Mortgage fraud: Good practice guidance note

Contents

1 Introduction

1.1 Intent and status of the guidance

This guidance note has been produced in consultation with members to assist lenders in identifying and mitigating possible vulnerabilities to fraud in the mortgage lending process.

It takes into account:
- The FCA's regulatory guide, *Financial Crime: A guide for firms* (first published December 2011)
- The FCA's June 2011 thematic review of lenders' systems and controls against mortgage fraud
- The Mortgage Conduct Of Business rules
- Previous versions of this guidance

The introduction provides the background to the problem of mortgage fraud that will be useful to newcomers to the issue. Good practice guidance and more detailed issues are dealt with in the remainder of the document.

The FCA has been consulted on this guidance and is aware of its contents.

The guidance has no regulatory status and some of the examples of good practice given may not be appropriate for all firms.

1.2 Background

Mortgage fraud tends to be cyclical in nature, exploiting weaknesses in regulatory mechanisms, in lenders' own systems and controls, government policy and within the conveyancing process.

In the past, for example, changes to government planning policy led to the development of a large number of centre-city flats, spawning the selling of the flats in bulk to individual investors or property investment clubs. Organised criminal gangs seek to take advantage of this market to artificially inflate the value of these apartments and gain the difference as profit. The mortgage industry's response led to a tightening of processes and controls in the valuation and conveyancing process, notably with the creation of the Disclosure of Incentives form, which must be completed by the conveyancer and is designed to draw all the relevant information about newly built, converted and renovated property transactions into a single form, to enable transparency about the transaction.

In more recent times, following the economic downturn in 2007-2008, significant levels of solicitor fraud were uncovered. Lenders responded by reviewing and implementing far more robust checks on conveyancing representatives.

The regulatory approach can often impact on the levels of fraud. Currently, mortgage brokers and intermediaries are regulated by the FCA, although on a company and not individual basis. The ability to hide behind a firm level regulation has been exploited by some individuals. The decision by the regulator to extend the Senior Managers and Certification Regime (SM&CR) to mortgage brokers may be significant. To combat intermediary fraud, the FCA strongly encourage lenders to report brokers via the 'Information from Lenders' scheme, further details of which are included at the end of this document.

With lenders increasingly relying on automated fraud detection systems, particularly at application process, it is likely that fraudsters will seek to develop sophisticated techniques to counter this and/or find other areas of weakness in the mortgage and conveyancing process. Lenders will need to ensure that these systems are backed up by complementary checks and controls.

1.3 What is mortgage fraud?

The **Fraud Act 2006** [1] introduced a general offence of fraud that can be committed in three ways:

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[1] http://www.opsi.gov.uk/Acts/acts2006/pdf/ukpga_20060035_en.pdf

- Fraud by false representation
- Fraud by failing to disclose information where there is a legal duty to do so
- Fraud by abuse of position

Dishonesty is a required element and the offence carries a maximum sentence of 10 years' imprisonment.

There are two broad categories of mortgage fraud:

- Mortgage fraud for property. Usually committed by an individual, in order to obtain a mortgage on a property on more favourable terms than they would otherwise have been able to attain, through, for example, the exaggeration of their income on the mortgage application.

- Mortgage fraud for profit. This is financially motivated and usually perpetrated by a 'fraud ring' involving more than one individual, with the intent of defrauding the lender of large sums of money. Though this is less common than frauds for property, it has a much greater impact as often there are links to other serious organised crime. It is likely to result in much greater losses for the lender and is inherently more difficult to detect.

There can be instances of overlap between the two categories, for example amassing a buy-to-let portfolio. More detail of how these frauds are perpetrated is outlined at section 1.5.

Mortgage fraud can involve more than one criminal act, whether it is fraud and/or money laundering. Fraudsters may indeed be prepared to make a loss on a transaction to successfully launder their criminally obtained money. Post the financial crisis there has been an increase in broader criminal acts such as theft of the mortgage monies, often involving sophisticated cybercriminals who will target buyers or the buyer's solicitors through the mis-direction of mortgage or deposit monies to an alternative bank account (so-called 'push' fraud). Further validation checks are being considered by those who operate payment systems in the UK.

Where a mortgage has been obtained fraudulently, the value of the mortgage represents proceeds of crime or criminal property. Any person who then acquires, uses, has possession of, enters into an arrangement with respect to or transfers the criminal property, will be at risk of engaging in money laundering under the Proceeds of Crime Act 2002 (POCA).

POCA contains three principal money laundering offences:

- concealing, disguising, converting, transferring or removing criminal property from the UK;
- entering into or becoming concerned in an arrangement in which someone knowingly or suspects facilitates the acquisition, retention, use or control of criminal property by or on behalf of another person; and
- acquiring, using or possessing criminal property.

The maximum penalty for any of the principal money laundering offences is 14 years imprisonment.

1.4 Firms' regulatory responsibilities

Firms must have due regard for the FCA's conduct requirements. The FCA's Principles for Businesses require that a firm must:

- 'conduct its business with due skill care and diligence' (Principle 2),
- take 'reasonable care to organise and controls its affairs responsibly and effectively, with adequate risk management systems' (Principle 3) and
- 'must deal with its regulators in an open and co-operative way, and must tell the FCA promptly anything relating to the firm of which the FCA would reasonably expect prompt notice' (Principle 11).

