

Karl Denninger – Roundup - Foreclosuregate Status

[There is a very important audio interview on KOH](#) that you need to listen to.

It's two hours, and that's a lot. But it's *important*.

In particular, listen to the couple of minutes starting at 12:30 in. Then listen to 6:30, and 42:30, right around 50:00 and then again **at 70:00 and finally, at 78:00 in.**

Pay attention to what's being said here.

First: The assertion is made that **the lenders and holders of the notes were paid in full.** That is, they have no economic damage from the default (!) due to the way they structured the deals.

Second: **The assertion is made that there was fraud in the inducement in all of these loans, in that there is an implied duty of dealing in good faith in all contracts that was violated by the banks that made knowingly bad loans – which we now have sworn testimony on.** While this is not settled by any means, *there is currently pending litigation on this point*, and if this approach wins, well, then you go – those contracts are voidable.

Third: **The allegation is made that the banks were not stupid – they knew the mathematics (as we all do now) and intentionally crashed the market.** That just compounds the second point.

Fourth: **MERS** has given sworn testimony that they have no economic interest **and have nothing to transfer.** Oh wait a second..... then how the hell do they transfer a deed they don't have (even though they're listed as Mortgagee) to someone who then forecloses – or alternatively, forecloses themselves on behalf of someone else?

[Incidentally, FDN has picked up on this too.](#) *Don't expect the entire "fraud in the inducement" line of inquiry to remain quiet for very long, and again, if this wins at trial – even once – you're gonna get this:*

[****storm]

The MERS problem is also outlined in a rather long and exhaustive paper in the [Cincinnati Law Review](#). The salient point is here:

With these services on offer, the mortgage finance industry quickly and wholeheartedly embraced recording and foreclosing its mortgage loans in MERS's name, rather than the actual parties in interest. Instead of legislation or a landmark court ruling, mortgage industry insiders report that the key development in the acceptance of MERS was the endorsement of credit rating agencies such as Moody's, Standard and Poor's, and Fitch Investment. 71 **For example, in 1999-before any significant appellate judicial opinion on the subject-Moody's Investors Services issued a report concluding that MERS's mechanism to put creditors on notice of a mortgage would not be harmed. 72 Moody's concluded without citation to any court opinion, or even to any state recording statute, that "subsequent creditors of the entity selling the mortgages to the MBS [mortgage backed securities] transactions [sic] should not be able to contest the conveyance of the mortgages based on lack of notice. 73**

Got that?

The agencies concluded **without any legal justification whatsoever** that this was all ok.

Since when does a ratings agency trump State Law?

There's been an awful lot of flip-flopping on many of these points in the last week. In particular, you've got people who were all over the fraud side of this that suddenly got *very quiet*.

One wonders why – and note, it's not that they're repudiating what they formerly said, *it's that they're saying nothing at all, and some are now trying to throw this back on the borrowers, making all sorts of claims of "unethical" behavior on their part.*

Let me be clear on my position: **This entire bubble was predicated on fraud – up and down the line. I'll simply quote Bill Black, since he's more concise than I can be:**

Nothing short of removing all senior officers who directed, committed, or acquiesced in fraud can be effective against control fraud. We repeat: Foreclosure fraud is the necessary outcome of the epidemic of mortgage fraud that began early this decade. The banks that are foreclosing on fraudulently originated mortgages frequently cannot produce legitimate documents and have committed "fraud in the inducement." Now, only fraud will let them take the homes. Many of the required documents do not exist, and those that do exist would

provide proof of the fraud that was involved in loan origination, securitization, and marketing. This in turn would allow investors to force the banks to buy-back the fraudulent securities. In other words, to keep the investors at bay the foreclosing banks must manufacture fake documents. If the original documents do not exist the securities might be ruled no good. If the original docs do exist they will demonstrate that proper underwriting was not done — so the securities might be no good. Foreclosure fraud is the only thing standing between the banks and Armageddon.

There's only one solution to all of this: **Take all of the big banks into receivership.**

Force these securities to be examined, those with fraudulent originations beyond their specifications to be unwound and put back on the securitizers.

This will detonate them. Since they're in receivership, their stockholders will wind up wiped out and their bondholders will take the hit as they are crammed down into equity.

Where intentional fraud is found in the inducement, [as has been alleged by Citibank's former chief underwriter in over 80% of production for 2007](#), people need to go to prison. A lot of people. And while this does not necessarily mean “free houses” it sure does mean rescission of the deal – and if that winds up forcing renegotiation of the terms (including principal), then so be it.

