

# THE MORTGAGE MARKET CRISIS, PART I: MORTGAGE FORECLOSURE ‘RESCUE’ SCAMS

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Mortgage fraud and related scams have been around for years.

Recently, though, the implosion of the mortgage market and decline in the economy has led to a sharp increase in mortgage fraud litigation. According to a Mortgage Fraud Report recently issued by the FBI, reports of suspected mortgage fraud rose 31% in fiscal 2007 from 35,617 to 46,717, and more than 33,000 such reports were filed in the first half of fiscal 2008. Tarter Krinsky & Drogin’s Litigation Department has been defending individual and corporate clients in mortgage fraud and related litigation

since long before the current proliferation.

One of the most widespread and fastest growing forms of mortgage fraud involves bogus “foreclosure rescue” scams, sometimes referred to as “equity stripping.” In these scams, unscrupulous individuals or companies, who may call themselves “foreclosure rescue specialists,” approach homeowners who are being threatened with, or are already in, foreclosure (often elderly and/or low-income individuals). The “rescue specialist” offers to help the frightened homeowner save his home and repair his credit when, in fact, the homeowner ends up being tricked into selling his home for an amount that is much less than the homeowner’s equity in the home.

One typical version of the scheme is as follows: The rescue specialist convinces the homeowner to sell his house to a

buyer selected by the rescue specialist. The buyer is a straw man, recruited by the rescue specialist solely for the purpose of obtaining a mortgage loan. The rescue specialist assures the homeowner that the straw man will deed the house back to the homeowner at the end of a period of time, usually one year. Thus, the homeowner is convinced to sell his house because he is led to believe the sale to the straw man is essentially a temporary sale which is designed to give the homeowner time to repair his credit. The new mortgage loan that is taken out by the straw man is for an amount in excess of the amount owed by the homeowner on the defaulted mortgage loan. The rescue specialist gives a modest amount of the proceeds on the new loan to the homeowner — often less than \$20,000 — and pays a fee to the straw buyer and pockets the balance of the mortgage proceeds. The homeowner, who has just sold his house to the straw man, has been led to believe that he has pre-paid a year’s worth of payments on the new loan when, in reality, no payments on the new mortgage are ever made. At the end of a year, the straw man becomes the subject of a foreclosure action and the homeowner, who has been reduced to the status of tenant in his home, faces eviction. The homeowner may have had substantial equity in his home at the time the rescue specialist convinced him to sell his house. In such cases, the homeowner’s equity is “stripped” from him in exchange for the nominal sum he receives at the closing of the new loan.

This is not the only form of foreclosure rescue fraud. Variations on theme abound. For instance, in a story reported in local newspapers earlier this year, two brothers were charged with grand larceny for the theft of the home of a retired New York City corrections officer who was suffering

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from dementia. The pair was arrested after the victim's daughter – a police officer – discovered that her father's home had been sold out from under him and a \$400,000 mortgage, for which he was responsible, had replaced a prior mortgage on which he had owed only \$180,000.

The effects of the "equity stripping" go well beyond the distressed homeowner. The con artists borrow money from unsuspecting lenders, with wide-ranging impacts. In a May 2008 ruling involving a property in Brooklyn, the court rescinded a 2004 deed made by a 76-year-old woman with dementia and voided a 2005 mortgage lien securing a loan to the con artists. (The mortgage was recorded after a notice of pendency.) This ruling will have major repercussions on the lender, its title insurer and a variety of others.

In the current environment, we can expect an increased incidence of mortgage foreclosure rescue scams and related consequences. Homeowners facing difficult economic circumstances, or foreclosure, must not involve themselves with people or companies claiming to be credit repair experts

or foreclosure rescue specialists without seeking independent legal advice. Unfortunately, in difficult economic times, fraudulent scams often proliferate. The prudent homeowner will act cautiously and seek legal counsel before entering into contracts or financial transactions.

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### ***About Debra Bodian Bernstein, Counsel***

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