55604

IN THE CIRCUIT COURT OF RALEIGH COUNTY, WEST VIRGINIA

LLOYD KEITH LILLY and
BARBARA LILLY, individually and
on behalf of all others similarly situated,

Plaintiffs,

v. **CIVIL ACTION NO. 03-C-778-K**

BANK ONE NATIONAL ASSOCIATION
COLUMBUS f/k/a BANK ONE WEST
VIRGINIA, N.A. and THOMAS M.
HAZLETT, HOMECOMINGS FINANCIAL NETWORK,
INC., a corporation, RESIDENTIAL FUNDING
CORPORATION, a corporation, as subsidiary of
GMAC and RESIDENTIAL ASSET SECURITIES
CORP. HOME EQUITY MORTGAGE ASSET
BACKED PASS, through the CERTIFICATE
SERIES 1999 -KS2, a trust, and O. GAY ELMORE,

Defendants.

MEMORANDUM IN SUPPORT OF MOTION FOR PRELIMINARY/TEMPORARY INJUNCTION

INTRODUCTION

Plaintiffs have moved for a preliminary/temporary injunction to enjoin the defendant Homecoming Financial Network, Inc. ("HFN") from charging illegal fees and charges and then moving to foreclose when people cannot pay illegal fees or collecting them under the threat of foreclosure.

STATEMENT OF FACTS

The Defendant HFN has proceeded against the named Plaintiffs in the ways described and in similar fashion to class members.

The Plaintiffs entered into the loan that is the subject of this action in December of 1998. The Plaintiffs' loan has been serviced by HFN since the loan origination in 1998.

In or around March 2003, HFN returned the Plaintiffs' payment of $1,450.00 and told the Plaintiffs' their home had been placed in foreclosure. When the Plaintiffs called to ascertain the amount they were required to pay to save their home from foreclosure, they were told that they needed to pay four monthly payments plus $650.00 in attorney fees.

Charge for Attorney's Fees and Return of Payments. On May 22, 2002, the Plaintiffs' May payment of $733.00 was returned to them and they were informed that their home had been sent to foreclosure. At this time, the Plaintiffs called HFN to ascertain the amount of money it would take to get their home out of foreclosure. HFN represented that the Plaintiffs would be required to pay a total of five monthly payments plus attorney fees of $725.00. The Plaintiffs sought the advice of counsel in order to save their home from foreclosure and informed HFN it was illegal to charge the Plaintiffs $725 in attorney fees to get their home out of foreclosure. The Defendant agreed to waive the illegal attorney fees and the Plaintiffs signed a forbearance agreement and paid the Defendant $3,606.00 on July 8, 2002. Yet beginning Aug, 2002, plaintiffs' billing statements included attorney fees of $751.30 appeared as "Fees and Expenses."

Charges for Duplicative Insurance On May 13, 2002, the Plaintiffs received a letter from HFN informing them that insurance had been force-placed on their account at a cost $328.00 year. The Plaintiffs informed the HFN that they already had homeowners insurance through Nationwide, but the Defendant refused to cancel the force-placed insurance.

B. Changes Resulting from the Securitized Predatory Lending Model.

HFN is pursuing foreclosure of many West Virginia homes for failure to pay charges not due.

The many subprime, broker-originated loans of the HFN serviced loans are not owned by but are serviced by HFN, a third party servicer. The joint United States Department of Housing and Urban Development ("HUD") and Department of Treasury Report on subprime predatory lending by the HUD-Treasury National Predatory Lending Task Force attributes in great measure the significant growth of predatory lending to the use of asset securitization. See HUD-Treasury Task Force Report On Predatory Lending at 39-41 (2000) (available at <www.hud.gov/pressrl/treasrpt.pdf>). Asset securitization has enabled subprime lending to expand exponentially over the last decade. See id.; see also Keith Wofford & David Burkhalter, *Predatory Lending and Home Equity Securitizations*, Moody's Investors Service at 1-3 (April 28, 2000). The asset securitization model has generated billions on Wall Street, largely on the backs of low income consumers.