The Systems and Controls chapter of the FCA's Handbook of Rules and Guidance requires firms to establish policies and procedures to ensure compliance with obligations under the regulatory system and for countering the risk of financial crime. Lenders must detail within their responsible lending rules how they incorporate anti-fraud controls into their affordability assessments. Firms are also obliged to notify the FCA of significant fraud, errors and other irregularities under the supervision manual of the FCA's Handbook.

Some measures taken by lenders may also be necessary to meet their obligations under the Money Laundering Regulations 2007.

The FCA's thematic review of firms' mortgage fraud systems and controls, published in June 2011, identified a number of good and poor practices.

Guidance from the review is included in a regulatory guide, Financial Crime: a guide for firms which was first published by the FCA in December 2011 updated most recently in April 2015. The guidance, like the thematic findings, does not contain rules and imposes no new requirements on firms. The guidance is non-binding. However, it does give guidance on how firms can assess and improve their existing approaches to meeting their legal and regulatory obligations with respect to financial crime.

The guidance is not designed to replace or supersede any of the existing regulatory conduct rules and guidance. The FCA asked firms to consider it and the findings of the thematic review and translate them into more effective policies and controls where necessary. The thematic focused on the following areas:

- Governance, culture and information sharing – firms should consider how management information can be improved and used more effectively to mitigate mortgage fraud.

- Applications, processing and underwriting – firms needed to consider whether underwriting resource was sufficient to ensure rigorous scrutiny was applied to mitigate fraud risks. The FCA identified niche business (including buy to let and sub-prime) and continue to be concerned that lenders ensure 'fast-track' loan processes are not abused.

- Managing relationships with third parties - the FCA saw scope for improving the management of third parties, particularly broker relationships. They consider it good practice for a firm to centralise responsibility for overseeing all third party relationships, and to carry out appropriate auditing of outsourced panel managers (e.g. an intermediary network).

- Compliance and internal audit – the FCA were concerned to find that very few lenders internal audit and compliance teams regularly monitored the adequacy of underlying customer take-on arrangements, the application process or third party relationships.

- Staff Training and awareness – the FCA see scope for improving internal training to focus specifically on mortgage fraud.

- Mortgage fraud prevention, investigations and recoveries – the FCA stressed that engagement with the IFL scheme was good practice, and noted scope for firms to clarify how reporting of frauds should be made and when, and improving understanding of exposure by undertaking back book reviews.

- Remuneration structures – Firms should consider how they incentivised those staff who prevented mortgage fraud.

The FCA have been careful to stress that firms should apply the examples of good and poor practice in a risk-based, proportionate, outcomes-focused way.

1.5 How does mortgage fraud occur?

1.5.1 Opportunistic (Fraud for Property)

This is undertaken by individual buyers where they obtain a higher value mortgage that they would normally have been granted or entitled to. This is committed by providing inaccurate, untrue or misleading information about their personal circumstances and/or the transaction or by failure to disclose. This may include false or misleading information about:

- Previous credit history (e.g. undisclosed CCJ's, defaults)
- Proposed residency of the property

- Income
- Employment
- Identity
- Source of funding for the purchase (e.g. monies for the deposit)
- Value of the property
- Purchase price and any payments to be made directly between seller and purchaser.

This list is not exhaustive.

There is an increasingly prevalent risk to lenders from the use of false documents obtained from the internet. The wide availability and quality of 'novelty' documents includes pay slips and P60s used to prove income, utility bills used to prove address and bank statements used to prove income and address.

In such circumstances, the fraud is committed to obtain a mortgage product which the borrower would not otherwise be entitled to, known as 'fraud for property'. This type of exploitation of products and lending criteria within the market is likely to always be present in some form, though the extent will vary according to market conditions. The predicate offence here is one of "fraud by false representation" as defined by the Fraud Act 2006. There is also however, a parallel offence of Money Laundering under POCA 2002.

Fraudsters may also seek to obtain access to government-led schemes (such as the Help to Buy or Right to Buy schemes) claiming eligibility under such schemes but producing evidence of income and circumstances to a lender which do not correspond.

1.5.2 **Organised (Fraud for Profit)**

Many cases of mortgage fraud are perpetrated by organised crime syndicates for the purposes of obtaining the mortgage advance. Such cases are generally more sophisticated than opportunistic frauds and the scale of the fraud much larger. This is known as 'fraud for profit'.

Criminal syndicates will often organise finance on a number of different properties at any one time. New-build apartment developments or large scale renovation projects have historically been attractive targets for organised crime gangs as they are able to buy in bulk with the opportunity to negotiate discounted prices and then obtain mortgages at higher values. Both buy-to-let mortgages and standard residential mortgages have been used in such frauds. Commercial properties may also be involved.

The nominated purchasers (who apply for the mortgage) can range from genuine purchasers, 'mortgage mules' – who are duped or coerced into the purchase – to complicit individuals or totally fictitious purchasers that rely upon false identities.

When the mortgage provider seeks repossession of the property, the criminal syndicate may raise additional mortgage funding from a different lender, effectively selling the property back to themselves.

As the second mortgage has been further inflated, the first mortgage is repaid together with any arrears. This leaves the crime syndicate with a substantial profit. The process can be repeated many times, until a lender forecloses on a property, to find it in disrepair and worth significantly less than the outstanding mortgage.

