

## **ABA/ NLADA 2005 Equal Justice Conference**

### **Pro Bono And Legal Services Partnering To Combat Predatory Foreclosure Practices**

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#### **Brief Description:**

Our workshop will explore with you the way to develop and coordinate legal service and pro bono attorneys and social service, bar association and law school resources to represent, educate and divert low and moderate income homeowners from foreclosure and predatory lending practices and how to develop a team of lawyers and foreclosure prevention community organizations to defend against predatory equity stripping scammers. We will also discuss how to develop and implement with the assistance of bar association and law school resources certain financial literacy programs to educate low and moderate income homeowners about predatory lending practices and the general public about financing home purchases.

#### **Topical Outline:**

- I. The illegal practice of foreclosure rescue scams is stripping vulnerable lower and middle income homeowners of millions of dollars in equity in their homes and gutting cities of valuable affordable housing. These insidious scams are calculated to create homelessness in their wake. The following statistics reported by the Minnesota Attorney General were cited in separate reports issued in June 2003 from the Annie E. Casey Foundation and the Mortgage Bankers Association of America:
  - a. The costs of predatory lending practices, including equity stripping, to American consumers top \$9 billion a year.
  - b. According to the Mortgage Bankers Association of America, in the 3 months that ended in June 2003, the percentage of home mortgages in foreclosure rose to a record of 404,400 out of 33.7 million mortgaged homes. The number is the highest rate in the 30 years that the association has been monitoring mortgages.
  - c. On average, consumers with sub prime mortgages were eight times more likely to lose their home in default than those with prime, conventional mortgages. For those who do not lose their homes to default, there are still

very high costs in the form of hefty fees, penalties and inflated interest rates.

- d. The Fannie Mae Foundation estimates that the total annual cost of fees paid from high-cost financial service-industries to be more than \$5.45 billion.
  - e. According to ACORN Minnesota, predatory lending affects more than 10,000 Minnesota homeowners annually and costs more than \$83 million in home equity, interest payments and mortgage insurance.
- II. Predatory lending has been defined as “engaging in deception or fraud, manipulating the borrower through aggressive sales tactics, or taking unfair advantage of a borrower’s lack of understanding about loan terms.” U.S. Dept. of Housing and Urban Development and U.S. Dept of the Treasury, Joint Report Recommendations to Curb Predatory Mortgage Lending 1. (2000). In the same report, the authors concluded that a loan can be considered predatory when lenders or brokers a) charge borrowers excessive, often hidden fees and at rates often higher than necessary to cover profit and risk, b) loan flipping by successively refinance of loans at no benefit to the borrower, c) make loans without regard to a borrower’s ability to repay, d) engage in high-pressure sales targeting on vulnerable populations such as elderly, low-to-moderate income families and those with medical care or other debts, e) steer unsophisticated borrowers who could qualify for prime products to the sub prime products, f) rushed or incomplete disclosure of loan terms, g) make loans with large prepayment penalties which make refinance difficult or impossible, h) engage in abusive collection and aggressive foreclosure practices. *See Predatory Lending: Recent Initiatives to Define and Eliminate Lending Abuse, Banking Law, Matthew Bender & Co., Inc. (2001).*
- III. Predatory lending practices are taking extreme advantage of low and moderate homeowners and are responsible for the loss of substantial equity in homes and directly contribute to the foreclosure of these homes. It is estimated that the high cost sub prime mortgages carry a delinquency rate at 20 times that of a conventional prime mortgage and the foreclosure rate of these loans have reached as high as 21% of all loans. *Preserving Homeownership: Community Development Implications of the New Mortgage Market, A Report Prepared by Neighborhood Housing Services of Chicago, March 25, 2004.* Most of the foreclosures occur in lower income and minority neighborhoods.
- a. Recent studies have shown that sub prime loans are a) three times more likely in low-income neighborhoods and disproportionately concentrated in low income neighborhoods, especially African-American neighborhoods, b) account for a substantially higher volume of foreclosures than total loan originations, c) are foreclosed more quickly than prime or FHA lenders, d) have default rates which are 3 times the rates for prime mortgages. Fishbein and Bunce, *Subprime Market Growth and Predatory Lending, Housing Policy in the New Millennium*, 2003.

IV. The coalition among Don't Borrow Trouble Minnesota, Minneapolis Legal Aid Society and Volunteer Lawyers Network demonstrates a successful legal project formula to combat predatory lending and equity stripping.

a. Don't Borrow Trouble Minnesota

- i. National movement pioneered in Boston and the Massachusetts Community Banking Council with the assistance of the National Consumer Law Center. Through the efforts of Freddie Mac and others the movement is being expanded to over 30 cities.
- ii. Minnesota coalition Don't Borrow Trouble Minnesota, administered through the Family Housing Fund, was launched March 5, 2003 with the support of over 60 organizations joined together to prevent predatory lending in the Twin Cities and Minnesota.
- iii. A help line for consumers was established by DBT and is hosted by the Greater Twin Cities United Way and is staffed by a trained housing specialist dedicated solely to the DBT program. The help line gives free advice for home buying, refinancing, debt consolidation and mortgage foreclosure advice.
- iv. A referral is made to a group of over 10 metropolitan non-profit housing and foreclosure prevention specialists who assist in homeownership education, housing and financial counseling and mortgage foreclosure prevention advice and assistance.
- v. A referral to Minneapolis Legal Aid Society for advice or representation is made when the screening through a proprietary software program identifies a predatory loan or an equity stripping case.

b. Financial Software

- i. DBT-MN and the law firm of Faegre & Benson of Minneapolis developed a proprietary software program to spot a predatory loan and equity stripping transactions.
- ii. Identification of a predatory loan utilizes a program which takes the actual loan provisions and compares the loan terms to interest rate, APR and other factors and arrives at a ranking which if enough indicia of "red flags" are found will conclude that the loan is predatory. (See Exhibit A.)
- iii. Identification of a potential equity stripping transaction by identifying a number of factors such as:

- known equity strippers,
- promises to save the homeowner from foreclosure through a number of “repurchase” offers all of which involved conveying the title to the property and the equity along with it to the scammer,
- actions to evict homeowners based on nonpayment of “rent” payable to the equity stripper.

c. Referral to Legal Aid and VLN for Predatory Lending/Equity Stripping Representation

- i. Case referrals come in from multiple sources, including: The DBT member foreclosure prevention housing specialists, other legal aid offices, attorneys representing clients in housing court at the time of eviction, the consumer protection division of the Minnesota Attorney General’s office, intake staff of Legal Aid and VLN, individual attorneys who are aware of the task force, and other sources.
- ii. Currently, staff at the Legal Aid Society of Minneapolis (which has received a grant from the Family Housing Fund as part of their participation in Don’t Borrow Trouble) screens all referrals for financial eligibility, status of the adverse proceeding, and general merits of the case. If the case does not appear to have merit, Legal Aid will advise the client or the housing counselor that no further services will be provided. If the case appears to have merit, Legal Aid will determine the appropriate step given the client’s income.
- iii. If the client’s income is more than 187.5% of the Federal Poverty Guidelines based upon family size, the effort is made to refer the case to a private attorney who is either part of the Equity Stripping Task Force or other legal referral service. If the client’s income is less than 187.5% of the Federal Poverty Guidelines based upon family size, Legal Aid will attempt to keep the case in-house, refer to another legal service program, or will try to refer the case to a member of the Task Force or other volunteer attorney through the VLN who is willing to volunteer to take the case pro bono. When determining which cases to pursue, either in-house or for referral to pro bono attorneys, a priority is given on cases where there is a likelihood of success in keeping the family in their home.
- iv. If the case is referred out, Legal Aid drafts a confidential memo to send to VLN and VLN sends the case to the Task Force attorney members under its confidential list serve for referral.

d. Organization and Coordination of the Task Force.

- i. The Task Force consists of private attorneys, both attorneys who will take cases pro bono and attorneys who will take cases for fees which can be negotiated depending on the client's financial situation, legal aid attorneys from the Legal Aid Society of Minneapolis and Southern Minnesota Regional Legal Services (St. Paul's legal aid office) and representatives from the Minnesota Attorney General's office.
- ii. Task Force members were recruited through the efforts of Legal Aid, VLN and DBT through a series of seminars addressed to the legal community about predatory lending and equity stripping. These seminars offering CLE credit were provided at low or no cost to attorneys who would agree to become involved with the Equity Stripping Task Force. Other attorneys who are VLN attorneys with Real Estate and Lending backgrounds have also been recruited to join the Task Force.
- iii. The Task Force meets monthly on the final Monday of each month and cases, strategy, proposed legislation, and recruitment procedures are discussed.
- iv. Ongoing seminars are offered to individual law firms and legal community at large again heightening the understanding and education level of attorneys regarding the predatory lending and equity stripping problem.
- v. Since its inception, cases range from simple advice through full representation and appeal.
- vi. The cases are extremely complicated and involve such legal theories and truth and lending violations, federal and Minnesota deceptive trade practice laws, equitable mortgage law, real estate settlement procedures law, and as many as ten to twenty other defenses not to mention common law fraud. The primary defenses relate to consumer protection law violations, breaches of fiduciary duties and the law of equitable mortgage.
- vii. The panel of attorneys will sometimes take the cases individually or partner with Legal Aid and co-counsel and have begun to develop resources including a brief bank, final order bank, sample complaints, answers and discovery documents as well as news articles and other resources. The Task Force is informal and flexible. To date, all of the cases referred with merit have been taken on for representation.

e. Demonstrated Value to Legal Services and to the Private Pro Bono Legal Provider.

- i. Legal Services attorneys provide a substantial benefit to the Task Force in access to pleadings, research, social service agencies and the pro bono attorneys provide resources such as expertise in real estate, mortgage foreclosure and pro bono financial litigation support and the like. Similarly, private pro bono attorneys provide law firm support and resources to the Legal Aid programs.

V. Participation of the American Bar Association Sections and Law School.

- a. The ABA Real Property Probate and Trust Law Section—Pro Bono Committee—Predatory Lending Subcommittee has developed public information articles and other education tools for addressing predatory lending through its committee members.
- b. The Committee is developing tools for counseling clients on how to spot and avoid predatory lending practices. For example, Debra Stark’s article, *Be a Hero to a Family in Need: Predatory Lenders Beware*”, July/August 2004 issue of Probate and Property.
- c. The Committee is also developing speakers resources to give presentations around the country on spotting and avoiding predatory lending.
- d. The Committee is developing proposed counseling requirements for consumers relating to predatory loans to prevent unfair deceptive practices into model legislation.
- e. The Committee, which is comprised of a number of law school professors, is discussing ways in which class work and curriculum on predatory lending and real estate fraud practices may become part of the curriculum at law schools.

VI. