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Is There a Wolf at Your Closing Table?

Be prepared to protect your company against closing-table fraud



Illustration: Dennis Wunsch

Across the industry, mortgage bankers have done a good job seeking out and incorporating new risk-management processes and technology to help uncover and deter mortgage fraud. Bankers often even collaborate with private companies that have developed risk-deterrence and fraud-detection software. In the past several years, the advent of automated-valuation models, identity verification technology and automated loan underwriting tools have helped reduce the cost of fraud in the mortgage industry as a whole.

Indeed, mortgage bankers and lenders seem to have covered all aspects of the loan-manufacturing process except for one: the closing table. This failure to incorporate meaningful risk-evaluation and deterrence tools at the back end of the loan process threatens to dampen the

many advances made in fraud detection and prevention.

In fact, fraud surrounding the escrow, title and closing processes is growing — not retreating. The FBI estimates that of the \$13 billion in mortgage fraud losses expected for 2012, about 15 percent of that amount (approximately \$2 billion) will be attributable to the closing table. In addition, a July 2012 report from the Financial Crimes Enforcement Network examining suspicious-activity reports filed between 2003 and 2011 reflected that fraud in this area is a growing concern, advancing 20 percent in the most recent reporting period.

Rules and regulations

Pressure to address this trouble has come mainly from government regulators, who have warned the industry about this risk for

many years. For instance, the Office of the Comptroller of the Currency announced in November 2001 that national banks were expected to oversee and manage their third-party relationships, an expectation that entails risk assessments, due diligence and ongoing oversight of their partners'

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activities. Likewise, in a December 2005 report on preventing, detecting and reporting mortgage fraud, Fannie Mae states in part that mortgage lenders must “know [their] business partners ... and consider using outside sources to ... selectively choose closing attorneys and settlement agents.”

Those aren’t the only entities weighing in on these matters. In 2007, for example, the National Credit Union Association acknowledged that third-party relationships are essential, but also warned that inadequately managing and controlling such relationships can cause a variety of problems, including legal disputes and financial losses. Although the agency said that it doesn’t want to “stifle the innovative use of third-party relationships to meet member needs and strategic objectives,” it emphasized the necessity of understanding risks and adequately controlling those risks, as well. Finally, this past April, the Consumer Financial Protection Bureau appeared to extend supervised-bank mandates to non-bank entities regarding their third-party service-provider risk management.

With all of this in mind, today’s mortgage bankers have to ask themselves questions, even in this risk-averse climate: Does my organization really know enough about its closing agents? Who are these agents? Are they experienced? Licensed? Insured? Do we care? Should we care?

Preventing fraud

Closing-table fraud involves many of the same elements as mortgage fraud at the origination stage, except that those who conspire to commit this type of fraud tend to fly under a lender’s radar screen. Realtors, sellers (including builders) and

closing agents have little contact during the loan origination because they do not participate in the loan-application process.

They do, however, play an enormous role in the real estate transactions that are the basis for mortgage loan transactions. Improper and illegal collaboration among borrowers, sellers, Realtors and closing agents creates an equally dangerous and costly scenario as any other fraud scheme. Foreclosure rescue scams, short-sale fraud, fraud for profit and Federal Housing Administration 203(k) loan-program fraud frequently require the complicity of attorneys, title agents, escrow agents, notaries and others who have an obligation to consumers and banks to act with fiduciary care, yet have no uniform standards or singular body for oversight.

Every day, mortgage bankers and lenders wire hundreds of millions of dollars into the accounts of borrowers and settlement companies about which they know very little. While they wait anxiously for their signed closing packages to return, their money lies exposed “on the street,” without guarantees of security. In addition, the cost of fraud has a heavy impact on consumers, not only when it comes to personal losses but also in regards to the impact it has on increasing the costs that surround the mortgage process.

Although there is no fool-proof method of preventing fraud — as fraudsters tend to change their tactics and methods regularly — mortgage bankers and lenders can arm themselves with more data about the closing process. They also should demand that their closing agents meet certain minimum levels of experience, insurance and overall reliability. Shining a light on the closing process and those who work with it can go a long way toward weeding out

the bad operators and defining a better process for the honest and orderly distribution of mortgage funds. Furthermore, in today’s fraud-infested environment, it’s highly desirable to have access to real-time data about the parties at the closing table and immediate access to key closing documents. It’s also desirable to have the ability to access detailed reports about a closing when audits or loss-mitigation efforts are required.

In short, closing-table data and fraud deterrence are readily available. There are online solutions that combine closing-table data collection, warehousing and reporting functions with closing agent registration and transaction-recording features that can help you close the gap between front-end fraud protection and back-end vulnerability to fraud. There are also third-party closing agent verification services that quickly can verify the credentials of the “professional” to whom mortgage bankers and lenders are wiring their closing funds.

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Closing-table fraud remains a glaring problem that has yet to be addressed seriously. With the financial industry facing what appears to be the last part of the mortgage process without adequate fraud protections, there is no room for error when it comes to covering all of your the bases in the fight against fraud.

Now is the time to incorporate the practices and procedures necessary to eliminate this type of fraud when the next housing boom occurs. Every Realtor, seller, closing agent and lender will only flourish under this protection as the bad actors are weeded out, consumer confidence grows in the process and insurance premiums drop from reduced incidents and claims. ●