IN THE COURT OF COMMON PLEAS OF FRANKLIN COUNTY, OHIO
GENERAL DIVISION

ANNIE R. SWAYNE, :

Plaintiff, : **Case No.: 05 CVC-04-4327**

v. : **Judge: Guy L. Reece, II**

BEEBLES INVESTMENTS, INC., et al. :

Defendants. :

FILED
COMMON PLEAS COURT
FRANKLIN CO. OHIO
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DECISION AND ENTRY
GRANTING IN PART AND DENYING IN PART
PLAINTIFF'S JANUARY 23, 2006
MOTION FOR SUMMARY JUDGMENT
AND
DENYING DEFENDANTS' FEBRUARY 9, 2006
MOTION FOR SUMMARY JUDGMENT

RENDERED THIS 3rd DAY OF NOVEMBER 2006.

REECE, J.

This matter is before the Court upon Plaintiff Annie Swayne's (hereinafter "Plaintiff") January 23, 2006 Motion for Summary Judgment; Defendants Beebles Investments, Inc. and Timothy R. Farkas' (hereinafter collectively "Defendants") February 9, 2006 Motion for Summary Judgment and Memorandum Contra Plaintiff's Motion for Summary Judgment; Plaintiff's February 27, 2006 Response to Defendants' Motion for Summary Judgment and Reply to Defendants' Memorandum Contra Plaintiff's Motion for Summary Judgment; Defendants' March 30, 2006 Reply to Plaintiff's Response to Defendants' Motion for Summary Judgment; and the parties' respective arguments presented during the August 30, 2006 oral arguments hearing. The parties' motions have been fully briefed and are deemed submitted to the Court pursuant to Loc.R. 21.01.

For the reasons that follow, the Court **GRANTS IN PART AND DENIES IN PART** Plaintiff's January 23, 2006 Motion for Summary Judgment and **DENIES** Defendants' February 9, 2006 Motion for Summary Judgment.

BACKGROUND

Plaintiff is a 77-year-old widow who, upon her husband's passing, received title to her home, located at 3823 Second Avenue in Columbus, Ohio, unencumbered by any debt. After a few years, Plaintiff's roof began to leak and her kitchen and bathroom needed extensive repairs. As Plaintiff could not afford the repairs on her fixed income of $1,206.00 per month, she contacted Defendant Beebles Investments, Inc. dba A-Loan, Co. (hereinafter "Beebles") for assistance.

Plaintiff met with Duane Scott (hereinafter "Scott"), a loan officer and operations manager for Beebles, and informed him that she needed money to repair her roof and kitchen. Initially, Scott attempted to broker a loan through lenders other than Beebles. However, as all of those lenders turned Plaintiff down because of her poor credit score, Defendant Timothy Farkas (hereinafter "Farkas"), president of Beebles, decided to loan Plaintiff the requested $20,000.00, with Beebles serving as the lender. Said loan was secured by a note and mortgage on Plaintiff's home.

The $20,000.00 loan was not a traditional loan; rather, it was a "balloon" loan, whereby Plaintiff did not have to make any payments on that loan for one full year, at which time a balloon payment of $25,612.11 would become due. Plaintiff maintains she did not understand at that time that the loan was a balloon payment loan. Plaintiff appears to have executed two loan applications for the at-issue $20,000.00 loan, with one set of documents dated as executed on June 27, 2002, and the second set dated as executed on June 28, 2002. While the June 27, 2002 set of loan application documents indicates Plaintiff was to make monthly payments on the loan in the amount of $250.00, the June 28, 2002 set reveals the monthly payments were set at $0.00. Likewise, while the Home Ownership and Equity Protection Act of 1994 document, dated as executed on June 27, 2002, indicates the loan's annual percentage rate is 37.918% and Plaintiff is to make monthly payments thereon in the amount of $250.00, the same document, dated as executed on June 28, 2002, indicates the annual percentage rate on Plaintiff's loan is 36.508% and Plaintiff is to make one final payment in the amount of $25,612.11.

On July 10, 2002, Plaintiff executed the loan agreement and mortgage documents with respect to her $20,000.00 loan (hereinafter "the loan agreement"). The Balloon Rider attached to the loan agreement, titled "Balloon Note Addendum – Conditional Right to Refinance" (hereinafter "Balloon Addendum"), provides Plaintiff with the right to refinance the loan upon the fulfillment of certain conditions. According to the Balloon Addendum, Plaintiff was guaranteed the right to "obtain a new loan with a new Maturity Date of August 1, 2032 and with an interest rate equal to the 'New Loan Rate'" as set forth in Section Three of the Balloon Addendum, provided Plaintiff met certain conditions outlined in Sections Two and Five of the Balloon Addendum. Specifically, Plaintiff could refinance and/or convert her balloon loan into a traditional 30-year loan provided she satisfied the following conditions: 1.) Plaintiff must still be the owner and occupant of the property at the time she executes her right to refinance; 2.) Plaintiff must be current in the monthly payments due on the note and not more than 30 days late on any of the twelve scheduled monthly payments immediately preceding the loan's maturity date; 3.) that there be no liens, defects, or encumbrances against the property, or other adverse matters affecting title to the property arising after the security instrument was recorded;

and 4.) that the New Loan Rate could not be more than five percentage points above the Note Rate.

In order to exercise her option to refinance and assuming those conditions were satisfied, Plaintiff was to provide Beebles, as the Note Holder, with written notice of her intent to exercise her Conditional Refinance Option no earlier than 60 calendar days and no later than 45 calendar days prior to the loan's maturity date, i.e., August 1, 2003. However, Section Five of the Balloon Addendum contains yet another condition, namely, that the Note Holder (Beebles) notify the Borrower (Plaintiff), at least 60 calendar days prior to the loan's maturity date, of the accrued but unpaid interest and other sums due on the note, as well as notify Plaintiff of her right to exercise her Conditional Refinance Option. At that point, Plaintiff would have had 30 days to provide Beebles with acceptable proof of her required ownership, occupancy and property lien status. Beebles would then advise Plaintiff of the new loan interest rate, new monthly payment amount, and the date, time and place where Plaintiff would appear to sign any documents required to complete the refinancing.

