THE CONCEPT AND FEDERAL CRIME OF MORTGAGE FRAUD

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ABSTRACT

The impact of mortgage fraud on the United States financial and economic system during the past twenty years has been severe and enduring. Nothing illustrates this fact better than the 2007–2008 financial crisis. Scholars and policymakers are convinced that the explosion in so-called liar's loans, which were securitized and sold to investors, played a key role in either causing or exacerbating the housing bubble and financial meltdown that led to the Great Recession.

Unfortunately, efforts to understand and address the problem of mortgage fraud are undermined by fundamental confusion regarding the nature of mortgage fraud as a federal criminal offense. Some of this confusion is due to the fact that there is no single federal mortgage fraud statute. Thus, almost every legal actor relies on the FBI's definition of mortgage fraud. Surprisingly, however, the influential FBI definition is plainly inconsistent in key respects with elements of the federal criminal statutes most often used to punish mortgage fraud. We should be concerned that the FBI, which investigates mortgage fraud, cannot get the basic definition of the crime of mortgage fraud right—and that scholars and commentators uncritically accept and use that problematic definition.

This Article provides scholars and lawmakers with an understanding of the meaning of mortgage fraud as a federal crime. In particular, it makes three practical contributions to public policy discourse regarding mortgage fraud. First, this Article distinguishes mortgage origination fraud from securities fraud involving mortgage-backed securities and other financial crimes related to the housing market. Second, this Article urges care in the use of the term "fraud." Not every misstatement in a mortgage application is fraud. Scholars who write about fraudulent mortgage loans must acknowledge that loan documents cannot have mens rea *and that not all mortgage application falsehoods warrant the imposition of criminal liability. Most importantly, this Article demonstrates why scholars and policymakers should take great care before using the FBI's deeply flawed definition of mortgage fraud.*

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INTRODUCTION

During the past ten years, scholars, policymakers, and journalists have examined in great detail the myriad causes and profound effects of the financial crisis that eventually led to the Great Recession.[1] The still-growing body of work on the subject is so immense that a recently published scholarly article referred to the "vast literature on the financial crisis" as "too vast to usefully cite."[2] In the immediate wake of the economic maelstrom, Congress created the Financial Crisis Inquiry Commission ("FCIC") "to examine the causes, domestic and global, of the current financial and economic crisis."[3] The FCIC's efforts culminated in the publication of a lengthy report[4] that explored, among other matters, the "crime-facilitative environments" in which mortgage fraud thrived prior to the Great Recession.[5] At the time the FCIC was conducting its landmark study, a consultant to the FCIC and prominent federal prosecutor summed up the conventional view that "mortgage fraud" was a key driver of the financial crisis:

> Mortgage fraud has been a significant contributor to the nation's financial woes, wreaking havoc from residential neighborhoods to global financial centers. It has contributed to a dramatic increase in home foreclosures, leaving clusters of empty and shuttered neighborhoods in many states. It has triggered a steep decline in home prices, devaluing many families' primary asset. Mortgage fraud has also destabilized our financial services sector and securities markets by reducing the value of mortgage-backed securities, causing enormous investor losses, driving some financial institutions out of business, and weakening others. The resulting credit squeeze has been harmful to homeowners and businesses across the country. Local governments and schools,

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1. The term "Great Recession" refers to the recession that began in December 2007 and ended in June 2009. *See* THE ASSOCIATED PRESS STYLEBOOK AND BRIEFING ON MEDIA LAW 123 (Thomas Kent et al. eds., 2016) (entry on "Great Recession") ("The recession that began in December 2007 and became the longest and deepest since the Great Depression of the 1930s. It occurred after losses on subprime mortgages battered the U.S. housing market. The National Bureau of Economic Research said it officially ended in June 2009, having lasted 18 months.").

2. Bernard S. Black, Charles K. Whitehead & Jennifer Mitchell Coupland, *The Nonprime Mortgage Crisis and Positive Feedback Lending*, 3 J.L. FIN. & ACCT. 1, 6 (2018). Just to give the reader a sense of its vastness, *see* Adam J. Levitin, *The Politics of Financial Regulation and the Regulation of Financial Politics: A Review Essay*, 127 HARV. L. REV. 1991, 1994 (2014) (book review) (discussing six books on the financial crisis); Andrew W. Lo, *Reading About the Financial Crisis: A Twenty-One-Book Review*, 50 J. ECON. LITERATURE 151 (2012). In the interests of space, the twenty-seven books that Levitin and Lo review are not listed here.

3. *See* Fraud Enforcement and Recovery Act of 2009, Pub. L. No. 111–21, § 5(a), (c), 123 Stat. 1617, 1625–28 (2009). For more background on the Financial Crisis Inquiry Commission, *see* About the FCIC at Stanford Law School, FINANCIAL CRISIS INQUIRY COMM'N, https://fcic.law.stanford.edu/about/history (last visited June 6, 2018).

4. *See* Financial Crisis Inquiry Comm'n, Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States (2011) [hereinafter FCIC REPORT].

5. *Id.* at 160–64.

> heavily dependent on property tax revenues, have also been negatively impacted.[6]

This view has persisted in the legal academic literature. Just recently, a scholar explained: "Mortgage fraud led to the collapse of international markets in August 2007 and created toxic assets, poisoning the financial system for years afterwards."[7]

No one doubts the impact that malfeasance and downright foolishness related to the residential mortgage market had on the economy during the Great Recession and the continuing problems that such wrongdoing presents.[8] Unfortunately, in discussions of the financial crisis and its aftermath, scholars, commentators, and policymakers often lump together various civil and criminal matters related to mortgages and real estate financing under one umbrella term: "mortgage fraud."[9] This tendency to use a single capacious term that covers so many disparate socio-legal phenomena can lead to confusion over the actual state of the federal criminal law governing financial frauds and may ultimately hamper efforts to propose effective mortgage fraud regulation.

This Article is the first scholarly work devoted specifically to the meaning of the federal crime of "mortgage fraud." Its goal is to provide guidance and clarity for those who wish to study, discuss, and analyze the concept of "mortgage fraud" from various legal, public policy, and empirical social science perspectives. The Article proceeds as follows: Part I provides the necessary financial and economic background to understand the legal regulation of mortgage fraud. Specifically, this Part addresses five key trends in the period leading up to the Great Recession, including a significant increase in nonprime lending, the rise of so-called "liar's loans," expanded securitization of mortgage debt, a remarkable bubble in housing prices and, finally, a dramatic increase in reported mortgage fraud. Part II reviews some of the key state and federal responses to the mortgage fraud crisis, including the passage of new state and federal legislation addressing mortgage fraud issues. Part II also briefly examines why some critics question the intensity and success of the federal government's anti-fraud efforts. Part III introduces the federal criminal

6. Benjamin B. Wagner, *Why Mortgage Fraud Matters*, 58 U.S. ATT'YS BULL. 1, 1 (2010). At the time that Wagner's article was published, he was the United States Attorney for the Eastern District of California and Co-Chair of the Mortgage Fraud Working Group of the Financial Fraud Enforcement Task Force ("FFETF"). *Id*. The FFETF is discussed in more detail *infra* notes 126–128, 144–146, and accompanying text.

7. J.S. Nelson, *Paper Dragon Thieves*, 105 GEO. L.J. 871, 873 (2017).

8. S. REP. NO. 111-10, at 2 (2009), *reprinted in* 2009 U.S.C.C.A.N. 430, 431 noted that:

> Our Nation is in the midst of its most serious economic crisis since the Great Depression . . . . As we learn more and more each day about the causes of this debacle, it is clear that unscrupulous mortgage brokers and Wall Street financiers were among the contributors to this economic collapse.

9. *See infra* Part V.B.

law of mortgage fraud. In particular, this part of the Article surveys the influential FBI definitions and classifications of mortgage fraud. Part IV digs more deeply into the federal crime of mortgage fraud. This part explores the essential elements of four of the federal criminal statutes used most often to punish mortgage origination fraud schemes and Supreme Court doctrine on these key statutory provisions.

Part V of this Article goes beyond recent economic history and federal criminal law doctrine to provide several practical suggestions for scholars and lawmakers who are interested in the regulation of the residential mortgage market. In particular, this Article argues that scholars should: (1) avoid using FBI mortgage fraud definitions, which are inconsistent in key respects with judicial doctrine in the field; (2) draw clearer lines between mortgage origination fraud and other forms of mortgage-related fraud, such as securities fraud involving mortgage-backed securities; and (3) carefully distinguish between mere misstatements to lenders and the types of fraudulent acts that are deserving of severe criminal punishment. Put simply, this Article implores scholars and lawmakers to be clear about what they mean by mortgage fraud so that we can determine what precise behavior is the problem, which laws currently cover the wrongdoing, and whether and how the improper acts should be punished.

I. THE MORTGAGE FRAUD EXPLOSION AND THE GREAT RECESSION

A. *Five Trends in Real Estate Finance*

The importance of mortgage fraud as a socio-legal phenomenon is most clearly illustrated by examining the role of mortgage fraud in the Great Recession. Aspects of this story, though vitally important, have been covered in great detail elsewhere.[10] Thus, this Article will only review five crucial trends that set the stage for the Great Recession: (1) the dramatic rise of nonprime lending; (2) a decline in home loan documentation standards; (3) the increased securitization of mortgage debt; (4) the formation of a bubble in housing prices; and (5) an explosion in potential mortgage fraud reports to the federal government. The preceding list is not exclusive,[11] but a brief discussion of these five interrelated trends in recent financial history establishes why mortgage fraud emerged as a matter of public policy concern.

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10. For a summary of the causes of the crisis, *see* Marc Jarsulic, *The Origins of the US Financial Crisis of 2007: How a House-Price Bubble, a Credit Bubble, and Regulatory Failure Caused the Greatest Economic Disaster Since the Great Depression*, *in* THE HANDBOOK OF THE POLITICAL ECONOMY OF FINANCIAL CRISES 22–46 (Martin H. Wolfson & Gerald A. Epstein eds., 2013).

11. This Article will not address the role that government policy played in the crisis. For an extensive discussion of regulatory failure, *see* KATHLEEN C. ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS: RECKLESS CREDIT, REGULATORY FAILURE, AND NEXT STEPS 149–223 (Oxford Univ. Press, 2011).

1. The Non-Prime Mortgage Market Expansion

The non-prime mortgage market, which includes both subprime and Alt-A loans,[12] greatly increased in size and importance in the decade before the Great Recession.[13] More and more loans were being made to riskier borrowers,[14] often with low (or no) down payments.[15] These nonprime loans carried higher interest rates than one would see in the prime mortgage market, though often they had had low introductory teaser rates, which eventually would reset to much higher rates.[16] During this period, nonprime loans grew from a fringe financial product to a significant part of the overall U.S. mortgage lending business.[17] One recent article notes that "[b]etween 2000 and 2005, nonprime originations rose from $125 billion to over $1 trillion, growing from roughly 10% to one-third of originations."[18] The

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12. Alt-A loans occupy the lending space between subprime and prime loans. *See* Zachary S. Gilreath, *The Culprit of the Great Recession: A Detailed Explanation of Mortgage-Backed Securities, their Impact on the 2008 Financial Crisis, and the Legal Aftermath*, 13 J. BUS. & TECH. L. 319, 326 n.85 (2018) (explaining that "Alt-A loans are those in which the risk profile falls between prime and subprime"); Cassandra Jones Havard, *Too Conflicted to Be Transparent: Giving Affordable Financing Its 'Good Name' Back*, 20 N.Y.U. J. LEGIS. & PUB. POL'Y 451, 481 n.157 (2017) ("Alt-A loans generally are larger in size than subprime loans and have significantly higher credit quality, with the majority having FICO scores above 680. For this reason, Alt-A loans are sometimes referred to as 'near prime.'") (citing THOMAS P. LEMKE, GERALD T. LINS & MARIE E. PICARD, MORTGAGE-BACKED SECURITIES § 3:8 (2016)).

13. Don Mayer, Anita Cava & Catharyn Baird, *Crime and Punishment (or the Lack Thereof) for Financial Fraud in the Subprime Mortgage Meltdown: Reasons and Remedies for Legal and Ethical Lapses*, 51 AM. BUS. L.J. 515, 547 (2014) (describing growth of subprime mortgage originations between 1996 and 2006, from "$70 billion a year to more than $600 billion at the subprime peak"); Charles W. Murdock, *The Big Banks: Background, Deregulation, Financial Innovation, and "Too Big to Fail,"* 90 DENV. U. L. REV. 505, 525 (2012) (detailing the astronomical increase in subprime and Alt-A loans in the early 2000s); Mark Totten, *The Enforcers & the Great Recession*, 36 CARDOZO L. REV. 1611, 1617 (2015) (same).

14. Atif Mian & Amir Sufi, *Household Debt and Defaults from 2000 to 2010: The Credit Supply View*, *in* EVIDENCE AND INNOVATION IN HOUSING POLICY 257, 260 (Lee Anne Fennell & Benjamin J. Keys eds., 2017) (asserting that "lenders from 2002 to 2005 became more willing to extend home purchase mortgages to households that were traditionally denied credit").

15. *See* James Charles Smith, *The Structural Causes of Mortgage Fraud*, 60 SYRACUSE L. REV. 473, 495 (2010) (discussing rise of mortgages with low or no down-payments); Dov Solomon, *From the Great Depression to the Great Recession: On the Failure of Regulation in the Mortgage Market*, 42 J. LEGIS. 162, 176–77 (2016) (discussing the dramatic relaxation of down payment requirements in the early 2000s).

16. Ryan Bubb & Prasad Krishnamurthy, *Regulating Against Bubbles: How Mortgage Regulation Can Keep Main Street and Wall Street Safe—From Themselves*, 163 U. PA. L. REV. 1539, 1557 (2015) ("About three-quarters of subprime mortgages issued from 2003 to 2007 were hybrid adjustable-rate mortgages (ARMs) that began with a fixed interest rate for an introductory period but reset to a potentially much higher adjustable interest rate after the introductory period expired.").

17. As one author observes: "The term 'subprime' has no distinct or universal definition." CYNTHIA KOLLER, WHITE COLLAR CRIME IN HOUSING: MORTGAGE FRAUD IN THE UNITED STATES 21 (Nicholas P. Lovrich ed., 2012); *see also* Oren Bar-Gill, *The Law, Economics and Psychology of Subprime Mortgage Contracts*, 94 CORNELL L. REV. 1073, 1087 (2009) (noting that "the boundaries of the subprime segment are arbitrary and blurry"); June Rhee, *Getting Residential Mortgage-Backed Securities Right: Why Governance Matters*, 20 STAN. J.L. BUS. & FIN. 273, 279 (2015) ("[D]espite the wide usage of the word 'subprime' in describing certain category of mortgages there is no universally agreed-upon definition of this word."). Generally, however, the subprime market is defined according to either borrower creditworthiness or loan price. *See* Bar-Gill, *supra* note 17, at 1087–88.

18. Black, Whitehead & Coupland, *supra* note 2, at 17.

increase in nonprime lending is all the more impressive when one considers the brief time frame in which much of this growth occurred. In the 2003–2005 period alone, subprime originations doubled and Alt-A originations more than tripled.[19] The subsequent decline in nonprime lending was just as remarkable. By 2009, nonprime loans had all but disappeared, counting for less than one percent of mortgage originations.[20]

2. Diminished Mortgage Underwriting Standards and the Rise of "Liar's Loans"

a. Low-Documentation Loans

The second pre-recession trend involved diminished mortgage underwriting standards.[21] In the decade prior to the Great Recession, lenders dramatically loosened their lending and verification standards for mortgages and home equity lines of credit, leading to "an increase in the number of loans with reduced hard information in the form of limited or no documentation."[22] In contrast to "full doc loans," which require borrowers to provide documented proof of income, employment, and assets,[23] these low-documentation loans permitted borrowers to obtain financing with limited or even no documentation of income, assets, or creditworthiness.[24] Collectively, the many types of no- and low-documentation loans[25] colloquially

19. *See* Christopher Mayer, Karen Pence & Shane M. Sherlund, *The Rise in Mortgage Defaults*, 23 J. ECON. PERSPS. 27, 28 (2009).

20. Black, Whitehead & Coupland, *supra* note 2, at 18 tbl.2 (citing INSIDE MORTGAGE FINANCE, THE 2010 MORTGAGE MARKET STATISTICAL ANNUAL (2010)).

21. *See* Kurt Eggert, *The Great Collapse: How Securitization Caused the Subprime Meltdown*, 41 CONN. L. REV. 1257, 1284 (2009) ("It appears clear that underwriting was degraded in the years prior to the subprime meltdown."). The term "underwriting" has multiple meanings in the world of law and finance. *See* Steven L. Schwarcz, *Macroprudential Regulation of Mortgage Lending*, 69 SMU L. REV. 595, 598 n.18 (2016) ("'Underwriting' means, in this context, the standards under which mortgage loans are made, or originated. In the context of issuing securities to investors, the term has a different meaning—the process by which securities firms sell those securities to the investors.").

22. Benjamin J. Keys, Tanmoy Mukherjee, Amit Seru & Vikrant Vig, *Did Securitization Lead to Lax Screening? Evidence from Subprime Loans*, 125 Q.J. OF ECON. 307, 323 (2010).

23. *See* Michael LaCour-Little & Jing Yang, *Taking the Lie Out of Liar Loans: The Effect of Reduced Documentation on the Performance and Pricing of Alt-A and Subprime Mortgages*, 35 J. REAL EST. RES. 507, 508 (2013) (describing "full doc" loans).

24. *See* Keys et al., *supra* note 22 at 323 ("[W]hereas limited documentation provides no information about income but does provide some information about assets, a no-documentation loan provides information about neither income nor assets."); LaCour-Little & Yang, *supra* note 23, at 508 (defining no-doc loans as those "for which assets, income, and employment are all omitted from the loan application and the lender generally relies solely on credit score and loan-to-value (LTV) ratio").

25. To simplify the discussion, this Article follows Keys et al., *supra* note 22, at 323, combining limited documentation and no-documentation loans into one category—"low-documentation loans." There were, however, many categories of low-documentation loans including: SIVA (stated income/verified assets), SISA (stated income/stated assets), and NINA (no income/no asset) loans. See LaCour-Little & Yang, *supra* note 23, at 508; Charles W. Murdock, *Why Not Tell the Truth?: Deceptive Practices and the Economic Meltdown*, 41 LOY.

came to be known as "liar's loans" or "liar loans."[26]

> The term liar's loan refers to mortgages that allow borrowers to falsify loan application information, possibly at the encouragement of brokers who have stronger incentives to close deals than to screen applicants. The common perception is that such falsification appears primarily among low- or no-documentation loans, where much of the recorded information is self-reported without strict verification.[27]

A lack of documentation itself, of course, is not proof of the falsity of one's representations; a borrower can honestly and accurately state her income and assets, regardless of whether the lender has asked for supporting documentation. Nevertheless, one article cites the following grim evidence regarding low-documentation loans:

> A 2006 survey of 2,140 mortgage brokers who sold lo-doc loans found that 43% knew that many borrowers lacked the income needed to qualify for full-documentation loans, in which income would be verified. The Mortgage Bankers Association for Responsible Lending compared 100 stated income loans with Internal Revenue Service records and found that 90% exaggerated income by 5% or more and "almost 60% of the stated amounts were exaggerated by more than 50%." . . . Fitch Ratings (Fitch) also reached troubling conclusions from its review of forty-five loan files in 2007. It found that 44% of the files included employment status or income that was inconsistent with other portions of the loan application or facially implausible.[28]

Further support can be found in a 2007 report on mortgage loans issued by the consulting firm BasePoint Analytics (now CoreLogic). The report's key findings were as follows:

> Material misrepresentation was prevalent among loan products that required little scrutiny of the borrowers' financial disposition. BasePoint Analytics, a

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U. CHI. L.J. 801, 843 (2010). There are also references to NINJA loans (no income, no job, no assets), though these may just be a type of SISA or NINA loan. *See* Kale Gans, *Anatomy of A Mortgage Meltdown: The Story of the Subprime Crisis, the Role of Fraud, and the Efficacy of the Idaho Safe Act*, 48 IDAHO L. REV. 123, 131 (2011) (explaining that a NINJA loan borrower "did not need to show any proof of income or assets in order to qualify for a loan—she merely needed to *state* her income and assets") (footnotes and citations omitted).

26. *See* ENGEL & MCCOY, *supra* note 11, at 36 ("Low-doc and no-doc loans were particularly noxious because they invited deception. They soon became known as 'liar's loans.' Borrowers could put whatever figure they wanted down for their income and not back it up with tax returns or pay stubs."); TOMSON H. NGUYEN, FRAUD AND THE SUBPRIME MORTGAGE CRISIS 36 (Marilyn McShane & Frank P. Williams III eds., 2011) ("[T]he growth of alternative loan products . . . allowed unscrupulous activities to flourish. These loans were also known as stated income loans, or 'liar loans,' and were much more likely to be open invitations to fraudsters."); Tomson H. Nguyen & Henry N. Pontell, *Mortgage Origination Fraud and the Global Economic Crisis: A Criminological Analysis*, 9 CRIMINOLOGY & PUB. POL'Y 591, 596 (2010) (referring to "no-documentation/low-documentation loans" as "liar loans"); Wei Jiang, Ashlyn Aiko Nelson & Edward Vytlacil, *Liar's Loan? Effects of Origination Channel and Information Falsification on Mortgage Delinquency*, 96 REV. OF ECON. & STAT. 1, 12 (2014).

27. Jiang et al., *supra* note 26, at 12.

28. *See* Black, Whitehead & Coupland, *supra* note 2, at 16 (footnotes and citations omitted).

> consulting firm that specializes in fraud detection software, analyzed more than 3 million loans and found that "as much as 70 percent of recent early payment defaults (EPDs) had fraudulent misrepresentations on their original loan applications; applications that contained misrepresentations were also five times as likely to go into default." The study also found that frauds included income inflated by as much as 500%, appraisals that overvalued the property by 50% or more, fictitious employers, and falsified tax returns.[29]

b. Who "Lied" in the Liar's Loans?

