



INDUSTRY ALERT: REVERSE MORTGAGE REFINANCING

Watch Out: Potential Fraudulent Appraisals

While the Department of Housing and Urban Development - Office of Inspector General (HUD OIG) recognizes that there are times when Home Equity Conversion Mortgages (HECM) refinances are beneficial to consumers, HUD OIG is issuing this industry alert to warn lenders, originators, and sponsors that the OIG has identified instances of fraudulent appraisals being used to increase HECM loan amounts in order to qualify senior borrowers for HECM refinancing. HUD OIG special agents have reviewed HECM refinances over the last several years and have identified indications of fraud in hundreds of HECM loans. Analysis of appraisals has revealed appraised values fraudulently inflated by 60 to 100 percent or more above actual market values.

Who is harmed?

The FHA pays inflated insurance claims when fraudulently over-valued properties are foreclosed, increasing losses to the FHA insurance fund.

Investors in the secondary market are also victims of these refinancing frauds. Investors pay premiums to purchase HECMs, based on expected terms and interest rates. When the borrower's original HECM is paid off early because of a fraudulently refinanced HECM loan, investors may lose money on the investment. Early payoffs from refinancing may negatively affect the prices that investors will pay for originated HECMs. To account for possible losses from refinances, investors may reduce the premiums they are will pay when purchasing HECM mortgages.

This reduction may affect profits of originating lenders. While lenders have done no or low cost origination fees in the past, they may now increase origination fees to senior borrowers to make up for lost income on the back end of the mortgage – sales to the secondary market.

Who Benefits?

HUD OIG has conducted initial investigations of several HECM originators who refinanced HECM loans using fraudulently overstated appraisals. HUD OIG also identified sponsors connected to large groups of the fraudulent mortgages. Loan officers, originators, and sponsors all stand to increase revenues from refinances. Analyses of these potentially fraudulent refinances also show that originators are using just a small group of appraisers who earn fees for producing inflated appraisals.

OIG Investigation Discoveries

HUD OIG has analyzed over 5,000 HECM refinances over the last several years. An initial analysis shows that a small group of HECM originators is responsible for a large percentage of potentially fraudulent HECM refinances, generally within relatively small geographic areas. Analyses of these refinances revealed one of the hallmarks of mortgage fraud: unexplained, large increases in appraised values in a relatively short period of time. HUD OIG's preliminary investigations have revealed HECM appraisals where appraisers claim the property values have increased by 60 to 100%, while other properties in the area are only appreciating 3 to 4%.

HUD OIG will investigate appraisers, loan officers, originators and sponsors who engage in fraudulent HECM transactions and will refer them for criminal, civil prosecution, or administrative sanctions as appropriate.

HUD OIG will be working with forensic appraisal services to further analyze hundreds of HECM to HECM refinances and HECM original loans to determine if further investigation is needed. These services can establish property comparables on past dates and determine if a property was over appraised at the time of the refinance. Further, in the future, the Federal Housing Administration is adopting a system to evaluate the quality of appraisals at the time of endorsement in order to catch these issues earlier.

OIG intends to investigate and refer for prosecution unscrupulous appraisers, loan officers, originating lenders, and sponsor lenders that foster this activity.

INDUSTRY WARNING

Underwriters should carefully scrutinize appraisals and appraisal comps on all HECM originations, and particularly on HECM refinances. Look for fraud indicators, such as a large increase in value over a relatively short period of time from the original HECM, changes in property descriptions, including square footage and neighborhoods, appraisal comps located relatively far from the subject property (particularly in urban areas), and the same appraisers or small group of appraisers being used by originators on refinances. Underwriters are reminded that they are responsible for being familiar with geographic areas in which properties are located and should question appraised values if they are out of line with the market.

REPORT

If you are aware of HECM refinancing fraud please file a hotline report using any of the following methods: 1) File at the HUD OIG's Website (<https://www.hudoig.gov/report-fraud>); 2) Send mail to HUD OIG Hotline, GFI, 451 7th Street, SW, Washington, D.C. 20410 ; 3) Email: hotline@hudoig.gov; or 4) call the appropriate Special Agent in Charge in the Office of Investigations at the phone numbers listed at the following web site: (<https://www.hudoig.gov/about/where-were-located>).