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Good morning. Today, I think that it is important that I focus my remarks on what FinCEN is trying to do to address a vulnerability in our Bank Secrecy Act/Anti-Money Laundering (BSA/AML) regime as it relates to mortgage brokers, and how this effort fits into FinCEN's overall initiative to combat mortgage fraud at all levels.<sup>1</sup>

When last I spoke to you two years ago, I discussed FinCEN's broad efforts working with regulators and law enforcement to fight mortgage fraud, and one of the key things I hoped to do at that time was to raise awareness of the mortgage fraud studies that FinCEN already had been putting out for years, and the data that we continue to publish, to promote market integrity and help banks and other financial institutions protect themselves from fraud.

FinCEN's efforts have included the analysis of Suspicious Activity Reports (SARs) and other data reported to FinCEN, often together with other data sets and information available to the Government, to support and inform regulatory and law enforcement investigations, proceedings, and prosecutions at the Federal, State, and local levels. Since 2006, FinCEN has published a broad range of information focused on mortgage fraud in order to advise the financial industry on trends and patterns, and to provide indicators to help protect itself against fraud and other financial crime.<sup>2</sup>

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<sup>1</sup> See [http://www.fincen.gov/news\\_room/speech/pdf/20090316.pdf](http://www.fincen.gov/news_room/speech/pdf/20090316.pdf)

<sup>2</sup> See *Mortgage Loan Fraud Update (SARs July 1 – Sept. 30, 2010)*, Jan. 2011, [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_3rd\\_Qtly\\_10\\_FINAL.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_3rd_Qtly_10_FINAL.pdf); *Mortgage Loan Fraud Update (SARs Apr. 1 – June 30, 2010)*, Dec. 2010, [www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_2nd\\_Qtly\\_10\\_FINAL.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_2nd_Qtly_10_FINAL.pdf); *Mortgage Loan Fraud Update: SAR Filings Jan. 1 - Mar. 31, 2010*, [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_1st\\_Qtly\\_10\\_FINAL.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_1st_Qtly_10_FINAL.pdf); Advisory to Financial Institutions on Filing Suspicious Activity Reports Regarding Home Equity Conversion Mortgage Fraud Schemes, Apr. 2010, [www.fincen.gov/statutes\\_regs/guidance/html/fin-2010-a005.html](http://www.fincen.gov/statutes_regs/guidance/html/fin-2010-a005.html); *Filing Trends in Mortgage Loan Fraud*, Feb. 2009, [http://www.fincen.gov/news\\_room/nr/pdf/20090225.pdf](http://www.fincen.gov/news_room/nr/pdf/20090225.pdf); *Mortgage Loan Fraud: an Update of Trends Based upon Analysis of Suspicious Activity Reports*, Apr. 2008, [http://www.fincen.gov/news\\_room/rp/files/MortgageLoanFraudSARAssessment.pdf](http://www.fincen.gov/news_room/rp/files/MortgageLoanFraudSARAssessment.pdf); *Suspected Money Laundering in the Residential Real Estate Industry*, Apr. 2008, [http://www.fincen.gov/news\\_room/rp/files/MLR\\_Real\\_Estate\\_Industry\\_SAR\\_web.pdf](http://www.fincen.gov/news_room/rp/files/MLR_Real_Estate_Industry_SAR_web.pdf); *Money Laundering in the Commercial Real Estate Industry*, Dec. 2006, [http://www.fincen.gov/news\\_room/rp/reports/pdf/CREAssessment.pdf](http://www.fincen.gov/news_room/rp/reports/pdf/CREAssessment.pdf); *Mortgage Loan Fraud: An Industry Assessment Based Upon Suspicious Activity Report Analysis*, Nov. 2006, [http://www.fincen.gov/news\\_room/rp/reports/pdf/mortgage\\_fraud112006.pdf](http://www.fincen.gov/news_room/rp/reports/pdf/mortgage_fraud112006.pdf).

After the release of our April 2008 mortgage loan fraud study, which provided an update of fraud schemes, with more details on complicit insiders,<sup>3</sup> we received feedback from Kieran P. Quinn, CMB, and past Chairman of the Mortgage Bankers Association, who stated that it is “*the authoritative source for data on fraud perpetrated against mortgage lenders and one which our members rely heavily on to spot trends and stay one step ahead of the fraudsters.*”

As FinCEN’s analysis has shown, criminal activity can arise at different times in the lifecycle of residential mortgage related transactions, affecting a range of persons in the primary and secondary markets. In the traditional money laundering sense, a criminal may attempt to invest the proceeds of illegal activity in a range of assets, including real estate, such as through direct purchase or in paying down loans.<sup>4</sup> The purpose of fraud, regardless of whether in conjunction with a mortgage or other real estate related transaction, is overwhelmingly for criminal profit, and the proceeds of such fraud often are laundered through one or more transactions involving financial intermediaries. The victim of mortgage fraud might be an individual person losing equity in a home, or could be a defrauded lender or investor.

In closing my remarks in 2009, I also previewed that as part of FinCEN’s overarching responsibility to promote market integrity and help institutions protect themselves from fraud, we would be reaching out to all of you “in the coming months” to “gather information about the possible impact of applying FinCEN’s AML program and SAR requirements to independent, non-bank mortgage companies.”