Alternatively the organised fraudster may never make a loan repayment at all. In this scenario, as the lender institutes proceedings to re-possess the property, it may be rented or let, creating additional income for the fraudster.

Corporate structures may sometimes be used instead of fictitious buyers, where the property in question is sold between related private companies at inflated values.

1.5.3 Use of professionals

Organised criminal gangs will often involve at least one naïve, negligent, coerced or complicit professional in the mortgage process, to provide reassurance and direction to the other professionals who are involved. There is evidence that lender staff, mortgage brokers/introducers, valuers, accountants, and solicitors/conveyancers have all been used in this way.

1.5.3.1 Intermediaries

Typically, intermediary-led fraud includes the presentation of false or inaccurate information to lenders in order to obtain a mortgage, failing to satisfy authorisation checks, and ‘gaming’ lender systems; including making multiple applications to lenders to secure advances.

1.5.3.2 Valuers

Typically this type of fraud will involve collusion of the valuer to distort the value of the property being purchased, in order to obtain a higher value advance from the lender. This can include a fraudulently inflated valuation, the non-disclosure of incentives to the purchaser which may distort the true value of the property, valuation of a non-existent property, and avoidance of stamp duty.

1.5.3.3 Solicitor/conveyancers

This can take a variety of forms including complicity with other professionals in the conveyancing transaction, (e.g valuer) material non-disclosure of information about details of the transaction to lenders which allows a fraud to occur, or takeover of client account details in order to misappropriate funds.

1.5.3.4 Accountants

Accountants can assist in perpetrating frauds by assisting in falsifying financial information or creating documentation in support of a fictitious person or company or otherwise.

2 Mortgage fraud risk areas and mitigation

Risks relating to six main areas associated with mortgage lending and processes are detailed below, including good practice for mitigating the risks.

- Application
- Account management
- Recovery of losses by lenders
- Lender controls
- Managing third party relationships
- Regulatory controls

2.1 Application Stage

2.1.1 General

Following an accepted offer to purchase the property and ‘agreement in principle’, the borrower will make a full mortgage application. This can be done currently on an advised or non-advised basis, which is the decision of the borrower, though the non-advised route is limited by virtue of the incorporation of the Mortgage Market Review (MMR) into the Mortgage Conduct Of Business (MCOB) rules. The lender will require detailed information before deciding whether, and how much, to lend to the borrower. Lenders usually require the following information as a minimum:

- Proof of identity
- Proof of current address
- Previous address history, if they have not been at their current address for a period of time, usually three years
- Anti-impersonation check, if the mortgage is applied for in a non face to face environment, e.g. telephone or internet sales
- If employed, proof of income from the employer (usually in the form of the three most recent payslips and the P60 form)
- If self-employed, copies of audited accounts (usually for the previous two financial years) and the relevant HMRC forms.
- Details of any previous/current mortgages/loans
- Details of the borrower’s wider financial circumstances (dependants, other sources of income, overtime, bonuses, outstanding personal finance agreement and credit cards, general monthly income and expenditure via bank statements, adverse credit such as CCJs defaults, repossessions etc)

The lender’s assessment of the borrower’s ability to repay the loan will take account of affordability and the borrower’s credit history and credit profile. The Mortgage Verification Scheme allows a lender to check an applicant’s stated income against the records held at HMRC and is an important tool in income verification checks. This scheme is not compulsory, however many lenders use the scheme.

Buy-to-let products are underwritten by the rental income that the property can command rather than the income of the borrower, although increasingly lenders will look at a borrowers’ income as part of the broader underwriting process.

The main areas of risk at application stage are detailed in the table below.

2.1.2 Application risk areas (Risks from the borrower and related third parties)

Fraud offences (under the Fraud Act 2006)

Area of Risk	Detail	Good Practice
Income/Employment details of applicant	Most lenders require three months evidence of regular income (or two years worth of accounts for self-employed applicants). In many cases of mortgage fraud, the income of the buyer will be totally fictitious or will have been inflated (whether acting alone or on the advice of a broker) in order to create an illusion of affordability that is much higher than reality. In order to evidence this supposed 'income', payslips and accounts will be falsified as part of the mortgage application. Lenders need to ensure that income information is appropriately verified, complying with the regulatory requirements around checking affordability.	Lenders could obtain evidence of income direct from the stated employer instead of relying on the applicant to provide it. Although labour intensive and not fool proof (i.e. fraudsters could still work the system by providing the name of an associate to verify their employment), it may reduce instances of falsified employment information. The lender can also look at the credit history of the individual to determine if they have met payments on other credit accounts as a guide to their income level and their propensity to repay. Lenders should verify income independently of applicant. Lenders should verify the stated rental income potential. The lender may also wish to request an applicant's permission to approach their tax office to confirm their earnings, or utilise the Mortgage Verification Scheme to check HMRC income data as verification against information supplied by the mortgage applicant where they suspect fraud. Lenders should consider how automated fraud detection systems may assist in the application process. Lenders should consider what tools are available to detect and deal with fake documentation.
Brokers/Introducers	The majority of high street lenders will work with a panel of approved brokers who act on their behalf to sell their mortgage products. Past experience indicates that there are increased risks of fraudulent behaviour in those mortgages where introduction by a broker is a feature. It is likely that a number of brokers will be complicit in some of these frauds. Proving broker complicity can be difficult.	Although brokers are usually put through a Know Your Customer (KYC) process when first 'approved' by a lender, this should not be regarded as a one-off exercise. Due diligence and audits/quality checks should be carried out on all brokers on the panel on an ongoing/regular basis, using a risk-based approach. This could include open source searches of the broker's public information, and physical office visits on an appropriate basis. For removing dormant intermediaries, lenders should have in place suitable,