The Court notes that, according to the terms of the Balloon Note attached to the Balloon Rider Addendum, Plaintiff was to pay an interest rate equal to 24.99% per annum on her $20,000.00 loan. Although the Note states the Borrower is to make monthly payments on the first of each month, beginning with September 1, 2002, the Note further states the monthly payments are to be in the amount of $0.00. However, the Federal Truth-In-Lending Disclosure Statement attached to the loan documents indicates the annual percentage rate on the loan is 41.657%. The record further reveals that Plaintiff received only $13,734.60 out of the $20,000.00 loan. Out of the remaining $6,265.40 that was distributed as settlement charges, $2,000.00 was disbursed to Beebles as loan origination and loan discount fees.

Plaintiff's deposition testimony reveals that, after executing the applicable loan documents, Plaintiff deposited the $13,734.60 loan proceeds into a joint checking account that Plaintiff kept with her daughter. It appears Plaintiff obtained said checking account so that her daughter could access the account assets in the event Plaintiff died, but instead of opening a "payable on death" account, Plaintiff opened the joint account. A portion of the loan proceeds was subsequently garnished out of that account due to a garnishment order placed thereon by Plaintiff's daughter's creditors. Plaintiff further testified that she used approximately $2,500.00 of the remaining money to "get caught up" on past due car payments, and another $3,000-$4,000.00 to pay past due credit cards and utilities bills. Plaintiff then became ill and used a portion of the money to pay for her medicine and various emergency paramedic services. Thus, Plaintiff did not use the loaned money to perform any of the repairs on her house.

As the loan's maturity date loomed and it became apparent that Plaintiff would not be able to repay the balloon loan, Plaintiff and Defendants entered into a Real Estate Purchase Statement, Agreement and Release on June 5, 2003 (hereinafter "the real estate agreement"). Therein, Plaintiff acknowledged that she made no payments toward her $20,000.00 balloon loan in the preceding year and that she made no improvements and/or repairs to her home. Plaintiff then deeded her property to Beebles in exchange for not having to pay off the mortgage, being released from the mortgage note, and avoiding any risk of foreclosure. Beebles, meanwhile, agreed to make the necessary repairs to the roof, kitchen and bathroom, and to rent the premises to Plaintiff for a two-year lease period at $450.00 per month. Pursuant to the terms of the real estate agreement, Plaintiff would have the option to buy her property back from Beebles at the end of the two-year lease period, provided she qualified for satisfactory financing. In the event

Plaintiff was not able to buy back her house, Beebles was to renegotiate the terms for an extended lease agreement.

Although the repairs on the house were performed, Plaintiff maintains the work done was of very poor quality. While the leaks above the fireplace were repaired, Plaintiff testified during her deposition that the roof now leaks in the utilities room, the floor tiles in the bathroom are coming off, and one of the replaced kitchen cabinets is coming off the wall. The record reveals Defendants paid approximately $25,000.00-$30,000.00 for those repairs.

Approximately five months later, on November 12, 2003, Beebles sold the property to PBL Family Limited (hereinafter "PBL") for $55,000.00. The record reveals that Plaintiff, since that time, has made rental payments to PBL. Furthermore, according to the December 1, 2003 Rental Agreement between Plaintiff and PBL, Plaintiff's rent increased to $500.00 per month.

Plaintiff initiated this action on April 15, 2005, alleging Defendants' conduct with respect to the loan and real estate transactions was unconscionable, that the resulting agreements are unconscionable and thus voidable, and that Plaintiff is entitled to rescission of the same along with appropriate equitable damages.

On January 23, 2006 Plaintiff filed a Motion for Summary Judgment. Therein, Plaintiff maintains she is entitled to summary judgment in her favor, as 1.) the July 10, 2002 balloon loan agreement with Beebles is unconscionable and therefore voidable; 2.) the terms of the June 5, 2003 real estate agreement are unconscionable and the agreement is therefore voidable; 3.) Defendants violated Ohio's Consumer Sales Practices Act; 4.) Defendants violated Ohio's Mortgage Brokers Act; 5.) Defendants committed fraud and fraudulently induced Plaintiff to enter into the balloon loan and mortgage agreement; 6.) Defendants breached the July 10, 2002 balloon loan and mortgage agreement; and 7.) Defendant Farkas should be held personally liable for Beebles' wrongdoings.

On February 9, 2006, Defendants filed their own Motion for Summary Judgment and a Memorandum Contra Plaintiff's Motion for Summary Judgment. Defendant Farkas maintains he is not personally liable to Plaintiff for any of the claims asserted in her Complaint, as there existed no contractual relationship between Defendant Farkas, personally, and Plaintiff. Defendants further argue the July 10, 2002 loan agreement was not unconscionable and did not contain unfair and unreasonable terms, as Defendants did not expect Plaintiff to actually pay the balloon payment at the end of the year. Rather, Defendants argue they expected Plaintiff to make the necessary repairs on her home and participate in credit rehabilitation, and then obtain financing to refinance the balloon loan. Defendants further argue that Ohio's Consumer Sales Practices Act does not apply to mortgage transactions, and they cannot be held to have violated Ohio's Mortgage Brokers Act as they did not act as mortgage brokers in connection with Plaintiff's loan transaction. Defendants likewise argue Plaintiff has not sufficiently established all of the elements of a fraud claim.

LAW & ANALYSIS

I. SUMMARY JUDGMENT

Ohio Civil Rule 56, which governs the procedure for granting a motion for summary judgment, provides that before summary judgment may be granted, a court must first determine: 1.) that there is no genuine issue as to any material fact that remains to be litigated; 2.) that the moving party is entitled to judgment as a matter of law; and 3.) that it appears from the evidence that reasonable minds can come to but one conclusion, and that conclusion, when viewing the evidence in a light most favorable to the party against whom the motion for summary judgment is made, is adverse to that same party. *Temple v. Wean United, Inc.* (1977), 50 Ohio St.2d 317, 327, 364 N.E.2d 267.

