

California Announces Creation of a Mortgage Fraud Task Force to Pursue Mortgage Fraud at “All Levels”

BY THE WHITE COLLAR CRIME AND REGULATORY ENFORCEMENT & THE GLOBAL BANKING AND PAYMENT SYSTEMS PRACTICES

On May 23, 2011, California Attorney General Kamala Harris announced the creation of a new Mortgage Fraud Task Force (“Task Force”) to address allegations of widespread fraud impacting the State of California. The objective of the 25-member Task Force (consisting of 17 lawyers and 8 special agents from the California Department of Justice) is to investigate and prosecute fraud and fraudulent lending practices at all levels, from origination through securitization. In deciding to form the Task Force, Attorney General Harris stated that “no case will be too big or too small to pursue.”

The Task Force will focus on allegations of mortgage fraud in three major areas: (1) fraud involving mortgage-backed securities sold to the state or its pension funds; (2) fraudulent lending practices, including deceptive marketing and failure to fully disclose loan terms; and (3) scams by consultants, lawyers, and others who charged fees in connection with foreclosure proceedings and/or loan modifications without delivering on their promises. The Task Force will operate out of offices in Los Angeles, Fresno, San Francisco, and Sacramento. The Attorney General’s Office has expressed its intention to pursue all avenues available to the State to rectify harms caused by mortgage fraud, which the Attorney General contends was a significant contributing factor to the housing crash and is a continuing financial drag on the economy in the State of California.

Attorney General Harris’s announcement comes on the heels of criticism for agreeing to a \$6.5 million settlement with former Countrywide Financial Corporation CEO Angelo Mozilo earlier this year. As Attorneys General across the country continue to investigate the mortgage lending industry, this new Task Force appears to be one of the more aggressive steps taken by a State Attorney General to pursue mortgage fraud. In fact, Attorney General Harris may prosecute certain cases under California’s False Claims Act (“FCA”), which she has described as a “powerful tool[] that California uniquely has . . . to pursue, in essence, what are false claims that are submitted to the state.”

The FCA permits the California Attorney General to seek up to three times the amount of actual damages incurred by the government. See Cal. Gov. Code § 12651. The government may seek damages against persons who knowingly present or cause to be presented a false or fraudulent claim for payment. Id. Under the FCA, “knowingly” is defined to include actual knowledge, deliberate ignorance to the truth, or falsity, or acts in reckless disregard to the truth. See Cal. Gov. Code § 12650(b)(3). Attorney General Harris, through the Task Force, may intend to utilize this broad definition to pursue claims for the “improper marketing” of securities to California investment boards.

During her 2010 campaign for the Attorney General's office, candidate Harris promised to leave no stone unturned in seeking to bring to justice those who were deemed to be responsible for perpetrating mortgage fraud. The formation of the Task Force appears to represent the focus of her efforts to make good on her promise. Given the political stakes and public scrutiny, it is likely that the Task Force will be aggressive and persistent in issuing inquiries and filing charges against various participants in the mortgage lending process.

In short, the creation of the California Task Force is a significant new development that underscores the need for industry leaders to be prepared to manage and properly respond to investigative inquiries by the Task Force, or other State Attorneys General who may follow California's lead. Given that California is aggressively expanding its efforts in this area, mortgage and banking companies should be aware of: (1) the importance of conducting thorough and effective internal inquiries; (2) developing practical steps and guidance for performing an inquiry; and (3) the creation and implementation of an action plan to respond to the initiation of an investigation by the Attorney General's Office, including how to interface with authorities and/or respond to inquiries from the Task Force.

Action Plan

Mortgage lenders, including banks, thrifts and mortgage companies, should solidify an action plan anticipating inquiries from the Attorney General's Office in the Task Force's three key areas of investigation, including a review of:

- activities involving the prior sale of mortgage-backed securities to California or its pension funds;
- current and past mortgage loan underwriting and marketing practices, including activities involving third party marketing arrangements;
- the extent to which claims have been brought against your organization regarding unfair or deceptive acts or practices in the mortgage lending context; and
- activities involving other third party arrangements, including relationships and arrangements with mortgage brokers, consultants, appraisers, closing agents, and lawyers handling foreclosure proceedings and loan modifications.

In addition, as part of your action plan, you may want to assess the extent to which fraudulent activities adversely impacted the mortgage lending program of your organization and be prepared to work with the Task Force regarding the same.

In this time of increased scrutiny, early planning and preparation may be the difference between an investigation and potential prosecution. Our lawyers have extensive knowledge and experience defending mortgage fraud-related cases, overseeing internal investigations, responding to subpoenas, working with government authorities, and litigating cases under the FCA. We will continue to monitor the Task Force and its activities and will provide updates as appropriate with respect to any new developments.



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