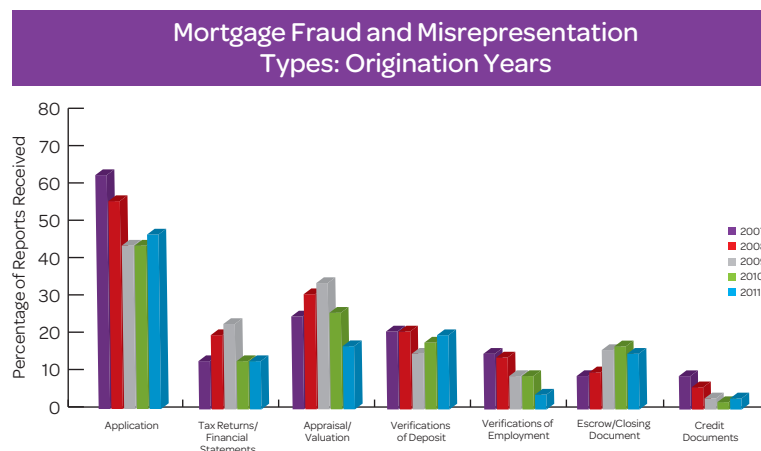


Figure 7



In a five-year fraud assessment, Figures 6 and 7 show each type of fraud and misrepresentation as a percentage of all incidents submitted to the

In first place for reported loans originated in 2011 is Los Angeles-Riverside-Orange County, CA. Sixteen percent of all MIDEX submissions included properties in this MSA.

MIDEX database. Note that the total percentage for each year exceeds 100 percent because most reported incidents involve more than one type of fraud or misrepresentation. Figure 6 contains fraud types broken down by investigation year, while Figure 7 shows a subset of this grouping, fraud types broken down by origination year.

Previous case reports have discussed the reasons for high numbers of reported Application misrepresentation. These percentages are hardly surprising, given that the application form is comprehensive in collecting borrower personal identity, employment, asset and liability information (all of which present verification challenges). Application fraud and misrepresentation includes, but is not limited to, the following categories on the loan application: incorrect name(s) used for the borrower(s); occupancy, income, employment, debt and asset misrepresentation; different signature(s) for the same name(s); invalid Social Security number(s); misrepresented citizen/alien status; incorrect address(es) or address history; and incorrect transaction type. Analysis of all loans investigated in 2011 shows a relatively stable 60 percent of all reports received having some type of Application misrepresentation or fraud. However, focusing on just those loans originated in 2011 reveals a lower number—only 47 percent of loans report Application misrepresentation or fraud. This is up slightly from 44 percent of originated loans in both 2009 and 2010.

Other trends include:

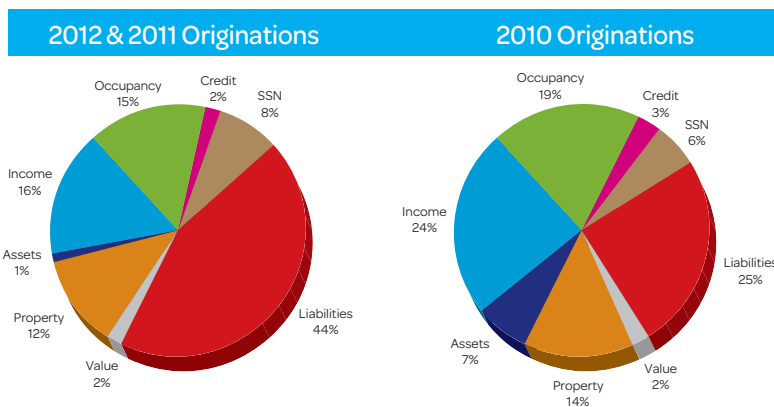
- MIDEX submissions for loans originated in 2011 report significantly fewer incidents of Appraisal fraud and misrepresentation than in previous years. At 17 percent in 2011, this type of misrepresentation is down from a high of 34 percent in 2009. In terms of all investigations completed in 2011, Figure 6 shows that the percentage of this type of misrepresentation has been relatively stable—31 percent in 2011, 33 percent in 2010, and 31 percent in 2009.
- Though reported Tax Return and Financial Document fraud and misrepresentation were down to nine percent for all 2011 investigations, they represented a higher percentage, 13 percent, in the pool of reported loans that were originated in 2011.
- The same trend is true for fraud and misrepresentation on Escrow and Closing Documents. While only six percent of all 2011 investigations reported this kind of misrepresentation, 15 percent of 2011 originations included it.
- The highest reported categories for all reported 2011 investigations are Application and Appraisal fraud and misrepresentation. The highest categories for reported 2011 originations are Application and Verification of Deposit (and other bank-related documentation) fraud and misrepresentation.
- Credit documentation fraud and misrepresentation for all reported 2011 investigations are down from previous years—seven percent in 2011, versus 10 percent in 2010, eight percent in 2009, and 12 percent in 2008 and 2007. Three percent of reported 2011 originations involve Credit Documentation misrepresentation.

