COMMONWEALTH OF KENTUCKY
FAYETTE CIRCUIT COURT
DIVISION 8
CASE NO. 09-CI-6405

BAC HOME LOANS SERVICING L.P. PLAINTIFF

VS. **DEFENDANTS' RESPONSE IN OPPOSITION TO PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT**

JOHNSON, *et al*. DEFENDANTS

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Come Defendants, Rickey Johnson and Jessica Short, by counsel, and hereby submit their Response in Opposition to Plaintiff's Motion for Summary Judgment. Plaintiff has not demonstrated that it is entitled to summary judgment on its claim and fails to offer any reason that it should be granted summary judgment on any of Defendants' counterclaims and thus, summary judgment should be denied.[1]

INTRODUCTION and MOTION STANDARD

This is a foreclosure case that has been converted to a consumer protection action by virtue of Defendants' counterclaims. Defendants have asserted counterclaims under the Truth in Lending Act, arguably the nation's most powerful Consumer Protection Act, as well as claims under the Kentucky Consumer Protection Act and other Kentucky statutes. These counterclaims could void the mortgage, dramatically reduce the sums the Defendants owe, and because of discretion granted trial courts under Regulation Z, could enable the trial court to allow Mr. Johnson and Ms. Short to pay any remaining sums owed in reasonable monthly installments.[2]

1 More to the point, Plaintiff does not make <u>any</u> mention of Defendants' counterclaims.

2 TILA at 15 U.S.C. § 1635 provides for extended rescission rights of home equity loans such as Defendants' loan in the event of violation of certain material provisions of TILA. A TILA rescission voids the mortgage, and

Thus, the nature of the counterclaims creates genuine issues of material fact that precludes summary judgment in favor of Plaintiff on its claim.

Summary judgment is proper only if the pleadings, materials from discovery, and affidavits submitted "show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." CR 56.03. Plaintiff has the burden of showing that "it would be impossible for [Defendants] to produce evidence at the trial warranting a judgment in his favor and against [Plaintiff]." *Paintsville Hospital Co. v. Rose*, 683 S.W.2d 255, 256 (Ky. 1985). In considering a motion for summary judgment, the evidence must be construed in the light most favorable to the non-moving party and all doubts resolved in the non-moving party's favor. *Dossett v. New York Mining and Manufacturing Co*., 451 S.W.2d 843, 845 (Ky. 1970).

Plaintiff has not even met the threshold burden on its own claims, much less Defendants' counterclaims, and thus, its motion must be denied. It is not the duty of Defendant to fill in the gaps of Plaintiff's Motion for Summary Judgment where it fails to address the claims and defenses and present its case and legal argument therefor for why it is entitled to judgment as a matter of law. *See Payne v. Chenault*, 343 S.W.2d 129, 132-33 (Ky. 1961) (emphatically stating that CR 56. is not to be used "for the purpose of testing the sufficiency of a party's evidence. Where there is a genuine issue on a material fact, and it is properly joined by the pleadings, a trial is the only battleground. Until the time of trial every litigant must have the opportunity to

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eliminates all settlement charges and finance charges from the transaction. In addition, consumers can recover a $4,000.00 statutory damage award for any failure to honor a valid TILA rescission and $4,000.00 for the original material violation that resulted in the extended rescission rights. A statutory TILA rescission basically reverses the rescission process under common law. Under TILA the mortgage is void, the amount owed is substantially reduced, and only after such reduction is the consumer required to make her tender. "Some courts have invoked their equitable discretion to grant the consumer the opportunity to pay the Consumer's Tender Obligation over an extended period of time, in effect, restructuring the mortgage to take into account the elimination of the finance charges as a result of the rescission of the transaction." *In re Stuart* 367 B.R. 541, 552 (Bkrtcy.E.D.Pa. 2007).

search for and secure whatever evidence may be necessary to perfect his case, and unless it is manifestly impossible for him to produce it he cannot be forced to a premature showdown in that respect by a motion for summary judgment."). Nevertheless, the following will demonstrate the material factual disputes concerning three key issues in the case: whether (1) Mr. Johnson and Ms. Short each received a separate copy of the material Truth in Lending Disclosures; (2) the the finance charge was under-disclosed by more than $35.00, which is the threshold for extended rescission rights under TILA for consumers defending foreclosures;[3] and (3) Plaintiff is entitled to demand payment on a Note that was made payable to a different entity (American Lending Group, Inc.).

ARGUMENT

On or around June 10, 2008, Rickey Johnson and Jessica Short entered into a refinancing transaction with American Lending Group, Inc. in which they borrowed $142,709.00 with an annual percentage rate of 6.862 % on a 30-year, fixed rate note ("the 6/10/08 loan"). *See* Truth in Lending Disclosure Statement attached hereto as Exhibit A. On December 17, 2009, Defendants rightfully rescinded the loan at issue in Plaintiff's Complaint. See Exhibit B. They rescinded based on violations of the Truth in Lending Act ("TILA"), 15 U.S.C. § 1601, *et seq*.:

1. The failure to provide a copy of the material TILA disclosures each to Jessica Short and Rickey Johnson as required by TILA 15 U.S.C. § 1632 and 12 C.F.R. § 226.17(d). Defendants only received one copy between them.

2. The failure to accurately disclose the finance charge, which was understated by more than $35.00. The inaccurate calculation of the finance charge resulted in an inaccurate amount financed and APR in violation of 15 U.S.C. § 1602(u) and 12 C.F.R. § 226.18.

3 Defendants contend that the finance charge was understated by more than $250.00.

The TILA violations give rise to the right to cancel the loan pursuant to 15 U.S.C. § 1635 and 12 C.F.R. § 226.23. The Defendants also have a claim in recoupment for statutory damages for the TILA violations. 15 U.S.C. § 1640. In addition to the TILA claims arising from the violations of TILA at the loan origination, Defendants also have state law claims arising from the same actions and conduct under Kentucky's Consumer Protection Act, KRS 367.220, for unfair, false, misleading, and deceptive trade practices. Defendants' claims under these state law and tort theories are supported by the same facts as those which give rise to the TILA claims. Plaintiff as assignee is liable for all claims and defenses to the same extent as American Lending Group, the original creditor. 15 U.S.C. § 1641(a). It is liable for the rescission to the same extent of American Lending Group. 15 U.S.C. § 1641(c).

If a creditor fails to furnish the material TILA disclosures or the notice of the consumer's right to rescind in the clear, conspicuous, accurate manner prescribed by the Act, the right to rescind remains unexpired until the expiration of three years, or the sale or transfer of the consumer's ownership interest in the property, whichever occurs first. *See* Reg. Z, 12 C.F.R. § 226.23(a)(3). *See also*, *Beach v. Ocwen Federal Bank*, 523 U.S. 410, 411 (1998). "When a consumer rescinds a transaction, the security interest giving rise to the right of rescission becomes void and the consumer shall not be liable for any amount, including any finance charge." Reg. Z. § 226.23 (d)(1). A valid rescission raises a genuine issue of material fact about an amount owed to Plaintiff, if Plaintiff is owed anything at all (see Part III below). This precludes summary judgment on Plaintiff's claim against Defendants.

I. Defendants had extended rescission rights because they did not receive the requisite number of TILA Disclosure Statements.

The amount financed, finance charge, and APR are "material" disclosures, 15 U.S.C 1602(a), mandated to be disclosed to a consumer in writing and in a form that she can keep, 12

C.F.R. 226.17(a). The material disclosures for the 6/10/08 loan were contained on the TILA Disclosure Statement, Exhibit A. Mr. Johnson and Ms. Short were each entitled to a separate copy of the TILA Disclosure Statement. 12 C.F.R. § 226.17(d). The following Federal Reserve Board staff commentary renders this beyond dispute: "In a transaction involving joint owners, both of whom are entitled to rescind, both must receive the notice of the right to rescind and disclosures. For example, if both spouses are entitled to rescind a transaction, each must receive two copies of the rescission notice (one copy to each if the notice is provided in electronic form in accordance with the consumer consent and other applicable provisions of the E-Sign Act) and one copy of the disclosures." Reg Z. Official Commentary § 226.23(b)(1). One copy between Defendants simply does not comply with TILA. They each have their own right to rescind the loan and a rescission by one consumer with the right is effective under TILA, 12 C.F.R. § 226.23(a)(4); thus, it only makes sense that they should each have their own requisite number of copies of the material and mandatory disclosures to be able to make that determination.

The undisputed evidence is that Defendants only received one copy between them. See Exhibit C (affidavit prepared the day Defendants arrived at the undersigned's office with their loan closing file) and Exhibit D (affidavit regarding the number of disclosures received from Plaintiff in discovery). Accordingly, there remains a factual dispute concerning whether Mr. Johnson and Ms. Short received the requisite number of material TILA disclosure statements – if they did not receive the requisite two disclosure statements, they were exercising and unexpired right to rescind when they canceled the transaction

II. Defendants had extended rescission rights because the finance charge was understated by more than $35.00

Congress and the Federal Reserve Board intended TILA to provide enhanced protection

to homeowner's facing foreclosure. Outside of foreclosure, "the amount disclosed as the finance charge must understate the finance charge by more than an amount equal to one-half of one percent of the total amount of credit extended" to result in extended rescission rights. 15 U.S.C.A. § 1605. By contrast, 15 USC § 1635(i), **Rescission Rights in Foreclosure**, states the finance charge shall be considered accurate only "if the amount disclosed as the finance charge does not vary from the actual finance charge by more than $35 or is greater than the amount required to be disclosed under this subchapter."

