Key Home-Saving Measures at Risk:
The Threat of H.R. 3915's Preemption Rule

Analysis by the
National Consumer Law Center
on the importance of state law claims against mortgage holders

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I. *Introduction*

H.R. 3915, the Mortgage Reform and Anti-Predatory Lending Act of 2007, passed the U.S. House of Representatives on November 15, 2007. The bill sets out a series of new federal rules designed to stop abuses in the predatory mortgage market.

While HR 3915 includes many positive features, it also includes a provision – Section 208[1] – that preempts all claims against assignees and holders when net tangible benefit or ability to pay issues are involved. While there are some exceptions to this wholesale preemption, *important claims that are currently saving homes all over the nation would be eliminated.*

HR 3915 fails to create the necessary incentives to abide by the new law because it does not establish sufficient enforcement or penalties for non-compliance. A key aspect of this problem is the proposed preemption in Section 208, which eliminates some of the primary tools currently used by homeowners to save their homes from predatory loans while minimizing Wall Street liability for core market abuses fueled by securitization money and the specifications of the secondary market. The state law claims preempted by Section 208 are an essential tool for saving homes from foreclosure and must remain available to address the problem loans held by this part of the mortgage industry.

Following is a discussion of Section 208, an analysis of the types of claims preempted, an examination of the importance of these claims in defending foreclosures,

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[1]SEC. 208. EFFECT ON STATE LAWS –

(a) In General- Section 129B(d) of the Truth in Lending Act (as added by section 204) shall supersede any State law or application thereof that provides additional remedies against any assignee, securitizer, or securitization vehicle, and the remedies described in such section shall constitute the sole remedies against any assignee, securitizer, or securitization vehicle, for a violation of subsection (a) or (b) of section 129B of such Act or any other State law the terms of which address the specific subject matter of subsection (a) (determination of ability to repay) or (b) (requirement of a net tangible benefit) of such section 129B.

(b) Rules of Construction- No provision of this section shall be construed as limiting--

(1) the application of any State law against a creditor;

(2) the availability of remedies based upon fraud, misrepresentation, deception, false advertising, or civil rights laws--

(A) against any assignee, securitizer, or securitization vehicle for its own conduct relating to the making of a residential mortgage loan to a consumer; or

(B) against any assignee, securitizer, or securitization vehicle in the sale or purchase of residential mortgage loans or securities; or

(3) the application of any other State law against any assignee, securitizer, or securitization vehicle except as specifically provided in subsection (a) of this section.

and examples of reported cases using such claims. The Appendices include narratives and examples of similar cases from attorneys in 13 states, followed by several court pleadings from some of those attorneys.

II. Explanation of Section 208

A. Broad Preemption of Core Claims

Section 208 first preempts claims against holders and assignees for any claims related to ability to repay (subsection (a) of new Section 129B of the Truth in Lending Act) and net tangible benefit (subsection (b) of new Section 129B):

> (a) In General- Section 129B(d) of the Truth in Lending Act (as added by section 204) shall supersede any State law or application thereof that provides additional remedies against any assignee, securitizer, or securitization vehicle, and the remedies described in such section shall constitute the sole remedies against any assignee, securitizer, or securitization vehicle, for a violation of subsection (a) or (b) of section 129B of such Act or any other State law the terms of which address the specific subject matter of subsection (a) (determination of ability to repay) or (b) (requirement of a net tangible benefit) of such section 129B.

This language appears to require that any claim brought against the holder challenging the terms of the loan or the circumstances surrounding the origination of the loan, which might be construed to address "the specific subject matter" of the federal requirement for the originator to ensure an ability to repay and a net tangible benefit, will be preempted because of Section 208. This broad language seeks to preempt any case with facts relating to the borrower's ability to pay the loan or the borrower's benefit from the loan, whether or not the claim itself uses such language directly.

One example of a case that uses claims against holders that appear to be in danger of being preempted by Section 208 is a case recently settled in Wheeling, West Virginia: Ameriquest Mortgage Company v. Eugene and Debra Brown, Ohio County, West Virginia, Civil Action No. 03-C-471. The Browns, who are uneducated African-Americans, were referred to Ameriquest by a debt collector. When the Browns took out the Ameriquest loan, they were told that their total monthly payments would be lower and that their other debts would be paid off. Instead, the new loan failed to pay off their other debts, yet charged them over $6000 in closing costs while providing them with only $4,600 in new money. It also increased the interest rate on the mortgage payments significantly and depleted the equity in their home. The payments on the Browns' Ameriquest loan were significantly higher than the payments on their previous mortgage, even though there was no escrow for taxes and insurance. These payments were not affordable from the first payment—even before the variable rate would increase after the teaser period, and even before premiums for forced placed insurance were added. The initial unaffordability of the loan would have been evident to anyone carefully reviewing the Browns' loan file. Moreover, the loan provided no benefit to the Browns—a point that was critical to the unconscionability claim. Although Ameriquest originated the loan and continued to service it, the loan was packaged and sold on the secondary market.

After the home was foreclosed upon and the Browns were facing eviction, a private law firm filed suit on the Browns' behalf, making unconscionability and unfair trade practice claims, among others. Public records reveal that the Browns are currently living in their home, and there are no liens on it. Under HR 3915, essential claims used to save their home would not have been available.

Notes from a Legal Services Attorney in Philadelphia

I've been representing homeowners in foreclosures for 10 years. . . . At least half of the people who have come to us with foreclosures have been the victims of abusive subprime loans, usually refinancings of mortgages that had better terms or new loans against homes that were free of mortgage debt (elderly homeowners who had paid their mortgages off or family members who inherited homes that had been paid off). Right now, I have 87 active cases; half of them involve abusive subprime loans.

In 36 of my cases, unfair trade practice claims or the common law defense of unconscionability are essential to any hope of my clients keeping their homes. I routinely use these claims quite successfully against the assignees of these loans (almost all loans are held by parties different than the original lender). . . . Assuming that these percentages are similar for my colleagues here, we have at least 200 active cases where unfair trade practice claims and unconscionability claims against assignees are vital to our homeowner clients. We are able to take just 1/3 of the foreclosure cases that come to us, we refer many subprime mortgage cases out to private attorneys, who also rely on unfair trade practice claims to represent the homeowners.

Unconscionability is the most hopeful defense for the cases where the mortgage payment was never affordable for the homeowner but we cannot identify direct misrepresentations and reliance (as required for claims of fraud and, in Pennsylvania, unfair trade practice). Given that Truth in Lending does not protect borrowers from payments they cannot afford (the disclosures required by TILA are pretty useless in these circumstances; they tend to be incomprehensible to our very low income clients. The most common reaction by my clients when I ask them why they signed for a loan they couldn't afford is, "I didn't understand that I couldn't afford it, why would they give me a loan that I couldn't pay?"), the defense that a loan is grossly inequitable often is the only defense. Unconscionability can be raised against the party foreclosing, even if that party is a holder in due course, as the defense goes to the terms of the loan, not the opposing party. So it means we can represent more homeowners; we don't have to plead in or separately sue the original lender. Trading this defense away would completely undermine our foreclosure defense practice for predatory subprime loans.

-- Beth Goodall, Community Legal Services, Philadelphia, Pennsylvania.

B. Holder Liability at Stake.

A holder can be liable for claims against the originator under any one of a number of theories, largely determined by a combination of factors including state law, the terms of the particular transaction, and the behavior and knowledge of the holder before and during the transfer of the note and mortgage to the holder. The liability of the holder comes in two basic forms: liability stemming from the actions of the mortgage originator (derivative liability) or liability for the assignee's own actions (direct liability).[2]

A holder's derivative liability is based simply on the fact that the holder is considered an assignee of the note and mortgage, and may be liable for all claims that could be made against the originator. An assignee generally can avoid derivative liability if it can show that it is a holder in due course. This is an affirmative defense, which, while often available, is not an automatic status conferred on every holder of every mortgage note, especially in today's mortgage market of adjustable rate loans with well-known defects.[3] In addition, federal claims, such as those made under the Truth in Lending Act, subject holders to derivative liability in some circumstances, notwithstanding their holder in due course status.

Even if the assignee is a holder in due course, and can avoid derivative liability, courts have held assignees liable for origination claims based on the holder's own conduct. For example, state common law and statutory claims may be available to hold the assignee liable based on theories of agency, joint venture, conspiracy, and aiding and abetting.

Michael Short's Loan and Servicing Problems

In the case of *Short v. Wells Fargo Bank Minnesota* (401 F.Supp. 2d 549 (S.D.W.V. 2005)), when the low- income homeowner went to Delta Funding to borrow less than $4000 to pay off some bills, he was provided a loan that refinanced his first mortgage loan and charged over 19% in up-front fees. The federal court held that both the assignee and the servicer of the loan—Wells Fargo Bank and Countrywide—could be found to be parties to a "joint venture" based on the existence of a Pooling and Servicing agreement between them. Thus, they both were responsible for the origination problems (no net tangible benefit) and servicing problems (as well as other claims) brought by the homeowner.

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[2] *See generally* National Consumer Law Center, *Cost of Credit* (3rd ed.2005), § 12.12.

[3] An assignee is a holder in due course only if it can show that a) the mortgage is a negotiable instrument as defined by Article 3 of the Uniform Commercial Code, b) the note was properly endorsed to the holder, c) the holder paid value for the mortgage, and d) the holder purchased it without notice that it is overdue and without notice that there is a defense about any nonpayment. *See* National Consumer Law Center, *Cost of Credit* (3rd ed. 2005), § 10.6.

C. Preserved Claims Leave Out Key Protections

Subsection 208(b)(1) appears to specify that holders still will be directly liable for their own actions when claims are for fraud, misrepresentation and deception, civil rights laws, and false advertising. Subsection 208(b)(2) appears to extend this preservation of actions against holders for these claims regardless of whether the holders are considered to be directly liable or liable based on their status as an assignee.

There are still many critical state claims that are not preserved, and thus may be preempted because of subsection (a). For example, the following state statutory or common law claims could be preempted against holders when they involve facts challenging the net tangible benefit or ability to pay of a home loan:

- common law unconscionability of contract;
- statutory unconscionability;
- breach of good faith and fair dealing;
- breach of fiduciary duty;
- unfair trade practice;
- breach of contract; and
- state consumer protection statute prohibiting specific activities, such as making loans with no net tangible benefit or without ascertaining the borrower's ability to repay the loan.

III. Preempted Claims Save Homes

Homeowners who have been victimized by predatory mortgages routinely bring actions against the holders of their loans under common law and statutory theories of unfairness, unconscionability, and breach of duty of good faith and fair dealing. These claims generally are used to challenge the overall damaging nature of the loan, sometimes known as a "net tangible benefit" claim, or to challenge the lender's failure to determine the homeowner's ability to pay the loan. Courts regularly allow these claims to go forward, and they are used to save homes around the nation. They are often the main claim used to protect against foreclosure—both because they encapsulate the predominant market abuses of today—unaffordable loans and loans grossly mismatched with the borrower's circumstances—and because, unlike fraud claims, they do not require proof of a series of specific elements.

The Case of Mary G. Noyes

Mrs. Noyes is 82 years old and a widow. She and her son, Thomas V. Noyes of Newbury, Massachusetts, obtained a subprime mortgage with Tribeca Lending Corporation. They filed a claim in bankruptcy court in Massachusetts to stop a foreclosure on their residence brought by the holder/assignee of the mortgage. The complaint alleged numerous forged closing documents; the unlawful practice of law by one of Tribeca's employees; and most significantly, that the loan was not in the borrowers' best interest (a claim challenging the net tangible benefit of the loan). The Noyes paid $22,773.94 in closing costs and were in default on the loan with Tribeca within 3 months. Although there are several federal and state claims pending, the primary claim that will provide relief from this mortgage is the Massachusetts unfair trade practice claim.

Such challenges are couched in different terms, determined by the rules and requirements of state law and by the facts of the individual cases. They boil down to the same problems: bad loans made with no real analysis of the homeowners' ability to repay or with no material benefit to the borrower. Claims against the holder that challenge loans based on theories related in any way to these claims appear to be preempted under Section 208, regardless of whether the claims specifically include the words "ability to repay" or "net tangible benefit." The preemption applies whether the claims were made for the assignee's own conduct or for the conduct of the originator for which the assignee is liable as an assignee of the law. This preemption of essential claims against assignees would eradicate the ability of homeowners to stop foreclosures, to void bad loans, or even to modify their loans, when the basis for their claim against the originator is grounded in an analysis similar to "net tangible benefit" or failure to determine the borrower's ability to repay the terms of the loan. Including the holder in the case is critical for the relief needed to address the problem: only the holder has the power to modify or cancel the loan.

Lawyers who represent homeowners in most states—both defensively against foreclosures[4] and affirmatively—routinely use non-fraud consumer claims to challenge the predatory nature of the loans. Appendix A includes discussions of such cases from lawyers in 13 states:

- California
- Florida

[4] In judicial foreclosure states, these claims can be raised as a defense against the foreclosure. In a non-judicial foreclosure state, it often is necessary to file bankruptcy to have these claims heard, because to stop a foreclosure in a non-judicial foreclosure state requires the filing of an independent, affirmative action, and the issuance of an injunction. In many of these states the bond requirements are prohibitively expensive, so that the only way to stop a foreclosure is to file a bankruptcy.

- Georgia
- Illinois
- Massachusetts
- New Jersey
- New York
- North Carolina
- Ohio
- Pennsylvania
- South Carolina
- Washington
- West Virginia

IV. History is Instructive: Making Holders of Bad Loans Responsible Does Not Reduce Credit Availability

All players involved in a bad mortgage loan must be part of the solution, just as they are now part of the problem. Wall Street's investment in subprime lending transformed the industry from a modest player into a significant portion of the market. The securitization process also resulted in product development aimed at secondary market sales, rather than at homeowners. Moreover, homeowners facing default and foreclosure must contend with rules set by the trusts holding pools of securitized loans.[5]

[5] These rules are set out in Pooling and Servicing Agreements.

Borrowers deserve direct access to the party who can save their home. This can only be ensured through applying assignee liability to every mortgage loan. Market incentives and interests must be aligned with those of the homeowners.

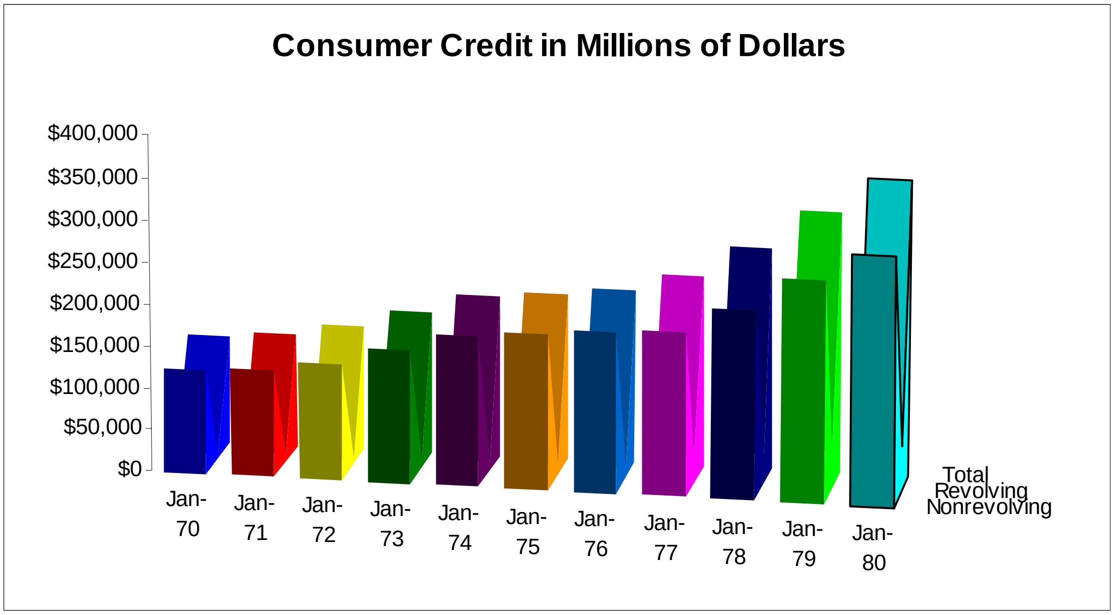
Opponents of assignee liability claim that a series of terrible events will befall the mortgage industry if full assignee liability is applied. This "sky is falling" list includes: a dramatic decrease in the availability of credit, particularly affecting minorities; ruinous effects on small businesses; unfair burden on the secondary market to police loans, as the process is so routinized and involves so many loans at any one time that a careful review of each loan would be nearly impossible and would dramatically increase the cost of credit.

A key perspective in analyzing these concerns is to look at what happened after the Federal Trade Commission passed the Preservation of Consumers Claims and Defenses Rule (commonly referred to as the "Holder Rule") in 1975.[6]

The Holder Rule applies liability for *all claims and defenses that could be brought against the seller* to assignees of loans used to purchase goods and services.[7] The rule reallocates the cost of seller misconduct from the consumer to the creditor,[8] so that a consumer who has been harmed may obtain a remedy by abrogating the Holder in Due Course doctrine. At the time the rule was proposed, the automobile dealers and other sellers of goods, argued that, if the rule passed, the cost of credit would increase, credit would be more difficult to obtain, retail merchants would be hurt, financial institutions would stop purchasing consumer loans altogether, businesses would suffer, and many would be forced out of business altogether.[9] The finance companies and the banks argued that they did not want the responsibility of policing sellers, sellers would not survive with the additional red tape, many consumers would stop paying on the loans without cause, and the rule would interfere with free competition.[10] These nightmare scenarios did not materialize. There was no reduction in available consumer credit; there were no indications that sellers were hurt in any way; there was no discernable increase in defaults.

The primary argument addressed by the FTC was that the proposed rule would increase the cost of credit or make it very difficult to obtain.[11] Following is a chart showing the level of credit in the United States from 1970 through 1980.

[6] 16 C.F.R. 433, 40 Fed Reg. 53506 (November 18, 1975).
[7] The transaction must involve a consumer credit contract and the seller must be in the business of selling goods or services to consumers. The assignee's liability is limited to the amounts paid by the consumer.
[8] Maberry v. Said, 911 F. Supp. 1393 , 1402 (D. Kan. 1995).
[9] 40 Fed. Reg. 53506 (November 18, 1975) at 53517.
[10] *Id.*.at 53518.
[11] *Id*



The level of "non-revolving credit" is indicated in the last column and includes auto loans, loans for mobile homes, education, boats, trailers and vacations but excludes all credit card loans. In 1970, total non-revolving credit in the US was approximately $124 billion; growth continued steadily through the 1970s, with not even a blip in 1975 and 1976 when the FTC rule was announced. By December 1980, total non-revolving credit in the United States was approximately $297 billion. In the space of ten years, consumer credit – notwithstanding the announcement and final promulgation of the holder rule halfway through that decade – had more than doubled.[12] The amount of outstanding consumer credit has continued to climb unabated since then: the outstanding amount of non-revolving debt increased over 500% during the seventeen years from January 1980 to December 2007.[13] In the area of auto loans, this FTC rule has not interfered with the securitization of auto credit.[14] Auto ABS volume for 2005 for prime and subprime loans combined exceeded $75 billion.[15]

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[12] Federal Reserve Statistical Release G.19, 1970 to 1980.
[13] The amount of non-revolving debt (in millions of dollars) was $295,524.23 in 1980 and grew to $1,580,039.43 (in millions of dollars) by December 2007. Federal Reserve Statistical Release G.19, 1980 & 2007, *available at* http://www.federalreserve.gov/Releases/g19/hist/cc_hist_nr.html.
[14] Letter from Vernon H.C. Wright, Chairman, American Securitization Forum, to Financial Accounting Standards Board (May 10, 2004), available at http://www.americansecuritization.com/uploadedFiles/FAS_140_Setoff_Isolation_letter_51004.pdf. The letter in part describes the FTC Holder Rule and its importance and describes the assessment used in the regular course of business to incorporate such liability into deals. It also states that buyers are willing to assume such risks and purchase such assets.

> For decades, a rule of the Federal Trade Commission (the "FTC Rule") has required every consumer credit contract (for instance, retail automobile installment loans) to include a legend to the effect that any purchaser of the contract is subject to all claims and defenses which the debtor could assert against the seller of the goods financed under the contract. This is to assure that consumers are not deprived of important defenses relating to payments owed on defective goods merely because their initial creditor sells the contract.

V. *Examples of Court Decisions Allowing Unconscionability and Unfairness Claims Against Holders*

The court decisions summarized below are just some examples in which all four prongs of the Section 208 preemption are present:

1) The terms or the origination practices of a mortgage loan are challenged;

2) State law claims were brought that relate to the loan's failure to provide a "net tangible benefit" or the lender's failure to determine the borrower's ability to repay;

3) Assignees of the loan are included in the case; and

4) The assignees are alleged to be liable either because they purchased loans originated in violation of the law or because the assignees themselves violated the law.[16]

<u>Commonwealth v. Fremont Investment & Loan et al., Findings of Fact and Conclusions of Law, No. 07-4373-BLS1 (Mass. Sup. Ct. Feb. 25, 2008)</u> **(Attached as Appendix B.)** Ruling prohibits Fremont from foreclosing on mortgages it is servicing without permission of Attorney General based on unfair nature of unaffordable mortgage loans. Abuses were comprised of "unsatisfactory lending practices" with regard to the origination of adjustable rate mortages, including: qualifying borrowers based only on the ability to pay the initial pre-reset payments; failure to verify income; substantial prepayment penalties and product features likely to require frequent refinancings. Fremont had voluntarily entered into agreement for Attorney General review of foreclosures and then terminated the agreement when objections were raised in most instances where the property was owner-occupied. The Attorney General sought an injunction based on the unfairness of the loans following termination of the voluntary agreement. Over a three year period, Fremont originated over 14,000 mortgages for owner-occupiers in Massachusetts; 3,000 are still outstanding and 2,500 are serviced by Fremont. Because Fremont securitized many of its loans, it appears that the loans in question are held by investors.

> The Uniform Commercial Code (the "UCC") provides that a buyer of many common types of receivables (for instance, credit card receivables, short term trade receivables and lease receivables) may be subject to all defenses or claims of the debtor against the seller… .
>
> Notwithstanding these risks, buyers are willing to purchase these types of assets. For instance, most retail auto installment paper is originated by auto dealers, who assign the paper to a finance company or bank. The finance company or bank may in turn transfer the paper into a securitization. The FTC and UCC rules about setoff are the same for both the initial purchase from the auto dealer and any subsequent transfer into a securitization.
>
> Banks and finance companies that buy this paper analyze potential setoff risks as analogous to other ordinary course seller risks that a buyer of any asset takes.

[15] ASF 2006 Retail Auto ABS Sector Review, *available at*

http://www.americansecuritization.com/uploadedFiles/Retail%20Auto%20Loan%20ABS%20Sector%20Panel%204pm.ppt#646,1,ASF 2006 Retail Auto ABS Sector Review.

[16] It is important to note that in almost all consumer cases *multiple* claims are generally filed, including breach of the applicable federal laws, such Truth in Lending and Real Estate Settlement Practices Act, unfair trade practices, unconscionability of contract, breach of fiduciary duty, fraud, deception and misrepresentation. As the complaint is filed before any discovery has taken place, the attorney rarely knows which claims will prove successful in saving the home. Many of the court decisions described in this section included multiple claims, some of which might be preempted under Section 208, and some of which would not be. Fraud and deception are very different claims than unconscionability and unfair trade practices, and are often harder to prevail on in litigation, as proof of these claims often requires proving the knowledge and intent of the defendant, and the reliance and direct harm caused on the homeowner.

Associates Home Equity Services, Inc. v. Troup, 778 A.2d 529 (N.J.Super. 2001) Assignee of note and mortgage brought foreclosure action, and homeowners filed counterclaim alleging violations of the Consumer Fraud Act (CFA), the Law Against Discrimination (LAD), the Fair Housing Act (FHA), the Civil Rights Act (CRA), and the Truth-In-Lending Act (TILA) by original lender and assignee. Dismissal of unconscionability claim reversed where allegations revealed that the higher interest rates and points charged to the borrowers may not have been warranted (net tangible benefit type of analysis).

Beneficial Mtg. Co. of Ohio v. Leach, 2002 WL 926759 (Ohio App. May 9, 2002). Defense to foreclosure brought by assignee was permitted to continue to trial when borrower alleged unconscionability of loan as a defense.

Cazares v.Pacific Shore Funding, 2006 WL 149106, (C.D.Cal. January 3, 2006). Court finds that in class action alleging excessive fees charged on home mortgages (similar to a "net tangible benefit" analysis), assignees can be liable under California statute prohibiting unfair practices for origination problems with loans, based on both derivative and direct liability.

Cooper v. First Government Mortg. & Investors Corp., 206 F.Supp.2d 33 (D.D.C. 2002). Motion to dismiss denied in case brought by homeowner against mortgage brokers, assignees, and settlement agents challenging excessive fees, and other costs, and onerous and unfair terms of mortgage loan (claims that could be otherwise construed to challenge the "net tangible benefit" of the loan).

Gilbert v. Security Finance Corp. of Oklahoma, Inc., 152 P.3d 165 (Okla. 2006). Borrower's guardian brought action against lenders and non-resident parent corporations and holding companies to recover for fraud, breach of fiduciary duty, and breach of the duty of good faith and fair dealing for consistent overcharging and flipping home equity mortgage (a "net tangible benefit" type analysis). The Oklahoma Supreme Court held that one corporation may be held liable for the acts of another under the theory of alter-ego liability if (1) the separate existence is a design or scheme to perpetuate a fraud, or (2) one corporation is merely an instrumentality or agent of the other. Evidence created jury question on parent corporation's liability for lenders' acts under alter-ego theory.

Hays v. Bankers Trust Co. of California, 46 F.Supp.2d 490 (S.D.W.Va. 1999). Borrower sued lenders and assignees of her loans, alleging that overcharges and other problems with the mortgage violated state statutory and common law prohibitions against unconscionability. The federal district court held, *inter alia,* assignee was a "holder" of borrower's note under West Virginia law; civil conspiracy claim applicable to assignee.

Herrod v. First Republic Mortg. Corp., Inc. 625 S.E.2d 373 (W.Va. 2005). The home mortgagors alleged that lenders made mortgage loan without regard to their ability to pay the loan, and charged excessive fees (a "net tangible benefit" type claim). The claims against the assignee of the original mortgagee included violations of Consumer Credit and Protection Act, fraud, unfair or deceptive practices, and unconscionability. The West Virginia Supreme Court held that a genuine issue of material fact precluded summary judgment as to assignee's liability under theories of joint venture, agency, or conspiracy.

In re Maxwell, 281 B.R. 101 (Bankr. 2002). Bankruptcy court held as against the holder of the loan that a mortgage refinancing agreement was unconscionable because the sum total of the contract's provisions drives too hard a bargain for court of conscience to assist it (same analysis as a "net tangible benefit" analysis).