It is one thing to say that mortgage loan applications in the period before and after the Great Recession contained pervasive factual errors. This does not answer the key question, of course, of who exactly were the "liars" or the sources of these misrepresentations. Charles Murdock spells out the question with respect to stated income loans, though the point is valid for all low-documentation loans:

> If stated income loans were categorized as liar's loans, then somebody must have been falsifying the borrower's income on the mortgage application. Three possibilities exist: (1) the borrower lied; (2) the borrower lied with the approval of the lender; and (3) the mortgage lender itself fabricated the borrower's income.[30]

For obvious reasons, most commentators claim that borrowers participated or otherwise were complicit in so-called liar's loans. This conclusion seems sound. It is highly implausible that borrowers did not play an active role in the application processes that led to so many loans containing misrepresentations.[31] But experts also do not discount the role that mortgage brokers, lenders, and "shady real estate professionals"[32] played in the information falsification process.[33] Professors Atif

29. Nguyen & Pontell, *supra* note 26, at 596 (emphasis added) (citing BASEPOINT WHITE PAPER, NEW EARLY PAYMENT DEFAULT-LINKS TO FRAUD AND IMPACT ON MORTGAGE LENDERS AND INVESTMENT BANKS 1–2 (2007)). The findings of the BasePoint study have been cited by scholars and the FBI. *See* FBI, 2006 MORTGAGE FRAUD REPORT (May 2007), *available at* https://www.fbi.gov/stats-services/publications/mortgage-fraud-2006 (citing the BasePoint report); Harold Barnett, *The Securitization of Mortgage Fraud*, 16 SOC. CRIME L. & DEVIANCE 65, 71 (2011) (same); Robert A. Kubica, *A Judicial Response to the Subprime Lending Crisis*, 2 N.E. U. L.J. 41, 49–50 (2010) (same); Todd J. Zywicki & Joseph D. Adamson, *The Law and Economics of Subprime Lending*, 80 U. COLO. L. REV. 1, 57 (2009) (citing the FBI 2006 MORTGAGE FRAUD REPORT, *supra* note 29, which relies upon the BasePoint report).

30. Murdock, *supra* note 25, at 844.

31. Jiang et al., *supra* note 26, at 12 ("[L]ow-documentation loans enabled borrowers to falsify employment information, including employment tenure and self-employment status, as well as income, assets, expenses, liabilities, and debt information."); Linn, *infra* note 92, at 9 (explaining that "criminal prosecutions brought by law enforcement officials in various regions of the country" provide "evidence of widespread schemes" involving borrowers and real estate professionals).

32. Linn, *infra* note 92, at 9 ("[B]orrowers and shady real estate professionals conspired to overstate incomes, make up fictitious assets or employment histories on loan applications, inflate home values, lie about the source of funds used to make the down payment, and lie about the home buyer's intention to occupy the property.").

33. *See* GRETCHEN MORGENSON & JOSHUA ROSNER, RECKLESS ENDANGERMENT: HOW OUTSIZED AMBITION, GREED AND CORRUPTION LED TO ECONOMIC ARMAGEDDON 283–84 (Henry Holt & Co. eds., 2011) (arguing that

Mian and Amir Sufi, who have written extensively about mortgage application misrepresentations, note that "the sheer scale of fraud by mortgage originators and banks is difficult to resolve with the view that the financial sector was an innocent bystander simply caught up in a bubble."[34] The evidence suggests that "[t]oo often brokers and lenders did whatever it took to close a loan,"[35] including "padding a borrower's income or assets (with or without the borrower's knowledge), commissioning inflated appraisals, manufacturing fake pay stubs and W-2s, altering credit reports, and creating fictitious checks and investment statements."[36]

Even ten years after the Great Recession, how to apportion misrepresentation blame among borrowers and other parties appears to be unsettled as an empirical matter. As recently as 2017, Mian and Sufi acknowledged this open issue:

> [W]ho committed the fraud? The borrower or the mortgage originator? Normally, it would be the duty of the mortgage originator to help stem misreporting. However, during the mortgage credit expansion from 2002 to 2005, we know originators failed to monitor and screen potential borrowers. In fact, there are numerous examples where mortgage brokers or originators may have falsified income information by borrowers without the borrowers' knowledge.[37]

An article in the New York Times agrees with this scholarly conclusion, noting: "We do not have a comprehensive accounting of the responsibility for each instance of fraud—how many by brokers, by borrowers, by both together."[38] Thus,

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although lies about income on liar loans "were the borrowers' ideas in some cases . . . the pressure to originate volume caused some lenders to falsify borrowers' mortgage applications routinely"); Adam B. Ashcraft & Til Schuermann, *Understanding the Securitization of Subprime Mortgage Credit*, 2 FOUNDS. & TRENDS IN FIN. 1, 5 (2016) (explaining that "[w]ithout adequate safeguards in place, an originator can have the incentive to collaborate with a borrower in order to make significant misrepresentations on the loan application"); Jason Scott Johnston*, Do Product Bans Help Consumers? Questioning the Economic Foundations of Dodd-Frank Mortgage Regulation*, 23 GEO. MASON L. REV. 617, 653 (2016) ("There is evidence that in their desire to leverage and speculate on rising housing prices during the early twenty-first-century housing boom, a large number of buyers, assisted oftentimes by independent mortgage brokers, deliberately misstated their income.") (footnotes omitted); Atif Mian & Amir Sufi, *The Macroeconomic Advantages of Softening Debt Contracts*, 11 HARV. L. & POL'Y REV. 11, 16 (2017) ("[T]he income of borrowers was systematically overstated by mortgage originators on mortgage applications.") (citing Tomasz Piskorski et al., *Asset Quality Misrepresentation by Financial Intermediaries: Evidence from the RMBS Market*, 70 J. Fin. 2635, 2672–73 (2015)); Atif Mian & Amir Sufi, *Fraudulent Income Overstatement on Mortgage Applications During the Credit Expansion of 2002 to 2005*, 30 REV. FIN. STUD. 1831, 1863 (2017) ("[P]ress reports show that fraudulent income overstatement was perpetrated by brokers originating mortgages designed to be sold into the non-agency securitization market."); Murdock, *supra* note 25, at 844–45 (discussing lender and broker complicity or participation in loan application misrepresentations).

34. Mian & Sufi, *supra* note 14, at 284.

35. ENGEL & MCCOY, *supra* note 11, at 30.

36. *Id.*

37. Mian & Sufi, *supra* note 33, at 1862–63.

38. Binyamin Appelbaum, How *Mortgage Fraud* Made the Financial Crisis Worse, N.Y. TIMES (Feb. 12, 2015), http://www.nytimes.com/2015/02/13/upshot/how-mortgage-fraud-made-the-financial-crisis-worse.html?_r=0 [http://perma.cc/ML7F-CWQL].

it is crucial to acknowledge that much of what is written about liar's loans may be based on assumptions (reasonable as they might be) as to the sources of mortgage application falsehoods.

c. The Decline of Liar's Loans

Not surprisingly, in the wake of the Great Recession, banks greatly tightened their lending standards and credit contracted.[39] Furthermore, Congress passed the Dodd-Frank Act,[40] which fundamentally changed the mortgage lending land scape.[41] As one legal scholar explains, "[m]ortgage originators now owe a duty of care to borrowers. Lenders must consider borrowers' abilities to repay (based on income, future income, and credit history, among other factors) before issuing a home loan unless the mortgage is a 'qualified mortgage.'"[42] In short, borrowers today "are made to undergo a more stringent and scrutinizing underwriting process than ever before," and "only the most credit worthy of borrowers can become homeowners."[43] Thus, for now at least, the most egregious types of low documentation loans are a thing of the (recent) past.

3. Securitization

The third relevant pre-Great Recession trend involves the increased securitization of mortgage loans and the rise of financial instruments such as collateralized debt obligations (CDOs) and credit default swaps.[44] This large and complex topic

39. Laurie S. Goodman, *The Rebirth of Securitization: Where is the Private-Label Mortgage Market?* 22 J. STRUCTURED FIN. 8, 11 (2016) ("After the crises, the market began to demand that loans be fully documented, and most lenders either eliminated non-traditional products, or became very selective in their use of these products."). The reasons for the post-Recession mortgage credit contraction are a topic of scholarly discussion. *See generally* Patricia A. McCoy, Symposium, *Has the Mortgage Pendulum Swung Too Far? Reviving Access to Mortgage Credit*, 37 B.C. J.L. & SOC. JUST. 213 (2017) (discussing the factors contributing to credit barriers and how this heavily affects minority households).

40. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010). Given the precise timing of its implementation, Dodd-Frank may not be responsible for the post-Recession credit contraction. *See* McCoy, *supra* note 39, at 220 ("There is no substantial evidence . . . that the new federal mortgage lending standards that went into effect in January 2014 contributed to the tightening of credit."). The timing here is key. Both the credit contraction discussed in the Symposium and the declines in MLF SARs to which I am referring occurred prior to the effective January 2014 date of the mortgage regulations mandated by Dodd-Frank. *Id.* at 219.

41. Dodd-Frank provides, *inter alia*, that "no creditor may make a residential mortgage loan unless the creditor makes a reasonable and good faith determination based on verified and documented information that, at the time the loan is consummated, the consumer has a reasonable ability to repay the loan." Dodd-Frank Wall Street Reform and Consumer Protection Act § 1411(a)(2) (codified at 15 U.S.C. § 1639c).

42. Chrystin Ondersma, *A Human Rights Approach to Consumer Credit*, 90 TUL. L. REV. 373, 393–94 (2015) (footnotes and citations omitted).

43. Christopher K. Odinet, *The Unfinished Business of Dodd-Frank: Reforming the Mortgage Contract*, 69 SMU L. REV. 653, 686 (2016).

44. Chapter Eight of the FCIC REPORT, *supra* note 4, at 127–55, which is entitled "The CDO Machine," provides background on the rise of financial instruments such as CDOs (collateralized debt obligations) and

has been covered in other places.[45] Thus, the treatment here is cursory.[46] Nonprime and liar's loans were securitized—packaged or bundled into financial products such as residential mortgage-backed securities ("RMBS" or "MBS")[47] that in turn were marketed to investors.[48] In the early 2000s, the percentage of mortgage loans that were securitized increased significantly.[49] Mortgage lenders adopted an "originate to distribute"[50] model, in which "[i]nvestors in the securitized mortgages then bore the interest rate, prepayment, and default risk associated with the underlying loans apart from a small residual interest typically maintained by the originator."[51] It is widely believed that competition between securitizers and rising demand for additional mortgage loans to securitize was connected to the diminished underwriting standards and the rise of the low-documentation loans described above.[52] One author sums up this perspective:

> The fraudulent misrepresentations of mortgage loan originators as well as borrowers never could have occurred on the scale that they did in the first place

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credit default swaps. *See also* Adam J. Levitin & Susan M. Wachter, *Explaining the Housing Bubble*, 100 GEO. L.J. 1177, 1238–49 (2012) (discussing CDOs and CDS).

45. *See* ENGEL & MCCOY, *supra* note 11, at 43–68 (discussing securitization of subprime loans); Ashcraft & Schuermann, *supra* note 33; Eggert, *supra* note 21, at 1257; Levitin & Wachter, *supra* note 44, at 1187–1202.

46. For discussion on the important distinction between securitization by Government Sponsored Entities ("GSEs"), such as Fannie Mae and Freddie Mac, and private mortgage securitization by non-GSEs, *see* Michael Simkovic, *Competition and Crisis in Mortgage Securitization*, 88 IND. L.J. 213, 257 (2013).

47. The SEC website defines mortgage-backed securities as "debt obligations that represent claims to the cash flows from pools of mortgage loans, most commonly on residential property." *Fast Answers: Mortgage-Backed Securities*, U.S. SEC. & EXCH. COMM'N,The https://www.sec.gov/fast-answers/answersmortgagesecuritieshtm.html (last modified July 23, 2010). The process is as follows: "Mortgage loans are purchased from banks, mortgage companies, and other originators and then assembled into pools by a governmental, quasi-governmental, or private entity. The entity then issues securities that represent claims on the principal and interest payments made by borrowers on the loans in the pool, a process known as securitization." *Id*. For a graphic representation of the mortgage securitization process, *see* Neil Fligstein & Alexander F. Roehrkasse, *The Causes of Fraud in the Financial Crisis of 2007 to 2009: Evidence from the Mortgage-Backed Securities Industry*, 81 AM. SOC. REV. 617, 620 fig.1 (2016).

48. *See* Ashcraft & Schuermann, *supra* note 33, at 196 (defining securitization as "[t]he process through which loans are removed from the balance sheet of lenders and transformed into debt securities purchased by investors"); Simkovic, *supra* note 46, at 217 ("Securitization is a method of financing whereby loan receivables or other cash flows are bundled into securities and sold to investors.").

49. *See* Keys et al., *supra* note 22, at 314 (noting growth in securitization rates "from less than 30% in 1995 to over 80% in 2006"); Shaun P. Martin, *Legal Winners and Losers in the Mortgage Crisis*, 24 CONN. INS. L.J. 245, 258 (2018) (stating that "[s]ecuritization levels peaked at roughly ninety percent of originated mortgages" prior to the collapse of the housing market).

50. The FCIC Report's glossary defines "originate-to-distribute" as follows: "When lenders make loans with the intention of selling them to other financial institutions or investors, as opposed to holding the loans through maturity." FCIC REPORT, *supra* note 4, at 524. In contrast, "originate-to-hold" is defined as "[w]hen lenders make loans with the intention of holding them through maturity, as opposed to selling them to other financial institutions or investors." *Id.*

51. Paul G. Mahoney, *Deregulation and the Subprime Crisis*, 104 VA. L. REV. 235, 243 (2018).

52. Simkovic, *supra* note 46 at 215 ("In the mid-2000s, competition between mortgage securitizers for loans led to deteriorating mortgage underwriting standards and a race to the bottom that ended in the late 2000s financial crisis."); Solomon, *supra* note 15, at 177 ("A number of factors can account for this lowering of credit standards, but most striking was the meteoric development of the securitization market.").

> and certainly could never have precipitated a global financial crisis had Wall Street investment banks not been prepared to buy up these mortgages worth billions of dollars, to securitize them, and to sell them to investors.[53]

Critics believe that fraud existed in the RMBS market[54]—that firms selling RMBS to the investing public[55] and the ratings agencies responsible for evaluating these securities[56] knew or should have known that many of the underlying loans were riskier or of much poorer quality than was represented to the investors that purchased these financial instruments.[57] Putting aside fraud, at the very least there is significant evidence that "willful blindness" existed throughout the securitization process:

> [M]arket participants were willfully blind at all stages of the lending, structuring, and purchase chain, from nonprime mortgage originators to the banks who packaged mortgages [into MBS] . . . the rating agencies who rated them, the money managers who purchased them, and the institutional investors who provided funds to these money managers.[58]

4. The Housing Bubble

The fourth trend that will be addressed here concerns a bubble in housing prices that developed prior to the Great Recession. This Article will not engage in the

53. David O. Friedrichs, *Mortgage Origination Fraud and the Global Economic Crisis: Incremental versus Transformative Policy Initiatives*, 9 CRIMINOLOGY & PUB. POL'Y 627, 629 (2010).

54. Totten, *supra* note 13, at 1620 (arguing that there was "fraud in the creation, package, and sale of residential mortgage-backed securities").

55. Fligstein & Roehrkasse, *supra* note 47, at 631 (claiming that "descriptive statistics corroborate other evidence that both mortgages and MBS were widely misrepresented to their buyers") (citing Piskorski et al., *supra* note 33, at 2672).

56. Mayer, Cava & Baird, *supra* note 13, at 555 ("The ratings industry's poor performance was instrumental in the damage to the world economy."); Murdock, *supra* note 25, at 852 ("Investors around the world put their trust in the rating agencies and their gold standard AAA rating. Unfortunately, the rating agencies were bought off by greed and their ratings were nothing more than complex lies.").

57. *See* Mayer, Cava & Baird, *supra* note 13, at 528 (alleging that "there is a common core of fraud and misrepresentation at all levels of the mortgage securitization food chain"); Murdock, *supra* note 25, at 881. Murdock states:

> Seldom has lying been so pervasive throughout a system. From customers, mortgage brokers, and banks, in creating the mortgages, to investment bankers and credit rating agencies in bundling, securitizing and selling mortgages and mortgage derivatives, to the government's lack of candor to Congress and the American people about the nature of the problem and what is being done to solve it.

Id.; *see also* Totten, *supra* note 13, at 1620 (claiming that "[t]he financial institutions behind these securities often misrepresented the risk of the underlying assets" and that fraud was committed "by the agencies that rated these securities, several of whom continued to give AAA ratings to toxic investments through the eve of the crisis").

58. Black, Whitehead & Coupland, *supra* note 2, at 37. Lending credence to this "willful blindness" narrative, Black, Whitehead, and Coupland even note, somewhat shockingly, that "[a]s the bubble grew and lo-doc lending and other forms of flaky lending grew with it, the banks steadily cut the percentage of loans that were reviewed." *Id.* at 17.

debate over the root causes of this housing bubble,[59] though increased securitization and diminished lending standards (both discussed above) may have played a role.[60] Once again, the numbers tell a remarkable story about just how historically unusual this era was:

> The decade leading up to the financial crisis of 2007-2008 witnessed unprecedented growth in U.S. house prices . . . For most of the twentieth century, house prices on average experienced essentially zero growth. From 1890 to 1997, house prices increased nationally by a *total* of 7%, an annual growth rate of 0.06%. But beginning in the late 1990s, house prices increased sharply. From 1997 to 2006, real house prices increased by 85%, an *annual* growth rate of about 7%.[61]

Moreover, the housing bubble was not evenly distributed nationally. In some areas, housing prices rose much greater than 7% annually;[62] prices even tripled in many major cities.[63] Ultimately, the real estate bubble eventually burst and housing prices dropped dramatically—by nearly 40% according to some sources[64]—"a fall greater than what occurred during the Great Depression."[65] The impact on homeowner wealth was severe. "In the aggregate, U.S. homeowners lost close to eight trillion dollars of housing equity between the high-water mark for housing prices, at the end of 2006, and the end of the first quarter of 2009."[66] Ryan Bubb and Prasad Krishnamurthy describe the effects as follows:

> The bursting of the bubble triggered a massive wave of mortgage defaults that ultimately caused a broader financial crisis and a sharp reduction in credit in the economy. It also led to a reduction in consumption by households, who suddenly found themselves much poorer and less able to borrow, which further slowed down the economy.[67]

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59. Scholars disagree on the causes of the housing bubble. *Compare* Levitin & Wachter, *supra* note 44, at 1181 ("The primary cause of the housing bubble was the shift from regulated, government-sponsored securitization to unregulated, private securitization as the principal method of funding mortgage loans."), *with* Bubb & Krishnamurthy, *supra* note 16, at 1558–60 (criticizing Levitin's and Wachter's "supply side" explanation of the bubble).

60. *See* John M. Griffin & Gonzalo Maturana, *Did Dubious Mortgage Origination Practices Distort House Prices?*, 29 REV. FIN. STUD. 1671, 1675 (2016) ("Rather than securitization alone, our evidence supports the hypothesis that dubious origination practices facilitated through securitization had an economically large distorting effect on house prices."); *Id.* at 1672 (arguing that "originator malfeasance in certain localities raised the credit supply; this drove up house prices relative to other areas and subsequently led to larger price crashes").

61. Bubb & Krishnamurthy, *supra* note 16, at 1549 (citations omitted).

62. *Id.* at 1550.

63. *Id.*

64. *Id.* at 1551 ("Beginning in 2006, house prices crashed, and, by 2012, they had fallen nationally almost 40% from their peak."); Steven L. Schwarcz, *Secured Transactions and Financial Stability: Regulatory Challenges*, 81 LAW & CONTEMP. PROBS. 45, 51 (2018) (stating that housing prices "collapsed by over 35%").

65. Schwarcz, *supra* note 64, at 51.

66. Smith, *supra* note 15, at 495.

67. Bubb & Krishnamurthy, *supra* note 16, at 1555.

5. The SARs Explosion

As mortgage underwriting standards declined and the use of so-called liar's loans exploded, indicators of mortgage origination fraud also increased dramatically prior to and in the immediate wake of the Great Recession. This discussion focuses on one valuable, though imperfect, indicator of mortgage origination fraud: Mortgage Loan Suspicious Activity Reports.[68] Pursuant to the Bank Secrecy Act,[69] financial institutions file Suspicious Activity Reports[70] (commonly referred to as "SARs") with the Financial Crimes Enforcement Network ("FinCEN")[71] when they detect potential illegal activity.[72] The SARs numbers related to the financial crisis are staggering. Mortgage loan fraud ("MLF") SARs grew from approximately 4,695 in 2001 to 92,561 in 2011[73]—an increase of over 1971%, or

68. As will be discussed below, SARs are an imperfect and indirect measure of mortgage fraud. See *infra* note 82.

69. The Bank Secrecy Act ("BSA") is the common or popular name for the Currency and Foreign Transactions Reporting Act, Pub. L. 91–508, 84 Stat. 1118 (1970) (codified as amended in scattered sections of U.S.C., including 31 U.S.C. §§ 5311–5326). The original BSA has been amended several times, including by the Money Laundering Control Act of 1986, the Annunzio-Wylie Anti-Money Laundering Act of 1992 and the USA Patriot Act in 2002. *See* Ernest L. Simons IV, *Anti-Money Laundering Compliance: Only Mega Banks Need Apply*, 17 N.C. BANKING INST. 249, 251–54 (2013) (reviewing statutory amendments to the BSA). For a summary of the BSA, *see* Robert Almon, Matt Greve & Nick Wamsley, *Financial Institutions Fraud*, 50 AM. CRIM. L. REV. 1023, 1053 (2013).

70. The Bank Secrecy Act empowers the Treasury Department to "require any financial institution, and any director, officer, employee, or agent of any financial institution, to report any suspicious transaction relevant to a possible violation of law or regulation." 31 U.S.C. § 5318(g)(1) (2012).; To effectuate this mandate, the Suspicious Activity Report ("SAR") was created by the Department of the Treasury, Office of Thrift Supervision, Office of the Comptroller of the Currency, Federal Reserve, and Federal Deposit Insurance Corporation. *See* Anti-Money Laundering Program and Suspicious Activity Report Filing Requirements for Residential Mortgage Lenders and Originators, 77 Fed. Reg. 8,148, 8,148 (February 14, 2012) (to be codified at 31 C.F.R. pt. 1010 and pt. 1029).

