Chapter 23
Real Estate Valuation Fraud

ABSTRACT

Valuation profession is a link between the borrower and the lender. Fraud is an intentional deliberate deception committed for illegitimate personal gain. There are several forms of real estate fraud, especially when the real estate market is facing a boom. The most widespread types of real estate fraud include the preparation of two sets of settlement statements, property flipping, and fraudulent qualifications. There are mainly three types of valuation to look out for. Valuation may be received from an unauthorized agency. Furthermore, a real valuation may be altered from the original to generate profit. Thirdly, intentional inflation of the value of a property will hide the real market value. It is usually difficult to spot real estate fraudulent activities, so deep investigations and professionalism is needed. This chapter explores real estate fraud.

INTRODUCTION

Fraud has been a major and an important topic in the business world. In its broadest sense, a fraud is an intentional or a deliberate deception committed for personal gain or to damage other individuals. Real estate fraud, on the other hand, is a narrowed topic that has been common lately. Real estate fraud refers to the act of any illegal activity with the purpose of misleading or misrepresenting valuable information on a mortgage loan application or other real estate related documents involving the transfer of money. Real estate fraud is usually referred to as mortgage fraud, since fraud takes place at the mortgage application. In order for fraud to take place in the mortgage application, one might overvalue his property. To do so, a valuer must appraise the property at a higher price than its market (actual) price in order to get a higher loan from a lending institution. Valuation profession is a link between the borrower and the lender. In this case the borrower is the one who wants to get a loan and the lender is the lending institution (ex. bank). Valuation fraud could happen at any level of these three parties. As a result "Valuation or assessment" is the nucleus of real estate fraud. Heavy penalties, including large fines and imprisonment can carry with real estate fraud. (Hill, xxxx). There has been many ways in which someone could commit real estate fraud, especially when the market is facing an increase or a boom in real estate sector. Some types of real

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estate fraud are more common or seen more often because of their simplicity. Some other types are less often seen and are more complicated. Both are treated the same in the eye of the law.

BACKGROUND

One of the most widespread types of real estate fraud is the preparation of two sets of settlement statements. In the first statement, which is provided to the seller, contains the accurate or real price of the selling property. It reflects the actual market price. The second statement, which is provided to the lender, reflects an embroidered property price. When the buyer gets the approval of the loan that is reasonably higher than it must be, the excess of money is distributed among the connivers. Another common real estate fraud type is property flipping. In this activity a buyer attempts to purchase a property at a low price, and resells it quickly at a much higher price. This might sound legal, unless when it entails false documents given by the buyer to the lender, it becomes fraud. Least but not last, fraudulent qualifications is also considered a type of real estate fraud. In this type of fraud, credit history and employment qualifications are fabricated by real estate agents in order to help buyers to become qualified buyer in the eye of the lender.

General History of Valuation Fraud

Valuation fraud is generally the hardest type of fraud to detect because even though a valuation may look valid in all its aspects, it may be a forgery. There are mainly three types of valuation to look out for. To begin with, a valuation may be received from a valuation company that is not authorized or registered to perform valuations. Furthermore a real valuation may be altered from the original form for numerous reasons, such as decrease taxes on a company or fool investors to generate profit. Last but not least the third type of valuation entitles intentionally inflating the value of a property. Some are advocate of the notion that valuation fraud was more recurring in the past where companies had more freedom to operate. In fact, after the big business scandals, such as the Enron case and others, businesses are forced to hire external auditors because it is now a worldwide accepted fact that accurate financial reporting is important to an institution's safety and soundness (Todd, 1999).

With so many constraints and regulation policies, corporations and other individual lost the freedom of valuing their assets without being monitored, evaluated and corrected by a neutral third party. On the other hand, others believe that valuation fraud has never had such a big and negative impact on the economy. The world has entered a global financial crisis in which the supply for money is outpaced by the demand for money. In other terms, banks and financial institutions were faced by a lethal liquidity crunch that shut many businesses out of the competition. A main reason for this collapse in the economy system can be tracked to the over or under valuation of properties, mortgages and real estate sites. Valuation fraud has undoubtedly added to the gravity and severity of this financial crisis. In fact, Whistleblower announces that the incidence of property valuation fraud rose 46% in the third quarter compared to the same period a year ago. In addition, according to research, property valuation fraud increased by 25% in 2009 and it seems that the trend of shifting to fraudulent schemes involving real estate will continue in the near future. It seems that valuation fraud is becoming a well known type of business crimes as time evolves.

The world has been harshly exposed to this type of fraud in all its forms since 2008, the beginning of the financial crisis. Although as stated above, more prevention plans are being implemented to detect such fraudulent activities, it is sadly true that voracity and greed are quickly becoming ac-