Q4 2009

Mortgage Fraud Risk Report

In depth analysis of nationwide risk as indicated by the Interthinx® Fraud Risk Indices

Executive Summary

While the overall Interthinx® Mortgage Fraud Risk Index remains elevated but unchanged from the previous quarter's value of 145 (n = 100), it is worth noting the reversal in a number of trends that have persisted over the last year or longer. It is not yet possible to determine whether these reversals represent normal fluctuations in fraud risk or herald a fundamental shift in long term trends.

- With the addition of several MSAs to the highest risk category, California moved into first place in the Mortgage Fraud Risk Index displacing Nevada, which had topped the rankings over the last five consecutive quarters.
- The indices for both California and Nevada fell slightly from a quarter ago but remain elevated at 222 and 220, respectively. The lowest risk states' indices increased, indicating a narrowing of the Mortgage Fraud Risk Index range from Q3 2009. This redistribution of fraud risk geographically is in direct contrast to the trend observed between Q3 2008 and Q3 2009.
- The Property Valuation Fraud Risk Index decreased 4% from the previous quarter, the first such decline since Q4 2007. Despite the quarter-on-quarter decrease, this index is up 40% over the last year and up more than 100% from two years ago. Schemes involving short sales, REO inventories, "wholesale" flipping, and refinancing by borrowers whose equity has been impaired by falling real estate values continue to drive this Index.
- The Occupancy Fraud Risk Index rose 16% since the last quarter, the first significant increase in the index since Q4 2006. The magnitude of the quarter-on-quarter increase suggests that occupancy fraud risk may become a serious issue going forward, as continuing price declines and "get rich quick" schemes lure investors back into the market and as builders face continuing difficulty in moving unsold inventory.
- The Employment/Income Fraud Risk Index increased 3% from a quarter ago, the first quarter-on-quarter increase since this index peaked in Q3 2007. The index declined by more than 50% by Q3 2009, likely due to the elimination of stated and low documentation loan programs, lenders' increased use of Internal Revenue Service data to verify income and to a reduced need for misrepresentation of income as housing generally becomes more affordable. The current quarter-on-quarter increase suggests that employment/income fraud risk may be poised for a rebound.

Mortgage Fraud Risk Hot Spots and Trends

The national Mortgage Fraud Risk Index remains elevated at 145 (n = 100). This index value is essentially unchanged from both a year ago and from last quarter, as decreases in the first two quarters of 2009 were canceled out by a sharp uptick in the third quarter. Figure 1 shows the distribution of current mortgage fraud risk in MSAs throughout the United States. Of the states that have consistently been well-represented in the "very high risk" category: The number of "very high risk" MSAs has increased in California, Arizona and Michigan, has decreased in Florida, Colorado and Ohio, and has remain unchanged in Nevada. The increase in the number of "very high risk" MSAs in California means that nearly all of the state's MSAs are now included in this category. Of the MSAs in states that were represented in the "very high risk category" for the first time in the last quarter, Charleston South Carolina, Portland Oregon, and Minneapolis-St. Paul Minnesota moved to lower risk categories. However, Bend Oregon and Washington DC remained in the highest risk category, and the Winchester, Virginia metro adjoining the Washington DC metro is a new addition to the "very high risk" category.

