



AMERICA'S FINANCIAL RECOVERY:
Protecting Consumers as We Rebuild



2011 PRESIDENTIAL INITIATIVE SUMMIT
April 11-12, 2011 • Charlotte, NC

Follow the Money: How Systemic Bank Fraud Contributed to the Financial Crisis

Barry Ritholtz

The National Association of Attorneys General
Presidential Initiative Summit

America's Financial Recovery: Protecting Consumers as We Rebuild

April 11-12, 2011

The Westin Hotel

Charlotte, NC

Bad Decision Making + Systemic Fraud = Financial Crisis

- 1 Ultra low interest rates led to a scramble for yield by fund managers;
- 2 Subprime lending by unregulated, non-banks who existed solely to sell these mortgages to securitizers;
- 3 Collapsed lending standards by non-bank underwriters allowed them to write many more mortgages; (writing mortgages for resale meant they only held briefly);
- 4 Poorly underwritten loans — essentially junk paper — were sold to Wall Street for securitization in huge numbers.
- 5 Massive ratings fraud of these securities by Fitch, Moody's and S&P led to a rating of this junk as TripleAAA.
- 6 Investment grade rated junk allowed scrambling bond managers (see #1) to purchase higher yielding paper that would not have otherwise been allowable.
- 7 Increased leverage of investment houses allowed huge securitization manufacturing process; iBanks also purchased this paper in enormous numbers;
- 8 Derivatives market allowed more leverage to take place. Firms like AIG wrote \$3 trillion in derivative exposure, much of it in mortgage and credit related areas.
- 9 Compensation packages in the financial sector were asymmetrical, where employees had huge upside but shareholders (and eventually taxpayers) had huge downside. This (logically) led to increasingly aggressive and risky activity.
- 10 Home prices that ran up due to low rates, sub-prime, came down when rates rose, credit tightened. This led to all of the above falling apart.

Today's presentation:



"OK, I'm now going to read out loud every single slide to you, word for word, until you all wish you'd just die."

Questions About the Crisis: *Follow the Money*



What was “Origination fraud”?

Who profited from the legal “shortcuts”?

Where are the conflicts of interest?

Can you ‘Mass Produce’ mortgages/foreclosures?!

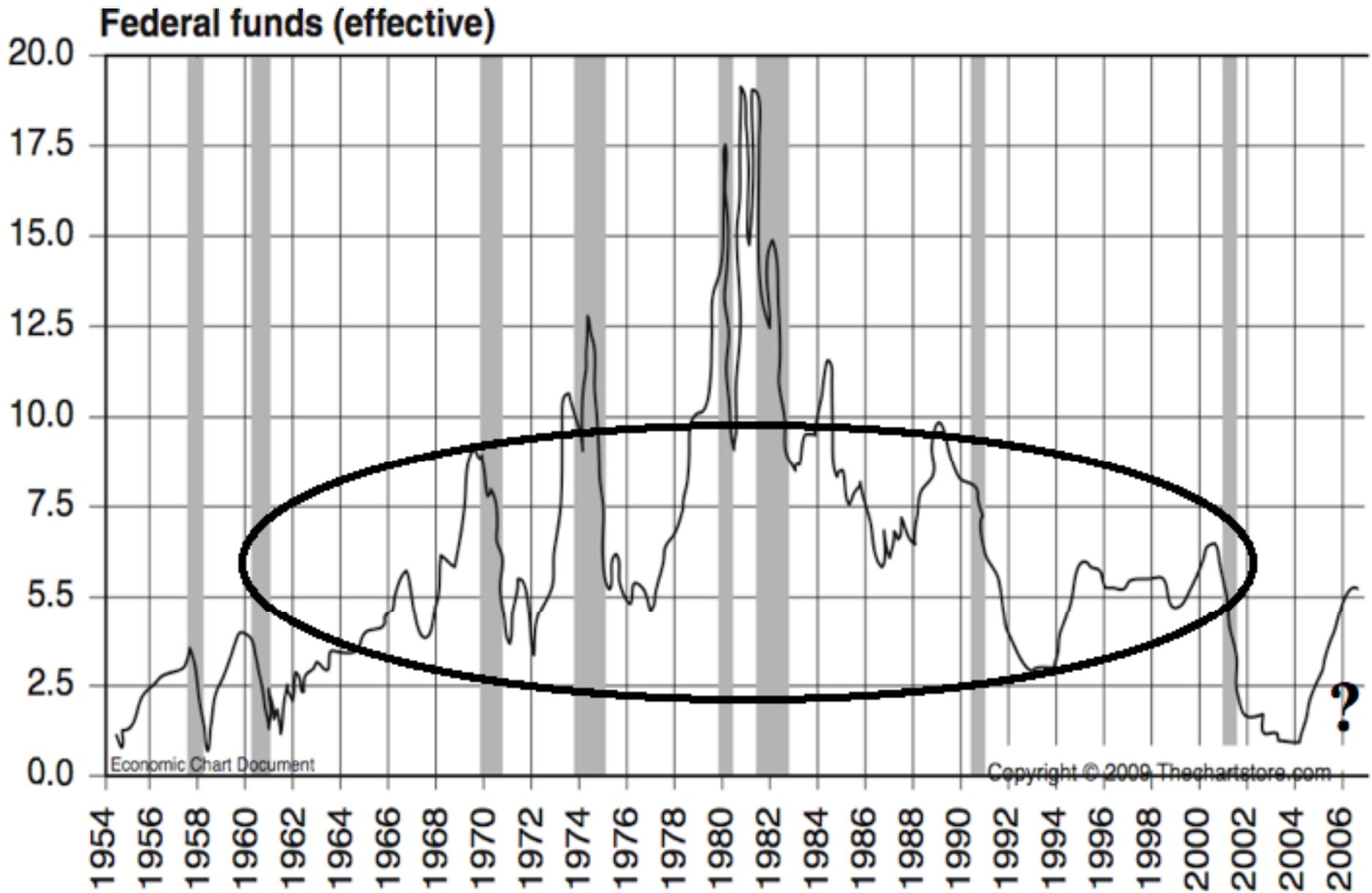
What are the ongoing bank frauds?

How many false affidavits have been filed in courts all over the country?

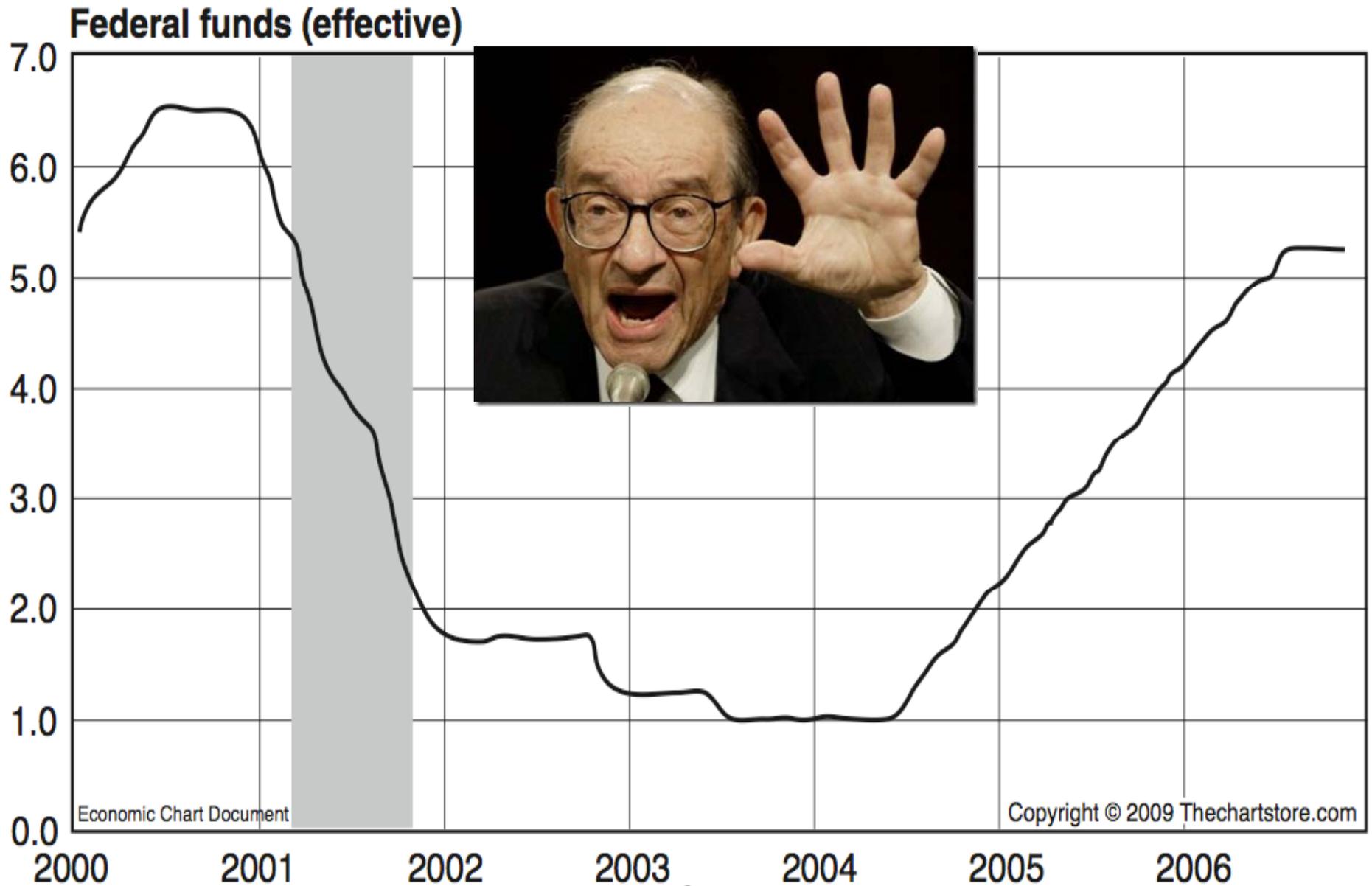
How is your own state doing?

