

2007 Texas TIPS Online Mortgage Fraud

March 15, 2007

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TYPES

- Fraud for Profit
- Fraud for Housing

Fraud for Housing

- ✓ Illegal actions perpetrated solely by the borrower
- ✓ Motive is to acquire and maintain ownership of a house under false pretenses


Fraud for Profit – "Industry Insider Fraud"

- ✓ Motive is to revolve equity
 - ✓ Falsely inflate the value of the property
 - ✓ Issue loans based on fictitious properties
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COMMON ELEMENTS of Fraud for Profit

- Property Flipping
- Nominee Loans/Straw Buyers
- Inflated Appraisals
- False Repairs
- Silent Second
- Fictitious/Stolen Identity
- Marketing Fees
- Trusts (e.g. 125 Proper Street Trust; Mary Smith Trust)

Players in a Flip

- Owner (**A**)
 - Investor (may be trust) (**B**)
 - Straw Buyer (**C**)
 - Lender
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- Mortgage Broker
- Appraiser
- Title Company
- Title Insurance Underwriter

How does a
Flip work?



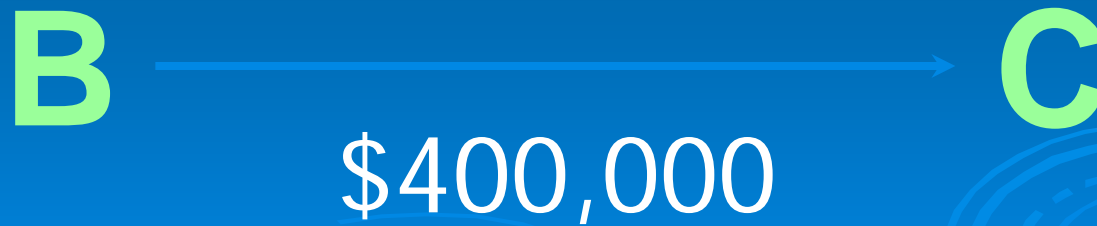
Flip



1st Contract



2nd Contract



Representations to Straw Buyer

- - Great investment
 - We do all the paperwork
 - We put the property in your name
 - We pay all the costs
 - We pay you a bonus at closing
 - We manage the property
 - We sell the property
 - We split the profits

**So What does the Straw
Buyer Contribute?**

His Credit



- **B** sends **C** to Broker
- Broker takes loan application
 - Inflates actual credit data
- Title Company sends commitment to Broker
- Broker may alter commitment to show **B** in title and omit **A**'s encumbrances
 - Broker gets inflated appraisal

- Broker sends loan application, appraisal, and commitment to Lender
- Title Company sends closing documents to Lender
- Lender funds
- Simultaneous closings
 - **A** receives actual price
 - **B** receives profit

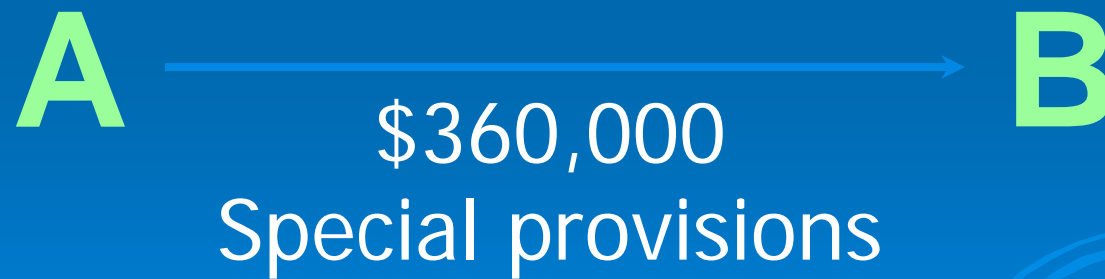
Dual Contracts and Payoffs



1st Contract



2nd Contract



Special Provisions Payments

- - Unexplained payoffs
 - Marketing Fees
 - Payoff unsecured debts
 - Payments for repairs

Foreclosure Schemes



- **A** is facing foreclosure
- **B** offers to help
- **B** convinces **A** to convey property to **B** for a year
 - **A** can rent
 - **B** will re-convey

