

### ***New Mortgage Fraud Law Creates Risks for REALTORS®***

*Georgia is now ranked first in the United States for reported cases of mortgage fraud. In response to skyrocketing losses, the Georgia Legislature has passed new legislation creating tough new criminal penalties for mortgage fraud. These laws will hopefully have the desired effect of cutting down on the numerous instances of mortgage fraud in Georgia. However, the laws are written so broadly that some practices once thought of by REALTORS® as creative ways to get a transaction closed, now constitute crimes. In an effort to prevent REALTORS® from unwittingly running afoul of our criminal laws, this article will explain the new law and provide examples of practices which may now constitute crimes.*

#### **The Law**

The Residential Mortgage Fraud Act ("RMFA") went into effect on May 5, 2005. The RMFA can be found in the O.C.G.A. §16-8100 to §16-8-106. This new law increases the penalty for perpetrators of residential mortgage fraud. **Mortgage fraud is now a felony, punishable by a term of imprisonment.** A single incident may result in a term of imprisonment between one to ten years, and/or a fine up to \$5,000.00. Those found guilty of multiple frauds may be imprisoned to a term of three to twenty years, and/or a fine of up to \$100,000.00. **The new law also provides for the forfeiture of all real and personal property involved in the fraud.**

Further, the new law amends the state Racketeer Influenced and Corrupt Organizations Act (the "RICO" statute) to include mortgage fraud as a possible racketeering offense. A racketeering offense may amount to a felony and is punishable by a term of imprisonment of between five to twenty years, or a fine of either \$25,000.00 or three times the amount of any pecuniary value gained from such violation, whichever is greater. This will allow the prosecution of a fraudulent buyer and any party who knowingly participated in the mortgage fraud, such as the mortgage broker, licensee, appraiser and closing attorney.

Apart from providing a stronger deterrence, the new law covers fraudulent activity in any part of the mortgage loan process, from the loan origination, negotiation, underwriting and signing of the loan documents to the closing of the loan. This means that any fraudulent activity relating to any document used in the process will be considered mortgage fraud. The documents include the uniform residential loan application, appraisal report, HUD-1 statement, W-2 form, income statements, employment letters, tax returns and pay stubs.

#### **Fraudulent Activity**

What kinds of fraudulent activities are considered mortgage fraud under the new law? The new law provides that the following conduct amounts to mortgage fraud:

1. Knowingly making any untrue statements or failure to state the truth during the loan process with the intention that it will be relied on by a mortgage lender, borrower or any other party to the mortgage lending process;
2. Knowingly using or facilitating the use of any deliberately untrue statement or omission during the loan process with the intention that it be relied on by a mortgage lender, borrower, or any other party to the mortgage lending process;
3. Receiving any proceeds or any other funds in connection with a residential mortgage closing that such person knew resulted from a violation of the above paragraphs;
4. Conspiring to violate any of the provisions of the paragraphs;
5. Filing or causing to be filed with the official registrar of deeds of any count of this state any document such person knows to contain a deliberate misstatement, misrepresentation, or omission.

### **The Law in Practice**

Let's look at the examples below to see the types of risk REALTORS® may face under the new law.

#### **Example #1**

REALTOR® A has a long standing relationship with a wealthy buyer who regularly purchases rental properties for investment. REALTOR® A finds the buyer a small house to buy for this purpose and the buyer puts the property under contract. The buyer uses a variety of mortgage lenders and often obtains more favorable financing by telling them that he is buying the property as his primary residence.

REALTOR® A knows that the buyer is not being truthful in making this representation. At the closing, the buyer is asked to sign an affidavit stating that he will be residing in the property. REALTOR® A is at the closing and says nothing as the buyer signs a false affidavit. Does REALTOR® A have criminal exposure under the Georgia Residential Mortgage Fraud Act for his actions?

#### **Answer:**

Under our new mortgage fraud law, the answer to this question is “yes”. There are two areas of criminal exposure.

First, REALTOR® A is receiving funds in connection with the closing of a residential mortgage loan (i.e. – the commission) that REALTOR® A knew resulted from the use of a false statement provided by the buyer to the mortgage lender with the intention that it be relied upon by a mortgage lender. This is now a crime.

While an argument can be made that the law only applied to buyers receiving mortgage funds illegally, this argument will not likely prevail. This is because the real estate commission is shown on the HUD and is normally paid “in connection” with the residential mortgage closing process.