Johnson v. Long Beach Mortgage Loan Trust 2001-4, 451 F.Supp.2d 16 (D.D.C. 2006). In case in which homeowner alleged that the contract was unconscionable (and other claims) on the basis of excessive fees (a claim similar to a "net tangible benefit analysis), the court allowed claim to proceed against mortgage assignee on the basis of agency.

M & T Mortgage Corp. v. Miller, 323 F.Supp.2d 405 (E.D.N.Y. 2004). Purchaser of mortgage settled foreclosure case, and claims were allowed to proceed against originators and others relating to unconscionability and fraud in sale of unaffordable homes to plaintiffs.

Short v. Wells Fargo Bank Minnesota, NA, 401 F.Supp. 2d 549 (S.D.W.V. 2005). When the low-income homeowner went to Delta Funding to borrow $2000 to $4000 to pay off some bills, he was provided a loan which refinanced his first mortgage loan and charged over 19% in up-front fees. The federal court held that both the assignee and the servicer of the loan, Wells Fargo Bank and Countrywide, could be found to be parties to a "joint venture" based on the existence of a Pooling and Servicing agreement between them, and thus responsible for both the origination problems (no net tangible benefit) and servicing problems (as well as other claims) brought by the homeowner. The homeowners' claims included unconscionability and breach of contract.

Williams v. First Government Mortg. and Investors Corp., 225 F.3d 738 (D.C. Cir. 2000). Unconscionability claim allowed against assignee in mortgage (net tangible benefit type and ability to pay type claims) case.

APPENDIX A

Claims for unconscionability, unfairness, breach of the duty of good faith and fair dealing, and related theories are used regularly against assignees by homeowners challenging a mortgage loan's failure to provide a net tangible benefit, or the originator's failure to determine the homeowner's ability to repay the loan. Below are recitations of the use of these claims by 26 legal services and private attorneys in 13 states. These are simply examples. These examples are written to highlight the claims that may be affected by the Section 208 preemption. In many of these cases, there are other claims included, such as Truth in Lending and fraud. As these claims presumably would not be affected by Section 208, they are not discussed.

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Summary

I have numerous cases against originators and holders challenging mortgages which are unaffordable to homeowners and which have no net tangible benefit. The claims include:

- unconscionable provision in a contract;
- breach of fiduciary duty; and
- unfairness.

Examples

Bautista, Jorge & Erika, Santa Cruz County (not filed). Homeowner induced by lender to purchase home that income would not support the interest payment. Put $70,000 in savings down on house.

Canlas, Ria & Rolando, San Mateo County, CIV 467920. Non-English speaking, fast food workers. Induced to purchase home where the income cannot cover the minimum interest payment.

DeLuna, Felipe & Martha, Santa Cruz County (not filed). Cannot speak or read English, induced to purchase home with loan where income cannot cover the minimum interest payment.

Hernandez, Ramon, Monterey (not filed). Cannot read or speak English. Induced to purchase home where income could not cover bare minimum interest payment.

Martinez/Ramirez, Santa Clara (not filed). Induced to purchase home where income could not cover bare minimum interest payment. Cannot read or speak English.

Mendoza, Jose Monterey, (not filed). Induced to purchase home where income could not cover bare minimum interest payment. Cannot read or speak English.

Romualdo, Fabian, Monterey, (not filed). Induced to purchase home where income could not cover bare minimum interest payment. Cannot read or speak English - Dayworker.

Valdovinos, Leopoldo, Santa Cruz, (not filed). Induced to purchase home where income could not cover bare minimum interest payment. Cannot read or speak English.

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Summary

Numerous cases against lenders and holders for the actions of the originators including (among other claims):

- constructive fraud;
- breach of duty of good faith and fair dealing.

Example

Carranza v. Option One Mortgage Lending, Inc., Indymac; filed in the Superior Court of California, in Los Angeles. Claims against the lender and the assignee include violation of the Unfair Business Act (B & P Code § 17200); constructive fraud; and breach of duty of good faith and fair dealing.

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Summary

Several cases against lenders and holders challenging net tangible benefit of mortgage loan, using, among other claims:

- Florida unfair trade practice claims.

Examples

Christina Bank & Trust, as Owner and Trustee of the Security National Funding Trust v. Peter Fernandes, et al, 12th Judicial Circuit Court for Manatee County, Florida, Case No: 2007-CA-6700. Defense of a mortgage foreclosure challenging bait and switch tactics on a high-cost adjustable-rate mortgage (ARM) against the assignee of the loan. Florida unfair trade practice claim pending along with other federal and state counts.

U.S. Bank National Association v. James Haggerty, et al., 12 Judicial Circuit Court for Manatee County, Case No: 2007-CA-4774. This case, also against the lender and the holder, involves a re-fi scam in which borrower was stripped of her equity and defrauded of title to her property (which might be construed to be a challenge under a net tangible benefit theory). Have Florida unfair trade practice claim against the broker and subsequent "purchaser" of the note.

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Summary

I litigate many predatory mortgages cases, both in defense of foreclosure and as affirmative claims. I regularly use the following state law claims:

- Georgia unfair trade practice;
- Georgia Residential Mortgage Act.

to challenge mortgage loans which are unaffordable, include illegal charges, or have other problems against the original lender and the assignee.

Example

Julien v. Ameriquest Mortgage Co., No. 1:06-CV-00320-CAP (N.D. Ga.).

Illinois - Legal Services

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Summary

The cases below are a sampling of the foreclosure cases and affirmative cases we have pending relating to predatory mortgage loans in East St. Louis, Illinois. We regularly include the following claims against the originators and the holders of these loans:

- unfair trade practices;
- unconscionable terms.

as well as other state and federal claims. Below are descriptions of a few of these pending cases.

Examples

Wells Fargo v. Cammie Palmer, et al., 05-CH-146 (St. Clair County, Illinois). Option One originated and Wells Fargo is the assignee who is seeking foreclosure. Affirmative defenses and counterclaims include (among others) unconscionability and violation of state consumer fraud law because the lender hired and supervised an appraiser that failed to follow uniform standards, did not determine loan's affordability at fully indexed rate, only at teaser rate.

Minnie Little v. Mortgage Lenders Network, USA, Inc., et al., 02-L-565 St. Clair County, Illinois). Minnie Little is a disabled woman who receives SSI. She is raising two daughters she adopted through the Illinois Department of Children and Family Services and receives adoption assistance. Ms. Little was close to paying off the home she was buying on a contract for deed basis when a mortgage broker and home improvement contractor convinced her to refinance her house and use the equity for home repairs. After doing some substandard work, the contractor absconded with the remaining funds. We have claims pending against all the actors, including the lender and the holder. In addition to a variety of other state and federal claims, the complaint alleges violations of the Illinois Consumer Fraud and Deceptive Business Practices Act. These allegations in the complaint include extending credit beyond ability to repay, switching Ms. Little from a 30-year fixed mortgage for which she applied to a 15-year balloon payment without any notice or expectation she'd be able to pay the balloon, including a prepayment penalty to go along with the balloon note, disbursing money to a contractor without assuring work was done and with indicia of problems with the contractor, not providing accurate and timely disclosures, and basing the loan on an inflated appraisal that did not accurately reflect the true value of the home.

Bank of New York v. Richardson, et al., 07-CH-852 (St. Clair County, Illinois). Aames originated the loan and the Bank of New York (formerly Bank One) is the assignee. In addition to a variety of federal and other state claims against both the originator and the assignee, we allege that Bank One knew of the problems in the loan and accepted assignment, and violation of the Illinois state consumer fraud law. The lender hired & failed to supervise appraiser who did not comply with uniform standards, lender made ARM loan that was unconscionable, lender accepted falsified documents from seller which it knew were falsified, assignee had actual knowledge of deceptions by lender, lender acted as assignee's agent by making loans to assignee's specifications.

In addition, we are litigating a number of cases relating to a widespread property flipping scheme in East St. Louis. There were over 80 property sales, all of which involved dilapidated homes being sold to unsophisticated, and often desperate, buyers just looking for a rental place to live. The seller plead guilty to mail fraud and is serving a 17 ½ year federal prison sentence. While the facts vary from case to case, we have alleged numerous counts of wrongdoing including consumer fraud against the lenders and their assignees. Each of these complaints allege falsified appraisals, falsified loan documentation created by the seller and others, and other unfair or deceptive acts. Many of the loans were extended beyond the borrower's ability to repay and almost all the borrowers have ended up in foreclosure, most within a very short time after closing. Many of the loans include unfair and unconscionable terms including balloon payments and adjustable rates that go as high as 17.25%. Many people were harmed by this scheme.

A) Ethel Hill v. Marvis Bownes, Meritage Mortgage, et al., 01-L-796 (consolidated with 02-LM-2055, 02-LM-2117, 04-L-66, 04-L-253) (St. Clair County, Illinois)
B) Option One Mortgage vs. Felecia McDougle, et al., 01-CH-251 (St. Clair County, Illinois)
Bank of New York v. Richardson, et al., 07-CH-852 (St. Clair County, Illinois)
C) Wells Fargo v. Cammie Palmer, et al., 05-CH-146 (St. Clair County, Illinois)
D) Wells Fargo v. Jeanette Norris, et al., 04-CH-97 (St. Clair County, Illinois)
E) Wells Fargo v. Gloria Neal, et al., 01-CH-396 (St. Clair County, Illinois)
F) Wells Fargo v. Denise Brown, et al., 00-CH-481 (St. Clair County, Illinois)

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Summary

We often bring claims under the Illinois state law prohibiting unfair practices, against holders/assignees of mortgage notes, relating to the origination practices. In the following two cases, the fees charged were far in excess of those normally charged in home mortgage transactions (a type of net tangible benefit claim) along with other irregularities. The first case is in the process of being settled, the second is in litigation.

Examples

ABN AMRO Mortgage Group, Inc. v. Coad, et al., Madison County, Case No. 04 CH 638. ABN is the holder and the unfair trade practice claim, based on the practices of the originator, was brought against ABN, the holder.

Washington Mutual Bank vs. Paulette M. Fuller, Madison County, Illinois, Case No. 04 Ch 753. The unfair trade practice claim was brought against assignee Washington Mutual.

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Summary

I represent clients in Massachusetts and Maine with predatory mortgages both to stop foreclosures and in affirmative actions. Claims against lenders and holders include the Massachusetts unfair trade practice (M.G.L.c.93A) raised to challenge the lack of net tangible benefit of the loan.

Example

Mary G. Noyes, U.S. Bankruptcy Court. Mrs. Noyes is a widow and aged 82 years. She and her son, Thomas V. Noyes of Newbury, Massachusetts received a subprime mortgage with Tribeca Lending Corporation, and then a foreclosure was filed on their residence brought by the holder/assignee of the mortgage. The complaint, seeking to stop the foreclosure, alleged numerous forged closing documents, the unlawful practice of law by one of Tribeca's employees, and most significantly, that the loan was not in the borrowers' best interest (a claim similar to no net tangible benefit). The Noyes paid $22,773.94 in closing costs and were in default on the loan with Tribeca within 3 months. Although there are several federal and state claims pending, the primary claim that will provide relief from this mortgage is the Massachusetts unfair trade practice claim.

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Summary

In New York, it is routine to hold the holder liable for the legal violations of the mortgage originator, as the courts have ruled on this question:

An assignee of a mortgage takes subject to all defenses and counterclaims that can be asserted against the assignor. *State Street Bank & Trust Co. v. Boayke,* 249 AD2d 535 (N.Y.A.D. 1998).

As a result, we regularly defend foreclosures and bring affirmative claims against originators and holders, based on New York unfair trade practices claims, among others.

Example

Tilton Jack v. American Brokers Conduit et al., United States District Court for the Eastern District of New York. The case was filed affirmatively; the borrower was not in foreclosure. This case is against an assignee in which the unfair trade practice (as well as the fraud) of the originator are two of our central claims. The client is an 82-year old widower who has owned his Brooklyn home for more than twenty years. In 2006, a mortgage broker/lender offered to refinance the client into a 1 percent mortgage, so that he could pay off debts and lower his monthly payment from $1,800 per month to $1,100 per month. Unbeknownst to the client, the 1 percent interest rate only lasted for one day. On the second day, the interest rate increased to 8.132 percent. The mortgage that the client received—a so-called Payment Option ARM loan—is one of the most complicated mortgage products marketed to consumers. In order for the client to make fully amortizing payments on the mortgage, he would initially have to pay about $2,830 per month, more than his monthly income. If the client chooses to pay the minimum payment, he causes his loan to amortize negatively, and when the principal balance of the mortgage reaches 110 percent, the minimum required payments will reach approximately $3,000/month—again, more than the client's monthly income.

The loan also contained a three-year prepayment penalty that increases in tandem with the negative amortization of the loan. Although the client provided the lender with documentation of his income (social security and pension), the lender opted to give him a stated-income loan, and blacked out all the income information on his income documents. Our claims are grounded in no net tangible benefit and making a loan which is unaffordable.

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Summary

In almost all of our predatory lending cases, we rely on these claims to save our clients' homes, and these cases are regularly against the holder:

- New York state unfair trade practice claims;
- unconscionability.

Examples

HSBC Bank USA, N.A., as Indenture Trustee for the Registered Noteholders of Renaissance Home Equity Loan Asset-Backed Notes, Series 2005-2 v. Anna B. Wilson et al., Kings County Supreme Court, Index # 2122/06.
Ms. Wilson is a 90-year-old woman on a very limited income. She was in a reverse mortgage and was deceived into leaving the reverse to enter into an Adjustable Rate Mortgage that was patently unaffordable. As a result, her home was foreclosed upon. To stop the foreclosure, we filed a counterclaim for unfair trade practice and used unconscionability as one of our affirmative defenses.

Petersen v. Aries Financial, LLC et al., United States District Court for the Eastern District of New York, Index # 06-cv-6663.
Ms. Petersen is a 74-year-old illiterate woman who was tricked into transferring her property to a sham LLC and then taking out a loan as the LLC with a 14% interest rate. She was not told about the LLC or the onerous terms of the loan, and instead was reassured by the broker and lender that this would allow her to save her home. Instead the loan cost her over $100,000 of equity and left her in a loan she cannot afford. In addition to other state and federal claims, the pleadings include claims based on unconscionability and unfair trade practice. Because the loan was taken out by a corporation (at least on paper) and our client was not staying at the property at the time she took out the loan, our federal claims are vulnerable and we are relying on our state law claims to save our client's home.

New Jersey - Legal Services

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Summary

The NJ law prohibiting unfair trade practices law is our state anti-predatory lending law. It is one of the most important tools in our toolbox. This state law, along with other state and federal laws, are essential tools, used often against lenders and assignees.

Examples

Hollis v. Deutsche Bank, US Bankruptcy Court Dist. Of NJ, Adversary Proceedings. Claims against the holder include New Jersey unfair trade practice, and aiding and abetting, as well as other claims. Multiple refinancing without regard to ability to repay and with no net tangible benefit. (Copy of the complaint **attached in Appendix C.**)

LaSalle v. Grizzle, Sup. Ct of NJ, Mercer County, Counterclaim, Third Party Complaint (defense of foreclosure). Claims against the holder include New Jersey unfair trade practice, and aiding and abetting, as well as other claims. Inflated appraisal, house flipped from foreclosure without improvements, unconscionable terms (net tangible benefit analysis).

Tribeca Lending v. Gilbert, Sup. Ct of NJ, Somerset County, Counterclaim, Third Party Complaint (defense of foreclosure). Claims against the holder include New Jersey unfair trade practice, and aiding and abetting, as well as other claims. Lending without regard for ability to repay, client was advised by originator to take out enough money to make a year of payments after which time they would refinance her into an affordable loan.

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Summary

In the past 24 months, I have litigated numerous mortgage cases which typically relate to loan origination or servicing claims. Most are filed in defense of foreclosure. In most cases, the current holder of the mortgage is sued in addition to mortgage brokers where applicable, originators and servicers.

In a typical mortgage origination case, the claims include:

- usury;
- state unfair trade practices;
- violations of the North Carolina Mortgage Lending Act.

The assignee is generally liable either as an assignee (unless the assignee affirmatively proves holder in due course status), or in the alternative, the assignee is directly liable for "taking" usurious payments in violation of North Carolina law.

Of the past 11 cases involving holders, 7 have settled. In one case the loan was canceled entirely. Without the participation of the holder, this result would not have been possible. In 5 cases, the clients received loan modifications that significantly altered their obligations to pay the holder, rendering the loans affordable and saving the homes. Of those 5, 4 loans were converted from adjustable to fixed rates. Each involved some degree of principle reduction. The 5th modified loan, a reasonable-tangible-net-benefit/high-cost-home-loan case, involved a principle reduction and interest rate reduction. Again, without the inclusion of the holder as a defendant, these results would not have been possible. Finally, one case settled for cash. The facts in that case were difficult, and the family was unable to keep the home.

I have several cases pending involving these claims, and many more waiting to be filed.

Because of confidentiality agreements, I am unable to provide specific details of these cases.

Ohio - Legal Services

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Summary

At the Equal Justice Foundation, we use the following claims regularly in predatory lending actions and as an affirmative defense to foreclosure against originators, servicers and holders:

- Ohio's Consumer Sales Practices Act (the Ohio unfair trade practice statute);
- unconscionability.

Examples

Beneficial Mortgage Co. of Ohio v. Leach, Franklin County Common Pleas Court, 1Case No. 99 CVE 5925

Fairbanks Capital Corp. v. Summerall, Franklin County Common Pleas Court, Case No. 101 CVE 7594

Olympus Servicing, LP v. McNeal, Franklin County Common Pleas Court, Case No. 02 CVE 8160

CIT Group/Consumer Finance v. Kemmer, Knox County Common Pleas Court, Case No. 104 FR 070286

First Tennessee Bank, NA v. Trotechaud, Franklin County Common Pleas Court, Case No. 06 CVE 3508

U.S. Bank NA as Trustee v. Clay, Franklin County Common Pleas Court, Case No. 05 CVE 10296

U.S. Bank NA as Trustee v. Smith, Fairfield County Common Pleas Court, Case No. 06 CV 1227

U.S. Bank NA as Trustee v. Yontz, Franklin County Common Pleas Court, Case No. 07 CVE 3230

Ohio - Legal Services

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Summary

I have been doing predatory mortgage lending work for legal aid programs in Dayton, Ohio since 2000. In my experience, most to almost all mortgage loans are assigned and/or securitized, often soon after they are made. A foreclosure is generally filed on behalf of an assignee. Meaningful relief to a borrower who faces unaffordable mortgage payments and/or an excessive total mortgage debt requires the ability to raise all claims against the holder of the loan, as it is only the holder of the loan who has the ability to void or change the terms of the loan.

We regularly use state claims such as the following to challenge the lack of affordability and other terms of these loans, using claims including:

- unfair trade practice;
- Ohio Mortgage Brokers Act;
- breach of fiduciary duty;
- undue influence;
- unconscionability.

Example

Louis J. Johnson v. First Horizon Home Loan Corp. US District Court, N.D. Ohio, W. Div. 3:07-cv-01260. (Holder will be added after discovery reveals the name.) This loan is barely affordable and soon will reset and will be unaffordable. Mr. Johnson's first mortgage is an exploding adjustable rate loan with 2 year teaser rate; his second mortgage has a balloon payment. Mr. Johnson is elderly and hard of hearing, bereaved, was on fixed income when the loan was originated. His home was over-appraised for more than it is worth. Claims against the lender include common law unconscionability, civil conspiracy with the broker, UDAP, violation of the Ohio Mortgage Brokers Act, breach of fiduciary duty, undue influence.

Ohio – Private Attorney

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Summary

We currently have over one dozen cases involving mortgage problems against holders of the loan using the following state claims:

- unconscionability;
- unfair acts and practices (Consumer Sales Practices Act in Ohio);
- breach of contract;
- breach of fiduciary duty.

Examples

Baldwin v. Foreclosure Solutions - Bankruptcy Adversary Action – 04-35811- U.S. Bankruptcy Court S.D. Ohio, - W.D. Bankruptcy adversary filed as part of Chapter 13 to prevent sheriff sale in foreclosure case. Claims on unfair practice under Ohio Act and unconscionability, negligence (as well as other violations) against the lender and the assignee. Loan involved issues of over-appraisal, foreclosure prevention scam, stated income loan and loan consolidation in new loan that was not supported by actual income of borrower. GMAC was assignee.

Clifford v. Countrywide – Federal Complaint – 2:07-CV 1226 – U.S. Federal District Court. S.D. Ohio – Columbus. Complaint filed against assignee involving multiple federal and state claims, including unfair trade practice, unconscionability, breach of fiduciary duty, breach of contract and civil conspiracy.

Studebaker & Mullins v ACC Capital Holdings (Ameriquest) et. al. – 3:07 CV 00421 – U.S. District Court, S.D. Ohio – Dayton. Complaint against lender and assignees (joinder of two borrowers) for overstated appraisals, bait and switch schemes regarding promised fixed rates and escrow versus receiving variable rate loans and no escrow (lack of affordability, no net tangible benefit). Claims include Ohio Mortgage Brokers Act, unconscionability, breach of fiduciary duty, breach of contract, negligent misrepresentation and professional negligence. Assignees are Citi Residential and Wilshire with Bank of New York and Deutsche as Trustee.

Deutsche Bank v Conway v. AMC Holdings (Ameriquest) et. al. 06- CV-06466, Montgomery County Ohio Common Pleas Court. Defense of foreclosure case against the assignee, following Chapter 7 bankruptcy. Affirmative defenses and third party complaint claims for terms and fees misrepresented to borrower and a promised fixed rate versus actual variable rate loan (potential for net tangible benefit analysis). Claims include breach of fiduciary duty, unconscionability, breach of contract, and Mortgage Broker Act violations. The assignee is Citi Residential.

Deutsche Bank v Bass v Dixon et. al 2006- CV- 00455 Montgomery County Ohio Common Pleas Court. Defense of foreclosure case following Chapter 7 bankruptcy. Affirmative defenses and third party complaint claims relate to the misrepresentation of loan terms and fees and the over appraisal of the property (could be a net tangible benefit analysis). Claims include breach of fiduciary duty, conspiracy and Mortgage Broker Act violations.

Ohio - Legal Services

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Summary

Cases include claims against assignees for making loans which are not affordable using, among others, the following claims:

- unconscionability;
- improvident lending;
- breach of fiduciary duty;
- negligence.

Example

Zeltner v. Midwest, Wood County Ohio. In this ongoing case against the assignee of the loan (the original lender is bankrupt) borrower who makes about $18,000 a year as a school bus driver tried to cancel the loans (one is a balloon piggyback) totaling $216,000 on her over-appraised home. The broker had the home for $248,000 but a retrospective appraisal reveals that at the time the loans were made the home value was only $165,000. After the homeowner canceled the loans, the broker convinced the borrower to sign the same, bad loans. These loans were processed as "no doc" loans. The now bankrupt lender, American Home Mortgage, did not want any income verification. Again the borrower attempted to cancel the loans (pursuant to Truth in Lending 3 day right of cancellation), but signs on the wrong line of notice of rescission and faxes to broker with a letter stating she can't afford the loans. Broker again promises to refinance. Her payments on these loans exceed her monthly income. Eight months after these bad loans were made, suit is filed. Common Law counts include unconscionability, improvident lending, fraud, negligence and breach of fiduciary duty.

Pennsylvania - Legal Services

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Summary

Regarding the importance of preserving unfair trade practice claims against holders in Pennsylvania:

1. The first three cases below involved purchase money mortgages. Unfair trade practice claims are often the only recourse for borrowers with predatory purchase money mortgages because HOEPA and TIL rescission do not apply to these purchase money mortgages.
2. Pennsylvania's unfair trade practice statute has a 6 year statute of limitations. As a legal services organization, our clients are unsophisticated and often don't come to us until well after the limitations period has run on federal claims. Often the unfair trade practice claim is our clients' only recourse.
3. Pennsylvania's statute includes a cancellation remedy for door-to-door transactions that is stronger than Truth in Lending rescission – if the lender does not honor the borrower's notice of cancellation, the entire debt can be cancelled. It's a very powerful remedy.

Examples

Joan Taylor v. MERS, Meritage Mortgage Corp., Resource Bancshares Mortgage Group, Inc.; Wilshire Credit Corporation; et al., 2002 . Filed in Pennsylvania Court of Common Pleas, removed to U.S. District Court E.D. Pa. by defendant title company. This case is a defense of a foreclosure and involves money damages. The state claims against the holder include unfair trade practice. The client is illiterate and as a first-time homebuyer was referred by housing counselor to a property flipper, who arranged financing for a house that was unlivable. There was an inflated appraisal and broker fee which the client never knew about and never authorized. The client sought a simple, 30-year, fixed-rate, prime rate mortgage. The broker pulled a bait-and-switch, and the client received two mortgages (80/20), the first an adjustable rate mortgage, the second a 15-year balloon mortgage with a 13.75% interest rate and prepayment penalty. The first mortgage included a yield-spread premium. The client rescinded the loan under the state unfair trade practice statute (using a net tangible benefit type analysis). The court granted summary judgment for lender on the federal and other state law claims, leaving only the unfairness claims against the holder for trial.

<u>Ronnetta Burton v. Bank of America, NationsCredit Financial Services Corp., et al.,</u> 2005 Philadelphia Court of Common Pleas. This case is a foreclosure defense and involves money damages. As the statute of limitations had run on all other state and federal claims the action was brought solely under the state <u>unfair trade practice statute</u>. This case involved a property flipping scheme. Flipper/seller sold the client an uninhabitable house, and promised repairs that were never made. The seller gave a mortgage to the client, then had Equicredit refinance the mortgage. Bank of America was current holder of loan. Client never knew of the refinancing. There was a complete failure to provide all required disclosures and there also was fraud and falsification of all the loan documents. The client was charged a broker fee, although she never knew about the broker and authorized payment. There were also improper charges for attorneys' fees, title insurance, as well as other mystery charges (payee identified, but not reason for charge.) This was a HOEPA loan, but no HOEPA notice was provided. No Truth in Lending notices of the right to rescind. The client was not credited with a down payment. All of this involves a net tangible benefit type analysis.

<u>Milagros Colon v. MERS</u>, GreenPoint Mortgage Funding, Inc. and Freddie Mac, 2006 – pending. U.S. Bankruptcy Court for E.D. Pa. Adversary complaint to proof of claim by MERS, foreclosure defense. The state claims here are unfair trade practice and unconscionability. This also involved a property flipping scheme. The illiterate, mentally retarded client purchased a house using seller arranged financing with a subprime purchase money mortgage with an interest rate of 9.125% and APR of 11.149%. Points, fees, and payoff of unsecured debts amounted to 22% of loan amount. Client's credit and income should have qualified her for a prime market loan, yet this was a "no doc" loan, even though the client receives SSI and this income could be easily verified. Client was required, as a condition of the loan, to pay off two accounts totaling close to $1000.00 held by debt buyers with loan proceeds, yet the debts were not client's. The client did not understand she was paying them and therefore could not object. The broker charged a mortgage broker's fee of 5% of the loan amount, although the client never met broker, had no idea a broker was involved, and there was no brokerage contract in violation of PA law. Client has no understanding of concept of mortgages, interest, settlement fees, etc., therefore could not shop for or negotiate better terms, did not understand she was getting a loan from a bank. The whole case boils down to a net tangible benefit analysis.

