

## **OUTLINE OF DEFENSES**

### **I. TRUTH IN LENDING ACT**

The Truth in Lending Act (“TILA”) begins at 15 U.S.C. § 1601. The law is implemented through Regulation Z which is found at 12 CFR 226.1 et seq. The law applies to certain credit transactions by creditors that involve a consumer transaction which is one which is primarily for personal, household or family purposes. The TILA mandates disclosures relating to both open and closed end loans that are primarily for consumer purposes. 15 U.S.C. § 1604. This discussion is focused on transactions relating to loans secured by a consumer’s principal dwelling.

TILA permits the recovery of actual and statutory damages as well as attorney’s fees. 15 U.S.C. § 1640. In connection with non-purchase money mortgages, the law also provides a right to rescind the loan until midnight of the third business day. 15 U.S.C. § 1635. The right to rescind is extended to as long as three years or until the property is transferred if the disclosures have not been properly made. 15 U.S.C. § 1635 (f).

Additionally, the Home Ownership and Equity Protection Act (“HOEPA”), 15 U.S.C. § 1639, applies substantive limitations on certain loans that are high cost loans. 15 U.S.C. § 1602 (aa). HOEPA provides for enhanced damages. 15 U.S.C. § 1640 (a)(4). HOEPA also extends liability for assignees beyond rescission. 15 U.S.C. § 1641 (d).

### **II. Real Estate Settlement Procedures Act**

The Real Estate Settlement Procedures Act (“RESPA”) begins at 12 U.S.C. § 1601. The law is implemented through Regulation X which is found at 24 CFR 3500 et seq. The law outlines the procedures for federally related loans. 12 U.S.C. § 2602 (1). It requires the use of a settlement statement. The most common forms used are the HUD 1

and the HUD 1 A form. The law does not provide for private causes of action for many of its provisions. The provision most often raised, and for which there is a right to a private cause of action, is the prohibition against kickbacks or unearned fees. 12 U.S.C. § 2607. For mortgage default issues, RESPA also provides the consumer the right to send a “qualified written request”. 12 U.S.C. § 2605 (e). A pattern of failing to timely acknowledge or provide information in response to a QWR can be the basis for a private action.

### **III. UNCLEAN HANDS**

In *Wells Fargo v. Neal*, 398 Md. 705, 922 A.2d 538 (2007) the court held that the failure of a servicer/lender to comply with the loss mitigation efforts required for an FHA loan can be raised as a defense to a foreclosure proceeding. The court couched the defense in terms of an unclean hands defense to the equitable foreclosure proceeding.

The violation of state or federal laws in connection with the loan origination or servicing may provide grounds to establish an unclean hands defense to any foreclosure proceeding. This extends to violations of laws which may not provide private causes of action. In *Neal*, the court found that the failure to comply with the FHA rules provided a defense but there was no private right of action if the rules were violated.

### **IV. STATE LAWS**

#### **a. Preemption**

As a preliminary matter, you must be familiar with the role of preemption in lending. Many state laws are either preempted by the operation of a federal law or by the actor’s status as a national bank, savings and loan or national credit union.

#### **b. Credit Grantor Credit Provisions**

## 1. CLOSED END

If not preempted, Maryland law provides two possibilities for the regulation of loan transactions secured by mortgages. For closed end loan, the creditor may make a written election to apply the provisions of the Credit Grantors Closed End Credit Provisions, § 12-1001, et seq of the Maryland Commercial Law Article. [for some reason unknown to me, the acronym commonly applied to this law is “CLEC”]. If a written election is made, then the remaining provisions of Title 12 of the Commercial Law Article have no application to the transaction. § 12-1013.1. This law tends to be very creditor friendly, however, it does provide substantial rights to the consumer borrower. One of the more significant is that the definition of credit grantor includes all assignees. Therefore, there can be no legitimate claims of holder in due course by assignees.

Additionally, the limitation on fees for consumer borrower prohibits fees for certain title and related fees that are retained by the credit grantor. § 12-1005 (d).