71. FinCEN was originally created by an order of the Secretary of the Treasury. *See* Treasury Order 105-08 (April 25, 1990) (establishing FinCEN as an office in the Office of the Assistant Secretary for Enforcement). After 9/11, the USA Patriot Act officially made FinCEN a bureau in the Department of the Treasury. *See* USA PATRIOT Act, Pub. L. No. 107-56, § 361 (2001), codified at 31 U.S.C. § 310(a) (2012)

72. *See* Ratzlaf v. United States, 510 U.S. 135, 138 (1994) ("Congress enacted the [BSA] . . . in response to increasing use of banks and other institutions as financial intermediaries by persons engaged in criminal activity. The Act imposes a variety of reporting requirements on individuals and institutions regarding foreign and domestic financial transactions.") (citations omitted). Pursuant to its statutory authority, the Treasury Department has issued several regulations requiring the filing of SARs by various entities, including, but not limited to, federal banks under OCC supervision, 12 C.F.R. § 21.11 (2012), and FDIC-insured state banks, 12 C.F.R. § 208.62 (2019). For background on financial institutions' internal SARs processes, *see* Stavros Gadinis & Colby Mangels, *Collaborative Gatekeepers*, 73 WASH. & LEE L. REV. 797, 872–89 (2016).

73. Fin. Crimes Enforcement Network, U.S. Dep't of Treasury, Mortgage Loan Fraud Update: Suspicious Activity Report Filings in Calendar Year 2012, 3 (2013), http://www.fincen.gov/pdf/MLF_Update_CY_2012_508_FINAL.pdf [hereinafter FinCEN 2012 MLF Update Report]. Another source pegged the number of MLF SARs at 93,508 in 2011. *See* U.S. Dep't of Justice, Office of the Inspector Gen., Audit of the Dep't of Justice's Efforts to Address Mortgage Fraud, 10 (2014), https://oig.justice.gov/reports/2014/a1412.pdf [hereinafter DOJ Mortgage Fraud Audit]. These minor differences do not affect the basic point: MLF SARs soared.

almost twenty times the number of filings, in just eleven years.[74] Much of that stunning growth occurred in a relatively short period of time in the early 2000s.[75]

As credit constricted and banks tightened their lending standards in the post-crisis period,[76] lenders' reports of possible mortgage fraud also declined. There were 69,277 MLF SARs in 2012, a twenty-five percent decline from 2011.[77] Still, even with this significant drop, there was a greater than 1300% increase in MLF SARs from 2001 to 2012.[78] The downward trend in reported MLF SARs apparently has continued. In 2014, there were approximately 33,000 MLF SARs filed for depository institutions,[79] and in 2015, the number declined further to around 26,000 MLF SARs for depository institutions.[80] This represents an enormous decline from the 2011 peak but still a much greater total than the pre-boom 2001 numbers noted above. Thus, if we accept SARs as a general proxy for actual criminal activity, mortgage fraud remained a significant problem even after the Great Recession ended.[81]

Although MLF SARs reports may be the best mortgage fraud proxy,[82] SARs filings can present a misleading measure of illegal activity,[83] especially within a

74. Other sources use different beginning and end dates to trace the SARs explosion, thus arriving at different rates of increase. *See* Nguyen & Pontell, *supra* note 26, at 596 (noting 1411% increase in SARs from 1997 to 2005); Sally S. Simpson, *Making Sense of White-Collar Crime: Theory and Research*, 8 OHIO ST. J. CRIM. L. 481, 495 (2011) ("Between 1997 and 2005, there was a 1,411% increase in the number of suspicious activity reports (SARs) that identified potential mortgage fraud."); NICHOLAS RYDER, THE FINANCIAL CRISIS AND WHITE COLLAR CRIME: THE PERFECT STORM? 55 (2014) (describing "significant increase in the number of . . . SARs submitted to FinCEN"); Smith, *supra* note 15, at 473 ("The past decade has witnessed an explosion of mortgage fraud, with reports to the federal government of suspected criminal behavior rising by a magnitude of over eighteen times from 2000 to 2008.").

75. Andrew J. Ceresney, Gordon Eng & Sean R. Nuttall, *Regulatory Investigations and the Credit Crisis: The Search for Villains*, 46 AM. CRIM. L. REV. 225, 237 (2009) ("The number of suspicious activity reports that financial institutions filed relating to mortgage fraud in 2004 was more than double that in 2003; in 2007, the number was more than six times the 2003 figure.") (footnotes omitted).

76. The reasons for the post-Recession mortgage credit contraction are a topic of significant scholarly discussion. *See generally* McCoy, *supra* note 39, at 213.

77. FinCen 2012 MLF Update Report, *supra* note 73, at 2.

78. *Id.* at 3.

79. Bridget Berg, *Regulatory Fraud Reporting: Lost in a Sea of Change*, MORTGAGE COMPLIANCE MAG (Mar. 2016), at 10, 12.

80. *Id.*

81. The Financial Crimes Enforcement Network maintains an online database that tracks SARs filings. See https://www.fincen.gov/reports/sar-stats. A search of mortgage fraud SARs from Depository Institutions and Loan or Finance Companies indicated that 24,223 mortgage fraud SARs were filed in 2016, and 18,521 SARs were filed in 2017. Of course, the FinCEN database includes many different forms of fraud related to mortgages, including loan modification fraud and reverse mortgage fraud.

82. KOLLER, *supra* note 17, at 88 ("Even if one disagrees that the 'reporting' of fraud cannot be a proxy for actual fraud occurrences, SARs arguably represent the industry's best guess as to the extent of fraud being committed on an annual basis.").

83. *See* Paul E. Carrillo, *Testing for Fraud in the Residential Mortgage Market: How Much Did Early-Payment-Defaults Overpay for Housing?*, 47 J. REAL EST. FIN. ECON. 36, 37–38 (2013) (discussing issues with using SARs to measure both reported and unreported potential fraud).

particular period of time.[84] For various reasons, SARs can both overestimate *and* underestimate the amount of actual financial malfeasance.[85] As to overestimation, reports of "suspicious" activity are not proof that violations of law actually have occurred.[86] Some suspicious activity will turn out to be just that—suspicious, but nothing more.[87] Activity that appears wrongful to a responsible officer at a covered lender may not ultimately be prosecutable as a criminal offense or give rise to civil liability.

In addition to normal uncertainty over suspected illegality, the law incentivizes financial institutions to report when in doubt. First, the legal penalties for failing to file a report are harsh.[88] Thus, "defensive filing" to avoid these sanctions is not irrational.[89] Second, federal law contains "a safe harbor provision that protects financial institutions and their agents from third-party civil liability stemming from the SARs they file."[90] This provision further encourages risk-averse financial institutions to report possible wrongdoing.

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84. FinCEN has noted that "[f]iling increases or decreases are not necessarily indicative of overall increases or decreases in MLF activities over the noted period, as the volume of SAR filings in any given period does not directly correlate to the number or timing of suspected fraudulent incidents in that period." FINCEN 2012 MLF UPDATE REPORT, *supra* note 73, at 2, n.3. One reason is that "[c]ompared to other SARs, MLF SARs showed a significant time lapse from the date that the suspicious activity occurred to the date that filers discovered and reported the activity." FIN. CRIMES ENF'T NETWORK, U.S. DEP'T OF TREASURY, MORTGAGE LOAN FRAUD UPDATE: SUSPICIOUS ACTIVITY REPORT FILINGS FROM OCTOBER 1–DECEMBER 31, 2009, 2 (July 2010), http://www.fincen.gov/pdf/MLF%20Update.pdf.

85. See William K. Black, *Neo-Classical Economic Theories, Methodology, and Praxis Optimize Criminogenic Environments and Produce Recurrent, Intensifying Crises*, 44 CREIGHTON L. REV. 597, 623–25 (2011).

86. Berg, *supra* note 79, at 10, 13 ("Often, the intent behind misrepresentation appears clear . . . [b]ut sometimes it is uncertain whether discrepancies are due to misunderstanding, incomplete documentation, or a true intent to defraud.").

87. Philip J. Ruce, *The Bank Secrecy Act: Considerations for Continuing Banking Relationships After the Filing of a Suspicious Activity Report*, 30 QUINNIPIAC L. REV. 43, 45–46 (2011) ("But SARs are just that—reports of suspicious activity. A financial institution will not generally conduct a complex investigation of every SAR it files; there are far too many reports for that.").

88. *See* 1 JOHN K. VILLA, BANKING CRIMES: FRAUD, MONEY LAUNDERING AND EMBEZZLEMENT § 6:78-6:79, at 520-27 (2018-19 ed.) (surveying criminal and civil penalties for violations of the Bank Secrecy Act, including failures to file SARs); 31 U.S.C. § 5321 (establishing civil penalties for willful violations of the applicable parts of the BSA or regulations promulgated thereunder); 31 U.S.C. § 5322 ("A person willfully violating this subchapter or a regulation prescribed . . . under this subchapter . . . shall be fined not more than $250,000, or imprisoned for not more than five years, or both.").

89. Christopher M. Straw, Note, *Unnecessary Risk: How the FDIC's Examination Policies Threaten the Security of the Bank Insurance Fund*, 10 N.Y.U. J. LEGIS. & PUB. POL'Y 395, 408 (2007) ("Because failure to file a SAR carries a heavy penalty, banks have engaged in what FinCEN describes as defensive filing—unjustified filings done solely to ensure that a bank is never subject to disciplinary action."). Defensive filing has obvious negative effects. *See id.* at 408–09 ("The sheer number of defensive filings has made SARs all but useless for combating money laundering.") (citing *Financial Services Regulatory Relief: The Regulators' Views: Hearing Before the Subcomm. on Fin. Insts. and Consumer Credit of the H. Comm. on Fin. Servs.*, 109th Cong. 34 (2005) (statement of Rep. Spencer Bachus, Chairman, Subcomm. on Fin. Insts. and Consumer Credit).

90. Jeffrey R. Boles, *Financial Sector Executives as Targets for Money Laundering Liability*, 52 AM. BUS. L. J. 365, 380 (2015) (citing 31 U.S.C. § 5318(g)(3) (2012)).

At the same time, underestimation of actual incidences of fraud is probably an even greater problem when relying on SARs as a proxy for criminal conduct.[91] Notably, until recently, non-bank residential mortgage lenders and originators (RMLOs) had no legal obligation to file SARs.[92] Thus, before this rule was changed,[93] William Black estimated that extrapolating from the SARs data to the total nonprime lending industry would have required multiplying MLF SARs by five "[b]ecause unregulated lenders originated nearly eighty percent of nonprime loans (and did so without any regulatory quality standards)."[94] In addition, we cannot assume that every violation of the law is actually detected.[95] Presumably, responsible lenders may never discover some well executed frauds,[96] and lenders with subpar fraud-detection systems may fail to identify even some poorly executed frauds. Finally, not all detected wrongdoing is ultimately reported. As William Black points out, lenders may hesitate to file SARs if doing so would trigger greater law enforcement scrutiny—especially if the lender's own insiders participated in fraud.[97]

B. *The Impact of the Mortgage Fraud Explosion*

As discussed thus far, prior to the Great Recession, the United States experienced what many observers believe was a toxic mix of wrongdoing related to the mortgage market. A housing bubble formed as lenders (who may have engaged in fraud) assisted by mortgage brokers (who also may have engaged in fraud)

91. Black, *supra* note 85, at 623 (explaining that "[t]he total SARs figure is only a faint indication of the true incidence of mortgage fraud").

92. Courtney J. Linn, *The Way We Live Now: The Case for Mandating Fraud Reporting by Persons Involved in Real Estate Closings and Settlements*, 16 J. FIN. CRIME 7, 10 (2009) ("The almost 500 percent increase in SAR filings by depository institutions between 2002 and 2005 tells only part of the story because during this period of time . . . vast segments of the real estate industry, including nonbank mortgage lenders, were exempt from SAR filing requirements."); Smith, *supra* note 15, at 480 ("SARs do not reveal the full extent of the current mortgage fraud problem. Non-federally insured institutions, including independent mortgage bankers and mortgage brokers, are not required to file reports.").

93. After the Great Recession ended, the Treasury Department, through FinCEN, issued regulations bringing RMLOs into the SARs-reporting world. *See* Anti-Money Laundering Program and Suspicious Activity Report Filing Requirements for Residential Mortgage Lenders and Originators, 77 Fed. Reg. 8,148 (Feb. 14, 2012) (to be codified at 31 C.F.R. pt. 1010 and pt. 1029) [hereinafter RMLO Rule Notice].

94. *See* Black, *supra* note 85, at 623.

95. *Id.* ("The FBI estimated that regulated lenders detect roughly one-third of the cases of mortgage fraud at their institutions prior to loan disbursement.") (citing Gretchen Morgenson, *A Road Not Taken by Lenders*, N.Y. TIMES, Apr. 6, 2008 at BU1).

96. Cases of so-called fraud for property or housing may never be detected. *See* Smith, *supra* note 15, at 478 ("Often, fraud for property goes undetected for a long time period. If the borrower never defaults, the lender does not incur an actual loss and it is highly probable that the borrower's fraud will never surface."); *infra* note 189 and accompanying text.

97. *Id.* at 623–24 ("Failure to file criminal referrals is logical (and incriminating) because . . . the FBI has reported that frauds in which lender personnel are involved cause eighty percent of total mortgage fraud losses."); Nguyen & Pontell, *supra* note 26, at 593 ("The underreporting of frauds discovered in subprime mortgage loans . . . by financial institutions does not come as a surprise because those culpable include the lenders themselves.").

extended nonprime residential mortgages and home equity loans to risky borrowers (who possibly engaged in fraud), which were then bundled into securities backed by these loans, the quality of which may have been misrepresented (perhaps fraudulently) by issuers and ratings agencies to the investing public.[98] Ultimately, the housing bubble burst, which most experts believe was the crucial event in triggering the Great Recession.[99]

The natural question, of course, is whether mortgage fraud actually *caused* the financial crisis. This is a much more challenging inquiry. The FCIC drew a connection between the decline in lending standards, the housing bubble, and the rise in mortgage fraud as follows: "Across the mortgage industry, with the bubble at its peak, standards had declined, documentation was no longer verified, and warnings from internal audit departments and concerned employees were ignored. These conditions created an environment ripe for fraud."[100] Still, the FCIC majority did not explicitly claim that mortgage fraud caused the Great Recession.

On the question of causation, the dissenting members of the FCIC were more direct, and more skeptical. They concluded that it was "likely that the housing bubble and the crisis would have occurred even if there had been no mortgage fraud."[101] In the FCIC dissenters' view, mortgage fraud was not "an essential cause of the crisis,"[102] but rather was "a contributing factor and a deplorable effect of the bubble."[103] Judge Richard Posner similarly concluded that it was "a mistake to blame home buyers (or home equity borrowers) for the banking collapse."[104] Although Posner conceded that "there were fools in both camps, and crooks as well (mostly it seems, among mortgage brokers),"[105] in his estimation, "they were

98. Cynthia A. Koller et. al., *When Moral Reasoning and Ethics Training Fail: Reducing White Collar Crime through the Control of Opportunities for Deviance*, 28 NOTRE DAME J.L. ETHICS & PUB. POL'Y 549, 555 (2014) ("Virtually all commentaries on the mortgage crisis have included some reference to the fraudulent activities of participants, ranging from home buyers to the rating agencies and beyond."); Mayer, Cava & Baird, *supra* note 13, at 565 ("In summary, from loan originations, to securitization, and to foreclosures, a great many financial institutions and their employees have engaged in deceitful behaviors that are either fraudulent or border on fraud.").

99. *See* Schwarcz, *supra* note 21, at 595 ("It is widely recognized that the bursting of the United States housing bubble was a primary precipitating factor of the 2007-2008 global financial crisis.") (citing Steven L. Schwarcz, *Securitization, Structured Finance, and Covered Bonds*, 39 J. CORP. L. 129, 130 (2013)).

100. *See* FCIC REPORT, *supra* note 4, at 160; *see also id*. at 187 ("Lax mortgage regulation and collapsing mortgage-lending standards and practices created conditions that were ripe for mortgage fraud."); KOLLER, *supra* note 17, at 128 (Respondents in author's study "generally agreed that the willingness of the financial and mortgage industries, investors and home buyers to accept the subprime mortgage product, and all of the monetary risk that goes along with it, was the major contributor to the fraud which accompanied it, rather than the lack of established regulation.").

101. *Dissenting Statement of Commissioner Keith Hennessey, Commissioner Douglas Holtz-Eakin and Vice Chairman Bill Thomas in* FCIC REPORT, *supra* note 4, at Financial 411, 424 [hereinafter FCIC DISSENTING STATEMENT].

102. *Id*.

103. *Id*.

104. Richard A. Posner, THE CRISIS OF CAPITALIST DEMOCRACY 77 (Harv. Univ. Press, 2010).

105. *Id*. at 78.

not the main drivers of the collapse."[106]

For the purposes of this Article, it is not necessary to resolve the ultimate issue of causation between mortgage fraud and the Great Recession.[107] After all, mortgage fraud need not have been a demonstrable "but for" cause of the Great Recession to be considered a public policy issue worth addressing.[108] As Robert Quigley points out, "[e]ven a small 'contributing factor' to a social ill as vast as the financial crisis may fairly be judged a serious ill itself."[109] Moreover, causation aside, the alleged explosion of unsavory borrower, broker, and lender behavior should have, at the very least, tipped bankers and regulators off to the fact that something had gone terribly awry with the mortgage market. The FCIC dissenters explained: "Even if the number of fraudulent loans was not substantial enough to have a large impact on the bubble, the increase in fraudulent activity should have been a leading indicator of deeper structural problems in the market."[110] Finally, even if mortgage fraud did not cause the financial crisis, "[t]he bad financial practices, and occasional outright fraud, associated with subprime and other nonstandard mortgages and their securitization allowed the housing bubble to grow much longer and larger than otherwise would have been possible."[111] In this view, mortgage fraud may not have been the spark, but it might have been financial crisis accelerant and kindling.[112]

II. STATE AND FEDERAL RESPONSES TO THE MORTGAGE FRAUD CRISIS

A. *State Criminal Legislation*

Regardless of whether mortgage fraud was a "but for" cause of the Great Recession, it is easy to see why federal and state lawmakers seized on mortgage fraud as an aspect of the financial crisis into which they could sink their regulatory teeth.[113] Mortgage fraud seemed to be an easily identifiable white collar crime

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106. *Id.*

107. *See* Robert Quigley, *The Impulse towards Individual Criminal Punishment After the Financial Crisis*, 22 VA. J. SOC. POL'Y & L. 103, 142 (2015) ("The FCIC majority's inability to quantify the impact of fraud on the bubble does not mean that impact was zero. Quantification is difficult precisely because of the feedback loops, like CDO pricing and public confidence in financial institutions, which made subprime contagion so dangerous and unpredictable.").

108. *See* RYDER, *supra* note 74, at 80 (contending that "mortgage fraud was an important factor that contributed towards the . . . financial crisis").

109. Quigley, *supra* note 107, at 142.

110. FCIC DISSENTING STATEMENT, *supra* note 99, at 424.

111. *See* Dean Baker, *Speculation and Asset Bubbles*, *in* THE HANDBOOK OF THE POLITICAL ECONOMY OF FINANCIAL CRISES 47, 55 (Martin H. Wolfson & Gerald A. Epstein eds., 2013).

112. *See* Ceresney, Eng & Nuttall, *supra* note 75, at 235 (observing that "[m]any have pointed to mortgage fraud as one of the major catalysts for the credit crisis"); RYDER, *supra* note 74, at 52 (stating that mortgage fraud was "the most prominent white collar crime associated with subprime lending and the financial crisis").

113. Directly after the Great Recession, in 2010, one scholar referred to mortgage fraud as "the number one white collar crime in the United States." Smith, *supra* note 15, at 473.

associated with the crisis that would be amenable to concrete legislative action.[114] In fact, even before the Great Recession officially began, Georgia, long-plagued by mortgage fraud,[115] became the first state in the U.S. with a dedicated criminal mortgage fraud statute in 2005.[116] As the financial crisis deepened, other states followed suit, criminalizing various forms of harmful mortgage-related behavior. In 2009, seventeen states introduced legislation addressing mortgage fraud issues and twelve states enacted such legislation.[117] By 2010, thirteen states had enacted statutes that specifically defined and criminalized mortgage fraud.[118] Since then, Connecticut,[119] Massachusetts,[120] and California[121] have also added new separate mortgage fraud crimes to the books. In sum, in the past decade or so, many states have sought to make clear that mortgage fraud is not merely a matter of civil dispute between lenders, borrowers, and other responsible parties. Instead, they have treated this conduct as a crime that warrants state prosecution and punishment.

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114. Further discussion is not warranted here, but there is scholarly debate of the meaning of the term "white collar crime." *See* Stuart P. Green, *The Concept of White Collar Crime in Law and Legal Theory*, 8 BUFF. CRIM. L. REV. 1, 2 (2004). The term is being used informally here as a synonym for financial crime.

115. *See* ALYSSA KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US 142 (Bloomsbury, 2009) ("For four years straight, from 2001 to 2005, Georgia led the nation in reports of real estate fraud. At one point Georgia had seven times as many fraud reports for subprime loans than it should have based on the usual rates that banks factor into their projections. . . . "); Smith, *supra* note 15, at 475 (noting that Georgia "was experiencing the highest rate of mortgage fraud in the nation") (citing MERLE SHARICK ET AL., MORTGAGE ASSET RESEARCH INST., EIGHTH PERIODIC MORTGAGE FRAUD CASE REPORT TO: MORTGAGE BANKERS ASSOCIATION 4 (2006), https://docplayer.net/20233728-Mortgage-asset-research-institute.html.).

116. *See* NGUYEN, *supra* note 26, at 31; *see* Stephen F.J. Ornstein & Matthew S. Yoon, *Georgia Residential Mortgage Fraud Act*, 59 CONSUMER FIN. L.Q. REP. 265 (2005) (briefly summarizing GA. CODE ANN. §§ 16-8-100 to 16-8-106 (2007)).

117. *See* MORTGAGE FRAUD 2009 LEGISLATION, NATIONAL CONFERENCE OF STATE LEGISLATURES, http://www.ncsl.org/research/financial-services-and-commerce/mortgage-fraud-2009-legislation.aspx (last updated March 18, 2010). *See also* NGUYEN, *supra* note 26, at 31 (noting that within two years of the passage of Georgia's residential mortgage fraud legislation, "seventeen states followed suit and introduced similar legislation").