		risk-based processes which reflect the size of the firm and the amount of dormant intermediaries. KYC processes may include checking the firm and its staff against fraud databases such as Hunter/SIRA and CIFAS. It is not enough to rely on the FCA register, as this only a 'snapshot'. Where a lender has cause to remove a broker from their panel for fraud or suspected fraud this should be reported to the FCA, via the Information from Lenders scheme set up 2006 in conjunction with the CML. Lenders should encompass IFL within their processes and procedures so that it can be used when necessary. Lenders should, where practicable, ensure that the broker is flagged on Hunter/ SIRA/ CIFAS. Ideally, lenders should share details of the firms (intermediaries, conveyancers and valuers) they have removed from their panels through these processes. Lenders and brokers have agreed a joint guidance on panel removal
Solicitors/Conveyancers	As with brokers, most lenders will have an approved panel of conveyancers, made up of solicitors and licensed conveyancers. Historically, in England and Wales, the panels were very broad, with limited due diligence checks. However, most lenders have now undertaken a review of their processes to appoint legal representatives, with many lenders introducing more robust checks on their panel firms, as a result, either by undertaking these checks themselves or using a panel manager to do so Most lenders use standardised instructions for all solicitors acting on the behalf of lenders via the CML Lenders' Handbook. The handbook is split into two parts; part one is standardised across the industry and is agreed with the relevant law society and the Council of Licensed Conveyancers. Part two is specific instructions that individual lender can amend. There are different handbooks for the different jurisdictions within	Due diligence should be carried out on solicitors at the onset of relationship and audits/quality checks on an ongoing/annual basis. Part of this due diligence can include checking whether a solicitor is accredited under relevant accreditation schemes such as the Law Society of England and Wales' Conveyancing Quality Scheme. Lenders should consider reducing the size of their panels in order to allow adequate KYC procedures and audits to be carried out – i.e. to have manageably sized panels. The FCA stressed this point in their recent thematic review of mortgage fraud. Lenders should ensure that their Part 2 of the handbook is up to date with their own requirements and is not open to fraud. Where a lender receives a request to change the conveyancing solicitor mid-way through the transaction process they should ensure that they contact the original solicitor and the borrower to confirm that this is correct. This can often be a sign of 'hijacking' the genuine solicitor's details in an attempt to abscond with the mortgage funds.

	the UK. Mortgage fraud against new-build properties, as outlined above, will require the conveyancer to either be negligent or complicit in the fraud (i.e. the non-declaration of transaction details to the lender). Conveyancer 'take-over' or hijacking fraud is common, whereby a transaction will commence and a conveyancer is appointed. Half-way through the process the lender and or/buyer will be contacted by a new solicitor, with all the details of the transaction, saying they are taking over the conveyancing process. The new 'conveyancer' will then, a week or so later, drawn down the funds. The original conveyancer will then contact the lender saying that the transaction is ready to complete and ask for the funds again. At this point the lender and or buyer will become aware of the fraud. Increasingly cybercriminals have been gaining sensitive client or conveyancer details by hacking email accounts and posing as conveyancer to mis-direct mortgage or deposit monies. Proving that solicitors/conveyancers are complicit or negligent can be difficult.	Solicitors are regulated by the Solicitors' Regulatory Authority (SRA), who have guidance regarding mortgage fraud. The Law Societies and the Council of Licensed Conveyancers also produce guidance about mortgage fraud for their members. Where a lender suspects or can prove that a legal professional is involved in mortgage fraud they should report them to the appropriate regulator, and where appropriate, law enforcement agencies. The Law Society and the SRA have issued warnings to their members about recent cyber-frauds targeting conveyancers. Lenders may wish to check the robustness of their panel firms' cyber security.
Valuations	Obtaining an accurate valuation is a critical aspect of the mortgage process. Lenders will use the valuation to calculate the level of the loan they offer which determines the risk and pricing of the deal. The majority of lenders outsource this work to a private company through 'panels'. Lenders will audit valuers once or twice a year to ensure standards are maintained. All valuations are undertaken according to the professional standards required in the Royal	Due diligence should be carried out on valuers at the onset of relationship and audits/quality checks on an ongoing/annual basis. Lenders should review their instructions to valuers to ensure that they are robust and are not open to fraud. This may include the following: (a)requiring the receipt of the CML Disclosure of Incentives Form for new-build, or conversion valuations; (b)Monitoring for trends such as Below Market Value transactions;