Courts have cautioned, however, that "[s]ummary judgment is a procedural device to terminate litigation and to avoid a formal trial where there is nothing to try. It must be awarded with caution, resolving doubts and construing evidence against the moving party, and granted only when it appears from the evidentiary material that reasonable minds can reach only an adverse conclusion as to the party opposing the motion." *Norris v. Ohio Standard Oil Co.* (1982), 70 Ohio St.2d 1, 2-3, 433 N.E.2d 615, citing *Morris v. First National Bank & Trust Co.* (1970), 21 Ohio St.2d 25, 28, 254 N.E.2d 683.

While considering motions for summary judgment, trial courts must also pay particular attention to the shifting burdens between the moving and non-moving parties. The moving party bears an initial burden of informing the court of the basis for its motion and of "identifying those portions of the record that demonstrate the absence of a genuine issue of material fact on the essential element(s) of the non-moving party's claim." *Dresher v. Burt* (1996), 75 Ohio St.3d 280, 293, 662 N.E.2d 264. If the moving party does not point to some evidence of the type listed in Civ.R. 56(C), which demonstrates that the non-moving party has no evidence to support its claims, a motion for summary judgment must be denied. Id. However, once the moving party meets its initial burden, the burden then shifts to the non-moving party to bring to the court's attention facts showing a genuine issue for trial, and if this reciprocal burden is not met, summary judgment must be granted. Id.

In determining whether there are genuine issues as to any material fact(s), courts must examine the applicable substantive law. *Miller v. Loral Defense Systems* (1996), 109 Ohio App.3d 379, 383, 672 N.E.2d 227. "A 'material fact' depends on the substantive law of the claim being litigated." *Hoyt, Inc. v. Gordon & Associates, Inc.* (1995), 104 Ohio App.3d 598, 603, 662 N.E.2d 1088, citing *Anderson v. Liberty Lobby, Inc.* (1986), 477 U.S. 242, 247-248, 106 S.Ct. 2505. "[T]he substantive law will identify which facts are material. Only disputes over facts that might affect the outcome of the suit under the governing law will properly preclude the entry of summary judgment. Factual disputes that are irrelevant or unnecessary will not be counted." *Miller*, 109 Ohio App.3d at 383, citing *Anderson*, 477 U.S. at 248.

II. UNCONSCIONABILITY

Unconscionability, defined as the "absence of meaningful choice on the part of one of the parties to a contract, combined with contract terms that are unreasonably favorable to the other party," is a question of law to be decided by the court. *Beneficial Mortgage Co. v. Leach*, Franklin App. No. 01AP-737, 2002-Ohio-2237, at ¶56, citing *Orlett v. Suburban Propane* (1989), 54 Ohio App.3d 127, 129, 561 N.E.2d 1066; *Jeffrey Mining Prod., L.P. v. Left Fork Mining Co.* (2001), 143 Ohio App.3d 708, 718, 758 N.E.2d 1173. "The unconscionability doctrine consists of two prongs: (1) substantive unconscionability, i.e., unfair and unreasonable contract terms, and (2) procedural unconscionability, i.e., individualized circumstances surrounding parties to a contract such that no voluntary meeting of the minds was possible." *Leach*, 2002-Ohio-2237, at ¶57, citing *Dorsey v. Contemporary Obstetrics & Gynecology* (1996), 113 Ohio App.3d 75, 80, 680 N.E.2d 240.

While substantive unconscionability involves factors related to the contract terms and their fairness, procedural unconscionability involves factors "bearing on the relative bargaining position of the contracting parties, such as 'age, education, intelligence, business acumen and experience, relative bargaining power, who drafted the contract, whether the terms were explained to the weaker party, whether alterations in the printed terms were possible, whether 'e were alternative sources of supply for the goods in question.'" *Cronin v. California Fitness*, Franklin App. No. 04AP-1121, 2005-Ohio-3273, at ¶12, quoting *Collins v. Click Camera & Video* (1993), 86 Ohio App.3d 826, 834, 621 N.E.2d 1294.

A. Unconscionability of the July 10, 2002 Loan Agreement

Plaintiff maintains the July 10, 2002 mortgage loan agreement, along with the Balloon Rider Addendum and Balloon Note attached thereto, are unconscionable and therefore voidable. Plaintiff maintains the terms of the loan agreement were not only unfair and unreasonable given the circumstances, but they were also unlawful in light of the provisions concerning a loan subject to the Home Ownership and Equity Protection Act of 1994. Plaintiff maintains the agreement is also procedurally unconscionable, as Defendants took advantage of Plaintiff's desperation, age, and lack of education and business acumen to induce her to agree to those terms. The Court, having considered the parties' arguments and having reviewed the evidence presented, finds said argument to be well taken.

In determining the reasonableness or fairness of the terms, "the primary concern must be with the terms of the contract considered in light of the circumstances existing when the contract was made," and the test to be used is whether the terms "are 'so extreme as to appear unconscionable according to the mores and business practices of the time and place.'" *Leach*, 2002-Ohio-2237, at ¶60, quoting 1 Corbin, Contracts (1863), Section 128, Note 2. The July 10, 2002 loan agreement required Plaintiff to pay a lump-sum amount of $25,612.11 at the end of one year, despite Plaintiff's fixed income of $1,206.00 per month and her then-existing debts, including $17,126.00 on a car loan, $2,663.00 in credit cards, and $227.00 in medical expenses. Defendants acknowledge they knew that Plaintiff would not be able to make the lump-sum payment when due, and were aware of the numerous lenders who had turned down Plaintiff's loan applications due to her poor credit history. Defendant Farkas himself acknowledged that "this would have been a bad loan for a bank." (Farkas Depo., at 75.) Defendants maintain the terms are not unreasonable, as they did not expect Plaintiff to be able to repay the balloon note when due. However, it is precisely because Defendants knew Plaintiff could not abide by the balloon payment terms, but included those terms in the loan agreement anyway, that the terms are substantively unconscionable. It matters not that Plaintiff had a conditional option to refinance the balloon loan when Plaintiff was not afforded the opportunity to take advantage of that option. Farkas' deposition testimony reveals that he does not normally do long-term loans, as they tie up his money, and he wanted his money back. Furthermore, Defendants knew about the poor state of Plaintiff's finances, knew that she could not pay off the balloon loan, and knew that no other lenders were willing to loan her money, and despite that knowledge Defendants entered into a loan agreement with Plaintiff under terms she could not possibly abide by.