So today, I would like to update you on that front, and explain our thinking behind our most recent regulatory initiatives. But before I go into those details on the regulatory side, let me spend a few minutes recapping some of what FinCEN has been doing in the past two years to combat mortgage fraud.

### ***FinCEN’s Ongoing Efforts***

Less than a month after the March 2009 MBA conference – on April 6, 2009 – Treasury Secretary Geithner, together with the Attorney General, Housing and Urban Development Secretary, and others, announced a multi-agency crackdown targeting loan modification fraud and foreclosure rescue scams; this included a new FinCEN-led effort to “marshal information about possible fraudulent actors, drawing upon a variety of data available to law enforcement, regulatory agencies, and the consumer protection community, for the purpose of identifying and proactively referring potential criminal targets to participating law enforcement authorities.”<sup>5</sup> On that day, FinCEN issued an advisory which provided indicators of loan modification/foreclosure rescue fraud, and requested that filers include the term “foreclosure rescue scam” in the SAR’s narrative section to assist law enforcement in identifying applicable filings.<sup>6</sup>

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<sup>3</sup> See [http://www.fincen.gov/news\\_room/rp/files/MortgageLoanFraudSARAssessment.pdf](http://www.fincen.gov/news_room/rp/files/MortgageLoanFraudSARAssessment.pdf)

<sup>4</sup> See *Suspected Money Laundering in the Residential Real Estate Industry*, Apr. 2008, [http://www.fincen.gov/news\\_room/rp/files/MLR\\_Real\\_Estate\\_Industry\\_SAR\\_web.pdf](http://www.fincen.gov/news_room/rp/files/MLR_Real_Estate_Industry_SAR_web.pdf) and *Money Laundering in the Commercial Real Estate Industry*, Dec. 2006, [http://www.fincen.gov/news\\_room/rp/reports/pdf/CREassessment.pdf](http://www.fincen.gov/news_room/rp/reports/pdf/CREassessment.pdf)

<sup>5</sup> See <http://www.treasury.gov/press-center/press-releases/Pages/tg83.aspx>; see also Treasury Department Press Release, Federal, State Partners Convene to Discuss Ongoing Anti-Fraud Efforts in Housing Markets (September 17, 2009), <http://www.treasury.gov/press-center/press-releases/Pages/tg291.aspx>

<sup>6</sup> See [http://www.fincen.gov/statutes\\_regs/guidance/pdf/fin-2009-a001.pdf](http://www.fincen.gov/statutes_regs/guidance/pdf/fin-2009-a001.pdf).

And in these past two years, we have redoubled our efforts to get information out to the financial industry. As I noted in 2009, FinCEN's analytical products are designed not only to provide insights into some of the ways we use the data filed under the BSA. These reports provide insights as to how FinCEN works with law enforcement to detect trends and evolving criminal activity to identify subjects and to target investigations and prosecutions. They are also designed in part to provide feedback on risks and vulnerabilities to better arm your financial institutions and customers to protect themselves from becoming victims of mortgage fraud. The continuing dialogue between the financial industry and government, through reporting, feedback, and discussions like at this conference today, promote our common goals.

In May 2010, FinCEN released its first public analysis of SARs containing information about potential foreclosure rescue scams. The report, *Loan Modification and Foreclosure Rescue Scams – Evolving Trends and Patterns in Bank Secrecy Act Reporting*,<sup>7</sup> involved an analysis of more than 3,500 SARs filed from 2004 through 2009, of which the great majority, 3,000, were filed in 2009. The report also revealed information on the impact of FinCEN's April 2009 advisory. It appears that the advisory resulted in significantly increased filings; however, FinCEN analysts found that filers continued to use a variety of descriptive terms for loan modification/foreclosure rescue scams.

As a result, FinCEN issued updated guidance in June 2010 to the financial industry concerning new scam techniques that financial professionals should watch for and report.<sup>8</sup> The guidance explained that including the term "foreclosure rescue scam" in the narrative enables law enforcement to search for and identify fraudulent activity more easily when reviewing SAR information, which assists in focusing investigative resources.

Early reports of loan modification/foreclosure rescue scams identified subjects purporting to be loan modification or foreclosure rescue specialists. These subjects targeted financially troubled homeowners with promises of assistance. The scams described in later reports reflected an evolution into "advance fee schemes," in which purported loan modification or foreclosure rescue specialists promised to modify a homeowner's mortgage for more favorable repayment terms. Following receipt of large advance fees, scammers rarely, if ever, provided any service. FinCEN will continue monitoring SARs reporting suspected loan modification/foreclosure rescue scams and will publish findings in future reports.