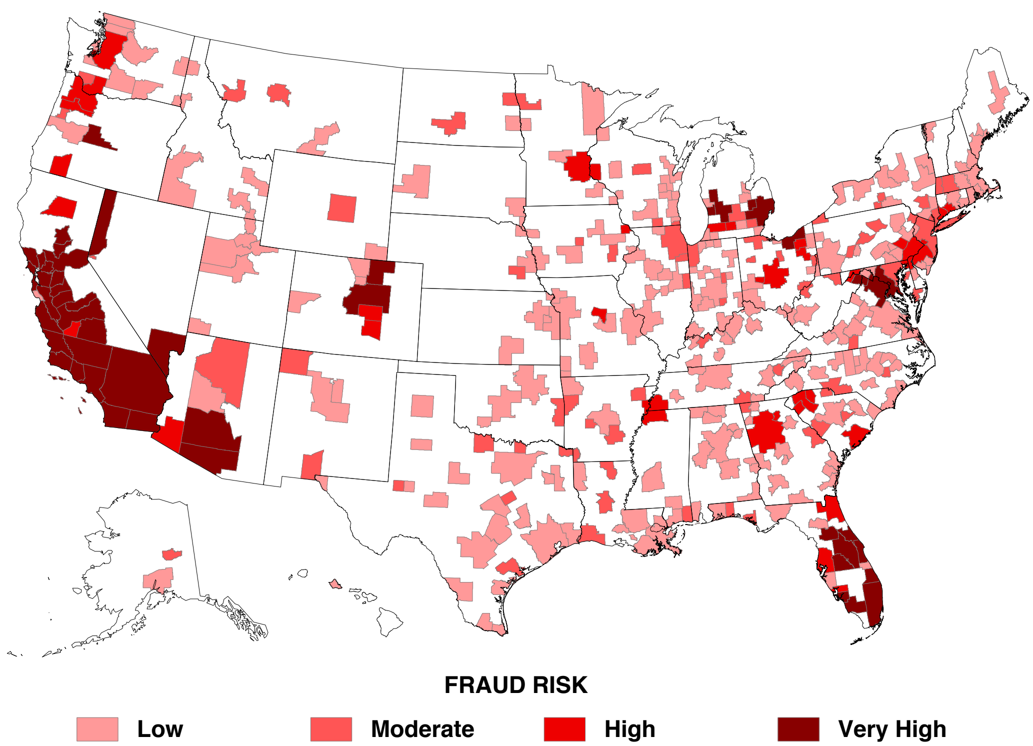


Figure 1: Mortgage Fraud Risk in Q4 2009 by Metropolitan Statistical Area (MSA)

Table 1 shows the Mortgage Fraud Risk Index for the 10 MSAs with the highest mortgage fraud risk. Seven of these are located in California, and as with past quarters, California's riskiest MSAs are concentrated in the inland regions of the state. This quarter, Modesto ranks worst nationally with an Index value of 303, compared to the national value of 145. Stockton, the most risky MSA the past two quarters, moves into second place with an index of 297. Cape Coral-Fort Myers Florida, Phoenix Arizona and Las Vegas Nevada complete the top 10. With the exception of Las Vegas, which has seen a 13% decrease in its index over the last year, all the other MSAs in the top 10 have seen increases of greater than 20%.

Rank	Metropolitan Statistical Area	Mortgage Fraud Risk Index Q4 2009	% Change Since Q4 2008	% Change Since Q3 2009
1	Modesto, CA Metro	303	71.8%	7.1%
2	Stockton, CA Metro	297	59.2%	-9.0%
3	Vallejo - Fairfield, CA Metro	297	83.7%	9.9%
4	Riverside - San Bernardino - Ontario, CA Metro	276	56.1%	-11.7%
5	Cape Coral - Fort Myers, FL Metro	271	70.0%	-0.1%
6	Salinas, CA Metro	266	29.1%	20.8%
7	Santa Rosa - Petaluma, CA Metro	242	58.0%	20.0%
8	Fresno, CA Metro	234	27.7%	-11.0%
9	Phoenix - Mesa - Scottsdale, AZ Metro	231	21.7%	-6.3%
10	Las Vegas - Paradise, NV Metro	229	-13.4%	-13.1%
United States		**145**	**-0.7%**	**0.2%**

Table 1: MSAs with the Highest Mortgage Fraud Risk Index in Q4 2009

Geographic Fraud Risk Migration

Mortgage fraud migrates geographically to take advantage of local market conditions. This section examines the geographic migration of mortgage fraud risk within the 50 States and the District of Columbia.

Figure 2 depicts the Fraud Risk Index for the individual states, with the ten highest risk states shown in red. California has the highest mortgage fraud risk, with an Index value of 222. Nevada, which had the highest index for the previous five consecutive quarters, drops to second place with an index of 220, and is closely followed by Arizona with an index of 211. Florida remains in fourth place with an index of 179, while Colorado is in fifth place at 153. The top 10 is rounded out by the capital region (Maryland, Washington DC and northern Virginia), and the hard-hit industrial states of Michigan and Ohio. The ten states with the lowest risk, shown in green, are West Virginia, Maine, Kansas, South Dakota, Montana, Wyoming, Alabama, Vermont, Mississippi and Iowa. The five lowest risk states have Index values of less than half the national value.

