51,258



IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF ARIZONA

SANDRA CRAWFORD, et al.,

Plaintiffs,

vs.

THE AMERICAN INSTITUTE OF PROFESSIONAL CAREERS, INC., et al.,

Defendants.

VICKIE LEE,

Plaintiff

vs.

RESOLUTION TRUST CORPORATION, in its capacity as Receiver for SECURITY SAVINGS AND LOAN ASSOCIATION, et al.,

Defendants.

SANDRA CRAWFORD,

Plaintiff,

vs.

RESOLUTION TRUST CORPORATION,

No. CIV 94-2402 PHX CAM
No. CIV 95-0366 PHX CAM
No. CIV 95-0376 PHX CAM
(consolidated)

ORDER

FEB 09 1996

in its capacity as Receiver for )
MERABANK, et. al., )
)
Defendants. )

Having considered defendant Student Loan Marketing Association's [Sallie Mae's] motion to dismiss, the court concludes as follows:

Background

The lead case in this group of consolidated cases [94-2402] was removed from state court on December 1, 1994 by the United States Department of Education after the plaintiffs filed a verified second amended complaint adding the department as a defendant. The court consolidated two similar cases, CIV 95-336 and CIV 95-376. Plaintiffs subsequently filed a third amended complaint in 94-2404 on behalf of plaintiffs, all persons who enrolled in American Institute's court reporting program from May of 1985 through December of 1992.

Plaintiffs are former students of American Institute's court reporter program. Defendants are American Institute, numerous student loan lenders and guarantors, referred to as Financial Defendants, and two school accreditation associations.

Plaintiffs allege in their third amended complaint that they relied on misrepresentations by American Institute to enroll in the program and take out student loans to fund their education. Plaintiffs further allege that American Institute acted as the agent for student loan lenders and guarantors, referred to in the complaint as the "financial" defendants. Plaintiffs further allege that the agencies that guaranteed or purchased their loans on the secondary

market are subject to defenses to enforcement of the student loans because those agencies are not holders in due course. Therefore, plaintiffs allege that the student loan defendants are liable for American Institute's misrepresentations.

Plaintiffs' first claim requests declaratory judgment that they do not owe the student loans to American Institute and the Financial Defendants; requests refunds for all payments; a permanent injunction from further collection or submission of adverse credit reports; an order requiring American Institute to cancel and withdraw all adverse credit reports and an order prohibiting American Institute and the financial defendants from transferring or assigning the loans during the pendency of this litigation. Count two of the third amended complaint alleges Arizona consumer fraud under A.R.S. §41-1522 against all defendants. Count three alleges state racketeering under A.R.S. §§13-2301(D)(4) and 13-2310 against all defendants. Count four alleges innocent misrepresentation against all defendants. Count five alleges negligent misrepresentation against all defendants. The sixth count alleges Arizona common law fraud against all defendants. Count seven of the third amended complaint alleges conspiracy to defraud against all defendants. Count eight alleges breach of contract against American Institute. In count nine, plaintiffs allege breach of third party beneficiary contract against the school accreditors ACICS and NCRA. Count ten alleges fraud in the inducement against all defendants. Count eleven alleges negligence against all defendants. Count twelve alleges breach of fiduciary duty against American Institute. Finally, count thirteen

of the third amended complaint alleges constructive fraud against American Institute. Although the complaint alleges class claims, this court has not yet certified a class in this case and no motion is pending.

The complaint in CIV 95-376 was filed by plaintiff Sandra Crawford on February 27, 1995. The complaint names as defendants the RTC[1] as receiver of Merabank, the original lender; Bank of America as trustee for Arizona Student Loan Finance Corporation [ASLFC]; Student Loan Marketing Association [Sallie Mae], which has consolidated plaintiff's student loans; Norwest Bank of Minnesota as trustee for the Higher Education Assistance Foundation Liquidating Trust [HEAF]; Great Lakes Higher Education Corporation as guarantor of Sallie Mae's consolidation of plaintiff's loan.

Counts one through five of the complaint in CIV 95-376 allege fraud, consumer fraud, negligent misrepresentation, state racketeering and negligence against the RTC, as receiver for MeraBank. Count six requests declaratory and injunctive relief against Norwest, as trustee for HEAF; Bank of America, as trustee for ASLFC; Sallie Mae and Great Lakes. Because the RTC has been dismissed, only the sixth count remains in this case.

Relevant to this motion to dismiss, Sallie Mae was created by Congress as a federally-chartered national secondary market for student loans. Sallie Mae was established with the specific purpose of providing liquidity for student loan investments. 20 U.S.C.A. § 1087-2. Sallie Mae acquires insured student loans under the Federal

[1] The RTC has already been dismissed from this action.

