



**Statement of James H. Freis, Jr, Director
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**Before the United States House of Representatives
Committee on Financial Services
Subcommittee on Housing and Community Opportunity**

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Chairwoman Waters, Ranking Member Capito, and distinguished members of the Subcommittee, I am Jim Freis, Director of the Financial Crimes Enforcement Network (FinCEN), and I appreciate the opportunity to appear before you today to discuss FinCEN's work in combating mortgage loan fraud and our role in the Administration's effort to address the current foreclosure rescue fraud problem. It is more important than ever for our government to be particularly vigilant in this regard, as the downturn in our economy and the government's efforts to improve conditions through the Financial Stability Plan have also created opportunities for those who resort to fraud.

FinCEN has unique contributions to make in this regard, as the authorities that we have been given by the Congress place us at the intersection of the law enforcement and regulatory communities and the financial industry. My testimony today will focus on a number of our ongoing strategic initiatives in the broad mortgage market under which our authorities are maximized to assist in the prosecution of fraudulent actors and to prevent the proliferation of such crimes.

Background on FinCEN

FinCEN's mission is to safeguard the financial system from the abuses of financial crime, including terrorist financing, money laundering, and other illicit financial activity. FinCEN works to achieve its mission through a broad range of interrelated strategies, including:

- Administering the Bank Secrecy Act (BSA) - the United States' primary anti-money laundering/counter-terrorist financing regulatory regime

- Supporting law enforcement, intelligence, and regulatory agencies through the sharing and analysis of financial intelligence
- Building global cooperation and technical expertise among financial intelligence units throughout the world.

To accomplish these activities, FinCEN employs a team comprised of just over 300 dedicated Federal employees, including analysts, regulatory specialists, international specialists, technology experts, administrators, managers, and Federal agents who fall within one of the following mission areas at FinCEN:

Regulatory Policy and Programs - FinCEN issues regulations, regulatory rulings, and interpretive guidance; assists State and Federal regulatory agencies to consistently apply BSA compliance standards in their examination of financial institutions; and takes enforcement action against financial institutions that demonstrate systemic non-compliance. These activities span the breadth of the financial services industries, including – but not limited to – banks and other depository institutions; money services businesses; securities broker-dealers; mutual funds; futures commission merchants and introducing brokers in securities; dealers in precious metals, stones, or jewels; insurance companies; and casinos.

FinCEN’s regulations serve essentially two purposes. First, we require financial institutions to be vigilant against criminal abuse by illicit actors trying to defraud the institution or its customers or to advance their criminal purposes by moving tainted funds through the legitimate financial system. Second, the recordkeeping and reporting obligations create a trail for law enforcement to literally “follow the money” in the investigation and prosecution of criminals. The two most prominent types of reports are those involving large amounts of cash (Currency Transaction Reports or “CTRs”) which would otherwise be unreported, and Suspicious Activity Reports (“SARs”), where the well-trained eye of the financial institution can help us sort out legitimate economic activity from possible criminal activity.

Analysis and Law Enforcement Support – FinCEN provides Federal, State, and local law enforcement and regulatory authorities with different methods of direct access to SARs, CTRs and other reports submitted by financial institutions pursuant to the BSA. FinCEN also combines BSA data with other sources of information to produce analytic products supporting the needs of law enforcement, intelligence, regulatory, and other financial intelligence unit customers. Products range in complexity from traditional subject-related research to more advanced analytic work including geographic assessments of money laundering threats.

International Cooperation – FinCEN is one of more than 100 recognized national financial intelligence units (FIUs) – a central government agency like FinCEN that collects, analyzes, and disseminates financial information to investigate and prosecute criminal activity. We coordinate activities with our FIU partners around the globe largely through a formal organization known as the Egmont Group, an essential focus being the sharing of lead information involving criminal activity that crosses national borders.

FinCEN plays a lead role in fostering international efforts to combat money laundering and terrorist financing among these financial intelligence units, focusing our efforts on intensifying international cooperation and collaboration, and promoting international best practices to maximize information sharing.

FinCEN Focus on Mortgage Fraud

FinCEN first focused on analyzing trends and patterns related to mortgage fraud back in 2002 in the context of an effort to identify areas of potential concern in the sales and management of real estate. Since that time, still within a robust housing market, it became apparent that our SAR data was a leading indicator that mortgage loan fraud was a serious, escalating problem. In our November 2003 SAR (Suspicious Activity Report) Activity Review, we published some of the results of two related FinCEN strategic analytical studies focused on SARs reported in 2001 and 2002.