Reg. Z defines "finance charge" as "the cost of consumer credit as a dollar amount," including "any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit." Reg. Z § 226.4(a) [emphasis supplied]. The finance charge as disclosed on the TILA Disclosure Statement is $3,723.55 (Principal amount of $142,709 *minus* Amount financed of $138,985.45). The HUD-1 Settlement Statement, however, lists several fees which should be included with the finance charge; the true finance charge is at least $55.00 more than what was disclosed, rendering the material disclosures inaccurate. Exhibit E, Settlement Statement. There can be no factual dispute that Defendants were overcharged for the recording fee (whether one relies on the Settlement Statement or the Itemization). *See* 12 C.F.R. § 226.4(e). The true charge was only $35 – thus on the recording fee overcharge alone, Defendants have met the $35 TILA rescission threshold. *Compare* Settlement Statement (Defendants' Exhibit E hereto) *with* Certification of the Fayette County Clerk attached to the Mortgage (Exhibit B to Plaintiff's Complaint).[4] Plaintiff has not offered any proof whatsoever to refute the under-disclosure of the finance

4 There is other evidence of the improper allocation of certain settlement charges to the amount financed; Defendants have met their burden to prevent summary judgment by showing that they meet (and exceed) TILA's $35.00 threshold.

charge; there clearly is a dispute in the facts, immunizing Defendants' claim from summary judgment.

III. There are sufficient factual issues to preclude summary judgment on Defendants' state law claims and Plaintiff's claim.

The evidence which supports their TILA claims, also support Defendants' consumer protection act claims. Actions with respect to (1) failing to provide accurate and meaningful disclosures under TILA, and (2) failing to honor the rescission request constitute unfair and misleading business practices of a sort prohibited under Kentucky law. There is sufficient evidence to show a factual dispute about these claims, making summary judgment impossible. Summary judgment, thus, must be denied on these counterclaims.

Finally, Plaintiff claims to hold the note with all proper endorsements. The Note Plaintiff attached its Complaint is unendorsed and made payable only to American Lending Group. *See* Complaint, Exhibit A. Plaintiff can make no demand on Defendants for any money and this was challenged by Defendants in the Answer and Counterclaim. The Note is similar to a check. The negotiation and enforceability of both notes and checks are governed by Article Three of the Uniform Commercial Code. To enforce a negotiable instrument, a person must be a holder of the note. KRS 355.3-301. To meet the definition of a "holder," the person must possess the note, and the note must be issued or indorsed to him or to his order or to bearer or in blank. KRS 355.1-201(2)(u).[5]

The requirement that the Plaintiff produce the Note presents an issue of more than mere "academic" interest. In today's environment, in which mortgage notes have been freely traded,

5 The foregoing is illustrated by official comments to the UCC § 355.3-203 that read as follows: "X signs a document conveying all of X's right, title, and interest in the instrument to Y. Although the document may be effective to give Y a claim to ownership of the instrument, *Y* is not a person entitled to enforce the instrument until Y obtains possession of the instrument. No transfer of the instrument occurs under Section 3-203(a) until it is delivered to Y." (emphasis added).

and serve as collateral for various investment vehicles this "owner of the claim issue" is more important than ever to a defendant in foreclosure to: (1) avoid having to re-pay an obligation previously thought to have been satisfied, (2) avoid the potentially expensive and stressful possibility of having to defend the same action twice, (3) avoid having to re-negotiate a settlement, (4) determine whether the holder or its servicer may be an entity that has received federal funds or may be otherwise obligated to take reasonable steps to modify the loan to protect tax payers, homeowners and property values, and ensure investors suffer minimal losses, (5) determine whether the obigation may have been paid by an insuror (for example AIG) or via credit default swap that could result in a subrogation claim against the debtor, and (6) benefit the debtor in the event another entity is the true holder and that entity is more amenable to loan modification or loss mitigation.

In the present case, Plaintiff purports to possesses the original Note, but has failed to answer very basic discovery questions about the Note. *See* Defendants' Motion to Compel.[6] It is Plaintiff's burden to present its proof and meet the standard for obtaining a summary judgment under CR 56.03. Defendants served discovery that when answered may shed light on all the foregoing issues. Among other things the discovery seeks production of the original note and requests identification of the color of the ink of each signature and indorsement. Plaintiff has failed to provide responses that would support its claim that it does indeed possess the original note with all proper indorsements.

WHEREFORE, Defendants requests that Plaintiff's Motion for Summary Judgment be

6 After initiating this action, Plaintiff now claims to hold the note with an endorsement from American Lending Group. As Plaintiff is supposed to be making the original Note available for inspection before the hearing on its summary judgment, Defendants are not in a position to make more specific challenges to what Plaintiff has without completing discovery (including under what circumstances it obtained an endorsement only after filing suit against Defendants). It remains to be seen, therefore, what challenges, if any, Defendants may make to Plaintiff's standing.

denied in its entirety.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I, the undersigned, do hereby certify that a true and accurate copy of the foregoing was this 14th day of July 2010 served by hand-delivery to:

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