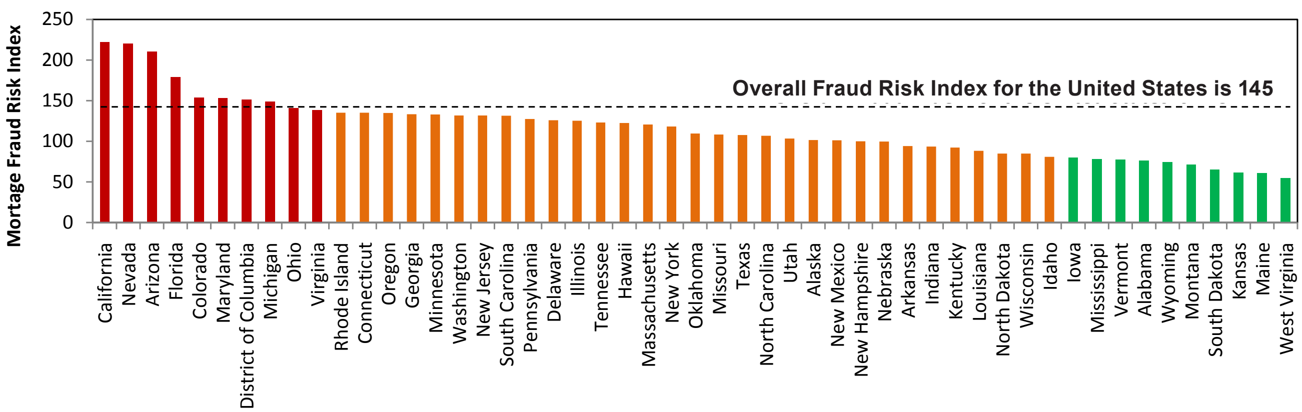


Figure 2: Mortgage Fraud Risk Index in Q4 2009 by State

Figure 3 shows the change in the Mortgage Fraud Risk Index from the last quarter. The indices for both California and Nevada actually fell by 10 and 31 points, respectively, from a quarter ago, but remain highly elevated. The much larger decrease in Nevada accounts for California moving to first place in the rankings. While the indices for the seven riskiest states all decreased from the last quarter, the indices for all ten of the least risky states increased. This represents a narrowing of fraud risk across the states, which is reflected in the decline in the Mortgage Fraud Risk Index spread from 215 points in Q3 2009 to 167 points in the current quarter. This is in direct contrast to the expansion of this index range observed between Q3 2008, when the range was 100, and Q3 2009, when it reached 215.