Family Education Loan Program [FFELP] from lenders and other holders, thus providing new funds with which more student loans can be made. Sallie Mae is also an eligible lender for consolidation loans made under the FFELP. 20 U.S.C.A. § 1078-3(a)(1).

Consolidation loans are authorized under FFELP. 20 U.S.C.A. §§ 1078-3 and 1087-2(o). The FFELP consolidation loan program provides that new loans may be made to eligible borrowers who received other FFELP loans in the past. 20 U.S.C.A. §1078-3(a)(1). The proceeds of a consolidation loan are paid by the lender to the holder of existing student loans to discharge the liability on those loans. 20 U.S.C.A. § 1078-3(b)(1)(D). Pursuant to statute, a consolidation loan is a "new loan" for purposes of §1074(a), 20 U.S.C.A. § 1078-3(e)(supp. 1995), which provides limitations on the amounts of loans covered by federal insurance for certain periods of time. 20 U.S.C.A. §1074(a) (supp. 1995).

Sallie Mae has moved to dismiss the complaints against it pursuant to Rules 12(b)(6) and 12(b)(1) alleging that plaintiff Sandra Crawford has failed to state a claim upon which relief can be granted because consolidation of the loans with Sallie Mae extinguished defenses to payment of the original loans and plaintiff expressly waived any defenses to enforcement of the original loans when she consolidated those loans with Sallie Mae.

Discussion

**I. Is Ms. Crawford's consolidation loan a new loan that discharged her original loans and extinguished any of her potential defenses to them?**

Sallie Mae argues that the consolidation loan obtained by Ms. Crawford, from it is a new loan that discharged her original student loans and extinguished any potential defenses to payment. Ms. Crawford responds that she consolidated her loans into a SMART LOAN with Sallie Mae, which is now the holder of the loan, and that this consolidation is not a new loan which extinguished enforcement defenses.

Sallie Mae cites numerous bankruptcy cases in which the courts have found the consolidation loans to be "new" loans for the limited purpose of defeating their dischargeability in bankruptcy. See Hiatt v. Indiana State Student Assistance Com'm, 36 F.3d 21 (9th Cir. 1994); In re Hesselgrave, 177 B.R. 681 (Bkrtcy. D.Or. 1995); In re Mendndez, 151 B.R. 972 (Bkrtcy. M.D. Fla. 1993); In re Saburah, 136 B.R. 246 (Bkrtcy C.D.Cal. 1992); United States v. McGrath, 143 B.R. 820(D.C.D. Md. 1992); In re Martin, 137 B.R. 770 (Bkrtcy W.D.Mo. 1992); In re McKinney, 1992 WL 265992 (N.D. Ohio 1992), rev'ing, 120 B.R. 416 (Bkrtcy. N.D.Ohio 1990). These courts have interpreted the loans as new loans to advance the strong public policy favoring non-dischargeability of student loans, In Re Saburah, 136 B.R. at 252, and to limit abuse of the GSL program by individuals who first avoid payment by consolidating and later file bankruptcy to avoid paying the balance of the loans, In Re Martin, 137 B.R. at 775. These courts have generally held that the statutory period to petition for

bankruptcy runs from the first repayment date under the consolidation loan. The defendant argues that because these courts have considered the loans to be "new" loans, the consolidation discharges all defenses under the prior loans. However, none of these cases hold that the loans are new loans so that all defenses to the loans that have been consolidated are waived as a matter of law upon consolidation. Moreover, the policy considerations that moved the bankruptcy courts to make the "new" loan determination do not apply to this case. Thus, dismissal is not appropriate for the defendant on this basis.

**II. Did Ms. Crawford expressly waive any defenses to the original loans by taking out her consolidation loan?**

Sallie Mae argues that when Ms. Crawford obtained the new consolidation loan, she expressly and knowingly waived any defenses to enforcement of the original student loans. Thus, the defendant argues, Ms. Crawford has no defenses to enforceability of the new loan made by it and her claims against Sallie Mae in the lead and individual case must be dismissed. Ms. Crawford argues that she did not waive her defenses, nor did she intend to waive those defenses.

Ms. Crawford argues that because the court must consider the language of the application/promissory note to resolve this issue a motion to dismiss is inappropriate. Normally, the court would agree. However, plaintiff has attached the Application/ Promissory Note as Exhibit D to the Third Amended Complaint. She has also attached her affidavit stating that she did not intend to waive her defenses when she signed the agreement. That affidavit is Exhibit C to the Third Amended Complaint. Because plaintiff has made this evidence part of

the pleadings, the court can consider the language of the note and affidavit on this motion to dismiss without converting the motion to a summary judgment motion.