118. *See* Smith, *supra* note 15, at 475 (citing Ariz. Rev. Stat. § 13-2320 (2010); Colo. Rev. Stat. § 18-4-401 (2004 & Supp. 2009); Fla. Stat. Ann. § 817.545 (West 2006 & Supp. 2010); Ga. Code Ann. §§ 16-8-100 to -106 (2007); Ky. Rev. Stat. Ann. § 286.8-990 (West 2009); Md. Code Ann., Real Prop. §§ 7-401 to -409 (LexisNexis 2003 & Supp. 2009); Minn. Stat. Ann. § 609.822 (West 2009); Miss. Code Ann. § 97-23-107 (West 1999 & Supp. 2009); Mo. Rev. Stat. § 570.310 (West 1999 & Supp. 2009); N.Y. Penal Law §§ 187.00-.25 (McKinney's 1999 & Supp. 2010); N.C. Gen. Stat. §§ 14-118.10 to .17 (2009); Utah Code Ann. §§ 76-6-120 to -1204 (2008); Wash. Rev. Code Ann. § 19.144.080 (West 2007 & Supp. 2010)). Smith also notes that in some states without dedicated mortgage fraud laws "acts of fraud committed in connection with mortgage lending will often violate other criminal statutes." *Id*. at 475–76.

119. *See* CONN. GEN. STAT. § 53-379a (effective October 2, 2011) (defining crime of residential mortgage fraud).

120. *See* MASS. GEN. LAWS CH. 266, § 35A(b) (effective August 7, 2010).

121. *See* CAL. PENAL CODE §532f (effective 2011) (defining the crime of mortgage fraud) (effective 2011); *see also* Nadia Mahallati, *California's Dedicated Mortgage Fraud Statute*, 41 MCGEORGE L. REV. 712, 713 (2010) (reviewing California's mortgage fraud statute).

B. *Federal Anti-Mortgage Fraud Efforts*

1. FERA and the FFETF

In the wake of the Great Recession, the federal government also turned its attention to mortgage fraud. On May 20, 2009, President Obama signed the Fraud Enforcement and Recovery Act of 2009 ("FERA"), which was designated specifically to improve enforcement of prohibitions on a wide range of financial frauds—including mortgage fraud.[122] The Act primarily attempted to attack mortgage fraud in two ways.[123] First, FERA made a key adjustment to existing federal law by expanding "the definition of a financial institution to include mortgage lending businesses not directly regulated or insured by the federal government,"[124] thus "making it a federal crime to defraud these types of institutions."[125] Prior to FERA, defrauding such mortgage lending businesses typically was not a federal offense.[126] Second, FERA also appeared to commit greater resources to prosecuting these financial crimes by authorizing the Department of Justice "to receive an additional $165 million for fiscal years 2010 and 2011 in order to pursue criminal, civil, and administrative investigations and prosecutions of financial frauds, including mortgage fraud."[127]

President Obama followed up on FERA with an Executive Order creating the Financial Fraud Enforcement Task Force ("FFETF"),[128] which replaced the

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122. Fraud Enforcement and Recovery Act of 2009, Pub. L. No. 111-21, 123 Stat. 1617 (2009) ("An Act to improve enforcement of mortgage fraud, securities and commodities fraud, financial institution fraud, and other frauds related to Federal assistance and relief programs, for the recovery of funds lost to these frauds, and for other purposes.").

123. See generally, Nicholas McCann, Note, *Federal Law Enforcement in the Home Mortgage Lending Market Enhanced by the "Fraud Enforcement and Recovery Act of 2009*," 22 LOY. CONSUMER L. REV. 354, 355 (2010).

124. U.S. Dep't of JUSTICE, Office of the Inspector Gen., AUDIT of the Dep't of JUSTICE'S Efforts to Address MORTGAGE Fraud, at 3 (2014) [hereinafter DOJ Mortgage Fraud Audit] (referring to Fraud Enforcement and Recovery Act of 2009, Pub. L. No. 111-2, sec. 2(b)(1), 123 Stat. 1617, 1617 (2009), codified at 18 U.S.C. § 27) ("'[M]ortgage lending business' means an organization which finances or refinances any debt secured by an interest in real estate, including private mortgage companies and any subsidiaries of such organizations, and whose activities affect interstate or foreign commerce."); *see also* Almon, Greve & Wamsley, *supra* note 69, at 1035 n. 76 (explaining that FERA "expanded the 'financial institution' definition found in 18 U.S.C. § 20(1) to include mortgage lending businesses") (citing 18 U.S.C. § 27).

125. DOJ MORTGAGE FRAUD AUDIT, *supra* note 73, at 3; *see also* Jim Moye, *Let's Put the Fear in the FERA! Suggestions to Make the Fraud Enforcement and Recovery Act of 2009 a Strong Fraud Deterrent*, 35 S. ILL. U. L.J. 421, 424 (2011) (noting that FERA "prohibits making false statements in a mortgage application to employees and agents of a mortgage company") (citing FERA, sec. 2, § 1014, 123 Stat. 1617, 1617–18).

126. Linda Marshall, *Making Choices: Charging and Plea Negotiations*, U.S. ATT'YS' BULL., May 2010, at 19 (explaining that prior to FERA "mortgage lending businesses were usually not covered by the bank fraud statute; bank fraud was limited to FDIC-insured institutions, credit unions, federal home loan banks, and other such entities"). Marshall notes that FERA was not retroactive. *Id.; see also* United States v. Bouchard, 828 F.3d 116, 126–27 (2d Cir. 2016) (declining to apply FERA retroactively to mortgage lending institutions).

127. DOJ MORTGAGE FRAUD AUDIT, *supra* note 73, at 3 (referring to FERA § 3(a), 123 Stat. 1617, 1619 (2009).

128. Exec. Order No. 13,519, 74 Fed. Reg. 60,123, 60,125 (Nov. 19, 2009).

Corporate Fraud Task Force created by President George W. Bush.[129] The FFETF specifically included a working group "tasked with combating a wide range of fraud in the mortgage, finance, and housing markets, including loan modification schemes, foreclosure rescue scams, loan origination fraud, reverse mortgage schemes, short sale frauds and builder bailout schemes."[130] Like the enactment of the state criminal mortgage fraud laws, the passage of FERA and President Obama's Executive Order creating the FFETF amounted to a declaration that mortgage fraud was not merely a matter of civil dispute between lenders and borrowers (as well as corrupt mortgage brokers and other responsible parties) but an offense against the public welfare that warranted federal criminal investigation and punishment.

2. Critiques of the Federal Mortgage Fraud Effort

Unfortunately, there are reasons to be skeptical about the vigor and success of the federal government's battle against mortgage fraud in the wake of the Great Recession.[131] First, the funding to the Department of Justice promised by FERA was never fully appropriated by Congress.[132] For example, in 2010, only $34.8 million was appropriated to the DOJ out of $160 million authorized by FERA.[133] Moreover, in 2011, only $20.2 million was appropriated to the DOJ out of $150 million authorized by FERA.[134] Thus, in a crucial two-year period right after the financial crisis, the DOJ obtained only $65 million out of $310 million in additional funding promised by FERA.[135] Digging deeper into the 2011 numbers is even more jarring, since the $20.2 million in additional funding for the DOJ that year was allocated entirely by Congress to the FBI (which had been promised $65 million by FERA), while the U.S. Attorneys' Offices, DOJ Criminal Division, and DOJ Civil Division all received none.[136]

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129. Exec. Order No. 13,271, 67 Fed. Reg. 46,091 (July 9, 2002). For a comparison of the FFETF and the CFTF, *see* Mary Kreiner Ramirez, *Prioritizing Justice: Combating Corporate Crime from Task Force to Top Priority*, 93 MARQ. L. REV. 971, 984–85 (2010). In 2018, President Trump issued an Executive Order terminating the FFETF and creating the Task Force on Market Integrity and Consumer Fraud. See Exec. Order No. 13,844, 83 Fed. Reg. 33,115 (July 16, 2018). I want to thank the editors of the AM. CRIM. L. REV. for drawing my attention to this executive order.

130. FRAUD ENFORCEMENT TASK FORCE, FIRST YEAR REPORT 3.5 (2010), http://www.stopfraud.gov/docs/FFETF-Report-LR.pdf. For background on the FFETF's Mortgage Fraud Working Group (MFWG), *see id.* at 4.5–4.15.

131. Many of these issues were explored in the DOJ MORTGAGE FRAUD AUDIT, *supra* note 73.

132. *Id.* at 3.

133. *Id.* at 4.

134. *Id.*

135. *See* Rena Steinzor, *White-Collar Reset: The DOJ's Yates Memo and Its Potential to Protect Health, Safety, and the Environment*, 7 WAKE FOREST J.L. & POL'Y 39, 59 (2017) (citing Jesse Eisinger, *Why Only One Top Banker Went to Jail for the Financial Crisis*, N.Y. TIMES MAG. (Apr. 30, 2014), http://www.nytimes.com/2014/05/04/magazine/only-one-top-banker-jail-financial-crisis.html).

136. DOJ MORTGAGE FRAUD AUDIT, *supra* note 73, at 4.

Second, it has been argued that insufficient personnel was devoted to combatting financial frauds in the early 2000s.[137] Prior to the Great Recession, law enforcement attention and resources were focused on fighting terrorism rather than white collar crime.[138] But as the warning signs of a mortgage fraud crisis emerged, it was not easy for the government to pivot back to address financial crimes.[139] Judge Jed Rakoff of the Southern District of New York, who became one of the fiercest critics of the lack of post-Great Recession criminal prosecutions of high-level Wall Street executives,[140] explains the issue as follows:

> [B]efore 2001, the FBI had more than one thousand agents assigned to investigating financial frauds, but after September 11 many of these agents were shifted to antiterrorism work. Who can argue with that? Yet the result was that, by 2007 or so, there were only 120 agents reviewing the more than 50,000 reports of mortgage fraud filed by the banks. It is true that after the collapse of Lehman Brothers in 2008, new agents were hired for some of the vacated spots in offices concerned with fraud detection; but this is not a form of detection easily learned, and recent budget limitations have only exacerbated the problem.[141]

Another harsh critic of the Government's sluggish reaction to the financial crisis, William Black, explains that as the financial crisis exploded, the FBI only increased the number of special agents investigating mortgage fraud from 120 in

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137. See William K. Black, *The Department of Justice "Chases Mice While Lions Roam the Campsite": Why the Department Has Failed to Prosecute the Elite Frauds That Drove the Financial Crisis*, 80 UMKC L. REV. 987, 998 (2012) ("Although the FBI warned about an epidemic of mortgage fraud as early as 2004, the director of the FBI at the time conceded that the agency did not get the resources it requested to address the issue.").

138. *See* Ceresney, Eng & Nuttall, *supra* note 75, at 238 ("Following the September 11th attacks, the FBI shifted more than 1,800 agents, nearly one third of all agents in criminal programs, including many of those trained in financial investigations, to counterterrorism and intelligence duties."); RYDER, *supra* note 74, at 89–93 (discussing the impact of the "War on Terror" on the FBI's efforts to battle white collar crime).

139. *See* Ceresney, Eng & Nuttall, *supra* note 75, at 238 ("In the years prior to the credit crisis, the FBI mounted several investigations into mortgage fraud, but its repeated warnings of the threat mortgage fraud posed and its requests for additional resources for non-terrorism investigations were left unaddressed by policymakers.") (footnotes omitted); RYDER, *supra* note 74, at 95 ("The diversion of resources away from mortgage fraud, despite several warnings and pleas from the FBI, left it unprepared and ill-equipped to deal with the incoming tsunami of mortgage fraud cases.").

140. For a discussion regarding the lack of successful criminal prosecutions against major financial players arising out of the Great Recession, *see* Adam J. Levitin, *The Politics of Financial Regulation and the Regulation of Financial Politics: A Review Essay*, 127 HARV. L. REV. 1991, 2026–27 (2014) (discussing JEFF CONNAUGHTON, THE PAYOFF: WHY WALL STREET ALWAYS WINS (Prospecta Press, 2012)); *see also* Nizan Geslevich Packin, *Breaking Bad? Too-Big-to-Fail Banks Not Guilty as Not Charged*, 91 WASH. U. L. REV. 1089, 1095 (2014) ("In fact, the DOJ has not pursued any of the large banks' executives that were personally involved in the scandals that took place in the last few years despite the fact that several government agencies clearly stated in reports that in their opinion, fraud and unethical behavior both caused and exacerbated the financial crisis.").

141. Jed S. Rakoff, *The Financial Crisis: Why Have No High Level Executives Been Prosecuted?*, N.Y. REV. BOOKS (Jan. 9, 2014), https://www.nybooks.com/articles/2014/01/09/financial-crisis-why-no-executive-prosecutions/. 9, 2014).

2007 to 180 in 2008.[142] Given that the FBI "received over 63,000 criminal referrals for mortgage fraud in fiscal year 2008,"[143] Black concluded that the FBI could "investigate only a tiny percentage of criminal referrals for mortgage fraud."[144] In contrast, Black and other scholars have noted that 1,000 FBI agents and forensic experts were assigned to the much smaller Savings and Loans crisis in the 1980s.[145] Once again, the importance of 9/11 cannot be underestimated, since the Savings and Loan crisis was many years before FBI focus turned to fighting acts of foreign terrorism on U.S. soil.

Furthermore, the FFETF does not seem to have been a great law enforcement success story.[146] The Task Force's nickname within the Justice Department—"the turtle"—while a bit cryptic, was clearly not intended to be flattering.[147] Pulitzer Prize-winning journalist Jesse Eisinger explains:

> After a promising start, the FFETF fizzled . . . . The task force had no operational powers to bring cases. The Justice Department struggled to staff it. It was just a coordinating committee to check in with offices around the country on their progress, with representatives from at least twenty-six federal agencies and departments . . . as well as state attorneys general, district attorneys and "other state, local, tribal and territorial representatives." It would meet once a month, often with staffers calling into conference calls in their principals' steads.
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> Because of the failure, no one at Justice oversaw the entirety of the investigative effort. No one person was responsible. Every case was discrete. Any national push to combat the financial crisis died.[148]

The turtle's sad fizzle, as described by Eisinger, makes one question the intensity and focus of the federal government's battle against mortgage fraud and other financial crimes. Perhaps, despite rhetoric to the contrary,[149] some FBI and DOJ

142. Black, *supra* note 137, at 998.

143. *Id.*

144. *Id.*

145. *Id.*; *see also* Sandra D. Jordan, *Victimization on Main Street: Occupy Wall Street and the Mortgage Fraud Crisis*, 39 FORDHAM URB. L.J. 485, 502 (2011) ("In the wake of the S&L crisis, strike forces were established in twenty-seven cities, 1,000 FBI investigators and agents were dispatched across the nation, accompanied by forensic accountants and many federal prosecutors."); Ceresney, Eng & Nuttall, *supra* note 75, at 238–39 ("By 2007, the number of FBI agents nationwide pursuing mortgage fraud had shrunk to about 100, in sharp contrast to the roughly 1,000 agents that were deployed on banking fraud during the S&L crisis of the 1980s and 1990s.") (footnotes omitted).

146. Mayer, Cava & Baird, *supra* note 13, at 579 (asserting that "[m]uch of the media is not impressed with the efforts of the task force to address the splintered and tepid efforts of the enforcement authorities").

147. JESSE EISINGER, THE CHICKENSHIT CLUB: WHY THE JUSTICE DEPARTMENT FAILS TO PROSECUTE EXECUTIVES 176 (Simon & Schuster, 2017) ("Within the department, its new task force became the butt of jokes, called the 'turtle,' or derided with the vaguely Yiddish-sounding 'Fuh-tuf-teh.'").

148. *Id.* at 175–76.

149. *See* Thomas N. Palermo, *Going "Cocoanuts": Looking at Modern Mortgage Fraud*, 57 FED. LAW. 38 (2010) ("Prosecuting mortgage fraud has become a major priority of the U.S. Department of Justice, and these

officials never truly bought into the idea that financial crimes such as mortgage fraud (as opposed to say, global terrorism) should be a top federal law enforcement priority in the post-9/11 world.[150] In support of this view, the DOJ Mortgage Fraud Audit "found that, despite public statements by the FFETF and the Department about the importance of pursuing financial frauds cases, including mortgage fraud, the FBI Criminal Investigative Division ranked Complex Financial Crimes as the lowest of the six ranked criminal threats within its area of responsibility."[151] Even more telling, the CID ranked mortgage fraud as the lowest subcategory threat within the Complex Financial Crimes category.[152] The DOJ Mortgage Fraud Audit thus concluded "based on the statistics provided by the FBI along with the relatively low ranking that mortgage fraud received on various FBI priority lists that mortgage fraud did not receive a priority ranking commensurate with DOJ's statements related to mortgage fraud."[153]

The third major reason for skepticism about the federal government's mortgage fraud initiatives concerns the Obama administration's inaccurate reported data about mortgage fraud prosecutions. In October 2012, Attorney General Eric Holder held a press conference and issued a press release to tout the results of one of the administration's anti-fraud efforts, the Distressed Homeowner Initiative.[154] This initiative was not focused on mortgage loan origination fraud; instead, it was geared towards combatting scams that rip off homeowners in financial distress who already had mortgages.[155] The DOJ Mortgage Fraud Audit summarized Holder's public claims as follows:

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criminal cases are percolating in ever greater numbers throughout the district courts around the United States."). One author claimed that the FBI even transferred 2,500 agents from terrorism to mortgage fraud, though no source was cited for this statistic. *See* Michael Shapiro, *The Prevalence of International Money Laundering Crimes and the Best Practices to Avoid It*, *in* INTERNATIONAL WHITE COLLAR ENFORCEMENT LEADING LAWYERS ON UNDERSTANDING CROSS-BORDER REGULATIONS, DEVELOPING CLIENT COMPLIANCE PROGRAMS, AND RESPONDING TO GOVERNMENT INVESTIGATION 51, 53 (2010), *available on* Westlaw, 2010 WL 271741, at *2.

150. *See* DOJ MORTGAGE FRAUD AUDIT, *supra* note 124, at 18–19 (discussing tensions between some U.S. Attorney's Offices and local FBI field offices with respect to mortgage fraud investigations and prosecutions); *Id.* at 29 (finding that "the FBI did not rank mortgage fraud among its highest ranked priority white collar crimes" and that "despite receiving additional funding from Congress to pursue mortgage fraud cases, the FBI adding new staff did not always use these new positions to exclusively investigate mortgage fraud").

151. *Id.* at 4.

152. *Id.* at 8 (finding that "mortgage fraud to be a low priority, or not listed as a priority, for FBI Field Offices in . . . Baltimore, Los Angeles, Miami, and New York"). Complex Financial Crime fell below Public Corruption, Southwest Border, Civil Rights, Violent Crime, and Organized Crime. *Id.* at 8, n. 9. And in the Complex Financial Crime category, Mortgage Fraud fell below Corporate and Securities/Commodities Fraud and Health Care Fraud. *Id.*

153. *Id.* at 11.

154. *Id.* at Appendix IV, 40–42 (reprinting Attorney General Eric Holder's Statement at the October 9, 2012 Press Conference on the Distressed Homeowner Initiative).

155. *Id.* at 2. Attorney General Eric Holder stated: "This landmark Initiative, spearheaded by the FBI, was launched to help streamline and advance investigations and prosecutions against fraudsters who allegedly targeted, and preyed upon, Americans struggling to keep their homes." *Id.* at Appendix IV, 40.

> During this press conference, the Attorney General announced that the initiative resulted in 530 criminal defendants being charged, including 172 executives, in 285 criminal indictments or informations filed in federal courts throughout the United States during the previous 12 months. The Attorney General also announced that 110 federal civil cases were filed against over 150 defendants for losses totaling at least $37 million, and involving more than 15,000 victims. According to statements made at the press conference, these cases involved more than 73,000 homeowner victims and total losses estimated at more than $1 billion.[156]

When the DOJ Office of the Inspector General asked for data to back up the administration's claims, the DOJ could not substantiate Holder's statements.[157] In fact, many of the statistics proffered by Attorney General Holder were simply wrong. Instead of 530 criminal defendants charged with criminal losses of $1 billion, subsequent reports placed the numbers at 107 criminal defendants and criminal losses of $95 million.[158] That is about one-fifth of the number of purported criminal defendants and around ten percent of the alleged criminal losses[159]—quite a discrepancy for publicly-touted government data.[160] Moreover, according to the Inspector General's report, the DOJ did not have an effective system in place for ensuring the accuracy of its mortgage fraud prosecution data and "continued to cite these seriously flawed statistics in mortgage fraud press releases that it issued."[161] Of course, poor statistical case tracking and inaccurate public reporting is not proof of a lack of prosecutorial success. On this score, it is worth noting that the DOJ took exception to the implication that mortgage fraud was not a top law enforcement priority, pointing out that "the number of mortgage fraud convictions more than doubled from FY 2009 to FY 2010, i.e., from 555 to 1,087 convictions, and then increased further in FY 2011 to 1,118 convictions."[162] Nevertheless, the findings of the Inspector General's report inspire general skepticism regarding the Obama administration's war on financial frauds, including mortgage fraud.

The exact extent to which the federal battle against mortgage fraud was sufficiently energetic or ultimately successful need not detain us. It is sufficient to note that policymakers recognized mortgage fraud as a major problem connected in some way to the Great Recession. Furthermore, federal and state lawmakers

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156. *Id.* at 23; *see also id.* at Appendix IV, 40–42 (reprinting Attorney General Holder's statement).

157. *Id.* at ii.

158. *Id.* at 28.

159. *Id.* at 28 (chart indicating 80% fewer criminal defendants, 76% fewer criminal victims, and 91% less in criminal losses); *see also* Mayer, Cava & Baird, *supra* note 13, at 579 (noting "a difference of eighty percent" in reported cases).

160. There were also errors in the reported numbers of civil defendants, civil victims, and the civil loss amounts. *See* DOJ MORTGAGE FRAUD AUDIT, *supra* note 124, at 28.

161. *Id.* at 25.

162. Memorandum from James J. Cole, Deputy Attorney General, U.S. Dep't of Justice, to Michael E. Horowitz, Inspector General, U.S. Dep't of Justice, (Feb. 21, 2014) (in DOJ MORTGAGE FRAUD AUDIT, *supra* note 124, at Appendix VI, 45).

addressed this issue with a variety of tools, including enacting new criminal mortgage fraud statutes, focusing resources and attention on the issue of mortgage fraud, and bringing civil and criminal actions against those who engaged in various forms of mortgage fraud.[163]

III. THE FEDERAL CRIME(S) OF MORTGAGE FRAUD

A. *Introduction: Fraud as a Socio-Legal Concept*

The discussion thus far has referred endlessly to the scourge of "mortgage fraud." But what exactly *is* mortgage fraud? This is a trickier question than it might seem because the term "mortgage fraud" lacks a precise legal meaning. Thus, legal actors who discuss or analyze mortgage fraud are compelled to choose among several possible meanings.