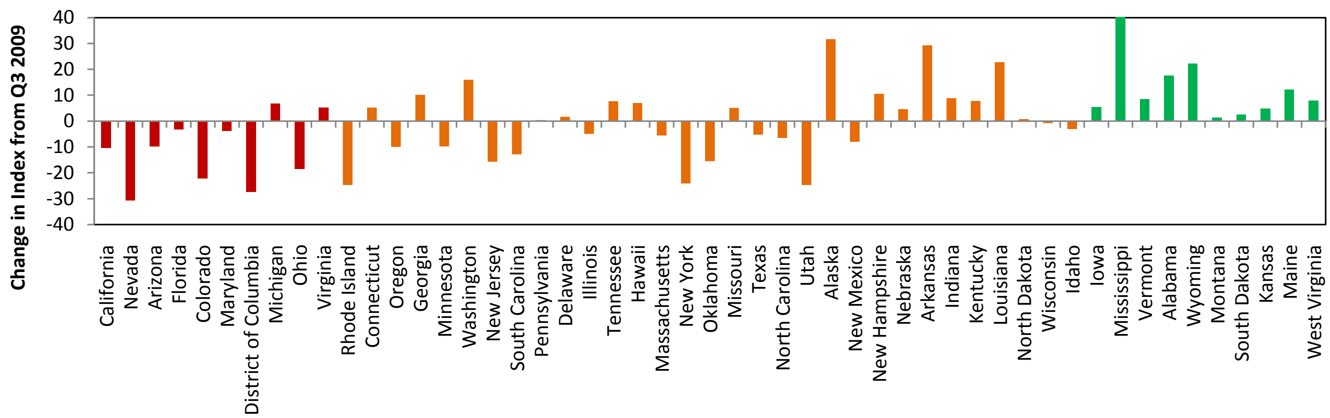
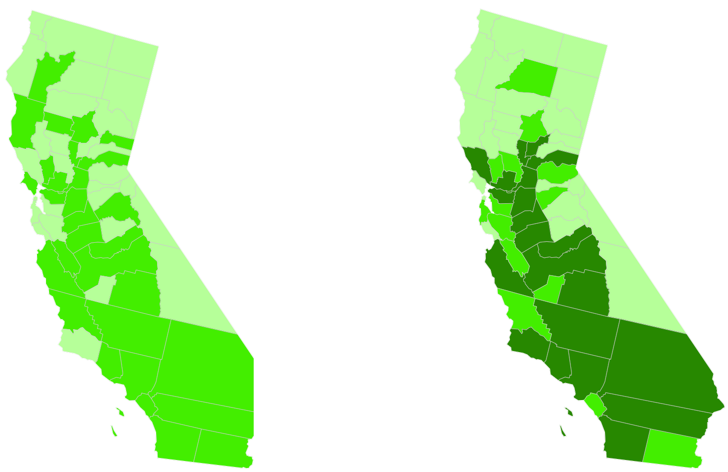


Figure 3: Change in Mortgage Fraud Risk Index between Q3 and Q4 2009 by State

California's movement into the top spot in the rankings is significant because of the sheer volume of loans issued in this state and the magnitude of the potential economic losses to lenders. In the past, numerous regions of relatively low risk counterbalanced and moderated California's overall fraud risk. However, as shown in Figure 4, the number of high risk counties in California has increased significantly, and fraud risk has spread dramatically throughout the state over the last year. In Q3 2008, the state's fraud risk was "relatively moderate", with no counties having an Index value exceeding 200. The relentless increase and spread of mortgage fraud risk between Q3 2008 and Q3 2009, starting in the Central Valley region, was described in the Interthinx Q3 2009 Fraud Risk report[1] and continues unabated. Despite the drop in the state's overall index from 230 to 220, the number of counties with very high mortgage fraud risk has increased from the last quarter, with four additional counties (Santa Barbara, Madera, Yuba and Sutter) breaching the 200 mark. Only one county that was previously above that benchmark dropped below 200 (Yolo).



MORTGAGE FRAUD RISK INDEX

less than 150 **150 to 200** **more than 200**

Figure 4: Mortgage Fraud Risk in California from 2008 Q3 to 2009 Q4

Type-specific Mortgage Fraud Risk Hot Spots and Trends

Interthinx tracks four type-specific fraud risk indices: Property Valuation, Identity, Occupancy and Employment/Income. This section examines the hot spots and trends for these type-specific fraud risks.

PROPERTY VALUATION FRAUD RISK INDEX

Property Valuation Fraud is perpetrated by manipulating property value to create "equity" which is then extracted from loan proceeds by various means. Table 2 shows that the four MSAs with the highest property valuation fraud risk are located in California, with Cape Coral-Fort Myers Florida rounding out the top 5. These MSAs have extremely high Index values in excess of 600, and their Property Valuation Fraud Risk Index values have increased 150% or more over the last year. Although the national index decreased 3.5% from the last quarter – the first quarter-on-quarter decrease since Q4 2007 – it has increased by 40% over the last year, continuing a strong trend that began in Q4 2006 when this index bottomed out as housing prices reached their peak.