➤ **B** then

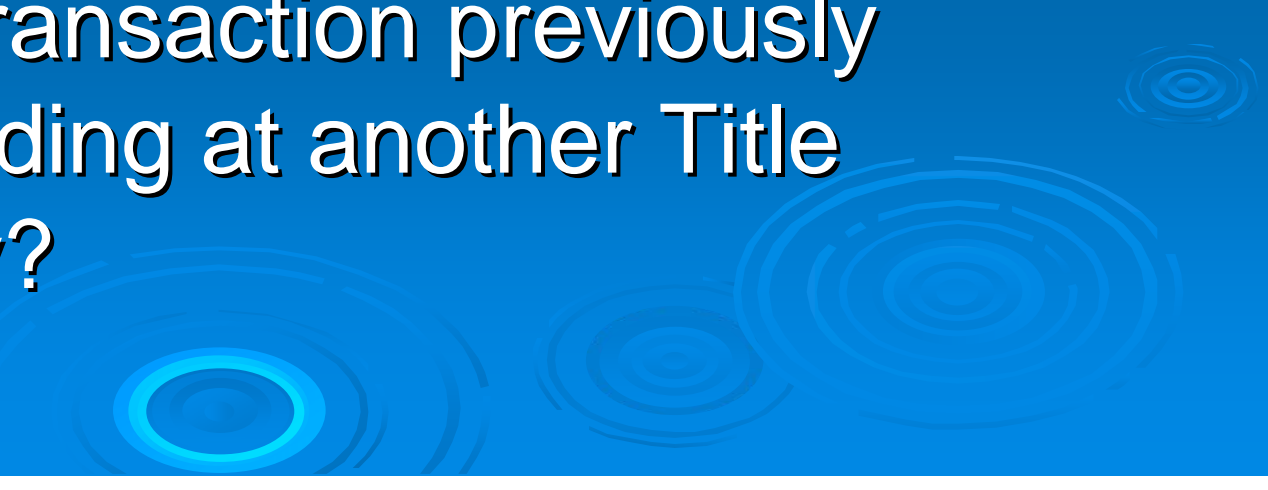
- Refinances
- Resells
- Takes equity
- Disappears

➤ Loan defaults

➤ Lender forecloses

Outside Counsel Identified Red Flags



- Is it an obvious flip?
 - No reasonable explanation for immediate increase in sales price?
 - Are there 2 contracts?
 - Has the transaction previously been pending at another Title Company?
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- Is the name of the Buyer changing after contract but before closing?
- Is the Lender changing in middle of transaction?
- Are commissions/closing costs
 - Not based on purchase price?

➤ Are you being asked

- To make disbursements not shown on settlement statement?
- To disburse Lender's funds before receipt of down payment?
- To allow Lender's funds to be used for down payment?

➤ Are you being asked

- To allow the seller to “loan” the down payment to the buyer through a “silent second”?
- To do anything inconsistent with Lender’s closing instructions?

- Do you know your customer?
- Is it a sub-prime Lender?
- Repeat buyers?
- Do buyers occupy the property?
- Frequency of transactions brought to you by **B**?

➤ Are you closing on documents

- Signed and notarized outside your presence?
- Are you being asked to notarize documents you did not witness being signed?

Attempts By The Lending Industry To Make The Title Company The “Policeman”

General Closing Instructions (some examples):

- If you know or should know of one of more of the following you must immediately contact the lender and postpone the closing:

- The property was conveyed within the previous six months (up to 18 months)
- The loan represents a increase over 25% of a previous loan in that same time period
- A full or partial transfer (except to the borrower) has occurred or will occur after the closing
- The earnest money deposit covers substantially all of the seller's profit or the down payment and may not be "real"
- Any material fact that may have an impact on the Lender's decision to make the loan.

- A fraud or scheme related to the transaction has been or may be committed
- Any party to the transaction has made a material misrepresentation or committed a falsehood
- A loan document or invoice has been tampered with, falsely generated or bears incorrect or false data, bears different names or addresses for the same parties, or bears a fictitious name
- A party's handwriting or signature is inconsistent on the loan documents
- A borrower is being paid to lend credit or his identity.

- Borrower's source of funds is different than specified in the specific closing instructions
- The mortgage broker is the same person or is owned or controlled by the same person as the Seller, Borrower, appraiser or any other interested party in the transaction
- Any interested party, except the seller, has had a prior interest in the property
- Borrower or seller appear to be coerced, under undue influence or incapable of reading or understanding the nature of the transaction

- There have been any changes to the sales price, or order or it appears the Earnest Money deposit is fictitious
- Borrower owns or occupies another residence and does not intend to occupy the property (unless the specific closing instructions identify the property as investment property)
- Any payments from the loan proceeds is ambiguous, has missing or incomplete information, lacks clear description, or appears unusual in any manner.