It is fair to assume that mortgage fraud is in some way related to the socio-legal concept of fraud. But fraud itself is a "ubiquitous and elusive"[164] concept that is notoriously challenging to define,[165] in part because it "is a legal concept designed to adapt alongside the evolving behaviors that it targets."[166] At the most basic level, fraud is "a generic term that encompasses the multifarious and often ingenious means by which one individual can gain an advantage over another through deliberate false suggestion, concealment, or misrepresentation of the truth."[167] But, of course, this type of dictionary definition barely begins to scratch the surface of the many "axes along which one might define fraud."[168] As Sam Buell explains:

> The most expansive conception of fraud would cover conduct and omissions as well as statements; encompass all acts that mislead, including negligent and even careful ones; impose further obligations of disclosure and care on actors in special relationships; permit all forms of sanctioning, civil and criminal; extend to deprivations of noneconomic as well as economic interests; and

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163. Smith, *supra* note 15, at 474–75 ("In response to the mortgage fraud epidemic, during recent years the federal government and the states have substantially increased the resources devoted to the investigation and prosecution of mortgage fraud crimes.").

164. Stuart P. Green & Matthew B. Kugler, *Public Perceptions of White Collar Crime Culpability: Bribery, Perjury, and Fraud*, 75 LAW & CONTEMP. PROBS. 33, 52 (2012) (observing that "the concept of fraud is both ubiquitous and elusive").

165. Ellen S. Podgor, *Criminal Fraud*, 48 AM. U. L. REV. 729, 738 (1999) ("Fraud . . . is not an easily defined term. The definition may change depending upon the statute in which the word appears.") (footnotes omitted).

166. Samuel W. Buell, *What is Securities Fraud?*, 61 DUKE L.J. 511, 520 (2011); *see also* Samuel W. Buell, *Novel Criminal Fraud*, 81 N.Y.U. L. REV. 1971, 1987 (2006) ("The law of fraud has expanded. The idea of what it means to take (or attempt to take) wrongfully by deception has grown to include more, and more elaborate, means and methods, while at the same time the means and methods of deception have evolved.").

167. Daniel T. Ostas, *When Fraud Pays: Executive Self-Dealing and the Failure of Self-Restraint*, 44 AM. BUS. L.J. 571, 571 (2007) (citing BLACK'S LAW DICTIONARY 685 (Thomson West, 8th ed. 2004); *see also* Mayer, Cava & Baird, *supra* note 13, at 521 ("'Fraud' is a generic word that includes a number of different kinds of actions, all of which can trigger civil or criminal liability; at its core, fraud is the intentional deception of a person or entity by another, made for monetary or personal gain.").

168. Buell, *What is Securities Fraud?, supra* note 166, at 520. Buell identifies six axes: (1) act; (2) fault; (3) context; (4) sanction; (5) harm; and (6) sector. *See id*. at 522–23.

> apply to a variety of interactions between individuals and the government in the realm of public and political functions.[169]

To simplify the discussion,[170] this Article focuses on the federal criminal law governing mortgage fraud.[171] Nevertheless, for many lawyers the basic concept of fraud is closely linked to civil tort liability for fraudulent misrepresentations or deceit—the common law tort of fraud—as reflected in the Restatement (Second) of Torts.[172] Thus, it is helpful, for comparative purposes, to keep the elements of civil fraud in mind as we discuss criminal fraud.[173] As one source explains, a plaintiff can recover for deceit if there is: (1) a defendant's misrepresentation of;[174] (2) a material;[175] (3) fact; (4) done with scienter;[176] (5) on which

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169. *Id.* at 524. Buell is careful, though, to distinguish an actor's goals from motives:

> Goals and motives are not to be confused. Goals are objectives; motives are reasons. Core fraud involves the goal of deception: the actor forms an objective of inducing action in another through deception and acts upon it. Her reasons for doing so may be simple or complex, financial or emotional, self- or other-regarding. Motive is of no consequence.

Id.

170. Even focusing on criminal law may not be as helpful as one hopes, given that "[w]hen it comes to fraud . . . the first-order question of substantive criminal law—what conduct constitutes the crime—is unusually unsettled and controversial." Buell, *Novel Criminal Fraud*, *supra* note 166, at 1972.

171. As noted earlier, there are now quite a few states that have specifically criminalized mortgage fraud. *See supra* notes 116–121 and accompanying text.

172. The Restatement (Second) of Torts provides: "One who fraudulently makes a misrepresentation of fact, opinion, intention or law for the purpose of inducing another to act or refrain from action in reliance upon it, is subject to liability to the other in deceit for pecuniary loss caused to him by his justifiable reliance upon the misrepresentation," RESTATEMENT (SECOND) OF TORTS § 525 (AM. LAW INST. 1977). *See also* RESTATEMENT (SECOND) CONTRACTS § 164(1) (AM. LAW INST. 1981) ("If a party's manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is justified in relying, the contract is voidable by the recipient.").

173. *See* Shannon M. Roesler, *Evaluating Corporate Speech about Science*, 106 GEO. L.J. 447, 473 (2018) ("Because courts use the common law of fraud as a reference point when analyzing statutory antifraud provisions, the basic common law elements are useful background.").

174. See Hillary A. Sale & Robert B. Thompson, *Market Intermediation, Publicness, and Securities Class Actions*, 93 WASH. U. L. REV. 487, 495–96 (2015) (citing WILLIAM L. PROSSER, HANDBOOK OF THE LAW OF TORTS § 105 (West Publishing Co., 4th ed. 1971)); *see also* Edward J. Normand, *Damages for Deceit: A Case Study in the Making of American Common Law*, 71 N.Y.U. ANN. SURV. AM. L. 333, 336 (2016) ("The typical elements of fraud are satisfied where for personal gain the defendant made an intentional and material misrepresentation of fact that reasonably induced the plaintiff to rely on the misrepresentation and thereby suffer damage."). I have fleshed out Sale and Thompson's list a bit with cites to some key sections from the Restatement (Second) of Torts.

175. *See* RESTATEMENT (SECOND) OF TORTS § 538(1) (AM. LAW INST. 1977) ("Reliance upon a fraudulent misrepresentation is not justifiable unless the matter misrepresented is material."). For the Restatement's definition of materiality, *see id.* § 538(2)(a) (stating that a matter is material if "a reasonable man would attach importance to its existence or nonexistence in determining his choice of action in the transaction in question"). The Restatement also has a less frequently quoted notion of materiality. *See id.* § 538(2)(b) (stating that a matter is material if "the maker of the representation knows or has reason to know that its recipient regards or is likely to regard the matter as important in determining his choice of action, although a reasonable man would not so regard it").

176. The Restatement explains the required mental state for fraudulent misrepresentation as follows, under the heading "Conditions Under Which Misrepresentation is Fraudulent (Scienter)." *Id.* § 526. A misrepresentation is

plaintiff relies;[177] (6) suffering damages as a consequence.[178] Although there have always been important definitional differences between civil and criminal conceptions of fraud, it is valuable to have these core elements of common law fraud in mind as we turn to the federal crime of mortgage fraud.

B. *FBI Definitions and Classifications of Mortgage Fraud*

So what is the federal crime of mortgage fraud or, more precisely, mortgage origination fraud?[179] Although the federal code currently contains over 4,000 crimes[180] and over 300 fraud and misrepresentation offenses,[181] no federal law specifically defines mortgage fraud.[182] Instead, mortgage fraud commonly is

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fraudulent if the maker: (1) "knows or believes that the matter is not as he represents it to be," *id.* § 526(a); (2) "does not have the confidence in the accuracy of his representation that he states or implies," *id.* § 526(b); or (3) knows that he does not have the basis for his representation that he states or implies. *Id.* § 526(c). *See also Scienter*, BLACK'S LAW DICTIONARY (10th ed. 2014) (defining scienter as both "[a] degree of knowledge that makes a person legally responsible for the consequences of his or her act or omission; the fact of an act's having been done knowingly," and "[a] mental state consisting in an intent to deceive, manipulate, or defraud"). A separate Restatement section provides for liability for negligent misrepresentations, particularly regarding business transactions. *See* RESTATEMENT (SECOND) OF TORTS § 552(1) (AM. LAW INST. 1977) ("One who . . . supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care . . . in obtaining or communicating the information.").

177. *See* RESTATEMENT (SECOND) OF TORTS § 525 (AM. LAW INST. 1977) ("One who fraudulently makes a misrepresentation of fact, opinion, intention or law for the purpose of inducing another to act or refrain from action *in reliance upon* it, is subject to liability to the other in deceit for pecuniary loss caused to him by his *justifiable reliance* upon the misrepresentation.") (emphasis added). The Restatement requires actual reliance on the misrepresentation and that the reliance be justified. *See id.* § 537(a)-(b). Reliance is also a part of contract defenses based upon fraud. See RESTATEMENT (SECOND) CONTRACTS § 164(1) (AM. LAW INST. 1981) ("If a party's manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is *justified in relying*, the contract is voidable by the recipient.") (emphasis added).

178. *See* RESTATEMENT (SECOND) OF TORTS § 546 (AM. LAW INST. 1977) (qualifying that liability for pecuniary loss is permissible if plaintiff's "reliance is a substantial factor in determining the course of conduct that results in his loss").

179. The distinction between mortgage origination fraud and other forms of mortgage-related fraud is discussed *infra* Part V.B. I am using the term "mortgage fraud" as synonymous with mortgage origination fraud for reasons that will become clearer below.

180. *See* Rachel E. Barkow, *Federalism and Criminal Law: What the Feds Can Learn from the States*, 109 MICH. L. REV. 519, 523–24 (2011) ("The number of federal criminal laws now hovers somewhere over 4,000, with roughly 40% of the laws passed after the Civil War coming in the 25-year period between 1970 and 1998."); Michael Cottone, *Rethinking Presumed Knowledge of the Law in the Regulatory Age*, 82 TENN. L. REV. 137, 141 (2014) ("Tellingly, no exact count of the number of federal statutes that impose criminal sanctions has ever been given, but estimates from the last fifteen years range from 3,600 to approximately 4,500."); Irina D. Manta, *Intellectual Property and the Presumption of Innocence*, 56 WM. & MARY L. REV. 1745, 1750 n.10 (2015) ("The current estimate is that there are between 4000 and 5000 federal criminal statutes, but nobody knows the exact number because no comprehensive list exists. There may also be over 300,000 different statutory or regulatory offenses that contain the possibility of criminal penalties.").

181. *See* William J. Stuntz, Commentary, *O.J. Simpson, Bill Clinton, and the Transsubstantive Fourth Amendment*, 114 HARV. L. REV. 842, 863 (2001) (citing, inter alia, Jeffrey Standen, *An Economic Perspective on Federal Criminal Law Reform*, 2 BUFF. CRIM. L. REV. 249, 289 (1998)).

182. *See* Ceresney, Eng & Nuttall, *supra* note 75, at 236 n.65 ("There is no single federal statute covering mortgage fraud."); Arthur Durst, *Property and Mortgage Fraud under the Mandatory Victims Restitution Act:*

prosecuted under a variety of federal criminal statutes, most notably the prohibitions on bank, wire, and mail fraud.[183] In addition, the federal code contains a provision that criminalizes the making of false statements to various financial institutions,[184] which frequently is violated in mortgage fraud schemes.[185]

In the absence of a single federal statute defining a crime of "mortgage fraud," commentators nearly always refer to the FBI's definitions and categorizations.[186] It is thus fair to say that the FBI definition has become the de facto definition of "mortgage fraud" in scholarly literature. In 2011, the FBI defined "mortgage

What Is Stolen and When Is It Returned?, 5 WM. & MARY BUS. L. REV. 279, 287 (2014) (observing that "[a]lthough there is no specific federal law against mortgage fraud, there are several federal criminal laws that ensnare mortgage fraudsters"); Christina M. Schuck, *A New Use for the Responsible Corporate Officer Doctrine: Prosecuting Industry Insiders for Mortgage Fraud*, 14 LEWIS & CLARK L. REV. 371, 373–74 (2010) ("Unlike other frauds such as health care fraud, there is no specific federal statute associated with mortgage fraud."); Smith, *supra* note 15, at 475 ("Although there is no single federal statute addressed to mortgage fraud, federal prosecutors can select from a wide variety of existing financial crime statutes, with bank fraud, mail and wire fraud, and money laundering most commonly used."); Nicole Stowell et al., *Mortgage Fraud: Schemes, Red Flags, and Responses*, 6 J. OF FORENSIC & INVESTIGATIVE ACCT. 225, 246–47 (2014) ("Although no federal mortgage fraud statute exists, federal law enforcement authorities employ a wide variety of statutes to investigate and prosecute mortgage fraud schemes. These statutes involve bank fraud, wire fraud, mail fraud, false statements, money laundering, conspiracy, equity skimming . . . social security number fraud, and false identification fraud.") (footnotes omitted); Daniel B. Mestaz, *Building a Mortgage Fraud Defense*, 47 ARIZ. ATT'Y 18, 21–22 (2011) (explaining that "[t]here is no federal mortgage fraud criminal statute *per se*").

183. *See* Linda Marshall, *Making Choices: Charging and Plea Negotiations*, U.S. ATT'YS' BULL., May 2010, at 18, 18–21 (reviewing statutes commonly applied to mortgage fraud); Mestaz, *supra* note 183, at 21–22 (explaining that "prosecutors proceed under a variety of statutes") (collecting statutes); Holly A. Pierson, *Mortgage Fraud Boot Camp: Basic Training on Defending a Criminal Mortgage Fraud Case*, CHAMPION, Sept.–Oct. 2007, at 14, 15 n.3 (collecting statutes). The three sources above cite, collectively, the following federal criminal statutes: 18 U.S.C. § 1014 (false statements to covered lenders); 18 U.S.C. § 371 (conspiracy to commit § 1014 violation); 18 U.S.C. § 1341 (mail fraud); 18 U.S.C. § 1343 (wire fraud); 18 U.S.C. § 1344 (bank fraud); 18 U.S.C. § 1349 (conspiracy to commit mail, wire, or bank fraud); 18 U.S.C. § 2 (aiding and abetting); 18 U.S.C. § 1956 (a) (money laundering); U.S.C. § 1005 (false entries to federally insured institutions); 18 U.S.C. § 1028 (identity theft); 18 U.S.C. § 1029 (credit card fraud); 18 U.S.C. § 1030 (computer fraud); 18 U.S.C. § 1519 (obstruction of justice); 18 U.S.C. §§ 1951–1961 (RICO); 18 U.S.C. § 1957 (monetary transactions with illegal proceeds); 18 U.S.C. § 1349 (conspiracy); 18 U.S.C. § 1342 (use of fictitious name or address in fraud); 18 U.S.C. § 2314 (transportation of stolen goods or securities); 18 U.S.C. § 1010 (false statements in HUD transactions); 42 U.S.C. § 408 (fraud related to Social Security documents).

184. *See* 18 U.S.C. § 1014 ("Whoever knowingly makes any false statement or report . . . for the purpose of influencing in any way the action of [listed entities] . . . shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.").

185. I may be putting the definitional cart before the horse here, since the statutes identified here are most often used in mortgage *origination* fraud schemes. One who believes that the concept of "mortgage fraud" is far broader than mortgage origination fraud could object to my selection of these four key mortgage fraud statutes as covering "mortgage fraud."

186. See, e.g., Marvin N. Bagwell, *Can't Live Without Air: Title Insurance and the Bursting of the Real Estate Bubble*, 30 PACE L. REV. 180, 224 (2009); Gabrielle A. Bernstein, *The Role of Expectations in Assessing Intended Loss in Mortgage-Fraud Schemes*, 2010 U. CHI. LEGAL F. 337, 339–41 (2010); Gans, *supra* note 25, at 145–46; Shayna A. Hutchins, *Flip That Prosecution Strategy: An Argument for Using RICO to Prosecute Large-Scale Mortgage Fraud*, 59 BUFF. L. REV. 293, 296–97 (2011); Jordan, *supra* note 145, at 499; KOLLER, *supra* note 17, at 27; Koller, et al., *supra* note 98, at 555; McCann, *supra* note 123, at 360; Nguyen, *supra* note 26, at 8–9; Nguyen & Pontell, *supra* note 26, at 592; Pierson, *supra* note 183, at 15; RYDER, *supra* note 74, at 53–54; Schuck, *supra* note 182, at 373–74; Stowell, et al., *supra* note 182, at 227; Totten, *supra* note 13, at 1619–20.

fraud" as "a material misstatement, misrepresentation, or omission relied on by an underwriter or lender to fund, purchase, or insure a loan."[187] This definition is similar to the mortgage fraud definition currently on the FBI's website:

> It is crime characterized by some type of material misstatement, misrepresentation, or omission in relation to a mortgage loan which is then relied upon by a lender. A lie that influences a bank's decision—about whether, for example, to approve a loan, accept a reduced payoff amount, or agree to certain repayment terms—is mortgage fraud.[188]

At an earlier point, however, the FBI defined mortgage fraud a bit differently as "the intentional misstatement, misrepresentation, or omission by an applicant or other interested parties, relied on by a lender or underwriter to provide funding for, to purchase, or to insure a mortgage loan."[189]

There are two key differences between the FBI's mortgage fraud definitions. First, the older FBI definition required that the misrepresentation be *intentional*, while present FBI definitions have no such explicit requirement. Second, current FBI definitions explicitly require *materiality*, whereas the older FBI definition of mortgage fraud did not have such a requirement. All of the FBI definitions share the important element of reliance by the lender or underwriter. As discussed below, the inclusion of reliance is problematic.

In addition to defining mortgage fraud, the FBI generally classifies mortgage fraud into two categories based upon the ultimate goals of the scheme:[190] fraud for property or housing and fraud for profit.[191] These two classifications of mortgage

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187. Fin. Crimes Intelligence Unit, Fed. Bureau of Investigation, 2010 MORTGAGE FRAUD REPORT: YEAR IN REVIEW 5 (2011) [hereinafter 2010 FBI Mortgage Fraud Report], http://www.fbi.gov/stats-services/publications/mortgage-fraud-2010/mortgage-fraud-report-2010; *see also* Fed. Bureau of Investigation, 2009 MORTGAGE FRAUD REPORT: "YEAR IN REVIEW" (2009) (citing FBI Fin. Crimes Sec., Fin. Institution Fraud Unit, MORTGAGE FRAUD: A GUIDE FOR INVESTIGATORS, (2003), http://www.fbi.gov/stats-services/publications/mortgage-fraud-2009); Off. of L. Enforcement Support, Fin. Crimes Enforcement Network, Mortgage Loan Fraud Connections with Financial Crime: An Evaluation of Suspicious Activity Reports Filed by Money Service Businesses, Securities and Futures Firms, Insurance Companies and Casinos 1 (March 2009) ("Mortgage loan fraud involves intentional misrepresentations to a lender for the purpose of obtaining a loan that would otherwise not be advanced by the lender.").

188. *Financial Institution/Mortgage Fraud*, FBI.GOV, https://www.fbi.gov/investigate/white-collar-crime/mortgage-fraud (last visited Sept. 12, 2019).

189. FED. BUREAU OF INVESTIGATION, 2008 MORTGAGE FRAUD REPORT: "Year in Review" (2008) [hereinafter FBI 2008 MORTGAGE FRAUD REPORT], http://www.fbi.gov/stats-services/publications/mortgage-fraud-2008.

190. There is a third possible category: fraud for other criminal purposes (such as money laundering). *See* FFIEC White Paper, *infra* note 192, at 4.

191. *See* Pierson, *supra* note 183, at 14 (citing FIN. CRIMES SEC., FED. BUREAU OF INVESTIGATION, FBI FINANCIAL CRIMES REPORT TO THE PUBLIC (Sept. 2006), http://www.fbi.gov/publications/financial/fcs_report2006/financial_crime_2006.htm; FFIEC FRAUD INVESTIGATIONS SYMPOSIUM, THE DETECTION, INVESTIGATION, AND DETERRENCE OF MORTGAGE LOAN FRAUD INVOLVING THIRD PARTIES: A WHITE PAPER 2 (Oct. 27–Nov. 7, 2003), http:// www.ffiec.gov/exam/3P_Mtg_Fraud_wp_oct04.pdf).

fraud are referenced in almost every book and article on the topic.[192] The FBI explains the first form of mortgage fraud as follows: "Fraud for property/housing entails misrepresentations by the applicant for the purpose of purchasing a property for a primary residence. This scheme usually involves a single loan. Although applicants may embellish income and conceal debt, their intent is to repay the loan."[193] Accordingly, the misrepresentations in a fraud for housing scheme, regardless of the source,[194] typically involve matters related to the borrower's creditworthiness and financial well-being,[195] such as the borrower's income, assets, and debts.[196]

Fraud for profit differs from fraud for housing in several key respects. First, fraud for profit may involve multiple loans[197]—not a single borrower applying for a single loan, as is often the case with fraud for housing.[198] Second, the cast of characters in fraud for profit schemes is often larger.[199] Perpetrators of fraud for profit frequently include industry insiders, such as "appraisers, accountants, attorneys, real estate brokers, mortgage underwriters and loan processors, settlement or

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192. *See, e.g.*, Bagwell, *supra* note 186, at 225–26; Bernstein, *supra* note 186, at 339–41; Carrillo, *supra* note 83, at 37; Gans, *supra* note 25, at 145–46; John M. Griffin & Gonzalo Maturana, *Who Facilitated Misreporting in Securitized Loans?*, 29 REV. FIN. STUD. 384, 388 (2016); Hutchins, *supra* note 186, at 296–97; Jordan, *supra* note 145, at 499; Koller, *supra* note 17, at 27; Koller, et al., *supra* note 98, at 555; McCann, *supra* note 123, at 360; Nguyen & Pontell, *supra* note 26, at 595; Schuck, *supra* note 182, at 373–74; Pierson, *supra* note 183, at 15; Totten, *supra* note 13, at 1619–20; Nguyen, *supra* note 26, at 8–9; RYDER, *supra* note 74, at 54.

193. FBI 2008 MORTGAGE FRAUD REPORT, *supra* note 190; Bernstein, *supra* note 187, at 341 ("Defendants commit fraud for housing in order to acquire property that they intend to maintain as a homeowner, and often carry out the fraud by making misrepresentations about their income and other information relevant to their credit rating, in order to obtain a loan that they intend to—and often do— fully repay.").

194. *See supra* notes 30–38 and accompanying text for discussion of the parties who might be responsible for the misrepresentations.