Plaintiff further argues that the loan agreement terms are unlawful. Plaintiff maintains the loan in question is covered by the Home Ownership and Equity Protection Act of 1994 (hereinafter "HOEPA"), and as such Defendants are not allowed to charge closing costs greater than 8% of the total loan amount. Furthermore, pursuant to R.C. §1321.571, Defendants cannot contract for and receive interest at a rate higher than 25.00% of the unpaid principal balance. The Court notes the closing costs associated with the July 10, 2002 loan were $6,265.40, approximately four times the allowed amount, and although the interest rate Plaintiff was charged was 24.99%,[1] the annual percentage rate on the loan was 41.657%.

Pursuant to 12 C.F.R. §226.32, a mortgage transaction covered by the statute, i.e., a consumer credit transaction that is secured by the consumer's principal dwelling, "shall not

[1] According to the loan documents, Plaintiff paid $1,000.00 in loan discount fees, otherwise known as "points." Points are ordinarily paid by a borrower so as to reduce the loan's interest rate. However, the loan documents herein reveal Plaintiff's interest rate was 24.99% out of a maximum rate of 25.00%.

include the following terms: (1) (i) Balloon payment. For a loan with a term of less than five years, a payment schedule with regular periodic payments that when aggregated do not fully amortize the outstanding principal balance. (ii) Exception. The limitations in paragraph (d)(1)(i) of this section do not apply to loans with maturities of less than one year, if the purpose of the loan is a 'bridge' loan connected with the acquisition or construction of a dwelling intended to become the consumer's principal dwelling." 12 C.F.R. §226.32(d)(1). As Plaintiff points out, the balloon loan offered by Beebles had a term of one year, and the loan was not a "bridge" loan.

Based on the foregoing, the Court finds the July 10, 2002 loan agreement is substantively unconscionable.

With respect to the procedural aspects of the two-prong unconscionability test, the Court notes Plaintiff was, at the time of the transaction, a 75-year-old widow, living on a fixed income of $1,206.00 per month, comprised of her deceased husband's social security and pension benefits, as well as disability benefits Plaintiff receives from the Ohio Bureau of Workers Compensation stemming from a back injury in 1972. The record further reveals Plaintiff has not worked since 1972, and the highest educational level she ever completed is the twelfth grade. Plaintiff admits she was desperate to repair her house. Her roof leaked over the fireplace area of the living room, the bathtub was unstable, starting to come off of the wall, and it leaked around the base, and the metal kitchen cabinets were coming off of the walls. During her deposition, Plaintiff stated on numerous occasions that she did not understand the balloon loan agreement at the time she executed the documents, that she believed Defendants would give her a set period of time within which she could repay the money, that she subsequently believed Defendants would give her two years to buy back her house, but that Defendants sold her home anyway and she did not know that she could buy her home back from PBL if she was able to obtain proper financing.

Plaintiff repeatedly stated that she was in a very bad financial state, was behind on her bills even though she tried to pay off as much as she could, that she attempted to bring her debts current using the loan money but became ill and had to expend more money on medicine and doctors' bills, and that she did not think anyone else would loan her money. Plaintiff also did not bring along a friend, family member, or attorney to the loan closing, but relied on the representations and loan explanations provided by Defendants.

On the other hand, Defendants began their relationship with Plaintiff acting as her mortgage brokers. They were well aware of her dire financial situation and her desperate need to repair her aging home. Defendants knew Plaintiff could not repay the balloon note according to the terms of the July 10, 2002 loan agreement, yet presented Plaintiff with pre-printed form documents whereby Plaintiff agreed to terms Defendants knew she could not satisfy. Defendants are experienced mortgage brokers, lenders, and real estate businessmen, with superior knowledge of the lending industry, superior business acumen and significantly greater bargaining power given the circumstances. Accordingly, the Court finds the circumstances sufficiently establish procedural unconscionability with respect to the July 10, 2002 balloon loan and mortgage agreement.

Based on the foregoing, the Court finds the loan transaction at issue was unconscionable and is voidable. The Court thus **GRANTS** Plaintiff's Motion for Summary Judgment with respect to her claim of unconscionability, as the same relates to the July 10, 2002 balloon loan and mortgage agreement and transaction.

B. Unconscionability of the June 5, 2003 Real Estate Agreement

Plaintiff further argues the June 5, 2003 Real Estate Purchase Statement, Agreement and Release (hereinafter "the real estate agreement") is likewise unconscionable and voidable. Said agreement provides that Plaintiff will deed her home to Beebles in exchange for a release from her debt on the balloon loan, the forgiveness of that debt, and that no foreclosure proceedings would be filed with respect to the loan. Plaintiff maintains the agreement is unconscionable because Defendants did not wait until the balloon note became due, and did not refinance Plaintiff into a 30-year loan despite her meeting the conditional refinance conditions, but rather approached Plaintiff prior to that date and induced her to sign the real estate agreement in exchange for not foreclosing on her home. Plaintiff argues Defendants, in exchange for a $13,000.00 check on a $20,000.00 loan, took her home and subsequently sold it to PBL for $55,000.00.

As the real estate agreement was procured in association with the balloon loan, and as the Court has determined said loan was unconscionable and thus voidable, the Court finds Plaintiff's arguments with respect to the voidability of the subsequent real estate agreement to be well taken. The same, if not more, dire and telling circumstances existed at the time of the real estate agreement as did at the time of the loan agreement, thereby rendering the real estate transaction both substantively and procedurally unconscionable.

The Court finds additional evidence of Defendants' unconscionable conduct surrounding the real estate agreement and transaction in the sale price of Plaintiff's home. In a letter addressed to "A Loan Company" and dated July 15, 2002, Craig Glass of Glass Appraisal Services states that, in his opinion, "the estimated market value of the property, as of July 15, 2002, is $55,000.00." The closing date of the at-issue balloon loan, as pre-printed on the loan documents, was July 10, 2002. However, the record also reveals that Defendants sold the property to PBL on November 12, 2003, for $55,000.00.