For that period, overall suspected fraudulent activity was only a small portion of the suspected illegal activity in connection with real estate transactions. Even among a relatively small sample, however, we noted that mortgage fraud was the predominant reported concern. We also explained the few instances of “flipping,” defined as “the buying and selling of the same property within a short period of times with the intention of making a quick profit,” warning that flipping activity is often coupled with mortgage fraud and other forms of fraud.¹

As we continued to follow the trends in SAR reporting from 2003 into 2004, FinCEN analysts noted a dramatic increase in the number of filings indicating suspected mortgage fraud, leading us to drill down more closely into this area.

For our first detailed study focusing exclusively on mortgage fraud, published in November 2006², we proceeded to go back to take a closer look at all of the mortgage fraud filings since the inception of the SAR reporting requirements, analyzing ten years of mortgage fraud reporting data nationwide. Depository institutions filed 82,851 SARs describing suspected mortgage fraud between April 1, 1996 and March 31, 2006. SARs pertaining to mortgage fraud increased by 1,411 percent in the nearly a decade between 1997 and 2005, compared to a 543 percent increase for SARs overall.

In the November 2006 study we explained a range of fraudulent schemes in an effort to provide the financial industry with “red flag” indicators that could help them protect their financial institutions and their customers from being victims of fraud. The report detailed that material misrepresentation/false statements were reported on approximately 2/3 of reports, and noted the vulnerabilities posed by automated processing and low documentation/no documentation loans. The report also explained that mortgage fraud can be divided into two broad categories:

¹ See http://www.fincen.gov/news_room/rp/files/sar_tti_06.pdf (pages 31-36)

² See http://www.fincen.gov/news_room/rp/reports/pdf/mortgage_fraud112006.pdf

- *Fraud for property* – homebuyers misrepresenting income or assets to purchase homes for personal use (approx. 2/3 of sample); and
- *Fraud for profit* – perpetrator intends to abscond with proceeds, with little or no intention to occupy the property; often committed with the complicity of industry insiders (approx. 1/3 of sample).

Since the publication of our first study in November 2006, FinCEN analysts have engaged in nearly 40 formal training events – in addition to other numerous speaking and outreach opportunities by FinCEN leadership - to educate the financial, regulatory and law enforcement communities.

FinCEN also published reports based on SAR analysis that indicated how proceeds of crime generally, although not necessarily connected to mortgage fraud, may be laundered through investments in commercial real estate³ and residential real estate.⁴ These reports, issued in December 2006 and April 2008, respectively, added to the earlier discussion of money laundering vulnerabilities from the 2003 SAR Activity Review report.

FinCEN issued its second study in the mortgage fraud area in April 2008, which provided an update of fraud schemes, with more details on complicit insiders.⁵ A key finding was a 50 percent increase in SARs that reported intercepting the suspected fraud prior to funding a mortgage (an indication of growing vigilance and awareness in the financial community). The report also noted that the total for mortgage fraud SARs filed reached 52,868, an increase of 42 percent from the previous year.

In February of this year, FinCEN issued its third strategic analytical report in the mortgage fraud area.⁶ Our third report looked at 62,084 SARs reporting mortgage fraud, the third most reported type of suspicious activity (following only BSA/structuring/money laundering, and check fraud). Filings had increased 44 percent from 43,000 the prior year.

A new trend that FinCEN spotted in that third round of analysis was the increase in mortgage fraud detection in connection with mortgage purchasers sending home loans back to originators for repurchase. Filing institutions referenced repurchase demands in 8 percent of filings. FinCEN also found that filing institutions referenced foreclosures in 13 percent of their SAR filings, insurers in 8 percent and early default payments in 2 percent of filings as indications of suspected fraud. These patterns of filings generally involved the detection of suspected fraud after the mortgage had been granted. That notwithstanding, there also was an increase in the percentage of SARs filed prior to granting the loan – 34 percent compared with 31 percent in the prior one-year period. In FinCEN's April 2008 report, the increase was 21 percent over the preceding decade. Once again, this reaffirmed the trends we had been seeing since we began examining this issue, and also indicated a growing vigilance and awareness within the financial industry.

³ See http://www.fincen.gov/news_room/rp/reports/pdf/CREassessment.pdf.

⁴ See http://www.fincen.gov/news_room/rp/files/MLR_Real_Estate_Industry_SAR_web.pdf.

⁵ See http://www.fincen.gov/news_room/rp/files/MortgageLoanFraudSARAssessment.pdf.

⁶ See http://www.fincen.gov/news_room/nr/pdf/20090225a.pdf.