There is no dispute that the waiver provision is in the Application/Promissory Note, which Ms. Crawford signed, and it provides, "[i]t is my understanding that Sallie Mae will advance funds on my behalf to creditors. . . in order to pay off those loans. . .I undertake a new obligation, which is not subject to any defenses I might have with respect to the loans selected for consolidation." The provision is part of the fine print of a pre-printed form contract.

Ms. Crawford argues that the purported waiver of rights is inadequate as it is within the fine print of the document and does not contain the word "waiver." At best, she argues, it is ambiguous and should be construed against the drafter, defendant Sallie Mae. Moreover, she argues that economic circumstances forced consolidation so the purported waiver will not be given effect.

Without an express reference to "waiver," such provisions are at best ambiguous. A waiver is given effect only when "it represents an intentional relinquishment of a known right." The parties must have equal bargaining power so that the choice was made freely and fairly and not forced by circumstances. A waiver will not be enforced it it is a product of coercion or inadvertence. Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp., 143 Ariz. 368, 385, 694 P.2d 198, 215 1984)(tort remedies); Manzanita Park v. Insurance Co. of North America, 857 F.2d 549, 555 (9th Cir. 1988)..

In this case, Ms. Crawford's affidavit filed with her amended complaint states that she was not aware of the waiver and did not intend to waive defenses. The provision was in the fine print of a pre-printed form contract. Ambiguous provisions in pre-printed forms are construed against the drafter, in this case Sallie Mae. Taylor v. State Farm Auto Ins., 175 Ariz. 1139, 854 P.2d 1134 (1993); Darner Motor Sales v. Universal Underwriters Ins., 140 Ariz. 383, 682 P.2d 388, 396 (1984); Anderson v. Preferred stock Food Markets, Inc., 175 Ariz. 208, 854 P.2d 1194 (App. 1993). Therefore, the alleged waiver should not be enforced against Ms. Crawford as a matter of Arizona law.

Moreover, even if the waiver had been clear, unambiguous forms will not be enforced by Arizona courts if the party to be bound did not receive full and adequate notice of the term in question. Gordinier v. Aetna Casualty & Sur. Co., 154 Ariz. 266, 272, 742 P.2d 277, 283 (1987). Ms. Crawford clearly did not receive full and adequate notice. Therefore, even if the waiver had been less ambiguous, the court still would not have enforced the waiver against Ms. Crawford.

In addition, Ms. Crawford consolidated for economic reasons. Therefore, the court would not enforce the waiver against her. See Salt River Project Agric. Improvement & Power Dist. v. Westinghouse Elec. Corp., 143 Ariz. 368, 385, 694 P.2d 198, 215 1984)(tort remedies); Manzanita Park v. Insurance Co. of North America, 857 F.2d 549, 555 (9th Cir. 1988).

The defendant also argues that Ms. Crawford waived her defenses when she requested a deferred payment on her loan. On May 6, 1992, Ms. Crawford requested forbearance on her loan because of financial hardship. In return for a three-month forbearance on her loan payments, she attested that, "I intend to repay my education loan account" and "I will resume monthly payment on 06/18/92." At that time, she did not assert any defenses or question her obligation in requesting an additional grace period. Therefore, the defendant argues that she again waived her defenses. Ms. Crawford responds that the language does not contain the key word "waiver" and that she never intended to release her loan repayment defenses.[2] In this case, the alleged waiver is even less clear than the waiver in the pre-printed form note and is insufficient as a matter of Arizona law.

**III. Was the consolidation of loans a novation that waived plaintiff's defenses to payment?**

The defendant argues that the consolidation is a novation that extinguished the defenses plaintiff had to payment of her original loans. Ms. Crawford argues that it was not a novation.

Novation is defined as the "substitution by mutual agreement of one debtor or of one creditor for another, whereby the old debt is extinguished or the substitution of a new debt or obligation for the existing one which is thereby extinguished." Western Coach Corp. v. Roscoe, 133 Ariz. 147, 152, 650 P.2d 449, 454 (1982). However, to constitute a valid novation, there must be an "extinguishment of a previously valid obligation and an agreement of all parties to a new,

[2] Ms. Crawford's affidavit is attached to the Third Amended Complaint as exhibit C.

valid contract." Id. Thus, novation requires mutual agreement. In this case, there was no mutual agreement by the parties that Ms. Crawford was waiving her defenses against payment of the loans. Thus, novation has not occurred and dismissal is not appropriate for Sallie Mae on this issue.

IT IS THEREFORE ORDERED THAT Defendant Student Loan Marketing Association's [Sallie Mae's] Motion to Dismiss [doc 16 in CIV 95-376] is denied.

DATED this 7th day of February 1995.

C.A. Muecke
U.S. District Judge