The more time goes on the deeper this rabbit hole gets and the more fraud we find evidence of. Contrary to the professed claims in the media, *this is not getting clearer and headed more toward “clerical errors”* - it is headed more toward *the entire financial system being one gigantic pyramid of fraudulent transactions layered upon each other, none of which were unwound during the so-called “bailouts.”*

Instead, it appears that government decided to attempt to *perpetuate* the debt and fraud ponzi schemes – likely because, arithmetic or not, *they knew that letting it all into the light of day would mean incalculable and insatiable demands for prosecution – at least figurative if not literal heads on pikes.*

If you think the idiocy and downplaying of reality is limited to the bankster apologists on CNBS, you're wrong. We also can look to Housingwire, [which put forth a pure fantasy piece](#) that included the following:

The real fact is that the ‘robo-signing’ scandal is a procedural one, albeit one that offends the very nature of due process.

....

The injured parties from this gross abuse of process are limited to the court, who has seen its rule of law mocked; and potentially investors, who must ultimately pay for the added time and expense of re-filing.

Forgery is not a “procedural issue.” It’s a felony act of perjury. Mocking the rule of law **is not a procedural matter** – it goes to the very heart of our legal system, not to mention *The Constitution*. There is this pesky thing called The 5th Amendment. I know that the mortgage and housing industries think that such matters lack substance in this case **but I’m quite sure that if the people decided to start stringing up lenders, bankers, and builders from lampposts en-masse, they’d change their tune about “procedural issues” and due process rights in a big damn hurry.**

Within minutes of the ‘robo-signing’ scandal, seemingly, commentators were giving credence to long-standing claims regarding the validity of MERS as a foreclosing party, who really owns the note, as well as highlighting put-back risks — a span of issues that are distinctly and utterly separate from the procedural challenges encompassed by ‘robo-signing.’

Nonsense. The entire “robo-signing” thing ***is part and parcel of the industry’s inability to produce factual documentation right up front.*** There are only two reasons not to produce the original paperwork, properly endorsed, instead of all this robo garbage:

1. You don’t have it **because you never got it**, and you’re trying to cover that up.
2. You don’t have it **because you intentionally destroyed it or are hiding it, as producing it would document that you did something fraudulent earlier on in the process (like at origination, for instance)**, and you’re trying to cover that up.

In short, there is no other explanation. A few lost pieces of paper here and there? Sure. A system that can’t produce **any** of the paperwork, properly endorsed over? That’s not accident – it’s an intentional act. Period.

In other words: massive GSE putbacks? Yes. Massive private-label putbacks? Eh, probably not so much. In either case, however, hardly does this seem to be the sort of end-of-the-world scenario that so many have painted recently.

Really? Remember, Lehman wasn't so much the end of the world *for Lehman per-se*, as it wasn't that big a firm. Rather it was the cascading credit default exposure that everyone was worried about.

Does anyone recall us actually fixing that by forcing it all onto regulated exchanges, where margin was maintained on a nightly basis so we know that everyone's good for the crap they're holding? Oh, I seem to remember that didn't happen.

Funny how everyone forgets that the nuclear device that started all this crap is still sitting on the board room table, it's still ticking, *and someone still has tape over the timer window so nobody can see how many more "ticks" we've got.*

The real brewing issue in the markets currently — and quietly — is one of investor confidence, borne most lately of horrible remittance reporting. Investors have had it with inaccurate reports from servicers, and some are threatening to ditch MBS markets altogether.

Getting lied to repeatedly has a way of doing that. You know, things like Clayton being revealed to have done diligence on these loans and finding them bogus, but then having them shoved into the securities anyway — **without disclosure to the buyers.** Or Citibank's chief underwriter stating under oath that **eighty percent** of production violated reps and warranties in 2007. *Eighty percent?!* Then you add stiff-arming to this by the securitizers for the original loan data. Gee, I wonder why they wouldn't want anyone to look *after their own people testified that they packaged up loans they knew were dogcrap and sold them on to investors!*

The third real issue facing mortgage markets today, quite frankly, is that political reality is allowed to subsume actual reality. This is the outcome that sees the mortgage industry eat its own, if it comes to pass.

In a word, **bull****.**

The "industry" *should eat its own.* What integrity does a fraud-laced process have? What sort of weight does someone who refuses to disclose what they did earlier on to a buyer command with a *new* buyer? Zero, that's what. Getting rooked once is a bad thing. *If you get rooked twice it's your own fault for trusting someone who has proved, through their own conduct, that they will **** you as long and as hard as they think they can get away with.* That is, buyers of these securities appear to now know **for a fact** that they were sold crap on purpose without proper disclosure.

