

# Investors Title

INNOVATIVE BY INSTINCT

## FRAUD ALERT

In our ongoing efforts to keep our approved providers, agents, and other partners informed of potential threats to their business, we distribute Fraud Alerts so that you are aware of potential threats and can take any steps you feel necessary to guard against them.



### SCAM 1: FRAUDULENT SHORT SALE FLIP TRANSACTIONS

Recently, we have seen an increase in fraudulent transactions involving distressed properties, foreclosure properties, and properties about to go into foreclosure, which threaten the lender's value in their security and the borrower's equity.

The scam:

- 1) A fraudster identifies a property owner that is under considerable financial pressure and is facing or in some stage of foreclosure.
- 2) The fraudster works with the property owner (either knowingly or unwittingly as an accomplice) in negotiation with the lender for terms of a short sale. The property owner could be complicit in the scheme to ultimately regain the property or could just be desperately trying to sell their house.
- 3) The fraudster may use artifices to enhance the deal with the lender, such as fake repair bills, fake contractor estimates, fake pictures, fake comparable sales, fake appraisals, etc. Generally, the party closing the transaction would never be aware of these artifices.
- 4) The lender is seduced into a lower than accurate short sale price, thereby forfeiting equity in the security.
- 5) The fraudster arranges for the creation of an "investment company" (or other straw man) to purchase the property in a transaction that appears to be "arms-length."
- 6) The fraudster negotiates a sale of the property from such "investment company" or straw man to either a bona fide purchaser for value or an affiliate of the original financially distressed owner.

- 7) The most telling part of this fraudulent scheme is the funding for the transaction. Generally, the fraudster arranges for the short sale purchase and the ultimate purchase to happen "back-to-back."
- 8) The fraudster convinces the party closing the transaction to "dry close" the short sale transaction and use the funds from the ultimate purchase to fund the short sale closing. This allows the fraudster to keep the difference between the short sale price and the ultimate price, without having ever invested anything in the property.
- 9) Potential outcomes:
  1. The lender and the original property owner are out the difference between the short sale price and the market price. The original property owner may still be responsible to the lender for the deficiency balance.
  2. This outcome is different because the original property owner is complicit in the fraudulent scam. The lender is seduced into forgiving the deficiency balance owed and the original property owner reacquires the property with a new lender and a lower loan balance.

In both potential outcomes, the lender has left money on the table. Furthermore, once the fraud is discovered, the lender is extremely upset with the party that closed the transaction.

## **HOW CAN YOU PROTECT YOURSELF AGAINST THIS SCAM?**

Short sale transactions are going to continue to happen and will remain a "fact of life" in today's world. You will not be able to simply avoid short sale transactions; however, when you are involved in a short sale transaction, the following tips should help you protect yourself:

- 1) Always require settlement funds to be presented in accordance with the settlement statement at each transaction. Do not allow the funds for a subsequent transaction to serve as funds for another transaction merely because "you have them in your escrow/trust account." The funds from that subsequent transaction belong to the parties in the subsequent transaction and not the parties in the first transaction. If you allow this to happen, you are unilaterally making a loan from one party to another. Written consent of the parties would not generally help in this situation, and the consent from the lender in the subsequent transaction would be an absolute necessity.
- 2) Be suspicious of any "windfall" in a transaction. Remember: if the deal is too good to be true, it probably is.
- 3) Be suspicious of any relationship between the parties that would indicate that the transaction is not at "arms-length." Evidence may include the origin of repair bills and contractor estimates. Ask questions about the parties and how they got involved in the transaction.

- 4) Be suspicious of any short sale transaction in which a third-party "advisor" has a financial interest in the transaction.
- 5) If the property owner is selling at a short sale, it does not necessarily mean that they are relieved of a deficiency amount owed. Make sure that you understand these consequences and advise the parties accordingly.

Be suspicious of short sale transactions and make sure that you understand the relationship of the parties, the flow of funds, and where the parties end up. Always remember that the lender would not sell for less than their loan amount unless the lender felt that it did not have a choice. If the property owner or the lender are fraudulently deceived, the party closing the transaction may be the last chance to protect them from harm.

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### **SCAM 2: PHONY QUITCLAIM / NON-WARRANTY DEEDS**

There has been a recent increase in the use of fraudulent quitclaim or non-warranty deeds purporting to vest title in a bona fide purchaser for value, which, in reality, is only a fraudster creating an appearance of ownership (and a cloud on title) without the knowledge of the rightful owner.



The scam:

- 1) A fraudster identifies a property for fraudulent acquisition. Generally, these properties are REO properties or vacant distressed properties, where the actual owner is not currently occupying the house. The actual owner could be occupying the house, but the fraud would be much easier to uncover in such an instance.
- 2) The fraudster executes and records a quitclaim or non-warranty deed to a newly created entity.
- 3) The quitclaim or non-warranty deed would be conveyed for little or no consideration.
- 4) In this fraud, there is generally not a mortgage or deed of trust recorded after the quitclaim or non-warranty deed.
- 5) In some instances, the fraudster may even move into a vacant property to further the appearance of ownership.
- 6) The fraudster attempts to sell the property and may even supply a fraudulent prior title policy.

## HOW CAN YOU PROTECT YOURSELF AGAINST THIS SCAM?

The public records are intended to protect property owners and, when used properly, will do so. When misused or misunderstood, the public records can create an illusion of ownership. While many property owners only understand that the deed represents ownership, real estate professionals understand that a broader investigation of the public records will ultimately reveal the true owner.

- 1) The first step in preventing this fraud is to perform a title search and investigation.
- 2) In a world where updating from a prior title policy is commonplace, do not rely upon a title policy received from the seller. Confirm the authenticity and contents of such a policy with the issuing underwriter.
- 3) Be suspicious of a property recently conveyed for little or no consideration using a quitclaim or non-warranty deed.
- 4) Be suspicious of a property where there is not a deed of trust or mortgage in the chain of title for the current owner. Of course there are cash transactions, but most people have to borrow money to purchase their home.
- 5) As an added precaution, you should go back in the title to the previous owner and try to make direct independent contact. Do not rely on the contact information provided by parties to the transaction.

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We are interested in alerting our approved providers, agents, and other partners in the real estate business of any and all external and internal threats and fraud scams. In the event that you become the target of a fraud scam, please share that with us so that we may alert others. You may email the facts about the attempted fraud scam to [riskmanagement@invtitle.com](mailto:riskmanagement@invtitle.com).

This Fraud Alert is a service of Investors Title. If you have any questions about this Fraud Alert or the contents hereof, please feel free to contact Jonathan Biggs, Vice President of Risk Management and Education at [riskmanagement@invtitle.com](mailto:riskmanagement@invtitle.com).

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