

# Mortgage Advice

## Don't Be an Unwitting Accomplice to Fraud

by: Chuck Simmons

Many people are blaming the financial crisis on the sub-prime mortgage industry. A "sub-prime" loan is a loan made to a borrower who is unable to qualify for a traditional mortgage because they don't meet specific criteria. The term "sub-prime" is most closely associated with below average credit but it can also be used to describe someone who can't verify income or assets. The main issue with the mortgage crisis did not have to do with people with bad credit as much as it had to do with those who were able to obtain mortgages without providing the necessary documentation to verify their financial worth or ability to repay the loan. This opened the door for unscrupulous originators and even some borrowers to falsify information in order to "trick" underwriters into thinking the borrower met all qualifications when, in fact, they did not. Borrowers were able to secure loans with low introductory rates that they normally could not afford.  As soon as the introductory period was up and the payments increased, borrowers could no longer make payments.  In most instances, the borrowers in these cases did not know that inaccurate information was being used and that the originator qualified them under false pretenses. Could this have been prevented? Yes.

> "Borrowers need to know what to look for and need to speak up when things don't seem right."

Below are a few instances where an alert borrower can stop fraud from happening and ensure they don't end up being another unsuspecting foreclosure statistic.

**Income Adjustments**

There used to be loan programs that did not require any sort of income verification. If a borrower's credit was good enough and they had some money to put down, the underwriter would approve the loan based on information on the application. That means that if the borrower didn't make enough to qualify for that $200,000 house but had good credit, the originator could raise their income on the application to try and gain an approval. No further verification was needed. These days, this is hard to get away with because most loan programs now require verification of all income sources. However, if an originator tells you they need to adjust your income in order to get you qualified, or if the loan documents you receive at application have an income amount higher than what you make, you need to ask more questions and find out what the originator is doing.

**Phantom Funds**

In addition to not verifying income, many of these programs also did not require verification of a borrower's assets. This meant that underwriters would accept whatever assets were stated on an application as being valid. Some loan programs required that a borrower have a certain percentage down or a certain amount left in reserves (such as a savings account) in order to qualify. Since no verification was needed, originators who had a borrower with good credit, but who perhaps did not meet the asset requirements would simply make up bank account names and numbers and enter random balances. This is also very hard to get away with, but is worth noting to make sure borrowers are always looking through their loan documents to verify assets are listed correctly. It is possible that an originator will not need to use every asset a borrower has to qualify, but all assets that are listed must be checked for accuracy.

**"Silent" Second Mortgages**

A question that still lingers is how a borrower with no down-payment can qualify for a loan where income and assets do not need to be verified. They can't. I am not aware of any programs that ever allowed borrowers to obtain loans for 100% of the purchase price without verifying income and assets. Yet it happened more often than you would think. How? Originators would prepare an application with all of the information they knew an underwriter would need to approve a loan. The application would have the right amount of income listed and more


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than enough assets. Since the application reflected a qualified borrower, the underwriter did not need to verify the income or source of funds to close. The originator would then help the borrower obtain secondary financing for the required down payment from a different source. This got the name "silent second" because the underwriter never knew the borrower was getting a loan for the down payment and would not have allowed it. If the HUD-1 Settlement Statement you sign on your first mortgage does not list any secondary financing, chances are your underwriter is not aware that you have that loan and would not allow it. Be sure to check your final documents to verify all sources of financing are listed on one HUD-1 Settlement Statement.  If not, there is a chance your originator is not being forthright with the underwriter.

These are just a few of the creative ways unscrupulous originators have used to commit fraud. As a borrower, you should always be wary of things that don't look right. If it seems too good to be true then chances are it is. If you are ever unsure of something an originator tells you, always double check with another source. Being a vigilant and informed borrower can help make sure you get into a house you can afford and will ensure that the dream of homeownership does not turn into a financial nightmare.

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