<u>Catherine Hill v. MERS</u>, 2006. Originally an adversary complaint objecting to proof of claim in U.S. Bankruptcy Court for E.D. Pa., removed to U.S. District Court for E.D. Pennsylvania. This is a foreclosure defense case involving a 2/28 ARM with an interest that only increases, can never go down. Client did not want an ARM. This is a HOEPA loan, and there are Truth in Lending and HOEPA disclosure violations. Additionally, there was a fraudulent notarization of mortgage. Interest rate increased from 8.625% to 10.75% at first rate change, causing the principal and interest payments to increase by 19%. Case uses a net tangible benefit type analysis. The claim most likely to save the home is the state unfair trade practice claim.

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Summary

I file cases challenging predatory mortgages using state law claims to challenge loans failure to have a net tangible benefit, often against assignee. Typical state claims include:

- unfair trade practice;
- breach of fiduciary duty.

Examples

Deneen v. Allied Home Mortgage Capital Corporation, et al. No. 1:07-cv-1425 - U.S. District Court for the Middle District of Pennsylvania. The case was filed against the lender and assignee to recover losses incurred by fraud of broker. The broker represented the loan to have a low interest rate that was fixed for five years, after which it would adjust. After the first month, the borrowers discovered that the adjustment was monthly beginning with month two of the loan. Claims, involving a net tangible benefit type analysis, include: i) violation of PA Unfair Trade Practices and Consumer Protection Law; and ii) breach of fiduciary duty.

Polinka v. United Medical Bank, et al. No. 06-6136 - Cumberland County, PA Court of Common Pleas. The case was filed under the state unfair trade practice statute against the holder to rescind a negative amortization loan where the lender misrepresented the terms and effects of the loan; the loan was inappropriate for the borrowers (a net tangible benefit type analysis), who have since filed a Chapter 7 bankruptcy. The lender's agents only disclosed to the borrowers just before closing that the loan had a negative amortization feature. The lender's representative understated the effect of the negative amortization during the five-year, pre-balloon period. Instead of the accrued interest being about $6,000, as represented, it will actually be about $30,000-$35,000. Claims include a violation of the Pennsylvania Unfair Trade Practices and Consumer Protection Law.

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Summary

Typically our cases challenging mortgage loans because they are unaffordable or do not benefit the borrower involve the following claims against the assignee:

- unfair trade practice;
- unconscionability.

Example

White Mountain Services Corp. v. Trice, Huntingdon County PA. The challenge was that the loan was unaffordable based upon the income of borrower. Claims included both unfair trade practice and unconscionability. Assignee was named as a defendant.

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Summary

In our mortgage cases challenging inability to pay and no benefit of the loan, we sue the assignee using state law claims which include:

- unconscionability;
- unfair trade practice.

Example

Deutsche Bank National Trust v. Deborah Cuculino, Philadelphia Court of Common Pleas, July Term 2007, No. 001003. The loan was made for the purpose of refinancing a prior mortgage to buy out a spouse's share in a divorce. The client had poor credit and had a difficult time qualifying for a loan. Someone in the closing process (I suspect the mortgage broker and title agent jointly) doctored the paperwork showing payoff amount for the prior mortgage to make it lower, thus allowing the client to qualify for the new loan. The end result is that the second loan did not pay off the first mortgage, and now she's facing foreclosure on both loans. In addition to the defenses of fraud, there are counterclaims under Pennsylvania' unfair trade practices statute.

In the mean time, the first mortgagee refused to accept the money that was sent unless my client signed a documents saying that she still owed additional money. Therefore, unconscionability is a defense to the foreclosure action in that "contract." All claims are against the holder of the mortgage.

Pennsylvania - Legal Services

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Summary

Currently, I have about ten cases in which unfair trade practice violations are plead as the main counterclaim and defense to foreclosure brought by the assignee.

Examples

McGee v. LaSalle Bank Nat'l Assn. as Trustee 2005-cv-5334-cv (Dauphin County Court of Common Pleas) Plead unfair trade practice violation for servicing and origination abuses. Led to favorable loan modification.

LaSalle Bank Nat'l Assn. as Trustee v. Rispoli, 2006-CV-4140-MF (Dauphin County Court of Common Pleas). In defense of foreclosure, plead unfair trade practice violation for servicing and origination abuses. Led to favorable loan modification.

McGee v. LaSalle Bank Nat'l Assn. as Trustee 2005-cv-5334-cv (Dauphin County Court of Common Pleas). Plead unfair trade practice violation for servicing and origination abuses. Led to favorable loan modification.

LaSalle Bank Nat'l Assn. as Trustee v. Rispoli, 2006-CV-4140-MF (Dauphin County Court of Common Pleas). In defense of foreclosure, plead unfair trade practice violation for servicing and origination abuses. Led to favorable loan modification.

Pennsylvania - Legal Services

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Summary

Working for the legal aid office in Philadelphia I've been representing homeowners in foreclosures for 10 years. During that entire time, at least half of the people who have come to us with foreclosures have been the victims of abusive subprime loans, usually refinancings of mortgages that had better terms or new loans against homes that were free of mortgage debt (elderly homeowners who had paid their mortgages off or family members who inherited homes that had been paid off). Right now, I have 87 active cases; half of them involve abusive subprime loans (the other half are foreclosures or bankruptcies on prime loans or miscellaneous consumer cases).

In 80% of my subprime loan cases (36 out of 45 cases), unfair trade practice claims or the common law defense of unconscionability are essential to any hope of my clients keeping their homes. I routinely use these claims quite successfully against the assignees of these loans (almost all loans are held by parties different than the original lender). The cases in which I do not rely on the state law claims are those in which I have a Truth in Lending rescission claim.) Assuming that these percentages are similar for my colleagues here, we have at least 200 active cases where unfair trade practice claims and unconscionability claims against assignees are vital to our homeowner clients. We are able to take just 1/3 of the foreclosure cases that come to us; we refer many subprime mortgage cases out to private attorneys, who also rely on unfair trade practice claims to represent the homeowners. Unconscionability is the most hopeful defense for the cases where the mortgage payment was never affordable for the homeowner but we cannot identify direct misrepresentations and reliance (as required for claims of fraud and, in Pennsylvania, unfair trade practice). Given that Truth in Lending does not protect borrowers from payments they cannot afford (the disclosures required by TILA are pretty useless in these circumstances, they tend to be incomprehensible to our very low income clients -- the most common reaction by my clients when I ask them why they signed for a loan they couldn't afford, "I didn't understand that I couldn't afford it, why would they give me a loan that I couldn't pay?"), the defense that a loan is grossly inequitable is often the only defense. Unconscionability can be raised against the party foreclosing, even if that party is a holder in due course, as the defense goes to the terms of the loan, not the opposing party, so we can represent more homeowners -- we don't have to plead in or separately sue the original lender. Trading this defense away would completely undermine our foreclosure defense practice for predatory subprime loans. **(See five attached complaints in Appendix D.)**

South Carolina – Private Attorney

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Summary

I represent homeowners trying to save their homes from foreclosure. I use the South Carolina unfair trade practice statute to raise problems with the affordability of the mortgage loans.

Example

Wells Fargo vs. Emily M. Harllin, pending in the Court of Common Pleas in Richland County, South Carolina. We have sued to affirmatively stop a foreclosure. The defendant is a 71-year-old woman who had a reverse mortgage. She had no house payment. Wells Fargo called her on the telephone and asked if she needed money. The next thing she knew she was in a loan which requires her to pay over $1800 per month. They falsified her income. We have sued under the State UDAP statute.

Washington – Private Attorney

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Summary

In my private practice, I represent many homeowners in their attempts to save their homes from foreclosure. I use unfair trade practice and unconscionability claims against lenders and holders on a regular basis. Below is one case that is, unfortunately, fairly typical, in both the fact pattern and the use of these claims:

Robertson v. New Century, King County Superior Court Case No. 06-2-33989-0SEA - Ms. Robertson is an elderly African American woman who has cleaned houses and cared for others all of her life. She owns her home because it was purchased by former employers for her. She was conned into a series of loans taking ever more equity from several lenders. Recently it started with Ameriquest, who used their typical practices to get her into a loan with massive fees, and she had no idea what she was signing. Within a couple of years, with ballooning mortgage payments, she was conned by a local broker into a loan with payments that exceeded her income. She realized that the payments were too high, but he told her to use the cash out to make the payments and then he would refinance her in a few years. She signed the first loan in 2002, another in 2004 and by 2006 was facing payments that were as much as her income. She scraped by because she was caring for another elderly ill woman at her home and receiving money for that work, but she was also out all the time looking for housecleaning and lawn mowing work to earn extra money. She was 89 years old and is now 90. In late 2006, I filed a lawsuit against the holder, New Century, Ameriquest, and the brokers. While I was litigating the case, unbeknownst to me, she was contacted by another broker in January 2007 who convinced her he was from New Century and could help her lower her payments. Instead he refinanced her again with New Century and I was required to file a separate lawsuit against the holder and the broker. Because of New Century's bankruptcy, if I cannot recover against the holder, my client will not have any form of recovery.

West Virginia - Legal Services

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Summary

Mountain State Justice, Inc. is a non-profit legal services office that handles hundreds of cases a year in which individuals face the loss of their homes to non-judicial foreclosure because they have been victimized by predatory lending practices. Currently, we have several hundred of these cases pending, and in the past five years we have used these claims to save several thousand homes from predatory mortgage lending and servicing. Essential to our ability to help these individuals save their homes is civil litigation in which we regularly assert common law claims and defenses against holders of these loans to address predatory lending practices in the origination and servicing of these loans. These cases almost always include claims for:

- unconscionable contract; and
- breach of the duty of good faith and fair dealing.

With respect to unconscionability claims, we are able to assert that entire loans and/or specific loan terms are void and unenforceable. These may include exploding adjustable rate loans, loans that exceed the actual market value of a home, loans underwritten without proper consideration of the borrower's ability to pay or whether it was beneficial to the borrower. The vast majority of the lawsuits we file to save people's homes include a count for unconscionable contract to remedy predatory loan origination arising out of the consumers' clear inability to pay to term at the time of origination, or the lack of substantial benefit of a refinancing to the borrower.

If we were unable to pursue the common law claims explained above, we would basically be stripped of our ability to save people homes, and hundreds of West Virginia families would lose their homes to foreclosure. These claims are by far the most effective mechanism to stave of foreclosures on predatory loans. Listed below are a few examples of the hundreds of cases in which such claims have been asserted against current holders of the loans**. (Also see two orders attached in Appendix E.)**

Examples

James Perry v. Wells Fargo Home Mortgage Inc., Civil Action No. 3:07-0217 (S.D. W. Va.)
Kathleen Bailey v. Beneficial West Virginia, Inc., Civil Action No. 05-2318 (Kan Cty Cir.

Ct) (Referred to arbitration).
Lillian Atkinson v. EMC Mtg. Corp, Civil Action No. 04-C-3162 (Kan Cty. Cir. Ct.).
Billy Ausbourne v. AMN-AMRO Mtg. Grp., Inc., Civil Action No. 04-C-95-S (Mer. Cty. Cir. Ct.).
Mary Jane Brown v. Saxon Mtg. Servs., Inc. Civil Action No. 07-C-2583 (Kan. Cty. Cir. Ct.)
Wavie Chappell v. Citifinancial, Inc. Civil Action No. 07-C-1594 (Kan. Cty. Cir. Ct.).
Audrey Crites v. Novastar Mtg., Inc., Civil Action No. 2:07-0104 (S.D.W. Va.).
Nancy Dix v. Flagstar Bnk., F.S.B, Civil Action No. 06-C-442 (Kan. Cty. Cir. Ct.).
John Jordan v. Wells Fargo Home Mtg. Inc., Civil Action No. 06-C-721 (Kan. Cty. Cir. Ct.).
Larry Lantz v. National City Mtg. Co., Civil Action No. 05-C-72 (Barbour Cty. Cir. Ct.).
Lillie Rose v. Wells Fargo Home Mtg., Inc., Civil Action No. 07-C-1593 (Kan. Cty. Cir. Ct.).

West Virginia – Private Attorney

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Summary

Unconscionability and unfair trade practice claims are the primary claims that I use in my practice. In the few years that I have been practicing, I have never filed a case in West Virginia that did not concentrate on those claims. They are regularly and successfully used against assignees of the loans. I personally regard the unconscionability claim as my greatest weapon against predatory lending. In West Virginia, it allows for voiding the loan altogether, actual damages, including emotional distress damages, and attorney fees. The purpose of unconscionability claims is to prevent oppression and unfair surprise by a party with superior bargaining power. Therefore, it is invaluable to successfully litigating these cases. Without these state law claims against holders, I, as a private practitioner, will not be able to continue taking these cases. The federal statutory claims provide insufficient remedies for my clients and, likewise, provide little incentive to for-profit lawyers for taking these cases on.

Examples

Ameriquest Mortgage Company v. Eugene and Debra Brown, Ohio County, West Virginia, Civil Action No. 03-C-471. The Browns, who are uneducated and unsophisticated African-Americans, were duped by Ameriquest into giving up an affordable, beneficial and prime loan for an oppressive, sub-prime loan that was destined for foreclosure. Ameriquest used a number of ploys to mislead the Browns, including: quoting an un-escrowed monthly payment as escrowed, baiting with terms that it did not intend to provide and switching the terms at the closing table, and fabricating the Browns' income while ignoring contrary income documentation that the Browns had provided when qualifying for the loan. The Ameriquest loan provided the Browns with less than $6,000 in new proceeds. For this meager sum, the Browns were charged more than $4,600 in closing costs. Moreover, the loan was not affordable and provided no benefit to the Browns. Instead it caused their payments to increase, significantly increased their total debt load, stripped them of thousands of dollars in home equity, reduced their available money because of the drain cost by the high payments, and set their course towards losing their home to foreclosure. My firm got involved in this matter after the Browns lost title to their home and were facing eviction. We brought both unconscionability and unfair trade practice claims. There were no federal statutory claims pled. Public records reveal that the Browns currently are living in their home, and there are no liens on it. Although Ameriquest originated the loan and continued to service it, it packaged it and sold it for securitization.

John William Hazlett and Aylea Zulieka Hazlett v. Homecomings Financial Network, Inc., et al., Marshall County, West Virginia, Civil Action No. 07-C-280, pending. This case involves a fraudulent appraisal (mobile home appraised as a stick built home); unprofessional closing; and no consideration of the ability to repay in "underwriting" the loan. Both unconscionability and unfair trade practice have been pled. The holder is included in the litigation. No federal statutory claims.

David and Lisa Millhouse v. Homecomings Financial Network, Inc., a corporation, Creve Coeur Mortgage Associates, Inc., a corporation, Samuel I. White, P.C., and Sarah A. Crichigno, Lucille A. Forsch d/b/a L.A. Forsch & Co., Ohio County, West Virginia, Civil Action No. 07-C-187, pending. This case also involves a fraudulent appraisal and lack of prudent underwriting. Both unconscionability and unfair trade practice claims have been pled. No federal statutory claims.

Deutsche Bank National Trust Company v. Glenn and Nanetta Pevarski v. Ameriquest Mortgage Company, Washington County, Ohio, Case No. 06FR531, pending. This case is very similar to Brown and includes: bait and switch tactics in selling the loan, which include morphing a fixed rate loan to an ARM, and the falsification of income by Ameriquest. Because the loan was not affordable, the Pevarskis are facing foreclosure. Unconscionability has been pled.

HSBC Bank USA, Inc. v. Ruby Dianne Strauss, Belmont Co., Ohio, Case No.06CV489, pending. This case involves a fraudulent appraisal; unprofessional closing; and no consideration of the ability to repay in "underwriting" the loan. Unconscionability has been pled.

The above are just examples; there are other cases as well.

APPENDIX B

IN HAND
02-25-08
S.A.S. M.+F
MASS A.G OFFICE
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COMMONWEALTH OF MASSACHUSETTS

SUFFOLK, SS.

SUPERIOR COURT
CIVIL ACTION
NO. 07-4373-BLS1

COMMONWEALTH OF MASSACHUSETTS,
Plaintiff

vs.

FREMONT INVESTMENT & LOAN, and FREMONT GENERAL CORPORATION,
Defendants

FINDINGS OF FACT AND CONCLUSIONS OF LAW ON PLAINTIFF'S MOTION FOR A PRELIMINARY INJUNCTION

The defendant Fremont Investment & Loan ("Fremont" or the "Bank") is a California state-chartered industrial bank that, between January 2004 and March 2007, originated 14,578 loans to Massachusetts residents secured by mortgages on owner-occupied homes. Of those loans, only roughly 3,000 remain active; roughly 2,500 continue to be serviced by Fremont. Most of these loans were made in what has become known as the "sub-prime" market, in which customers who generally would not have qualified for traditional prime mortgages were provided loans at higher rates of interest. Not surprisingly, in these times, a significant number of these loans are in default and Fremont seeks to foreclose on some of them. On October 4, 2007, the Commonwealth of Massachusetts, acting through the Massachusetts Attorney General, filed the instant complaint alleging that Fremont, in its past lending practices in the sub-prime market, has engaged in unfair and deceptive acts or practices in violation of G.L. c. 93A, § 2. The Attorney General now moves for a preliminary injunction that would bar Fremont, during the pendency of this action, from initiating or advancing any foreclosure on any residential mortgage loan in Massachusetts without the written consent of the Attorney General's Office.

BACKGROUND

On March 7, 2007, after having being advised of charges of unsound banking practices brought against it by the Federal Deposit Insurance Corporation ("FDIC"), Fremont, without admitting the alleged charges, entered into a Stipulation and Consent to the Issuance of an Order to Cease and Desist ("Consent Agreement"). Under the Consent Agreement, Fremont was ordered to cease and desist from, *inter alia*:

- (b) "operating the Bank without effective risk management policies and procedures in place in relation to the Bank's primary line of business of brokered subprime mortgage lending;"

- (d) "operating with inadequate underwriting criteria and excessive risk in relation to the kind and quality of assets held by the Bank;"

- (f) "operating with a large volume of poor quality loans;"

- (g) "engaging in unsatisfactory lending practices;"

- (l) "marketing and extending adjustable-rate mortgage ("ARM") products to subprime borrowers in an unsafe and unsound manner that greatly increases the risk that borrowers will default on the loans or otherwise cause losses to the Bank, including ARM products with one or more of the following characteristics:

  (i) qualifying borrowers for loans with low initial payments on an introductory or "start" rate that will expire after an initial period, without an adequate analysis of the borrower's ability to repay the debt at the fully-indexed rate;

  (ii) approving borrowers without considering appropriate documentation and/or verification of their income;

  (iii) containing product features likely to require frequent refinancing to maintain an affordable monthly payment and/or to avoid foreclosure;

  (iv) including substantial prepayment penalties and/or prepayment penalties that extend beyond the initial interest rate adjustment period;

  (v) providing borrowers with inadequate and/or confusing information relative to product choices, material loan terms and product risks, prepayment penalties, and the borrower's obligations for property taxes and insurance;

  (vi) approving borrowers for loans with inadequate debt-to-income analyses that

> do not properly consider the borrowers' ability to meet their overall level indebtedness and common housing expenses; and/or
>
> (vii) approving loans or 'piggyback' loan arrangements with loan-to-value ratios approaching or exceeding 100 percent of the value of the collateral;" and

- (m) making mortgage loans without adequately considering the borrower's ability to repay the mortgage according to its terms."

Consent Agreement at 2-4.[1]

On or about July 10, 2007, Fremont and the Massachusetts Attorney General entered into a Term Sheet letter agreement ("Term Sheet") that set forth a procedure that Fremont agreed to follow before foreclosing on any of the Massachusetts residential mortgage loans it continued to own or service. In a nutshell, under the Term Sheet, Fremont agreed to provide the Attorney General with the Loan Documentation regarding a troubled loan at least 90 days before commencing any foreclosure proceeding.[2] During that 90 day period, the Attorney General could object to the foreclosure, and state her reasons for doing so. If there were an objection, Fremont agreed not to proceed with the foreclosure and instead to negotiate in good faith to resolve the Attorney General's objection, perhaps by agreeing to revise the terms of the loan or arranging for replacement financing. If no resolution could be reached, Fremont was free to proceed with foreclosure, but only after giving the Attorney General fifteen days advance notice, which

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[1] As has already been noted by the Court, this Consent Agreement was a settlement of the charges brought by the FDIC, without any admission of wrongdoing by Fremont. As a result, this Court does not consider this Consent Agreement to be evidence that Fremont had engaged in any of the conduct it agreed to "cease and desist" from doing in the future. This Court discusses the Consent Agreement, not because it is evidence of Fremont's past conduct (which it is not), but because it is too important a part of the background and context of this action to be ignored.

[2] Under certain conditions, Fremont could ask the Attorney General to expedite her review of the Loan Documentation and wait only 45 days before commencing a foreclosure proceeding.

allowed her time to determine whether she would seek to enjoin the foreclosure.

Pursuant to this Term Sheet agreement, Fremont sent the Attorney General the Loan Documentation for 119 loans subject to a 90 day review. On October 4, 2007, the Chief of the Consumer Protection Division of the Attorney General's Office wrote that the Attorney General objected to foreclosure as to all of them. Fremont had also sent the Attorney General the documentation for another 74 loans which it wished to foreclose upon, subject to an expedited 45 day review. As to each of the 74 loans, Fremont represented that the homes to be foreclosed upon were not owner-occupied and that Fremont had been unable to contact the borrower, despite repeated attempts to do so. As to these 74 loans, also on October 4, the Attorney General objected to foreclosure as to only one. In short, on October 4, 2007, the Attorney General objected to every foreclosure proposed by Fremont except as to those loans where the home was not owner-occupied and Fremont had been unable to contact the borrower. That same day, it filed the complaint in the instant action.

The Term Sheet agreement was terminable at will by either party. On December 10, 2007, Fremont exercised its right to terminate in a letter to the Attorney General, writing that "it is now apparent that the Attorney General has no intention of engaging in a meaningful review process on a borrower-by-borrower basis, but rather is seeking wholesale discontinuance of all foreclosure referrals and sales." In that same letter of termination, Fremont stated that it was committed to continue to attempt loan modifications and other means of "workout" to avoid foreclosure, and would continue to provide the Attorney General with a loan file prior to referring the loan for foreclosure.

With the Term Sheet agreement no longer in force, the Attorney General asks this Court to enjoin Fremont from initiating or advancing any foreclosure without the Attorney General's written consent. Alternatively, she proposes a more limited preliminary injunction in which Fremont would be enjoined from initiating or advancing any foreclosure of what she characterizes as "Presumptively Unfair Loans," which she defines as ARMs with a low introductory rate of three years or less in which either (a) the combined loan-to-value ratio was 90 percent or higher, (b) the loan was approved on a "stated income" basis, meaning that Fremont essentially accepted the borrower's statement of income without requiring verification, or (c) the loan had a prepayment penalty. However, the Attorney General offered one exception to the prohibition on foreclosure of Presumptively Unfair Loans – Fremont could proceed with the foreclosure if it could demonstrate the presence of one of three Mitigating Factors: (1) the borrower consented in writing to the foreclosure, (2) the property was vacant and uninhabitable, or (3) the property was a vacant investment property. The Attorney General would have 45 days to verify the existence of the Mitigating Factor and determine whether to dispute it. If she did dispute it, Fremont would need the approval of the Court to proceed with the foreclosure. As to loans that were not Presumptively Unfair, under the alternative proposed by the Attorney General, Fremont would be required, as under the Term Sheet agreement, to provide the Attorney General with loan documentation at least 90 days prior to initiating the foreclosure and, if she objected to the foreclosure, Fremont would need court approval before proceeding with the foreclosure.

FINDINGS OF FACT

"By definition, a preliminary injunction must be granted or denied after an abbreviated presentation of the facts and the law." Packaging Industries Group, Inc. v. Cheney, 380 Mass. 609, 616 (1980). In other words, in finding the facts on a motion for preliminary injunction, this Court must "play the cards it is dealt," which may be a far more modest deck than it may be dealt at trial, after discovery has been completed. Consequently, the preliminary findings of fact below are based on the affidavits and attached exhibits furnished by the parties, as well as reasonable inferences from that evidence.

During the relevant time period in question – January 2004 to March 2007, when Fremont stopped originating residential mortgage loans – Fremont was a substantial lender in the sub-prime mortgage market. It is difficult to ascertain from this record what percentage of Fremont's residential loans could fairly be characterized as sub-prime loans, but this Court estimates that it was between 50-60 percent.[3] In all (or virtually all) of these loans, Fremont did not interact directly with the borrower. Rather, these loans were brought to Fremont by mortgage brokers who were independent contractors, compensated through a broker's fee that was paid upon the closing of the loan. Typically, the broker would contact one of Fremont's account executives to request a certain loan product and provide the borrower's credit report and loan application. The account executive would determine if the prospective borrower was "prequalified" and, if so, send the broker a non-binding interest rate quote on the requested loan product, and set forth the conditions the borrower needed to meet to obtain the loan. Once the borrower had agreed to proceed with the loan, the broker would send the account executive the documentation necessary to satisfy the prequalification conditions, generally the appraisal of the property, the required disclosures, and documentation regarding employment and income. All of this information was then sent to an account manager at one of Fremont's operation centers, where it would be examined by the underwriting department for final approval. If approved, the loan would

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[3] 38.4 percent of the loans were fixed rate loans, which this Court assumes were generally not sub-prime. This Court infers that the vast majority of the 64 percent of loans that were ARMs were sub-prime, in large part because a substantial percentage of Fremont's loans – 38.4% – were "stated income" loans, and this Court expects that all or virtually all of these "stated income" loans were sub-prime ARMs.

proceed to closing, with the Bank retaining an attorney to protect its interests at the closing.

As noted, 38.4 percent of these loans were "stated-income" loans in which the borrower was permitted to state his income without having to provide the usual verifying documentation, such as income tax returns, W-2s, or pay stubs. For these loans, the only "underwriting" that Fremont did regarding the income stated was to compare the salary stated with the salary typical for such an occupation in that geographic area, using data obtained from salary.com. These loans were, in theory, designed for those borrowers who could not verify their income with income tax returns or who had unreported income, but the extraordinarily high percentage of these loans – 38.4 percent – strongly suggests that they were not limited to these rather unusual circumstances. Since there was a substantially greater risk that the borrower had inflated his income with "stated-income" loans, the borrower paid a higher interest rate than for documented loans.