Federal action vs State AG Investigation

Fed Funds Rate, 1954-2006

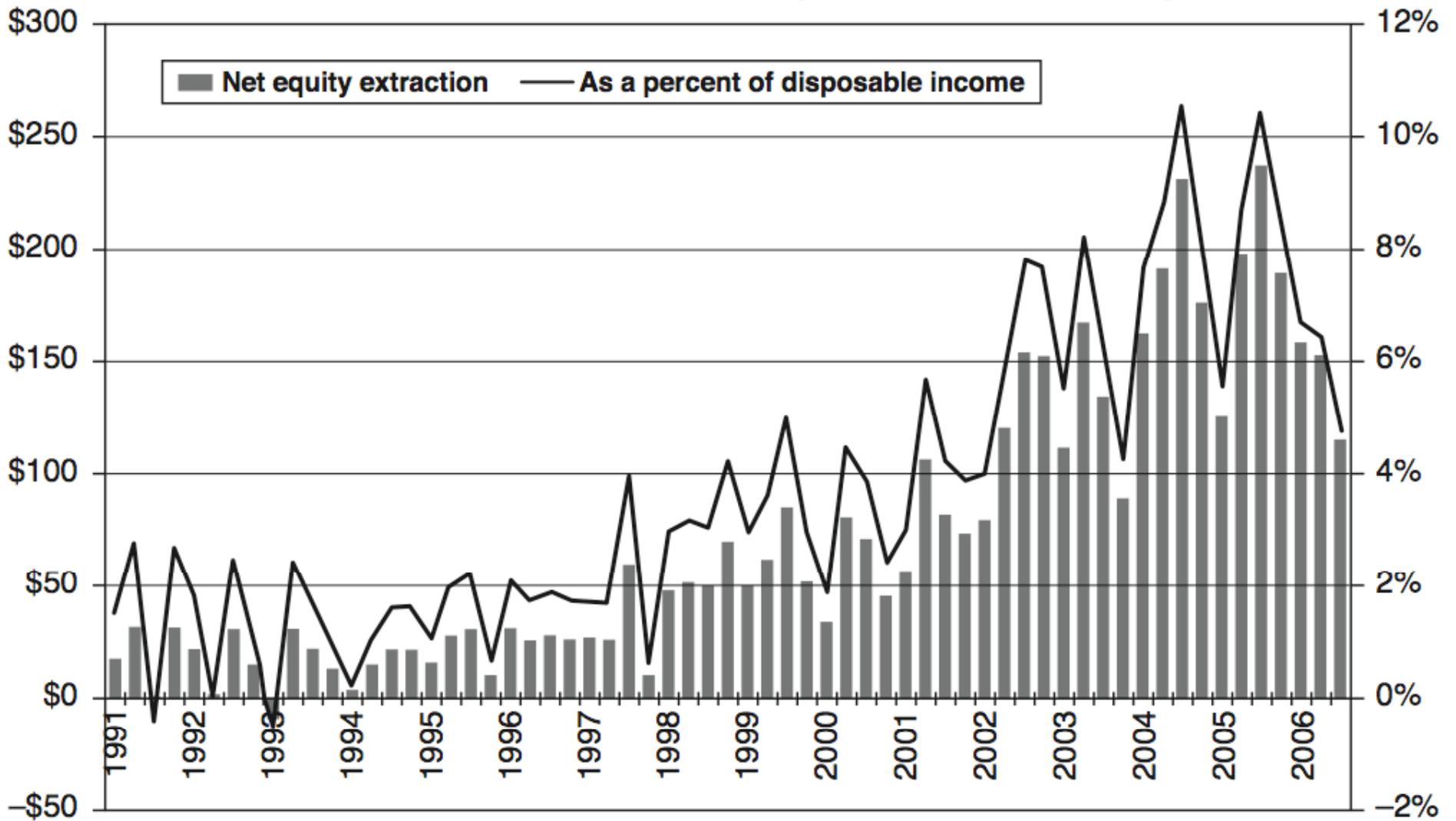


Federal Funds Rate 2000-06

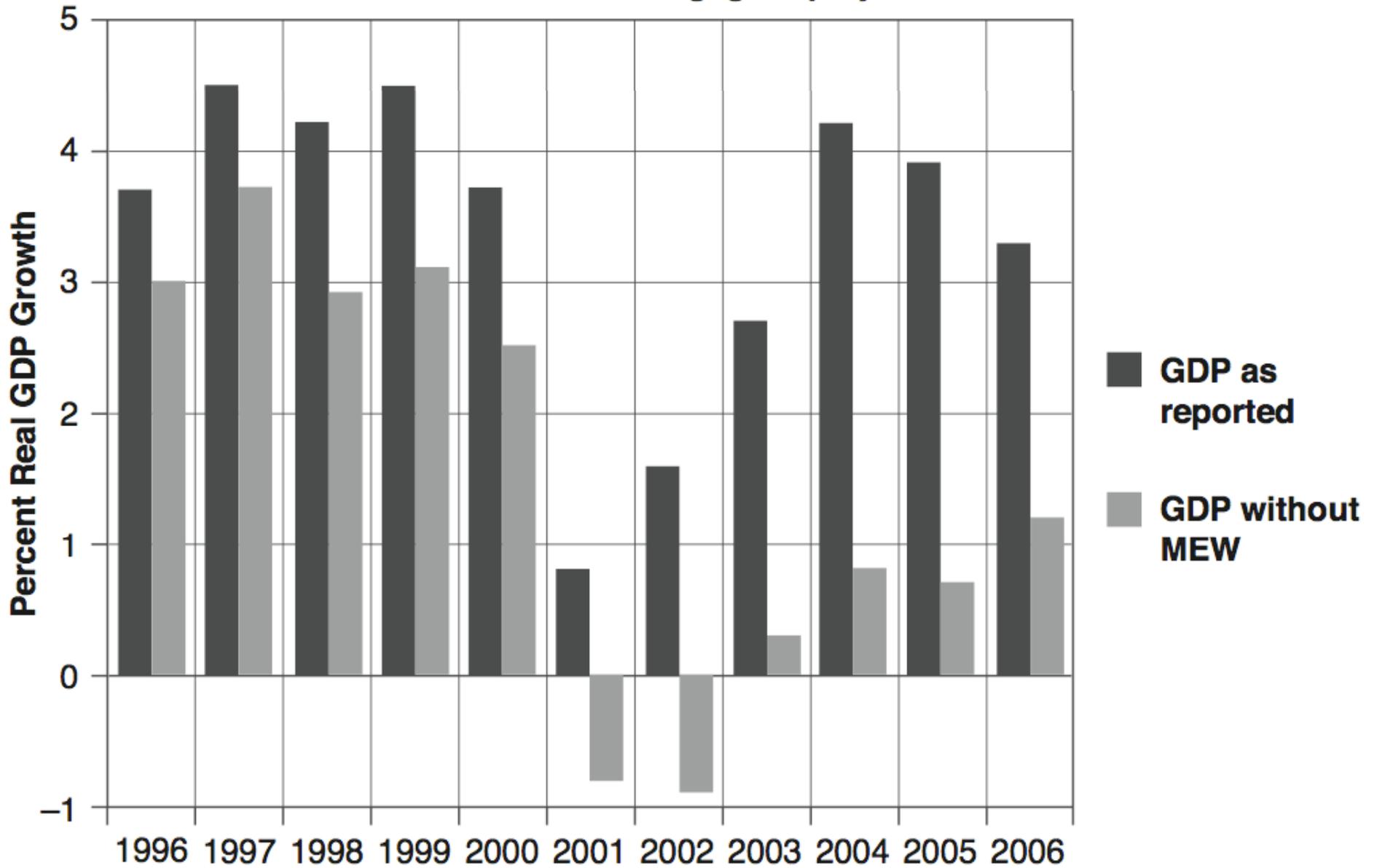


Living Standards = Flat Wages + Home Equity

MEW, Billions Dollars, Quarterly, Greenspan-Kennedy

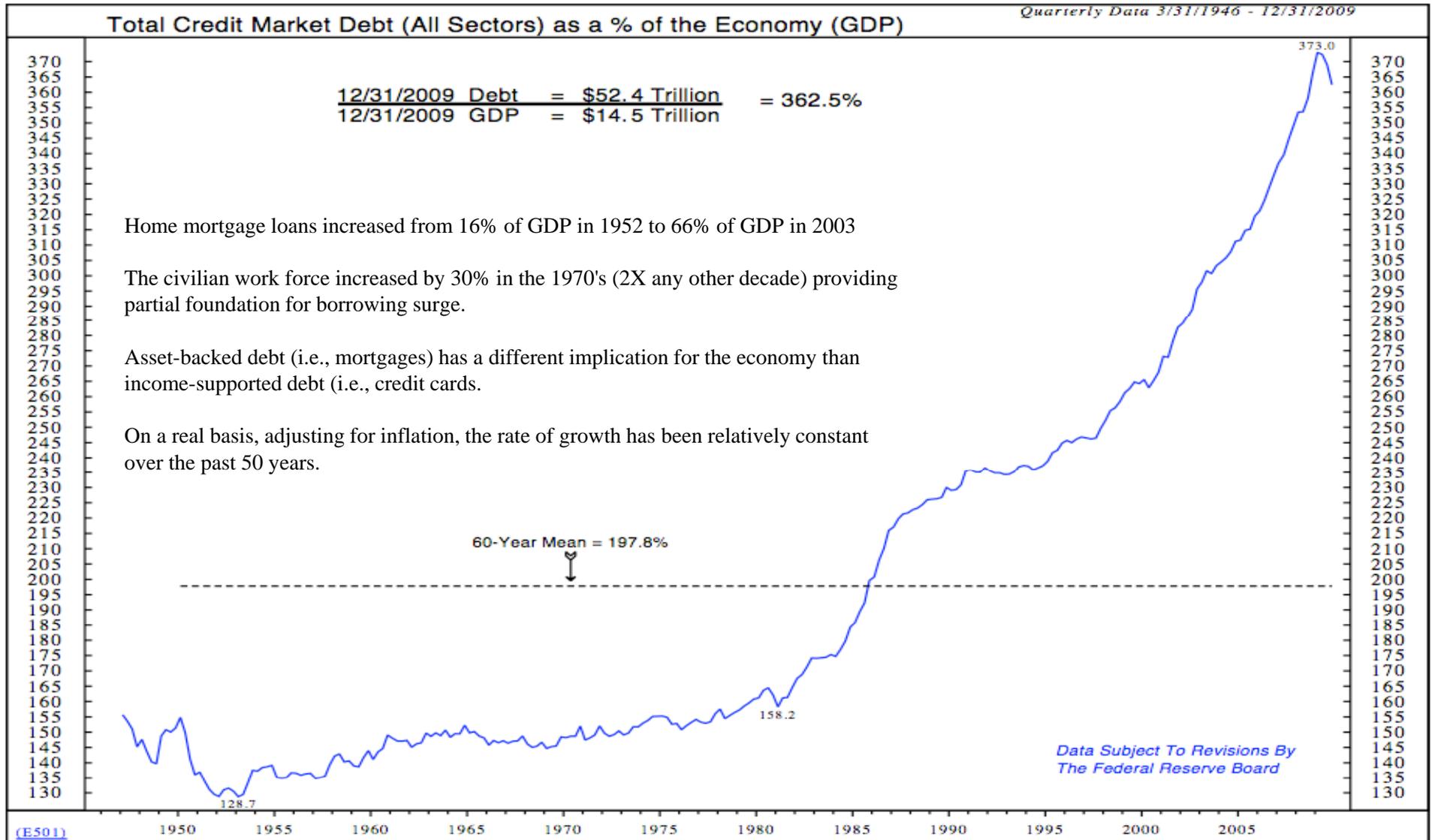


GDP Growth: With and Without Mortgage Equity Withdrawal

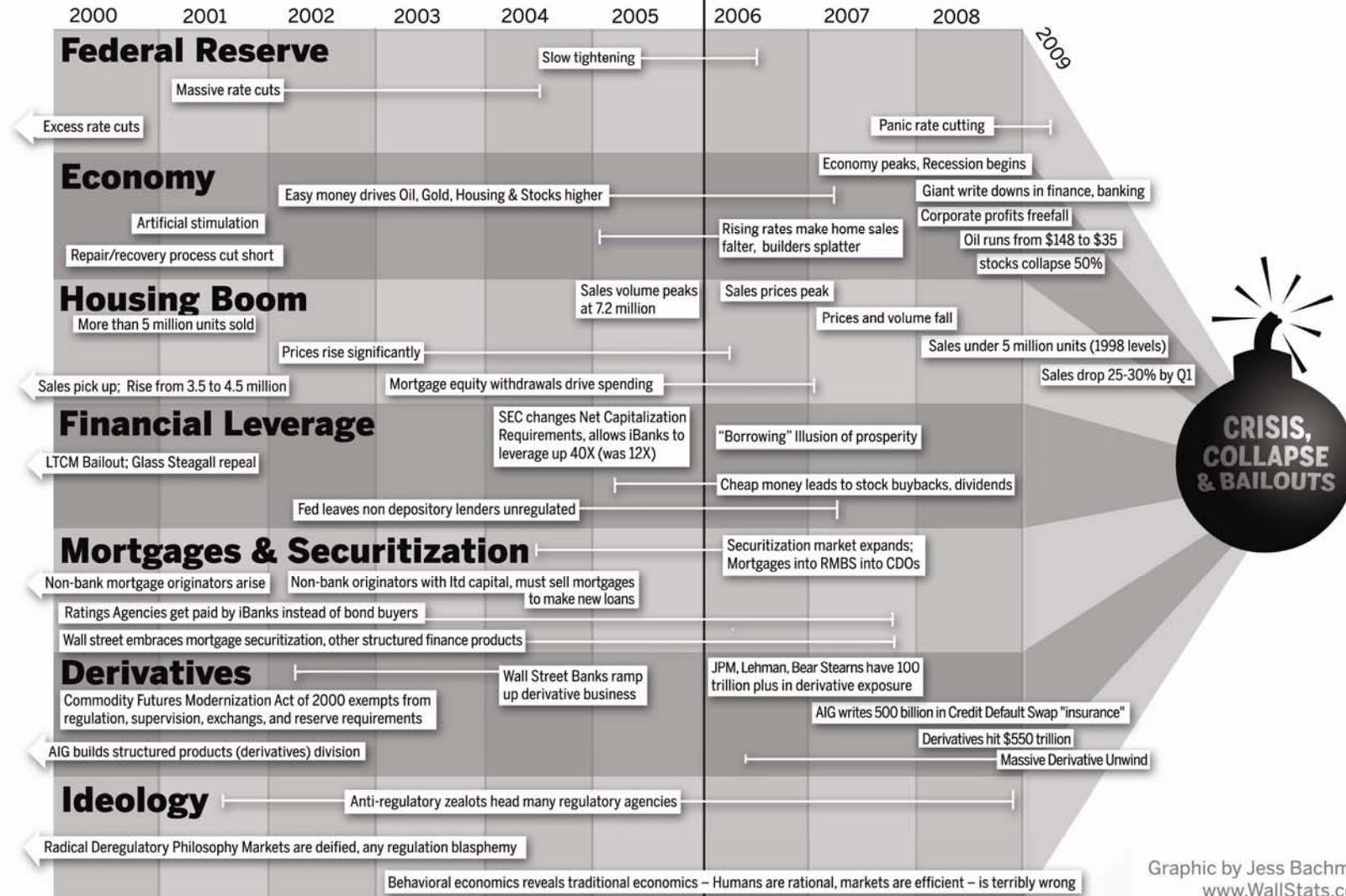


Total Credit Market Debt/GDP

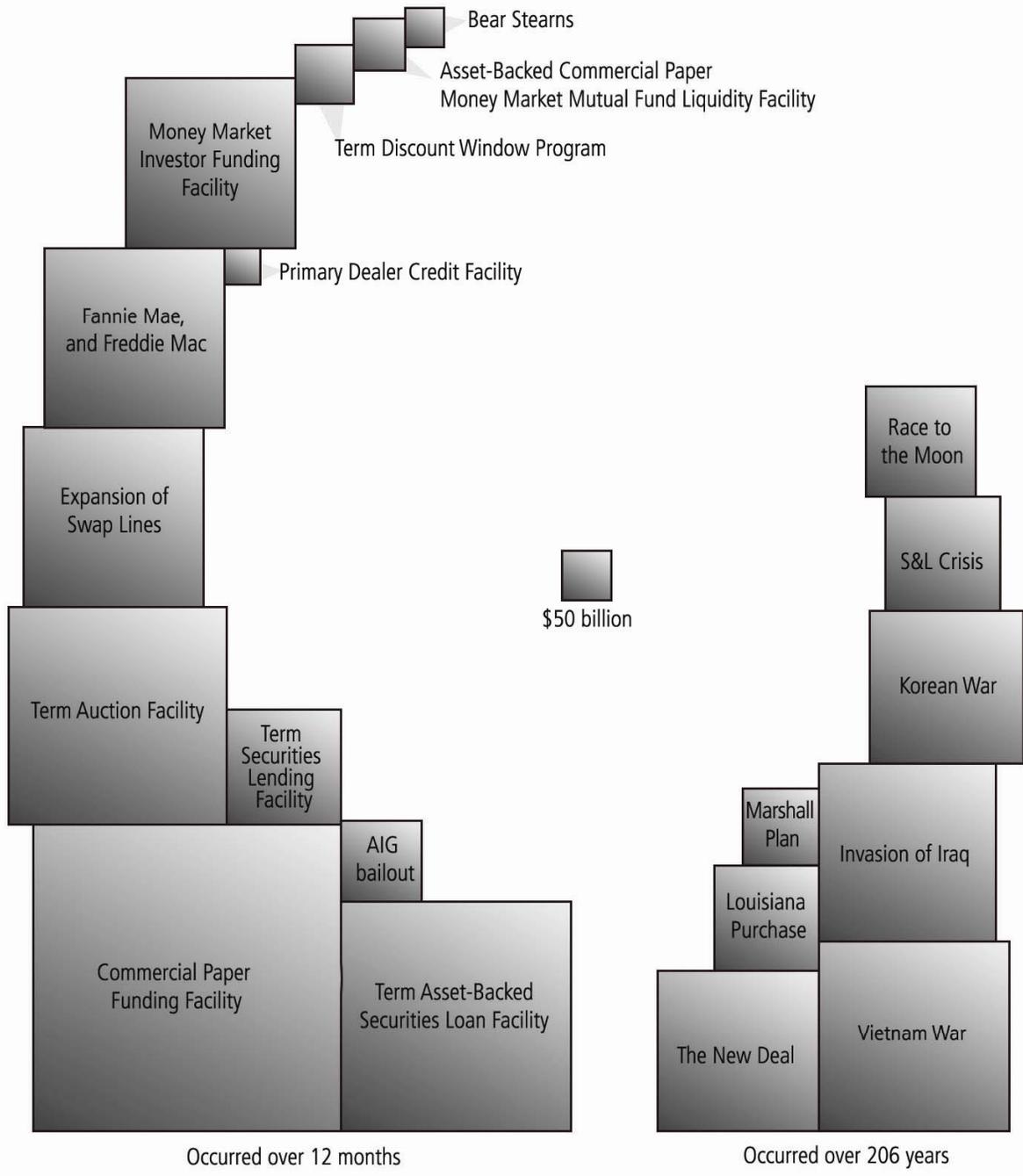
(Quarterly Data 1946 - 2009)



Anatomy of a Collapse



Graphic by Jess Bachman
www.WallStats.com



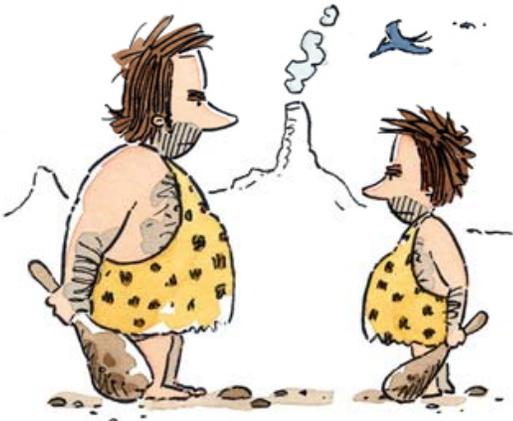
Occurred over 12 months

Occurred over 206 years



The Credit
Bubble and
Housing
Boom's
Shaky
Foundation

A Brief History of Commercial Credit



• 1 Million B.C. -----//---[2002-07]---//--2010-->



Origination Fraud: Lenders Get “Creative”

The business of banks is identifying good lending risks...

