Australian Citizens Party

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MEDIA RELEASE

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Royal Commission spotlights the mortgage fraud that could implode the banking system

In its first fortnight of hearings, the Banking Royal Commission drew the nation's attention to the huge problem of mortgage fraud. The hearings showed that each of the big four banks, which together control 80 per cent of banking in Australia, have engaged in fraud on a massive scale. The fraud is not confined to the margins of the home loan business, but infects the majority of mortgages, which means most borrowers can't afford their loans. The bottom line is there is nothing real propping up the Australian housing market—it is a bubble of lies, and it would only take a slight shock to burst the bubble and bring down the entire banking system.

Until now, a small number of individuals and organisations, including the Citizens Electoral Council, have been warning of this danger. The Royal Commission has forced everyone to look at it. A shocked Robert Gottliebsen fretted in the 21 March *Australian Business Review* that the extent of the fraud means the Reserve Bank shouldn't raise interest rates. "Reserve Bank Governor Philip Lowe must [be] becoming increasingly concerned at the revelations at the banking royal commission", Gottliebsen wrote. "Lowe now knows that some if not all the banks have let their credit standards slip…. The false income statements on bank loan applications are contributing to widespread mortgage stress because incomes have not been rising. If Lowe increased interest rates it would cause a lot of people to throw in the towel and sell up and if that resulted in a setback to the housing market the loan dominoes falling would cause considerable bank losses."

Analysts at giant investment bank UBS went further, warning that a possible consequence of the Royal Commission exposing the fraud could be a credit crunch—like the total breakdown in bank lending that happened in the 2008 global financial crisis. UBS analyst George Tharenou told ABC News reporter Stephen Letts on 24 March: "In this scenario there is a risk of a pick-up in arrears as existing borrowers become financially stressed, and could precipitate a broad-based credit event."

Mortgage fraud worse than reported

Mortgage fraud is a crisis, even worse than revealed in the Royal Commission. The most authoritative analysis comes from Denise Brailey of the Banking and Finance Consumers Support Association (BFCSA), who estimates that 80 per cent of all mortgages are "sub-prime" interest-only loans, of which 70 per cent of borrowers don't know they are interest-only.

Mrs Brailey is one of Australia's leading experts on bank fraud. A trained criminologist, for decades she has advocated on behalf of thousands of bank victims to save their homes. She has also testified before numerous Parliamentary inquiries.

The BFCSA has made a submission to the Royal Commission, which reveals how the fraud is perpetrated. The information comes from the thousands of cases Denise Brailey has worked through personally, and her interviews with countless victims and mortgage brokers. She explained the key elements of the fraud in a two-part interview with *The CEC Report* on 22 March. (Click here to view Part 1.)

The BFCSA submission exposes:

- The mortgage fraud is driven by the banks, not brokers. The banks employ Business Development Managers to give brokers 30 hours of minimal training, which includes encouraging the brokers to practice on their families—this has led to many brokers' family members also losing their homes due to unaffordable loans.

- The components of the "black box" of the fraud machine include the (usually) 11-page Loan Application Form, of which the borrowers only see three pages, while the balance is filled out according to banks' specifications; and the "serviceability calculator", which the banks control and brokers can only access with a password, and which ignores actual living expenses in favour of the Henderson Poverty Index that assumes all borrowers live on bread and water.

- The unaffordability of loans is hidden for the first 3-5 years by various buffer loans, including credit cards with large limits and personal overdrafts, which the borrowers use to make their initial repayments. On average, the borrower's debt increases by $150,000 in the first five years.

The need for buffers proves the loans are unaffordable. When the buffers run out, banks avert defaults by refinancing the loans.

- The banks securitise these dodgy loans, and on-sell them to investors as Residential Mortgage Backed Securities (RMBS). It is the payment stream that is securitised, but the investors wouldn't know that the payments are not coming from the incomes of the borrowers, but from extra credit from the banks—a huge Ponzi scheme at the heart of Australia's financial system.

Prepare for a crash

The shocking level of fraud in mortgage lending is a huge, immediate threat to Australia's banks and economy. The dramatic rise in house prices since 2000 has completely distorted the Australian economy, such that financial services (dominated by mortgage lending), real estate and construction are Australia's three largest economic sectors, and collectively account for more than a quarter of all economic activity. The government must face the reality, informed by the Royal Commission and the BFCSA, that mortgage fraud, and not real demand, has fuelled the extraordinary expansion of these sectors, which means it's a house of cards that could come crashing down from just a small interest rate rise, or any other event that drives up the cost of living for mortgage-stressed borrowers. A rise in defaults will crash the housing market, destroy the jobs of hundreds of thousands of construction workers, bankrupt the big banks which have made mortgages more than 60 per cent of their business, and plunge Australia into economic chaos.

The CEC calls on the government to take two actions in response to the mortgage fraud and the economic threat it has created:

1. Expand the powers and duration of the Royal Commission, so it can investigate every aspect of the criminal fraud in the system, especially the complicity of the regulators APRA and ASIC, without hindrance, and hear testimony from real experts such as Denise Brailey;

2. Implement a structural, "Glass-Steagall" separation of the banking system, which will be a firewall to protect the real economy from a banking crash, and will stop banks from the gambling in mortgage backed securities and other derivatives that has been integral to their mortgage control fraud.

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