195. *See, e.g.*, United States v. Vargas, 629 F. App'x 415, 416 (3d Cir. 2015) (with the assistance of a mortgage broker, "defendants repeatedly falsified employment information, inflated income, concealed debt, and lied about their primary residence, in order to obtain mortgage loans").

196. *See* FBI 2010 MORTGAGE FRAUD REPORT, *supra* note 188, at 17 (explaining that fraud for housing may "involve falsifying a borrower's financial information—such as income, assets, liabilities, employment, rent, and occupancy status—to qualify the buyer, who otherwise would be ineligible, for a mortgage loan"); Gans, *supra* note 25, at 146 (explaining that "there is misrepresentation of income, assets, or debts . . . frequently in 'liar loan' situations") (footnotes and citations omitted); Totten, *supra* note 13, at 1619 (explaining that "'[f]raud for housing' or 'fraud for property' schemes typically aim to put a person in possession of a dwelling or property for which that person would not otherwise qualify").

197. FBI 2008 Mortgage Fraud Report, *supra* note 189.

198. These lines can be blurry, as in cases of fraud connected to the borrower's refinancing of a home mortgage or home equity lines of credit. *See* United States v. Edelkind, 467 F.3d 791 (1st Cir. 2006) (prosecuting a defendant for falsehoods related to numerous real estate-related loans including mortgages, mortgage refinancing, and home equity loans).

199. *See* Pierson, *supra* note 183, at 15 ("Unlike fraud for housing, fraud for profit often involves multiple conspirators acting in concert. Adding to the complexity of these cases, it is not always obvious which participants in the loan process are involved in any given fraudulent scheme."); *see also* DOJ MORTGAGE FRAUD AUDIT, *supra* note 73, at 18 ("Mortgage fraud cases often involve a number of defendants with varying levels of complicity. Generally, mortgage fraud schemes require the participation, or at least acquiescence, of a number of players, such as straw buyers, real estate agents, appraisers, mortgage brokers, and closing attorney/agent.").

title insurance employees, mortgage brokers, and loan originators,"[200] who "use their insider knowledge to override lender controls."[201] For this reason, the FBI has referred to fraud for profit as "industry insider fraud,"[202] though the terms may not be exactly synonymous. According to the FBI, eighty percent of all mortgage fraud involves industry insiders.[203] Third, and related to the first two points, fraud for profit typically involves more elaborate schemes than fraud for housing.[204] These more complex and financially harmful schemes historically have received the most attention from law enforcement agencies.[205]

Fourth, and finally, in contrast to fraud for housing or property, the named property buyer and mortgage borrower in a fraud for profit scheme generally does not intend to reside in the property or repay the loan.[206] Some sources refer to the

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200. McCann, *supra* note 123, at 361 (2010) (citing FBI 2008 MORTGAGE FRAUD REPORT, *supra* note 189); *see also* Pierson, *supra* note 183, at 15 ("Unlike fraud for housing, fraud for profit often involves multiple conspirators acting in concert. Adding to the complexity of these cases, it is not always obvious which participants in the loan process are involved in any given fraudulent scheme."); Smith, *supra* note 15, at 478 ("Often fraud for profit involves multiple transactions and the use of one or more 'industry insider' intermediaries, such as a corrupt mortgage broker, real estate appraiser, or settlement agent.").

201. Schuck, *supra* note 182, at 374–75 (citing FED. BUREAU OF INVESTIGATION, FINANCIAL CRIMES REPORT TO THE PUBLIC: FISCAL YEAR 2007 (2007), https://www.fbi.gov/stats-services/publications/fcs_report2007).

202. *Id.* at 361 ("The federal government focuses on investigating fraud for profit, which is more egregious than fraud for housing, and is sometimes referred to as 'industry insider fraud.'") (citing FED. BUREAU OF INVESTIGATION, FINANCIAL CRIMES REPORT TO THE PUBLIC: FISCAL YEAR 2007 (2007), https://www.hsdl.org/?abstract&did=486259).

203. *See* FCIC REPORT, *supra* note 4, at 160 (citing Mortgage Fraud and its Impact on Mortgage Lenders, Hearing Before the H. Fin. Serv. Subcomm. on Hous. and Cmty. Opportunity, 108th Cong. (2004) (statement of Chris Swecker, Assistant Director, Criminal Investigative Division, FBI). McCann, *supra* note 123, at 361 ("Fraud perpetrated by industry insiders accounts for 80 percent of all reported fraud losses.").

204. It is not necessary to catalog the innumerable mortgage fraud for profit schemes here, though one of the most well-known is "property flipping."

> Property flipping is best described as purchasing properties and artificially inflating their value through false appraisals. The artificially valued properties are then repurchased several times for a higher price by associates of the "flipper." After three or four sham sales, the properties are foreclosed on by victim lenders. Often flipped properties are ultimately repurchased for 50–100 percent of their original value.

United States Department of Justice, FEDERAL BUREAU OF INVESTIGATION (FBI), FINANCIAL CRIMES REPORT TO THE PUBLIC, D-2 (2005), https://www.fbi.gov/stats-services/publications/fcs_report2005; *see also* 2010 FBI MORTGAGE FRAUD REPORT, *supra* note 188 (also describing property flipping); Smith, *supra* note 15, at 479 (describing flipping). Property flipping must not be confused with loan flipping, which harms homeowner-borrowers. *See* Baher Azmy, *Squaring the Predatory Lending Circle*, 57 Fla. L. Rev. 295, 335 (2005) ("Loan flipping refers to the repeated refinancing of a borrower's loan (typically within the first five years of the loan) through another fee-loaded loan and without any reasonable benefit to the borrower.").

205. T. Dietrich Hill, *The Arithmetic of Justice: Calculating Restitution for Mortgage Fraud*, 113 COLUM. L. REV. 1939, 1944 (2013) ("Professional loan origination schemes, the most common kind of fraud, can easily be repeated to multiply the ill-gotten gains with a neverending supply of fake names or willing accomplices. Because of this, they tend to be more serious, and to be prosecuted more often, than individual mortgage frauds.").

206. Fraud for profit schemes may involve "straw buyers." *See* United States v. Parish, 565 F.3d 528, 531 n.2 (8th Cir. 2009) ("A straw buyer is a person who obtains a loan for the purchase of property the straw buyer never intends to own or occupy."). For examples of cases involving straw buyers, *see, e.g.*, United States v. Scott, 877

making of false statements regarding the borrower's intent to use a property as a primary residence as "occupancy fraud."[207] The motivation behind such misrepresentations is plain: borrowers who actually live in a residence that secures a loan obtain much lower interest rates[208] and other favorable loan terms, such as lower down payment requirements.[209] The perils of such misrepresentations are also plain: lenders may end up with riskier borrowers, including those who are "over-leveraged from holding multiple mortgages"[210] and thus are more likely to default.[211] It should be observed, though, that occupancy misrepresentations could be made in both fraud for property or fraud for profit schemes.

IV. JUDICIAL DOCTRINE ON MATERIALITY, RELIANCE, AND INTENT

The FBI has proffered an influential definition of mortgage fraud that, while not legally binding, has become the de facto definition of mortgage fraud in scholarly and public policy discussions of the subject. Presumably, to some extent, this definition represents the DOJ's and FBI's understanding of one key form of mortgage-related criminal activity that warrants investigation, prosecution, and punishment. Unfortunately, scholarly reliance on this definition is quite problematic.[212] To understand why the FBI mortgage fraud definition is flawed, one needs to

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F.3d 30, 33 (1st Cir. 2017), *cert. denied*, 138 S. Ct. 2635 (2018); United States v. Appolon, 695 F.3d 44, 51 (1st Cir. 2012); United States v. Hill, 643 F.3d 807 (11th Cir. 2011).

207. Erwin J. Shustak, *Recent Developments and Issues in Mortgage Fraud Cases*, *in* Mortgage and Finance Fraud Litigation Strategies: Leading Lawyers on Managing the Complexities of Fraud Cases, Understanding Government Regulations, and Structuring an Effective Litigation Plan 59, 66 (2015), *available on* Westlaw at 2015 WL 7300485, at *5.

208. Griffin & Maturana, *supra* note 192, at 391 (explaining that "originators charge lower interest rates and require smaller down payments for owner occupants"); Jiang, Nelson & Vytlacil, *supra* note 26, at 12 (noting that "borrowers purchasing a second home or investment property could falsely claim that the property will be owner occupied and used as a primary residence, thereby securing a lower interest rate").

209. George Lefcoe, *Should We Ban or Welcome "Spec" Home Buyers?*, 36 J. LEGIS. 1, 5 (2010) (explaining that "many spec buyers commit occupancy fraud, lying about their intentions to reside in the mortgaged property in order to qualify for low- or no-down payment loans with favorable interest rates," which "enables them to benefit from leverage, magnifying their gains if home prices go up while leaving the mortgage lender with the losses if prices go down") (footnotes and citations omitted).

210. Jiang, Nelson & Vytlacil, *supra* note 26, at 12.

211. Eggert, *supra* note 21, at 1288 ("Lenders should naturally be interested in whether borrowers live or will live in the property secured by a loan, as subprime default rates are higher where the owner does not occupy the house."); Griffin & Maturana, *supra* note 192, at 391 ("Borrowers who own and occupy a property are less likely to default than borrowers who do not occupy the property."); Shustak, *supra* note 207, at *5 (stating that "[t]here is a much lower incidence of mortgage foreclosures and defaults for owner-occupied properties").

212. Not everyone is a fan of the FBI's definitions and classification of mortgage fraud. William Black criticizes the FBI for adopting Mortgage Bankers Association's two-part classification of mortgage fraud, which he believes to be "facially absurd." Black, *supra* note 137, at 1013. Black argues that "[t]he MBA represents mortgage bankers, some of the worst actors in the fraud at the core of the financial crisis." *Id*. at 1013–14. Black believes that the MBA's borrower-focused view of mortgage fraud (adopted by the FBI) does not fully account for the criminal activities of bank insiders—control frauds that profit insiders but ultimately cripple and damage financial institutions. *Id*. at 1014–15; *see also id*. at 988 ("The MBA . . . is the trade association of the 'perps' and the FBI has accepted uncritically the MBA's 'definition' of 'mortgage fraud.' That definition defines out of existence accounting control fraud.").

understand judicial doctrine related to the primary federal statutes under which mortgage origination fraud is punished. This section provides this necessary doctrinal background on four key "mortgage fraud" statutes: 18 U.S.C. § 1014 (false statements to lenders); 18 U.S.C. § 1341 (mail fraud); 18 U.SC. § 1343 (wire fraud); and 18 U.S.C. § 1344 (bank fraud).

A. *Materiality*

Unlike common law fraud tort claims,[213] not all federal criminal offenses involving misrepresentations require proof of materiality.[214] For those federal criminal offenses that lack express materiality requirements,[215] the courts analyze the statutory text and, at times, legislative history, to determine whether to require proof of materiality as an element of the offense.[216]

Approximately twenty years ago, the Supreme Court decided two key cases concerning materiality in federal criminal statutes that have great importance for mortgage origination fraud prosecutions. First, in *United States v. Wells*, the Supreme Court held that 18 U.S.C. § 1014,[217] the federal statute that criminalizes making false statements to banks,[218] does *not* contain a materiality requirement.[219] In contrast to *Wells*, where the Court declined to read a materiality requirement into § 1014,[220] just two years later the Supreme Court in *Neder* unanimously held that

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213. *See supra* notes 170–76 and accompanying text.

214. *See* United States v. Allen, 116 F. App'x 210, 216 (10th Cir. 2004) (explaining that the Supreme Court "has not moved uniformly to read a materiality requirement into all of the fifty-four sections of the U.S. Code criminalizing false statements that . . . expressly lack such a requirement").

215. For example, "[t]he federal statute prohibiting false statements to Government officials punishes 'whoever, in any matter within the jurisdiction of the executive, legislative, or judicial branch of the Government . . . makes any materially false, fictitious, or fraudulent statement or representation.'" United States v. Alvarez, 132 S. Ct. 2537, 2546 (2012) (citing 18 U.S.C. § 1001). The Supreme Court has stated: "It is uncontested that conviction under this provision requires that the statements be 'material' to the Government inquiry, and that 'materiality' is an element of the offense that the Government must prove." United States v. Gaudin, 515 U.S. 506, 509 (1995). It is not clear, however, how much work the materiality requirement in 18 U.S.C. § 1001 does under current judicial interpretations of the statute. *See* Lisa Kern Griffin, *Criminal Lying, Prosecutorial Power, and Social Meaning*, 97 CAL. L. REV. 1515, 1561 (2009) ("Materiality as it is currently construed means nothing more than relevant or on topic, and the definition thus encompasses even patently harmless lies.").

216. Furthermore, those federal offenses that do have materiality requirements do not necessarily adopt the Restatement of Tort's definition of that key concept. *See* Universal Health Servs., Inc. v. United States, 136 S. Ct. 1989, 2002–03 (2016) (discussing materiality requirements found in federal fraud statutes).

217. *See* 18 U.S.C. § 1014 (2011) ("Whoever knowingly makes any false statement or report . . . for the purpose of influencing in any way the action of [listed entities] . . . shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.").

218. The text of the statute lists numerous specific entities, including*, inter alia*, mortgage lending businesses, institutions insured by the Federal Deposit Insurance Corporation, and State-chartered credit unions. *See* 18 U.S.C. § 1014 (2011). In the interest of brevity, covered entities are referred to here as lenders or banks.

219. United States v. Wells, 519 U.S. 482, 498–99 (1997).

220. At the time that *Wells* was decided, it went against the great weight of circuit court precedent. *See Wells*, 519 U.S. at 486 n.3 (detailing a nine to one circuit split); Evan C. Zoldan, *The King Is Dead, Long Live the King!: Sovereign Immunity and the Curious Case of Nonappropriated Fund Instrumentalities*, 38 CONN. L. REV. 455, 505–06 (2006) (explaining that the *Wells* Court held "that the plain language of the statute controlled, notwithstanding the nearly uniform courts of appeals decisions and legislative history to the contrary.").

the federal wire, mail, and bank fraud statutes all required proof of a misrepresentation's materiality to sustain a criminal conviction.[221] The basic materiality principles established by *Wells* and *Neder* remain good law: proof of materiality is not required in § 1014 cases,[222] whereas proof of materiality is required for cases brought under the federal bank, wire, and mail fraud statutes.[223]

B. *Reliance, Loss, and Damages*

Even as *Neder* held that the federal bank, wire, and mail fraud statutes require proof of materiality, the Supreme Court emphatically declared that these three statutes did not require proof of justifiable reliance or actual damages.[224] The Court stated:

> The common-law requirements of "justifiable reliance" and "damages," . . . plainly have no place in the federal fraud statutes. . . . By prohibiting the "scheme to defraud," rather than the completed fraud, the elements of reliance and damage would clearly be inconsistent with the statutes Congress enacted.[225]

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221. *See* Neder v. United States, 527 U.S. 1, 25 (1999) (holding "that materiality of falsehood is an element of the federal mail fraud, wire fraud, and bank fraud statutes."); *see also* Ellen S. Podgor, *Arthur Andersen, LLP and Martha Stewart: Should Materiality Be an Element of Obstruction of Justice?*, 44 WASHBURN L.J. 583, 589 (2005) (explaining that "the *Neder* Court was unanimous in its finding that mail, wire, and bank fraud required the government to prove materiality as an element of the offense.").

222. As the Seventh Circuit stated: "[I]f you make a knowingly false statement intending to influence a bank, it's no defense that you didn't succeed in influencing it or even that you couldn't have succeeded. Materiality is not an element of the offense punished by section 1014." United States v. Phillips, 731 F.3d 649, 652 (7th Cir. 2013) (en banc) (Posner, J.) (citing United States v. Lane, 323 F.3d 568, 582–83 (7th Cir. 2003); United States v. Wells, 519 U.S. 482, 484 (1997)). *See also* United States v. Sandlin, 589 F.3d 749, 754 (5th Cir. 2009) ("A false statement need not be material nor relied upon by the bank to violate Section 1014."); United States v. Swanquist, 161 F.3d 1064, 1075 (7th Cir. 1998) ("[M]ateriality is not, and never was, an element of the crime of knowingly making a false statement to a federally-insured bank under § 1014.").

223. *See* Jones v. United States, No. 5:13-CV-414-D, 2016 WL 8999383, at *7 n.1 (E.D.N.C. Sept. 21, 2016), *appeal dismissed*, 680 F. App'x 258 (4th Cir. 2017) ("In contrast to false statements under 18 U.S.C. § 1014, bank fraud under 18 U.S.C. § 1344 requires materiality."). The exact meaning and content of the materiality requirements under federal fraud statutes is a separate, important question, which will not be addressed here. For discussion on this issue, *see* Lauren D. Lunsford, *Fraud, Fools, and Phishing: Mail Fraud and the Person of Ordinary Prudence in the Internet Age*, 99 KY. L.J. 379, 380 (2010–2011) (explaining courts of appeals "have interpreted the materiality requirement differently, creating a split in the circuits as to what federal prosecutors have to prove in order to convict a defendant of mail fraud.").

224. The Supreme Court has "construed identical language in the wire and mail fraud statutes *in pari materia*." Pasquantino v. United States, 544 U.S. 349, 355 n.2 (2005) (italics in original). *See also in pari materia*, BLACK'S LAW DICTIONARY 911 (Thomas West, 10th ed. 2014) ("It is a canon of construction that statutes that are *in pari materia* may be construed together, so that inconsistencies in one statute may be resolved by looking at another statute on the same subject."); BRYAN A. GARNER, A DICTIONARY OF MODERN LEGAL USAGE 451 (Oxford University Press, 2d ed. 1995) ("The common maxim is that statutes *in pari materia* are to be construed together.").

225. *Neder*, 527 U.S. at 24–25.

Over the past twenty years, the federal circuit courts repeatedly have reiterated the anti-reliance principle enunciated in *Neder* in a variety of bank, wire, and mail fraud cases.[226]

Furthermore, the Supreme Court itself has shown no intention of retreating from *Neder*'s anti-harm and anti-reliance principles in federal criminal fraud cases. Three examples illustrate the Court's resolve. First, in 2008, the Supreme Court extended *Neder*'s anti-reliance teachings to a RICO case,[227] holding that "[u]sing the mail to execute or attempt to execute a scheme to defraud is indictable as mail fraud, and hence a predicate act of racketeering under RICO, *even if no one relied on any misrepresentation*."[228] Second, in a 2014 bank fraud case, the Supreme Court "unanimously rejected the argument that . . . the defendant's scheme must create a risk of financial loss to the financial institution."[229] Justice Kagan, writing for the Court, pointed out that the defendant's argument "fits poorly" with *Neder*'s "prior holding that the gravamen of § 1344 is the 'scheme,' rather than 'the completed fraud,' and that the offense therefore does not require 'damage' or 'reliance.'"[230] Third, and finally, in 2016, the Supreme Court made this anti-reliance

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226. *See, e.g.*, United States v. Weaver, 860 F.3d 90, 95 (2d Cir. 2017) ("With respect to damages . . . the government 'need not prove that the victims of the fraud were *actually* injured, but only that defendants *contemplated* some actual harm or injury to their victims.'") (quoting United States v. Greenberg, 835 F.3d 295, 306 (2d Cir. 2016) (emphasis in original); United States v. Graham, 477 F. App'x 818, 824 (2d Cir. 2012) (explaining that "'justifiable reliance' is not an element of mail fraud or wire fraud under federal criminal law"); United States v. Bradley, 644 F.3d 1213, 1239 (11th Cir. 2011) ("Significantly, the mail and wire fraud statutes 'punish unexecuted as well as executed schemes.' It is therefore unnecessary that the victim actually relies on the misrepresentation or omission; proof of intent to defraud is sufficient.") (quoting Pelletier v. Zweifel, 921 F.2d 1465, 1498 (11th Cir.1991)); Mendez Internet Mgmt. Servs., Inc. v. Banco Santander de Puerto Rico, 621 F.3d 10, 15 (1st Cir. 2010) (stating that "unlike common-law fraud, mail and wire fraud does not require first-party reliance"); United States v. Pizano, 421 F.3d 707, 722 (8th Cir. 2005) ("Under the bank fraud statute, the Government need not prove that the financial institution actually relied on the defendant's misrepresentations."); United States v. Daniel, 329 F.3d 480, 486 (6th Cir. 2003) (stating that the Supreme Court's decision in *Neder* "makes it even clearer that actual reliance is not required for mail or wire fraud"); United States v. Barrett, 178 F.3d 643, 648 (2d Cir. 1999) ("[T]he bank need not be actually victimized as long as a defendant acted with the requisite intent. Therefore, actual or potential loss to the bank is not an element of the crime of bank fraud but merely a description of the required criminal intent.") (citing United States v. Stavroulakis, 952 F.2d 686, 694 (2d Cir. 1992)).

227. RICO is the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961–1968.

228. Bridge v. Phoenix Bond & Indem. Co., 553 U.S. 639, 648 (2008) (emphasis added).

229. Peter MacKenna, *Financial Institutions Fraud*, 54 AM. CRIM. L. REV. 1333, 1341 (2017) (citing Loughrin v. United States, 573 U.S. 351, 366 n.9 (2014)).

230. *Loughrin*, 573 U.S. at 366 n.9 (2014) (citing Neder v. United States, 527 U.S. 1, 25 (1999)). In *Loughrin*, the Court acknowledged that a "defendant's scheme to obtain bank property by means of a false statement may not succeed," but explained that the Court had "long made clear that such failure is irrelevant in a bank fraud case, because § 1344 punishes not "completed frauds," but instead fraudulent "scheme[s]." *Id.* at 360–62 (quoting *Neder*. 527 U.S. at 25). The *Loughrin* case involved 18 U.S.C. § 1344(2), as opposed to § 1344(1). *See infra* notes 252 and accompanying text for a discussion of the two parts of 18 U.S.C. § 1344. There is nothing in *Loughrin* that would suggest that § 1344(1) and § 1344(2) cases can be distinguished in terms of the need to prove risk of financial loss.

point even more plain, explaining that the federal bank fraud statute does not demand "a showing of ultimate financial loss" on the part of the bank.[231]

Like the federal bank, wire, and mail fraud statutes, many federal courts have held that reliance or actual loss is not required for a conviction under § 1014.[232] Over thirty years ago, the Fifth Circuit observed: "It is settled law that a section 1014 offense is 'a crime of subjective intent that requires neither reliance by the lending institution nor an actual defrauding for its commission.'"[233] Nothing has changed in the intervening decades. For instance, in 2003, the Seventh Circuit observed: "[M]uch like materiality, loss is not an element under § 1014. Because the lack of loss is not a defense, evidence regarding the lack of loss is irrelevant."[234] Taking the point even further, the Eleventh Circuit has stated that the bank in a § 1014 case does not even need to be aware of the defendant's false statement—just making the statement alone with requisite intent is enough to trigger criminal liability.[235] In sum, § 1014 is similar to federal bank, wire, and mail frauds (and dissimilar from the common law conception of fraud) in that it rejects the need to prove loss or actual reliance.