Compared to 30 Year Fixed Mortgage

1. 2/28 ARMs
2. Interest Only
3. Stated Income Loans (No doc)
4. Piggyback Mortgages (1st plus 2nd)
5. Negative Amortization Loans
6. Payment “Option”
7. No money down (100% LTV)
8. NINJA (No Income, No Job, No Assets)

. . . Or was it ?

Origination Fraud: Why Did Lenders Accept Stated Income Loans?

“Eliminate the verification of income for a mortgage borrower, and you eliminate your ability to predict the likelihood of repayment or default.”

-Michael White, CountryWide Subprime Unit

2004: FBI Warns Rampant Mortgage Fraud Reaching Epidemic Proportions

Rampant fraud in the mortgage industry has increased so sharply that the FBI warned Friday of an "**epidemic**" of financial crimes which, if not curtailed, could become "the next S&L crisis."

Assistant FBI Director Chris Swecker said the booming mortgage market, fueled by low interest rates and soaring home values, has attracted unscrupulous professionals and criminal groups whose fraudulent activities could cause multibillion-dollar losses to financial institutions.

"It has the potential to be an epidemic," said Swecker, who heads the Criminal Division at FBI headquarters in Washington. "We think we can prevent a problem that could have as much impact as the S&L crisis," he said. -CNN

Lend-to-Sell-to-Securitizers Model Systemized Fraud

How Fraud led to a Credit Bubble

1. Traditional underwriting standards ignored
2. Extreme growth in “hot” areas vs. core business
3. Automation of traditional human judgment (Zippy)
4. Extreme leverage
5. Insufficient Loss Reserves
6. Little Retention of Loan
7. Extreme compensation of Sales People and Management

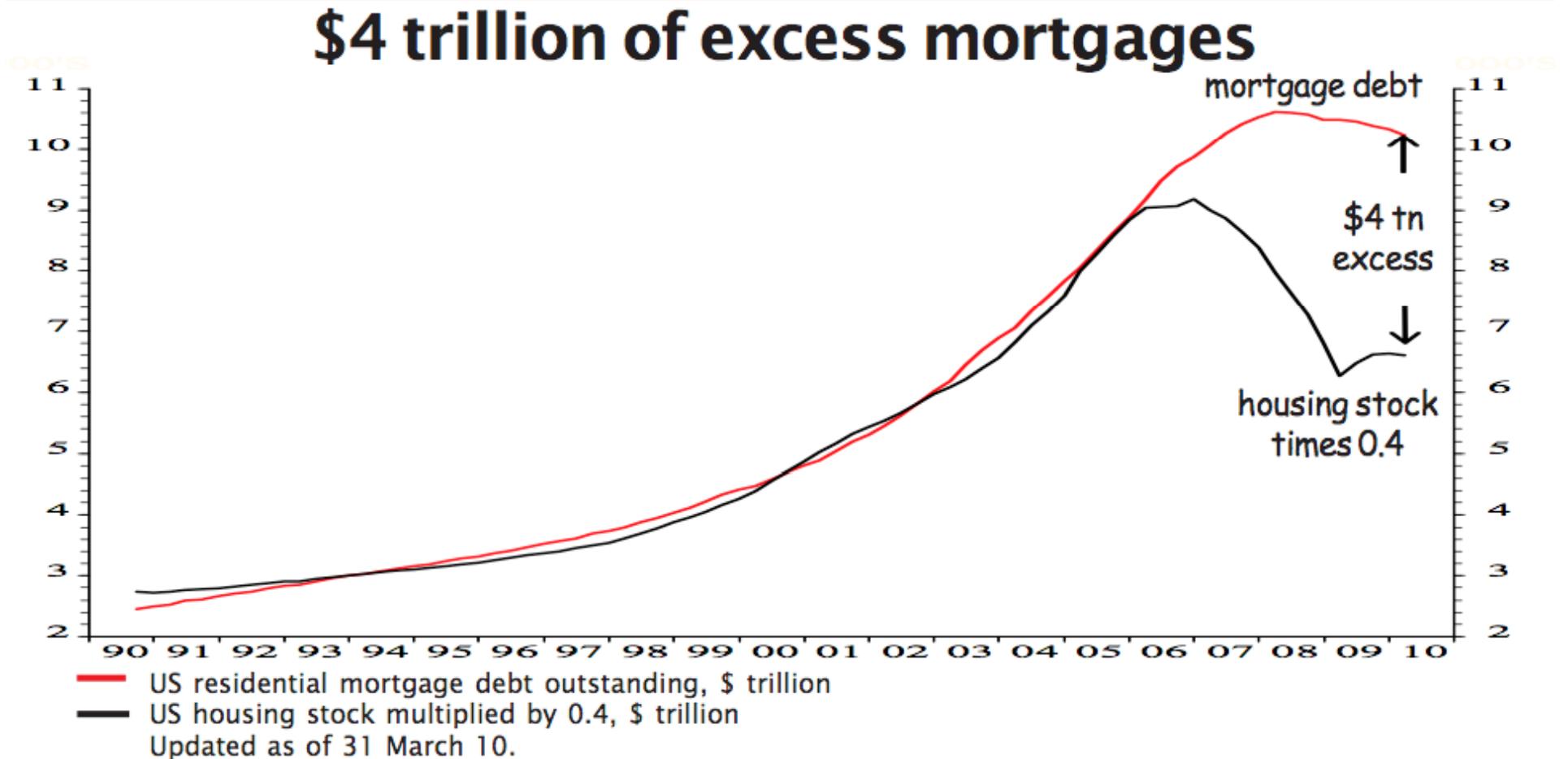
How did two \$15k strawberry pickers qualify for \$750k mortgage?

What Were the Warranties of Sold Mortgages

Excess Mortgage Debt

1990: \$6 trillion of housing collateral could support \$2.5 trillion of mortgages
2006: \$23 trillion of housing collateral could support \$10 trillion of mortgages
2010: \$16 trillion of housing collateral could support \$6 trillion of mortgages.

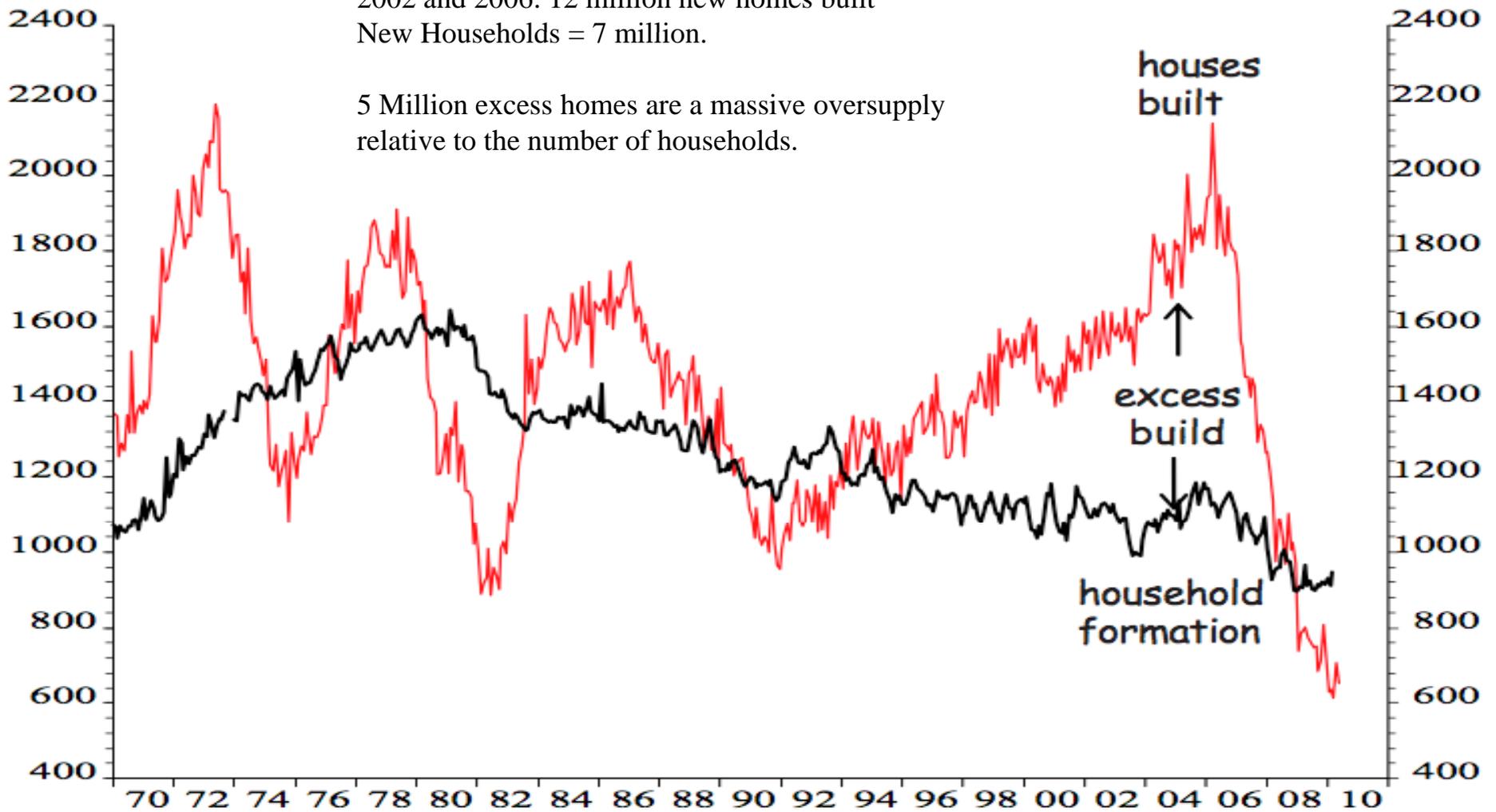
Problem is, mortgage debt has remained at \$10 trillion – \$4 trillion too high.