The very essence of a sub-prime mortgage loan is that the bank is lending money to a borrower who poses a greater than average credit risk, and demands a higher rate of interest in return for that increased risk. In order to reduce the interest rate, virtually all Fremont sub-prime mortgages were ARMs, with a low introductory rate (pejoratively referred to as a "teaser rate") which would continue generally for two or three years, at which time the loan would be adjusted to a variable rate based on a market rate of interest – the 6-month London Interbank Offered Rate ("LIBOR"), plus an additional percentage to reflect the high risk of the loan (known as the "rate add," e.g. LIBOR plus 5). The introductory rate would be considerably lower than the adjusted rate, so the amount of mortgage interest would substantially increase once the adjusted rate kicked in even if the LIBOR had not changed or had even fallen (known as "payment shock"). Most ARMs limit the extent of the payment shock by limiting the percentage increase that may occur during each period of adjustment, so the adjustable interest rate would increase with each adjustment until it would reach the LIBOR plus the rate add (but not exceed the maximum interest rate cap). Most of the ARMs that Fremont provided were 2/28 or 3/27, meaning they were 30 year loans where the introductory rate remained for two or three years, with adjustments every six months after the introductory period. The lower the introductory rate and the lower the limits on the interest rate increase that may occur upon each adjustment, the longer it would take for the actual interest rate to reach the LIBOR plus the rate add. Once it reached that level, the interest rate would increase or decrease based on changes in the market rate of interest.

In determining whether a borrower qualified for the loan, Fremont's underwriting department generally looked at the debt-to-income ratio, that is, the ratio between the borrower's monthly debt payments (including the applied-for mortgage) and his monthly income. While there were exceptions, generally the borrower needed to have a debt-to-income ratio less than or equal to 50 (sometimes 55) percent in order to qualify.[4] In calculating the prospective borrower's monthly debt payments, Fremont's underwriters used the monthly mortgage payments for the introductory period, not the monthly mortgage payment that would be due under the "fully indexed rate," that is, the LIBOR at the time of the inception of the loan plus the rate add. As a result, many marginal credit risks qualified for ARMs based solely on the low introductory rate, but would not have qualified using the fully indexed rate.[5]

Even relying on the low introductory rate to determine the debt-to-income ratio, there

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[4] For all of Fremont's originated loans during the relevant time period, which included both fixed rate loans and ARMs, the average debt-to-income ratio was 42.76 percent.

[5] The evidence in the preliminary injunction record does not permit this Court to infer the percentage of overall borrowers who would fit into this category, or their overall number. The evidence is sufficient to infer that the number of these borrowers was substantial, based on Fremont's willingness to lend to poor credit risks and the substantial difference between the debt burden with the introductory rate vs. fully indexed rate.

were still interested borrowers who did not qualify. For these borrowers, Fremont offered what it called an extended amortization option, which was essentially a 40 year note, with monthly payments reduced from the 30 year note because they were spread out over the 40 year period, with a balloon payment due at the end of 30 years (since the loan would not be fully amortized by that time). 12.2 percent of all Fremont's originated loans contained this extended amortization option with a balloon payment after 30 years.

Not surprisingly, the poor credit risks who were the target audience for sub-prime mortgage loans also often had little or no savings, so Fremont offered borrowers mortgage loans that required little or no down-payment, referred to in the lending industry as loans with a loan-to-value ratio equal to or approaching 100 percent. While some first mortgages provided 100 percent financing, most 100 percent financing was accomplished with a first mortgage providing 80 percent financing and a second mortgage providing the remaining 20 percent financing, referred to in the industry as "piggy-back loans."

The benefit to consumers from sub-prime mortgages was that they were eligible to obtain mortgages they would not otherwise have been eligible to obtain, albeit at higher rates of interest, and thereby could purchase homes they would not otherwise have been able to purchase. Consumers obtaining sub-prime mortgages shared the same risks that every person faced who stretched themselves financially to purchase their home – the usual danger of being unable to meet the mortgage payments because of a future reduction in income from the loss of a job or a sudden increase in other expenses, perhaps resulting from an illness in the family. These risks were greatest for those borrowers with the highest debt-to-income ratios and the fewest assets, since they had no cushion to deal with financial adversity. Some of these consumers, however, faced an especially grave risk – those with 2/28 or 3/27 ARMs with low introductory rates, who qualified for a mortgage only based on those low introductory rates and would not have otherwise qualified if the fixed index rate had been used by Fremont's underwriting department to determine eligibility. As to these loan customers, when the payment shock set in, their debt would exceed 50% of their income, sometimes by a considerable amount, and they foreseeably could no longer afford to pay the mortgage. These customers, often relying on the advice of their mortgage broker, generally understood that they would need to refinance the loan at or before the date the introductory rate ended so that they could continue to pay the low monthly payments provided by the so-called teaser rate and avoid the payment shock that would force them into foreclosure. However, what these customers often did not understand was that, if they had purchased a 100 percent financing mortgage, whether through a single loan or piggyback loans, they would only be eligible for refinancing if the fair market value of their property increased during those two or three years of the introductory rate because, if it fell, they would not be able to refinance their home for more than it was worth. For these borrowers, unless their income considerably increased, they would be doomed to default and foreclosure if the housing market fell (as, of course, it did).

Consequently, it is hardly surprising that when the Attorney General looked carefully at the Loan Documentation that Fremont provided on August 30, 2007 regarding 98 loans that it proposed to foreclose it found that:

- All 98 were ARMs. 93 had two year introductory rates, while four had a three year rate.
- All would produce payment shock when the introductory rate period concluded. The introductory rate on these loans varied from 6.1 percent to 12.4 percent. The payment shock increase could increase the interest rate 3 percent, with the potential of another 1.5 percent interest hike every six months.

- 90 percent of the 98 had a 100 percent loan-to-value ratio.[6]

14 of the 98 loans had a prepayment penalty, in which the borrower was required to pay up to six months worth of interest if he paid off the note (through sale or refinancing) before a designated period. For 13 of these 14, the prepayment penalties applied only during the introductory period; [7] for one, it extended through the first year of the payment shock period. Consequently, for these borrowers who were eligible for the loan only because the teaser rate was used to calculate the debt-income ratio, the timing of refinancing was critical – they could not afford to pay the mortgage after payment shock set in but they would pay a substantial prepayment penalty if they refinanced during the introductory period. Consequently, these borrowers had little real discretion as to when to refinance; for all practical purposes, it was essential that they close on the refinanced loan right when the introductory rate ended. If they were unable to refinance during this brief window, they would be unable to afford the mortgage payments, which would place them in default, which would increase the amount needed to refinance, which would make it even harder to qualify for the refinancing.

All of the dangers this Court has cited are present even if the loan application accurately states the borrower's income. All of these dangers obviously are exacerbated if the loan application wrongly inflates the borrower's income or assets, because then the debt-to-income ratio used by underwriting to determine whether the prospective borrower qualifies for the loan is based on an inflated income figure. It is too strong to say that "stated income" loans invite the

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[6] 30 of the 98 loans were structured to amortize over 40 or 50 years, with a balloon payment due on the 30th year. While it is not surprising to find these loans in trouble, the record sheds no light as to whether extended amortization loans were more difficult to refinance.

[7] 12 imposed prepayment penalties over two years; 1 imposed it only for the first year of the loan.

borrower to commit such fraud, because the borrower is required to state his income on the loan application under the pains and penalties of perjury. However, it is fair to infer that "stated income" loans present a far greater risk of fraud than full documentation loans, because not only is the lender for these loans not requiring any documentation of the borrower's income, expenses, or employment but the lender is also implicitly telling the borrower that it will not verify the borrower's statements on the loan application by looking at these documents. Not surprisingly, 50 of the 98 loans in the Attorney General's sample of loans targeted by Fremont for foreclosure were "stated income" loans.[8]

The preliminary injunction record reflects that, at least in a few of these mortgage loans, the loan application falsely described the borrower's occupation and substantially inflated the borrower's income. Specifically, the Attorney General submitted eight affidavits from lenders facing foreclosure. In six of these applications, the borrower's stated income was substantially inflated on the loan application. In each of these six false loan applications, this Court finds that the mortgage broker either prepared the loan application and inflated the income without the borrower's knowledge or permission (even though each borrower signed the loan application under the pains and penalties of perjury) or acted in complicity with the borrower in misrepresenting the borrower's income in order for the borrower to qualify for the loan. There is no evidence that Fremont knew of these misrepresentations. Nor is there any evidence that Fremont willfully blinded itself to the fact that some of the mortgage brokers who brought loans to it were knowingly inflating the borrower's income. Nor does this Court find, based on this record, that Fremont recklessly supervised its brokers by continuing to do business with them

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[8] The affidavit of the Attorney General's financial investigator who conducted this analysis is unclear as to whether the actual number of the "stated income" loans was 50 or 60. This Court has chosen the lower number, thereby giving Fremont the benefit of the ambiguity.

after Fremont learned that the brokers had a pattern or practice of inflating the borrower's income on the loan applications they had submitted. In short, with respect to the falsified loan applications, the evidence in the record reflects that Fremont was a victim of these misrepresentations and did not encourage or tolerate them.

Nor does this record reflect that Fremont made false representations to borrowers regarding the terms of their loan. From the few closing documents that are before the Court, there is no evidence that the terms were concealed or misrepresented in the closing documents. Nor is there any evidence that Fremont representatives made such misrepresentations. Indeed, apart from the closing attorney that Fremont retained, the borrowers who submitted affidavits did not appear to speak directly with any Fremont representative; they spoke only with their mortgage broker. To be sure, there is evidence that, in some of the loan transactions, the brokers had mischaracterized the loan terms and made vague promises of refinancing that they reneged upon when the time for refinancing arose, but there is no evidence that Fremont joined in making any of these misrepresentations or baseless promises or even knew of them. There is also evidence that at least some of the borrowers either did not read the closing documents or did not truly understand their terms, but this Court does not find Fremont responsible for that misunderstanding, especially since many of the loan documents are forms required under federal law.

The remaining question, then, for this Court is whether the Attorney General is likely to prevail in proving that certain of the sub-prime mortgage loans offered by Fremont were, as the Attorney General describes it, "structurally unfair," whose issuance was an unfair act or practice in violation of G.L. c. 93A, § 2. This Court will address that question in its Conclusions of Law.

CONCLUSIONS OF LAW

G.L. c. 93A, § 2(a) makes unlawful any "[u]nfair or deceptive acts or practices in the conduct of any trade or commerce." G.L. c. 93A, § 2(a). The Supreme Judicial Court has stated "that the following are 'considerations to be used in determining whether a practice is to be deemed unfair: (1) whether the practice ... is within at least the penumbra of some common-law, statutory, or other established concept of unfairness; 2) whether it is immoral, unethical, oppressive, or unscrupulous; (3) whether it causes substantial injury to consumers (or competitors or other businessmen).'" Datacomm Interface, Inc. v. Computerworld, Inc., 396 Mass. 760, 778 (1986) quoting PMP Assocs., Inc. v. Globe Newspaper Co., 366 Mass. 593, 596 (1975), quoting 29 Fed. Reg. 8325, 8355 (1964). An act or practice that is deceptive or fraudulent may be found to be unfair, but an act or practice need not be deceptive or fraudulent to be unfair. See Massachusetts Farm Bureau Federation, Inc. v. Blue Cross of Massachusetts, Inc., 403 Mass. 722, 729 (1989). An act may be unfair even if it does not violate a statute, or a regulation issued under G.L. c. 93A, § 2. See Schubach v. Household Finance Corp., 375 Mass. 133, 137 (1978) ("We reject the argument that an act or practice which is authorized by statute can never be an unfair or deceptive act or practice under § 2(a) of G.L. c. 93A."). "[W]hether an act or practice violates a statute or rule promulgated under G.L. c. 93A, § 2, is but one of several factors to be applied to all the circumstances of the transaction ... in determining whether it is unfair or deceptive." Billingham v. Dornemann, 55 Mass. App. Ct. 166, 176 (2002). Similarly , as the Supreme Judicial Court has made clear, an act may violate Chapter 93A without constituting a cause of action under any common law tort:

> Chapter 93A is "a statute of broad impact which creates new substantive rights and provides new procedural devices for the enforcement of those rights." Slaney v. Westwood Auto, Inc., 366 Mass. 688, 693 (1975). The relief available under c. 93A is "sui generis. It is neither wholly tortious nor wholly contractual in nature, and is not

> subject to the traditional limitations of preexisting causes of action." Id. at 704. It "mak[es] conduct unlawful which was not unlawful under the common law or any prior statute." Commonwealth v. DeCotis, 366 Mass. 234, 244 n. 8 (1974). Thus, a cause of action under c. 93A is "not dependent on traditional tort or contract law concepts for its definition." Heller v. Silverbranch Constr. Corp., 376 Mass. 621, 626 (1978). See Nei v. Burley, 388 Mass. 307, 313 (1983) ("[A]nalogies between common law claims for breach of contract, fraud, or deceit and claims under c. 93A are inappropriate because c. 93A dispenses with the need to prove many of the essential elements of those common law claims").

Kattar v. Demoulas, 433 Mass. 1, 12-13 (2000).

Here, at the time that Fremont issued the mortgage loans at issue in this motion, there was no federal or Massachusetts statute or regulation applicable to all mortgage loans that expressly prohibited Fremont from issuing adjustable rate mortgage loans, loans with a loan-to-value ratio of 100 percent, "stated income" loans, or loans with a prepayment penalty. Nor was there any federal or Massachusetts statute or regulation applicable to all mortgage loans that provided that a borrower could not qualify for a mortgage loan if his debt-to-income ratio exceeded 50 percent or some other percentage ceiling. Nor was there any federal or Massachusetts statute or regulation applicable to all mortgage loans that prohibited these practices from occurring together – that is, there was no federal or Massachusetts statute or regulation that expressly declared that a bank could not issue a 2/28 ARM, stated income loan with a loan-to-value ratio of 100 percent and a prepayment penalty for the early payoff of that loan (through sale or refinancing) to a borrower with a debt-to-income ratio exceeding 60 percent. Nor is there any indication from the record that it was unusual for sub-prime lenders to engage in any or all of these practices.

There were, however, Massachusetts statutes and regulations that prohibited many of these practices in "high cost mortgage loans," defined as a loan secured by the borrower's principal dwelling in which:

- for a first mortgage, the interest rate exceeded by more than 8 percentage points the yield on United States Treasury securities having comparable maturity periods,

<u>or</u>

- the total points and fees were greater than 5 percent of the total loan or $400, excluding up to 2 "bona fide loan discount points" paid by the borrower to lower the benchmark rate of interest.

G.L. c. 183C, § 2. The Predatory Home Loan Practices Act ("the Act"), enacted on August 9, 2004 and made effective on November 7, 2004, prohibited lenders from making a "high cost mortgage loan" "unless the lender reasonably believes at the time the loan is consummated that 1 or more of the obligors will be able to make the scheduled payments to repay the home loan based upon a consideration of the obligor's current and expected income, current and expected obligations, employment status, and other financial resources other than the borrower's equity in the dwelling which secures repayment of the loan." G.L. c. 183C, § 4. The Act provided lenders with a safe harbor in making a reasonable determination regarding the borrower's ability to repay – if the borrower's debt-to-loan ratio was 50 percent or less, the borrower was presumed able to make the scheduled payments. <u>Id.</u> See also 209 CMR 32.34(c) (same). The Act also prohibited lenders from adding prepayment fees or penalties to high cost mortgage loans. <u>Id.</u> at § 5. A violation of the Act was deemed a violation of Chapter 93A. <u>Id.</u> at § 18(a).

The spirit of the Act is that a lender engages in predatory lending, which is an unfair act in violation of Chapter 93A, when it makes a loan charging either high points, fees, or interest to a borrower whom the lender reasonably believes will be unable to make the scheduled payments and will therefore face the likelihood of foreclosure. It is noteworthy that the issuance of such a loan is deemed to be unfair under Chapter 93A even if the lender provides fair and complete disclosure of the terms of the loan and the borrower is fully informed of the risks he faces in accepting the loan. The unfairness, therefore, does not rest in deception but in the equities between the parties. See <u>Swanson</u> v. <u>Bankers Life Co.</u>, 389 Mass. 345, 349 (1983) ("In determining whether an act or practice is unfair, as opposed to deceptive, we must evaluate the equities between the parties"). The Legislature plainly deemed it predatory and, thus, unfair for a lender to make a high cost home loan, quickly reap the financial rewards from the high points, fees, or interest, and then collect the balance of the debt by foreclosing on the borrower when, as the lender reasonably should have foreseen, he cannot meet the scheduled payments. The Legislature, equally plainly, was disturbed by mortgage foreclosures of the borrower's principal dwelling, and thought it unfair for a lender to issue a mortgage loan that the lender reasonably believes will result in foreclosure of the borrower's home, even if the high cost of the loan fairly reflects the risk of the loan. .

The Attorney General has not alleged or sought to prove that the loans at issue in this case were "high cost mortgage loans" governed by the Act. Yet, it is reasonable for this Court to consider whether the loans at issue in this case fall within the "penumbra" of the concept of unfairness reflected in the Act. This Court finds that, as to some types of loans, they do. Under the Act, it was unfair to issue a mortgage loan when the lender reasonably believed that the borrower could not meet the scheduled payments. In the instant case, for those home mortgage loans which:

1. were adjustable rate loans with an introductory period of three years or less (generally, a 2/28 or 3/27 ARM);
2. with an introductory or "teaser" rate for the initial period that was significantly lower than the "fully indexed rate," that is, at least 3 percent below the "fully indexed rate;"[9]
3. where the debt-to-income ratio would have exceeded 50 percent had Fremont's

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[9] As an example, if the teaser rate is 7 percent, but the rate will reset to the six-month LIBOR plus a margin of 6 percent, the fully indexed rate will be 11 percent if the six-month LIBOR at the time of the loan origination is 5 percent.

underwriters measured the debt, not by the debt due under the teaser rate, but by the debt that would be due at the "fully indexed rate,"

the lender reasonably should have recognized (in the absence of significant liquid or easily liquidated assets) that the borrower would not be able to meet the scheduled payments once the "teaser" rate expired at the close of the introductory period. Loans with these three characteristics, therefore, were doomed to foreclosure unless the borrower was able to refinance the loan at or around the close of the introductory period. If housing prices declined, however, refinancing was not reasonably likely for these loans if they bore a fourth characteristic – a loan-to-value ratio of 100 percent <u>or</u> a substantial prepayment penalty (that is, a prepayment penalty beyond the "conventional prepayment penalty," defined in the Act, G..L. c. 183C, § 2),[10] <u>or</u> a prepayment penalty that extended beyond the introductory period.

Consequently, for loans with these four characteristics, the lender reasonably should have recognized that, after the introductory period, the borrower would be unlikely to make the scheduled mortgage payments and the loan was doomed to foreclosure unless the fair market value of the property had increased, thereby enabling the borrower to refinance the loan and obtain a new "teaser" rate for the introductory period. Given the fluctuations in the housing market and the inherent uncertainties as to how that market will fluctuate over time, this Court finds that it is unfair for a lender to issue a home mortgage loan secured by the borrower's principal dwelling that the lender reasonably expects will fall into default once the introductory period ends unless the fair market value of the home has increased at the close of the introductory

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[10] The Act defines a "conventional prepayment penalty" as "any prepayment penalty or fee that may be collected or charged in a home loan, and that is authorized by law other than this chapter, provided the home loan (1) does not have an annual percentage rate that exceeds the conventional mortgage rate by more than 2 percentage points; and (2) does not permit any prepayment fees or penalties that exceed 2 per cent of the amount prepaid." G..L. c. 183C, § 2.

period. To issue a home mortgage loan whose success relies on the hope that the fair market value of the home will increase during the introductory period is as unfair as issuing a home mortgage loan whose success depends on the hope that the borrower's income will increase during that same period.[11]

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[11] While the fair market value of housing in Massachusetts has risen 603% from 1980 to the third quarter of 2007 (compared to inflation of slightly over 250% during that period), its long-term investment value does not mean that these prices can reliably be expected to increase each year. Office of Federal Housing Enterprise Oversight, Change in OFHEO State House Price Indexes (2007 Q3 Data); Consumer Price Index, Inflation Calculator. Over the past 20 years, housing prices in Massachusetts have fallen twice, in 1989-1992 and 2006-2007. See Kristopher Gerardi, Adam Hale Shapiro, and Paul Willen, "Subprime Outcomes: Risky Mortgages, Homeownership Experiences, and Foreclosures," Working Papers: Federal Reserve Bank of Boston, www.bos.frb.org/economic/wp/index.htm at 48. Similarly, the New York Stock Exchange's Dow Jones Index increased 1,678% between the beginning of 1980 and the end of the third quarter of 2007, but it, too, experienced three significant periods of negative and/or stagnant growth, in 1978-1982, 1987-1991, and 2001-03. Dow Jones Industrial Average, viewed at finance.yahoo.com/echarts. While in hindsight these price drops may be seen as predictable, considering, in the words of former Federal Reserve Board Chief Alan Greenspan, the "irrational exuberance" of these markets, they are rarely reliably predicted before they happen and do not occur in easily predictable cycles.

The empirical data in the Federal Reserve Bank Working Paper cited above demonstrate the extraordinary impact of falling housing prices on foreclosures. The study estimated that, over the past 12 years, 18 percent of borrowers who purchased their homes with sub-prime mortgages suffered a foreclosure, as compared to only 3 percent who purchased their homes with prime mortgages. Subprime Outcomes at 2. The study found that:

> [H]ouse price appreciation plays a dominant role in generating foreclosures: homeowners who have suffered a 20 percent or greater fall in house prices are about fourteen times more likely to default on a mortgage compared to homeowners who have enjoyed a 20 percent increase. We attribute most of the dramatic rise in foreclosures in 2006 and 2007 in Massachusetts to the decline in house prices that began in the summer of 2005. Subprime lending played a role but that role was in creating a class of homeowners who were particularly sensitive to declining house price appreciation, rather than, as is commonly believed, by placing people in inherently problematic mortgages.

Id. at 1. The study also determined that rates of foreclosure "are highly sensitive," not only to house prices, but "to the initial combined loan-to-value ratio at origination ...." Id. at 2. The authors wrote:

> Subprime lenders created a group of borrowers that were much more likely to default for

Therefore, just as a high cost mortgage loan is treated as structurally unfair under the Act if the lender reasonably believed at the time the loan was issued that the borrower would be unable to make the scheduled payments, this Court finds that it is within the penumbra of that concept of unfairness that <u>any</u> mortgage loan secured by the borrower's principal dwelling should be presumed to be structurally unfair if the loan possesses the four characteristics described above:

1. The loan is an ARM with an introductory period of three years or less;
2. The loan has an introductory or "teaser" rate for the initial period that is at least 3 percent lower than the fully indexed rate;
3. The borrower has a debt-to-income ratio that would have exceeded 50 percent if the lender's underwriters had measured the debt, not by the debt due under the teaser rate, but by the debt due under the fully indexed rate; and
4. The loan-to-value ratio is 100 percent <u>or</u> the loan carries a substantial prepayment penalty <u>or</u> a prepayment penalty that extends beyond the introductory period.

The effect of the presumption is to shift the burden of production to the lender to demonstrate that the loan was not actually unfair, perhaps by s howing that the borrower had other assets that realistically could have enabled the borrower to meet the scheduled payments and avoid foreclosure, or other reasonable means of obtaining refinancing even if the fair market price of

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> at least two reasons. First, while they did not invent zero-equity borrowing, they did allow a much larger fraction of borrowers to start homeownership with no cushion against negative [house price appreciation]. Second, subprime lenders allowed borrowers with a history of cash flow problems and with monthly payments that exceeded fifty percent of current income to enter homeownership.

<u>Id.</u> at 4. In short, the study confirms the extraordinarily high risk of foreclosure that arises in a volatile housing market when subprime lenders approve loans with the four characteristics identified above.

the mortgaged home had fallen. This presumption would not change the burden of proving a Chapter 93A violation; the burden of proving that the loan was unfair remains with the plaintiff borrower.

The Attorney General justly may ask why "stated income" applications loans are not included among the characteristics used to determine whether a loan is presumptively unfair, since "stated income" loans are so prone to foreclosure. The reason is that "stated income" loans are no more prone to foreclosure than full documentation loans if the statements in the application are accurate; they become more prone to foreclosure only if the applicant (or the broker with the acquiescence or ignorance of the applicant) falsely inflates his income or assets. While such loans may not be prudent for a bank to issue because they fail to protect the bank from the risk of fraud, they cannot be said to be unfair to the borrower for this reason. In other words, a borrower may not fairly complain that a bank was unfair to him by giving him an opportunity to lie on his loan application without any meaningful risk of getting caught.

Fremont justly may ask why this Court is extending to <u>all</u> home mortgage loans this principle – that it is unfair for a lender to approve a home mortgage loan secured by the borrower's principal residence when the lender reasonably should have recognized that the loan is doomed to foreclosure unless the borrower's income or the fair market value of the residence increases – when the Legislature declared this to be an unfair act only for <u>high cost</u> mortgage loans. The reason is that this Court does not believe the Legislature believed this practice to be tolerable for mortgage loans that did not meet the definition of high cost mortgage loans. Rather, this Court believes that the Legislature thought it sufficient to focus on high cost mortgage loans because it did not imagine that lenders would issue loans with this degree of risk unless they were high cost mortgage loans. What has changed since the Legislature promulgated the Act is the increasing prevalence of mortgage-backed securities, which enabled lenders such as Fremont to assign large quantities of their high-risk mortgages, take a quick profit, and avoid the risks inherent in the loan.[12] Consequently, since those purchasing the mortgages to package them as mortgage-backed securities were careless in evaluating the risks of these loans, lenders such as Fremont could profit from sub-prime mortgages that fell below the definition of high risk mortgage loans. As the mortgage market changes, so, too, must the understanding of what lending conduct is unfair.

Fremont also justly may observe that the lending conduct this Court describes as unfair was not generally recognized in the industry to be unfair at the time these loans were made. Yet, for at least three reasons, this does not mean it is inappropriate for this Court to find its conduct to be unfair. First, as noted earlier, the meaning of unfairness under Chapter 93A is not fixed in stone; nor is it limited to conduct that is unlawful under the common law or prior statutes. See Kattar v. Demoulas, 433 Mass. at 12-13. Rather, it is forever evolving, not only to adapt to changing social, economic, and technological circumstances, but also to reflect what we have learned to be unfair from our experience as a commonwealth. See Nei v. Burley, 388 Mass. 307, 313 (1983) ("This flexible set of guidelines as to what should be considered lawful or unlawful under c. 93A suggests that the Legislature intended the terms 'unfair and deceptive' to grow and change with the times."); Lowell Gas Co. v. Attorney General, 377 Mass. 37, 51 (1979) (citations omitted) (quoting Judge Learned Hand's view that part of the Federal Trade Commission's duty is "to discover and make explicit those unexpressed standards of fair dealing which the

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[12] See Interagency Guidance on Subprime Lending, issued by the United States Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve Board, the FDIC, and the Office of Thrift Supervision, March 1, 1999 at 6 ("Strong demand from investors and favorable accounting rules often allow securitization pools to be sold at a gain, providing further incentive for lenders to expand their subprime lending program.).

conscience of the community may progressively develop.")