C. *Mental States*

All four primary mortgage origination fraud statutes require some proof regarding knowledge, intent, scienter, or *mens rea*.[236] We can begin with § 1014.

231. Shaw v. United States, 137 S. Ct. 462, 467 (2016).

232. *See* United States v. Taylor, 808 F.3d 1202, 1205 (9th Cir. 2015) (holding "that proof of a risk of loss to a financial institution is not required for conviction of making a false statement in violation of § 1014."); United States v. Grant, 211 F. App'x 889, 893 (11th Cir. 2006) (explaining that the bank need not be aware of or "actually be deceived by the false statements when they are made.") (citing United States v. Johnson, 585 F.2d 119, 124–25 (5th Cir. 1978)); Elliott v. United States, 332 F.3d 753, 764 (4th Cir. 2003) ("Because materiality is not an essential element of § 1014, it would be nonsensical for us to require the Government to nonetheless prove that the financial institution faced a risk of financial loss. We decline to do so."); United States v. Whaley, 786 F.2d 1229, 1232 (4th Cir. 1986) (stating that § 1014 "does not require actual reliance on the part of the lender."); United States v. Shaid, 730 F.2d 225, 232 (5th Cir. 1984) (explaining that § 1014 requires "neither reliance by the bank officers nor an actual defrauding."); United States v. Durey, 715 F.2d 352, 353 (7th Cir. 1983) ("Actual reliance by the savings and loan on a defendant's false statements is not necessary for a conviction under § 1014."); United States v. Whitman, 665 F.2d 313, 318 (10th Cir. 1981) (observing that "actual reliance need not be proved by the Government in a section 1014 prosecution."); United States v. Sabatino, 485 F.2d 540, 544 (2d Cir. 1973) (explaining that prosecution did not need to prove bank reliance under § 1014).

233. United States v. Davis, 752 F.2d 963, 969 (5th Cir. 1985) (quoting United States v. Bowman, 783 F.2d 1192, 1199 (5th Cir. 1986)).

234. United States v. Lane, 323 F.3d 568, 583 (7th Cir. 2003).

235. United States v. Grant, 211 F. App'x 889, 893 (11th Cir. 2006) ("We focus on the defendant's conduct-not whether the bank was aware or unaware of that conduct.").

236. For discussion on the distinction between the concepts of *mens rea* and scienter, *see* Jennifer Kulynych, *Intent to Deceive: Mental State and Scienter in the New Uniform Federal Definition of Scientific Misconduct*, 1998 STAN. TECH. L. REV. 2, 40 (1998) (explaining that these two terms "were once used interchangeably, as labels for a morally blameworthy state of mind," but that "[t]oday, scienter retains its connotation as a synonym for criminal intent, but mens rea (or the term 'mental state') is often used in a broader sense, to describe the various levels of awareness that a defendant may have of the facts and circumstances of an offense"). Unfortunately, both Congress and state legislatures often fail to make matters regarding scienter or *mens rea* sufficiently clear. *See* Eric A. Johnson, *Rethinking the Presumption of Mens Rea*, 47 WAKE FOREST L. REV. 769,

Prosecutions under § 1014 require both: (1) a false statement;[237] and (2) the defendant's knowledge of falsity.[238] Thus, courts have held that there is no criminal liability under § 1014 for true statements,[239] or mere omissions.[240] Moreover, the knowledge of falsity requirement seems to foreclose the possibility of a prosecution under § 1014 for mere negligence.

Furthermore, in addition to knowing falsity, the defendant in a § 1014 case must act with a very specific purpose: influencing a statutorily prescribed entity.[241]

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770 (2012) ("Legislatures routinely fail to identify the culpable mental states associated with particular objective elements of crimes."); Dan M. Kahan, *Is Chevron Relevant to Federal Criminal Law?*, 110 HARV. L. REV. 469, 477 (1996) ("Congress is notoriously careless about defining the mental state element of criminal offenses.").

237. An action alone, without any statement, cannot give rise to criminal liability under § 1014. The classic case of an action without a statement would be merely depositing a bad check. In Williams v. United States, 458 U.S. 279 (1982), the Supreme Court explained that although the petitioner "deposited several checks that were not supported by sufficient funds, that course of conduct did not involve the making of a 'false statement,' for a simple reason: technically speaking, a check is not a factual assertion at all, and therefore cannot be characterized as 'true' or 'false.'" *Id.* at 284. The Courts of Appeals, however, have effectively limited the application of the Court's *Williams* decision, in a series of cases in which the defendant made misrepresentations in addition to passing a bad check. *See, e.g.*, Elliott v. United States, 332 F.3d 753, 762 (4th Cir. 2003) ("There is a fundamental difference, however, between checks drawn on an account containing insufficient funds, on the one hand, and affirmative misrepresentations made on the check itself, on the other."); United States v. Hord, 6 F.3d 276, 286 (5th Cir. 1993) (holding that the defendant's "use of forged signatures, false drawee bank and payee information, and inaccurate routing and account information on the checks he deposited, constituted 'false statements' under § 1014).

238. *See* United States v. Watts, 72 F. Supp. 2d 106, 109 (E.D.N.Y. 1999) ("In a false statement prosecution under § 1014, the government must prove beyond a reasonable doubt, as an essential element of the offense, that the statement at issue was false and that the defendant knew the statement to be false at the time it was made."); *see also* United States v. Colon-Rodriguez, 696 F.3d 102, 104–05 (1st Cir. 2012) (stating that § 1014 requires proof that "the defendant acted knowingly.") (quoting United States v. Alfonzo–Reyes, 592 F.3d 280, 291 (1st Cir. 2010) (internal quote marks omitted); United States v. Hill, 643 F.3d 807, 857 (11th Cir. 2011) (stating that § 1014 requires the government show that "the defendant knowingly made a false statement or report."); United States v. Fontenot, 665 F.3d 640, 644–45 (5th Cir. 2011) (stating that § 1014 requires proof that "the defendant knowingly and willfully made a false statement to the bank," and that "defendant knew that the statement was false when he made it.") (quoting United States v. Sandlin, 589 F.3d 749, 753 (5th Cir. 2009)) (internal quotation marks omitted).

239. *See* United States v. Miller, 734 F.3d 530, 543 (6th Cir. 2013) (reversing 18 U.S.C. § 1014 conviction because government failed to prove that the defendant had made an actual false statement).

240. *See* United States v. Kurlemann, 736 F.3d 439, 445 (6th Cir. 2013) ("Whether made orally or offered through a written report, a 'false statement' must be that—a statement, a 'factual assertion' capable of confirmation or contradiction. An omission, concealment or the silent part of a half-truth, is not an assertion. Quite the opposite. Omissions are failures to speak.") (citing Williams v. United States, 458 U.S. 279, 284 (1982)). But see Villa, *supra* note 88, § 4:5, at 206 (explaining that some "courts . . . have recognized that an omission of information on a loan application form 'where an honest statement would otherwise be made' may also constitute a false statement") (quoting United States v. Wells, 63 F. 3d 745, 752 (8th Cir. 1995), judgment vacated on other grounds, 519 U.S. 482 (1997)).

241. *See* 18 U.S.C. § 1014 (listing covered entities). The lender's knowledge in a § 1014 case is of no import. *See, e.g.*, United States v. Khounthavong, No. CR 13-904-R, 2015 WL 300481, at *2 (C.D. Cal. Jan. 21, 2015) ("It is irrelevant whether the lenders should have or could have taken additional steps or required additional information before funding the loans. It is equally irrelevant that the lender may have been aware that loan documents submitted by defendants were false.").

A defendant who does not have or cannot form such a purpose cannot be prosecuted under § 1014.[242]

The federal wire and mail fraud statutes also have scienter or *mens rea* requirements. Courts have held that mail and wire fraud are both specific intent crimes,[243] requiring proof of an intent to defraud.[244] The Fourth Circuit explains:

> [T]he mail fraud and wire fraud statutes have as an element the specific intent to deprive one of something of value through a misrepresentation or other similar dishonest method, which indeed would cause him harm. In this way [the defendant] is correct to assume that to convict a person of defrauding another, more must be shown than simply an intent to lie to the victim or to make a false statement to him.[245]

Issues of proof aside,[246] the wire and mail fraud statutes' specific intent requirements arguably mean that "[a] defendant has a complete defense if he believes the deceptive statements or promises to be true or otherwise acts in good faith,"[247]

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242. A fascinating federal appellate case from the 1970s illustrates this point regarding the mental capacity to form purpose. The Ninth Circuit, in an opinion written by then Circuit Judge Anthony Kennedy, held that the district court erred in preventing the defendant from introducing evidence—specifically medical testimony regarding brain scans—to demonstrate that he was incapable of forming the intent necessary to violate 18 U.S.C. § 1014. *See* Jason P. Kerkmans & Lyn M. Gaudet, Daubert *on the Brain: How New Mexico's* Daubert *Standard Should Inform Its Handling of Neuroimaging Evidence*, 46 N.M. L. REV. 383, 403 (2016) (citing United States v. Erskine, 588 F.2d 721 (9th Cir. 1978)). Kennedy explained that the defendant's theory was that he was "incapable of acting with an intent to influence the bank," *Erskine*, 588 F.2d at 723, which presumably would "require testimony concerning the defendant's incapacity to act for a specific purpose or to comprehend a causal connection between the information he submitted to the bank and its decision to lend him money." *Id.* Putting aside whether the expert was qualified to make such a judgment in that case, the Ninth Circuit held that "the defendant was entitled to introduce competent evidence pertaining to the defense of lack of specific intent." *Id.* As Kennedy explained: "While the competence and persuasiveness of the offered testimony can be questioned, the relevance of the subject matter cannot be." *Id.*

243. *See* Stephen F. Smith, *Proportional Mens Rea*, 46 AM. CRIM. L. REV. 127, 133 (2009) ("Generally speaking, crimes of specific intent prohibit conduct only when engaged in for some specified bad purpose or objective."). For an exploration of the meaning of specific intent, *see* Eric A. Johnson, *Understanding General and Specific Intent: Eight Things I Know for Sure*, 13 OHIO ST. J. CRIM. L. 521, 522 (2016).

244. *See* United States v. Phipps, 595 F.3d 243, 245–46 (5th Cir. 2010) ("Mail and wire fraud are both specific intent crimes that require the Government to prove that a defendant knew the scheme involved false representations."); *see also* United States v. Britton, 289 F.3d 976, 981 (7th Cir. 2002) (explaining, in mail fraud case, that "[i]ntent to defraud requires a willful act by the defendant with the specific intent to deceive or cheat, usually for the purpose of getting financial gain for one's self or causing financial loss to another") (citing United States v. Davuluri, 239 F.3d 902, 906 (7th Cir. 2001)); *see also* United States v. Howard, 619 F.3d 723, 727 (7th Cir. 2010).

245. United States v. Wynn, 684 F.3d 473, 478 (4th Cir. 2012).

246. Obviously, proving a defendant's intent to defraud is tricky. *See* Buell, *What is Securities Fraud, supra* note 166, at 532 (discussing the "nearly unavoidable evidentiary problem" raised in fraud cases related to the defendant's awareness). Thus, the Eleventh Circuit stated, in a wire fraud case, that "a jury may infer the 'intent to defraud' from the defendant's conduct and circumstantial evidence. Evidence that the defendant profited from a fraud may also provide circumstantial evidence of the intent to participate in that fraud." United States v. Machado, 886 F.3d 1070, 1083 (11th Cir. 2018).

247. *See* Charles Doyle, *Mail and Wire Fraud: A Brief Overview of Federal Criminal Law*, CONG. RESEARCH SERV., at p. 5 (July 21, 2011) (citing United States v. Coughlin, 610 F.3d 89, 98 (D.C. Cir. 2010); *see also* United States v. Maxwell, 579 F.3d 1282, 1301 (11th Cir. 2009)).

though the defendant may not be entitled to a specific "good faith" jury instruction.[248] In addition, it would seem that mere negligence cannot support a conviction for wire or mail fraud, though recklessness might suffice.[249]

Scienter or *mens rea* standards under the federal bank fraud statute are more complicated than the requirements under the wire and mail fraud statutes. Some of this complexity is due to the fact that the bank fraud statute, 18 U.S.C. § 1344,[250] has two different, though overlapping[251] paths to criminal liability.[252] The government in a § 1344(1) case must show that the defendant: (1) acted knowingly;[253] and (2) had the requisite intent to defraud a bank or financial institution.[254] A classic mortgage origination fraud scheme in which a borrower knowingly lies about material facts on the borrower's loan application in order to receive mortgage funding from a bank would fall squarely within the ambit of § 1344(1).[255] For

248. *See* United States v. Kismat, 570 F. App'x 155, 158 (3d Cir. 2014) (explaining in bank and wire fraud case that "[a]cting 'with the intention or the purpose to deceive or to cheat' is incompatible with acting in good faith, and thus it was unnecessary for the district court to give an additional good faith instruction").

249. *See* United States v. Kennedy, 714 F.3d 951, 958 (6th Cir. 2013) (proving the defendant's reckless disregard of the truth was sufficient to sustain convictions for mail and wire fraud) (citing United States v. DeSantis, 134 F.3d 760, 764 (6th Cir.1998)); *see also* Buell, *What Is Securities Fraud, supra* note 166, at 558 (collecting mail and wire fraud recklessness cases). Buell questions whether recklessness ought to suffice in mail and wire fraud cases. *See id.* (citing "a long line of [securities fraud] cases interpreting the federal mail, wire, and bank fraud statutes that—alarmingly . . . hold that recklessness can 'establish' the specific intent to defraud").

250. 18 U.S.C. § 1344. The full text is as follows:

> Whoever knowingly executes, or attempts to execute, a scheme or artifice—
>
> (1) to defraud a financial institution; or
>
> (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises;
>
> shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.

Id.

251. Shaw v. United States, 137 S. Ct. 462, 468 (2016) (explaining that the two sections of § 1344 "overlap substantially but not completely").

252. Prior to the Supreme Court's decision in Loughrin v. United States, 134 S. Ct. 2384 (2014), courts did not always distinguish between cases brought under § 1344(1) and § 1344(2). *See* United States v. O'Donnell, 840 F.3d 15, 18 n. 1 (1st Cir. 2016) (explaining that "prior cases did not always distinguish between the two subsections of the statute in the way that *Loughrin* now requires").

253. *See* United States v. Rizk, 660 F.3d 1125, 1135 (9th Cir. 2011) (stating that 18 U.S.C. § 1344(1) requires proof that "the defendant knowingly executed or attempted to execute a scheme to defraud a financial institution") (quoting United States v. Warshak, 631 F.3d 266, 312 (6th Cir. 2010)); *see also* United States v. Musselwhite, 709 F. App'x 958, 976 (11th Cir. 2017) ("A conviction for bank fraud under 18 U.S.C. § 1344 requires proof beyond a reasonable doubt that . . . the defendant acted knowingly.").

254. *See Loughrin*, 134 S. Ct. at 2389–90 ("That is because the *first* clause of § 1344, as all agree, includes the requirement that a defendant intend to 'defraud a financial institution"; indeed, that is § 1344(1)'s whole sum and substance."); *see also* United States v. Rizk, 660 F.3d 1125, 1135 (9th Cir. 2011) (18 U.S.C. § 1344(1) requires proof that the defendant took the proscribed actions "with the intent to defraud"). I am using the terms bank and financial institution synonymously here. *See* 18 U.S.C. § 20 (defining financial institution).

255. 18 U.S.C. § 1344(2).

cases brought under § 1344(2),[256] the government needs to prove that the (1) defendant intended to obtain bank property[257] and (2) the obtaining of bank property occurred "by means of false or fraudulent pretenses, representations, or promises."[258] Although § 1344(2) requires an intent to obtain bank property, *Loughrin* held that § 1344(2) does not require that the defendant specifically intended to defraud a bank.[259] This means that § 1344(2) also covers situations where the fraudster engages in deception to obtain bank property within a third party's control.[260] In sum, just as with wire fraud, mail fraud, and § 1014 cases, bank fraud liability under § 1344 requires some proof of the defendant's mental state.[261]

V. SCHOLARLY AND NORMATIVE IMPLICATIONS

Thus far, this Article has discussed the key role that mortgage fraud played in the financial crisis and reviewed many of the key legal principles regarding four of the federal criminal statutes most often used to prosecute mortgage origination fraud. This Part goes beyond this important economic history and federal criminal law doctrine to address three concrete, practical implications for scholars and policymakers. First, there is substantial tension between the FBI's influential mortgage fraud definition and the doctrinal requirements of four of the federal criminal statutes most often used to punish mortgage origination fraud. Second, there is unfortunate confusion between mortgage origination fraud and other forms of financial wrongdoing such as securities fraud involving mortgage backed securities and mortgage rescue frauds. Keeping these categories distinct is best for making policy on how to regulate the mortgage market. Third, scholars doing valuable empirical and quantitative work on real estate finance should be careful about distinguishing between the presence and quantifiable effects of widespread factual misstatements and inaccuracies in mortgage applications and criminal fraud in the mortgage market.

Not all falsehoods are fraud. In the context of a discussion of securities fraud, Professor Buell explains:

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256. 18 U.S.C. § 1344(2) (making it a crime to knowingly execute or attempt to execute a scheme or artifice "to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises").

257. *Loughrin*, 134 S. Ct. at 2389.

258. *Id.*

259. *Id.* at 2387; *see also id.* at 2389 (explaining that § 1344(2) "covers property 'owned by' the bank but in someone else's custody and control (say, a home that the bank entrusted to a real estate company after foreclosure)").

260. *Id.* at 2389.

261. In *Loughrin*, Justice Alito criticized the majority for dicta that, in his estimation, confused the bank fraud statute's *mens rea* standard. *See Loughrin*, 134 S. Ct. at 2397–98 (Alito, J., concurring). Specifically, Justice Alito asserted that "[t]he majority reads the word 'knowingly' out of the statute." *Id.* at 2398. It is not clear how the lower courts will read the part of the Supreme Court's *Loughrin* opinion to which Justice Alito is referring, though it seems hard to argue with Justice Alito's basic point that the introductory "knowingly" language in § 1344 applies to both § 1344(1) and § 1344(2).

> Fraud is among the most serious, costly, stigmatizing, and punitive forms of liability imposed on actors in modern corporations and financial markets. Its reach extends across all state and federal jurisdictions, over virtually all forms of civil and criminal sanctions, and into nearly every realm of financial engineering and economic exchange. If the legal system cannot be clear on what fraud is, then policymakers and the general public are not likely to get very far in understanding what of legal significance has happened when something goes wrong in the markets, much less in knowing what to do about it.[262]

Buell's point applies with equal force here. As a normative matter, policymakers cannot decide how to regulate or eliminate mortgage fraud if they are unclear as to what the concept of mortgage fraud entails. Given this confusion, it is not surprising that there is a striking dearth of scholarship that has addressed the normative questions of whether, why, and when mortgage loan borrowers who make misrepresentations are deserving of criminal punishment rather than just civil liability.[263] To figure out when and how to punish morally culpable borrowers, lenders, and brokers, clearly delineating what conduct is "fraudulent" is vital.

Table 1: FBI Definition of Mortgage Fraud v. Federal Criminal Mortgage Fraud Statutes

Element	FBI Mortgage Fraud Definition (2011)	18 U.S.C. § 1014 (False Statements to Lenders Statute)	Federal Wire, Mail, and Bank Fraud Statutes
Materiality	Required.	Not required, but statement must be made for the purpose of influencing the lender.	Required.
Scienter/ Intent	Not mentioned.	Required.	Required.
Reliance	Required.	Not required.	Not required.

262. Buell, *What is Securities Fraud, supra* note 166, at 521–22 (footnote omitted).

263. *See* Buell, *What is Securities Fraud, supra* note 166, at 566 ("[T]he lack of conceptual distinctions between civil and criminal fraud has produced hazy doctrine on mental state. Criminal sanctions for securities fraud should be reserved for those who deserve the most blame and for those whose conduct calls for the most strongly deterrent of sanctions.").

A. *The FBI's Problematic Mortgage Fraud Definition*

For many years, the DOJ and the FBI have promoted and published an influential and oft-cited definition of mortgage fraud that conflicts with the text of, and Supreme Court doctrine on, at least four key federal criminal statutes.[264] If this Article makes any contribution to the scholarly and public policy literature on mortgage fraud, it is to urge scholars and policymakers either to avoid using the FBI's definition of mortgage fraud altogether or, at the very least, acknowledge that the FBI's definition does not accurately represent the elements of four of the federal criminal laws used most often to punish false statements to mortgage lenders. The following table is a useful tool for comparing the FBI mortgage fraud definition to the four federal criminal statutes discussed in this Article.

The table highlights the major problems with the FBI's definition of mortgage fraud. First, and most important, the FBI definition includes reliance, which is inconsistent with unwavering judicial doctrine on financial frauds.[265] The federal courts have made clear in a variety of factual contexts that proof of reliance or damages is not required for cases brought under either § 1014 or the federal bank, wire, and mail fraud statutes.[266] Moreover, the Supreme Court has evidenced no tendency towards relaxing its anti-reliance stance. If anything, during the past ten years, the Court has demonstrated a willingness to expand its core reliance holdings to a variety of novel contexts.[267]

Second, the FBI mortgage fraud definition makes no mention of the defendant's mental state.[268] In contrast, the federal bank, wire, mail, and fraud statutes, as well as § 1014, all have some required scienter or *mens rea* requirements.[269] This omission raises the question of whether the FBI's mortgage fraud concept even includes negligent misrepresentations.

Using the terms employed by a Professor Sam Buell, one must be careful to distinguish cases involving "core fraud" from cases involving mere misrepresentation: "Core frauds require everything needed to establish a misrepresentation, plus something more that, in general, is highly significant in law: the actor's level of

264. *See supra* note 187 and accompanying text (discussing 2011 FBI mortgage fraud definition).