US Homebuilder's Construction Binge

2002 and 2006: 12 million new homes built
New Households = 7 million.

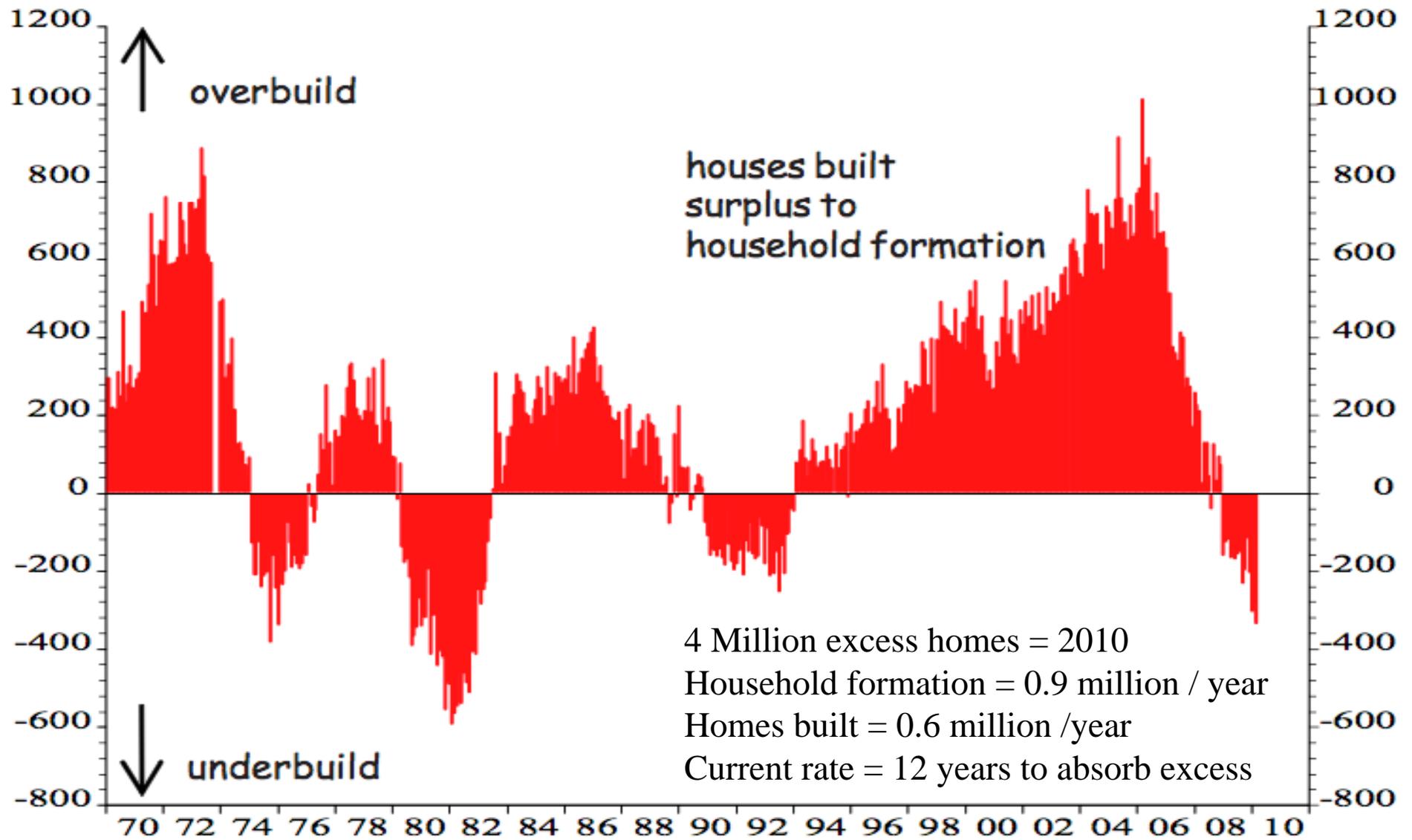
5 Million excess homes are a massive oversupply
relative to the number of households.



— US: net* new housing units created, thousands, annualised rate
— US: number of households created, thousands, annualised rate
Updated as of 31 May 10.

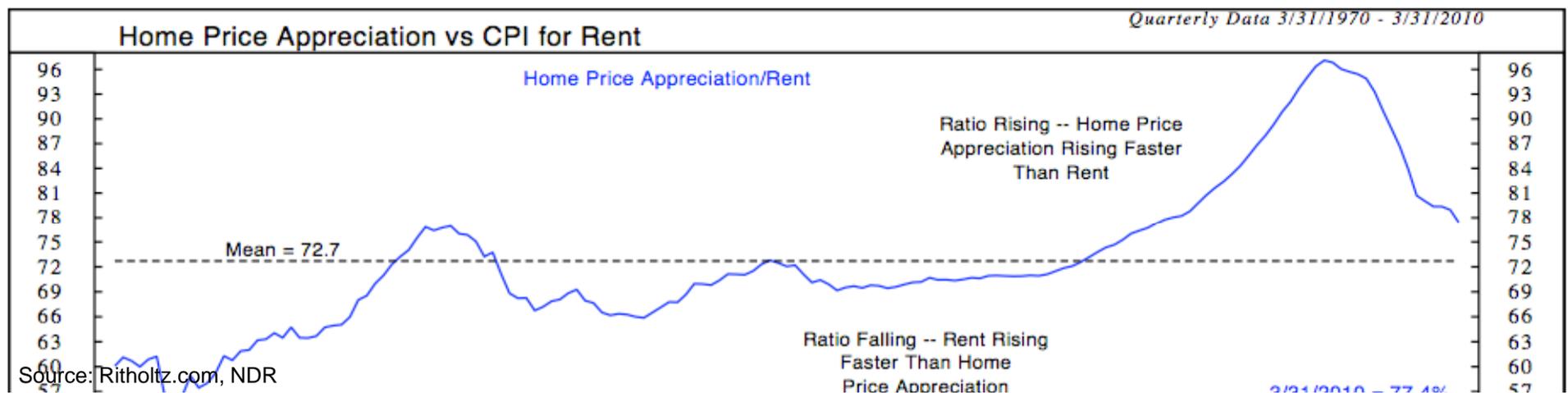
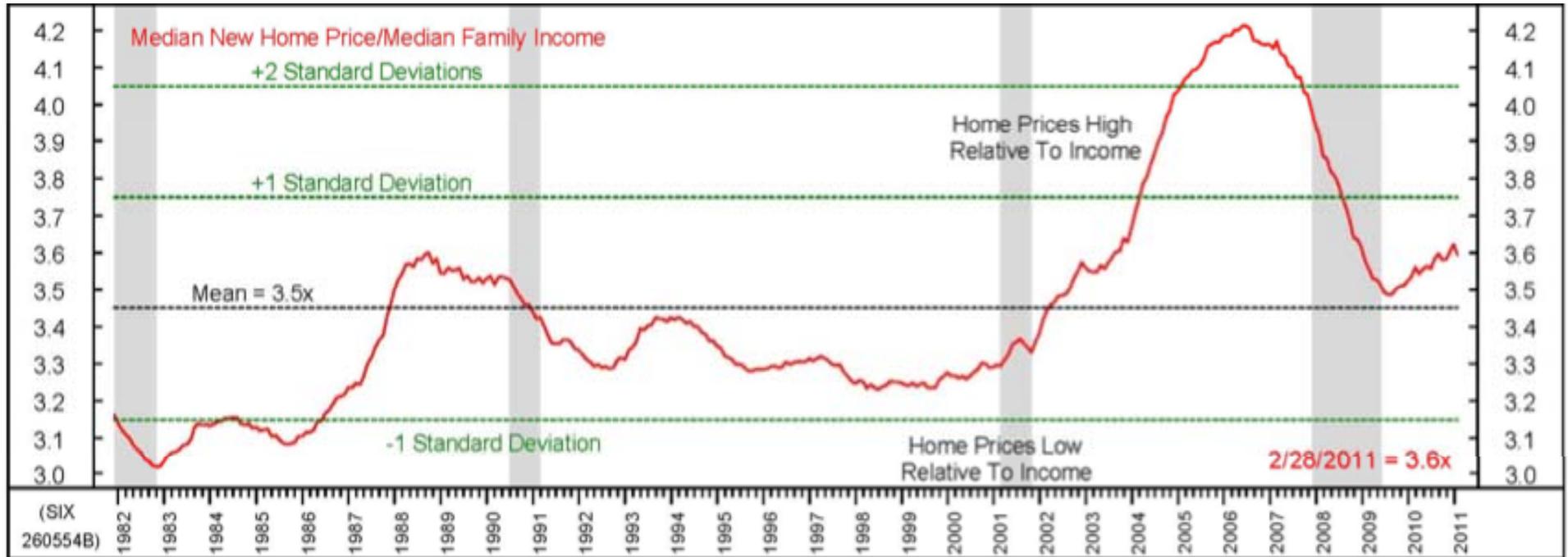
* housing units created less units destroyed

US Homebuilder's Construction Binge



US net new housing units created surplus to household created, thousands, annualised rate. Updated as of 31 May 10.