Defendants maintain that, while Plaintiff could not qualify for a loan back in 2002, and while they were the only ones who would lend her money at the time based on her bad debt and low income, the "plan" all along was that Plaintiff, after repairing her home and thereby increasing its value, would be in a better financial situation so as to qualify for a 30-year loan in light of the increased value of her sole asset. However, Defendants also argue that they added value to the home subsequent to lending money to Plaintiff, as they allegedly paid approximately $25,000.00-$30,000.00 in repairs to the home. That Defendants would argue they added value to the home, when they sold it for exactly the same amount that the home was appraised in 2002, is truly outrageous and a testament to the unconscionability inherent in this transaction.[2]

Based on the foregoing, the Court finds the real estate transaction at issue was unconscionable and is voidable. Accordingly, the Court **GRANTS** Plaintiff's Motion for Summary Judgment with respect to her claim of unconscionability, as the same relates to the June 5, 2003 real estate agreement and transaction.

III. THE OHIO MORTGAGE BROKERS ACT

The Ohio Mortgage Brokers Act, R.C. §1322.01, et. seq., states, in pertinent part, that "[n]o mortgage broker, * * * shall do any of the following: * * * (B) Make false or misleading statements of a material fact, omissions of statements required by state law, or false promises regarding a material fact, through advertising or other means, or engage in a continued course of misrepresentations; (C) Engage in conduct that constitutes improper, fraudulent, or dishonest dealings; * * * (E) Knowingly make, propose, or solicit fraudulent, false, or misleading statements on any mortgage document or on any document related to a mortgage, including a

[2] Despite the Glass Appraisal Services appraisal of $55,000.00 on July 15, 2002, Farkas testified during his deposition that Plaintiff's home, at the time she deeded it over to Beebles in 2003, was not more than "$30,000 tops. Maybe on a great day, 35 grand. I would say when she deeded that property to me, it wasn't really worth too much more than what I had in it." (Farkas Depo., at 98.)

mortgage application, real estate appraisal, or real estate settlement or closing document. * * * (F) Knowingly instruct, solicit, propose, or otherwise cause a buyer to sign in blank a mortgage related document." R.C. §1322.07.

Defendants are licensed mortgage brokers. Plaintiff approached Defendants in June 2002 in an effort to obtain mortgage broker services from them. The record reveals Defendants pulled Plaintiff's credit report and began the brokerage process, but were unable to secure a lender on her behalf. Only after becoming privy to the information with respect to Plaintiff's financial state did Defendants, in effect, change hats and start acting as Plaintiff's lender.

Plaintiff argues Defendants violated Ohio's Mortgage Brokers Act in four ways: 1.) they placed Plaintiff in a one-year balloon note despite HOEPA's prohibitions against a balloon loan with a terms of less than five years; 2.) they had Plaintiff sign a blank loan application document that was completed by someone other than a loan officer or mortgage broker; 3.) they confused Plaintiff by providing her with three good faith estimates within two days; and 4.) they charged Plaintiff $1,000.00 in points to reduce her interest rate but failed to actually reduce her rate.

Defendants argue the loan was offered through Beebles only after the brokering attempts had failed, and they therefore did not represent Plaintiff as mortgage brokers and cannot be held to have violated Ohio's Mortgage Brokers Act. The Court is not persuaded by that argument.

As the Harrison County Common Pleas Court held in *Myer v. Preferred Credit* (2001), 117 Ohio Misc.2d 8, a mortgage broker is a fiduciary with a duty to act in the best interest of the client and cannot engage in self-dealing and double dealing. *Myer*, 117 Ohio Misc.2d at paragraph ten of the syllabus. As the court held therein, "[t]he law is jealous to see that a trustee [fiduciary] shall not engage in double dealing to his own advantage and profit. The reason is not difficult to discover when it is remembered that a trusteeship [fiduciary] is primarily and of necessity a position of trust and confidence, and that it offers an opportunity, if not a temptation, to disloyalty and self-aggrandizement. The connotation of the word and name 'trustee' ['fiduciary'] carries the idea of a confidential relationship, calling for scrupulous integrity and fair dealing." *Myer*, 117 Ohio Misc.2d at 22, citing *In re Estate of Binder* (1940), 137 Ohio St. 26, 37-38, 27 N.E.2d 939. Although *Myer* addressed issues of dual agency and hidden mortgage broker kick-backs, the Court finds the analysis in *Myer* is equally applicable to the case at bar. The Court particularly notes the following language: "A fiduciary owes the duty of good faith and loyalty to his principal * * * A fiduciary must act in accordance with the highest standard of integrity, with utmost good faith, and with scrupulous openness, fairness, and honesty, and a court of equity can and will require such behavior * * * Abuse of a relation of trust or confidence for personal aggrandizement is the cardinal sin of a fiduciary, and courts are quick to denounce, prevent, or remedy any such action." *Myer*, 117 Ohio Misc.2d at 24, citing 49 Ohio Jurisprudence 3d (1984) 66, 71, Fiduciaries, Section 13.

The record reveals Plaintiff contacted Beebles after seeing and/or hearing an advertisement indicating Beebles could obtain a loan for someone who, like Plaintiff, has no or bad credit history. When Plaintiff approached Beebles, Scott attempted to broker a loan for her but was unable to find a willing lender due to her minimal income and bad debt. The record is clear that Plaintiff approached Defendants and sought from them mortgage brokerage services. The fact that Defendants then decided to use the information obtained during the mortgage brokerage process and themselves lend the money to Plaintiff does not relieve Defendants from the duties initially undertaken as Plaintiff's mortgage broker. The at-issue balloon loan was offered to Plaintiff with Defendants' knowledge that Plaintiff had been turned down by numerous lenders, that no other lender would loan Plaintiff money, and that Plaintiff was in desperate need of a loan so that she could repair her leaky roof, bathroom and kitchen.