The second area of possible criminal exposure is that REALTOR® A can also be accused of facilitating the use of an untrue statement made during the loan process with the intent that it be relied on by the mortgage lender. In a criminal context, the term “facilitate” means the act of making it easier for another to commit a crime. The question which will undoubtedly be litigated in the next few years is whether REALTOR® A facilitates the use of an untrue statement (and commits a crime) by sitting at the closing table and saying nothing when REALTOR® A knows that a false statement is being signed which will be relied upon by the mortgage lender.

While I would argue that to commit a crime, REALTOR® A must commit a specific unlawful act or engage in some affirmative wrongdoing (as opposed to simply refraining from being a whistleblower) REALTOR® A nevertheless faces a risk of prosecution if he or she does nothing.

Finally, while this should be the least of their worries, REALTORS® in this situation may also find themselves in violation of Georgia License Law which provides that licensees can be sanctioned up to and including the revocation of their licenses for “being or becoming a party to any falsification of any...other document involved in any real estate transaction.” O.C.G.A. §43-40-25(a) 28. The question which again has not yet been clearly decided is whether a REALTOR® A can become a party to a falsification of a document by being aware that the document is false and saying nothing.

It is important to emphasize that in the example described above, REALTOR® A had actual knowledge that the affidavit being signed was false. In many cases, REALTORS® will not have any knowledge that a false document is being signed. In cases where the REALTOR® is an innocent bystander to a crime, the REALTOR® should not be at risk of being criminally prosecuted.

What should REALTOR® A do if he or she is sitting at the closing table and knows that the buyer is signing false documents? First, REALTOR® A should pull the buyer aside and advise him that 1) he appears to be breaking the law and should immediately consult with an attorney and 2) if he goes through with signing the false document, REALTOR® A will have no choice but to reveal the fraud to the closing attorney. The ability of REALTOR® A to take this aggressive position with his or her client is bolstered by the new language in all GAR brokerage agreements. Specifically, these agreements now give REALTORS® the right to:

“report any suspicious, unusual and/or potentially illegal or fraudulent activity (including but not limited to mortgage fraud) to:

1. Governmental officials, agencies and/or authorities and/or
2. Any mortgage lender, mortgage insurer, mortgage investor and/or title company which could potentially be harmed if the activity was in fact fraudulent or illegal”

The other alternative is for REALTOR® A to inform all parties that he or she can no

longer participate in the transaction and to forego your commission. While this is certainly an unpleasant alternative, knowingly receiving illegal funds from the residential mortgage closing is far worse.

### **Example #2**

REALTOR<sup>®</sup> A is representing a seller of a condominium unit which at most is worth \$150,000.00. The unit has been on the market for more than two years without any serious buyers. A buyer comes along and makes a full price offer. The offer is immediately accepted by the seller.

Prior to closing, the buyer approaches the seller and says that he will walk away from the deal unless the contract sales price is increased by \$100,000 so that a contractor can be paid at the closing for certain repairs that the buyer plans to do after the closing. Your seller asks for your advice in this situation. How do you respond?

### **Answer:**

This scenario certainly sounds like a classic case of mortgage fraud. However, while the above transaction raises red flags for possible mortgage fraud, REALTORS<sup>®</sup> should be careful not to point a finger too quickly at either the buyer or a seller. REALTORS<sup>®</sup> involved in these types of situations, should first call their brokers to get specific advice on how best to navigate these difficult waters. What often separates legal from illegal activity is whether all parties are willing to reflect the true and complete nature of the transaction in writing. In other words, is the buyer willing to execute an amendment to the contract (rather than a completely new contract) disclosing that the purchase price is being increased by \$100,000.00 and that this sum of money will be paid to a contractor at closing to perform certain repairs after closing? If the contract reflects the true and complete nature of the transaction, and the REALTOR<sup>®</sup> is not aware of any criminal activity, the REALTOR<sup>®</sup> should be insulated from criminal exposure. However, if the parties are unwilling to reflect the true and complete transaction in the contract, the REALTOR<sup>®</sup> should advise all parties that he or she will be obligated to reveal the true and complete nature of the transaction to the authorities to avoid the possibility of being treated as an accomplice to a crime.