Today, FinCEN is releasing its new report, *Mortgage Loan Fraud SAR Filings In Fourth Quarter and Calendar Year 2010*,<sup>9</sup> which provides **full year data** showing the number of SARs involving mortgage loan fraud (MLF SARs) increased 4 percent in 2010, however the growth rate of MLF SARs began to slow over the last two to three years. FinCEN's report found that references to bankruptcy have steadily increased over time in MLF SAR filings. Beginning with this report, FinCEN will be releasing data on a quarterly basis for almost 600 urban areas and 960 counties reported in MLF SARs, with historical data going back to 2006. As part of FinCEN's commitment to the Open

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<sup>7</sup> See [http://www.fincen.gov/news\\_room/rp/files/MLFLoanMODForeclosure.pdf](http://www.fincen.gov/news_room/rp/files/MLFLoanMODForeclosure.pdf)

<sup>8</sup> See [http://www.fincen.gov/statutes\\_regs/guidance/pdf/fin-2010-a006.pdf](http://www.fincen.gov/statutes_regs/guidance/pdf/fin-2010-a006.pdf)

<sup>9</sup> See [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_4th\\_Qtly\\_10\\_FINAL\\_508.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_4th_Qtly_10_FINAL_508.pdf)

Government Initiative,<sup>10</sup> we are providing this information to the public to assist financial institutions, community advocacy groups, and others, to identify areas with high degrees of potential mortgage fraud.

Today's report also calls attention to continued abuses related to so-called debt elimination scams.<sup>11</sup> Debt elimination scams were cited in nearly 1,300 MLF SARs in 2010. In these SARs, filers noted subjects sending a variety of documents or bogus payment methods to financial institutions, in attempts to eliminate or satisfy mortgage obligations. In addition, MLF SARs filed in 2010 explicitly referenced flopping in 112 SARs. This compares with relatively stable occurrences of suspicious activity involving broker price opinions and short sales in 2010. Flopping occurs when a foreclosed property is sold at an artificially low price to a straw buyer, who quickly sells the property at a higher price and pockets the difference. Also, beginning with this mortgage fraud report, FinCEN has added new interactive data analysis features that provide additional information and explanation of MLF SARs.

And later this week, FinCEN will issue another SAR analysis focused on fraud in the commercial real estate financing arena. This is not the first time FinCEN has focused on the commercial real estate area, however. In December 2006, FinCEN issued a study highlighting money laundering trends in the commercial real estate industry.<sup>12</sup>

The study we will issue in the coming days found that incidents of suspicious activity in commercial real estate financing as reported by depository institutions filing SARs almost tripled between 2007 and 2010. In contrast to mortgage loan fraud SARs, which are mostly submitted by large financial institutions, filings reporting potential commercial real estate fraud came from institutions of varying sizes and locations, indicating that fraud associated with financing of commercial real estate affects a broad range of reporting institutions.

The analysis shows that the largest class of suspicious transactions was for loans under \$1 million, or roughly 45 percent of SARs examined. Nine percent of transactions reported in the SARs examined were valued at \$10 million or more. This study of potential fraudulent activity not only can assist depository and other financial institutions to spot and report illicit activity to FinCEN, it also provides useful information to Federal, State, and local law enforcement and regulators. Accompanying this study, FinCEN will also issue an advisory to alert filers to the various types of commercial real estate fraud and provide tips on how to best report the activity in SARs.

As this brief overview has shown, FinCEN is regularly pulling together, analyzing and releasing valuable data on mortgage fraud, which serves as another tool to fight scammers and mortgage fraud and we have a dedicated section on our Web site to highlight this information.<sup>13</sup> In particular, publications such as FinCEN's quarterly mortgage fraud reports contain new information on reported suspicious activities based on location, types of scams, and other trends that can help law enforcement to further

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<sup>10</sup> See the White House Web site regarding the Open Government Initiative, Open Government Policy, <http://www.whitehouse.gov/open/about/policy>

<sup>11</sup> FinCEN's November 2006 report on mortgage loan fraud brought attention to the emergence of these debt elimination scams and noted a significant increase in related SARs between 2004 and 2005 – from 87 SARs in 2004 to 283 SARs in 2005. See note 2.

<sup>12</sup> See [http://www.fincen.gov/news\\_room/rp/reports/pdf/CREassessment.pdf](http://www.fincen.gov/news_room/rp/reports/pdf/CREassessment.pdf)

<sup>13</sup> See <http://www.fincen.gov/mortgagefraud.html>

investigate mortgage loan fraud, and financial institutions to detect and report such fraud. The report that FinCEN issued in January 2011 contained the following key findings:

- More than 80 percent of MLF SARs involved suspicious activity amounts under \$500,000.
- Nearly all MLF SARs with reported loss amounts indicated amounts under \$500,000. However, over 75 percent of MLF SARs did not indicate loss amounts.
- Filers identified over half of SAR MLF subjects in the 2010 third quarter as borrowers.
- California and Florida had the highest number of subjects, followed by New York and Illinois. Based on subjects per capita, Florida and California switched places in the first and second place rankings, while Nevada and Arizona replaced New York and Illinois as third and fourth highest per capita.

In December 2010, FinCEN issued two mortgage fraud reports that analyzed SAR data filed between January and June 2010.<sup>14</sup> Taken together the reports show that SARs indicating mortgage loan fraud climbed 7 percent. Another key finding was that references to bankruptcy have steadily increased, rising to 7 percent of mortgage loan fraud SAR filings in the first half of 2010, compared to 1 percent in 2006 and 2007.