Analysis of all loans investigated in 2011 shows a relatively stable 60 percent of all reports received having some type of Application misrepresentation or fraud.

- The most significant drop in reported fraud and misrepresentation for loans originated in 2011 is in Verification of Employment and Bank Statement Documentation. Only four percent of loans reported involved this type. Previous years reported nine percent (2010, 2009), 14 percent (2008), and 15 percent (2007).

Though broken down using slightly different categories than MIDEX, Fannie Mae's most recent analysis of 2011 originations includes some parallels to the reported incidents discussed above. In Figure 8, issues associated with Property were down to 12 percent in 2011, and misrepresentation of Income and Occupancy (two categories that are large parts of MIDEX application information) were also reported as falling from the previous year. Fannie Mae reports a significant jump in misrepresented Liabilities from 2010 to 2011/12—up from 25 to 44 percent.

Figure 8



Source: Fannie Mae, Fraud Findings Statistics, January 2012

In the coming years, as the industry continues to uncover and document fraud schemes such as Loan Modification Schemes, Short Sale Fraud and schemes involving Foreclosed Properties, it is expected that these types will soon join the categories noted above as among the most reported kinds of mortgage fraud and misrepresentation.

Collusion, The New Normal

Just as the financial world failed to realize the impact of Fraud for Profit until significant damage was done, the mortgage industry is now waking up to an increase in instances of collusion, the sophistication of these schemes, and the larger resultant losses. Fraud investigators and industry insiders know that fraudulent or misrepresented deals often do not involve just one person, acting independently. As the market has evolved, the obvious crush of fraud and misrepresentation in the foreclosure, short sale and REO worlds has forced the issue of collusion to the forefront.

The highest reported categories for all reported 2011 investigations are Application and Appraisal fraud and misrepresentation. The highest categories for reported 2011 originations are Application and Verification of Deposit (and other bank-related documentation) fraud and misrepresentation.

Consider the following trends from incidents reported to MIDEX in Figure 9:

Figure 9

Reported Undisclosed Non-Arm's Length Transactions in MIDEX Incidents



In Figure 9 and the discussion of reported collusion in MIDEX incidents, “collusion” refers to incidents of subscriber-verified undisclosed non-arm’s length transactions. While submissions with reported collusion among mortgage industry professionals in 2011 investigations (for any loan origination year) have fallen, it is significant that instances reported for loans originated during the past three years show increased percentages over previous years. Seven percent of MIDEX submissions for loans originated in 2009 reported evidence of collusion. For loans originated in 2010, that number rose to 9.7 percent, followed by 6.8 percent for 2011 originations. For previous origination years, reports contained a relatively constant percentage below five percent. This means that not only are more incidents involving multiple professionals being noted—but, as incidents submitted to MIDEX, they are being investigated, verified and reported. According to the FBI’s *Financial Crimes Report to the Public for FY 2010-2011*, “current investigations and widespread reporting indicate a high percentage of mortgage fraud involves collusion by industry insiders, such as bank officers, appraisers, mortgage brokers, attorneys, loan originators and other professionals engaged in the industry.” Because these complex relationships have traditionally been difficult and laborious to prove, more easily verified forms of fraud are reported instead. For this reason, the number of collusion schemes is likely to be considerably underreported.

Consider the facts for a case reported to MIDEX in 2011. Over a four-year period, 26 loans were originated by three loan officers at a single originating company. One of these loan officers was also an underwriter and approved several of the loans, while another of the loan officers was the seller on three of the loans. The loans contained inflated appraisal values and misrepresentation of income, employment, debts and occupancy. The same closing agent closed nine of the loans, each with misrepresentation on the HUD-1 Settlement Statement. The paralegal at the closing agency was also the owner of the real estate agency who worked 10 of the transactions. All 26 of the appraisals with inflated property values were prepared by three appraisal companies. Some of the appraisals also involved appraiser identity

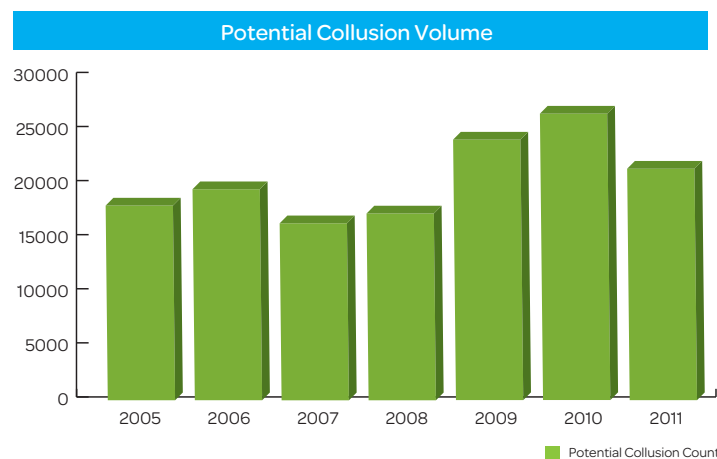
According to the FBI’s *Financial Crimes Report to the Public for FY 2010-2011*, “current investigations and widespread reporting indicate a high percentage of mortgage fraud involves collusion by industry insiders.”

theft. One of these appraisal companies was owned by a married couple, each of whom contributed to the inflated appraisals. This couple has the same last name as the seller of four of the properties. None of these relationships was disclosed on loan documentation.

The LexisNexis Collusion Indicator Index (CII) was created to help the mortgage industry better understand and pinpoint areas of potential collusion amongst buyers and sellers, saving them time and resources in investigations to detect and prevent mortgage fraud. The CII is a ranking of states based on factors indicative of potential collusion activity. Whereas the MIDEX data discussed above includes reported collusion activity perpetrated by mortgage industry professionals, data used in the CII highlights potential collusion activity by individuals without regard to profession. This data is an analysis of deed transfers where it has been determined that there is a potential relationship between the borrower and the seller—particularly, when a property has been transferred at a loss between relatives and known associates. These relationships are potential undisclosed non-arm’s length transactions, though it should be noted that a fraction of them could be disclosed and legitimate. Thus, the CII does not rank the amount of actual collusion activity in a state, but rather, the calculation of these relationships utilizes factors such as cohabitation, shared assets, business connections, as well as other complex criteria derived from public record data.

Based on LexisNexis property data as shown in Figure 10, on a national level, instances of possible undisclosed non-arm’s length transactions increased in years 2009 – 2011.

Figure 10



Judged purely by transaction volume, the amount of deed transfers that fit the criteria for potential collusion activity showed marked growth during these years. Though it could be argued that a large percentage of sales during the past few years included a loss—the sales included in this analysis also meet the non-arm’s length relationship criteria. These transactions often have a higher fraud risk element because of these relationships.

The LexisNexis Collusion Indicator Index (CII) was created to help the mortgage industry better understand and pinpoint areas of potential collusion amongst buyers and sellers, saving them time and resources in investigations to detect and prevent mortgage fraud.

Using relationship data in conjunction with deed transfer data, LexisNexis is able to identify the states with the highest potential collusion over the most recent five year period. This is accomplished in two ways in Tables 4 and 5: first, a wide-angle look at deeds where properties were transferred among individuals likely to be related with a 20 to 95 percent decrease in price; and second, a more focused look at deeds where properties were transferred among individuals likely to be related with a 50 to 95 percent decrease in price.

The first three columns of Tables 4 and 5 show the ranking of states with the most serious potential collusion activity. The remaining columns of the tables show the rankings and a numerical measure for the same 10 states in preceding years, back to 2007. The numerical measure of each state’s potential collusion activity is represented by the CII. A CII of 0 would indicate no discernible collusion for a state. A CII of 100 would indicate that the potential collusion for a state is level with expectations, given the number of recorded deed transfers for that state. Appendix III at the end of this report explains how the CII is calculated.

Table 4

LexisNexis Collusion Indicator Index (CII) By State Properties with a 20 - 95% Decrease in Sales Price										
State	2011		2010		2009		2008		2007	
	Rank	CII	Rank	CII	Rank	CII	Rank	CII	Rank	CII
Alabama	1	331	1	362	1	426	1	465	4	205
New York	2	224	3	234	4	267	7	301	7	155
Kentucky	3	178	6	199	6	206	13	166	14	104
Pennsylvania	4	176	4	219	3	276	4	357	6	179
Iowa	5	175	2	241	n/a	236	n/a	226	n/a	98
New Jersey	6	148	5	215	5	224	5	341	5	192
Wisconsin	7	137	8	179	8	181	11	201	10	132
New Mexico	8	127	7	199	2	368	n/a	458	n/a	178
Texas	9	123	15	120	16	135	17	142	22	66
Illinois	10	97	17	116	22	115	21	130	20	73

Table 5

LexisNexis Collusion Indicator Index (CII) By State Properties with a 50 - 95% Decrease in Sales Price										
State	2011		2010		2009		2008		2007	
	Rank	CII	Rank	CII	Rank	CII	Rank	CII	Rank	CII
Vermont	1	626	n/a	630	n/a	501	3	515	n/a	163
Alabama	2	493	1	394	1	516	4	437	7	147
Pennsylvania	3	357	5	273	6	332	8	308	10	113
Louisiana	4	344	9	208	8	304	9	301	n/a	101
Kentucky	5	334	3	318	4	376	12	269	13	103
New York	6	326	7	262	7	307	10	301	11	110
New Jersey	7	308	6	269	5	342	5	391	4	151
Iowa	8	274	8	227	9	258	18	170	24	60
Oregon	9	232	4	283	3	454	1	597	3	172
Washington, DC	10	216	28	91	14	207	15	188	21	66

Further analysis of Tables 4 and 5 shows that:

- Six states—Alabama, New York, Kentucky, Pennsylvania, Iowa and New Jersey—rank highly on both tables as areas with high percentages of potential non-arm’s length transaction activity.

- In Table 4, for properties transferred with a 20 to 95 percent loss, Alabama consistently ranks first. In 2011, its CII was 331, over three times what would be expected based on the state's recorded deed transfers. This number is highest in the five-year study in 2008, when the state had a CII of 465.
- In Table 5, for properties transferred with a 50 to 95 percent loss, Vermont's high percentages of potential non-arm's length transactions are notable. In 2011, the state's CII was 626. Vermont's CII's were also high in 2010 (630), 2009 (501) and 2008 (515), though for two of these years Vermont's sample size was not statistically rankable.
- In general, CII's are higher in Table 5 than in Table 4, which calls attention to the fact that the higher the loss (or discount) incurred at deed transfer, the more likely it is that there are potential non-arm's length transactions.

These statistics—warning lights for industry investigators—highlight the need to focus on all of the parties in a loan transaction. As shown in the data above, when significant percentages of deed transactions involve non-arm's length relationships, attention must be paid to these transactions.

Final Remarks

This New Normal, using public record data to predict risk and pinpoint potential collusion, requires that connections be made. Traditional sources still have value, but do need to be supplemented by emerging technology to address evolving fraud types. The key is to identify undisclosed relationships.

Huge monetary and reputational losses, an underperforming economy, and the large numbers of problem loans being serviced demand an enterprise approach to the business of fraud detection. Due diligence is required on the part of any participant in the industry of both its employees and any third party or vendor relationships. In today's loan transactions, credentialing should be composed of basic identity verification and in-depth research on the individuals and companies involved.

Appendix I

Source and Analysis of the LexisNexis Mortgage Fraud Data

The statistical data presented in Figures 5 – 7 and Tables 1 – 3 of this report were derived from information in a cooperative mortgage fraud database operated by LexisNexis. The Mortgage Industry Data Exchange (MIDEX®) contains information about licensing, public sanctions and incidents of alleged fraud and misrepresentation by mortgage industry professionals reported by MIDEX subscribers.

The MIDEX statistical data discussed in this document were derived from the incidents that MIDEX subscribers describe in reports to LexisNexis. (Agreeing to submit reports describing their fraud investigation findings to the non-public section of the MIDEX system is required for those who wish to access other subscribers' non-public reports.) Only material misrepresentations are permitted to be included in these reports. That is, companies only submit reports to MIDEX in those cases where, knowing what they know after thorough investigations, they would not have originated, bought or insured the loans in question.