## 2. OPEN END LOANS

For an open end transaction, the creditor may elect to apply the provisions of the Credit Grantor Revolving Credit Provisions, § 12-901 et seq. (“CGRCP”) Similar to CLEC, if a written election is made, then the remaining provisions of Title 12 of the Commercial Law Article have no application to the transaction. § 12-913.1.

Additionally, the limitation on fees for consumer borrower prohibits fees for certain title and related fees that are retained by the credit grantor. § 12-905 (b).

### c. FIRST LIEN LOANS

If CLEC or CGRCP does not apply, then the type of the loan will determine what other provision of Article 12 will apply. For most closed end first lien loans the

various items required to be filed with the order to docket. § 7-105.1 (d). This includes the debt instrument and an affidavit of ownership. § 7-105.1 (d)(2)(iii). The impact of these issues is discussed below under standing. **The borrower has the right reinstate up to 1 business day before the sale. § 7-105.1 (h).**

## V. STANDING

### a. HOLDER MUST FORECLOSE

It is elementary that the person who holds the loan should be the only person who can pursue foreclosure. The problem is that the world of financing has changed. The process of “securitization” has made the issue of ownership difficult if not impossible to answer. The issue became so widespread that the Judges sitting on the federal bench in Ohio implemented their own rules to make sure the person filing the action to foreclose was the proper party. *In re Foreclosure Cases*, 521 F. Supp. 2d 650, 654 (N.D. Ohio 2007).

**The new foreclosure law requires an affidavit of ownership.** See § 7-105.1 (d)(2)(iii).

### b. LOST NOTE

The law requires a copy of the original note. There has been rash of lost note affidavits under the prior foreclosure laws. Often, the lost note affidavits did not meet the standards under Maryland law. Section 3-309 (a) of the Maryland Commercial Law

Article provides:

(a) A person not in possession of an instrument is entitled to enforce the instrument if (i) the person was in possession of the instrument and entitled to enforce it when loss of possession occurred, (ii) the loss of possession was not the result of a transfer by the person or a lawful seizure, and (iii) the person cannot reasonably obtain possession of the instrument because the instrument was destroyed, its whereabouts cannot be determined, or it is in the wrongful

provisions of § 12-101 et seq will apply. [It should be noted that § 12-103 (b)(3) provides that if it is a refinance, then the fee limitations of the Maryland Secondary Mortgage Loan Law, discussed below, will apply.]

§ 12-125 requires that a lender provide a financing agreement within ten days of the application. The financing agreement is required to make various disclosures relating to the terms of the loan. If the financing agreement provides that it is subject to change, then the lender must provide a final commitment agreement at least 72 hours before settlement. Violations of this provision can be remedied through damages and attorneys. There is a similar requirement under CLEC and CGRCP, § 12-1022 and § 12-922, respectively.

**c. SECOND MORTGAGES**

The Maryland Secondary Mortgage Loan Law, § 12-401 et seq., limits both the fees and provisions that may be contained in a second mortgage governed by it. The law applies to both open end and closed end loans. The fee limitations are set forth at § 12-404-406. It also contains a prohibition on false advertising. § 12-403. The law also applies to unlicensed or licensed lenders. § 12-401 (b). It also applies to sale leaseback transactions. § 12-401 (d). The penalties include the loss of the right to collect interest. § 12-413. The Court of Special Appeals recently held that the statute of limitations for enforcement of the penalties is 3 years but it runs from each collection of interest.

**d. NEW FORECLOSURE LAWS**

The new foreclosure laws provide a series of requirements for lenders and rights for borrowers. The lender must provide a notice of intent to foreclose. § 7-105.1 (c). It must include the amount due to reinstate the loan. § 7-105.1 (c)(4)(ii). There are

possession of an unknown person or a person that cannot be found or is not amenable to service of process.

Notwithstanding, the person who has lost their note, will also the right to foreclose under the new law since they will not be able to meet the requirements. See § 7-105.1

(d)(2)(iii).