### ***Residential Mortgage Fraud***

Fraud in the residential mortgage markets may occur in a variety of situations, affecting a variety of actors. Fraud may occur at the loan origination stage, involving material misrepresentations or omissions, false statements, straw buyers, false appraisals, identity theft, etc.<sup>15</sup> Fraud may occur in the context of loan modifications, including when unscrupulous actors seek to take advantage of homeowners struggling to meet their mortgage payments.<sup>16</sup> Fraud may occur in home equity conversion loans (“HECMs”), commonly known as reverse mortgages.

The difficult economic environment and associated financial uncertainty has resulted in an increasing number of senior citizen homeowners accessing equity in their homes through reverse-mortgage programs as a way to ease their financial situation. As a result, senior citizen homeowners who use equity conversion programs to meet their financial needs are increasingly becoming a target for scammers. Given this increased potential for fraud, FinCEN, in consultation with the Housing and Urban Development-Office of Inspector General (HUD-OIG) and the U.S. Secret Service, issued an advisory in April 2010 to highlight reverse mortgage fraud schemes potentially related to the Federal Housing Administration’s (FHA’s) HECM program so that financial institutions may better assist law enforcement when filing SARs.<sup>17</sup>

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<sup>14</sup> See [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_1st\\_Qtly\\_10\\_FINAL.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_1st_Qtly_10_FINAL.pdf) and [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update\\_2nd\\_Qtly\\_10\\_FINAL.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update_2nd_Qtly_10_FINAL.pdf)

<sup>15</sup> For a description of commonly reported fraud related to loan origination, see, e.g., *Mortgage Loan Fraud: An Industry Assessment Based Upon Suspicious Activity Report Analysis*, Nov. 2006, [http://www.fincen.gov/news\\_room/rp/reports/pdf/MortgageLoanFraud.pdf](http://www.fincen.gov/news_room/rp/reports/pdf/MortgageLoanFraud.pdf)

<sup>16</sup> See *Mortgage Loan Fraud: Loan Modification and Foreclosure Rescue Scams*, May 2010, [http://www.fincen.gov/news\\_room/rp/files/MLFLoanMODForeclosure.pdf](http://www.fincen.gov/news_room/rp/files/MLFLoanMODForeclosure.pdf)

<sup>17</sup> See FinCEN Advisory FIN-2010-005, Advisory to Financial Institutions on Filing Suspicious Activity Reports Regarding Home Equity Conversion Mortgage Fraud Schemes, April 27, 2010, [http://www.fincen.gov/statutes\\_regs/guidance/pdf/fin-2010-a005.pdf](http://www.fincen.gov/statutes_regs/guidance/pdf/fin-2010-a005.pdf)

The advisory provided examples of common scams and potential “red flags” of fraudulent activity related to HECMs. The advisory also highlighted trends that law enforcement and HUD-OIG officials identified involving thefts from seniors by family members, loan officers, appraisers, and others, as well as the use of unsuspecting seniors in property flipping schemes. The advisory also suggested key words for financial institutions to use when completing SARs involving fraud related to the HECM program so that FinCEN analysts can more easily identify and further warn law enforcement of possible fraud. In issuing the HECM fraud advisory, FinCEN, HUD, law enforcement, and other government agencies are actively working with financial institutions to help reduce the incidence of HECM fraud and victimization.

### ***Financial Fraud Enforcement Task Force (FFETF)***

In November 2009, President Obama established the Financial Fraud Enforcement Task Force (FFETF) to hold accountable those who helped bring about the last financial crisis, and to prevent another crisis from happening.<sup>18</sup> The Treasury Department and FinCEN are among the members of the Task Force.<sup>19</sup> FinCEN also co-chairs, together with the Executive Office for U.S. Attorneys, the Task Force’s Training and Information Sharing Committee.

FinCEN has had a dynamic role in the FFETF anti-mortgage fraud initiative through information sharing based on SAR data, and support to law enforcement investigations and prosecutions. SARs are one of the best sources of lead information for law enforcement in fighting financial crime.

FinCEN has actively participated in the FFETF’s Mortgage Fraud Working Group (MFWG), including in the MFWG’s Mortgage Fraud summits around the country.<sup>20</sup> In February 2010, the FFETF began holding mortgage fraud summits in areas where the mortgage fraud problem is particularly severe, in order to meet with community members, banking, mortgage/real estate industry representatives, and law enforcement officials to discuss the problem of mortgage fraud from a national, State, and local perspective. The regional summits had several purposes: to highlight and learn more about the nature of the mortgage fraud problem and emerging trends in different parts of the country; and to help coordinate law enforcement agencies to work together, particularly in advance of the national sweep. FinCEN participated in all of the summits, which were held in Miami, Phoenix, Detroit, Fresno, and Los Angeles.

FinCEN supported these summits by providing analytical products, including a State overview of SAR filings; an overview of BSA data combined with HUD data on loan defaults, FHA claims, and HECMs; and lead information on potential targets. FinCEN has proactively worked to share information and investigative techniques to leverage among multiple Federal, State, and local agencies as well as across the country, strategies that work to detect criminals and hold them accountable.

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<sup>18</sup> See Executive Order 13519 (November 17, 2009).