Second, Fremont had more than fair warning of the dangers posed by the loans bearing the four characteristics identified above. On October 8, 1999, in its Interagency Guidance on High LTV Residential Real Estate Lending, issued by the United States Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve Board, the FDIC, and the Office of Thrift Supervision, lending institutions were warned:

> Recent studies indicate that the frequency of default and the severity of losses on high LTV [loan-to-value] loans far surpass those associated with traditional mortgages and home equity loans. The higher frequency of default may indicate weaknesses in credit risk selection and/or credit underwriting practices, while the increased severity of loss results from deficient collateral protection. In addition, the performance of high LTV borrowers has not been tested during an economic downturn when defaults and losses may increase.

Id. at 2 (footnote omitted). In this report, a high LTV real estate loan was defined as a loan on a residential property that equaled or exceeded 90 percent of the real estate's appraised value, unless the loan had appropriate credit support, such as mortgage insurance or other readily marketable collateral. Id. at 1. It was reasonable to expect that the frequency of default and the severity of losses would be even greater as the LTV approached 100 percent. Indeed, an Office of the Comptroller of the Currency Advisory Letter (AL 2003-2), issued by the Deputy Comptroller for Compliance, dated February 21, 2003 forewarned that it may be found unfair to extend loans bearing the four characteristics identified by this Court:

> The terms 'abusive lending' or 'predatory lending' are most frequently defined by reference to a variety of lending practices. Although it is generally necessary to consider the totality of the circumstances to assess whether a loan is predatory, a fundamental characteristic of predatory lending is the aggressive marketing of credit to prospective borrowers who simply cannot afford the credit on the terms being offered. Typically, such credit is underwritten predominantly on the basis of the liquidation value of the collateral, without regard to the borrower's ability to service and repay the loan according to its terms absent resorting to that collateral. ... When a loan has been made based on the foreclosure value of the collateral, rather than on a determination that the borrower has the capacity to make the scheduled payments under the terms of the loan, based on the

> borrower's current and expected income, current obligations, employment status, and other relevant financial resources, the lender is effectively counting on its ability to seize the borrower's equity in the collateral to satisfy the obligation and to recover the typically high fees associated with such credit. Not surprisingly, such credits experience foreclosure rates higher than the norm.

Id. at 2.

Third, even the federal agencies whose failure to monitor lending practices contributed to the current sub-prime lending crisis now recognize that mortgage loans bearing these four characteristics generally are imprudent and present an unacceptable risk of foreclosure. The most recent Statement on Subprime Mortgage Lending issued on July 10, 2007 by the United States Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve Board, the FDIC, the Office of Thrift Supervision, and the National Credit Union Administration recognizes the "substantial risks to both consumers and lenders" of sub-prime ARM loans bearing certain characteristics, including low teaser rates. Federal Register, Vol. 72, No 131, 37569 (July 10, 2007) at 37572. Specifically, the Statement declares:

> Prudent qualifying standards recognize the potential effect of payment shock in evaluating a borrower's ability to service debt. An institution's analysis of a borrower's repayment capacity should include an evaluation of the borrower's ability to repay the debt by its final maturity at the fully indexed rate, assuming a fully amortizing repayment schedule.

Id. at 37573. Although this Statement did not address specifically whether it would be unfair under consumer protection principles for a lender to approve a loan that the borrower could not afford to repay at the fully indexed rate, the Statement did characterize as a "fundamental consumer protection principle" that loans should be approved "based on the borrower's ability to repay the loan according to its terms." Id. at 37574. In essence, now that the foreseeable perils of these sub-prime lending practices have been experienced, to the great detriment of homeowners, financial institutions, the securities market, and the overall economy, these federal agencies have belatedly recognized that it is both imprudent and unfair to approve a mortgage loan that the borrower cannot reasonably be expected to repay if housing prices were to fall. Just because we, as a society, failed earlier to recognize that loans with these four characteristics were generally unfair does not mean that we should ignore their tragic consequences and fail now to recognize their unfairness. In short, approval of loans bearing these four characteristics, in the absence of other liquid or easily liquidated assets or special circumstances, was unfair before and it is unfair today, even if we were too blind earlier to recognize its unfairness.

To be sure, the fact that Fremont's loans bearing these four characteristics were not generally recognized to be unfair at the time these loans originated is not irrelevant to this Court's consideration of this case. This Court will certainly take that factor into account in determining what preliminary injunctive remedy is appropriate to address the unfairness.

Moreover, even if a Fremont loan were to be preliminarily found unfair (rather than simply presumptively unfair), that finding does not mean that the borrower is released from his obligation to repay this debt. The borrower received the money that was lent pursuant to a written loan agreement and presumptively is expected to repay the loan. The impact of this preliminary injunction will be nil upon a borrower who can afford to repay the loan; its impact will be felt only by those who cannot afford to repay the loan in full and now face the risk of foreclosure. The reason is that the unfairness of these loans rests in their vulnerability to foreclosure, not in the rate of interest charged or their lending terms.

In determining whether to grant a preliminary injunction, this Court must perform the three-part balancing test articulated in Packaging Industries Group, Inc. v. Cheney, 380 Mass. 609, 616-617 (1980). First, the court must evaluate the moving party's claim of injury and its likelihood of success on the merits. Id. at 617. Second, it must determine whether failing to issue a preliminary injunction would subject the moving party to irreparable injury -- losses that cannot be repaired or adequately compensated upon final judgment. Id. at 617 & n. 11. Third, "[i]f the judge is convinced that failure to issue the injunction would subject the moving party to a substantial risk of irreparable harm, the judge must then balance this risk against any similar risk of irreparable harm which granting the injunction would create for the opposing party." Id. at 617. In balancing these factors, "[w]hat matters as to each party is not the raw amount of irreparable harm the party might conceivably suffer, but rather the risk of such harm in light of the party's chance of success on the merits. Only where the balance between these risks cuts in favor of the moving party may a preliminary injunction properly issue." Id. When the preliminary injunction is sought by the Attorney General, this Court must also consider whether a preliminary injunction would serve the public interest. Commonwealth v. ELM Medical Laboratories, Inc., 33 Mass. App. Ct. 71, 83 (1992). See also Brookline v. Goldstein, 388 Mass. 443, 447 (1983).

This Court finds that the Attorney General is likely to prevail in proving that many of the mortgage loans issued by Fremont secured by the borrower's primary residence that bear the four characteristics outlined above are not merely presumptively unfair but actually unfair under Chapter 93A. This Court also finds that, with a carefully measured preliminary injunction, the balance of harms favors the Attorney General. This Court recognizes that an overly broad preliminary injunction may not achieve a balance of harms that favors the Attorney General.

The Court's preliminary injunction shall require the following procedure before Fremont initiates a foreclosure proceeding:

1. Before initiating or advancing a foreclosure on any mortgage loan originated by Fremont that is (a) NOT presumptively unfair, because it does not possess each of the four characteristics identified above, or (b) NOT secured by the borrower's principal dwelling, or (c) that is secured by a dwelling that is vacant or uninhabitable, Fremont shall first give

the Attorney General 30 days advance written notice so that the Attorney General can verify that the proposed foreclosure falls outside the scope of this Preliminary Injunction. If the Attorney General has not given written notice of an objection to Fremont by the 30th day, based on her finding that the loan is presumptively unfair and is secured by the borrower's principal dwelling and that the dwelling is both inhabited and inhabitable, Fremont may proceed with the foreclosure. If the Attorney General has given written notice of an objection, Fremont shall proceed in accordance with paragraph 2 below.

2. Before initiating or advancing a foreclosure on any mortgage loan originated by Fremont (1) (a) that is presumptively unfair, because it possesses each of the four characteristics identified above, and (b) secured by the borrower's principal dwelling, and (c) where the dwelling is neither vacant nor uninhabitable, or (2) in which the Attorney General has provided a written objection in accordance with paragraph 1 above, Fremont shall give the Attorney General 45 days advance written notice of the proposed foreclosure, identifying the reasons why foreclosure is reasonable under the circumstances and/or why the Attorney General's written objection under paragraph 1 above is in error. If the Attorney General has not given written notice of an objection to Fremont by the 45th day, Fremont may proceed with the foreclosure.

3. If the Attorney General has timely given a written objection under paragraph 2 above, the Attorney General and Fremont shall within the next 15 days attempt to resolve their differences regarding the foreclosure. If these differences have been resolved, the Attorney General will notify Fremont in writing that she has withdrawn her written objection. If these differences are not resolved, Fremont may proceed with the foreclosure only with the prior approval of this Court (or a special master appointed by this Court), which it may seek on the16th day.

4. In considering whether to approve the foreclosure, this Court will determine (a) whether the loan is actually unfair and is actually secured by the borrower's primary residence that is both inhabited and inhabitable, (b) whether Fremont has taken reasonable steps to "work out" the loan and avoid foreclosure, and (c) whether there is any fair or reasonable alternative to foreclosure. This Court will seek to expedite these decisions but, if the number of such matters grows too large, this Court may need to appoint a special master to assist the Court.

In designing this preliminary injunction, this Court anticipates that Fremont will act responsibly in attempting to "work out" mortgage loans prior to instituting foreclosure, and that the Attorney General will act judiciously in determining which loans do not warrant foreclosure. This Court also recognizes that, while it can establish a process that will permit the parties to resolve the vast majority of these issues, it cannot delegate to any party the power ultimately to determine whether a mortgage loan is actually unfair or whether foreclosure is the proper last resort.

Nothing in this Preliminary Injunction is intended in any way to interfere with or be inconsistent with the FDIC's Consent Agreement with Fremont. That Consent Agreement expressly declares that its provisions do not bar a state Attorney General from seeking further remedies against Fremont for unfair or deceptive practices. Consent Agreement at 23. Implicitly, if the Attorney General were to prevail, preliminary injunctive relief ordered by a court to ameliorate the adverse consequences of Fremont's unfair practices are also not barred by the Consent Agreement. Nor are the terms of this Preliminary Injunction so harsh as to interfere with the FDIC's objective of restoring Fremont to firmer financial footing through the restoration of sound banking practices.

Finally, this Court emphasizes that borrowers who have received presumptively unfair loans from Fremont should not interpret this preliminary injunction to mean that they have been released from their obligation to repay these loans. They have not been given any such release. Borrowers share with Fremont the responsibility for having entered into a mortgage loan that they now cannot repay. The spirit of this decision is simply that Fremont, having helped borrowers get into this mess, now must take reasonable steps to help them get out of it.

ORDER

For the reasons stated above, this Court hereby **ALLOWS** the Attorney General's motion for a preliminary injunction to the extent that, pending final adjudication or further orderr of this Court, this Court **ORDERS** as follows:

1. Before initiating or advancing a foreclosure on any mortgage loan originated by Fremont that is (a) NOT presumptively unfair, because it does not possess each of the four characteristics identified above, or (b) NOT secured by the borrower's principal dwelling, or (c) that is secured by a dwelling that is vacant or uninhabitable, Fremont shall first give the Attorney General 30 days advance written notice so that the Attorney General can verify that the proposed foreclosure falls outside the scope of this Preliminary Injunction.

If the Attorney General has not given written notice of an objection to Fremont by the 30th day, based on her finding that the loan is presumptively unfair and is secured by the borrower's principal dwelling and that the dwelling is both inhabited and inhabitable, Fremont may proceed with the foreclosure. If the Attorney General has given written notice of an objection, Fremont shall proceed in accordance with paragraph 2 below.

2. Before initiating or advancing a foreclosure on any mortgage loan originated by Fremont (1) (a) that is presumptively unfair, because it possesses each of the four characteristics identified above, and (b) secured by the borrower's principal dwelling, and (c) where the dwelling is neither vacant nor uninhabitable, or (2) in which the Attorney General has provided a written objection in accordance with paragraph 1 above, Fremont shall give the Attorney General 45 days advance written notice of the proposed foreclosure, identifying the reasons why foreclosure is reasonable under the circumstances and/or why the Attorney General's written objection under paragraph 1 above is in error. If the Attorney General has not given written notice of an objection to Fremont by the 45th day, Fremont may proceed with the foreclosure.

3. If the Attorney General has timely given a written objection under paragraph 2 above, the Attorney General and Fremont shall within the next 15 days attempt to resolve their differences regarding the foreclosure. If these differences have been resolved, the Attorney General will notify Fremont in writing that she has withdrawn her written objection. If these differences are not resolved, Fremont may proceed with the foreclosure only with the prior approval of this Court (or a special master appointed by this Court), which it may seek on the16th day.

4. In considering whether to approve the foreclosure, this Court will determine (a) whether the loan is actually unfair and is actually secured by the borrower's primary residence that is both inhabited and inhabitable, (b) whether Fremont has taken reasonable steps to "work out" the loan and avoid foreclosure, and (c) whether there is any fair or reasonable alternative to foreclosure. This Court will seek to expedite these decisions but, if the number of such matters grows too large, this Court may need to appoint a special master to assist the Court..

Ralph D. Gants

Ralph D. Gants
Justice of the Superior Court

DATED: February 25, 2008

APPENDIX C

FORM 104 (10/06)

ADVERSARY PROCEEDING COVER SHEET (Instructions on Reverse)	**ADVERSARY PROCEEDING NUMBER** (Court Use Only)

PLAINTIFFS Thomas J. Orr, Trustee and Phyllis A. Hollis, Debtor 321 High Street, Burlington, NJ 08016	**DEFENDANTS** Ameriquest Mortgage,Co., Ameriquest Mortgage Securities,Inc., Deutsche Bank National Trust,Co., AMC Mortgage Svcs.
ATTORNEYS (Firm Name, Address, and Telephone No.) Margaret Lambe Jurow, Esq., Attorney for Phyllis A. Hollis 100 Metroplex Dr., Suite 402, Edison, NJ 08818	**ATTORNEYS** (If Known)
PARTY (Check One Box Only) ☐ Debtor ☐ U.S. Trustee/Bankruptcy Admin ☐ Creditor ☐ Other ☑ Trustee	**PARTY** (Check One Box Only) ☐ Debtor ☐ U.S. Trustee/Bankruptcy Admin ☐ Creditor ☑ Other ☐ Trustee

CAUSE OF ACTION (WRITE A BRIEF STATEMENT OF CAUSE OF ACTION, INCLUDING ALL U.S. STATUTES INVOLVED)
Complaint for recovery of damages, punitive and treble damages, and related statutory relief

NATURE OF SUIT

(Number up to five (5) boxes starting with lead cause of action as 1, first alternative cause as 2, second alternative cause as 3, etc.)

FRBP 7001(1) – Recovery of Money/Property
☐ 11-Recovery of money/property - §542 turnover of property
☐ 12-Recovery of money/property - §547 preference
☐ 13-Recovery of money/property - §548 fraudulent transfer
☑ 14-Recovery of money/property - other

FRBP 7001(2) – Validity, Priority or Extent of Lien
☐ 21-Validity, priority or extent of lien or other interest in property

FRBP 7001(3) – Approval of Sale of Property
☐ 31-Approval of sale of property of estate and of a co-owner - §363(h)

FRBP 7001(4) – Objection/Revocation of Discharge
☐ 41-Objection / revocation of discharge - §727(c),(d),(e)

FRBP 7001(5) – Revocation of Confirmation
☐ 51-Revocation of confirmation

FRBP 7001(6) – Dischargeability
☐ 66-Dischargeability - §523(a)(1),(14),(14A) priority tax claims
☐ 62-Dischargeability - §523(a)(2), false pretenses, false representation, actual fraud
☐ 67-Dischargeability - §523(a)(4), fraud as fiduciary, embezzlement, larceny

(continued next column)

FRBP 7001(6) – Dischargeability (continued)
☐ 61-Dischargeability - §523(a)(5), domestic support
☐ 68-Dischargeability - §523(a)(6), willful and malicious injury
☐ 63-Dischargeability - §523(a)(8), student loan
☐ 64-Dischargeability - §523(a)(15), divorce/sep property settlement/decree
☐ 65-Dischargeability - other

FRBP 7001(7) – Injunctive Relief
☐ 71-Injunctive relief – reinstatement of stay
☐ 72-Injunctive relief – other

FRBP 7001(8) Subordination of Claim or Interest
☐ 81-Subordination of claim or interest

FRBP 7001(9) Declaratory Judgment
☐ 91-Declaratory judgment

FRBP 7001(10) Determination of Removed Action
☐ 01-Determination of removed claim or cause

Other
☐ SS-SIPA Case – 15 U.S.C. §§78aaa *et.seq.*
☐ 02-Other (e.g. other actions that would have been brought in state court if unrelated to bankruptcy case)

☑ Check if this case involves a substantive issue of state law	☐ Check if this is asserted to be a class action under FRCP 23
☑ Check if a jury trial is demanded in complaint	Demand $

Other Relief Sought

Phyllis A. Hollis 07-22759

New Jersey Kathryn C. Ferguson

BANKRUPTCY CASE IN WHICH THIS ADVERSARY PROCEEDING ARISES		
NAME OF DEBTOR Phyllis A. Hollis		BANKRUPTCY CASE NO. 07-22759
DISTRICT IN WHICH CASE IS PENDING New Jersey	DIVISIONAL OFFICE Trenton	NAME OF JUDGE Kathryn C. Ferguson

RELATED ADVERSARY PROCEEDING (IF ANY)		
PLAINTIFF	DEFENDANT	ADVERSARY PROCEEDING NO.
DISTRICT IN WHICH ADVERSARY IS PENDING	DIVISIONAL OFFICE	NAME OF JUDGE
SIGNATURE OF ATTORNEY (OR PLAINTIFF) Thomas J. Orr	Margaret L. Jurow	
DATE 11-19-07	PRINT NAME OF ATTORNEY (OR PLAINTIFF) THOMAS J. ORR	

MARGART L. JUROW, ESQ.
Legal Services of NJ.

INSTRUCTIONS

The filing of a bankruptcy case creates an "estate" under the jurisdiction of the bankruptcy court which consists of all of the property of the debtor, wherever that property is located. Because the bankruptcy estate is so extensive and the jurisdiction of the court so broad, there may be lawsuits over the property or property rights of the estate. There also may be lawsuits concerning the debtor's discharge. If such a lawsuit is filed in a bankruptcy court, it is called an adversary proceeding.

A party filing an adversary proceeding must also must complete and file Form 104, the Adversary Proceeding Cover Sheet, if it is required by the court. In some courts, the cover sheet is not required when the adversary proceeding is filed electronically through the court's Case Management/Electronic Case Files (CM/ECF) system. (CM/ECF captures the information on Form 104 as part of the filing process.) When completed, the cover sheet summarizes basic information on the adversary proceeding. The clerk of court needs the information to process the adversary proceeding and prepare required statistical reports on court activity.

The cover sheet and the information contained on it do not replace or supplement the filing and service of pleadings or other papers as required by law, the Bankruptcy Rules, or the local rules of court. The cover sheet, which is largely self-explanatory, must be completed by the plaintiff's attorney (or by the plaintiff if the plaintiff is not represented by an attorney). A separate cover sheet must be submitted to the clerk for each complaint filed.

Parties. Give the names of the parties to the adversary proceeding exactly as they appear on the complaint. Give the names and addresses of the attorneys if known.

Signature. This cover sheet must be signed by the attorney of record in the box on the second page of the form. If the plaintiff is represented by a law firm, a member of the firm must sign. If the plaintiff is pro se, that is, not presented by an attorney, the plaintiff must sign.

THOMAS J. ORR
Counselor at Law
By: Thomas J. Orr, Esq.
321 High Street
Burlington, New Jersey 08016-4411
(609) 386-8700
Attorney for Thomas J. Orr, Trustee, Plaintiff

LEGAL SERVICES OF NEW JERSEY
By: Margaret Lambe Jurow, Esq.
100 Metroplex Drive, Suite 402
Edison, New Jersey 08818
(732) 572-9100
Attorneys for Phyllis Hollis, debtor, Plaintiff

In Re: PHYLLIS A. HOLLIS, Debtor.	UNITED STATES BANKRUPTCY COURT DISTRICT OF NEW JERSEY Case No. 07-22759(KCF)
THOMAS J. ORR, Trustee and PHYLLIS A. HOLLIS, individually, debtor, Plaintiffs, v. AMERIQUEST MORTGAGE COMPANY, AMERIQUEST MORTGAGE SECURITIES, INC., DEUTSCHE BANK NATIONAL TRUST COMPANY, AMC MORTGAGE SERVICES, JOHN DOES 1-5, Defendants.	Adv. Pro No. 07-

COMPLAINT FOR RECOVERY OF DAMAGES, PUNITIVE AND TREBLE DAMAGES AND RELATED STATUTORY RELIEF

1. The above-captioned bankruptcy case was commenced by Phyllis A. Hollis ["the Debtor"] on September 6, 2007 [the Petition Filing Date] by her filing of Voluntary Petition. That case remains pending in this District.

2. Thomas J. Orr, Trustee, Plaintiff herein, is the duly appointed and acting Chapter 7 Trustee for the Debtor.

3. This Court has jurisdiction pursuant to 28 U.S.C. 1334 and 28 U.S.C. §157.

4. Venue is properly laid in this district pursuant to 28 U.S.C. §1409.

5. This matter is a core proceeding pursuant to 28 U.S.C. §157(b).

INTRODUCTION

6. This action arises out of a series of predatory mortgage loans that Ameriquest fraudulently induced Ms. Hollis to purchase. These loans failed to provide Ms. Hollis with a reasonable, tangible, net benefit and as such constitute prohibited unconscionable business practices. Ms. Hollis and the trustee seek to enforce the rescission of the most recent loan pursuant to the Truth in Lending Act, and seek an award of damages resulting from Defendants' predatory lending practices.

PARTIES

7. Plaintiff, Phyllis A. Hollis, is the debtor and a consumer who resides at and owns the property located at 38 Hilliard Road, Old Bridge, Middlesex County, New Jersey.

8. Plaintiff, Thomas J. Orr, was appointed as interim case trustee on September 7, 2007. Mr. Orr conducted a meeting of creditors on October 9, 2007. No trustee was elected at the meeting of creditors. Pursuant to 11 U.S.C. §702(d) Mr. Orr serves as the case trustee with the authority and duty to collect and reduce to money property of the estate.

9. Defendant Ameriquest Mortgage Company (hereinafter "Ameriquest") is a Delaware incorporated sub-prime mortgage originator with headquarters in California and branch offices throughout the United States, and is the entity that originated the mortgage on the property located at 38 Hilliard Road, Old Bridge, New Jersey in which Phyllis Hollis resides.

10. Defendant Deutsche Bank National Trust Company (hereinafter "Deutsche Bank") provides investment banking services to its clients, including mortgage lenders seeking to securitize mortgages through mortgage backed securities. Deutsche Bank alleges that it is the Trustee of a securitized pool of Ameriquest-originated mortgages known as Ameriquest Mortgage Securities, Inc., Asset-backed Pass-Through Certificates Series 2005-R2 pursuant to a pooling and servicing agreement dated March 1, 2006 (hereinafter "the trust") which Deutsche Bank alleges includes a mortgage and loan that is the subject of this complaint.

11. Defendant Ameriquest Mortgage Securities, Inc. (hereinafter "AMS"), with a business address located at 1100 Town & Country Road, Suite 1100, Orange, California 92868, is a wholly owned subsidiary of Ameriquest and has served as the depositor in the transactions described herein.

12. AMC Mortgage Services with a business address located at 1100 Town & Country Road, Suite 1100, Orange, California 92868, is a wholly owned subsidiary of Ameriquest, and served as the mortgage servicer in the transactions described herein.

13. John Does 1-5 are fictitious names representing additional parties who may have liability in this matter.

FACTUAL ALLEGATIONS

14. Phyllis A. Hollis is an African American woman.

15. Ms. Hollis is an unsophisticated consumer.

16. Ms. Hollis' only substantial asset is the home located at 38 Hilliard Road, Old Bridge, New Jersey where she resides.

17. Ms. Hollis purchased her house in July 1999 for approximately $147,000.00. At the time of purchase Ms. Hollis had a fixed rate purchase money FHA insured mortgage.

18. In October 2000, Ms. Hollis obtained a second home equity mortgage in the amount of $42,300.00. The proceeds of this loan were used in large part for home improvements.

19. In November 2001, an Ameriquest representative solicited Ms. Hollis and offered to refinance her home and combine the two mortgages in a way that would be beneficial to her.

20. Ms. Hollis spoke to an Ameriquest agent known to her as Gabriel.

21. Gabriel told Ms. Hollis that her overall interest rate on a new Ameriquest loan would be lower than the rate she already had on her current loans.

22. In November 2001, Ms. Hollis had a 7.25% fixed rate 30 year first mortgage with a principal balance of approximately $145,000.00 and a 14.25% 20 year second mortgage with a principal balance of approximately $43,000.00.

23. In November 2001, Ameriquest sold Ms. Hollis an adjustable rate 30 year mortgage at a rate of 8.85% adjustable after 2 years every six months to LIBOR plus 6.5%.

24. Ameriquest did not explain to Ms. Hollis what an adjustable rate mortgage was.

25. Ms. Hollis' initial monthly payment was less than $50.00 per month lower than her prior combined mortgage payments. Under the new Ameriquest mortgage she would make payments substantially longer than under her old loans.

26. Ameriquest charged in excess of $12,000.00 in fees for the transaction.

27. In February 2006, Ameriquest again solicited Ms. Hollis to refinance her mortgage. She talked to an Ameriquest representative known to her as Tom.

28. Ms. Hollis met with Tom at Ameriquest's office in East Brunswick.

29. Ms. Hollis inquired whether there was any opportunity for her to obtain a fixed rate mortgage.

30. Ameriquest told Ms. Hollis that she was not eligible for a fixed rate mortgage.

31. Ameriquest advised Ms. Hollis to take out a larger mortgage than the one she had and pay down other debts. Ameriquest advised that if she did so her credit would be improved and that Ameriquest would get her a better lower mortgage in the future.

First Ameriquest Mortgage:

32. Ameriquest induced Ms. Hollis to enter into the First Ameriquest Mortgage using unconscionable commercial practices, deception, fraud, false pretense and/or misrepresentation.

33. Upon information and belief, the First Ameriquest Mortgage was made without regard for Ms. Hollis's ability to repay.

34. The First Ameriquest Mortgage stripped equity from Ms. Hollis's home without providing her with a tangible, net benefit in exchange.

35. In connection with the First Ameriquest Mortgage, Ameriquest charged Ms. Hollis 4.520% in “discount points,” but did not provide any benefit to Ms. Hollis in exchange.

36. An Ameriquest representative told Ms. Hollis that Ameriquest would lower her interest rate and lower her monthly mortgage payments. The refinance accomplished neither.

37. An Ameriquest representative advised Ms. Hollis that it would be advantageous to pay off unsecured debt using her home equity. Paying unsecured debt from her home equity was disadvantageous to Ms. Hollis insofar as it increased her monthly mortgage payment and exposed Ms. Hollis to a higher risk of foreclosure and lowered her credit score.