Securitization is similar to issuing a corporate bond, except that the lender does not promise to repay principal and interest to the investor, but rather promises to use the consumers' loan payments to repay investors. It works like this: An entity driving the system, known as the master lender, enters into a series of agreements through which groups of mortgage loans are brokered, originated and funded pursuant to underwriting guidelines laid out by the master lender. Once the loans are funded, they are transferred into a trust created by the master lender. The trust issues securities which are sold to investors. The trust in turn uses the funds from investors to buy more mortgage loans from a front end lender, who either originates the loans through a broker, or who underwrites the origination of loans. Finally, the consumers' loan payments are used to repay the investors who purchased the securities. The right and duty to collect payments from the borrower, is severed from the principal of the loans and sold to another entity or retained by the lender.

The rights and obligations of the master lender, the trust, the originating lender and the servicer, are typically spelled out in a lengthy contract called a "pooling and servicing agreement" or "PSI." These pooling and servicing agreements set forth who is going to service the loans for the trust and who services servicing fees for the various services. The servicer's income is derived totally from the various fees for servicing the loan at various stages.

Actions of the front lender or loan originator are, as a practical matter, directed by the terms and conditions set forth in loan purchase agreements and pooling and servicing agreements, which are drafted by the master lender which may be a holding company for a lender or who can appear as an assignee or servicer on certain documents. See, e.g., England v. M.G. Investments, 93 F. Supp. 2d 718, 722 n.5 (S.D.W. Va. 2000).

C. History of Local Lending in West Virginia.

With home loans and refinancing by banks and various local lenders for a hundred years, abuses like those engaged in by HFN did not arise. First, such lenders did not routinely add illegal charges, and did not return payments and then seek to foreclose. These lenders were locally based and felt an obligation to the community at large, and even if they had been so inclined, such a stunt would not be tolerated.

The duty of a lender to pursue alternatives to foreclosure was seldom an issue because it was always in the lender's economic interest to work out any practical alternatives possible. The lender did not want to take the home because of community pressure, an economic interest in keeping customers, and the potential for loss on a foreclosure sale. This has changed with mortgage loan servicers which have an economic interest in pursuing foreclosure since their fees are tied to specific services and no longer own the loans.

LEGAL DISCUSSION

A. Standard for Granting Preliminary Injunction.

Rule 65 of the *West Virginia Rules of Civil Procedure* provides for preliminary injunctions. W. Va. R. Civ. P. 65(a). In determining whether to grant a preliminary injunction, the Court should employ the balance of hardship test:

> Under the balance of hardship test the . . . court must consider, in 'flexible interplay,' the following four factors in determining whether to issue a preliminary injunction: (1) the likelihood of irreparable harm to the plaintiff without the injunction; (2) the likelihood of harm to the defendant with an injunction; (3) the plaintiff's likelihood of success on the merits; and (4) the public interest.

Jefferson County Bd. of Educ. v. Jefferson County Educ. Ass'n, 183 W. Va. 15, 24, 393 S.E.2d 653, 662 (1990) (citing Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bradley, 756 F.2d 1048, 1054 (4th Cir.1985)). As the following discussion concludes, the Plaintiffs have shown a high likelihood of success on the merits. Additionally, the likelihood of harm to the Plaintiffs outweighs any harm to the Defendant. Finally the public interest is served by granting the injunction. Accordingly, the injunction should be granted.

B. Equitable Relief is Requested to Stop Illegal Charges and Foreclosures Resulting Therefrom.

HFN adds impermissible fees, such as attorneys fees or inspection fees. These charges are illegal under West Virginia law. West Virginia law makes very clear that no charges be added that are not authorized by Chapter 46A:

> (a) Except for reasonable expenses including costs and fees authorized by statute, incurred in realizing a security interest, the agreement with respect to a consumer credit sale or a consumer loan may not provide for charges as a result of default by the consumer other than those authorized by this chapter.