Rank	Metropolitan Statistical Area	Property Valuation Fraud Risk Index Q4 2009	% Change Since Q4 2008	% Change Since Q3 2009
1	Vallejo - Fairfield, CA Metro	801	446.0%	16.1%
2	Modesto, CA Metro	787	206.9%	5.4%
3	Stockton, CA Metro	783	224.2%	-6.1%
4	Riverside - San Bernardino - Ontario, CA Metro	713	202.8%	-10.7%
5	Cape Coral - Fort Myers, FL Metro	671	158.7%	0.3%
United States		**273**	**40.3%**	**-3.5%**

Table 2: MSAs with the Highest Property Valuation Fraud Risk

Figure 5 illustrates that the sharp rise in the property valuation fraud risk index (dark blue) over the last two years offset decreases in the occupancy and employment/income fraud risk indices to become the major driver of the overall fraud risk index. This is also shown in Figure 6 by the strong correlation between the overall risk levels and property valuation fraud risk for MSAs throughout the United States.

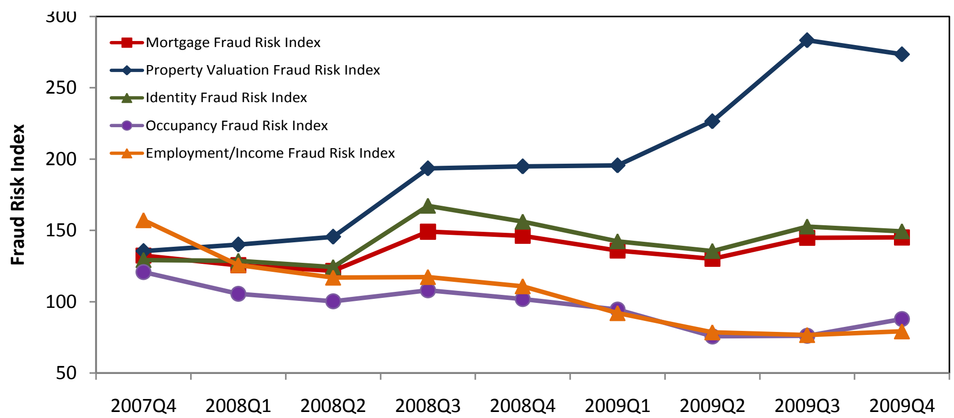


Figure 5: Mortgage Fraud Indices 2007 Q4 to 2009 Q4

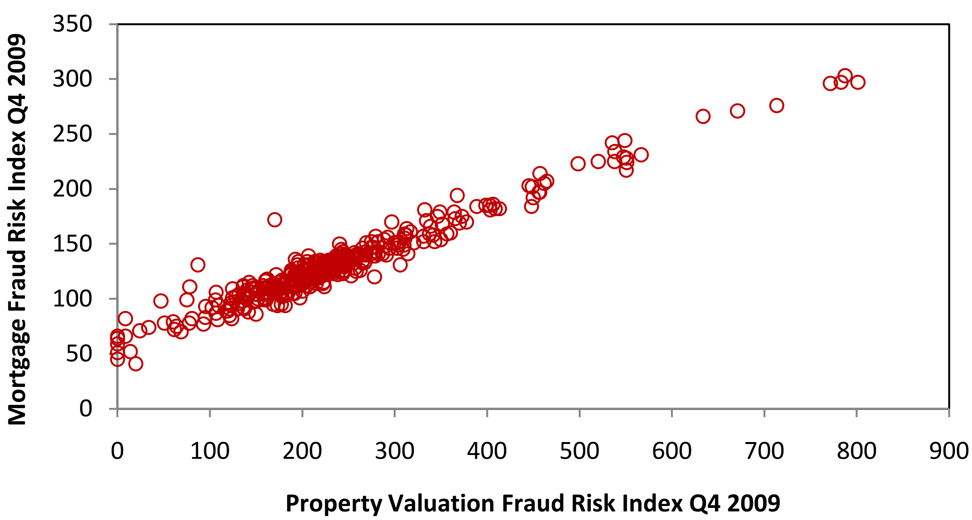


Figure 6: Mortgage Fraud Risk Index and Property Valuation Fraud Risk Index 2009 Q4 for all MSAs

It is no surprise that the states with the highest risk for property valuation fraud are also the states with the highest levels of "underwater" borrowers and foreclosure activity, as shown in Figures 7 and 8. Property valuation fraud risk in these geographies can be expected to continue at extremely high levels as "shadow" foreclosure inventories are released into the market, further depressing prices and encouraging additional walk-aways.

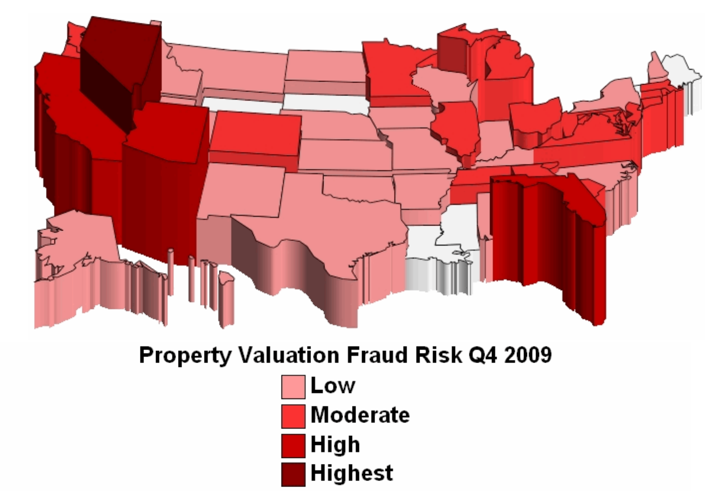


Figure 7: Underwater Loans and Property Valuation Fraud Risk Index 2009 Q4 by state
Elevation represents % of underwater loans[2].

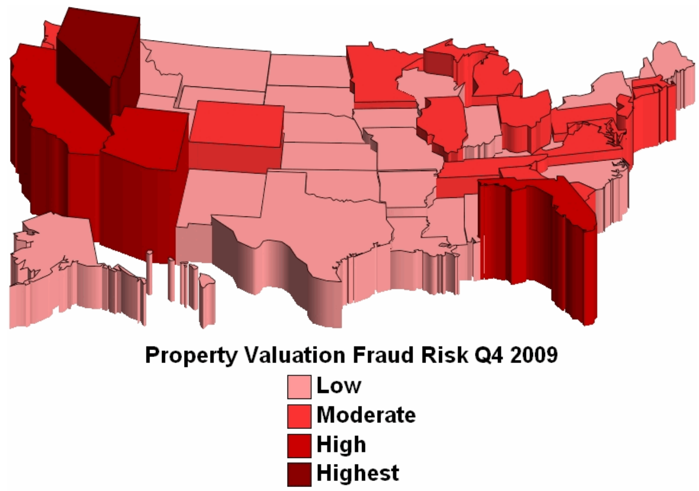


Figure 8: Foreclosure Rate and Property Valuation Fraud Risk Index 2009 Q4 by state
Elevation represents Foreclosure Rate in 2008[3].

EMPLOYMENT/INCOME FRAUD RISK INDEX

Employment/Income Fraud occurs when an applicant's income is misrepresented in order to qualify for a loan. Table 3 shows that while the Employment/Income Fraud Risk Index is down 29% over the last year, it increased 3.4% over the last quarter – the first increase since the Index peaked in Q3 2007 at 197. It is too soon to tell whether this uptick portends a rebound in employment/income fraud risk or whether it reflects a temporary "blip" associated with schemes involving the Federal First-time Homebuyer Tax Credit Program due to expire on April 30, 2010.

Index risk levels for the top five MSAs, four of which are in California, increased more than 20% from the last quarter. In contrast to the overall fraud risk in California, which is concentrated in the inland regions, employment/income fraud risk is greatest in MSAs along the coast where prices have not declined as much. Exaggerated employment/income occurs most often in high-cost MSAs where borrowers have difficulty meeting lenders' debt-to-income criteria. Reading PA, which also has a very high Occupancy Fraud Risk Index, rounds out this group.