## **VI. Protection of Homeowners in Foreclosure Act**

The law was enacted initially as emergency legislation on May 26, 2005. Most of the legal publishers have overlooked this fact and state the law became effective on October 1, 2005. The legal publishers are simply wrong. In the last legislative session, PHIFA was substantially changed. Below is a summary of the provisions of what I refer to as the 2005 Maryland Protection of Homeowners in Foreclosure Act and the recently enacted 2008 Maryland Protection of Homeowners in Foreclosure Act.

### **THE 2005 MARYLAND PROTECTION OF HOMEOWNERS IN FORECLOSURE ACT**

- I. Major areas of the law:
  - a. Required additional notice to homeowners of foreclosure proceedings. Subsection ( a-1) added to Section 7-105 – Homeowner to be provided notice that an Order to Docket has been filed along with specific warning in 14 pt type size.
  - b. Regulation of “Foreclosure Consultants” Definitions at Sec 7-301 and other provisions at Sec. 7-305-307.
  - c. Rights to cancel post foreclosure transactions Sec. 7-310-311
  - d. Rights to cancel transactions relating to assignment of surpluses Sec. 7-314-315
  - e. Provides remedies for violations of Act. Sec. 7-318-321
- II. Additional Notice to Homeowners

Under prior law, the homeowner was only entitled to be mailed notice of a sale not more than 30 days before a scheduled nor less than 10 days before the sale. As a result, the homeowner was often the last to know that a sale was moving forward. This allowed scam artists to pretend to have superior knowledge than the homeowner. This “advantage” was improperly used by scam artists. The law added a requirement that the homeowner be given notice within 2 days after an order to docket was filed that a foreclosure was docketed.

NOTE: the law was also amended under subsection (h) to provide that a homeowner does not re-acquire rights if a foreclosure sale is not settled.

- III. Foreclosure Consultants.
  - a. Definition of “foreclosure consultant” very broad and based on acts.
  - b. Any agreement for assistance can be canceled at any time
  - c. Any agreement must include specific disclosures and must set forth the compensation to be received by the foreclosure consultant
  - d. Be accompanied by a notice of right to cancel
  - e. Cannot take any fees until all services performed
  - f. Obtain power of attorney from homeowner other than to review documents
- IV. Post Foreclosure Sales or other transfers
  - a. Any sale or other arrangement after a foreclosure is initiated against a homeowner now has specific requirements including:
    - i. A “Notice of Deed or Transfer of Title” must be provided in 12 point type. The document must include the entire agreement of the parties and contain specific disclosures as to the parties, the terms of the transaction, the consideration, any liabilities that the homeowner will remain responsible for since many of these transactions involved taking the property “subject to existing liens”.
    - ii. The homeowner must be provided notice of a right to cancel the transaction in 14 point type on a separate document (not on the back of any document). The right to cancel may not be conditioned by a return of any funds and can be given in any manner. The 3 business day period for exercise of the right to cancel does not begin to run until homeowner is provided notice of right to cancel.
    - iii. There are specific requirements and prohibitions that apply to foreclosure purchasers. This includes requiring compliance with the Home Ownership and Equity Protection Act. See Sec. 7-311.
    - iv. Requirement that a foreclosure purchaser split any sale revenues with the homeowner if the property is sold within 18 months.
- V. Surpluses
  - a. Any acquisition of the right to a foreclosure surplus now requires:
    - i. Written Contract with specific provisions similar to the provisions applicable to post foreclosure sales discussed above
    - ii. Homeowners has the right to cancel agreement up until 10 days after audit
- VI. General Provisions applicable to all sections.
  - a. Limit interest on any funds advanced to 8%

- b. Right to cancel cannot be conditioned, e.g., return of funds
- c. Right to cancel does not begin to run until notice of right is given
- d. Right to Cancel must be on separate paper and not on back of any document
- e. There are certain provisions that are void including waiver of any provisions of the law, any choice of law other than Maryland law or venue that is outside the County where the property is located or any fees in excess of the Circuit Court filing fees.
- f. Effective date: May 26, 2005
- g. Lawyers, mortgage brokers, bankers, current holder of secured claims and realtors exempt from provisions of Act.