	Institution of Chartered Surveyors' (RICS) Red Book, subject to specific lender requirements. The Red Book requires valuers to use comparable evidence in support of their valuation. Similarly with conveyancers, lenders can give specific instructions to valuers over and above the Red Book. Obtaining comparables for new-build properties in regeneration areas can prove difficult, and has been a factor in the recent frauds. Where a valuer is complicit in fraud it is likely to lead to significant losses for lenders. As valuers visit the properties it is possible for fraudsters to intimidate them into producing inflated valuations. Due to the importance of the valuation in the lending process, negligence can also lead to significant losses for lenders. It is difficult to prove if a valuer is complicit in a fraud.	(c) The name of the person in attendance at the time of the survey is provided on the valuation form; and (d) The valuer obtaining the name of the vendor and including it on the valuation form. **All surveyors have to be members of the RICS.** Where a lender suspects or can prove that a valuer is fraudulent they should report them to RICS. Lenders can use Automated Valuation Models (AVMs) to cross check against physical valuations and identify inconsistencies which trigger further investigation of an individual or firm valuation. Lenders should also keep track of Below Market Valuation transactions, particularly if they involve the use of the same professionals. Use of the internet such as google maps can also assist lenders in assessing whether a property exists at all or is in keeping with its description.
Insider collusion/staff involvement in fraud	Some frauds are aided by insiders within the lender's organisation. This could be by giving intermediaries information about the underwriting process, in order for an application to be successful, or knowingly allowing fraudulent applications to be processed. It is difficult to prove if a staff member is complicit in a fraud.	Lenders should take a risk-based approach to manage employee vetting and monitoring, depending on the size and make-up of the organisation. Having sufficient audit trails in place for mortgage processing systems which can identify which member of staff has accessed a system at a given date/time can assist with the identification of insider fraud. Lenders may use ongoing employee vetting tools, such as Credit Reference Bureaus, and credit scoring. However, this should be managed accordingly within the organisation
Accountants	Accountants can assist in perpetrating frauds by assisting in falsifying financial information; creating documentation in support of a fictitious person or company or otherwise.	Lenders should monitor transactions where the same professionals are used together – this can indicate collusion. Running checks on the accountant within CIFAS / National Hunter etc to establish involvement in fraudulent transactions, which may trigger further investigation of an individual or firm Checking financial information against that held by authorities such as HMRC.

2.1.3 Warning signs at application stage

Criminal methodologies are constantly evolving; however there are a number of warning signs which may point to an attempt to fraudulently obtain a mortgage. None of the following should be regarded in themselves as absolute proof of actual or attempted mortgage fraud, but may indicate further investigation/checking is warranted before a decision to lend or release funds is taken.

- Are all the questions on the application form completed?
- Does the borrower live locally to the property being purchased?
- Is the professional (e.g conveyancer, broker, valuer) the borrower is using based locally to where they live?
- Is the transaction introduced by a broker? If so, is the broker local to the purchaser/property being purchased?
- The property is not consistent with the purchaser's circumstances e.g. too big/small.
- Does the purchaser's declared income appear high for their age or type of employment/role?
- Are there inconsistencies in the purchaser's address history?
- Is the purchaser's supporting paperwork of good quality, e.g. payslips show payroll number?
- The purchaser is retaining an existing, more substantial property, than the one they are purchasing. It is possible that the purchaser may let the property being purchased and obtain the advantage of higher LTV/better product
- Does the borrower seem unusually disinterested in the purchase? If so, they may be a 'front' purchaser
- Is the seller a private company or have they recently purchased the property from a private company?
- Has the property being purchased been owned by the seller for less than 6 months? If so, what is the explanation for the quick sale?
- Is the property being sold between two members of the same family or between those who have known associations?
- Has the value of the property increased or decreased significantly in a short period of time? If so, is the change in line with the property market conditions in the area?
- Is it likely that any incentives or discounts will be offered to the borrower to secure the sale? If so, have these been declared?
- If the borrower is accessing a government scheme to purchase the property, does the information they have provided appear to conflict with the eligibility requirements under the scheme?
- Is the deposit being paid by someone other than the purchaser? If so, why?
- Are the same professionals acting on every transaction in the chain? e.g. accountant/solicitor etc.
- Poor quality documentation e.g. spelling errors
- Inconsistent address history

- Multiple applications for different people but looking to purchase the same property with the same current address, employment, professionals etc

- Change in solicitor details (such as firm, address, bank account details) during the application process

2.2 Account management

2.2.1 General

Mortgage fraud may occur at the application stage of the process. This can be ongoing throughout the relationship if any further advances are obtained on the existing loan. Where the mortgage has been obtained by deception, the full value of that mortgage will then represent the proceeds of crime, which subsequently becomes an offence under the POCA 2002. Monthly repayments on fraudulently obtained mortgages may often also be sourced from proceeds of crime.

The main areas of risk which have been identified during the period of the loan are detailed in the table below.

2.2.2 Account management risk areas

Fraud Offences (under the Fraud Act 2006) & Money Laundering Offences (under Proceeds of Crime Act 2002)

Area of Risk	Detail	Best Practice
Monthly repayments/Redemption of loan	Repayments of the loan can be made from the proceeds of crime. This is a form of reverse money laundering, where clean funds have been lent and are repaid with criminal property. This scenario can include mortgage redemption, where completion of the mortgage is followed by an almost immediate full redemption. An indicator of this is if the mortgage repayments are being made from someone other than the borrower.	Usually difficult to trace where the funds for monthly repayments have originated. One suggestion is for a mandatory current account held with the lender for repayment purposes, which would make the trail of transactions easier to identify. The lender may also wish to use exception reports to identify third party payments. Lenders may also wish to monitor mortgages which are redeemed within very short time scales.
Flexible mortgage products/Drawdowns	The ‘flexible’ mortgage product can be susceptible to money laundering. The nature of the drawdown facility, where a borrower can ‘borrow’ additional funds (up to an agreed level) and then repay as and when they wish to, provides opportunities to launder monies. The destination of the funds ‘drawn down’ may not be known, as it relies upon information provided by the borrower to the lender. The origin of the funds for repayment is also unknown. These products can be susceptible to account take-overs and fraudulent draw-downs can occur as a result.	The nature of the product can be susceptible to money laundering. Lenders should ensure that these products are robustly underwritten and that KYC and due-diligence checks are made prior to future draw-downs on a risk based approach.

Further loans/Advances	Further advances on an existing mortgage could pose a significant risk because minimal due diligence is carried out on the borrower/property as they are an existing customer.	Full due diligence to be carried out on all applications for further advances.
Deeds/Registration of charges	Solicitors may not register the lender's charge and abscond with the funds, leaving the lender with no security. The purchase price on the Land Registry document may differ to that of the loan offer.	A deeds checking procedure would help identify the early signs of the charge not being registered. Where the deed has been registered this could then be used to check any price discrepancies. If there is a price discrepancy the lenders should raise it with the conveyancer. Lenders should promptly release redeemed charges, to avoid delay in the registration.
Mortgage Arrears	Early arrears on a mortgage account can be a sign of a fraudulently obtained mortgage. Similarly, if a mortgage has been in arrears for some time this can be an indicator for fraud.	Have a process in place to monitor arrears activity and refer these for further investigation if deemed suspect.

3 Recovery of losses by lenders

Lenders will always look to recover the full value of their advance where they are a victim of a fraud. Where house prices are increasing and a fraud is detected, it is unlikely that a lender will make a loss. Where house prices are static or falling lenders may face a shortfall between the re-sale price and the mortgage.

Most lenders will investigate such losses to determine if the professionals involved have been negligent. If this is the case, the lender will pursue a negligence claim against the individual's or firm's professional indemnity insurance (PII). Lenders should ensure that the PII cover that the professional has in place is adequate.

Where it is not possible to re-coup losses via a PII claim the lender may wish to pursue civil or criminal proceedings against the fraud ring themselves to recover losses. Pulvers v Chan and Others [2007] EWHC 24006, where an indemnity insurer successfully pursued a civil recovery case against a fraud ring, provides a precedent for this.

Some lenders will insure themselves against fraud losses and where there is no evidence of negligence by a third party, the lender will claim against this insurance.

This facility for recovering losses via negligence claims under PII or the lender's own insurance is generally available for approximately 6 to 10 years.

The Land Registration Act 2002 provides that, where there has been a mistake in the Land Register that affects the lenders' interest, compensation is available from the Land Registry, Lenders should be aware of the circumstances and limitations of this redress. Guidance on rectification and indemnity is here.

4 Lender controls

4.1 General

All UK lenders have controls in place with regards to detecting fraudulent applications for mortgages. Many lenders have highly automated systems, which are backed up by appropriate checks and controls.

There is no single solution and not all lenders' systems and control will be the same. Individual lenders should know their business, the risk of fraud associated with the products they offer and have sufficient defences in place.

Lenders should have internal processes in place to review and update these controls on a regular basis and in response to spikes in fraudulent mortgage activity. The FCA advocates a risk-based approach to the lenders' processes and controls which reflects the size or risk appetite of the business. The FCA requires lenders to detail how they incorporate anti-fraud controls into their affordability assessments as part of their responsible lending policies.

The following should be considered:

- KYC for each borrower on mortgage applications
- Use of automated fraud detection systems at the application process
- Use of verification tools such as the Mortgage Verification Scheme with HMRC, where there are suspicions as to the stated income.
- Due diligence carried out on brokers/intermediaries, solicitors and valuers at the onset of relationship and audits on an ongoing/annual basis – see section 5
- Reassessment of mortgage accounts before any further advances are released
- Linked current account for mortgage monthly repayments

4.2 Internal culture, training and governance

It is important that checks and controls within the mortgage process are backed up by a robust anti-fraud corporate culture and corporate governance regime. Whilst this should cover all types of fraud, mortgage fraud should be highlighted as a particular risk.

Good practice includes:

- Regular review of fraud risk and risk appetite at Board / senior management level supported by focused management information and regular risk assessments.
- Clear senior management responsibility for fraud prevention.
- Appropriate remuneration structures – these should incentivise detection of fraud but not encourage overlooking fraud risks to achieve sales.
- Use of the lender's compliance or internal audit function to independently assess the effectiveness of processes and controls.
- Mortgage fraud awareness training for all employees likely to be involved in mortgage sales or administration.

5 Managing third party relationships

Given the risks highlighted in Section 2.1.2, lenders need to have appropriate processes and controls in place to manage relationships with solicitors, individual brokers, broker networks and clubs and valuers. Lenders need to ensure that:

- The number of solicitor / broker / valuer relationships that they set up within panels is appropriate to their capacity and capability to manage them and the types of lending they undertake.
- All professional third parties that they deal with have appropriate professional indemnity insurance cover.
- They undertake appropriate due diligence to vet new third party relationships.
- They re-assess existing relationships where business levels have been dormant for some time.
- They monitor the performance of the third party to check for indicators of fraud or of negligence / poor quality of work that could facilitate fraud.

Not only does this make sense in terms of fraud prevention but proper processes and controls will also pick up on poor quality of lending and / or professional incompetence which also reduce profitability through higher bad debt provisions and, in some cases, create the opportunity to claim back fees, commission etc.