<sup>19</sup> See remarks of Timothy Geithner, Secretary, U. S. Department of the Treasury, on “The Financial Fraud Enforcement Task Force,” Nov. 17, 2009, [www.fincen.gov/whatsnew/html/20091117.html](http://www.fincen.gov/whatsnew/html/20091117.html)

<sup>20</sup> See <http://www.fincen.gov/fraudentaskforce.html> ; <http://www.justice.gov/opa/pr/2010/February/10-opa-192.html> ; <http://www.justice.gov/opa/pr/2010/March/10-opa-316.html>; and <http://www.stopfraud.gov/news/news-04232010.html>

## ***Supporting Law Enforcement Efforts***

FinCEN also provides direct case support on foreclosure rescue/loan modification scam cases, created a repository within its existing database of information related to both suspects and perpetrators associated with loan modification/foreclosure rescue scams, and disseminated a perpetrator list to law enforcement on a quarterly basis. Additionally, in recognition of the impact of loan modification/foreclosure rescue scams on the states, and the critical role of State authorities in combating this type of crime, FinCEN provided outreach to State-based organizations through the National Association of Attorneys General (NAAG) and the National District Attorneys Association (NDAA), and provided training and case support for their efforts.

FinCEN analysis and many law enforcement investigations have revealed mortgage related fraud to be part of organized criminal activity involving multiple properties and various types of criminal activity.<sup>21</sup> On June 17, 2010, Attorney General Eric Holder announced the results of a nationwide effort, Operation Stolen Dreams, which targeted mortgage fraud perpetrators throughout the country. The sweep, organized by the FFETF, was the largest collective enforcement effort to date in confronting mortgage fraud.<sup>22</sup>

One of the first indictments of the sweep came out of the U.S. Attorney's Office in Atlanta.<sup>23</sup> This case is also the first prosecution involving falsified alterations to a Multiple Listing Service (MLS) routinely relied upon by appraisers, realtors, tax assessors, and others in the mortgage industry to establish accurate property valuations. The defendants profited from the corruption of an FHA-insured program designed to assist seniors 62 years or older with cash for equity in their homes, or with funds toward the purchase of a home.

The defendants faked down payments and arranged inflated appraisals to create bogus equity of up to \$100,000 in the properties securing these reverse mortgage loans, while diverting loan proceeds to themselves. One defendant used the stolen identities and passwords of realtors to increase MLS listing and sale prices in support of inflated appraisals to create the substantial equity required to remain in the properties. Both defendants pled guilty on April 8, 2010, in separate cases, to conspiracy to defraud reverse mortgage lenders and the HUD/FHA insurer of the loans. One defendant pled to an additional count of bank fraud and the other to an additional count of aggravated identity theft. These cases were investigated by HUD-OIG and the FBI, assisted by the U.S. Secret Service, FinCEN, and by local law enforcement including the DeKalb County Police Department, DeKalb County Probation Office, and the Cobb County Sheriff's Department.

Oftentimes, mortgage fraud may only be discovered after default or in the context of foreclosure proceedings, repurchase demands, or insurance investigations.<sup>24</sup> FinCEN has determined, as a result of individual investigations and through its broader analyses, that criminal activity and actors in the

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<sup>21</sup> See, e.g., Department of Justice, Press Release, Financial Fraud Enforcement Task Force Announces Results of Broadest Mortgage Fraud Sweep in History (June 17, 2010), <http://www.justice.gov/opa/pr/2010/June/10-opa-708.html>; and speech of Attorney General Eric Holder at the Operation Stolen Dreams Press Conference (June 17, 2010) (noting participation of FinCEN), <http://www.justice.gov/ag/speeches/2010/ag-speech-100617.html>

<sup>22</sup> See <http://www.stopfraud.gov/news/news-06172010.html>

<sup>23</sup> See <http://atlanta.fbi.gov/dojpressrel/pressrel10/atl040810.htm>

<sup>24</sup> See, e.g., *Mortgage Loan Fraud Update: Suspicious Activity Report Filings from July 1 – September 30, 2009* (February 2010), [http://www.fincen.gov/news\\_room/rp/files/MLF\\_Update.pdf](http://www.fincen.gov/news_room/rp/files/MLF_Update.pdf)

residential mortgage market may be connected with a range of other organized criminal activity affecting a range of financial institutions.<sup>25</sup>

In addition to supporting investigations of mortgage loan fraud and loan modification fraud, FinCEN provides analytical support for a wide range of other cases being investigated by Federal, State, and local law enforcement agencies and other authorities.<sup>26</sup> FinCEN analysts also supported U.S. Attorneys' Offices prosecuting a number of cases, assisted regional Mortgage Fraud Task Forces by providing strategic information on mortgage fraud hotspots within local jurisdictions, and supported the Executive Office for United States Attorneys (EOUSA) in identifying areas in greatest need of additional resources for combating mortgage fraud, by highlighting areas with high concentrations of suspected fraud.

### ***Regulatory Initiatives***

It is against this backdrop of FinCEN's experience with these law enforcement investigations, as well as the analytical studies I have previously mentioned, that we have seen a regulatory gap between the BSA's coverage of depository institutions and residential mortgage lenders and originators in that the latter are currently not subject to SAR reporting and other BSA requirements.