Although Defendants maintain Ohio's Mortgage Brokers Act does not apply to them, as they ultimately served as Plaintiff's direct lender, the Court finds Defendants originally provided mortgage broker services to Plaintiff and the subsequent events in question derive from this initial relationship. Having established a fiduciary relationship with Plaintiff, Defendants had a legal obligation to act in good faith toward Plaintiff and to resist the temptation for "personal aggrandizement." However, rather than acting in the best interest of the client, Defendants took advantage of Plaintiff's inexperience, age, and financial situation to make a loan with extraordinarily high rates which did not serve Plaintiff's best interests, a loan that Defendants knew Plaintiff could not repay. Defendants claim the original loan was made so that Plaintiff could pursue other financing options using the increased value of a repaired home. However, Defendants knew or should have known that such a project would be impossible to realize with the $13,734.60 that Plaintiff received from the loan, especially since it cost Defendants approximately $25,000.00-$30,000.00 to make the same repairs. Based on the foregoing, and in light of the particular circumstances inherent in this action, the Court finds the prohibitions contained in Ohio's Mortgage Brokers Act continued to apply to Defendants even after they took off the "mortgage broker" hat and replaced it with a "lender" hat.

As the Court has already addressed Plaintiff's arguments with respect to Defendants' HOEPA violations, it will not repeat the same herein. At a minimum, the Court notes the at-issue balloon loan was not a "bridge" loan as defined by 12 C.F.R. §226.32(d)(1)(ii) and had a term of less than five years. Furthermore, the record reveals Plaintiff was charged various loan fees that were greater than 8% of the total loan amount.

With respect to Plaintiff's argument that she signed the loan application in blank, the Court notes Plaintiff's exhibits submitted during the August 30, 2006 oral arguments hearing indeed show a blank application was signed, without any information listed therein with respect to Plaintiff's income, expenses, assets and liabilities. Furthermore, Defendants have not presented any evidence to dispute Plaintiff's argument that the person who interviewed her and completed the application was Elizabeth Farley, Defendant Farkas' secretary, who is not a licensed loan officer or mortgage broker.

Finally, the record reveals Defendants provided Plaintiff with different good faith estimates, setting forth different payment obligations and interest rates, as is evident from the two sets of documents dated June 27, 2002, and June 28, 2002, respectively. The settlement statement associated with the at-issue balloon loan further reveals Plaintiff was charged $1,000.00 for a loan discount fee, also known as "points," yet Plaintiff's interest rate on the loan was 24.99%; the highest interest rate that could have been charged on the loan is 25.00%.

As the *Myer* court held, "[a] broker owes a special duty of fair dealing where he is acting for an inexperienced or aged principal," further noting that a fiduciary's duty of good faith and loyalty prohibits self-dealing.[3] *Myer*, 117 Ohio Misc.2d at 24, citing 12 Corpus Juris Secundum (1980) 169, Brokers, Section 56. Based on the foregoing, the Court finds Defendants, who initiated their fiduciary relationship with Plaintiff as her mortgage brokers, violated Ohio's Mortgage Brokers Act by engaging in conduct that was improper, fraudulent and misleading, by

[3] "Self-dealing is aptly described as follows: 'Basically, self-dealing relates to transactions wherein a [fiduciary], * * * acting for himself and also as [fiduciary], a relation which demands strict fidelity to others, seeks to consummate a deal wherein self-interest is opposed to duty. * * * Equity, in such cases, pauses not to inquire, whether the [principal] has sustained a loss.'" *Myer*, 117 Ohio Misc.2d at 25, citing *In re Estate of Binder*, 137 Ohio St. at 27; *First Natl. Bank of Birmingham v. Basham* (1939), 238 Ala. 500, 191 So. 873, 125 A.L.R. 656.

acting in a manner inconsistent with Plaintiff's best interest, and by breaching their duties to Plaintiff by engaging in dishonest dealings designed for Defendants' gain.

Accordingly, the Court **GRANTS** Plaintiff's Motion for Summary Judgment with respect to Plaintiff's claim of a violation of Ohio's Mortgage Brokers Act.

IV. THE OHIO CONSUMER SALES PRACTICES ACT

The Ohio Consumer Sales Practices Act, R.C. §1345.01, et seq., (hereinafter "CSPA") makes it unlawful for a supplier to commit an unconscionable act or practice in connection with a consumer transaction. R.C. §1345.03(A). Plaintiff argues that Defendants are "suppliers," as defined in the CSPA, and are therefore governed by the provisions and requirements set forth in the CSPA.

The Court notes R.C. §1345.01 creates an exception for mortgage brokers and lenders, as it defines a "consumer transaction" as a transaction that "does not include transactions between persons, defined in sections 4905.03 and 5725.01 of the Revised Code, and their customers * * *." R.C. §1345.01(A). Dealers in intangibles are excluded from the CSPA as they are among those defined in R.C. §5725.01. Dealers in intangibles "includes * * * business[s] that consist primarily of lending money * * * whether on their person's own account with a view to profit or as agent or broker for others, with a view to profit or personal earnings." R.C. §5725.01(B)(1).

Recently, Ohio Senate Bill 185 was passed with the intent to remove mortgage brokers and lenders from the "dealers in intangibles" exception. However, Senate Bill 185 is to go into effect on January 1, 2007. Defendants cannot be held to have violated an Act that has yet to be applied to them. Accordingly, the Court **DENIES** Plaintiff's Motion for Summary Judgment with respect to Plaintiff's claim of a violation of Ohio's Consumer Sales Practices Act.

V. FRAUD

The elements of fraud include: "(a) a representation or, where there is a duty to disclose, concealment of a fact, (b) which is material to the transaction at hand, (c) made falsely, with knowledge of its falsity, or with such utter disregard and recklessness as to whether it is true or false that knowledge may be inferred, (d) with the intent of misleading another into relying on it, (e) justifiable reliance upon the representation or concealment, and (f) a resulting injury proximately caused by the reliance." *Mussivand v. David* (1989), 45 Ohio St.3d 314, 322, 544 N.E.2d 265, citing *Burr* v. *Stark County Board of Commrs.* (1986), 23 Ohio St.3d 69, 491 N.E.2d 1101, paragraph two of the syllabus. See also *Nu-Trend Homes* (Sept. 12, 1995), Franklin App. No. 94APE10-1483, 1995 Ohio App. LEXIS 3968, at *19-20, citing *Cross v. Ledford* (1954), 161 Ohio St. 469, 475, 120 N.E.2d 118; *Schwartz v. Capital Savings & Loan Co.* (1978), 56 Ohio App.2d 83, 86, 381 N.E.2d 957.

