U.S. Department of Justice

Executive Office for United States Trustees

Office of Research and Planning *Washington, D.C.*

FACT SHEET ON FINAL REPORT OF BANKRUPTCY FORECLOSURE SCAM TASK FORCE

Bankruptcy courts, lenders, homeowners, and even “innocent bystanders” are being victimized by bankruptcy foreclosure fraud scams operating in the Los Angeles area, according to a report recently issued by a public sector-private sector task force. The report, prepared by the Bankruptcy Foreclosure Scam Task Force of the United States Bankruptcy Court for the Central District of California, identifies five different kinds of bankruptcy foreclosure scams.

The task force investigated the growing practice of filing for bankruptcy to delay or defraud creditors–-especially home lenders--without intending to comply with the requirements for obtaining a bankruptcy discharge or completing a repayment plan. The task force was created in 1996 by Geraldine Mund, Chief Bankruptcy Judge for the Central District of California, in response to a rash of cases filed solely to stall foreclosure.

“The task force report is an important assessment of one of the most extensive abuses of the bankruptcy court in Southern California,” according to Maureen Tighe, United States Trustee for the Central District of California. The United States Trustee Program is a component of the Justice Department that supervises the administration of bankruptcy cases. Tighe was appointed United States Trustee in April; she served on the task force in her former role as Deputy Chief of the Major Frauds Section of the Office of the United States Attorney for the Central District of California.

“The United States Trustee Program has been seeking fines and sanctions routinely when the operators of these foreclosure scams can be identified,” Tighe continued. “The Program has also made referrals and assisted law enforcement in numerous criminal investigations of these scams, leading to numerous indictments and convictions.”

Jerry Patchan, Director of the Executive Office for United States Trustees, added: “The task force has done fine work in illuminating a serious problem. The Executive Office recognizes the effect of these bankruptcy foreclosure scams, particularly in the Central District of California. We intend to continue working with the courts to seek effective ways to address these problems.” The Executive Office for United States Trustees, located in Washington, D.C., oversees the Program’s substantive operations and handles its administrative functions.

Five Scams Identified

Filing a bankruptcy petition automatically stays--stops for a period of time--all actions against the debtor or the debtor's property, including collection, foreclosure, and repossession. In recent years, the report states, some people in the Central District of California "have apparently created whole businesses out of the delay possibilities provided by the automatic stay." These entities often advertise as "foreclosure services" or "mortgage consultants."

The report identifies five kinds of scams:

! **The fractional interest transfer scam.** A bankruptcy debtor receives a 5 percent or 10 percent interest in property that is held by another borrower who faces foreclosure. Because the interest is then held by a bankruptcy debtor, the original borrower's creditors cannot foreclose until the bankruptcy judge lifts the automatic stay.

  One San Bernardino, Calif., homeowner facing imminent foreclosure was approached by a scam perpetrator, and agreed to sign deeds of trust and grant deeds transferring fractional interests in her property, according to the report. The homeowner paid the foreclosure consultant a few hundred dollars per month. The recipients of the fractional interests included homeless individuals and apparently fictitious people. Eight of them filed for bankruptcy one after the other. Each filing stayed foreclosure on the homeowner's home, causing a 10-month delay between the first filing and the completed foreclosure.

! **Serial filings by related debtors.** The same individual or related individuals file several bankruptcy cases in a row to delay foreclosure.

! **Voluntary dismissals of serial Chapter 13 cases.** The debtor asks the court to dismiss the case. When a bankruptcy trustee obtains dismissal of a case for failure to appear or make required mortgage payments, the dismissal order usually prohibits the debtor from refiling for bankruptcy within 180 days. A voluntary dismissal avoids this prohibition. The debtor can immediately refile, renewing the automatic stay.

! **Involuntary petition scams.** Under certain circumstances, the Bankruptcy Code permits creditors to file "involuntary petitions" against borrowers. In this scam, an entity will file–-for a fee--a bankruptcy petition against an individual facing foreclosure, causing the automatic stay to take effect on the individual’s behalf.

! **Phony alias amendments to petitions.** The bankruptcy petition is amended to add an alias name of the debtor. The alias is actually the name of an unrelated person. The amended petition is recorded or otherwise used to stop eviction or foreclosure proceedings against the unrelated person.

Many Victims

The task force report points out that bankruptcy foreclosure scams harm the bankruptcy courts, lenders, homeowners, and innocent bystanders.

! Bankruptcy cases filed solely for delay crowd the **bankruptcy courts**. They also take more clerical and judicial time and attention than the average case, the report states, because they usually involve more relief from stay motions, orders to show cause, and motions and orders to dismiss.

! **Lenders** receive no payments for months or years while the repeated transfers and bankruptcy filings invoke the automatic stay.

! Many foreclosure services falsely promise **homeowners** that they will work out problems with lenders. Some debtors do not even know that bankruptcy petitions have been filed in their names; a debtor may think the foreclosure service is working out the lender’s problems, when in reality the service simply placed the debtor in bankruptcy to obtain the stay’s temporary protection. Other debtors may not know that properties have been transferred into their names to delay foreclosure in fractional interest scams.

! Some bankruptcy foreclosure scams involve the use of false Social Security numbers, harming the credit records of **innocent bystanders**--the real holders of those Social Security numbers.

Varied Recommendations

The task force’s proposals for combating bankruptcy foreclosure scams emphasize administrative, practice, and rule changes implemented by the bankruptcy courts. The task force also proposes changing various judicial case management practices, and amending the Federal Rules of Bankruptcy Procedure, the Bankruptcy Code’s automatic stay provision, and state and federal criminal laws.

The task force report **does not** touch upon whether a debtor should be able to obtain Chapter 7 discharge of credit card or other unsecured debt that could be partially repaid under Chapter 13. “By contrast to those arguments over the appropriate *scope* of consumer discharges, the cases of concern here do not seek *any* discharge, because they are never intended to be completed. All they seek is the automatic stay,” the report explains.

Lisa Hill Fenning, Bankruptcy Judge for the Central District of California, heads the task force, which also includes five other Central District bankruptcy judges as well as representatives from the United States Trustee’s Office, the United States Attorney’s Office, the Federal Bureau of Investigation, the Internal Revenue Service, the Federal Trade Commission, the California Department of Real Estate, and the Los Angeles County District Attorney’s Office. Private sector task force participants are the Legal Aid Foundation of Los Angeles, the Los Angeles Housing Law Project, Public Counsel, Bank of America, Great Western Savings Bank, Home Savings of America, and Experian.

Contact: Maureen Tighe
United States Trustee, Region 16
(213) 894-0405

Public Information Officer
Executive Office for United States Trustees
(202) 305-7411

7/13/98