As I previewed in my remarks before this same conference in March 2009, to address concern among regulators, law enforcement, and Congress over abusive and fraudulent sales and financing practices in both the primary and secondary residential mortgage markets, FinCEN issued an Advance Notice of Proposed Rulemaking (ANPRM) in July 2009 to solicit public comment on a wide range of questions pertaining to the possible application of AML program and SAR regulations to non-bank residential mortgage lenders and originators.<sup>27</sup>

Let me provide a bit more background. When FinCEN first identifies a new category of entities to consider for regulation, we must clearly define the affected entities. And while the content of our rules differs slightly from industry to industry, there are three basic components: 1) requiring financial institutions to be vigilant in order to make it more difficult for criminals to move funds through the financial system; 2) keeping records of transactions available for law enforcement; and 3) reporting to FinCEN certain information, such as on SARs, that has a "high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism."<sup>28</sup>

The ANPRM expressed FinCEN's inclination to develop AML program and SAR regulations for a specific subset of loan and finance companies: non-bank residential mortgage lenders and

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<sup>25</sup> See *Mortgage Loan Fraud Connections with Other Financial Crime: An Evaluation of Suspicious Activity Reports Filed by Money Services Businesses, Securities and Futures Firms, Insurance Companies and Casinos*, Mar. 2009, [http://www.fincen.gov/news\\_room/rp/files/mortgage\\_fraud.pdf](http://www.fincen.gov/news_room/rp/files/mortgage_fraud.pdf)

<sup>26</sup> See <http://www.justice.gov/opa/pr/2011/February/11-crm-236.html> and <http://www.stopfraud.gov/news/news-06162010-04.html>

<sup>27</sup> See [http://www.fincen.gov/news\\_room/nr/pdf/20090715.pdf](http://www.fincen.gov/news_room/nr/pdf/20090715.pdf)

<sup>28</sup> See 31 U.S.C. § 5311.



originators.<sup>29</sup> The 2009 ANPRM suggested that any new rules likely would contain standards and requirements analogous to those currently applicable to Federally regulated depository institutions.<sup>30</sup>

### *Notice of Proposed Rulemaking*

After careful review and consideration of comments received in response to the ANPRM, in December 2010, FinCEN took the next step and issued a Notice of Proposed Rulemaking (NPRM)<sup>31</sup> that would require non-bank residential mortgage lenders and originators, like other types of financial institutions, to establish AML programs and file SARs.<sup>32</sup>

In both the ANPRM and the NPRM, FinCEN proposed an *incremental* approach to implementation of AML and SAR regulations for a broad category of financial institutions - loan and finance companies - that would focus first on those business entities that are engaged in residential mortgage lending or origination and are not currently subject to any AML or SAR program requirement under the BSA. Residential mortgage lenders and originators (*e.g.*, independent mortgage loan companies and mortgage brokers) are primary providers of mortgage finance—in most cases dealing directly with the consumer—and are in a unique position to assess and identify money laundering risks and fraud while directly assisting consumers with their financial needs and protecting them from the abuses of financial crime.

So, taking a step back, what are we trying to do? FinCEN believes that new regulations requiring residential mortgage lenders and originators to adopt AML programs and report suspicious transactions would augment FinCEN's initiatives in the mortgage fraud area. Among other benefits, such regulations would complement efforts underway by these companies to comply with the nationwide licensing system and registry under development since the passage of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 ("SAFE Act").<sup>33</sup> As mortgage companies and brokers implement systems and procedures to comply with the SAFE Act, there will be opportunities for them to review and enhance their education and training programs to ensure that employees are able to identify and deal with fraud, money laundering, and other financial crimes appropriately.

The NPRM is complementary to ongoing regulatory reform and is looking to guard against mortgage fraud including such activities as false statement, use of straw buyers, fraudulent flipping, and even identity theft associated with mortgage finance. These illegal activities, and others, have been identified in information provided by SARs.

Now what are the next steps? The comment period on the NPRM closed in February, so we are now working through the issues raised by the comments that were provided, and considering development of final regulations, but let me explain some high-level issues and note the consistent level of support on the overall principles.

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<sup>29</sup> *Id.* See also note 7, *supra*. In this case, and throughout this NPRM, the term "residential mortgage originator" is defined to include, among other persons, entities commonly referred to as brokers in the residential mortgage sector.

<sup>30</sup> See <http://edocket.access.gpo.gov/2009/pdf/E9-17117.pdf>

<sup>31</sup> See <http://edocket.access.gpo.gov/2010/pdf/2010-30765.pdf>

<sup>32</sup> See [http://www.fincen.gov/news\\_room/nr/pdf/20101206.pdf](http://www.fincen.gov/news_room/nr/pdf/20101206.pdf)

<sup>33</sup> See Title V of Division A of the Housing and Economic Recovery Act of 2008, Public Law 110–289, 122 Stat. 2810 (2008), *codified at* 12 U.S.C. 5101, *et seq.*

First, with regard to the question about AML program and SAR reporting, some questioned whether an AML program rule was needed. It is important to understand what an AML program is designed to do. We refer to the “four pillars” of AML for a reason, as each one is critical to holding up the overall structure of the program. Without one, the others will fail. The pillars of an effective AML program are: (1) the development of internal policies, procedures, and controls; (2) designation of a compliance officer; (3) an ongoing employee training program; and (4) an independent audit function to test programs.<sup>34</sup> It would be difficult to expect useful SAR reporting without the pillars of an AML program firmly in place.