Plaintiff argues that Defendant Farkas made the following material misrepresentations, knowing that Plaintiff would rely upon them: 1.) that she qualified for the $20,000.00 balloon loan; 2.) that in the event she was unable to re-pay the loan in one year, Plaintiff would then have the right to refinance the loan for a 30-year term; 3.) that if Plaintiff was unable to repay the $20,000.00 loan in one year, she would face foreclosure; 4.) that Beebles would lease the property at 3823 Second Avenue to Plaintiff for two years and then allow her to buy it back; 5.) that if Plaintiff was not in a position to buy back the property after two years, Beebles would renegotiate the terms for an extended lease agreement. Plaintiff further argues these statements were made falsely, with Defendants' knowledge of their falsity or with such utter disregard and recklessness as to whether they were true or false that knowledge may be inferred.

Defendants argue that there was no fraud and that no representation was ever made to Plaintiff that she could afford the balloon note on the loan. Defendants claim that both sides knew that alternative financing would have to be found. Defendants also argue that any statements made regarding foreclosure were not fraudulent because, if Plaintiff failed to refinance or extend the mortgage or pay Beebles, she would then indeed have faced foreclosure.

The Court finds the record clearly establishes, and neither party disputes, that Plaintiff was never in a financially sound position so as to be able to afford the loan or repay the same. Based on Plaintiff's fixed limited income, the amount of the balloon loan, and the amount of money she actually received from that loan, there was virtually no possibility of repayment based solely on Plaintiff's meager means. Defendants hold themselves out to be experienced professionals in the mortgage brokerage and lending industries, and as such they knew or should have known that, given Plaintiff's financial obligations and the amount of money she ultimately received from the loan, i.e., \$13,734.60, Plaintiff would not be able to make the necessary repairs to her home and reduce her already existing debt to such an extent so as to qualify for a 30-year loan, especially since Defendants knew that no other lenders would loan money to Plaintiff. As Farkas' deposition testimony reveals, the repairs themselves cost between \$25,000.00 and \$30,000.00. Defendants maintain they lent Plaintiff the money supposedly on the condition that Plaintiff would make repairs to her house, pay down her debt, and thereafter become eligible for refinancing. However, Defendants knew that out of the \$20,000.00 balloon loan Plaintiff would only receive \$13,734.60. Thus, Defendants knowingly misrepresented to Plaintiff that she could 1.) afford the loan on her assets alone and 2.) that she would be able to qualify for refinancing based on those assets, even after receiving and using the loan proceeds.

Defendants argue that they never intended for Plaintiff to repay the balloon loan; rather, Plaintiff's loan could either be refinanced through a new lender or the loan could be converted into a 30-year loan. However, when the Court inquired how can a 70-year-old's credit history be rebuilt and repaired in one year when she didn't qualify for such loans at the time, Defendants' counsel was not able to explain. Instead, Defendants argued Plaintiff was to use the loan proceeds and repair her home, after which she would qualify for one of those two loans. Defendants' counsel acknowledged that Farkas did not know what the repairs were at the time he loaned Plaintiff the money and argued that, as a lender, Beebles is not obligated to investigate whether the loan requested is sufficient to cover the repairs needed. While ordinarily a lender may not have an obligation to a borrower to ascertain whether the money borrowed is sufficient to meet the borrower's needs, when Beebles represented to Plaintiff that she would qualify for a 30-year loan after making the repairs using the loan money, Beebles was obligated to investigate the accuracy of its representations before making them.

Furthermore, once Plaintiff's loan neared its maturity date, it was apparent to Defendants that Plaintiff would not be able to make the balloon payment. Plaintiff's testimony indicates that she requested a refinance on multiple occasions, but that Farkas refused to refinance, telling Plaintiff that she was not qualified. Farkas then drafted a real estate agreement through which Plaintiff deeded her house to Beebles. The agreement was drafted such that Plaintiff was induced into believing that she would be able to repurchase her house after the two-year lease period. However, as Plaintiff had satisfied the conditions set forth in Section Two of the Balloon Note Addendum, she was entitled to refinance her loan and convert it into a 30-year loan, and there was no need for her to deed over her home. The record further reveals that, only six months after the parties executed the real estate agreement, whereby Plaintiff was to rent her home for two years at $450.00 per month and would then be allowed to buy back her house, Defendants sold the house to PBL, who then raised Plaintiff's rent to $500.00 per month.

The Court notes that, during the August 30, 2006 oral arguments hearing, counsel for Plaintiff and counsel for Defendants both acknowledged that there are no genuine issues of material fact herein, and this case should be decided on their competing motions for summary judgment. Accordingly, and based on the foregoing, the Court finds Plaintiff has sufficiently establishes that, 1.) by lending her the money, Defendants knowingly misrepresented to Plaintiff that the loan terms were lawful and favorable to her, and that she could afford to repay the balloon loan; 2.) by granting Plaintiff a conditional right to refinance, Defendants knowingly misrepresented to Plaintiff that she could refinance the balloon loan into a 30-year loan; 3.) by entering into the real estate agreement, Defendants knowingly misrepresented to Plaintiff that she had to deed over her home in order to avoid foreclosure and that she could buy it back after renting the same for two years. Plaintiff, as an elderly woman, with limited education and income, and no experience with the lending industry, reasonably relied upon those misrepresentations, which were material to her decisions to enter into the transactions and agreements. Defendants used their superior knowledge and experience in lending matters, as well as superior bargaining position, and induced Plaintiff to believe that she could afford the unusually expensive loan by giving her the loan, that she would be able to refinance her balloon loan or convert it into a 30-year loan, that she had no option but to deed her house to Beebles because she did not qualify to refinance, and that, in two years, she could buy back her house. Each of those misrepresentations led Plaintiff to act to her detriment, culminating in her losing a home that she previously owned debt-free.