Rank	Metropolitan Statistical Area	Employment/Income Fraud Risk Index Q4 2009	% Change Since Q4 2008	% Change Since Q3 2009
1	Santa Barbara - Santa Maria - Goleta, CA Metro	171	47.8%	85.8%
2	Santa Rosa - Petaluma, CA Metro	156	-5.7%	44.2%
3	Salina, CA Metro	152	20.3%	26.3%
4	Reading, PA Metro	140	48.8%	47.3%
5	San Luis Obispo - Paso Robles, CA Metro	140	26.7%	25.8%
United States		**79**	**-28.5%**	**3.4%**

Table 3: MSAs with the Highest Employment/Income Fraud Risk

OCCUPANCY FRAUD RISK INDEX

Occupancy Fraud is perpetrated by investors who falsely claim the intent to occupy the purchased property so as to obtain a mortgage with lower down payments and/or interest rates. The Occupancy Fraud Risk Index jumped 16% from last quarter after decreasing steadily since the Index peaked in Q4 2006 at 187. Following the very slight increase recorded between Q2 and Q3 2009, the Interthinx projection that this Index was poised for a rebound appears to be confirmed. Investor demand, stoked by plentiful inventories and the expected release of "shadow" inventory by lenders in 2010, is likely to propel this Index higher for the foreseeable future.

Table 4 identifies the top five MSAs in the Occupancy Fraud Risk Index. Reading, PA, with a nearly 400% increase, has surged to the top. The metros of Miami, currently in 2nd place, and Detroit, currently in 4th place, have been in the top five for three consecutive quarters. The California metros of Modesto and Fresno round out the table.

Rank	Metropolitan Statistical Area	Occupancy Fraud Risk Index Q4 2009	% Change Since Q4 2008	% Change Since Q3 2009
1	Reading, PA Metro	178	382.6%	171.8%
2	Miami - Fort Lauderdale - Pompano Beach, FL Metro	151	25.8%	28.2%
3	Modesto, CA Metro	142	24.0%	38.9%
4	Detroit - Warren - Livonia, MI Metro	135	-28.3%	13.5%
5	Fresno, CA Metro	134	19.6%	15.7%
United States		**88**	**-13.8%**	**15.5%**

Table 4: MSAs with the Highest Occupancy Fraud Risk

IDENTITY FRAUD RISK INDEX

Identity fraud is frequently used in mortgage fraud schemes in order to hide the identity of the perpetrators and/or to obtain a credit profile that will meet lender guidelines. The Identity Fraud Risk Index has remained relatively constant over the last two years, declining 2% from the previous quarter and 4% from a year ago. Table 5 shows that the top five MSAs are concentrated in the Southeast. The Florida metros of Naples-Marco Island and Miami bracket this group, which also includes Jackson Mississippi, Nashville Tennessee and Augusta Georgia. Over the last year, all five of these MSAs have experienced increases of greater than 50%.

Rank	Metropolitan Statistical Area	Identity Fraud Index Q4 2009	% Change Since Q4 2008	% Change Since Q3 2009
1	Naples - Marco Island, FL Metro	290	56.1%	5.8%
2	Jackson, MS Metro	255	97.1%	140.4%
3	Nashville - Davidson - Murfreesboro - Franklin, TN Metro	250	52.3%	39.4%
4	Augusta - Richmond County, GA-SC Metro	240	115.4%	94.8%
5	Miami - Fort Lauderdale - Pompano Beach, FL Metro	238	53.0%	12.8%
United States		**149**	**-4.3%**	**-2.2%**

Table 5: MSAs with the Highest Indentity Fraud Risk

Extended Forecast

The Interthinx Fraud Risk Indices have proven to be a leading indicator of foreclosure activity. Therefore, the regions that currently have high Fraud Risk Indices are likely to have high foreclosure rates going forward, particularly if housing prices continue on their downward trajectory and if there is no significant improvement in general economic conditions. Based on the Fraud Risk Indices, regions that bear close scrutiny going forward include:

- California, which rose by 61 to the highest Index of 222, experienced the largest one year increase. Seven of the ten highest risk MSAs are located in California, and many of its counties have index values greater than 200.
- Nevada, which despite losing the number one spot, still has a Mortgage Fraud Risk Index of 220.
- Arizona, which also has an Index value over 200.
- Florida, which has the fourth highest Index and contains a number of very high risk MSAs: Cape Coral-Fort Myers (in the top 5 MSAs for both mortgage fraud risk and property valuation fraud risk), Miami-Fort Lauderdale-Pompano Beach (in the top 5 MSAs for both identity and occupancy fraud risk), and Naples-Marco Island, (the highest identity fraud risk nationwide).