Residential Real Estate Relative to Median Income, Rent



Follow the Money:

Emphasis on Speed & Cheapness (Dubious Legality be damned!)

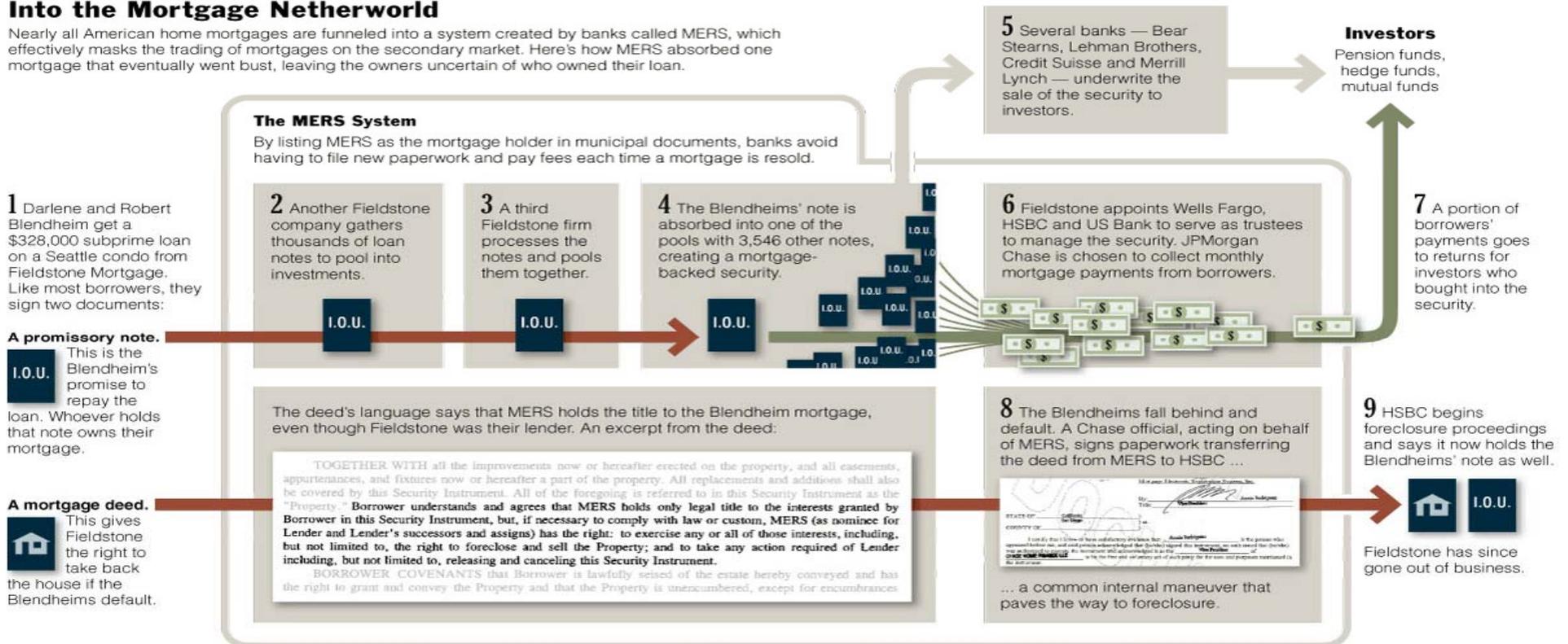
1. MERS
2. Mortgage Pools (Warranties & Reps)
3. Bad Securitization (Quality)
4. “Misplaced” Mortgage Notes
5. Force-Placed Insurance
6. Illegal “Pyramid” Servicing Fees
7. Document Fraud for Sale
8. False Affidavits, Perjury (Robo-Signing)
9. Foreclosure Mills, Process servers exasperate problem
10. Active Servicemen losing homes while on tour of duty

Follow the Money: MERS

1. “Legal Fiction” created by banks without authority or enabling legislation
2. MERS helped banks circumvent mortgage filing fee requirements
3. No fees = made mass-securitization of mortgages financially feasible
4. Allowed Notes/Mortgages to be shifted rapidly to multiple subsequent owners
5. Substantial percentage of MERS assignments were for entities that did not exist
6. Currently: Losing rulings 3-to-1 standing/right to foreclose (4.11.11 Salazar in California)

Into the Mortgage Netherworld

Nearly all American home mortgages are funneled into a system created by banks called MERS, which effectively masks the trading of mortgages on the secondary market. Here's how MERS absorbed one mortgage that eventually went bust, leaving the owners uncertain of who owned their loan.



Follow the Money: Force-Placed Insurance

“Evidence of abuses and self-dealing in the force-placed insurance industry suggests that there may be far larger problems in how servicers are handling distressed loans than the sloppy document recording that has been the recent focus of industry woes.”

-[American Banker](#), November 2010

UPDATE: New Questions about Banks' Force-Placed Insurance Deals

[American Banker](#), April 12, 2011

Agent, Writer

The top servicers' approaches to force-placed insurance

Wells Gets commissions from three force-placed insurers it works with, the company says

B of A Acquired Balboa Insurance Group, which writes force-placed insurance, in its purchase of Countrywide

JPMorgan Has told some borrowers that an affiliate will reinsure “some or all of the coverage and premiums” placed on their homes

Sharing in the Profits

How servicers make money arranging force-placed coverage

Commissions

To replace lapsed homeowners coverage, the servicer, working through a subsidiary, buys policy from insurer

Servicer advances premiums to insurer

Insurer pays portion of premium back to subsidiary as a commission

Servicer bills borrower for the policy

If borrower defaults, cost of insurance is subtracted from proceeds to investors from foreclosure sale



Reinsurance

To replace lapsed coverage, servicer buys policy on home from insurer

Servicer advances premiums to insurer

Subsidiary of servicer reinsures part of the policy, gets a cut of premiums

If necessary, subsidiary buys letter of credit from another party

Servicer bills borrower for the policy

If borrower defaults, cost of insurance is subtracted from proceeds to investors from foreclosure sale

Follow the Money: Servicing Errors and Fraud

National Consumer Law Center: 50% of cases are “servicer driven foreclosures.”

When a payment is received past due, a late fee is assessed versus next month’s payment.

The borrower makes his regular payment, but instead of being applied to P&I, it goes towards the fee. And since there is now a new shortfall, the borrower gets assessed an “insufficiency” fee and a late fee. These fees “**pyramid.**”

Two late fees, and some pooling and servicing agreements require a broker price opinion (BPO), typically about \$250. Less than an appraisal, it’s a drive by photo shoot/price guesstimate of what it might be worth.

Despite making all of their payments, out of the blue, this borrower gets a call from the servicer, or worse, a foreclosure notice.

Since when does delinquency inevitably = default?

Follow the Money: Document Fraud for Sale



DOCX's GetNet™ Document Recovery solution is a national network of runners that is engaged to provide document recovery, expedited recordation services, title searches, and insurance submissions.

The service is unique in that our clients can request that DOCX obtain any missing recordable documents through this web site through our online GetNet™ Work Order Form. Status of existing projects can also be obtained through our Online Services. We also accept work orders the "old fashioned" way via fax or mail. Upon receipt of the work order, DOCX will access the national network of runners, place the order and follow up to ensure prompt delivery.

GetNet™ was designed to assist mortgage servicers in meeting agency certifications and to avoid costly penalties for filing late satisfaction pieces.

GetNet™ Features

- A National Network of title runners retains presence in every county jurisdiction nationwide.
- Obtains missing mortgage documents, assignments, title policies and LGC/MICs.
- Expedites recordation by physically walking documents in to county recorder offices.
- Provides title searches to identify mortgage holders.
- Provides online reporting capabilities.

GETNET™ RATE SHEET

XCODE	SERVICE	AMOUNT
INF1	Obtain PIN Number from Online Public Records	\$5.50 + SH
INF2	Obtain from Online Public Records Lot Block or Section	\$5.50 + SH
INF3	Obtain Property Address	\$5.50 + SH
INF4	Obtain Recorded Mortgage, Book, Page or Instrument Number	\$12.95 + TPC
INF5	Obtain Vehicle Identification Number	\$12.95 + SH
CT01	Cursory Title Search to Identify Mortgagee of Record	\$15.95 + TPC
TS01	Perform Complete Title Search	\$15.95 + TPC
SI01	Obtain Copy of Mortgage	\$12.95 + TPC
SI02	Cure Defective Mortgage	\$12.95 + TPC
SI03	Retrieve Certified Copies of Mortgages	\$12.95 + TPC
PA01	Obtain Copy of Power of Attorney or Name Certification	\$12.95 + TPC

Follow the Money: Bank Outsourcing to Low Cost Legal Bidders Part of the Problem

“Fannie Mae was warned in a 2006 internal report of abuses in the way lenders and their law firms handled foreclosures, long before regulators launched investigations into the mortgage industry’s practices.

The report said foreclosure attorneys in Florida had “routinely made” false statements in court in an effort to more quickly process foreclosures and raised questions about whether some mortgage servicers or another entity had the legal standing to foreclose.”

Fannie Report Warned of Foreclosure Problems in 2006

WSJ, MARCH 25, 2011

Follow the Money: False Affidavits Suborning Perjury

“When Stephan says in an affidavit that he has personal knowledge of the facts stated in his affidavits, he doesn’t.

When he says that he has custody and control of the loan documents, he doesn’t.

When he says that he is attaching ‘a true and accurate’ copy of a note or a mortgage, he has no idea if that is so, because he does not look at the exhibits.

When he makes any other statement of fact, he has no idea if it is true.

When the notary says that Stephan appeared before him or her, he didn’t.”