- If any real estate commissions are excessive for the market area
- The property tax assessment is 10% or more of the appraised value shown on the Specific Closing Instructions

Federal Criminal Liability

- Wire Fraud and Aiding and Abetting 18 USC § § 1343 and 2
- Bank Fraud and Aiding and Abetting 18 USC § § 1344 and 2
- Conspiracy to Commit to Bank and Wire Fraud

Proposed State Legislation

- To define mortgage fraud and provide liability to persons involved.
- HB 716 and HB 2204 (minor differences)
 - Amend the Business and Commerce Code to add Chapter 28 Residential Mortgage Fraud Act
 - Defines Mortgage Fraud as:

- (1) with the intent to mislead:
- (A) knowingly, and with the intent that the misstatement, misrepresentation, or omission be relied on by a mortgage lender, borrower, or other party to the mortgage lending process:
 - (i) makes a misstatement, misrepresentation, or omission during the mortgage lending process; or
 - (ii) uses or facilitates the use of a mortgage lending process document during the mortgage lending process that contains a misstatement, misrepresentation, or omission; or

- (B) files or causes to be filed with a county clerk or governmental entity a mortgage lending process document concerning residential real property, knowing that the document contains a material misstatement, misrepresentation, or omission;
- (2) derives a direct financial benefit in connection with a residential mortgage closing that the person knows resulted from conduct described by Subdivision (1); or
- (3) conspires to engage in conduct described by Subdivision (1).

- Mortgage lending process document includes:
 - A contract for sale of real property
 - loan application and supporting documents
 - appraisals
 - HUD -1 Settlement Statements
 - certificate or affidavit of fact
 - a legal instrument related to the transaction
 - any required disclosure

- HB 716 makes an offense a second degree felony (2-20 years and up to \$10,000 fine), with repeat offenses as first degree felonies (life or for any term of not more than 99 years or less than 5 years and up to \$10,000 fine).
- HB 2204 makes an offense a third degree felony (2-10 years and up to \$10,000 fine), with repeat offenses as second degree felonies, but also adds the offense to the Organized Crime enhancement in Penal Code Chapter 71)

SB 1307

- Adds Chapter 28 to Business and Commerce Code for Residential Mortgage Fraud (similar provisions to HB 716 and 2204)
- Criminal penalties depend on amount of loan involved (<\$100,000, third degree felony; \$100,000 but <\$200,000, second degree; \$200,000 and up, first degree)
- Includes enhancement for pattern of violations.
- Imposes a \$5 fee on each closing, to be used by AG to fund investigations of mortgage fraud and to pay for prosecuting attorneys.

HB 3681 and SB 1308 (companion)

- Adds sections to Finance Code (§343.105), Insurance Code (§§2651.254 , 2652.007 and 2652.154) and Occupations Code (§1103.406)
- Contains similar provisions regarding definition of residential mortgage fraud (Fin. Code)
- Contains an express liability provision
- Provides for vicarious liability of the employer or principal of anyone who commits a violation while participating in the transaction as an employee or agent.

Ins. Code §2651.254 Liability of Title Insurance Companies

- A title insurance company that issues an insured closing and settlement letter in accordance with Section 2702.001 is liable for losses incurred by any party to a real estate closing transaction resulting from residential mortgage fraud under Section 343.105, Finance Code, committed by the title insurance company's title insurance agent or its employee in the transaction for which the insured closing and settlement letter was issued.

Ins. Code §2652.007 Duty and Liability of Escrow Officers

1. Escrow Officer must close in accordance with the definition of “closing the transaction” and
 2. in compliance with all directions and instructions of the lender.
 3. May execute a lender’s closing instruction to evidence receipt of the instructions and agreement to follow (attempt to avoid P-35)
- Provides that if the escrow officer violates 1. or 2. she is liable for all losses to a lender resulting from residential mortgage fraud, committed by any party.

Ins. Code §2652.154

- An escrow officer who is an employee of a title insurance agent or direct operations is an agent for the title insurance agent or direct operations with respect to the closing of a real estate transaction

Occupations Code §1103.406

- Provides civil liability of appraisers for material inaccuracies, whether intentional, or by carelessness or negligence.

HB 3151

- Establishes a Task Force comprised of various officials, including the Commissioner of Insurance, to study “occurrences in this state of fraudulent purchases of property, including fraudulent purchases made by use of false appraisals, documents, or identities.”