W. Va. Code § 46A-2-115.[1] In addition, expressly prohibited are collection costs and attorneys fees. See W. Va. Code §§ 46A-2-127(g) (prohibiting "[a]ny representation that an existing obligation of the consumer may be increased by the addition of attorney's fees, investigation fees, service fees, or any other fees or charges when in fact such fees and charges may not legally be added to the existing obligation"); 46A-2-128(c) (declaring as unconscionable "[t]he collection or the attempt to collect from the consumer all or any part of the debt collector's fee or charge for services rendered"). See e.g., Armstrong v. First Collect, Inc., No. 2:97-CV-0092, slip op. at 7-11 (S.D.W. Va. Sept. 11, 1998) (Ex. A). Accordingly, the Defendant's imposition of such fees or charges is illegal under West Virginia law.

C. Similar Relief Has Been Granted to Prevent Servicing Abuses By Circuit Courts in This State.

Two other servicers who engaged in similar conduct have been temporarily enjoined from charging illegal fees and foreclosures until those charges have been refunded and reformed. First, Fairbanks Capital Corp. was temporarily enjoined from all foreclosures as a result the fees therefrom (See Temp. Inj. Order, Overbaugh v. Fairbanks Capial Corp, No. 03-C-2 (Cir. Ct. Lincoln Co. Jan. 8, 2003) (Ex. B); Def. Trustee's Position Re: Prelim. Inj. Relief (Ex. C) (describing duty of the trustee).) Also, EMC Mortgage Corporation, another national servicer was similarly enjoined from all foreclosures and charging illegal fees. (See Ex. D.)

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[1] The "reasonable expenses including costs and fees authorized by statute, incurred in realizing on a security interest" include only (i) reinstatement period fees for publication costs, etc. after foreclosure is initiated for loans originated by banks and savings and loans, and Fannie & Freddie, etc. held loans *Wes t Virginia Code* §46A-2-115(b) and (ii) those charges expressly permitted by *West Virginia Code* section 38-1-7. Under section 38-1-7, **after the foreclosure sale**, the trustee may collect a commission on the sale as permitted by that section. The only other statutorily authorized charges include bona fide late fees. See W. Va. Code §§ 46A-3-112 -113.

The Final Injunctive Order entered by the Court in the Fairbanks Order describes the illegalities of adding illegal fees to the account:

> 2. Fees. (a) The Defendants shall not add any fees to the accounts of any class members other than bonafide late fees ("delinquency fees") consistent with *W. Va. Code* § 46A-3-112 (not exceeding fifteen dollars), in no event sooner than ten days after the due date of the scheduled installment and only after the time period set forth in the applicable note, and agreed deferral charges consistent with *W. Va. Code* § 46A-3-114. See attached schedule Exhibit A. Attorneys fees and other fees not set forth above are not permitted. Escrow amounts include only amounts authorized by the original loan agreement or later arms length agreement (a) as are necessary to pay taxes or (b) as are necessary for escrowed privately-placed insurance or for forced placed insurance only during those months in which the consumer actually has no insurance. These are permitted to be collected through foreclosure but foreclosure will not be pursued for nonpayment of insurance only.
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> **EXHIBIT A**
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> **Schedule of Permissible Default Fees**
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> 1. Delinquency fee ("late fees") imposed no sooner than ten days after the due date of the scheduled installment in accord with the loan payment.
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> 2. The following reinstatement period fees (between notice of foreclosure sale and sale date) only for loans held by federal home loan board, federal home loan mortgage corporation, and government national mortgage association: (a) publication costs, (b) essential appraisal fees after loans referred to trustee for foreclosure, ©) title check and lienholder notification fee notification fee not to exceed $200, (d) actual certified mailing cost paid to post office.
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> 3. Deferral charges under W. Va. Code § 46A-3-114.
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> Not permitted (not inclusive) are
> - property inspection fees
> - attorneys fees
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> This schedule does not preclude post-foreclosure sale commissions and expenses under W. Va. Code § 38-1-7.

(Final Order, Lucas v. Fairbanks, Civ. No. 03-C-2, (Cir. Ct. Lincoln County, Jan. 27, 2004)(Ex.E).

CONCLUSION

This case is no different from those servicing abuse cases where statewide injunctions have been granted. HFN has a pattern and practice of charging illegal fees and threatening foreclosure until the fees and charges are paid. The injunction should accordingly be granted.

KEITH and BARBARA LILLY,
individually and on behalf of
all others similarly situated,
By Counsel.

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