Also, I have talked about FinCEN’s efforts working with law enforcement to hold accountable those involved in mortgage fraud, but we also have to keep in mind that it is in everyone’s interest to *prevent* the fraud before it occurs. Prevention is a core purpose behind FinCEN’s regulatory requirements for AML programs. We need to also focus our efforts to ensure our financial industry partners are knowledgeable of risks and vigilant against criminal abuse.

With all of FinCEN’s AML regulations, businesses would be required to implement risk-based programs that take into account the unique risks associated with that particular business’ products and services, as well as the businesses’ size, market, and other issues. Thus, each business’ AML program would necessarily be different than those of businesses with different product, geographic and other risks. Current research demonstrates that one of the predominant risks of criminal activity is mortgage fraud. Therefore, under a risk-based approach, we would expect this to be one of the areas of concentration in a new AML program.

Once again, the AML program serves as a critical foundation for effective SAR reporting. It is also important to emphasize that the SAR obligations under FinCEN’s rules come with a statutory and regulatory safe harbor against any liability for reporting of required information to FinCEN.<sup>35</sup> We recognize the sensitivity of the personal financial and commercial information that can be communicated through SARs, and that we receive this in the public trust.

FinCEN appreciates the support from the MBA comment letter calling the NPRM a “measured and balanced approach.”<sup>36</sup> FinCEN’s NPRM for residential mortgage lenders only imposes SAR and AML program obligations. It doesn’t make residential mortgage lenders “financial institutions” under our regulations, so there is no responsibility for Currency Transaction Report (CTR) filing or record retention. But just to clarify, even though residential mortgage lenders aren’t financial institutions, they are still subject to the 8300 requirement, for the rare occasions when they are involved in transactions involving the receipt of more than \$10,000 in currency.

So how are we approaching issues surrounding examination? The effective regulation of new financial sectors can be difficult when there isn’t a primary Federal regulator because there isn’t any effective way to examine the newly regulated institutions for BSA compliance. Included as part of the Fiscal Year 2012 budget proposal, the Administration proposes a legislative amendment to FinCEN’s statutory authorities that would allow for reliance on examinations conducted by a State supervisory agency for categories of institutions not subject to a Federal functional regulator. This would capture

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<sup>34</sup> See 31 U.S.C. § 5318(h).

<sup>35</sup> See 31 U.S.C. § 5318(g)(3).

<sup>36</sup> See <http://www.regulations.gov/#!documentDetail;D=FINCEN-2010-0001-0008.1>

most nonbank financial institutions currently subject to IRS examination as delegated through a Memorandum of Understanding. With respect to mortgage lenders and originators, we will explore the possibility of working with State regulators. If Congress agrees, we see this could be a good opportunity to consider a new level of cooperation with States on examination issues, so we will explore that going forward.

Along these lines of partnering with the States, the MBA noted in its comment letter that FinCEN should consider working with State banking regulators, based in particular on their familiarity “with residential mortgage lenders and originators’ compliance needs with state law and regulations as well as with federal requirement under the Real Estate Settlement Procedures Act (RESPA), Truth in Lending (TILA) and other statutes and regulations.”<sup>37</sup> This approach was echoed by the Conference of State Banking Supervisors (CSBS), who confirmed in their public comment letter that they will work with FinCEN on facilitating our work with the States.<sup>38</sup>

We recognize that many who commented on the NPRM specifically asked for guidance as to what will be expected on compliance, as well as help in identifying indicators or “red flags” of suspicious activity. We particularly appreciated the comments as to recommended red flags, and we welcome further industry input in identifying those, which could be helpful in combination with our own experience.

### ***Incremental Approach***

I want to turn back now to the issue of the incremental approach. So what is our thinking behind this? With this NPRM, we aren’t covering other sectors of the lending world, or non-lenders but loan-related entities (servicers) yet, but we do have the authority and willingness to seriously consider this possibility in the future. However, we first need to identify which other sectors we should consider, and conduct a cost/benefit analysis. We then need to address issues in terms of effective implementation, especially where there may not be a single Federal regulator, as well as resource limitations, to thoughtfully see any additional expansion through.

Because of the potential for criminal abuse in a wide range of financial transactions, some of those that commented on the NPRM and the ANPRM urged *against* an incremental approach and recommended that we go even farther than mortgage lenders and brokers right now. Specifically, a few commenters cautioned that FinCEN should not delay implementation of rules for other consumer and commercial finance companies.

Arguably, the absence of rules for these other types of loan or finance companies might be exploited by criminals insofar as they may shift the focus of their criminal enterprises from residential to other consumer and commercial finance businesses. As noted in the 2009 ANPRM, FinCEN is inclined to defer regulations for commercial real estate finance businesses and other types of consumer and commercial finance businesses until further research and analysis can be conducted to enhance our understanding of the number and kinds of businesses in their sector, their business operations, and money laundering vulnerabilities.