The table below sets out best practice for management of professional third parties - the list is not exhaustive. As with all fraud controls, lenders must assess the fraud risks they face and adopt appropriate controls to mitigate the particular risks that they face.

Some lenders outsource panel management to a third party panel manager – lenders then have responsibility for checking that the panel manager performs robust due diligence and performance monitoring as above.

However panels are managed, where lenders have concerns about fraudulent practice by a conveyancer / broker / valuer they should use the appropriate cross-industry routes to pass on their concerns.

	Conveyancers	**Brokers**	**Valuers**
Panel size	• Clear internal ownership • Close liaison between the in-house legal and fraud teams • Action to reduce panel size if there is concern that panel has become too large to effectively manage	• Clear internal ownership that balances relationship management with independent scrutiny • Action to reduce panel size if there is concern that the panel has become too large to effectively manage	• Clear internal ownership that balances relationship management with independent scrutiny • Action to reduce panel size if there is concern that the panel has become too large to effectively manage
Appropriate PI cover	Production of PI certificate.	Production of PI certificate	Production of PI certificate.
Vetting new relationships	• Documentation from conveyancers– e.g. Practising certificate, headed letter from senior partner, PI certificate • Risk-based firm visits • Checks against Law Societies / SRA / CLC records • Relevant accreditation e.g. CQS, SLC • Internet searches on firm & key individuals • Phone call to confirm	• Checks against FCA register • Face to face inspections • Internet searches • Phone call to confirm that contact details are genuine • Focused scrutiny of initial case submissions • Check against available intelligence and fraud databases	• Checks against RICS records • Internet searches • Phone call to confirm that contact details are genuine • Focused scrutiny of initial case submissions • Check against available intelligence and fraud databases

	that contact details are genuine • Check against available intelligence and fraud databases		
Re-assessment of dormant relationships	• Clear policy on length of dormancy before action is taken & regular review of panel composition • Vetting as above – focusing on evidence of takeover retaining original name on change of partner or other key staff	• Regular review of panel & action against poor performers • Vetting as above for brokers wanting to re-join the panel	• Regular review of panel & action against poor performers • Vetting as above for valuers wanting to re-join the panel
Performance & quality monitoring	• Regular dialogue with panel members. • Checks that funds are dispersed as per the instructions held • Monitoring of time taken to register charges • Review of fraud & arrears cases to check solicitor performance. • List of firms with whom you will not do business.	• Checks on quality of applications received – monitors to be independent of managers who manage the day to day relationships. • Quality control review of submitted applications. • Lenders may wish to consider the working together guidance document for context around the lender/intermediary relationship	• Monitoring of submitted cases & regular dialogue with panel members. • Sample checks – AVM checks, second valuer opinion, sense check against local knowledge. • Review of fraud & arrears cases to check valuer performance • List of firms with whom you will not do business

6 Regulatory controls

The mortgage end-to-end process is regulated by:

6.1 FCA: Financial Conduct Authority

The regulation of most mortgage sales is overseen by the Financial Conduct Authority (FCA). The FCA regulate lenders, mortgage introducers and mortgage brokers. Although regulations surrounding lenders are strictly adhered to and monitored, it is recognised that closer monitoring and supervision of individuals could be beneficial in the other two areas.

The FCA's Mortgage Conduct of Business rules are based on the principle that firms must treat their customers fairly. The FCA has a strict definition of what it calls a regulated mortgage contract. To qualify as a regulated mortgage contract the borrower must be an individual or trustee and the property must be at least 40% occupied by the borrower or a member of his/her immediate family. As a result of the Mortgage Credit Directive, the definition of a regulated mortgage contract was extended to include some buy-to-let mortgages, defined as consumer buy-to-let mortgages and second charge loans.

Regardless of mortgage type, lenders and their intermediaries still have a responsibility to ensure that they are not used to the purposes of financial crime.

Contact details: For financial crime reports:

Central Intelligence & Tasking Team
Financial Crime and Intelligence Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Email: fcid@fca.gov.uk

For Information from Lenders (IFL) reports:

Mortgages Supervision Team
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Email: ifl@fca.gov.uk

6.2 Other professional regulators

Other professionals involved in the mortgage and property process are subject to their own regulatory and/or professional standards regimes. Regulators across the sectors collaborate to prevent mortgage fraud. Some of the main professional regulators are set out below for information.

6.2.1 SRA: Solicitors Regulation Authority

The SRA regulates the activities and professional standards of solicitors in England and Wales. Experience suggests a significant number of organised mortgage frauds involve either complicit or negligent actions by a solicitor. Professional standards are set for solicitors by the relevant Law Society and the standard retainer between a conveyancer and a lender is outlined in the CML's Lenders' Handbook.

Contact details: Fraud and Confidential Intelligence Bureau
Email: fraud@sra.org.uk

6.2.2 CLC: Council of Licensed Conveyancers

The CLC regulates the activities and professional standards of Licensed Conveyancers in England and Wales. Professional standards are set out in the CLC's Handbook.

Contact details: *Email: clc@clc-uk.org*
Telephone: 0207 250 8465

6.2.3 LSS: Law Society of Scotland

The LSS regulates the activities and professional standards of solicitors in Scotland. Professional Standards are set out in the Society's Rules and Guidance.