FinCEN's fourth and most recent detailed analytical publication focusing on mortgage fraud was issued in March of this year.⁷ That analysis showed that thousands of subjects reported by depository institutions for suspected mortgage loan fraud were also reported by at least one other type of financial institution -- money services business, securities broker and dealer, insurance company, and casino and card club -- for suspicion of being involved in other financial crimes such as check fraud, money laundering, stock manipulation, structuring to avoid currency transaction reporting requirements and others. The interconnected nature of suspicious activity across multiple financial sectors covered by FinCEN's regulations as revealed in this study underscores the immense value of combining insights from the different sectors for the purpose of detecting and thwarting criminal activity.

In calendar year 2008, the total number of SARs filed related to mortgage fraud was 64,816, an increase of 22.6% over the previous year. This increase does not necessarily reflect a continuing rise in the amount of fraud in the mortgage industry. A large portion of the filings represent fraud in the original mortgage fraud application that was only uncovered months or years later when a mortgage went into default. FinCEN's analysis in this area is ongoing, and we will continue to make public relevant findings to help the financial industry protect itself and its customers from becoming victims of fraud, while we also continue to support law enforcement efforts to hold criminals accountable.

Additional Law Enforcement Support Provided by FinCEN

While the above information illustrates FinCEN's proactive analytical work on mortgage loan fraud, it is just one component of our dedication to this issue. A second involves our efforts in close cooperation with criminal investigators and prosecutors to hold accountable those persons engaged in criminal activity.

On an interagency basis, FinCEN is actively involved with a number of initiatives that focus on combating fraud: The Bank Fraud Working Group and the Mortgage Fraud Working Group, sponsored by the Department of Justice, and the President's Corporate Fraud Task Force which is run out of the Department of Justice. FinCEN staff regularly briefs the Mortgage Fraud Working Group on our latest mortgage fraud trends and patterns and we have hosted the Bank Fraud Working Group for discussions on the issue. FinCEN also provides technical advice and analytical support to prosecutors at the Federal and State levels.

In addition to the published analytical reports, FinCEN provides both strategic and tactical support to the law enforcement and financial regulatory communities to investigate and prosecute fraud. For instance, we have supported the FBI in their investigations in the mortgage fraud area, providing information to their Financial Crimes Intelligence Unit to assist in identifying potential investigative targets.

⁷ See http://www.fincen.gov/news_room/rp/files/mortgage_fraud.pdf.

FBI Deputy Director John S. Pistole, in his recent Congressional testimony focusing on the FBI's mortgage fraud efforts, spoke to the importance of utilizing lead information from SARs in their efforts to combat fraud; and he also noted the many interagency efforts the FBI has underway with FinCEN and others to tackle mortgage fraud.⁸

FinCEN has provided analytical support to the FDIC in their work with problem institutions, where BSA data is proving very valuable to their investigations in the mortgage fraud area. Last summer, FinCEN also supported SEC efforts to identify potential securities fraud linked to mortgage fraud.

FinCEN is also partnering with numerous other Federal agencies in a broad, multi-agency task force headed by the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), in coordination with the Inspector General for the Board of Governors of the Federal Reserve System. This proactive initiative combines law enforcement civil and criminal resources to deter, detect, and investigate instances of fraud in the Term Asset-Backed Securities Loan Facility (TALF). More broadly, we are working with Office of Inspector General (OIG) offices around the country to support their efforts to root out the waste, fraud, and abuse in a range of government programs.

On March 13th FinCEN entered into a Memorandum of Understanding (MOU) with SIGTARP that provides them direct access to Bank Secrecy Act (BSA) reports. FinCEN is also providing regular training to the SIGTARP staff on money flows and on how to effectively use BSA data for their analytical purposes, and is currently working with the SIGTARP's Investigations Division and Counsel to develop a joint advisory to send to financial institutions on reporting suspicious activity related to criminal use of TARP funds.

FinCEN is also providing the HUD-IG technical training and support to use BSA data in mortgage fraud cases and assisting them in a strategic effort to proactively identify mortgage fraud in FHA loans by generating leads and potential investigative subjects through SAR analysis. These leads will assist them by identifying potential fraud by industry insiders, finding mortgage fraud "hot spots," and reducing labor intensive research for investigators by centralizing and streamlining the identification of potential frauds as reported in SARs.

FinCEN has also facilitated requests from law enforcement through our PATRIOT Act section 314(a) program where law enforcement indicated that mortgage fraud was a component of their significant money laundering investigations. This is a unique authority provided by Congress that allows FinCEN to reach out to the financial industry to identify previously unknown bank accounts and transactions. These new leads often advance law enforcement investigations, including for the purpose of seizing and forfeiting criminal proceeds, some of which might be available for restitution for victims.