38. The mortgage required Ms. Hollis to pay a prepayment penalty if the loan was paid within the first three years. Ms. Hollis had not been told of the pre-payment penalty prior to closing.

Second Ameriquest Mortgage:

39. On or about February, 2006 Ameriquest solicited Ms. Hollis to refinance her mortgage yet again.

40. On or about February 9, 2006, Ms. Hollis gave Ameriquest a thirty-year mortgage for $242,226.00 (“Second Ameriquest Mortgage”) in exchange for a loan. The interest rate was adjustable beginning at 9.3%. The initial monthly payments of principal and interest on the loan were $2054.47 excluding property insurance or tax escrow.

41. Ameriquest induced Ms. Hollis to enter into the Second Ameriquest Mortgage using unconscionable commercial practices, deception, fraud, false pretense and/or misrepresentation.

42. To induce her to enter into the Second Ameriquest Mortgage, an Ameriquest representative told Ms. Hollis that a new mortgage would reduce Ms. Hollis’s monthly mortgage payment and “repair her credit” so that she would qualify for a fixed rate mortgage.

43. Ameriquest failed to provide Ms. Hollis with a tangible, net benefit in connection with the Second Ameriquest Mortgage.

44. In connection with the Second Ameriquest Mortgage, Ameriquest charged Ms. Hollis "discount points," but did not provide any benefit to Ms. Hollis in exchange for same.

45. Ameriquest did not provide Ms. Hollis with proper disclosures as required by the Federal Truth in Lending Act, including but not limited to:

(a) Contradictory, misleading and erroneous notice of right to cancel;

(b) Failure to disclose the finance charge, amount financed, and Annual Percentage Rate accurately.

46. Ms. Hollis and Mr. Orr exercised the right to rescind the Second Ameriquest Mortgage on by sending a Notices of Rescission of Mortgage to Ameriquest, AMC Mortgage Services, AMS, Deutsche Bank and Citibank via regular and certified mail, return receipt requested.

The Ameriquest/AMS/Deutsche Bank relationship:

47. Pursuant to certain contracts between them, Ameriquest, AMS and Deutsche Bank embarked upon a profit-seeking business venture creating, selling, and managing investment securities including Real Estate Mortgage Investment Conduits (REMICs).

48. Upon information and belief, Deutsche Bank provided funding to Defendant Ameriquest either directly or indirectly in order to enable Ameriquest to make mortgage loans.

49. Ameriquest made subprime residential mortgage loans, such as the mortgage that is the subject of the instant foreclosure action.

50. Ameriquest sold certain mortgage loans to Defendant AMS pursuant to a "Mortgage Loan Purchase Agreement" or similar agreement between them.

51. Upon information and belief, AMS purchased the mortgages in order to serve as a Special Purpose Entity, a bankruptcy remote entity established in order to protect the trust from the potential insolvency or liability of the originator of the mortgages and to enhance the rating of the securities by agencies such as Standard and Poor's.

52. AMS assigned a pool of mortgages to Deutsche Bank as Trustee for the creation of securitization trusts.

53. As Trustee, Deutsche Bank invited investors to buy certificates representing beneficial interests in the trust of pooled mortgage loans. Investors were to be compensated through interest payments made by the mortgagors.

54. All three parties in this venture are aware that Ameriquest engages in a practice of lending based primarily upon the value of the collateral with less emphasis upon borrower's ability to repay.

55. All three parties in this venture are aware that Ameriquest uses underwriting standards less stringent than those of more traditional lenders, and the offering prospectus for the certificates informs potential certificate holders that Ameriquest's less stringent underwriting standards may result in losses allocated to the offered certificates.

56. All three parties in this venture are aware that as a result of Ameriquest's underwriting standards, the mortgage loans are likely to experience rates of delinquency, foreclosure and bankruptcy that are higher than those experienced by mortgage loans underwritten in a more traditional manner.

FIRST COUNT

(TILA Violation – Second Ameriquest Mortgage)
(Against Deutsche Bank, Ameriquest and AMS)

57. Plaintiffs Thomas J. Orr and Phyllis A. Hollis repeat and reallege all paragraphs above as if fully set forth herein.

58. The transaction between Ameriquest and Ms. Hollis resulting in the Second Ameriquest Mortgage was a consumer transaction, and was a non-purchase money mortgage secured by Ms. Hollis's primary residence.

59. At all times relevant to the transaction resulting in the Second Ameriquest Mortgage, Ameriquest was a creditor under the federal Truth in Lending Act, 15 U.S.C.A. § 1601 *et seq.* ("TILA") and as such was required to provide notices of the right to rescind the mortgage and deliver material disclosures including, but not limited to, the amount financed, finance charge and annual percentage rate to Ms. Hollis consistent with the Act.

60. In connection with the Second Ameriquest Mortgage, Ameriquest failed to comply with applicable mandatory disclosure provisions of TILA. Specifically, Ameriquest failed to provide Ms. Hollis with proper and accurate written rescission notices and accurate material disclosures as required by TILA.

61. In light of these violations, Ms. Hollis was and is entitled to rescind the Second Ameriquest Mortgage.

62. Ms. Hollis exercised her right to rescind the Second Ameriquest Mortgage on November 7, 2007 by sending a Notices of Rescission of Mortgage to Ameriquest, AMC Mortgage Services, AMS, and Deutsche Bank via regular and certified mail, return receipt requested.

63. Mr. Orr also exercised the bankruptcy estate's right to rescind the Second Ameriquest Mortgage on November 14, 2007 by sending a Notices of Rescission of Mortgage to Ameriquest, AMC Mortgage Services, AMS, and Deutsche Bank via regular and certified mail, return receipt requested.

64. Upon information and belief, Deutsche Bank, Ameriquest and/or AMC Mortgage Services failed to comply with their rescission obligations under TILA.

65. The TILA violations were apparent on the face of the documents, resulting in assignee liability.

WHEREFORE, Plaintiffs Thomas J. Orr and Phyllis A. Hollis seek a judgment as follows:

A. Rescission of the Second Ameriquest Mortgage, including a declaration that the estate and/or Ms. Hollis are not liable for any finance charge or other charge imposed in connection with either transaction;

B. Declaratory and injunctive relief voiding the Second Ameriquest Mortgage;

C. Awarding actual damages;

D. Awarding statutory damages;

E. Awarding attorneys fees and costs; and

F. Granting such other relief as the court deems just and equitable.

SECOND COUNT
(Consumer Fraud – First and Second Ameriquest Mortgages)
(Against Ameriquest)

66. Plaintiffs Thomas J. Orr and Phyllis A. Hollis repeat and reallege all paragraphs above as if fully set forth herein.

67. Defendant Ameriquest engaged in unconscionable commercial practices, deception, fraud, false pretense, false promise and/or misrepresentations relating to the First and Second Ameriquest Mortgages, detailed in the allegations of fact, above.

68. Alternatively, or in addition, Defendant Ameriquest engaged in acts of omission, including but not limited to knowing concealment, suppression and omissions of material facts in connection with the First and Second Ameriquest Mortgages, detailed in the allegations of fact, above.

69. The foregoing acts by Ameriquest constitute violations of New Jersey's Consumer Fraud Act, N.J.S.A. 56:8-2 at seq., as a result of which Phyllis A. Hollis and the debtor's estate suffered ascertainable loss.

WHEREFORE, Plaintiffs Thomas J. Orr and Phyllis A. Hollis seek a judgment as follows:

A. Declaratory and injunctive relief declaring the First and Second Ameriquest Mortgages void and unenforceable;

B. Declaratory and injunctive relief rescinding and/or reforming the First and Second Ameriquest Mortgages;

C. Awarding actual damages;

D. Awarding treble damages;

E. Awarding costs and attorneys fees; and

F. Granting such other relief as the court deems just and equitable.

THIRD COUNT

(Common Law Fraud/Fraud in the Inducement – First and Second Ameriquest Mortgages)
(Against Deutsche Bank, Ameriquest and AMS)

70. Plaintiffs Thomas J. Orr and Phyllis Hollis repeat and reallege all paragraphs above as if fully set forth herein.

71. Ameriquest misrepresented material facts to Ms. Hollis in order to induce her to enter the First and Second Ameriquest Mortgages.

72. At all times relevant, Ameriquest made its misrepresentations knowingly, and AMS and Deutsche Bank knowingly obtained the fruits of the fraud.

73. Ameriquest made the misrepresentations with the intent that Ms. Hollis rely on them.

74. Ms. Hollis reasonably relied on Ameriquest's misrepresentations.

75. Ms. Hollis suffered damages as a result of the fraud.

WHEREFORE, Thomas J. Orr and Phyllis A. Hollis seek a judgment against Ameriquest, as follows:

A. Declaratory and injunctive relief declaring the First and Second Ameriquest Mortgages void and unenforceable;

B. Declaratory and injunctive relief rescinding and/or reforming the First and Second Ameriquest Mortgages;

C. Awarding actual damages;

D. Awarding punitive damages; and

E. Granting such other relief as the court deems just and equitable.

FOURTH COUNT

(Aiding and Abetting Common Law Fraud/Concert of Action)
(Against Deutsche Bank and AMS)

76. Plaintiffs Thomas J. Orr and Phyllis A. Hollis repeat and reallege all paragraphs above as if fully set forth herein.

77. Upon information and belief, Deutsche Bank and AMS aided and abetted Ameriquest in the commission of fraud.

78. Upon information and belief, Deutsche Bank and AMS had knowledge of the fraudulent lending practices of Ameriquest.

79. Upon information and belief, Deutsche Bank and AMS actively, knowingly and substantially participated in the commission of fraudulent lending by financing Ameriquest's fraudulent lending activities with knowledge thereof.

80. Alternatively or in addition, Deutsche Bank and AMS acted in pursuance of a common plan to commit a tortious act, actively take part in it, or further it by cooperation or request, or lent aid or encouragement to Ameriquest, or ratified and adopted the Ameriquest acts done for its benefit.

81. Alternatively or in addition, Deutsche Bank and AMS accepted the fruits of fraud with knowledge thereof.

82. Damages to the Plaintiffs were proximately caused thereby.

WHEREFORE, Thomas J. Orr and Phyllis A. Hollis seek a judgment against Defendant Deutsche Bank National Trust Co. and against Defendant AMS as follows:

A. Rescinding Mortgage; and

B. Granting the Plaintiffs' claim of recoupment and/or setoff, including equitable relief seeking the satisfaction, or reformation of the mortgage transaction as appropriate; and

C. Awarding restitution of the value conferred upon Deutsche Bank and AMS; and

D. Awarding actual damages; and

E. Awarding punitive damages; and

F. Granting such other relief as the court deems just and equitable.

Dated: 11-19-07

THOMAS J. ORR
Counselor at law
Attorneys for Plaintiff, Thomas J. Orr, trustee
Thomas J. Orr

By: /s/ Thomas J. Orr
Thomas J. Orr, Esq.

Dated:

LEGAL SERVICES OF NEW JERSEY
Attorneys for Plaintiff Phyllis A. Hollis
Margaret Jurow

By: /s/ Margaret L. Jurow
Margaret Lambe Jurow, Esq.

JURY DEMAND

Plaintiffs hereby request trial by jury.

SERVICE UPON ATTORNEY GENERAL

Service of a copy of the complaint in this matter is being made upon the Attorney General of the Sate of New Jersey, pursuant to the Consumer Fraud Act for the purpose of encouraging intervention, by mailing a copy of said complaint to Anne Milgram, Attorney General, Office of the Attorney General, Hughes Justice Complex, P.O. Box 080, 25 West Market Street, Trenton, NJ 08625-0080.

Dated: 11-19-07

THOMAS J. ORR
Counselor at law
Attorneys for Plaintiff, Thomas J. Orr, trustee

Thomas J. Orr

By: /s/ Thomas J. Orr
Thomas J. Orr, Esq.

Dated: 11-19-07

LEGAL SERVICES OF NEW JERSEY
Attorneys for Plaintiff Phyllis A. Hollis

Margaret Jurow

By: /s/ Margaret L. Jurow
Margaret Lambe Jurow, Esq.

APPENDIX D

Elizabeth C. Goodell, Esquire
bgoodell@clsphila.org
Id. No. 80155
COMMUNITY LEGAL SERVICES INC.
3638 N. Broad Street
Philadelphia, PA 19140
215-227-2400

For Defendant
Proceeding IFP

WELLS FARGO BANK N.A. TRUSTEE	:	COURT OF COMMON PLEAS
Plaintiff	:	
	:	PHILADELPHIA COUNTY
v.	:	
	:	TERM 2006
V. M.	:	
Defendant	:	NUMBER xxxx

ANSWER AND NEW MATTER

ANSWER

1. It is admitted that Plaintiff is Wells Fargo Bank National Association as Trustee. However, as this is a mortgage foreclosure, the chain of assignments to Plaintiff must clearly establish its right to foreclose on the mortgage at issue. The assignment to Wells that is referred to in the foreclosure complaint identifies the assignee as “Wells Fargo National Association as Trustee.” The Plaintiff and the assignee are therefore not the same. Further, neither the assignment nor the complaint identifies for whom or what Wells Fargo is a trustee. The complaint therefore does not properly identify the plaintiff. Foreclosure should therefore be denied.

2. Admitted.

3. Admitted.

4. It is admitted that Defendant signed loan papers. However, upon information and belief, the loan was set up based on income information that was not true or on underwriting standards that are unconscionable, as the loan payment was never affordable for Ms. M., as set forth below under New Matter.

5. It is admitted that Ms. M. signed a mortgage. However, it is denied that Plaintiff can foreclose for the reasons set forth in paragraphs 1 and 4 above, including that Plaintiff has not properly established its standing to bring a foreclosure.

6. It is denied that the mortgage now secures the property, as Defendant rescinds the transaction under the Truth in Lending Act.

7. It is admitted that Ms. M. was never able to afford the loan. However, it is denied that Plaintiff should be granted a judgment in foreclosure for the reasons set forth above and below under New Matter.

8. Denied for the reasons set forth above and below under New Matter.

9. Admitted.

WHEREFORE, Defendant prays this Court to find that the mortgage is unconscionable and the result of deceptive practices, deny Plaintiff's request to execute on Ms. M's home; grant other relief as is equitable; and award Defendant costs and attorneys fees.

NEW MATTER

1. Defendant V. M. is 68 years old and has lived in her home at 1841 Glenifer Street, Philadelphia for 20 years. Her home is the mortgaged property at issue in the instant foreclosure case.

2. Ms. M.'s income is now approximately $788 per month, a combination of her social security benefits and a small monthly pension. Her income was not more than that amount at the time the loan originated.

3. The mortgage loan that Plaintiff has foreclosed on originated in September 2004 by the lender Argent Mortgage.

4. The notice of default attached to the foreclosure complaint is dated November 7, 2005 and states that the loan was three months in default when the letter was sent – which implies that the default began in September 2005 – less than one year after the loan was originated.

5. Upon information and belief, the loan was originated by Argent under agreement with Plaintiff, and pursuant to Plaintiff's underwriting terms, so that the loan could be purchased and securitized in a trust for which Plaintiff is the trustee.

6. The loan payment of $434.76 per month does not include the taxes and insurance. When taxes and insurance are added, the monthly housing expense is approximately $535 per month, leaving Ms. M. only about $253 per month for heating, electricity, phone, water, food, medical expenses, home maintenance and other living expenses.

7. When the foreclosure first began, Ms. M.'s counsel requested all loan origination documents from Plaintiff, including all versions of the loan application and verification of income, to learn what income information was included in the loan

application to support a loan that was clearly unaffordable for Ms. M.. Plaintiff provided some loan origination documents, but not loan applications or income verification.

8. Upon information and belief, Argent used loan income that Ms. M. did not in fact have in arranging the loan.

9. The loan is an example of what has come to be called "predatory lending":

a. The mortgage payment clearly did not leave Ms. M. enough income each month to make that payment plus the utility bills, food and home maintenance.

b. Given that the loan went into foreclosure less than one year into its 30 year term, the loan was obviously "lending based on the value of the asset securing the loan rather than a borrower's ability to repay". Hargraves v. Capitol City Mortgage Corp, 140 F.Supp. 2nd 7, 20-21. See also Assocs. Home Equity Servs., Inc. v. Troup,343 N.J.Super. 254, 778 A.2d 529 (2001) (a characteristic of predatory lending is that the terms are so onerous there is a strong likelihood the borrower will be unable to repay the loan).

10. Defendant hereby rescinds the transaction pursuant to the Truth in Lending Act. Ms. M. does not recall having received the disclosures required under the Truth in Lending Act and, despite a formal discovery request in the instant foreclosure action to Plaintiff to produce them, Plaintiff has not done so. Defendant therefore avers on information and belief that the disclosures were not delivered as required.

First Defense: Unconscionability

11. Defendant incorporates all paragraphs above herein.

12. Based on the above-described context and nature of the loan transaction, the mortgage and the note which the mortgage secures are unconscionable, and thus unenforceable under Pennsylvania law.

WHEREFORE, Defendant requests that this Court enter judgment in her favor, order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice. In the alternative, Defendant asks the Court to set equitable terms for the repayment of any debt owed to Plaintiff and dismiss the foreclosure action with prejudice.

Second Defense: Deceptive Practices

13. Defendant incorporates all paragraphs above herein.

14. The lender knew or should have known that income information on the loan application was not accurate for Ms. M..

15. The lender paid a "yield spread premium" to a mortgage broker in connection with the loan, which means the lender essentially paid the broker to arrange a higher interest rate than Ms. M. was eligible for, without Ms. M.'s knowledge or consent.

16. Due to the circumstances set forth above, it is averred that the mortgage loan at issue here resulted from unfair and deceptive practices prohibited by Pennsylvania's Unfair Trade Practices and Consumer Protection Law, 73 P.S. §101 et seq.

WHEREFORE, Defendant requests that this Court enter judgment in her favor, order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice. In the alternative, Defendant asks the Court to set equitable terms for the repayment of any debt owed to Plaintiff and dismiss the foreclosure action with prejudice. Defendant further requests that the Court award Defendant attorneys fees and costs pursuant to 73 P.S. §209.

Third Defense: Equity

17. Defendant incorporates all paragraphs above herein.

18 Given the above-described predatory lending circumstances, it would be inequitable for the court to strictly enforce any contractual foreclosure remedy.

WHEREFORE, if the instant complaint is not dismissed, Defendant requests that this Court deny Plaintiff the foreclosure remedy and grant a more equitable remedy, such as a loan modification or rescission, and such other relief as is just and proper.

Fourth Defense: Truth in Lending Rescission

19. Defendant incorporates all paragraphs above herein.

20. Defendant's rescission of the loan under the Truth in Lending Act voids the mortgage.

WHEREFORE, Defendant requests that this Court enter judgment in her favor, order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice. In the alternative, Defendant asks the Court to set equitable terms for the repayment of any debt owed to Plaintiff and dismiss the foreclosure action with prejudice

4-16-07 /s/ Elizabeth C. Goodell

Date: _________________ ___________________________________

ELIZABETH C. GOODELL, ESQUIRE
Attorney for Defendant

COMMUNITY LEGAL SERVICES
BY: ELIZABETH GOODELL, ESQUIRE
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Attorney for Defendant
Proceeding IFP

BANK OF AMERICA	:	COURT OF COMMON PLEAS
Plaintiff	:	
	:	PHILADELPHIA COUNTY
v.	:	
	:	TERM 2007
C. M.	:	
Defendant	:	NUMBER

ANSWER, NEW MATTER AND COUNTERCLAIM

1. It is admitted that Plaintiff is as named.

2. Admitted.

3. Admitted that Plaintiff is seeking foreclosure on the mortgage, which is dated and recorded as set forth in paragraph 3 of the Complaint. However, the loan, made by Plaintiff "s/b/m" Fleet National Bank, is a stark example of predatory lending, a loan given to a mentally ill homeowner whose low, fixed monthly income never offered any hope of making the loan payments. Ms. M. herein raises the defenses of unconscionability, unclean hands and equity. See New Matter below.

4. It is admitted that the debt was secured by a mortgage, but the mortgage is now void pursuant to the Truth in Lending Act. See New Matter below.

5. It is admitted that the property is as described, but the mortgage is now void pursuant to the Truth in Lending Act. See New Matter below.

6. Admitted. Ms. M. is also the resident of the property.

7. It is admitted that Ms. M. is not current on the payments. Ms. M. was never able to afford the payments, a fact that must have been obvious to Plaintiff "s/b/m" Fleet National Bank,

8. Denied as a conclusion of law.

9. Admitted.

10. Admitted that Ms. M. was not granted HEMAP assistance, as one of the requirements is that she be able to afford the mortgage on her own within two years. As she never had enough income to afford the loan, she was of course denied HEMAP assistance.

11. Admitted.

WHEREFORE, Defendant requests that the Court issue an order finding that the mortgage is void and dismiss the instant foreclosure action with prejudice.

NEW MATTER

12. Defendant incorporates all paragraphs above by reference as if set forth herein in full.

13. Defendant, C. M. (hereinafter "Ms. M." or Defendant) is 64-years old and has lived in the house at issue for her entire life.

14. Ms. M. has a mental illness and has been under the supervision of a psychiatrist for at least ten years.

15. Ms. M. and her brother and sister inherited the house when their mother died about ten years ago. Her brother died about seven years ago and her sister gave up her interest in the property, leaving Ms. M. as the only owner of the house as of August of 1999.

16. After her brother died, Ms. M. was alone in managing the house and her finances for the first time in her life.

17. Ms. M.'s monthly income is now approximately $638 in disability benefits, supplemented by approximately $100 per month in food stamps. Her income was about the same back in 1999 when the house was deeded into her name along.

18. In early 2000, First Union National Bank made a loan to Ms. M. with a principal balance of $27,000 and a monthly payment of approximately $150.

19. In July of 2002, CitiFinancial Inc. made a loan to Ms. M. with a principal balance of approximately $10,400 and a monthly payment of approximately $180. The CitiFinancial loan did not refinance the First Union loan, so Ms. M. had a combined payment on the two mortgages of $330 per month, without an escrow for taxes and insurance, out of her monthly income of $638. Therefore, in July of 2002, Ms. M. was already over her head in mortgage debt.

20. In October of 2002, about three months after the CitiFinancial loan, Plaintiff's predecessor, Fleet Bank, made a loan to Ms. M. with a principal balance of $50,000. Ms. M. does not recall the amount of the monthly payment under the 2002 Fleet loan.

21. The 2002 Fleet loan refinanced the CitiFinancial loan, paying approximately $10,400 to Citi. The 2002 Fleet loan did not refinance the First Union loan.

22. Ms. M. made the payments under the 2002 Fleet loan mostly by using the money she received from the 2002 Fleet loan.

23. By mid-2004, Ms. M. was in dire financial trouble. Having used all of the money from the 2002 Fleet loan, she could no longer make the payments on the loan.

24. Ms. M. therefore called the Fleet office that made the 2002 loan and asked if there was a way to lower her payment. The Fleet loan officer told her to borrower more money.

25. In August of 2004, Fleet made a new loan to Ms. M. in the amount of $80,000. The monthly payments due under the loan were and are $492.

26. The 2004 Fleet loan refinanced the 2002 Fleet loan but did not refinance the First Union loan.

27. Therefore, Ms. M.'s combined mortgage payments after the 2004 Fleet loan were $642 per month. The mortgage loan payments were more than her monthly income, without an escrow for taxes and insurance.

28. Ms. M. made the payments on the 2004 Fleet loan by using the money from the 2004 Fleet loan.

29. When the money from the 2004 Fleet loan ran out, Ms. M., obviously, could not make the payments and Plaintiff filed this foreclosure action.

DEFENSES
<u>UNCONSCIONABILITY, UNCLEAN HANDS, EQUITY</u>

30. Defendant incorporates all paragraphs above herein.

31. Ms. M.'s mental illness made her especially vulnerable to the sales practices of Fleet Bank which allowed two loans to be made to her that she obviously could not afford.

32. Her mental illness and obvious vulnerability combined with her severe financial distress at the time of the second Fleet loan transaction, which severe financial distress was in large part caused by the prior Fleet loan, left her without a meaningful choice.

33. The terms of both loans were grossly one-sided and unfavorable to Ms. M., as the loan terms were tantamount to her surrendering her home, since foreclosure was inevitable.

34. Both Fleet loans, especially the second loan upon which Plaintiff seeks to foreclosure, are predatory loans as recognized by Pennsylvania's legislature, Pennsylvania's Department of Banking, and Pennsylvania's Commonwealth Court. (*Mortgage Foreclosure Filings in Pennsylvania: A Study by The Reinvestment Fund for the Pennsylvania Department of Banking*.; "Losing the American Dream: A Report on Residential Mortgage Foreclosures and Abusive Lending Practices in Pennsylvania." March 16, 2005, Pennsylvania Banking Secretary A. William Schenck, III.; McGlawn v. Pa. Human Relations Comm'n, 891 A.2d 757 (Comwlth. Ct. 2006).

35. One common feature of a predatory loan is that such loans are "based on the value of the asset securing the loan rather than the borrower's capacity to repay it." McGlawn v. Pa. Human Relations Comm'n, 891 A.2d 757, 769 (Comwlth. Ct. 2006), citing Hargraves v. Capital City Mortgage Corp., 140 F.Supp.2d 7, 21 (D.D.C.2000).

36. It is also characteristic of predatory loans that they "do not fit the borrower either because the borrower's needs are not met or because the terms are so onerous there is a strong likelihood the borrower will be unable to repay the loan." Id.,

citing <u>Assocs. Home Equity Servs., Inc. v. Troup</u>, 343 N.J.Super. 254, 778 A.2d 529 (2001).

37. Plaintiff having acquired the lender that made predatory loans to Ms. M. with knowledge or reckless to the fact that Ms. M. would certainly lose her home because of the loans, has unclean hands in this matter.

38. The defense of unclean hands is grounds for denying equitable relief to Plaintiff in these circumstances. Shapiro v. Shapiro, 415 Pa. 503, 506 (1964); Doherty v. Adal Corp., 437 Pa. 109, 112 (1970); Brentwater Homes, Inc. v. Weibley, 471 Pa. 17, 18 (1977)

39. This Court generally has the equitable power to deny the foreclosure relief sought by Plaintiff (an order allowing sale of Ms. M.'s home). Greentree Consumer Discount Co. v. Newton, 909 A.2d 811, 816-817 (Pa. Super. 2006); Fleet Real Estate Funding v. Smith, 366 Pa.Super. 116, 530 A.2d 919, 923 (1987).

WHEREFORE, Defendant requests that the Court deny the foreclosure remedy to Plaintiff either by finding that the loan and mortgage contracts are void or, in the alternative, by fashioning another equitable remedy that allows Defendant to remain in her home; and that the Court dismiss the instant foreclosure action with prejudice.

