

U.S. Trustee Program Initiative Combats Bankruptcy-Related Mortgage and Real Estate Fraud

Written by:

Sandra R. Klein

Acting Chief, Criminal Enforcement Unit

Over 10 million bankruptcy cases have been filed in the last decade. Although the vast majority of these cases have been filed as a last resort by individuals or entities in dire financial straits, others have been filed as part of well-orchestrated mortgage and real estate fraud schemes. As part of its role as a “watchdog”¹ over the bankruptcy system, the United States Trustee Program (“Program”) has initiated and maintained efforts to combat such fraud through its criminal enforcement efforts.

Criminal Enforcement Efforts

In keeping with its mission to protect the integrity of the bankruptcy system, the Program has a statutory duty to refer suspected criminal conduct to United States Attorneys and to assist in prosecuting bankruptcy crimes.² To carry out its mission, the Program works closely with law enforcement agencies and participates in more than 50 bankruptcy fraud and mortgage fraud working groups across the country.

After identifying mortgage and real estate fraud schemes that involve or are related to bankruptcy filings, the Program pursues civil enforcement actions and, where appropriate, makes criminal referrals to law enforcement partners such as the Federal Bureau of Investigation, Department of Housing and Urban Development Office of Inspector General, Internal Revenue Service–Criminal Investigation and Social Security Administration Office of Inspector General.

In some districts, Program attorneys are designated as Special Assistant U.S. Attorneys who assist with the prosecution of bankruptcy fraud cases, including those involving mortgage and real estate fraud. Nationwide, Program employees – whether attorneys, bankruptcy analysts or paralegals – also testify as witnesses before grand juries and during criminal trials on a number of bankruptcy-related topics. To obtain more information about the Program’s criminal enforcement efforts, please see *Criminal Referrals by the United States Trustee Program, Fiscal Year 2008*, available at http://www.usdoj.gov/ust/eo/public_affairs/reports_studies/index.htm.

¹ H.R. Rep. No. 95-595, at 4 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 5966.

² *See* 28 U.S.C. § 586(a)(3)(F).

Common Schemes

There are many different mortgage and real estate fraud schemes through which perpetrators fraudulently exploit the bankruptcy system to further their criminal endeavors. The Program has been actively involved in deterring such fraud cases, including schemes that range from the intentional failure to disclose real estate on Schedule A to more complex schemes that involve properties located and bankruptcy cases filed in numerous states across the country. Although these schemes vary in their scope and complexity, they frequently have common characteristics. Two of these schemes are described here.

Foreclosure Rescue Schemes

One form of bankruptcy-related mortgage fraud is the “foreclosure rescue” scheme. In this scheme, homeowners whose properties are in foreclosure are contacted, usually through the mail, by a “financial consultant.” The consultant fraudulently tells the homeowners that he/she will locate a lender to refinance the homeowners’ delinquent mortgage. Homeowners are instructed to make their mortgage payments to the consultant. The consultant does not, and never intends to, locate a new lender. Instead, the consultant files bankruptcy cases in the name of the homeowners, frequently without the homeowners’ knowledge or consent. This allows the consultant to stall foreclosure while continuing to collect mortgage payments from the victims.

Property Title Fraud

“Property title fraud” is another form of bankruptcy-related mortgage fraud. Although this fraud is similar to the foreclosure rescue scheme described above, there is a major difference in that the perpetrator convinces the victims to deed their properties to him/her for little or no consideration. After the perpetrator acquires title to the victims’ properties, the victims are told that the perpetrator will negotiate reduced payments or short sales with the lenders or locate other lenders to refinance their homes. The homeowners are required to pay rent to the perpetrator, who does not pay the existing mortgage or seek new financing. Fractional interests of the properties are often deeded to shell companies controlled by the perpetrator. The perpetrator then files serial bankruptcy cases in the names of the victim homeowners and/or in the names of the shell companies. This tactic complicates and delays foreclosure for months or even years, because the lenders must seek relief from the automatic stay in each bankruptcy case.

Recent Prosecutions

The following five prosecutions illustrate some of the recent mortgage and real estate-related fraud schemes that the Program has combated along with its law enforcement partners.

- In April 2009, four defendants in the District of Maryland pleaded guilty in an out-of-the-ordinary foreclosure rescue scheme. One defendant aired television commercials promising to help people facing foreclosure and eviction. Victims were invited to attend meetings and were put on the defendant’s “financial diet,” which involved not making

mortgage payments for a year and signing blank chapter 13 bankruptcy forms. Using the victims' pre-signed forms, the co-conspirators filed "bare-bones" chapter 13 petitions in the victims' names. If the victims had not pre-signed the forms, the co-conspirators created false bankruptcy documents by copying a signature from one document and electronically pasting it onto another. The victims were told that the defendant would use "his good credit" to refinance their homes temporarily, and that the homes could be repurchased in one year. During the closing, the victims learned that they would be required to pay rent to the defendant and that the rental payments would be much higher than their mortgage payments. Most of the victims defaulted, were evicted by the defendants, and lost their homes. The U.S. Trustee's Baltimore and Greenbelt offices referred these matters and worked closely with the U.S. Attorney's office on the investigation and prosecution.

- In January 2009, two individuals from Los Angeles were convicted in the District of Kansas of six counts of mail fraud, six counts of aggravated identity theft and one count of conspiracy in connection with their operation of a nationwide "foreclosure rescue" scheme. The defendants sent out more than 1,000 solicitations a day, promising homeowners that they would not have to make mortgage payments for two years. At the direction of the defendants, homeowners transferred fractionalized interests in their properties to fictitious companies and paid the defendants monthly fees ranging from \$500 to \$2,000. The defendants placed the fictitious companies in bankruptcy, thereby invoking the automatic stay to halt collection activities against the homeowners. When the victims stopped paying, the defendants stopped filing serial bankruptcy cases, the lenders foreclosed and the victims lost their properties. A Bankruptcy Analyst from the Wichita office testified during trial and provided substantial assistance during the investigation and prosecution in this case.
- In September 2008, a defendant in the Eastern District of Virginia was sentenced to 70 months in prison and ordered to pay approximately \$4 million in restitution after pleading guilty to mail fraud and bankruptcy fraud. The defendant operated a scheme in which he repeatedly conveyed two properties he owned and caused mortgage payoff checks to be diverted to mail drops that he opened. During his chapter 11 bankruptcy case, the defendant falsely testified at a hearing that he would not sell any of his property without bankruptcy court permission. In actuality, one of his properties had gone to settlement a few days before he testified. The Program's Alexandria office referred the matter and the Assistant U.S. Trustee served as a Special Assistant U.S. Attorney in the case.
- In August 2008, a defendant in the District of Arizona was sentenced to 33 months in prison and ordered to pay more than \$86,000 in restitution for engaging in a foreclosure rescue scheme in which the defendant solicited individuals who were facing foreclosure and convinced them to quit claim their properties to him, but he never recorded the quit claim deeds. Instead, he filed fraudulent bankruptcy cases in the homeowners' names without their knowledge or consent. The Program's Phoenix office referred the matter and a Bankruptcy Analyst from that office assisted in the investigation and prosecution.

- In June 2008, a defendant in the Northern District of Illinois was sentenced to 135 months in prison and ordered to pay approximately \$187,000 in restitution for making false representations that his company could stop foreclosures and eliminate homeowners' mortgage debt. The defendant told his victims that mortgage debt was illegal and that the mortgage companies would forgive the debt when faced with lawsuits filed by his company. He charged the homeowners a large retainer and monthly fees and did nothing other than file serial bankruptcy petitions to delay foreclosure. The U.S. Trustee's Chicago office referred the matter and the Regional Criminal Coordinator assisted in the prosecution as a Special Assistant U.S. Attorney.

These five prosecutions – which represent just a handful of the many cases in which the Program is involved – demonstrate that bankruptcy-related mortgage and real estate fraud schemes are a nationwide problem that the Program is working to combat.

Conclusion

By participating in working groups that target mortgage and real estate fraud, directly identifying possible criminal conduct, making referrals to U.S. Attorneys and other law enforcement agencies, and assisting in prosecutions, the United States Trustee Program weeds out mortgage and real estate fraud when it enters the bankruptcy system. The Program encourages all members of the bankruptcy community to assist the Program in this effort. To report suspected bankruptcy-related crimes, please contact your local office of the U.S. Trustee or submit a referral via the Program's Bankruptcy Fraud Internet "Hotline" at <http://www.usdoj.gov/ust/eo/fraud/index.htm>.