VII. Penalties and enforcement provisions

- a. AG can enforce
- b. Private right to enforce includes damages and attorneys fees. Court can award treble damages if done willfully or knowingly. Note: Willful in civil setting is other than by accident.
- c. Criminal penalty is misdemeanor with up to 3 years and \$10,000 fine but is not subject to 1 year statute of limitations.

**THE 2008 MARYLAND PROTECTION OF HOMEOWNERS  
IN FORECLOSURE ACT**

The world has changed. Many of the exemptions have disappeared. The persons protected by the law has been enlarged to include those in default at least 60 days on their home mortgages. The time to rescind has been expanded to 5 days from receipt of the notices required by the Act.

## FORECLOSURE DEFENSE EXERCISES

### I. PRE-LITIGATION PRACTICE TIPS

Obtain all documents you can from any source. Use a QWR under RESPA.

### II. INJUNCTIONS

Exceptions to Injunction Requirement

- a. New Rules
- b. Truth in Lending – federal preemption
- c. Legal fiction of no default

### III. COUNTERCLAIMS & THIRD-PARTY CLAIMS

Counterclaims are allowed in foreclosure proceedings. *Fairfax Sav., F.S.B. v. Kris Jen Ltd. Partnership*, 338 Md. 1, 655 A.2d 1265 (1995). There is no case that addresses it but there is no prohibition on third party claims in foreclosure actions. Since the holder of the loan is not a party, the holder will need to be invited to the party through a third party complaint.

### IV. JURY DEMANDS

At first glance, it appears there is no right to a jury trial in connection with a foreclosure proceeding. The foreclosure proceeding is considered an action in equity there is no right to jury trial. However, the foreclosure proceeding is permitted by statute and rules. The legislature may not create equitable causes of action through statutes. *Martin v. Howard Co.*, 349 Md. 469, 709 A.2d 125 (1998).

Further, the foreclosure procedure includes possession issues in the nature of ejectment. Ejectment actions are actions at law, which would entitle a person to a trial by

jury. If an action consists of both legal and equitable issues, the legal issues should be tried first to preserve the right to trial by jury. *Higgins v. Barnes*, 310 Md. 532; 530 A.2d 724 (1987).

Additionally, there may issues of fact relating to the defenses. If these include legal issues, that may involve fact issues relating to the foreclosure, the legal issues should be presented to the jury first under Maryland law. *Higgins v. Barnes, supra*.

## V. EXCEPTIONS

Exceptions are to be filed within 30 days of the report of sale. See Maryland Rule 14-305 (d)(1). However, exceptions filed before the sale is ratified may be heard by the court. Under the current rules, a request for hearing on the exceptions may be made but it is the discretion of the court whether to hold a hearing. A hearing is required for the court to set aside the sale. Rule 14-305 (d)(2). Exceptions have been historically limited. There are equitable issues that have been successful, e.g., lender advised that sale would not occur and homeowner did not take action based on that information.

## VI. BANKRUPTCY

Due to a lack of adequate notice or an opportunity to be heard under the old law, bankruptcy was the preferred method of addressing a foreclosure. The bankruptcy laws provide for an automatic stay. 11 U.S.C. § 362. The bankruptcy had to be filed before the sale to stop the foreclosure. Actions taken in violation of the automatic stay are void. *In Re Lampkin*, 116 B.R. 450, (Bkrcty.D.Md.,1990).

The most common bankruptcy used in connection with stopping a foreclosure sale is a Chapter 13 proceeding. 11 U.S.C. § 1301 et seq. Chapter 13 is a debt adjustment plan which provides a mechanism for a debtor to cure pre-petition arrearages of a secured debt

as part of the debtor's payment plan. 11 U.S.C. § 1322 (b)(3). There is no equivalent provision for a Chapter 7 liquidation bankruptcy. A chapter 7 will delay the foreclosure proceeding by operation of the automatic stay but it will not provide a resolution to the problem by itself.