⁸ Pistole, John. Statement Before the Senate Judiciary Committee, Washington, D.C. 11 February 2009. See <http://www.fbi.gov/congress/congress09/pistole021109.htm>

The Administration's Response to Foreclosure Rescue Fraud

On February 18th, President Obama announced a series of initiatives to address the nation's housing crisis and help American homeowners. The Making Home Affordable programs were designed to keep mortgage rates low, allow responsible homeowners to refinance into affordable mortgages or alter at-risk loans and help homeowners lower their monthly mortgage payments. But just as the Administration intensifies its efforts to help American homeowners, those who would seek to prey on the most vulnerable are intensifying their tactics as well, often through purported "mortgage modification" and "foreclosure relief" companies.

On April 6th, Treasury Secretary Geithner, along with Attorney General Holder, Secretary of Housing and Urban Development Donovan, and Federal Trade Commission Chairman Leibowitz, announced a major interagency effort to combat foreclosure rescue scams. Two specific initiatives were included as the Treasury's primary efforts to the joint response.

First, FinCEN issued an advisory⁹ to help financial institutions spot questionable loan modification schemes and report that information for law enforcement purposes. The advisory provides "red flags" for financial institutions that may indicate a loan modification or foreclosure rescue scam.

Second, the Treasury announced an advanced targeting effort - coordinated by FinCEN - to deter fraudulent activity and combat fraudulent loan modification schemes. FinCEN, working with our partners from the law enforcement and regulatory communities, is utilizing information provided by the financial industry, along with other information supplied by participating agencies, to identify possible loan modification fraud suspects for civil and criminal investigations. This research initiative uses SAR filings specifically related to loan modification/ foreclosure rescue to identify targets for referral to appropriate law enforcement authorities.

By serving as a networking and deconfliction center, FinCEN is also helping law enforcement agencies streamline and coordinate their efforts so that the resources of multiple investigative and prosecutorial agencies are focused in the most efficient way. This cooperative effort will maximize government resources to shut down fraudulent companies more quickly than before, target companies that otherwise would have gone unnoticed 'under the radar', and will increase our knowledge of how these companies operate, enhancing our efforts to identify and prosecute every individual involved in a mortgage rescue scam.

FinCEN is proactively reaching out to State-based organizations such as the National Association of State Attorneys General and National District Attorneys Association to involve their members in this initiative and to solicit input on their ongoing activities. While Federal criminal investigators and prosecutors are committed to pursuing the most

⁹ http://www.fincen.gov/statutes_regs/guidance/pdf/fin-2009-a001.pdf

egregious organized criminal actors, it is critical that we involve our State and local partners to avoid letting criminals slip below the radar screen. FinCEN can play a natural role here through its relationships not only with all major Federal law enforcement agencies and U.S. Attorneys' offices across the country, but also its longstanding support of State law enforcement coordinators in all fifty States, as well as police forces in many major municipalities.

We have also participated in Neighborworks-organized teleconferences with participants from Federal, State, local and non-profit organizations and followed up with a detailed memorandum on FinCEN's strategy and solicited input. Any feedback will only serve to complement FinCEN's proactive research initiative of Suspicious Activity Report filings specifically related to loan modification/ foreclosure rescue to identify targets for referral to appropriate law enforcement authorities.

Conclusion

FinCEN is proud to play its part in supporting the Administration's and the Treasury Department's broader efforts as part of the Financial Stability Plan, including the Making Home Affordable programs. While it is impossible to eliminate the possibility of abuse or fraud in broad fiscal stimulus programs, new efforts to spur economic growth and promote responsible homeownership should rightfully be accompanied by renewed vigilance to mitigate criminal tendencies that could undermine the effectiveness of these critical policy initiatives.

The cornerstone of prevention is having the appropriate intelligence for detection, and aggressive action at the earliest stages will make it more difficult for bad actors to engage in fraudulent activity. None of the analytical work FinCEN is doing to fight mortgage fraud and to curb the system of abuse that is exploiting our nation's housing rescue programs would be possible without the SARs, and other BSA reports, that financial institutions file. And those of us who receive and use this information have an important public trust to uphold. This is a responsibility the 300 men and women that make up FinCEN take very seriously. We greatly value our partnership with the financial industry to advance our shared goals of protecting against abuse of the financial system. Educating financial institutions and the general public about risks and vulnerabilities, and, where possible, using regulatory authorities to help mitigate them, will remain key components of our Government strategy to prevent financial crime.

Those who nonetheless violate the law should be held accountable. The law enforcement and prosecutorial resources of the Justice Department, the States, and consumer protection authorities such as the FTC are working hard to prosecute and shut down the unscrupulous opportunists who prey on the economic hardships of others. FinCEN will continue to seek to leverage its expertise, information, and longstanding relationships with a broad range of Federal and State, criminal and civil enforcement authorities, to promote the use of all available tools in furtherance of the objective that crime should not pay.

Thank you for inviting me here today. I am happy to answer any of your questions.