None of these banks has any reason to expect that any of these buyers would ever do business with them again under any set of terms or conditions. In fact, this alone ought to be enough to put them all out of business – permanently.

The reality here is that what we have is a bunch of piranhas in a tank that have been feasting on Americans for two decades. Now the Americans are down to bare femurs, tibia, fibula and ribcages – **they're out of assets to strip and out of payments to poach.**

So now we get to the fun part, where the ravenous piranha, devoid of any sense of ethics and willing to eat literally anything, turn on their buddies and start tearing them apart.

And the Housing Fraud Continues

by: Karl Denninger May 31, 2010 |



[Karl Denninger](#)

From a report emailed to me over the weekend:

At the core of the foreclosure-prevention strategy is ignoring delinquencies. The percentage of older delinquent loans not yet in foreclosure is startling: 60% have at least 12 missed payments, and 35% have at least 18 missed payments. Add to this that three-fourths of delinquent loans are not in foreclosure, and we see that hidden losses well exceed those in the open.

Uh, they're not being "ignored" - this is systemic and intentional fraud.

Remember, these loans are either being held by someone or securitized into some sort of package. When you have a loan that has no chance of "curing" (to cure a loan with 12 missed payments the borrower would have to come up with the 12 payments to bring it current!) that loan should be carried at its recovery value - that is, the value of the collateral that can be seized and sold, LESS the cost of eviction, remediation and resale.

Does anyone recall all the entries I've written about getting competent legal and accounting (tax) advice before proceeding with any sort of action regarding walking away, short sales or foreclosure? This same report says:

Many homeowners would be better off going into foreclosure, than doing a short sale. Short sales are fraught with potential legal, credit, and complicated tax issues. For example, someone who refinanced could owe capital gains taxes, which are not forgiven under federal and California temporary debt relief acts. In the foreclosure route, borrowers can live in their house mortgage-free for at least one year, maybe two years. Both short sales and foreclosures are reported as “account not paid in full”, and are equally damaging to a credit score. An exception exists if short sellers can negotiate better terms with their lender on recourse liens. The other possible advantage to a short sale is the ability to get a mortgage again in 2 years (Fannie, Freddie), rather than having to wait 3-5 years after a foreclosure.

Homeowners pursue short sales, unaware of the problems they are creating for themselves. **Their agents never warned them of deficiencies, ruined credit, taxes due on forgiven debt, or legal consequences. Agents made flowery promises to get listings, and now the lawsuits are starting.**

No, really? You mean that people in the real estate business are less than truthful with their clients? That would never, ever happen with licensed professionals, right?

Then there's this, which I also have written about:

Another gray area is junior lien holders asking buyers for additional payments. As the market improved, juniors were no longer content with \$3k thrown to them from the senior. They now want 10% of the junior note. They argue the additional payment is legal practice because the payment is made to escrow and appears on the HUD-1. **However, they are actually hoping the senior lien holder does not read the HUD-1.** The California Association of REALTORS® position is that all payments made by the buyer or agent in the purchase of a short sale must be part of the written short sale agreement signed by the senior lien holder. **Concealing payments from seniors is loan fraud, and omitting these payments from the HUD-1 closing statement may violate RESPA. Some seniors reinstate their security interests because of the fraud.** It's surprising that the biggest banks are responding, when pressed on the fraud of their request, “just do it if you want the deal done”.

Right. Big banks saying "just do it"? Why would they do that? Is it so they can re-instate their security interests? No, nobody would ever do anything that hoses the consumer, would they? Naw.....

Few people understand that the bank that gave them their mortgage turned around and sold it into a mortgage bond, and the “bank” on their mortgage statement is actually a servicer.

Actually, it's a bit more complicated than that.

As I've been working on (and writing on) for a long time, and as a few attorneys are now starting to understand, ***the entirety of this process was corrupted and is rife with outright fraud from top to bottom.***

Let's go through a (partial) list of the problems:

- The originator of the loan (which often was some chop-shop mortgage boutique) was the place that got funding via a warehouse line of credit with a major bank. They paid the seller of the house. The seller thus is "whole" and has no further interest.
- The originator was shortly paid in full when the loan was sold to a major bank that was intending to (or did) securitize the paper. They were also paid in full ***and thus have no further legal interest in the property or the paper.***
- The banks, in turn, set up "bankruptcy remote" trusts to hold all this paper. This is (of course) done so that whatever happens to the paper doesn't impact the bank's earnings itself. Or does it.... we will get to that later.
- Many of the assignments from this point onward in the loan are legally defective. In particular, many of the assignments of the loans were made *in blank*, that is, in bearer form. *But in most states trusts cannot hold bearer paper of any sort - period.* In addition, in many states you cannot record a bearer instrument. To get around recording fees the industry has even created its own "clearing house" called MERS, which alternately claims to be an agent or the actual holder in due course, whichever suits the position of the trust (or itself) any given time. Whether this is legal under state law varies from jurisdiction to jurisdiction - what is known is that only one state has actually made the "reach around" games MERS plays explicitly legal.
- The trusts that are the "vessel" in which the securitized instruments are formed and then sold to investors thus hold paper they can't legally hold. This may in fact be sufficient to ***void the trust.*** Worse, they issued prospectuses and offering circulars to investors claiming that they had *good recordable title* to each and every loan in the trust. In many cases they never did and can't cure this retroactively. That is, ***there is at least the appearance of fraud in the sale of these securities, in that the buyers were led to believe they were buying a note backed by a security interest in an asset, when in fact there is no such backing at all - the note is a "bare" promissory note!***
- Cities, counties and states were ripped off to the tune of hundreds of billions of dollars over the previous ten years as a consequence of these intentional failures to properly record. *Specifically, the states, counties and localities have laws governing the requirement to record and pay doc stamps - that is, taxes - on transactions of this sort.* The necessity of recording these transactions varies from jurisdiction to jurisdiction, and thus the economic

damage done by this avoidance varies, but the banksters and their cronies simply kept this money instead of filing and remitting it to the taxing authorities as required by law.

The mess doesn't end here. If you buy a house where the original note was not satisfied in full and a full chain of assignments cannot verify that all security interests are released ***the title chain is severely clouded, perhaps to a degree that is almost impossible to unravel.*** Wise title insurance companies are beginning to recognize this problem and refuse to issue owners policies against properties where a broken chain of assignment exists, ***especially where a foreclosure or short sale took place,*** as those properties ***may*** still have an enforceable lien against them!

I recently spoke with an attorney who is aggressively pursuing these issues when his clients are faced with foreclosure, with some (and likely growing) success. He related to me that he spoke with the FCIC and was asked "Well, what is your solution? Are you asking that we nationalize all the (large) banks?"

If that's not an admission that ***FCIC knows the large banks were and are complicit in this and if forced to admit the truth in their financial statements would be rendered insolvent*** I don't know what is.

We have fixed nothing, but the can-kicking has also not pushed the bar very far down the road. The gambit was that the economy would return to a "boom" in the two years that have passed, and that the problems would be "absorbed" in that time.

It hasn't happened.

Now we're faced with having structuralized a \$1.5 trillion annual budget deficit into the indefinite future while those who were "helped" by HAMP and similar programs are facing re-default a few months to a couple of years down the road. DTIs over 60% virtually guarantee that outcome. At the same time the holders of these notes were sold a bill of goods and ***eventually*** some of them will wise up to the fact that the so-called "bankruptcy remote trusts" that allegedly hold the paper (and thus immunize the banks that created them) are legally defective. Those holders, when (not if) they suffer actual principal and coupon loss, can be reasonably expected to pursue their remedies at law with the aim of voiding the trust and opening the assets of the creating financial institution to attack.

If this line of inquiry is pursued it is entirely possible that these trusts would in fact be voided, and the resulting exposure landing on the major financial institution balance sheets would render them insolvent.

Again, we had the choice in 2007 and 2008 to force the institutions that did these things to "eat their own cooking", which would have likely bankrupted many or even most of them. But while we need a banking system, *we do not need any particular set of individual banks*. Instead of "bailing people out" and playing "extend and pretend" we could (and should) have taken the \$700 billion in TARP funds and used it to charter 10 *new* banks with strictly-limited 10:1 leverage and reserve ratios, which would have provided the ability to take up \$7 trillion in new and rollover lending - and let the overlevered behemoths fail.

Yes, the FDIC would have had to step in, and it might have cost us a trillion or more in FDIC insurance payouts. But even that would have been cheaper than what we have done, and in addition, we would have a safe, sound and stable financial system today.

Instead we have allowed the banksters to rob us once again, fixing nothing. As this mess continues to unravel - and it will - we will find that in fact we have simply blown more than \$4 trillion in borrowed funds and in fact gotten nothing in return for it.

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Mr. Denninger is the former CEO of MCSNet, a regional Chicago area networking and Internet company that operated from 1987 to 1998. MCSNet was proud to offer several "firsts" in the Internet Service space, including integral customer-specified spam filtering for all customers and the... [More](#)