265. I am discussing federal law here; under some state statutes, reliance is an element of the crime of mortgage fraud. *See, e.g.*, Barrios v. State, 75 So. 3d 374, 376 (Fla. Dist. Ct. App. 2011) ("A conviction for mortgage fraud will be vacated where there is no proof of reliance on the misrepresentation by the victim."); *see also* Pizzo v. State, 910 So. 2d 287, 293 (Fla. Dist. Ct. App. 2005) ("The victim's reliance on the fraudulent or false representation is also an essential element of the crime of mortgage fraud.").

266. *See supra* Part IV. B.

267. *See supra* notes 229–33 and accompanying text.

268. *See* Elonis v. United States, 135 S. Ct. 2001, 2009 (2015) ("The 'central thought' is that a defendant must be 'blameworthy in mind' before he can be found guilty, a concept courts have expressed over time through various terms such as mens rea, scienter, malice aforethought, guilty knowledge, and the like.") (quoting Morissette v. United States, 342 U.S. 246, 252 (1952)).

269. *See supra* Part IV.C.

mental state, fault, culpability, or moral blameworthiness."[270] If the FBI's notion of mortgage fraud is consciously situated outside of "core fraud," then the official understanding of "mortgage fraud" promulgated by the federal criminal law enforcement establishment differs from any idea of mortgage origination fraud derived from the federal bank, wire, mail, and fraud statutes and § 1014. In any case, putting aside the FBI definition, if mortgage fraud as a socio-legal concept is distinct in terms of scienter from the four federal statutes used most often to prosecute mortgage origination fraud, scholars should make this clear in their work.

Third, the FBI's definition of mortgage fraud includes materiality. As discussed earlier, the Supreme Court made clear in *Wells* that § 1014 does not technically require proof of materiality.[271] On the other hand, the government must prove materiality in bank, wire, and mail fraud cases.[272] If the FBI's meaning of mortgage fraud lines up with the elements of these particular federal offenses, then materiality is an element of mortgage fraud and the FBI's definition is correct.[273] Furthermore, even though § 1014 technically does not require proof of materiality, its statutory standard comes rather close to a materiality standard.[274] Thus, it is not unreasonable for the FBI definition to include materiality.

Given judicial doctrine regarding reliance, mental states, and materiality, a more accurate definition of mortgage fraud would be:

> As a federal crime, mortgage origination fraud entails a defendant's intentional misrepresentation of fact related to a mortgage loan application, with knowledge of falsity, that is either: (1) material; or (2) made to influence the lender's decision to extend credit. Neither proof of reliance, nor actual damages are required elements of mortgage origination fraud.

B. *Non-Origination Mortgage Fraud?*

Journalists, lawmakers, and scholars should be aware that some authors use the term "mortgage fraud" to cover not only mortgage origination fraud, but also other forms of financial wrongdoing related to the mortgage market.[275] Most important,

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270. Buell, *What is Securities Fraud, supra* note 166, at 529. *Id.* at 530 ("[A] basic structural difference exists between the idea of core fraud . . . and the idea of misrepresentation. . . . Core fraud is necessarily a goal-oriented behavior. Misrepresentation need not be.").

271. *See supra* notes 218–25 and accompanying text.

272. *See supra* Part IV.A.

273. Some state mortgage fraud laws also require proof of materiality. *See, e.g.*, Shew v. Horvath, No. 8:16-CV-766-T-33JSS, 2017 WL 1399797, at *10 (M.D. Fla. Apr. 19, 2017), ("The mortgage fraud statute criminalizes only material misstatements made during the mortgage lending process.") (citing FLA. STAT. § 817.545(2)(a) (2018)), *aff'd*, 712 F. App'x 949 (11th Cir. 2017)).

274. *See* Sampathkumar v. Holder, 573 F. App'x 55, 57–58 (2d Cir. 2014) ("To be sure, materiality is not an element of the offense punished by § 1014 . . . . But the specific intent required by the statute—that is, the intent to influence the bank—approaches a materiality requirement.") *cert. denied sub. nom.* Sampathkumar v. Lynch, 135 S. Ct. 2919 (2015).

275. *See, e.g.*, Linda S. Finley, *What's Fraud Got to Do With It? Seeking Civil Relief in Residential Mortgage Fraud Cases, in* MORTGAGE AND FINANCE FRAUD LITIGATION STRATEGIES: LEADING LAWYERS ON MANAGING

"[s]ome observers use the term 'mortgage fraud' to include mortgage-backed securities fraud, which involves wrongdoing related to the packaging, selling, and valuing of residential and commercial mortgage-backed securities."[276]

As an example, a recent law review article discusses the district court's opinion in *Federal Housing Finance Agency v. Nomura Holding America, Inc.*[277] The author explains that the Federal Housing Finance Agency ("FHFA"), "a little-known federal agency that acts as a conservator for Freddie Mac and Fannie Mae," sued "eighteen banks for alleged *mortgage fraud*."[278] Although J.S. Nelson's article addresses a matter of great import, a close reading of the article, as well as the district court and circuit court opinions,[279] makes clear that the *Nomura* lawsuit involved litigation over what is more commonly referred to as securities fraud. To be sure, mortgages were involved in the *Nomura* case: the securities at issue in *Nomura* were mortgage-backed securities.[280] But the FHFA's fraud allegations were based upon the defendant financial institutions' misrepresentations in the sale of these MBS to investors, not misrepresentations by the initial homebuyers or mortgage borrowers to their lenders.[281] Thus, the claims in *Nomura* were made under 1933 Securities Act and state blue sky laws.[282] The same was true in many other MBS fraud cases brought in the wake of the Great Recession.[283]

THE COMPLEXITIES OF FRAUD CASES, UNDERSTANDING GOVERNMENT REGULATIONS, AND STRUCTURING AN EFFECTIVE LITIGATION PLAN 1 (2014), available on Westlaw, 2014 WL 3725822, at *1 (arguing that "the media, consumers, consumer advocates, and even mortgage industry members often confuse or intermingle" the terms mortgage fraud and predatory lending "to the extent that the original definition of mortgage fraud becomes muddled").

276. *See* DOJ MORTGAGE FRAUD AUDIT, *supra* note 73, at 2 (explaining that "the FBI considers this type of misconduct to be a form of securities fraud and not mortgage fraud").

277. Fed. Hous. Fin. Agency v. Nomura Holding Am., Inc., 104 F. Supp. 3d 441, 466 (S.D.N.Y. 2015), *aff'd*, 873 F.3d 85 (2d Cir. 2017), *cert. denied*, 138 S.Ct. 2679 (2018).

278. Nelson, *supra* note 7, at 902 (emphasis added and citation omitted). Nelson states that sixteen of the eighteen banks settled out of court, while only two banks went to trial: Nomura Holdings of Japan and the Royal Bank of Scotland (RBS). *Id.* (citing Peter Eavis, *Judge's Ruling Against 2 Banks Finds Misconduct in '08 Crash*, N.Y. TIMES (May 11, 2015), http://www.nytimes.com/2015/05/12/business/dealbook/nomura-found-liable-in-us-mortgage-suit-tied-to-financial-crisis.html [https://perma.cc/68KN-Q4VD]).

279. The ultimate district court opinion in *Nomura* ran nearly 160 printed pages, and the Second Circuit's opinion was almost 80 pages long itself. *See* Fed. Hous. Fin. Agency v. Nomura Holding Am., Inc., 104 F. Supp. 3d 441, 466 (S.D.N.Y. 2015), *aff'd*, 873 F.3d 85 (2d Cir. 2017), *cert. denied*, 138 S. Ct. 2679 (2018).

280. Federal Housing Finance Agency v. Nomura Holding America, Inc., 873 F.3d 85, 100–06 (2d Cir. 2017) (describing the transactions involved).

281. *Nomura*, 873 F. 3d at 97 (explaining that the FHFA brought actions against financial institutions that sold private-label securitizations to government sponsored entities, "alleging that the offering documents used in those transactions overstated the reliability of the loans backing the securitizations, in violation of the Securities Act and analogous provisions of certain 'Blue Sky laws.'").

282. In the *Nomura* case, the FHFA alleged that the defendants were "liable under Sections 12(a)(2) and 15 of the Securities Act of 1933. . . and parallel provisions of the District of Columbia's and Virginia's Blue Sky laws." *Nomura*, 104 F. Supp. 3d at 454; *Nomura*, 873 F.3d at 97 (explaining that the district court "found that Defendants violated Sections 12(a)(2) and 15 of the Securities Act. . . and analogous provisions of the Virginia and D.C. Blue Sky laws") (citations omitted).

283. *See* Penny Shane, *The Present and Future of Securities Litigation*, *in* NEW DEVELOPMENTS IN SECURITIES LITIGATION: LEADING LAWYERS ON ADAPTING TO TRENDS IN SECURITIES LITIGATION AND

Admittedly, neither J.S. Nelson nor any other commentator would be technically wrong to refer to securities fraud involving MBS as "mortgage fraud." After all, if this Article has demonstrated anything, the latter term is not a well-defined legal concept. Nevertheless, the scholarly and policymaking discourse on financial crime would benefit from drawing a clear line between crimes involving mortgage loan applications and fraud related to the sales of mortgage-backed securities to investors.[284] Treating these two forms of fraud distinctly does not mean that both are not important forms of criminal conduct that warrant scholarly, legislative, and law enforcement attention. Such separation also does not mean that we are ignoring the well-documented, connected roles that both forms of fraud played in the Great Recession. Still, discussions of financial crimes raise complex issues regarding the required elements of particular offenses (especially related to materiality, reliance, damages, and scienter), the allocation of limited law enforcement resources to combat white collar crime, and possibly even the perils of over-criminalization.[285] With so many policy-making and doctrinal issues on the table, grouping mortgage origination fraud in with securities fraud involving mortgage-backed securities confuses more than it clarifies.

For the same reason, it can be unwise to lump in mortgage or foreclosure rescue frauds,[286] such as the type that the federal government battled in the Distressed Homeowner Initiative,[287] along with mortgage origination fraud.[288] Nevertheless, fraud in the mortgage application process by borrowers and brokers, among others, presents profoundly different legal and policymaking issues than scams aimed at

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REGULATORY ENFORCEMENT 129, 131 (2014) ("The 2007 housing crisis generated a wave of securities litigation related to real estate mortgage-backed securities (RMBS) against entities involved in assembling or selling these instruments."); *see also* Fligstein & Roehrkasse, *supra* note 47, at 621 ("In the mortgage securitization industry, securities fraud usually takes the form of misleading securities buyers about the quality or composition of the mortgage assets underlying MBS.").

284. *See* Totten, *supra* note 13, at 1654 (separating out the following "seven deadly sins"—"predatory lending; discriminatory lending; mortgage fraud; mortgage rescue fraud; abuses in servicing and foreclosure; fraud in the creation, packaging, and sale of RMBS; and fraud by the credit rating agencies") (footnotes omitted). An ideal level of separation and clarity can be found in Nguyen & Pontell, *supra* note 26, which specifically refers to mortgage origination fraud, even in the article title.

285. *See* Todd Haugh, *Overcriminalization's New Harm Paradigm*, 68 VAND. L. REV. 1191, 1194 (2015) ("Definitions vary, but overcriminalization can be described as the proliferation of criminal statutes and overlapping regulations that impose harsh penalties for unremarkable conduct (i.e., conduct that should be governed by civil statute or no statute at all).") (footnote omitted).

286. Zachary E. Davies, Comment, *Rescuing the Rescued: Stemming the Tide of Foreclosure Rescue Scams in Washington*, 31 SEATTLE U. L. REV. 353, 355–57 (2008) (describing foreclosure rescue scams); *see, e.g.*, Stowell, Pacini, Schmidt & Keller, *supra* note 183, at 228 ("Foreclosure rescue schemes involve con artists seeking out homeowners who have fallen behind on their mortgage payments and are facing possible foreclosure."); Nicole Scott, *Turning Restitution Upside-Down: The Mortgage Fraud Restitution Formula Amidst Volatile Housing Prices*, 14 NEV. L.J. 640, 643 (2014) ("Criminals promise to 'stop or delay the foreclosure process,' and, in return, homeowners sign over their property to the criminals.").

287. *See supra* note 154 and accompanying text.

288. *See* Davies, *supra* note 286, at 355–57 (referring to foreclosure rescue scams as "a type of mortgage fraud"); Stowell, Pacini, Schmidt & Keller, *supra* note 182, at 233 (identifying loan modification schemes as a type of mortgage fraud); *Id.* at 227 (identifying foreclosure rescue as a type of mortgage fraud scheme).

homeowners, who already have mortgages, that find themselves at peril of losing their homes.[289] Thus, using the term "mortgage fraud" for both forms of fraud is less than ideal.

In sum, this Article's treatment of mortgage fraud as mortgage origination fraud does not mean that other socially significant forms of financial fraud are not equally deserving of scholarly attention and law enforcement investigation. Rather, the only aim here is clarity in the use of potentially confusing terms. When someone says that mortgage fraud is a problem that requires law enforcement action, others should know what they are talking about. Similarly, when social scientists do empirical work on "mortgage fraud," the academy should have a clear sense of what they are evaluating and quantifying. If one wants to argue that mortgage fraud increased dramatically just prior to the Great Recession, it is important to know whether they are talking about mortgage origination fraud, securities fraud involving mortgaged backed securities, or mortgage rescue fraud. Three different phenomena to define and quantify. Three different problems that might have different regulatory solutions. Three types of arguably malevolent actions that might be covered by different federal and state criminal laws.

C. *Fraudulent Loans?*

Scholarly research confirms that a staggering number of mortgage loan applications prior to and during the Great Recession contained misrepresentations about matters such as borrower income that would normally be considered crucial information for responsible lenders.[290] Furthermore, in recent years, social scientists have explored the important relationships between the characteristics of certain loan applications (such as reduced documentation and the presence of misrepresentations) and subsequent events such as loan default.[291] This empirical work has tremendous value for those who want to understand the role that so-called liar's loans played in the financial crisis,[292] and the perils of reduced mortgage underwriting standards.

Nevertheless, scholars and policymakers must take great care to delineate between misstatements and misrepresentations on mortgage loan applications, no matter how egregious they may be, and the socio-legal concept of fraud. In legal discourse, policing the boundaries between three very different types of claims or

289. Totten, *supra* note 13, at 1620 (stating that a typical mortgage rescue fraud scheme "involves a promise for services, an upfront fee for those services, and then a failure to deliver part or often all of the services promised").

290. *See* Black, Whitehead & Coupland, *supra* note 2, at 17 (summarizing evidence); Mian & Sufi, *supra* note 14, at 281 ("The fact that fraudulent overstatement of income was a prominent part of the mortgage credit boom is one of the most rigorously established facts in the literature.") (collecting sources).

291. *See, e.g.*, Griffin & Maturana, *supra* note 192, at 416 (concluding that apparent misrepresentation patterns in the loans studied were surprisingly similar for full and low/no documentation loans); LaCour-Little & Yang, *supra* note 23, at 541 (finding "that reduced documentation does increase the likelihood of loan default after controlling for other risk factors").

292. *See supra* note 26 and accompanying text (defining and discussing "liar's loans").

assertions is vital. First, one can make empirical statements about the prevalence of certain types of misstatements in mortgage loan applications and the effects of such misrepresentations upon financial institutions and the economy. For example, one might attempt to identify a statistically significant relationship between loan applications that contain false statements regarding the borrowers' intent to occupy the properties and subsequent loan defaults. That would be a classic empirical claim. Second, one might make doctrinal assertions regarding the required elements of mortgage fraud, or mortgage origination fraud, as a federal or state crime or civil tort. A statement that the federal bank, wire, and mail fraud statutes do not require proof of damage or reliance by the lender would fall into this category. Third, one can make normative claims regarding what types of mortgage misrepresentations, under an ideal policy, should give rise to civil or criminal liability. Thus, a scholar might argue that mortgage origination fraud should not be treated as a criminal offense at all unless the bank suffers significant financial loss. That might not be the current state of federal law, but perhaps it ought to be.

As shown above, the boundaries between different types of claims are too often fuzzy in mortgage fraud discourse; numerous articles refer to "fraudulent loans" or cite sources that contend that large numbers of loans were procured due to fraud.[293] But fraud, whether civil or criminal, has certain required elements. If liar's loans involved fraud, then we need to figure out, as a threshold matter, who lied. This is not overly legalistic, semantic nitpicking. It is not enough just to call loans that contain false statements fraudulent or liar's loans. Loans cannot commit fraud. Loans cannot have *mens rea*, knowledge of falsity, or fraudulent intent. If there is no liar or fraudster, there is no fraud. And, as this Article discusses at length, who lied in the liar's loans is an open question.[294]

Moreover, even if borrowers made misrepresentations on their loan applications, we cannot assume that they acted with the requisite mental state or *mens rea* to trigger civil or criminal liability. Finally, even if the relevant actors possessed the mental states required to prove fraud, we cannot assume that the misrepresentations were material or, in the alternative, made to influence a lender.[295]

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293. For example, Mian and Sufi's article is replete with references to fraud; even the article title, "Fraudulent Income Overstatement on Mortgage Applications During the Credit Expansion of 2002 to 2005," invokes fraud. *See* Mian & Sufi, *supra* note 33. Similarly, Griffin and Maturana make clear that they are intentionally using the word fraud instead of just misreporting: "Since the misreporting also has the profit-making motives of intent, and the facts suggest that the relevant parties had information to be sufficiently aware of the misreporting, fraud seems the more accurate, but less politically correct wording." Griffin & Maturana, *supra* note 192, at 388–89. This point is well-taken—especially in scholarship that is focused particularly on the likelihood that factual misrepresentations were made knowingly. But my argument about hesitancy about using the word fraud has little to do with political correctness or the fact that someone will be offended by the term fraud. I simply want to caution against calling a socio-legal phenomenon "fraud" without clearly explicating what the term entails and how it relates (or should relate) to federal criminal law on financial frauds.

294. *See supra* notes 31–38 and accompanying text.

295. As discussed above, materiality is not technically a required element for criminal prosecutions under 18 U.S.C. § 1014, though materiality is a required element under the bank, wire, and mail fraud statutes. *See supra* Part IV.A.

In short, legal actors must be careful not to assume that the mere existence of large numbers of loans with pervasive errors is conclusive proof of fraud—a socio-legal term that is so pregnant with distinctive meanings to lawyers (especially with respect to materiality and scienter). Frankly, using the term fraud in this context is not necessary in most cases. One can make the same rhetorical point by highlighting the deleterious impacts of pervasive misstatements on mortgage loan applications without calling the underlying behavior "fraud."[296] If one does feel compelled to use the term fraud,[297] at the very least, it is worth making clear how the term "fraud" is being used, the relationship between any utilized conception of fraud, and how the term fraud might be used in legal discourse. Thus, policymakers, journalists, and scholars from other disciplines will understand that those invoking fraud are using an understanding of mortgage fraud that is untethered to the specific elements of the types of federal criminal fraud statutes this Article addresses.

CONCLUSION

As is often the case with major historical events, scholars, policymakers, journalists, and other social observers have profound disagreements over the essential lessons that should be gleaned from the Great Recession.[298] As discussed earlier, even the Financial Crisis Inquiry Commission ended up producing dissenting opinions. It seems rather hard to dispute, however, that the Great Recession illustrates, among many other matters, the importance of mortgage fraud—however the term is defined—as a socio-legal phenomenon. It is unhealthy for the financial system and the economy as a whole when extraordinarily large numbers of borrowers or brokers knowingly or intentionally make significant misrepresentations in mortgage loan applications or misstatements to influence lenders who extend credit. The danger is especially acute when the loans originated based upon those

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296. For example, one interesting article concludes that "[p]ersonal asset misreporting by borrowers was associated with very poor outcomes for a U.S. bank making loans in the residential mortgage market during the 2004 to 2008 period." Mark J. Garmaise, *Borrower Misreporting and Loan Performance*, 70 J. FIN. 449, 479 (2015). Garmaise, however, does not assume that the borrowers engaged in fraud, nor does he refer to the loans as fraudulent.

297. *See supra* note 293 and accompanying text.

298. Andrew Lo writes, in his review of 21 books concerning the financial crisis:

> Given the complexity of the events surrounding this debacle, the best hope for arriving at a deeper understanding of financial crises and how to respond to them is through the collective intelligence of all economists, each of us laboring to develop our own interpretation that can inform and improve the consensus. Like the characters in *Rashomon*, we may never settle on a single narrative that explains all the facts; such a "super-narrative" may not even exist. But by working with a common set of facts, we have a much better chance of responding more effectively and preparing more successfully for future crises.

Lo, *supra* note 2, at 177. For those who are not familiar with the movie to which Lo is referring, "Akira Kurosawa's great film 'Rashomon' portrays a rape and a murder from four conflicting perspectives, leaving the disoriented viewer in the dark about what really happened." Christopher Benfey, *Afraid of the Dark, Afraid of the Light*, N.Y. TIMES, Oct. 14, 2018, at BR 12.

misstatements are then widely securitized and sold as financial instruments to the investing public.[299]

With this danger in mind, this Article improves the scholarly and public policy discourse on mortgage fraud in three concrete ways. First, this Article has demonstrated that the widely-cited and influential FBI definition of mortgage fraud is inconsistent in key respects with the elements of several of the federal criminal statutes most often used to punish mortgage origination fraud. Second, this Article has called for commentators to distinguish mortgage origination fraud from other forms of financial wrongdoing, including securities fraud involving mortgage backed securities and foreclosure rescue scams aimed at ripping off homeowners. These are distinct white collar crimes, which raise distinctive doctrinal and policymaking issues.

Third, and finally, this Article argues that scholars should recognize that the federal crime of mortgage origination fraud requires more than showing the existence of pervasive factual misrepresentations in mortgage loan applications to trigger criminal liability. Loan applications, as packed with falsehoods as they might be, cannot commit fraud. At the very least, fraud as a socio-legal concept requires a fraudster acting with *mens rea* or scienter. Understanding that principle is a perfect starting point for both legal and social science scholarship on mortgage application misrepresentations.

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299. *See* Quigley, *supra* note 107, at 112–13 ("Narratives of the crisis branch out differently, but they share a common root: the securitization of residential mortgages, particularly risky or 'subprime' mortgages, and the development and propagation of financial instruments the value of which depended on these mortgages."); Steven L. Schwarcz, *Securitization, Structured Finance, and Covered Bonds*, 39 J. CORP. L. 129, 130 (2013) ("The securitization of subprime mortgage loans is widely viewed as a root cause of the global financial crisis.").