The reports submitted to LexisNexis include the following information about each incident:

- Location of the collateral (state, city and address, to the extent known)
- Names of the originating entity and the loan officer who took the application
- Date the misrepresentation took place
- The method used to verify the existence of the reported misrepresentation(s)
- A short narrative description of the misrepresentation(s) found during the MIDEX subscriber's investigation

- Names of any other professionals who appear to be in a position to influence the accuracy of the information found to be misrepresented; e.g., the name of the appraiser and appraisal firm in cases where the property value is found to be significantly inflated
- A certification from an authorized individual at the submitting mortgage entity that the report is, to the best of his/her knowledge, complete and accurate

The LexisNexis staff reviews the reports to assure they meet submission standards for severity and consistency. Submissions are input directly by MIDEX subscribers via an online form, or data entry staffers convert hard copy submissions to a standard, searchable format for inclusion in the MIDEX system. After reading the report's narrative description, LexisNexis will classify the incident as involving one or more of the types of misrepresentations listed in Figures 6 – 7.

If LexisNexis makes any changes to a submitted report, it is returned to the submitting subscriber for review prior to its being entered into the system.

The subscribers participating in the MIDEX system represent a wide range of mortgage entities. They include secondary market agencies, major private mortgage insurance companies and lenders that account for the vast majority of wholesale lending in the country.

Appendix II Computation of the Mortgage Fraud Index (MFI)

The Mortgage Fraud Index, or MFI, is an indication of the amount of mortgage-related fraud and misrepresentation involving industry professionals found through MIDEX subscriber fraud investigations in various geographical areas within any particular year. It involves very straightforward calculations.

To come up with Tables 1 and 2's MFI for loans investigated and originated in 2011 in a sample state (e.g., Florida) the LexisNexis staff determines the percentage of all MIDEX fraud reports that were submitted for loans originated on properties located in Florida in 2011. They determined that, to date, 8.74 percent of MIDEX reports submitted from across the country by subscribers for 2011 originations involved loans on Florida properties. But according to HMDA data, Florida had 3.85 percent of the nation's total 2010 mortgage originations—the most recent year such data are available.

If mortgage fraud and misrepresentation by industry professionals were distributed throughout the country like originations, then we would expect approximately 3.85 percent of such mortgage fraud to occur in Florida. But the 8.74 percent MIDEX fraud figure for Florida in 2011 was over two times its origination figure. Therefore, the 2011 Origination MFI for Florida, as of this report's date, is:

$$\text{MFI FL/2011} = (8.74/3.85) \times 100 = 227$$

This is, of course, a dynamic figure. Often, a fraud investigation is not completed until a year or two after the loan was originated. LexisNexis will continue to receive Florida fraud reports for another two to five years from its MIDEX subscribers that find misrepresentation in their 2007-2011 books of business. Therefore, Florida's (and all other states') MFI figures will continue to change somewhat in future Periodic Reports, especially those containing recent years like 2010 and 2011.

It should be noted that the MFI is based on the number of fraud and misrepresentation incidents reported for each state, and not the dollar amounts of those mortgages. Therefore, a fraud on a \$120,000 loan in Birmingham, Alabama, is counted the same as a fraud on a \$720,000 loan in Los Angeles, California. Also, there is currently no distinction made between purchases, refinances or home improvement loans in these figures.

Appendix III

Source and Analysis of the LexisNexis Collusion Indicator Index (CII)

Identifying potential relationships between borrower and seller entities connected with a property transaction is a calculation that leverages a parallel-processing computing platform from HPCC Systems to perform large scale graph analytics and contains roughly 4 billion relationships between 283 million active identities. During the analytics process that calculates potential collusion, it expands to 140 billion data points.

The CII in Tables 4 and 5 are determined by the percentage of deeds believed to involve individuals in non-arm's length relationships using the data described on the prior pages. For example, for properties with a 20 – 95 percent decrease in sales price in 2011, Alabama's CII is 331. To date, .8130 percent of deeds with potential collusion identified across the country involved Alabama properties. But according to recorded deed transfer data, Alabama had .2456 percent of the nation's total deed transfers in 2011. If this potential collusion activity were evenly distributed among states, we would expect approximately .2456 percent of potential collusion activity to occur in Alabama. But the .8130 percent collusion figure is over three times its deed transfer figure. Therefore, the 2011 CII for Alabama, as of this report's date, is:

$$\text{CII AL/2011} = (.8130/.2456) \times 100 = 331$$

Foreclosures and quit claims have been excluded from calculations, as have any transactions under \$10,000.

For more information:

Call 866.858.7246 or

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