Based on the foregoing, the Court finds Plaintiff has sufficiently established the existence of fraud with respect to Defendants' actions herein. Accordingly, the Court **GRANTS** Plaintiff's Motion for Summary Judgment with respect to her fraud claim.

VI. BREACH OF CONTRACT

According to the terms of the July 10, 2002 loan agreement, Defendants were to refinance Plaintiff's balloon loan provided Plaintiff satisfied the conditions of the Balloon Note Addendum. Plaintiff maintains that, as the conditions were satisfied, she had a right to refinance and Defendants were required to inform her of her right to refinance. Plaintiff maintains Defendants breached the terms of the loan agreement by failing to refinance her balloon loan, despite her meeting the requisite conditions, and by inducing her into deeding her home over to Beebles.

Plaintiff further argues Defendants breached the June 5, 2003 real estate agreement by selling Plaintiff's house to PBL only five months after executing said agreement, which gave Plaintiff the right to buy her house back from Beebles after renting the same for two years.

However, as the Court has found those agreements to be unconscionable and voidable, and as Plaintiff seeks to void those agreements and be placed back in the same condition she was prior to entering into the agreements, the Court finds there is no need to address Plaintiff's arguments with respect to the alleged breaches of those agreements.

VII. APPLICABILITY OF CORPORATE SHIELD DOCTRINE

It is a fundamental aspect of corporate law that, ordinarily, corporate shareholders, officers, and directors are not liable for the debts of the corporation. *Belvedere Condominium Unit Owners' Assn. v. R.E. Roark Companies* (1993), 67 Ohio St.3d 274, 287, 617 N.E. 2d 1075, citing Presser, Piercing the Corporate Veil (1991) 1-

4. However, equity demands that an exception to this rule be provided to "protect creditors of a corporation from shareholders who use the corporate entity for criminal or fraudulent purposes. * * * Under this exception, the 'veil' of the corporation can be 'pierced' and individual shareholders held liable for corporate misdeeds when it would be unjust to allow the shareholders to hide behind the fiction of the corporate entity. Courts will permit individual shareholder liability only if the shareholder is indistinguishable from or the 'alter ego' of the corporation itself." Id. Specifically, courts disregard the corporate form and hold individual shareholders liable for the corporation's wrongdoing when "(1) control over the corporation by those to be held liable was so complete that the corporation has no separate mind, will or existence of its own, (2) control over the corporation by those to be held liable was exercised in such a manner as to commit fraud or an illegal act against the person seeking to disregard the corporate entity, and (3) injury or unjust loss resulted to the plaintiff from such control and wrong." *Belvedere Condominium Unit Owners' Assn.*, 67 Ohio St.3d at 289.

Farkas maintains he cannot be personally liable for the wrongdoings, if any, of Beebles, as he was but an agent of the corporation. Plaintiff, meanwhile, argues Beebles' corporate veil should be pierced and Farkas held liable, as Farkas was the alter ego of the corporation. The record reveals that Farkas is a 50% shareholder of Beebles, with the remaining 50% held by Farkas' brother, who merely provided the start-up money for the corporation. Farkas, as the president and sole corporate officer of Beebles, has complete control over Beebles. As Farkas himself stated during his deposition, " * * * I control it all. I handle all – everyday functions. Everything." (Farkas Depo., at 18.) Farkas further testified that he is in charge of "problem solving, paying bills, legal work, accounting work, aggressive advertising, taking risks." (Id., at 21.) Farkas testified that he personally approves all of the loans made by Beebles and he was the one who determined that Plaintiff was eligible for a loan from Beebles and determined the terms of that loan. (Id., at 51-52.) Furthermore, Farkas was the one who determined Plaintiff did not qualify for refinancing, and denied her request to convert her balloon loan into a 30-year loan, arguing Plaintiff failed to fix up her home and he does not usually like to do long-term loans because "[i]t just ties up all of your money. I need to keep things going and keep advertising, and I need – I wanted my money." (Id., at 91.) Farkas also was the one who drafted the real estate agreement, pursuant to which Plaintiff could buy back her home after two years, and he was the one who decided to sell Plaintiff's home to PBL soon thereafter because, according to Farkas, "[Plaintiff] was getting behind on her rent, and that's another reason why I sold it. * * * Yep. So I didn't want to deal with it because I wanted my money." (Id., at 88-89, 99, 109.) These actions were committed by Farkas, were fraudulent, and were committed in the name of Beebles, a corporation that had little or no independent existence outside of Farkas' will. Based on the foregoing, the Court finds Defendant Farkas' fraudulent conduct, as well as his control over Beebles and over these events, was so complete that he should be held personally liable for the harm caused to Plaintiff.

Accordingly, as Plaintiff has sufficiently satisfied the elements with respect to the piercing of the corporation's veil, as enumerated in *Belvedere Condominium Unit Owners' Assn.*, the Court **DENIES** Defendants' Motion for Summary Judgment with respect to Defendant Farkas being shielded from liability for Beebles' wrongdoings.

Based on the foregoing, the Court **GRANTS** Plaintiff's January 23, 2006 Motion for Summary Judgment with respect to 1.) Plaintiff's claim of unconscionability, as the same relates to the July 10, 2002 loan agreement and transaction and the June 5, 2003 real estate agreement and transaction, 2.) Plaintiff's claim pursuant to Ohio's Mortgage Brokers Act, and 3.) Plaintiff's fraud claim; **DENIES** Plaintiff's January 23, 2006 Motion for Summary Judgment with respect to Plaintiff's claim pursuant to Ohio's Consumer Sales Practices Act; and **DENIES** Defendants' February 9, 2006 Motion for Summary Judgment with respect to Farkas' personal liability.

Furthermore, the Court **REFERS** this matter to Magistrate Pamela Broer-Browning for determination of appropriate damages within 90 days of the Court's decision.

IT IS SO ORDERED.

GUY L. REECE, II, JUDGE

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