Contact Details: *Email: lawscot@lawscot.org.uk*
Telephone: 0131 226 7411

6.2.4 LSNI: Law Society of Northern Ireland

The LSNI regulates the activities and professional standards of solicitors in Northern Ireland. Professional standards are set out in the Society's Practice Regulations, which are legislation enabled by the Solicitors (Northern Ireland) Order 1976 (as amended).

Contact details: *Email:enquiry@lawsoc-ni.org*
Telephone: 028 9023 1614

6.2.5 RICS: Royal Institution of Chartered Surveyors

The RICS is the professional body that both represents the interests of surveyors and produces professional standards and guidance for all practitioners. The surveying standards are set out in the 'Red Book' which is frequently amended to ensure that it remains relevant and up-to-date.

Contact details: Email: regulation@rics.org
Telephone: 020 7695 1670

6.3 Disciplinary measures

All supervisory bodies have disciplinary procedures in place. Reports of fraud and suspected are required from lenders in order for these bodies to take such action. The FCA has a formal whistle blowing system for intermediaries in the Information from Lenders Scheme, described earlier in this document. Lenders can report intermediaries they can prove or suspect of being fraudulent. Similarly, the SRA and RICS both have channels to receive such information from lenders.

7 The role of the police and National Crime Agency

7.1 The police response

Where lenders believe that a mortgage fraud has taken place, they should consider reporting the crime to Action Fraud and/or the local police force, or the City of London Police, who are the lead force for economic crime in England & Wales.

Lenders should note that in recent years, fraud and financial crime has decreased in priority and consequently fraud squads within forces across the country have been shrunk and many have closed. This combined with the complexity and broad geographical spreads of such offenses (often crossing police boundaries) have led to lenders' reports of mortgage fraud not being pursued by the police.

7.2 The role of the National Crime Agency

Lenders' engagement with the National Crime Agency (NCA) will predominately be under POCA 2002. Where a lender has suspicions regarding activity on a live account they are required to submit a suspicious activity report (SAR) to the NCA. Submitting a SAR/consent request does not mean that the crime will be registered with the police. If the lender wishes to report a crime they must do so with the police separately.

The NCA took over the functions of a number of former individual agencies, including the Serious Organised Crime Agency and the National Fraud Authority. NCA has an Economic Crime Command, with a focus on fraud, money laundering, bribery and corruption.

Annex A

Mortgage fraud Indicators from the Royal Institution of Chartered Surveyors

Instructions to valuer

- Request for specified valuer by introducer or applicant
- Valuer out of area
- Requests for divergence from Red Book
- Terms of Engagement outside panel manual/lender instructions
- One applicant purchasing several properties in quick succession
- Multiple off plan purchases
- Full post-code not on instructions
- Introducer made inspection appointment
- No applicant name on instructions
- Instructions issued at week-ends
- Connections between seller/estate agent and introducer/broker/financial adviser
- Applicant telephone number same as introducer
- Report to broker/intermediary and not to lender
- Sub-prime mortgage providers
- Lender identity not disclosed
- Owner/occupier applicant to move over large distances
- No applicant name
- Incorrect applicant name
- High loan-to-value ratio
- Direct sales without estate agents

Site notes

- No site notes on file
- Site notes incomplete – or too complete, i.e. fabricated
- Site notes do not appear simultaneous – e.g. not wet when stating heavy rain
- Site notes too 'pristine' in condition
- New-build incentives not checked when appropriate
- Discrepancies between information in instruction and on-site facts – e.g. type, names
- Type and construction not listed
- Accommodation not listed
- No evidence of external measurements for buildings insurance
- Comparables supplied by broker/seller
- No comparables on site notes
- Applicant not present at inspection for re-mortgage
- Introducer present at inspection

Buy-to-Let

- Houses in Multiple Occupation (HMOs) passed off as Assured Shorthold tenancies
- Market volatility not evident
- Buy-to-Let properties with no evidence of letting or planned lettings
- Buy-to-Let properties with no similar rental evidence listed
- Rental/Income stream valuations instead of comparables

Valuation report

- Discrepancies with site notes/information on instructions
- Incomplete
- Lender not as original instructions
- Time from inspection to report more than a few days
- Valuation report not dated or signed – note electronic sign-off

Seller/buyer transaction
- No evidence of ‘proper marketing’
- Connected contracts/agency deals, e.g. seller to manage buy-to-let property
- Not an ‘arms length transaction’
- Property investment clubs/syndicates and other apparent collective investments

Post valuation
- Objections from introducer/seller to be named as source of information
- Complaints/queries direct from introducer/borrower – not via lender
- Unusual or defective rental agreements to support lettings information
- Lack of site notes
- Lack of comparable transactions in site notes
- Rental income allegedly above normal Assured Shorthold Tenancy levels

Annex B

Mortgage fraud indicators from the Solicitors Regulatory Authority

- Failure to respond to correspondence or delay in responding.
- Late in registering charges or payment of stamp duty.
- Failure to undertake proper or full searches.
- Failure to redeem mortgages.
- False representations to clients or other solicitors.
- Failure to comply with lenders conditions.
- Deposits paid direct to vendor.
- ‘Back to Back’ or sub sales not reported to lender.
- Failure to notify lender of existing mortgage.
- Failure to honour undertakings.
- Acting on all sides of transaction.
- Cut price conveyancing.
- Failure to return deeds.

END