-Thomas A. Cox, a retired lawyer, describes GMAC’s foreclosure process

Legally “Impossible” Foreclosures

- Lawsuit accuses Bank of America of seizing wrong house: Dr. Alan Schroit filed the lawsuit Monday in the 122nd State District Court in Galveston against the bank with which he has neither a relationship nor a mortgage. ([The Galveston County Daily News](#))
- Christopher Hamby of Wheelwright, Ky., filed a lawsuit against Bank of America for repossessing his home by mistake and refusing to pay for damages other than replacing the locks. ([Floyd County Times](#))
- Jason Grodensky bought his modest Fort Lauderdale home in December, he paid cash. But seven months later, he was surprised to learn that Bank of America had foreclosed on the house, even though Grodensky did not have a mortgage. ([Sun Sentinel](#))
- A Hampton Pennsylvania woman is suing Bank of America, saying one of its contractors wrongly repossessed her home, padlocked the doors, shut off the utilities, damaged the furniture and confiscated a pet parrot, though her mortgage payments were on time. ([Pittsburgh Post-Gazette](#))
- Charlie P. and Maria Cardoso of New Bedford claimed that their home in Florida was free of any mortgage. They filed a lawsuit for a wrong foreclosure, claiming that the Bank of America had foreclosed. Their lawyers argued that the Bank had already been notified about the wrong foreclosure, in July, despite which it got foreclosed ([South Coast Today](#))
- A Las Vegas woman whose condo was mistakenly emptied in a bungled foreclosure action could be the first person to benefit from a new state law. Nilly Mauck, left Las Vegas in mid-December for a snowboarding trip to Utah and returned to stay with a friend for a few days when she received a disturbing phone call. Something was amiss at the Coronado Palms condominium on Badura Avenue that she had owned for the past two years. ([Las Vegas Sun](#))
- Ricky Rought paid cash to the Deutsche Bank National Trust Company for a four-room cabin in Michigan with the intention of fixing it up for his daughter. Instead, the bank tried to foreclose on the property and the locks were changed, court records show. ([Dealbook](#))
- Sonya Robison is facing a foreclosure suit in Colorado after the company handling her mortgage encouraged her to skip a payment, she says, to square up for mistakenly changing the locks on her home, too. ([Colorado Springs Business Journal](#))
- Thomas and Charlotte Sexton, of Kentucky, were successfully foreclosed upon by a mortgage trust that, according to court records, does not exist. ([NYT](#))
- Ron and LaRhonda Wilson Sr. in a process that allows debtors to reorganize their finances. Lawyers representing Option One Mortgage Corp. alleged that Mr. Wilson was delinquent in mortgage payments and late charges, and asked to foreclose in March 2008, documents show. That foreclosure motion included a document now central to the case being pursued by the trustee: an affidavit submitted by Dory Goebel, an employee at a predecessor company to Lender Processing called Fidelity National Information Services Inc. In a notarized “affidavit of debt,” Ms. Goebel said the Wilsons were delinquent on monthly payments between November 2007 and February 2008, according to documents. The Wilsons’ lawyer subsequently proved to the court that the Wilsons had made debt payments, according to court documents. ([WSJ](#))

Faith in key institutions – Legal System, Banking, Government – is crucial for Capitalism to function.

Why Capitalism Works And Other Systems Fail:

“In the West, this formal property system begins to process assets into capital by describing and organizing the most economically and socially useful aspects about assets, preserving this information in a recording system—as insertions in a written ledger or a blip on a computer disk—and then embodying it in a title. A set of detailed and precise legal rules governs this entire process. Formal property records and titles thus represent our shared concept of what is economically meaningful about any asset. They capture and organize all the relevant information required to conceptualize the potential value of an asset and so allow us to control it . . .

The reason capitalism has triumphed in the West and sputtered in the rest of the world is because most of the assets in Western nations have been integrated into one formal representational system . . . By transforming people with real property interests into accountable individuals, formal property created individuals from masses. People no longer needed to rely on neighborhood relationships or make local arrangements to protect their rights to assets. They were thus freed to explore how to generate surplus value from their own assets.”

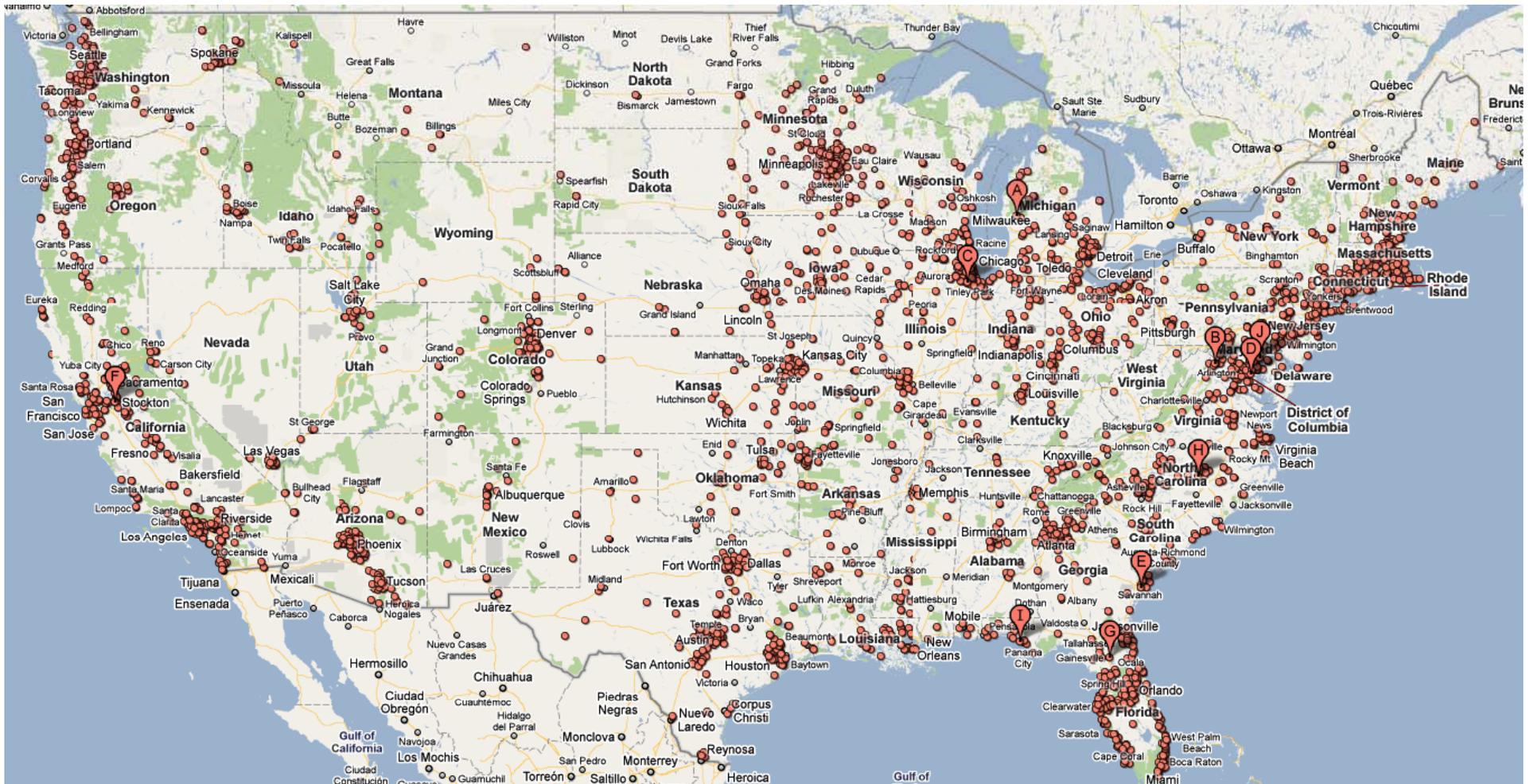
-Hernando de Soto, The Mystery of Capital

How is your own state doing?



Your state and local foreclosure market,
as seen through Google Maps

Welcome to Foreclosure Land

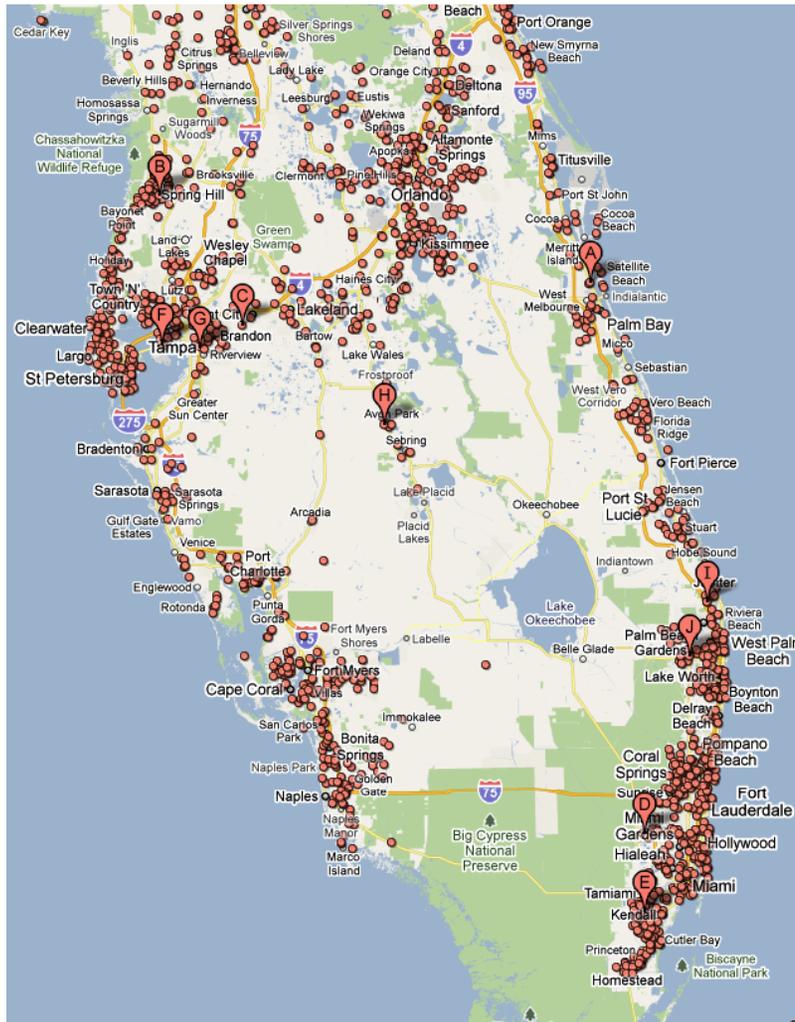


Using GoogleMaps to find foreclosures:

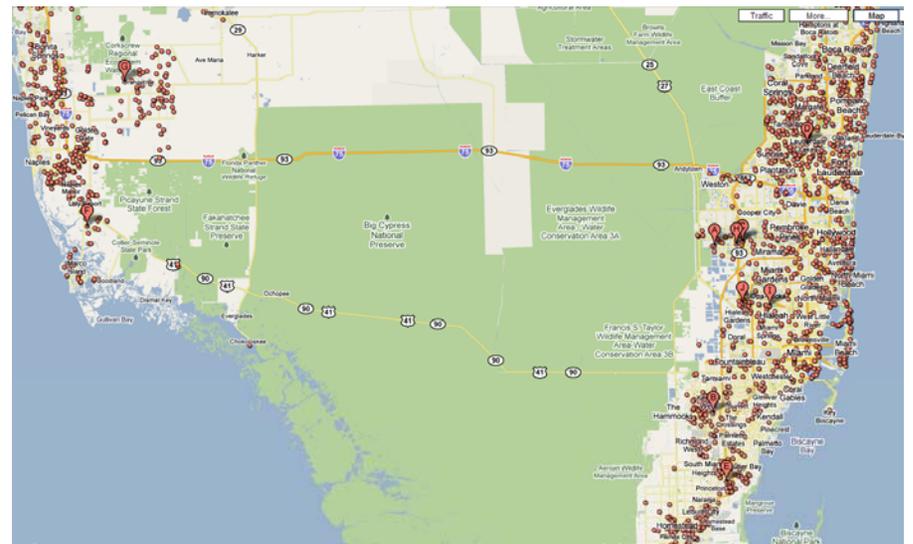
1. Punch your local address into Google Maps.
2. Your options are Earth, Satellite, Map, Traffic and . . . More. (Select “More”)
3. The drop down menu gives you a check box option for “Real Estate.”
4. The left column will give you several options (You may have to select “Show Options”)
5. Check the box marked “Foreclosure.”

Google Map Foreclosure Tricks

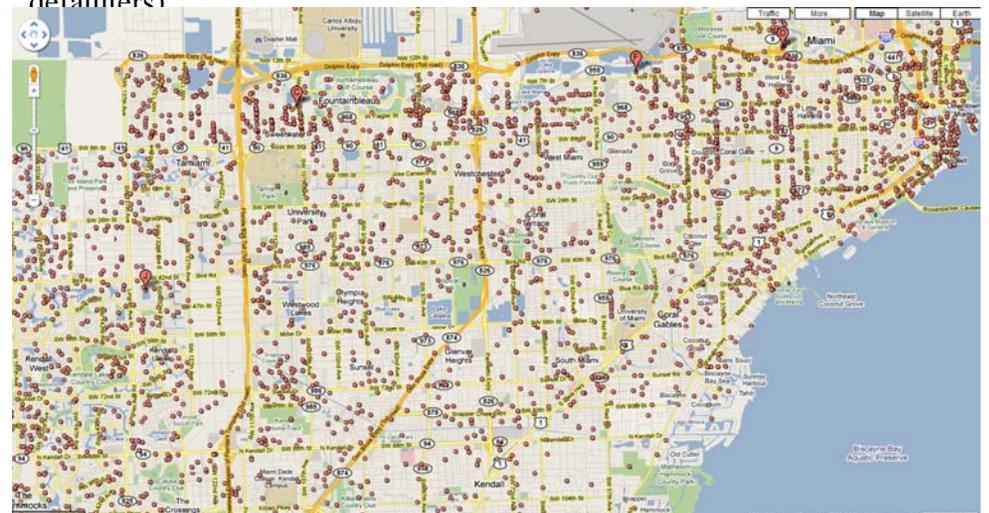
Lets zoom the map on to the state of Florida
(A state that knows a thing or two about bad real estate)



Then we can zoom closer — to South Florida
(Thank goodness the Everglades stemmed the tide of foreclosures!)



Zoom a bit more . . . Welcome to Miami!
(Playground to wealthy S.Americans, Europeans, and other defaulters)



The National Foreclosure Steamroller Continues . . .

Let's Go Shopping . . . On Miami Beach!

(I'm sure easy financing is still available)

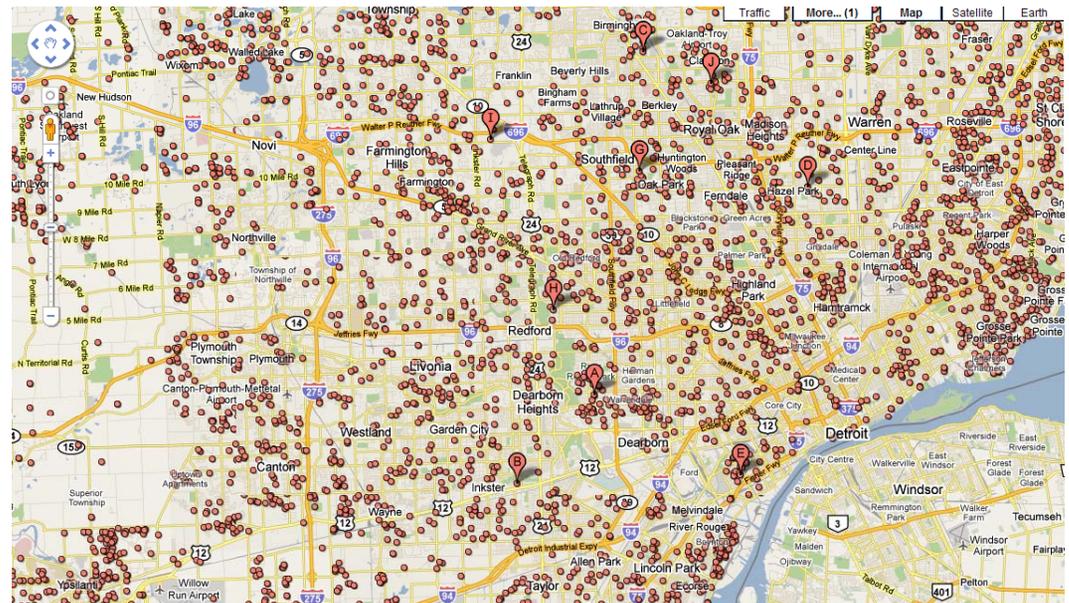
Real estate
from \$ to \$
Hide options
Listing type: For rent For sale Foreclosure
Bedrooms: Studio 1 2 3 4+
Bathrooms: 1 1.5 2 3+
Area: at least to at most sqft

- 7325 Carlyle Ave, Miami Beach**
Foreclosure: \$57,500
0 bed 2 bath
"A homestead property! Sold as-is. This property is eligible under the Freddie mac first look initiative thru 12/21/10. Home warranty offered for owner..." [listhub.net](#)
- 821 Euclid Ave, Miami Beach**
Foreclosure: \$229,500
2 bed 2 bath
"This 2 Bed/2 Bath home located in Miami Beach, FL is listed as Foreclosure sale. This is the final step in the foreclosure process." [watchforeclosure.com](#)
- 8336 NE 3rd Ave, Miami**
Foreclosure: \$59,900
4 bed 2 bath 2 parking
"Currently listed at \$49,900, this 1500 square ft. Home boasts 4 bedroom(s) and 2.00 bath(s). This foreclosure property located in Miami is priced to sell and..." [ushud.com](#)
- 3301 NE 5th Ave, Miami**
Foreclosure: \$15,000
1 bed 1 bath
"Home auction (12/11/2010 - Florida - Bid Live or Online). All homes open for inspection from 11AM to 4PM Visit [www.Auction.com](#) for property details." [listhub.net](#)
- 2500 NW 13th St, Miami**

3425 Collins Ave
Miami Beach, FL 33140 - [more info](#)
Foreclosure: \$48,900
1 bath
[watchforeclosure.com](#)
[Directions](#) [Search nearby](#) [Save to...](#) [more](#)

A Quick Look at Detroit:

After I showed this Google trick online, Jonathan Miller (who runs the RE Appraisal firm Miller Matrix) noted his wife's family came from Detroit, where the map is nearly solid RED



The State Attorneys General
are the country's best hope for:

1. Property Rights
2. Rule of Law
3. Due Process
4. Restoration of confidence
5. Justice . . . ?

Congress for Sale: 2009 Lobbying \$3.49 Billion

- *Derivative trading banks* spent \$28 M to save \$5-7 billion collateral allocations

\$ = Annual profits \$3 billion
(risk remains on the taxpayers)

- *Auto Dealers* spent < \$10M dollars (\$6.3m lobbying, + \$3.4m campaign contributions)

\$ = Saved undisclosed added interest, fee kickbacks, other over-priced loans worth \$20 billion annually to dealers.



What can be done *right now*?

1. Panel to advise and recommend areas for investigation
2. Deep dive into illegalities: Investigate wrongdoing
3. Cannot settle until *after* extensive review of bank fraud, bad actors, financial shortcuts, illegalities
4. Use your Subpoena Power
5. Find out “Who gave the orders to _____ ?”
6. Joint information clearing house amongst AGs regarding bank fraud
7. Active Cooperation with Criminal Prosecutors
8. Educate public regarding Bank Fraud
9. Establish that “Fraud does not pay”

for more information, contact

Barry L. Ritholtz

CEO, Director of Equity Research

Fusion IQ

535 Fifth Avenue, 25th floor

New York, NY 10017

212-661-2022 x7104

516-669-0369

The Big Picture

<http://www.ritholtz.com>