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<sup>37</sup> See <http://www.regulations.gov/#!documentDetail;D=FINCEN-2010-0001-0008.1>

<sup>38</sup> See <http://www.regulations.gov/#!documentDetail;D=FINCEN-2010-0001-0011.1>

FinCEN will continue to study a range of consumer and commercial finance businesses with a view toward determining the extent to which it is appropriate to expand the scope of the definition of loan or finance company proposed in this NPRM in a future rulemaking. In addition, one commenter urged FinCEN to implement such requirements for persons involved in real estate closings and settlements.<sup>39</sup> There are many variables to consider and we will need your input as to where to prioritize in order to make the right cost/benefit determinations as to the businesses and professions to include in any future regulatory proposal.

A further consideration for FinCEN in proposing an incremental approach is how to ensure awareness within the industry and enforce compliance. The degree of effective implementation by industry has a direct impact on the extent to which we achieve the intended law enforcement objectives. Regulations without appropriate guidance to the industry could have negative consequences including a misallocation of resources. This may create a false sense of compliance, or even put “good” actors that try to comply at a disadvantage to those that ignore obligations. These limitations could apply with respect to any newly regulated industry, but could be magnified if resources are stretched too thin. This concept is one that we are mindful of, and was a factor in our proposal to pursue an incremental approach.

And of course, we will also keep in mind an appropriate implementation period after announcing a final rule if there is agreement to go forward.

### ***Outreach and Education***

Historically, FinCEN has done a great deal of outreach to the financial industry to educate them on their regulatory responsibilities, working hard to strike a balance within our resource and budgetary limitations. I strongly believe that engaging in this type of outreach with the industry is fundamental to the work that FinCEN is doing.

I also recognize that many of the non-bank mortgage lenders and brokers that will be impacted if this rule goes forward will be smaller businesses, and FinCEN has worked hard in recent times to focus our outreach and education specifically to smaller entities. In fact, just last month, I spoke to a group of community bankers in order to highlight FinCEN’s year-long outreach program tailored to community banks and other small depository institutions.<sup>40</sup>

And effective March 1, 2011, FinCEN’s rules and regulations have been reorganized within a new Chapter X of Title 31 of the Code of Federal Regulations (CFR).<sup>41</sup> As noted in the final rule published in the Federal Register on October 26, 2010,<sup>42</sup> the reorganization streamlines the BSA regulations into general and industry-specific parts, allowing a financial institution to look only in the sections that apply to it, making the regulatory obligations more clear and as a result making it easier to facilitate compliance.

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<sup>39</sup> See <http://www.regulations.gov/#!documentDetail;D=FINCEN-2010-0001-0004.1>; <http://www.regulations.gov/#!documentDetail;D=FINCEN-2009-0003-0011.1>; and <http://www.regulations.gov/#!documentDetail;D=FINCEN-2009-0003-0008.1>

<sup>40</sup> See [http://www.fincen.gov/news\\_room/nr/pdf/20110222.pdf](http://www.fincen.gov/news_room/nr/pdf/20110222.pdf)

<sup>41</sup> See [http://www.fincen.gov/news\\_room/nr/pdf/20110301.pdf](http://www.fincen.gov/news_room/nr/pdf/20110301.pdf)

<sup>42</sup> See <http://edocket.access.gpo.gov/2010/pdf/2010-25914.pdf>

What we announced from the beginning is that this will help new sectors identify their obligations under the BSA in a more organized and understandable manner. We believe this step will promote compliance with the regulations, especially among financial sectors newer to these regulatory requirements, and provide a foundation for more logical evolution over time. Non-bank mortgage lenders and brokers would be the first entirely new financial sector to be included since this reorganization went into effect. With this reorganization, there is a mutual benefit to both the financial industry and government, and this theme of cooperation between government and regulated industry is an essential part of the good government process.

### ***Conclusion***

On that note, I would like to conclude with how this regulatory component fits in with everything that we are doing in the mortgage fraud area.

For almost all Americans, the purchase of a home, and the mortgage that helps them finance it, is the biggest investment a person will make in a lifetime. And although the level of homeownership has fallen slightly, from 69 percent in 2004, down to 66.9 percent in 2010,<sup>43</sup> there are few types of financial activity that affect so many Americans.

Now think also of the vulnerability of a home purchase to criminal abuse – the home purchase is a big ticket item, so every single successful fraud has the potential for a significant profit. Multiply that by millions of transactions a year and we can see clearly why we have a need to be vigilant.

The best advice I can give to any sector covered by our regulations, including non-bank mortgage lenders if this rule goes final, is to keep in mind the reasons behind the rule. We have a shared goal in keeping fraud and other criminal activity out of the financial system. We also want to preserve the legitimate business model of mortgage lenders and brokers, and prevent the taint of a few bad apples from undermining consumer confidences in your businesses.

When I spoke with you in 2009, I welcomed your help in looking at rules for mortgage brokers, and this time I welcome all public comment and guidance as to whether there are other sectors or entities for which it makes sense to have rules to expand this public-private partnership to keep fraud out of the mortgage markets and to continue helping the economy and legitimate markets recover.

Thank you for working together with us so far, and we commit to working with the financial industry as we go forward.

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<sup>43</sup> See <http://www.census.gov/hhes/www/housing/hvs/annual10/ann10ind.html> (Table 14)