

Fraud for Profit



By Patrick E. Fitzmaurice

April 26, 2010

A Legal Definition Of Fraud

- A claim for fraud requires a plaintiff to allege and ultimately establish the “five fingers of fraud”
- A Representation of a material fact or, in some cases, the omission of a material fact
- Falsity
- Scierter (or knowledge)
- Reliance
- Injury
- The fraud plaintiff is required to allege the circumstances of the fraud with particularity. This typically requires the plaintiff to include in his complaint allegations concerning specific dates and times on which the allegedly fraudulent statements were made. *Compare* NY CPLR 3016 (b) (“Where a cause of action or defense is based upon misrepresentation, fraud, mistake, willful default, breach of trust or undue influence, the circumstances constituting the wrong shall be stated in detail”) *with* Federal Rule of Civil Procedure 9(b) (“In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge and other conditions of a person’s mind may be alleged generally”).

First Finger: Representation of a material fact

- Courts have not given a precise definition of the term “materiality” as it relates to fraud. Whether particular facts are “material” for purposes of a fraud claim will depend on the facts and circumstances in each case.
- Guidelines
- In a criminal fraud case, the U.S. Supreme Court held that a false statement is material if it has a natural tendency to influence, or is capable of influencing, the decision of the person or entity to whom or which it is addressed.
- Some courts have held that if a statement is made with the specific intent that the other party rely on it, and the other does act in reliance on the statement, the speaker will not be allowed to deny the other party’s claim that the statement was material.

Second Finger: Falsity

- There are several different types of falsity:
- Plain falsehood – a lie
- A statement that conveys a false impression, even if no specific part is false
- Omission – failing to say something you should
- Concealment – the cover up.
- Silence?

Third Finger: Scienter or Knowledge

- Person making the representation must
 - Know the representation is false
 - Intend to convey false information
 - Fraud will also be found where the speaker makes a statement recklessly – without knowing or caring whether the statement is true or without a genuine belief in the truth of the statement.
 - Fraud liability will be found where the speaker makes a statement that implies he has knowledge about a subject, when he actually does not. In short, it is fraud to say you know something that you do not actually know.

Fourth Finger: Reliance

- The defrauded party must rely to its detriment on the fraudulent representation.
- Reliance can take the form of either action or inaction.

Fifth Finger: Injury

- To be actionable, a fraud must cause injury.
- Such injury could take the form of a monetary loss (this is the most common form).
- The loss must be one that can be clearly defined and ascertained – speculative harm is not enough.

Case Study No. 1

- Borrower makes a representation on his loan application that he intends to occupy the mortgaged property as his primary residence.
- 60 days after closing, file shows that utility bills for mortgaged property are being sent to old address and property records show old address is still in the Borrower's name.
- Has the Borrower committed fraud?

Case Study No. 2

- In Mortgage Loan Purchase Agreement loan seller (who originated the loan) makes a representation that:
 - It has not misstated or omitted any material fact about the mortgage.
 - Assume the same facts as Example No. 1.
 - Assume further that loan seller did not do anything to determine whether the borrower is residing in the mortgaged premises as of the date of the loan sale.
- Has the seller committed fraud?



Sonnenschein
SONNENSCHN NATH & ROSENTHAL LLP