If buyers or sellers ask whether a specific activity constitutes mortgage fraud, REALTORS<sup>®</sup> should make every effort not to give advice in this area. Instead, REALTORS<sup>®</sup> should refer the party to an attorney to avoid giving advice where the consequences of being wrong could be a criminal sanction. Alternatively, the REALTOR<sup>®</sup> can disclose how he or she will be proceeding (or not proceeding) in the transaction, and recommend that the party seek legal counsel.

### **Example #3**

REALTOR<sup>®</sup> B is representing a buyer who falls in love with an expensive new home. The buyer has sufficient income to make the mortgage payments but does not have money for a down payment. The buyer asks REALTOR<sup>®</sup> B for her help in figuring out some way for the buyer to purchase the home. REALTOR<sup>®</sup> B talks with a mortgage broker who suggests increasing the purchase price of the property by 10% with the

seller taking back a second mortgage and note for the 10% increase in the purchase price. He further explains that the seller and the buyer can then sign a separate agreement in which the seller agrees after closing to forgive the second mortgage.

Can REALTOR® B safely assume that this plan is safe since it was suggested by the mortgage broker?

**Answer:**

The answer to this question is “no”. REALTORS® sometimes forget that there is a difference between a mortgage broker and a mortgage lender. Mortgage brokers do not lend their own money to buyers. Instead, they shop for available mortgage loans and receive a fee for procuring them on behalf of buyers. A mortgage lender is normally loaning funds of the lender for whom the mortgage lenders works. While most mortgage brokers are honest, there are always a few rotten apples in every barrel.

A dishonest mortgage broker may encourage buyers and REALTORS® not to disclose certain information on their loan application or in the sales contract because the information, if disclosed, will prevent the ultimate mortgage lender from approving the loan. The dishonest mortgage broker may not care if there is a greater risk of a loan default because of the deception so long as the mortgage broker is paid his or her commission. As a result, when a REALTOR® suspects mortgage fraud involving a mortgage broker, it is important to try to get confirmation in writing from the actual mortgage lender that the questionable arrangement is in fact acceptable to the mortgage lender. If the confirmation the REALTOR® receives lacks credibility, the REALTOR® should not hesitate to talk to someone higher in authority with the mortgage lender until the REALTOR® is satisfied.

The biggest problem in this example is that once parties begin to discuss with each other how to make untrue statements, omissions or false documents that will be relied on by a mortgage lender in the mortgage lending process, it opens the door to a further criminal charge of conspiracy to violate our new mortgage fraud laws.

A person commits the offense of conspiracy to commit a crime when the person, together with one or more persons, conspires to commit any crime and any one or more of such persons does any overt act to effect the object of the conspiracy (see O.C.G.A. § 16-4-8). A prosecutor does not need to prove an express agreement between the parties in order to establish a conspiracy. The State only needs to prove that two or more persons tacitly came to a mutual understanding to accomplish or to pursue a criminal objective. (See McCright v. State, 176 Ga. App 486 (1985.)).

So what should the REALTOR® do if he or she finds him- or herself in the middle of this type of transaction? Unfortunately, even if the REALTOR® does not actively participate in the deception, it is a crime for the REALTOR® to knowingly receive funds from a mortgage loan closing which the REALTOR® knows were obtained by making a false statement or omission or using a false document.

Therefore, the REALTOR® should tell the parties that the sales contract must reflect the true and complete transaction. If there is an unwillingness on the part of the parties to do this, the REALTOR® should either withdraw from the transaction without receiving a commission or become a whistle blower and reveal the fraud.

### **Conclusion**

The new Residential Mortgage Fraud Act significantly ups the ante in defining mortgage fraud very broadly and criminalizing all activities where complete and truthful disclosure is not made to the mortgage lender in obtaining mortgage financing. The sanctions which the Georgia Real Estate Commission can impose (previously seen as burdensome) will now appear like a cake-walk compared to these new, tougher criminal sanctions. The law will likely create numerous situations where brokerage firms seeking only to conduct themselves properly will likely need to seek legal counsel to help them evaluate their criminal risk in these areas and how best to proceed when confronted with violations of the law. Prosecutors have indicated that they plan to aggressively enforce the new law. Arrests have already been made under the new mortgage law. Hopefully, their focus will be on the major offenders rather than those who inadvertently break the law. However, with the adverse publicity which can result to a brokerage firm if one of its licensees is arrested for mortgage fraud, brokerage firms would be well advised to educate their agents on the new law to reduce the exposure to criminal claims.

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