Interthinx also projects that while interest rates remain low, the predominant fraud type will continue to be related to property valuation as speculative investors and "flipping" return to the market, and as consumers attempt to refinance their mortgages despite reduced equity in their properties. Interthinx also expects a rebound in Occupancy fraud, particularly in light of investor demand, fueled by ample inventories and the expected release of "shadow" inventory. Interthinx expects that the Fraud Risk Index will continue to rise through 2011 as a wave of ARMs, the majority of which contain negative amortization features, recast for the first time.

About the Interthinx Fraud Risk Indices

The Fraud Risk Indices are calculated based on the frequency with which indicators of fraudulent activity are detected in mortgage applications processed by the Interthinx FraudGUARD® system, a leading loan-level fraud detection tool available to lenders and investors.

The Interthinx Fraud Risk Indices consist of the Mortgage Fraud Risk Index, which measures the overall risk of mortgage fraud, and the Property Valuation, Identity, Occupancy and Employment/Income Indices, which measure the risk of these specific types of fraudulent activity.

The Mortgage Fraud Risk Index considers 40+ indicators of fraudulent activity including property mis-valuation; identity, occupancy and employment/income misrepresentation; non arms-length transactions; property flipping; straw-buyers; “silent seconds”; and concurrent closing schemes. The four type-specific indices are based on the subset of indicators that are relevant to each type of fraudulent activity.

Each Index is calibrated so that a value of 100 represents a nominal level of fraud risk, a value calculated from the occurrence of fraudulent indicators between 2003 and 2007 in states with low foreclosure levels. For all five indices, a high value indicates an elevated risk of mortgage fraud and each Index is linear to simplify comparison across time and location.

The Interthinx Indices are leading indicators based predominantly on the analysis of current loan originations. FBI and FinCEN reports are lagging indicators because they are derived primarily from Suspicious Activity Reports (SARs), the majority of which are filed after the loans have closed. The time lag between origination and the SAR report can be several years. For this reason, the Interthinx Fraud Risk Indices’ top geographies and type-specific findings may differ from FBI and FinCEN fraud reports.

About the Interthinx Mortgage Fraud Risk Report

The Interthinx Fraud Risk Report represents an in-depth analysis of residential mortgage fraud risk throughout the United States as indicated by the Interthinx Fraud Risk Indices. It is published quarterly, on the last day of the month following the end of quarter. As part of the Fraud Risk Report, Interthinx will report on the geographic regions with the highest Mortgage Fraud Risk Index as well as those with the highest Property Valuation, Identity, Occupancy, and Employment/Income Fraud Risk Indices. The Interthinx Fraud Risk Indices track these risks in all States, Metropolitan areas, Counties and county equivalents, throughout the United States.

References

1. Interthinx: *Mortgage Fraud Risk Report*, Q3 2009.
2. WSJ.com: *"One in Four Borrowers is Underwater"*, November 24, 2009.
3. RealtyTrac: *U.S. Foreclosure Market Report*, 2008.

About Interthinx

Interthinx, Inc., a Verisk Analytics subsidiary, is a leading provider of proven risk mitigation and regulatory compliance tools for the financial services industry. Used at every point in the mortgage lifecycle to prevent mortgage fraud, compliance violations and to assess risk, Interthinx is relied upon by more than 1,100 customers, including 15 of the top 20 mortgage lenders and three of the top five largest financial institutions. With technology that earned Mortgage Technology Magazine's prestigious 10X Award as "a diagnostic and corrective solution of the highest order," Interthinx expertise in predictive analytics, data mining, and risk scoring sets the industry standard and directly increases the value of client portfolios. For more information, visit www.interthinx.com or call (800) 333-4510.

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