<u>COUNTERCLAIM FOR INFLICTION OF EMOTIONAL DISTRESS</u>

40. Defendant incorporates all paragraphs above herein.

41. When Fleet made the loan to Ms. M., Fleet did so with knowledge or in reckless or in negligent disregard for the fact that she could not afford the loan payment on her monthly income of approximately $638; and with knowledge or in

reckless or negligent disregard for the fact that the loan would result in the loss of Ms. M.'s home.

42. Fleet's actions in setting up two loans that Ms. M. could clearly not afford have caused Ms. M. intense and predictable anxiety and physical illness. She suffers from an anxiety disorder to start with, and her inability to keep up with the loan payments and the threat of losing her home have brought on severe anxiety attacks and hyperventilation. She suffers from a heart condition, and her anxiety has exacerbated it.

43. Having acquired Fleet by merger, Plaintiff is liable for claims that could be raised against Fleet.

WHEREFORE, Defendant asks this Court to find that Plaintiff is liable for damages for infliction of emotional distress; to award Defendant damages including punitive damages; to offset any amount owed by Defendant to Plaintiff against the damages awarded; and to order Plaintiff to pay to Defendant any remaining damages.

Date: ________________

/s/ Elizabeth C. GOODELL
____
ELIZABETH C. GOODELL, ESQUIRE
Attorney for Defendant
Community Legal Services
3638 N. Broad Street
Philadelphia, PA 19140

Notice to Plead: To Plaintiff You are hereby noticed to file a response to the within New Matter and Counter Claim within 20 days of service or suffer a judgment by default.

Elizabeth C. Goodell, Esquire
Attorney for Defendant

COMMUNITY LEGAL SERVICES

BY: ELIZABETH GOODELL, ESQUIRE
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Philadelphia, PA 19140
(215) 227-2400 ext. 2424

Attorney for Defendant
Proceeding IFP

	:	COURT OF COMMON PLEAS
Interstate TD Investments	:	
Plaintiff	:	
	:	PHILADELPHIA COUNTY
v.	:	
	:	Term 2006
	:	
G. L.	:	NUMBER xxxx
Defendant	:	

ANSWER, NEW MATTER AND COUNTER CLAIM

ANSWER

1. It is admitted Plaintiff is as named and that the public records indicate that Plaintiff is the assignee of the mortgage.

2. It is admitted that Defendant is G. L. and that Ms. L. is the owner and resident of the property at issue. It is denied that Ms. L. is “mortgagor” for the reasons set forth below.

3. It is admitted that Defendant, G. L., borrowed money from Plaintiff's predecessor, Beneficial Consumer Discount Company, on or about January 18, 2002. However, Ms. L. specifically asked if the loan would be against the house and was told that it would not by the Beneficial employee/loan agent. Ms. L. relied on his false representation in signing the loan documents. The mortgage was therefore obtained by fraud and is void. The loan transaction also violated Pennsylvania's Act 6 and Unfair Trade Practices and Consumer Protection Law, as set forth more fully below under New Matter.

4. It is admitted that Ms. L. has not made a number of payments due under the loan. However, it is denied for the reasons set forth above and under New Matter below that the debt can be accelerated under a mortgage, as the mortgage was obtained by fraud.

5. It is admitted that Defendant is in default under the loan. As set forth above and below under New Matter, it is denied that Plaintiff can foreclose on a mortgage.

6. Denied for the reasons set forth above and below under New Matter.

7. Denied for the reasons set forth above and below under New Matter.

8. Ms. L. does not recall receiving the notice required by Act 6 and Act 91 and therefore denies that the notices were sent. Defendant requests a copy of the certified mail receipt identified by Plaintiff in paragraph 8 of the complaint.

WHEREFORE, Defendant prays this court to dismiss the instant complaint with prejudice and award Defendant attorneys fees and costs pursuant to 41 P.S. §503 and 73 P.S. §201-9.2.

NEW MATTER

9. Defendant, G. L., here incorporates all paragraphs above.

10. Prior to the current loan with Beneficial, Ms. L. had one loan with Beneficial which was not secured by a mortgage. The loan originated in November 1999 and was co-signed by her father, Jerry L..

11. Because Ms. L. already had a loan from Beneficial, Beneficial contacted her to see if she would take out another loan.

12. The first name of the person from Beneficial who contacted Ms. L. about taking out a new loan was Jeff.

13. Ms. L. specifically asked Jeff if the new loan would be "against the house", because Ms. L. did not want a debt against the house.

14. Jeff answered Ms. L.'s question by saying no, the loan would not be against the house.

15. Ms. L. went to Beneficial's office and met with Jeff to sign the new loan documents.

16. Jeff showed Ms. L. where to sign on several documents.

17. Ms. L. did not notice that any of the documents stated that the loan would be a mortgage.

18. Because of the high interest rate, 22%, the loan at issue here falls under the requirements of 15 U.S.C. §1602(aa) and §1639, under the Truth in Lending Act.

19. Pursuant to 15 U.S.C. §1639(a), Beneficial had to deliver to Ms. L. a disclosure at least three days before the closing of the loan, stating, among other information, that the loan would be a mortgage against her home.

20. Ms. L. did not receive the disclosure required by 15 U.S.C. §1639(a) at least three days before the loan closing, which would have warned her in a simple single-page notice that the loan would be a mortgage debt.

21. 41 P.S. §401 requires that a mortgage lender send the disclosures required by the Truth in Lending Act.

22. Beneficial's failure to deliver the "§1639" disclosure to Ms. L. is therefore a violation of 41 P.S. §401.

23. Beneficial's failure to deliver the "§1639" disclosure and its representation to Ms. L. that the loan would not be against the house constituted fraud and a violation of Pennsylvania's Unfair Trade Practices and Consumer Protection Act, 73 P.S. §201-1 et seq.

24. Plaintiff is not a holder in due course regarding the debt it is seeking to collect, for reasons including but not limited to: Plaintiff became the owner of the debt after it was in default.

25. Because the loan falls under the requirements of 15 U.S.C. §1602(aa) and §1639, the current owner of the debt is liable for all claims that could be raised against the original creditor, pursuant to 15 U.S.C. §1641(d).

26. Plaintiff is therefore liable for all claims Ms. L. may have against Beneficial.

WHEREFORE, Defendant prays this court to dismiss the instant complaint with prejudice and award Defendant attorneys fees and costs pursuant to 41 P.S. §503 and 73 P.S. §201-9.2.

COUNTER CLAIMS

27. Defendant, G. L., here incorporates all paragraphs above.

WHEREFORE, Defendant prays this court to award her actual and punitive damages for fraud; or actual damages, treble damages, attorneys fees and costs pursuant to 73 P.S. §201-9.2; or actual damages, fees and costs pursuant to 41 P.S. §§ 503, 504; and damages pursuant to 15 U.S.C. §1540(d). Where a statute of limitations has expired, Defendant prays that the damages be awarded in recoupment against the debt sued upon. Defendant further prays that the damages be offset against the debt sued upon, that the Court find that Defendant owes no debt to Plaintiff; and that the foreclosure complaint be dismissed with prejudice.

Respectfully submited

/s/Elizabeth C. Goodell

Elizabeth C. Goodell, Esquire
Attorney for Defendant

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Attorney for Defendant
Proceeding IFP

DLJ MORTGAGE CAPITAL, INC.	:	COURT OF COMMON PLEAS
Plaintiff	:	
	:	PHILADELPHIA COUNTY
v.	:	
	:	TERM 2006
L. W.	:	
Defendant	:	NUMBER xxxx

ANSWER, NEW MATTER AND COUNTERCLAIMS

Defendant L. W. hereby responds to Plaintiff's foreclosure complaint. Defendant F. W. died in October of 2005.

1. (a) Denied. Defendant has been unable to find any documentation that DLJ Mortgage Capital Inc. is a holder of a mortgage on her home. Undersigned counsel has access to two on-line resources for identifying mortgages and assignments of mortgage. Print-outs from these two resources regarding Defendant's home are attached hereto as Exhibit 1. Both resources show the mortgage referred to by Plaintiff – to National Future Mortgage recorded on August 30, 2000 – but no assignments after the original mortgage. Further, as set forth below, Defendant has discovered that the mortgage was originated in an illegal manner which casts doubt on the legitimacy of any subsequent assignments.

   (b) Admitted.

   (c) Admitted.

2. (a) Denied. F. W. is deceased.

(b) Admitted.

(c) Denied. F. W. is deceased.

(d) Admitted in part, denied in part. L. W. is the real owner of the property, however, L. W.' signature on the mortgage upon which Plaintiff seeks to foreclose was obtained by fraud.

(e) Denied as a conclusion of law.

3. (a) It is denied that the mortgage can be enforced, as it was obtained by fraud and in violation of statute, as set forth in detail below under New Matter.

(b) Denied. There is no evidence that an assignment of mortgage was ever recorded.

(c) Admitted in part; denied in part. It is admitted that Defendant signed a document that turned out to be a mortgage. However, it is denied that the mortgage can be enforced, as it was obtained by fraud and in violation of statute, as set forth in detail below under New Matter.

(d) Admitted.

(e) Denied. The averment in the complaint is not sufficient to prove an assignment of mortgage to Plaintiff. The Pa. Rules of Civil Procedure require either that the instrument be attached or a recording citation provided. Plaintiff has complied with neither requirement, having only stated that the recording date and citation are "as recorded".

(f) It is denied that Plaintiff attached all the necessary documents. Plaintiff did not attach an assignment of mortgage.

4. Admitted in part, denied in part. It is admitted that, after her husband died, Defendant did not make payments on the mortgage because (a) she had been told by the originators of the loan that the loan was her husbands only and that she was not and would not be responsible for the loan; and (b) she cannot afford the payments. However, it is denied that the mortgage can be foreclosed because the mortgage was obtained by fraud and in violation of statute, as set forth in detail below under New Matter.

5. Denied for the reasons set forth in Paragraphs 3 and 4 above.

6. Denied for the reasons set forth in Paragraphs 3 and 4 above.

7 (a) & (b) Denied as conclusions of law.

8. Admitted.

9. Admitted.

WHEREFORE, Defendant requests that the Court order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice.

NEW MATTER

FACTS IN SUPPORT OF DEFENSES AND COUNTERCLAIMS

1. The mortgagee on the mortgage that Plaintiff seeks to foreclose is National Future Mortgage (hereinafter referred to as "National Future").

2. National Future originated the mortgage and the loan secured by the mortgage under an illegal agreement with home improvement contractors Jerry Gilbert and Craig Gilbert, as set forth below.

3. In or about late 1999, Richard Forte, the president of National Future, was contacted by a lawyer who operated as a title insurance agent and settlement agent for mortgage loans. The title agent, Paul Gelman, asked Richard Forte if National Future Mortgage would allow Jerry Gilbert to originate mortgage loans in Pennsylvania using the name of National Future Mortgage.

4. Pursuant to the agreement, Richard Forte agreed and knew that National Future Mortgage would perform no origination services for any of the loans, and agreed and knew that the Gilberts would undertake a range of actions on behalf of National Future Mortgage, including but not limited to: Representing to potential borrowers, lenders and others that National Future Mortgage was originating the loans; collecting information from potential borrowers; filling out applications in the names of the potential borrowers and stating on the applications that National Future Mortgage was submitting the application; submitting the applications and numerous other documents on behalf of National Future Mortgage; deciding the amount of the fee to be paid to National Future Mortgage and reaching agreement with lenders for the payment of such fees; negotiating for yield spread premium payments (lender-paid fees to the broker) on behalf of National Future Mortgage; obtaining loan commitment agreements from lenders on behalf of National Future Mortgage; and setting up loan closings in which National Future Mortgage would be paid various fees from the loans.

5. National Future Mortgage remained in control of the undertaking with the Gilberts in the following ways:

a. National Future Mortgage controlled the use of its licenses and could have withdrawn permission to the Gilberts at any time.

b. National Future Mortgage controlled the loan origination fees. The checks for such fees were always made payable to NFM and it was within the discretion of NFM to pay or not to pay the Gilberts for the work that NFM had authorized.

c. National Future Mortgage controlled which lenders the Gilberts could deal with, as the Gilberts could only apply to the lenders that had an agreement to accept loans from National Future Mortgage.

6. Under the agreement to originate the loans, Paul Gelman would receive the loan funds and issue checks to disperse the loan proceeds. Gelman would deliver checks payable to National Future Mortgage to the Gilberts. The Gilberts would deliver the check or checks for the origination fee or broker fee to National Future Mortgage and National Future Mortgage would then pay most of the fee back to the Gilberts.

7. The Gilberts, Paul Gelman and National Future Mortgage originated between fifty and sixty loans under the agreement from late-1999 through April of 2002.

8. The Pennsylvania Mortgage Bankers and Brokers Act, 63 P.S. §456.501 et. seq., prohibits a person without a license from operating as a mortgage broker or lender in Pennsylvania, 63 P.S. §456.303(a) and §456.314(a), and prohibits any party with a license under the Act from consenting to a violation of the statute, 63 P.S.314(c).

9. The federal Real Estate Settlement and Procedures Act (RESPA), 12 U.S.C. §2601 et seq. prohibits giving and receiving any portion of any settlement charge in a mortgage loan closing to a party that performed no services. 12 U.S.C. §2607(b)

10. A loan secured by defendant L. W.' home was among the loans that resulted from the agreement.

11. L. W. (hereinafter “Mrs. W.” or “Defendant”) purchased her home at 2936 Kip Street in Philadelphia in 1997 (hereinafter referred to as “the house” or “Mrs. W.’ home”).

12. Mrs. W. was married to F. W. at the time she purchased the property, but she purchased it in her own name only.

13. In the summer of 2000, Mrs. W.’ husband came into contact with Interstate Remodeling Contractors, a corporation owned and operated by Jerry Gilbert and Craig Gilbert.

14. Mr. W. arranged for Jerry Gilbert and Craig Gilbert to come to the house to discuss home repairs.

15. On or about August 3, 2000, Jerry Gilbert and Craig Gilbert met with Mr. W. at the house.

16. Mr. W. called Mrs. W. in from the back yard while he was meeting with the Gilberts and asked her to sign a contract for home repairs. When Mrs. W. asked Mr. W. how much the repairs were going to cost, Mr. W. told her not to worry about it.

17. The contract signed by Mrs. W. on August 3, 2000 called for the installation of 12 windows, 2 security doors, a gas heater and a window air conditioner. A copy of the contract that was left with Mr. W. is attached here as Exhibit 2.

18. Although the house was in Mrs. W.’ name alone, the Gilberts dealt only with Mr. W. regarding the loan and interacted with Mrs. W. only to get her signature on a few documents, including the home repair contract described above.

19. The home repair contract stated the price of the work to be $15,400. See Exhibit 2.

20. Because of the Gilberts' course of conduct in many transactions (as set forth above and in further detail below), Plaintiff believes and avers that the work to be performed under the contract was worth far less than the price stated by the Gilberts and that the Gilberts deliberately stated a price that was grossly inflated as part of a plan to misappropriate loan funds.

21. Pursuant to their agreement with National Future Mortgage that they could originate loans acting as National Future Mortgage, the Gilberts created documents which evidence a loan from National Future Mortgage to F. W., with a mortgage on the house.

22. a. The Gilberts brought the loan documents they prepared to the house to be signed on or about August 18, 2000 (the date that appears on the loan documents).

b. Mrs. W. found Craig Gilbert and Jerry Gilbert meeting with her husband on that day as she was coming home from the grocery store.

23. Mrs. W. remembers only Craig Gilbert and Jerry Gilbert present with her husband on the day the loan papers were signed.

24. Mrs. W. asked if she needed to be present; Craig Gilbert answered that she did not, that the loan was her husband's.

25. Mrs. W. asked again if the home repair loan was going to be her loan. Both Jerry Gilbert and Craig Gilbert answered that it would not be her loan, it would be her husband's responsibility.

26. That Jerry Gilbert and Craig Gilbert told Mrs. W. that the loan was not going to be her responsibility in response to her questions on the occasion when the Gilberts had to obtain Mrs. W.' signature on the mortgage is circumstantial evidence that the Gilberts intended that Mrs. W. would rely on that representation in signing the mortgage.

27. Mrs. W. then went into the kitchen to put groceries away while her husband signed papers with the Gilberts.

28. Some minutes later, her husband called Mrs. W. back into the room to sign a paper. Mrs. W. signed the paper in reliance on the representation the Gilberts had made that she would not be responsible for the loan.

29. The Gilberts did not give Mrs. W. copies of any of the documents the she signed or any of the documents that her husband signed.

30. Mrs. W. was never given the notices of right to cancel the loan to which she was entitled under both federal and state law.

31. As a result of the home repair financing contract, 12 windows and 2 doors were installed at the house, but the W.' did not receive a heater and air conditioner.

32. The papers that the Gilberts left with Mr. W. indicate a loan from National Future Mortgage to F. W. in the amount of $25,500 with an interest rate of 14%, an annual percentage rate of 15.202%, a monthly payment of $302.14, and a balloon payment of $22,991.41 after 15 years.

33. A true and correct copy of the settlement statement for the loan left with Mr. W. is attached hereto as Exhibit 3, and indicates that:

a. $1,275 and $6, respectively, were paid to National Future Mortgage as a loan origination fee and a credit report fee;

b. A total of $1,140 was paid to Paul Gelman/Hunter Agency for various fees;

c. $4,610.50 was distributed as "disbursements to borrower".

d. Most of the remainder of the $25,500 (approximately $17,545) was to be paid to various creditors, including the City of Philadelphia for property tax and water liens.

34. Mrs. W. does not know how much the Gilberts collected for the home repairs.

35. The recorded mortgage indicates a security interest given by Mrs. W., notarized by Paul Gelman. A copy of the mortgage as recorded is attached here as Exhibit B to the complaint.

36. As set forth above, Mrs. W. remembers only Jerry Gilbert and Craig Gilbert as present at the signing of the loan documents. She therefore avers that Paul Gelman did not properly notarize the mortgage.

37. It is apparent now that the loan documents were fraudulent and that the Gilberts prepared papers that created a false appearance of a loan from National Future Mortgage that never existed (as set forth more fully below).

38. For the following reasons, it is now apparent that National Future Mortgage did not make a loan to Mr. and Mrs. W.:

a. In litigation concerning one of the other loans originated under the agreement among the Gilberts, NFM and Paul Gelman, Paul Gelman produced a copy of a check that apparently funded three separate loans supposedly originated by National Future Mortgage. A true and correct copy of the check with deposit slip is attached here as Exhibit 4.

i. The loan involved in the prior litigation closed on August 18, 2000, the same date as the W. loan.

ii. One of the loan amounts listed on the deposit slip is $25,500, the same amount as the W. loan. Plaintiff therefore believes and avers that the check provided the funds for the W. loan.

iii. The check is a cashier's check purchased from Commerce Bank, rather than a check drawn on an account owned by NFM.

iv. The Gilberts used accounts with Commerce Bank to conduct their home repair and loan transactions. Plaintiff therefore believes and avers that the funds for the loan came from the Gilberts, not National Future Mortgage.

b. Richard Forte, president of National Future Mortgage, testified that National Future Mortgage did not perform origination services on any of the loans in which the Gilberts were involved, which rules out the loan underwriting and transfer of funds that would have been done by National Future Mortgage if it were the lender.

39. Mr. W. payments under the loan to <u>Key Home Equity Services</u> until his death in October of 2004.

40. Therefore, Defendant avers that, somehow, a loan that National Future Mortgage never made was transferred by National Future Mortgage to Key Home Equity Services.

41. Mrs. W. does not know if Key in fact made a payment to any party for the National Future loan and demands proof that Key was a purchaser for value from National Future Mortgage.

42. Mrs. W. also demands proof that Plaintiff was a purchaser for value of the loan.

43. Approximately $15,000 has been paid on the loan to date.

44. Assuming that the Gilberts themselves funded the loan out of their own funds:

a. There was never a loan contract between the W.' and the Gilberts that could bind them to repay the Gilberts;

b. Mrs. W. does not have an equitable duty to repay the Gilberts, as their own deceptive conduct created the debt in the first place;

c. The loan documents that created an appearance of a loan from National Future Mortgage could not legally bind Mrs. W. to make payments to any purported assignee of a loan that did not exist;

d. Mrs. W. does not have an equitable duty to make further payments to any purported assignee of the loan, as she has already paid far more than the value of the home repairs she received; and, further, if any party received funds from Key in the sale of the $25,500 fraudulent loan to Key, that party is liable for repaying the sum to Key, and the sale price should be repaid down the line of assignments.

e. Mrs. W. is entitled to a legal holding that there is no legitimate loan or mortgage and that further payment on the fraudulent loan is not required.

FIRST DEFENSE

<u>ILLEGALITY OF CONTRACT</u>

45. Defendant incorporates all paragraphs above by reference as if set forth herein in full.

46. The loan and mortgage contract which Plaintiff seeks to enforce is illegal under Pennsylvania law for reasons including but not limited to the following.

47. a. The loan and mortgage transaction was initiated as a home improvement contract and constitutes a home improvement financing contract within the meaning of Pennsylvania's Home Improvement Financing Act (HIFA), 73 P.S. § 500-101 *et seq*.

b. The transaction was structured in violation of an express prohibition in HIFA against charging consumers fees, costs, commissions or other charges not authorized by the act, 73 P.S. § 500-407 and/or in violation of an express prohibition against including consolidation of other debt, 73 P.S. §500-408.

48. As set forth above, the loan and mortgage transaction violated the Pennsylvania Mortgage Bankers and Brokers Act, 63 P.S. §456.501 et. seq.

WHEREFORE, Defendant requests that the Court find that the loan and mortgage contracts are illegal and void, order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice.

SECOND DEFENSE

FRAUD AND UNFAIR AND DECEPTIVE PRACTICES

49. Defendant incorporates all Paragraphs supra by reference as if set forth herein in full.

50. The lender violated the Unfair Trade Practices and Consumer Protection Law (the "UTPCPL"), 73 P.S. §201-1 et seq. for reasons including but not limited to the following.

51. The loan originators deceived Mrs. W. when she asked them if she would be responsible for the loan. They told her that she would not be responsible for the loan when in fact her house, which was not in her husband's name, could be taken if the loan payments were not made.

52. Mrs. W. would not have signed the loan document if the loan originators had not deceived her when she asked them if she would be responsible for the loan.

53. The Gilberts' misrepresentation constituted both common law fraud and a violation of the UTPCPL.

54. Because the loan transaction originated with a solicitation of Mrs. W. at her home, Mrs. W. has a right to cancel the transaction that does not begin to run until she is given notice of the right and an address to which to send her cancellation. 73 PS sec 201-7.

55. Mrs. W. was never given notice of her right to cancel the transaction, either under state or federal law. She therefore has the right to cancel the transaction and she is exercising the right to cancel.

56. The steps taken by National Future Mortgage, the Gilberts and Paul Gelman to misrepresent that National Future Mortgage was the originator of the loan violates the following prohibitions of the UTPCPL against:

a. Passing off goods or services as those of another, 73 P.S. §201-2(4)(i);

b. Causing likelihood of confusion or of misunderstanding as to the source, sponsorship, approval or certification of goods or services, 73 P.S. §201-2(4)(ii);

c. Causing likelihood of confusion or of misunderstanding as to affiliation, connection or association with, or certification by, another, 73 P.S. §201-2(4)(iii);

d. Representing that goods or services have sponsorship, approval, characteristics (etc.) that they do not have or that a person has a sponsorship, approval, status, affiliation or connection that he does not have, 73 P.S. §201-2(4)(v); and

e. Fraudulent or deceptive conduct which creates a likelihood of confusion or of misunderstanding, 73 P.S. §201-2(4)(xxi).

57. Mrs. W. had no way of knowing of the deceptive conduct committed by National Future Mortgage in allowing the Gilberts to operate as National Future Mortgage and in issuing false loan documents that created an appearance of a loan from National Future Mortgage.

WHEREFORE, Defendant requests that the Court find that the loan and mortgage contracts are void, order Plaintiff to release the mortgage of record and return the loan note marked satisfied, and dismiss the instant foreclosure action with prejudice.

COUNTERCLAIMS

COUNT I
ACT 6 of 1974

1. Defendant incorporates all Paragraphs supra by reference as if set forth herein in full.

2. As set forth above, the transaction was structured in violation of an express prohibition in HIFA, section 500-407, against charging consumers fees, costs, commissions or other charges not authorized by the act.

3. As set forth above, all the loan fees included in the loan were paid to parties who participated in the deceptive origination of the loan and all fees were therefore unreasonable and excessive.

4. Under Act 6 of 1974, Mrs. W. is entitled to offset against any debt she may be found to owe damages of three times the amount of the excess charges paid; and is entitled to an award of reasonable attorney's fees and costs. 41 P. S. §§502, 503.

COUNT II
RESPA

5. Defendant incorporates all Paragraphs supra by reference as if set forth herein in full.

6. As set forth above, the loan violated the federal Real Estate Settlement Procedures Act (RESPA).

WHEREFORE, pursuant to12 U.S.C. §2601 et seq., Defendant requests that the Court award, as an offset against any debt she may be found to owe, damages; and award reasonable attorney's fees and costs.

COUNT III

UTPCPL

7. Defendant incorporates all Paragraphs supra by reference as if set forth herein in full.

8. As set forth above, the loan violated Pennsylvania's Unfair Trade Practices and Consumer Protection Law (UTPCPL).

WHEREFORE, pursuant to 73 P.S. §201 et seq., Defendant requests that the Court award, as an offset against any debt she may be found to owe, damages and triple damages; and award reasonable attorney's fees and costs.

/s/ Elizabeth C. Goodell

Date: ________________ ________________________________

ELIZABETH C. GOODELL, ESQUIRE
Attorney for Defendant
Community Legal Services
3638 N. Broad Street
Philadelphia, PA 19140

COMMUNITY LEGAL SERVICES
BY: ELIZABETH GOODELL, ESQUIRE
Id. # 80155
3638 N. Broad Street
Philadelphia, PA 19140
(215) 227-2400, ext. 2424

Attorney for Defendant
Proceeding IFP

CERTIFICATE OF SERVICE

I, Elizabeth C. Goodell, Esquire, attorney for Defendant, hereby certify that on this date I served a true and correct copy of Defendant's Answer, New Matter and Counterclaims on the Attorney for Plaintiff, identified below, by First Class U.S. Mail, postage prepaid at the address listed below:

Barbara Fein, Esquire
425 Commerce Drive
Suite 100
Fort Washington, PA 19034

Date: ________________

____
ELIZABETH C. GOODELL, ESQUIRE
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Tele.: (215) 227-2400

Attorney for Defendant

BANK OF NEW YORK Plaintiff, vs. S. H. L. Defendant	PHILADELPHIA COUNTY COURT OF COMMON PLEAS CIVIL DIVISION TERM 2007 No. xxxx

DEFENDANT'S ANSWER AND NEW MATTER

Defendant S. H. L., by counsel, hereby answers the complaint in foreclosure.

1. Admitted.

2. Admitted.

3. It is admitted that defendant signed mortgage loan documents prepared by America's Wholesale Lender and that the mortgage was recorded as set forth. However, the loan is unconscionable and predatory; and is rescinded under the Truth in Lending Act.

4. Admitted.

5. Admitted in part and denied in part. It is admitted that Defendant has missed monthly mortgage payments, but it is denied as a conclusion of law for the reasons set forth above and in greater detail in New Matter below that the entire principal balance and all interest are collectible forthwith.

6. Denied for the reasons set forth above and under New Matter.

7. Denied as a conclusion of law.

8. Denied. The notice attached to the complaint does not comply with Act 91, as it does not include a list of housing counseling agencies.

9. Admitted.

WHEREFORE, Defendant requests that the complaint in foreclosure be dismissed with prejudice.

New Matter

10. Defendant S. L. is 46 years old and has lived at the property for 7 years. His home is the property against which Plaintiff seeks to foreclose.

11. Plaintiff's loan was originated by America's Wholesale Lenders on or about March 9, 2006.

12. Mr. L. is a Korean immigrant with a very limited command of English.

13. Mr. L.'s income was, at the time of the loan, between $800 and $1100 per month.

14. To get the loan approved, the loan processor exaggerated Mr. L.'s monthly income on the loan application to $4397 per month.

15. Mr. L. suffers from severe psoriasis which has left him unable to work.

16. The monthly payment of approximately $755 (including taxes and insurance) was not manageable for Mr. L., and he fell behind within a few months after the first payment was due.

17. Undersigned counsel evaluated the loan under the Truth in Lending Act (TILA) and found material errors in the disclosures required by TILA. The errors give rise to the right to rescind the loan.

<u>First Defense: Unconscionability and Predatory Lending</u>

18. The preceding paragraphs are realleged and reincorporated herein.

19. The loan upon which Plaintiff seeks to foreclosure, is a predatory loan as recognized by Pennsylvania's legislature, Pennsylvania's Department of Banking, and Pennsylvania's Commonwealth Court. (Mortgage Foreclosure Filings in Pennsylvania: A Study by The Reinvestment Fund for the Pennsylvania Department of Banking.; "Losing the American Dream: A Report on Residential Mortgage Foreclosures and Abusive Lending Practices in Pennsylvania." March 16,

2005, Pennsylvania Banking Secretary A. William Schenck, III.; McGlawn v. Pa. Human Relations Comm'n, 891 A.2d 757 (Comwlth. Ct. 2006).

20. One common feature of a predatory loan is that such loans are "based on the value of the asset securing the loan rather than the borrower's capacity to repay it." McGlawn v. Pa. Human Relations Comm'n, 891 A.2d 757, 769 (Comwlth. Ct. 2006), citing Hargraves v. Capital City Mortgage Corp., 140 F.Supp.2d 7, 21 (D.D.C.2000).

21. It is also characteristic of predatory loans that they "do not fit the borrower either because the borrower's needs are not met or because the terms are so onerous there is a strong likelihood the borrower will be unable to repay the loan." Id., citing Assocs. Home Equity Servs., Inc. v. Troup, 343 N.J.Super. 254, 778 A.2d 529 (2001).

22. Another common feature of predatory loans is flipping, or successive refinancings. McGlawn v. Pa. Human Relations Comm'n, 891 A.2d 757, 770 (Pa. Comwlth. Ct. 2006).

23. Defendant's vulnerability combined with severe financial distress caused by prior predatory loans at the time of the loan at issue here, left him without a meaningful choice in response to the broker and lender's efforts to draw him into a new loan.

24. The terms of the loan was grossly one-sided and unfavorable to Mr. L., as the loan terms were tantamount to surrendering his home, since foreclosure was inevitable.

25. This Court generally has the equitable power to deny the foreclosure relief sought by Plaintiff. Greentree Consumer Discount Co. v. Newton, 909 A.2d 811, 816-817 (Pa. Super. 2006); FL.t Real Estate Funding v. Smith, 366 Pa. Super. 116, 530 A.2d 919, 923 (1987).

WHEREFORE, Defendant requests that the Court deny the foreclosure remedy to Plaintiff either by finding that the loan and mortgage contracts are void or, in the alternative, by fashioning another equitable remedy that allows Defendant to remain in his home; and that the Court dismiss the instant foreclosure action with prejudice.

Second Defense: Unclean Hands

26. The preceding paragraphs are realleged and reincorporated herein.

27. Upon information and belief, Plaintiff contracted with America's Wholesale Lender for said lenders to originate loans that would be securitized under Plaintiff's ownership. As such, Plaintiff was involved from the beginning in the origination of a predatory loan and has unclean hands in this matter.

28. The defense of unclean hands is grounds for denying equitable relief to Plaintiff in these circumstances. Shapiro v. Shapiro, 415 Pa. 503, 506 (1964); Doherty v. Adal Corp., 437 Pa. 109, 112 (1970); Brentwater Homes, Inc. v. Weibley, 471 Pa. 17, 18 (1977).

WHEREFORE, Defendant requests that the Court deny the foreclosure remedy to Plaintiff either by finding that the loan and mortgage contracts are void or, in the alternative, by fashioning another equitable remedy that allows Defendant to remain in his home; and that the Court dismiss the instant foreclosure action with prejudice.

Third Defense: Lack of Jurisdiction

29. The preceding paragraphs are realleged and reincorporated herein.

30. The foreclosure notice sent by Plaintiff does not comply with the legal requirements set by Act 91.

31. Compliance with Act 91 is required for a court to have jurisdiction over a mortgage foreclosure.

WHEREFORE, Defendant requests that the Complaint be dismissed.

Fourth Defense: Truth in Lending Rescission

32. The preceding paragraphs are realleged and reincorporated herein.

33. The lender violated the Truth in Lending Act, as set forth above, because the disclosures provided to Defendant were not accurate.

34. The lender's violation of the Truth in Lending Act entitles Defendant to rescind the note and mortgage relied upon by Plaintiff, pursuant to 15 U.S.C. §1635.

35. As the result of the rescission, the note and mortgage upon which Plaintiff bases its claims are void and Defendant's liability for any costs, fees, charges, points or finance charges imposed as a condition of the loan are eliminated pursuant to the Truth in Lending Act and 12 C.F.R. 226.23(d).

WHEREFORE, Defendant requests that this Court find that the mortgage underlying this action is null and void; that Plaintiff's complaint be dismissed with prejudice; and that Defendant be awarded attorneys fees and costs.

Respectfully submitted,

/s/ Elizabeth C. Goodell

ELIZABETH C. GOODELL, ESQUIRE
Counsel for Defendant

APPENDIX E

IN THE CIRCUIT COURT OF KANAWHA COUNTY, WEST VIRGINIA

BARBARA S. HARPER and
CLIFFORD O. HARPER,

Plaintiffs,

v.

CIVIL ACTION NO. 01-C-1341

CONSECO FINANCE SERVICING
CORP., a corporation; MG INVESTMENTS,
INC., a corporation, d/b/a PREMIER
MORTGAGE COMPANY ("PMC"), and
WILLIAM BLEDSOE,

Defendants.

ORDER

Pending before the Court is Count I (Unconscionability) of the Plaintiffs' Complaint. After having considered a full evidentiary showing by the parties in the trial of this matter, as is required by *West Virginia Code* section 46A-2-121(2), the Court FINDS and CONCLUDES that the loan between the Plaintiffs and the Defendants was induced by unconscionable conduct and contains unconscionable terms, in violation of *West Virginia Code* section 46A-2-121(1). Accordingly, the Court FINDS the loan agreement between the Plaintiffs and Defendants, executed on March 4, 1998, is unenforceable as a matter of law.

FINDINGS OF FACT

1. The Defendant, Conseco Finance Servicing Corp. ("Conseco") is a large national corporations in the business of making home equity loans. The Defendant, MG Investments, which is now defunct, was a national corporation headquartered in Indiana.

2. The Harpers are unsophisticated consumers with little understanding of financial matters. Barbara Harper has a tenth grade education and her GED certificate. She works in a grade school cafeteria. Clifford Harper is a former construction worker who currently unloads barges on the

Kanawha River. He has a high school education.

3. The disparity of bargaining positions between the Plaintiffs and Defendants was grossly unequal.

4. The Plaintiffs were not provided with any document that they could keep prior to the loan closing.

5. The loan, which was closed on March 4, 1998, was closed in a hurried manner, creating confusion. The Harpers were simply directed to just "sign here, sign here, sign here," and papers were pushed in front of them without sufficient explanation.

6. The Defendant, William Bledsoe, misrepresented to the Harpers that the rate would go down, when in fact it would not.

7. Bledsoe also misrepresented that the Plaintiffs could lock in the rate in two years.

8. Bledsoe had directed the Plaintiffs not to make their monthly payments on their existing loans because the loans would be paid off with the loan closed on March 4, 1998. As a result, when the Harpers arrived to close the loan, they were behind on their other loan payments. This created an unnecessary pressure for the Harpers to close the loan on March 4, 1998.

9. The loan is based on an inflated appraisal and well exceeds the market value of the Harpers home. The Harpers' home was valued by Plaintiffs' expert, appraiser Jeff Barth, as valued at approximately $62,500 in 1998. An appraiser obtained by the Defendant, William Bledsoe, inflated the value of the Harpers' home to $98,000, primarily by using comparable that were outside the residential setting of the Plaintiffs' residence. Consequently, the loan, which was for $82,000, exceeded the market value of the Plaintiffs home by $19,500.

10. The loan contained excessive fees, charged by the Defendant, MG Investments totaling $5,750. Neither William Beldsoe not MG Investments performed services to justify such a large fee.

11. Included in the loan was $100 for insurance, through a friend of the Defendant, William Bledsoe, but no such insurance was ever provided.

12. The loan contains an exploding ARM, which may adjust up to 17.29%.

CONCLUSIONS OF LAW

13. The Court may declare any contract unconscionable and unenforceable, "if the court as a matter of law finds: (a) The agreement or transaction to have been unconscionable at the time it was made, or to have been induced by unconscionable conduct, or (b) Any . . . part of the agreement to have been unconscionable at the time it was made." W. Va. Code § 46A-2-121(1).

14. When there is a claim of an unconscionable contract, state law requires a full evidentiary presentation. See id. § 46A-2-121(2). Parties must be allowed to present evidence as to the contract's commercial setting, purpose, and effect:

> A determination of unconscionability must focus on the relative positions of the parties, the adequacy of the bargaining position, and the existence of meaningful alternatives available to the plaintiffs. A bargain may be unconscionable if there is "gross inadequacy in bargaining power, together with terms unreasonably favorable to the stronger party . . . ." Gross inadequacy in bargaining power may exist where consumers are totally ignorant of the implications of what they are signing, or where the parties involved in the transaction include a national corporate lender on one side and unsophisticated, uneducated consumers on the other.
>
> ***
>
> Inasmuch as the evidence before the court suggests that the bargaining power of the plaintiffs may have been grossly inadequate and that the plaintiffs may not have had any meaningful alternative to obtaining the loans from defendants, a question of fact exists as to whether the transactions were unconscionable.

Hager, 37 F. Supp. 2d at 786-87 (citations omitted); see also Knapp v. American Gen. Fin., Inc., 111 F. Supp. 2d 758, 764-65 (S.D.W. Va. 2000) (summary judgment inappropriate).

15. There disparity of bargaining positions in this situation was nearly identical to a circumstance the Supreme Court of Appeals of West Virginia concluded were "grossly unequal." See

Arnold, 204 W. Va. 229, 236, 511 S.E.2d 854, 861 (1998).

16. Further, the Court FINDS and CONCLUDES the loan was induced by unconscionable conduct due to the following:

(a) The closing was hurried without sufficient explanation of the documents;

(b) Bledsoe induced the Harpers to sign the agreement by misrepresenting that the rate would go down and they could lock in the rate in two years when in fact the loan could never go down and the Plaintiffs would not be permitted to lock in the rate; and

(c) Blesdsoe misrepresented that the loan would save them money.

17. Additionally, the Court FINDS and CONCLUDES the loan contains several unconscionable terms:

(a) An exploding ARM that may adjust up to 17.29% and could never go down below the initial 11.29%;

(b) The loan was well in excess of the market value because it was based upon an improper valuation of the market value of the Plaintiffs' home, and practically speaking could never be refinanced;

(c) The fees charged by MG Investments are excessive for the services performed;

(d) The Harpers were charged $100 for insurance they never received; and

(e) Finance charges were included in the principal of the loan. Under applicable West Virginia law, the "principal," see W. Va. Code § 46A-1-102(36), in these loans includes the following:

(i) the net amount paid on behalf of the debtor:

Payoff to Beneficial	$	60,449.86
Payoff to Commercial Credit	$	11,472.00
Payoff to Beneficial	$	2,238.63
Insurance to Dillon Ins.	$	100.00
Cash to Borrowers	$	1,015.39
Subtotal	$	*75,275.88*

(ii) plus additional charges permitted by the chapter, see W. Va. Code § 46A-3-109(a)(5), *i.e*, reasonable closing costs, see W. Va. Code § 46A-1-102(7):

[a]	Abstract or title search to Johnson Law Office	$	400.00
	Title examination to Johnson Law Office	$	50.00
[b]	Document preparation to Johnson Law Office	$	50.00
	Settlement or closing fee to Johnson Law Office	$	50.00
	Courier fee – Closing package to Johnson Law Office	$	20.00
[c]	Title Insurance to Security Title	$	257.00
[d]	Recording fees	$	25.00
[e]	Appraisal fee to Carol Elswick	$	325.00
	TOTAL PRINCIPAL		**$76,452.88**

(iii) The Defendant cannot include in the principal the following charges, which are within the definition of "loan finance charge, . . . charges . . . imposed directly or indirectly by the lender as an incident to the extension of credit," W. Va. Code § 46A-1-102(26):

Loan Origination Fee to MG Investments, Inc.	$	5,000.00
Processing fee to MG Investments, Inc.	$	250.00
Document Prep fee to MG Investments, Inc.	$	150.00
Underwriting fee to MG Investments, Inc.	$	350.00

The charges listed immediately above fall within the definition of "loan finance charge." See W. Va. Code § 46A-1-102(26) ("[C]harges . . . imposed directly or indirectly by the lender as an incident to the extension of credit.").

18. Were the Defendants to apply the contract rate in the Note to the "true" principal – *i.e*, minus the finance charges listed above in accordance with West Virginia statutory definition – the monthly payments and total payments would have been less than what has been charged.

19. The Court is not persuaded by the Defendant's argument that the loan saved the Harpers money in that it reduced the Harpers' initial monthly payments, because the duration of the loan is thirty years, longer than the terms of prior loans. Over the life of the loan the Harpers would have had to pay more for the new loan than they would their prior indebtedness.

20. Having concluded that the loan was induced by unconscionable conduct and contained grossly unfair and unconscionable terms, the Court FINDS and CONCLUDES the loan agreement is unenforceable as a matter of law.

WHEREFORE, consistent with the Court's findings of fact and conclusions of law set forth above, the Court ORDERS as follows:

1. The Clerk of the County Commission shall properly record and index this Order as a RELEASE of the Deed of Trust on the Plaintiffs' property as appearing in the Office of the Clerk of the County Commission of Kanawha County at Trust Deed Book 2424, pages 571-578 and any assignment of the Deed of Trust.

2. The Defendant, Conseco and its successors and assigns, shall take action consistent with the Court's Order to reflect termination of the security interest.

3. Conseco, its successors and assigns are hereby ENJOINED from attempting to collect any future payments under the loan.

4. Conseco shall pay the Plaintiff a civil penalty of $3,000 pursuant to *West Virginia Code* sections 46A-5-101(1) & -106 and judgment is so ENTERED, in addition to the prior Judgement Order; and

5. The action has concluded and all issues are resolved, except for determination of reasonable attorney fees and the cost of this litigation.

The Court notes the objection of the Defendant, Conseco, to the findings and conclusions set forth in this Order.

ENTER this 12th day of Nov, 2002.

Date 11-12-02
Certified copies sent to
✓ counsel of record BP/ PMB
__ parties
__ other ____ (please indicate)
By
✓ certified/1st class mail
__ fax
__ hand delivery
__ interdepartmental
Other directives accomplished
Deputy Circuit Clerk

HONORABLE LOUIS H. BLOOM

STATE OF WEST VIRGINIA
COUNTY OF KANAWHA, SS
I, CATHY S. GATSON, CLERK OF CIRCUIT COURT OF SAID COUNTY AND IN SAID STATE, DO HEREBY CERTIFY THAT THE FOREGOING IS A TRUE COPY FROM THE RECORDS OF SAID COURT
GIVEN UNDER MY HAND AND SEAL OF SAID COURT THIS 13th DAY OF November, 2002
Cathy S. Gatson CLERK
CIRCUIT COURT OF KANAWHA COUNTY, WEST VIRGINIA

IN THE CIRCUIT COURT OF KANAWHA COUNTY, WEST VIRGINIA

FILED

CAROLYN OSBURN,

Plaintiff,

2005 MAY 19 PM 2:40

CATHY S. GATSON, CLERK
KANAWHA CO. CIRCUIT COURT

v.

Civil Action No. 02-C-1164

COMMUNITY HOME MORTGAGE, LLC, d/b/a COMMUNITY MORTGAGE GROUP, a limited liability company, and OPTION ONE MORTGAGE CORPORATION,

Defendants.

MAY 25 2005

JUDGMENT ORDER

Pending before the Court is Count VI (Predatory Lending) of the Plaintiff's' Complaint. After having considered a full evidentiary showing by the parties in the trial of this matter, as is required by *West Virginia Code* section 46A-2-121(2), the Court FINDS and CONCLUDES that the loan between the Plaintiffs and the Defendants was induced by unconscionable conduct and contains unconscionable terms, in violation of *West Virginia Code* section 46A-2-121(1). Accordingly, the Court FINDS the loan agreement between the Plaintiff and Defendants, executed on November 12, 1999, is unenforceable as a matter of law.

FINDINGS OF FACT

1. The Defendant, Option One Moprtgage Corp. ("Option One") is a large national corporation from Irvine, California in the business of making home secured loans.

2. The Plaintiff, Carolyn Osburn, is a single mother on a fixed income with two children, ages fifteen and three. She is unsophisticated in financial matters.

3. The disparity of bargaining positions between the Plaintiff and Defendant was grossly unequal.

4. The Plaintiffs was not provided with any document that she could keep prior to the loan

Return: Mountain State Justice
923 Quarrier St
Charleston WV 25301

closing. At some point, the loan broker forged the Plaintiff's name to a loan application.

5. (a) The loan is based on an inflated appraisal of the Plaintiff's home. The Defendant valued the Plaintiff's home at $25,000 in a subsequent Broker Price Opinion.

(b) The appraiser and the broker had an arrangement to inflate appraisals for loans. Evidence was produced at trial that demonstrated the broker encouraged loan officers to use the appraiser Jack Weaver because of his ability to inflate appraisals.

(c) At trial several witnesses testified they had the market value of their home inflated for loans with Defendants, which evidence demonstrated a pattern of using inflated appraisals to justify loans.

6. The loan, which was closed on November 12, 1999 was closed in a hurried manner, creating confusion. The closing agent went over only one document entitled "Closing Checklist,." rather than all the documents Ms. Osburn was directed to sign. The closing agent then flipped through the papers from across a table, exposing only the signature lines, and had Ms. Osburn sign them without significant explanation or opportunity to fully review them. At no time did anyone mention that the loan included a balloon payment. At no time did anyone mention the loan included a prepayment penalty.

7. Several witnesses also testified loan terms were suppressed from them and they would not have signed loan papers with the Defendants had they been aware of the true terms. The evidence demonstrated Option One and its agents had a pattern of suppressing balloon payments and other terms from borrowers.

8. The loan contained excessive fees, charged by the Defendant, Community Home Mortgage and Option One totaling $2,962.90. Neither of the Defendants performed services to justify such large fees.

9. After fifteen years of monthly payments of $368.61 (totaling $65,981.19), a massive balloon payment of $32,530.07, which is very close to the amount initially paid out for Ms. Osburn's benefit, comes due. Ms. Osburn has no ability to make such a payment and would never have signed the loan had she known she would be required to make such a large payment.

CONCLUSIONS OF LAW

10. The Court may declare any contract unconscionable and unenforceable, "if the court as a matter of law finds: (a) The agreement or transaction to have been unconscionable at the time it was made, or to have been induced by unconscionable conduct, or (b) Any . . . part of the agreement to have been unconscionable at the time it was made." W. Va. Code § 46A-2-121(1).

11. When there is a claim of an unconscionable contract, state law requires a full evidentiary presentation. See id. § 46A-2-121(2). Parties must be allowed to present evidence as to the contract's commercial setting, purpose, and effect:

> A determination of unconscionability must focus on the relative positions of the parties, the adequacy of the bargaining position, and the existence of meaningful alternatives available to the plaintiffs. A bargain may be unconscionable if there is "gross inadequacy in bargaining power, together with terms unreasonably favorable to the stronger party . . . ." Gross inadequacy in bargaining power may exist where consumers are totally ignorant of the implications of what they are signing, or where the parties involved in the transaction include a national corporate lender on one side and unsophisticated, uneducated consumers on the other.
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> ***
>
> Inasmuch as the evidence before the court suggests that the bargaining power of the plaintiffs may have been grossly inadequate and that the plaintiffs may not have had any meaningful alternative to obtaining the loans from defendants, a question of fact exists as to whether the transactions were unconscionable.

Hager v. American Gen. Fin., Inc., 37 F. Supp. 2d 778, 786-87 (S.D.W. Va. 1999) (citations omitted); see also Knapp v. American Gen. Fin., Inc., 111 F. Supp. 2d 758, 764-65 (S.D.W. Va. 2000) (summary judgment inappropriate).

12. The disparity of bargaining positions in this situation was nearly identical to a circumstance the Supreme Court of Appeals of West Virginia concluded were "grossly unequal." See Arnold v. United Cos. Lending Corp., 204 W. Va. 229, 236, 511 S.E.2d 854, 861 (1998).

13. Further, the Court CONCLUDES the loan was induced by unconscionable conduct due to the following:

(a) The closing was hurried without sufficient explanation of the documents;

(b) The closing agent misrepresented terms of the loan; and

(c) The terms were concealed from the Plaintiff during the closing; and

(d) The Plaintiff's name was forged to an application;

14. Additionally, the Court CONCLUDES the loan contains several unconscionable terms:

(a) An illegal balloon payment;

(b) The loan was based upon an improper valuation of the market value of the Plaintiffs' home, and practically speaking could never be refinanced; and

(c) The fees charged by Defendants are excessive for the services performed.

15. Finance charges were included in the principal of the loan. Under applicable West Virginia law, the "principal," see W. Va. Code § 46A-1-102(36), in the loan includes the following:

(a) the net amount paid on behalf of the debtor:

First Century Bank	$	21,948.23
City National	$	1,660.00
First Century	$	2,822.00
Cash to borrower	$	7,659.71
Taxes - 1999	$	107.30
Total:	$	34,197.24

(b) plus additional charges permitted by the chapter, see W. Va. Code § 46A-3-109(a)(5), *i.e.*, reasonable closing costs, see W. Va. Code § 46A-1-102(7):

(a)	Title examination	$	400.00
	Title insurance	$	132.00
(b)	Closing fee	$	150.00
(d)	Recording fees	$	20.50
(e)	Appraisal fee	$	375.00
	Subtotal:	$	1,077.50
	Total Principal:	$	35,274.74

Defendant cannot include in the principal the following charges:

Broker fee (CMG)	$	1635.00
Processing fee (CMG)	$	415.00
Tax service contract (Option One)	$	70.00
Funding Fee (Option One)	$	50.00
Underwriting fee (Option One)	$	495.00
Flood certification fee (Option One)	$	12.00
Interest (14 days)	$	165.90
Settlement fee (Bonnie Sue Fleming)	$	100.00
Courier fee (Bonnie Sue Fleming)	$	20.00
Total	$	2,962.90

The charges listed immediately above fall within the definition of "loan finance charge." See W. Va. Code § 46A-1-102(26) ("[C]harges . . . imposed directly or indirectly by the lender as an incident to the extension of credit.").

16. The contract rate of interest is 11.150%. Application of the contract rate of interest to the principal yields a lower monthly and total payment stated in the Note and disclosures.

17. The Note fails to provide the appropriate disclosures required for balloon notes by West Virginia law.

18. Also included in the loan is a prepayment penalty, which penalized Ms. Osburn six months interest if she were to have prepaid the loan in the first five years.

19. Were the Defendants to apply the contract rate in the Note to the "true" principal – *i.e.*, minus the finance charges listed above in accordance with West Virginia statutory definition – the monthly payments and total payments would have been less than what has been charged.

20. Having concluded that the loan was induced by unconscionable conduct and contained grossly unfair and unconscionable terms, the Court **CONCLUDES** the loan agreement is unenforceable as a matter of law.

WHEREFORE, consistent with the Court's findings of fact and conclusions of law set forth above, the Court **ORDERS** as follows:

1. The Clerk of the County Commission of Mercer County shall properly record and index this Order as a RELEASE of the Deed of Trust on the Plaintiffs' property as appearing in the Office of the Clerk of the County Commission of Mercer County at Trust Deed Book 850 pages 712-719 and any assignment of the Deed of Trust.

2. The Defendant, OptionOne and its successors and assigns, shall take action consistent with the Court's Order to reflect termination of the security interest.

3. Option One, its successors and assigns are hereby **ENJOINED** from attempting to collect any future payments under the loan.

4. Option One shall pay the Plaintiff a civil penalty of $3,790 pursuant to *West Virginia Code* sections 46A-5-101(1) & -106 and judgment is so **ENTERED**, in addition to the prior Judgement Order.

The Court notes the objection of the Defendant, Option One, to the findings and conclusions set forth in this Order.

ENTER this 19TH day of May, 2005.

HONORABLE CHARLES E. KING

Bren J. Pomponio (State Bar ID No. 7774)
Mountain State Justice, Inc.
922 Quarrier St., Ste. 525
Charleston, WV 25301
COUNSEL FOR PLAINTIFF

STATE OF WEST VIRGINIA
COUNTY OF KANAWHA, SS
I, CATHY S. GATSON, CLERK OF CIRCUIT COURT OF SAID COUNTY AND IN SAID STATE, DO HEREBY CERTIFY THAT THE FOREGOING IS A TRUE COPY FROM THE RECORDS OF SAID COURT.
GIVEN UNDER MY HAND AND SEAL OF SAID COURT THIS 20TH
DAY OF May 2005
Cathy S. Gatson CLERK
CIRCUIT COURT OF KANAWHA COUNTY, WEST VIRGINIA

M. David Griffith (State Bar ID No. 7720)
Robinson & McElwee
P.O. Box 1791
Charleston, WV 25326-1791
COUNSEL FOR DEFENDANT
OPTION ONE MORTGAGE CORPORATION

WEST VIRGINIA
IN MERCER COUNTY COMMISSION CLERK'S OFFICE

This MAY 2 4 2005 1:03 PM

the foregoing writing was presented in said office and duly admitted to record therein

Teste: Clerk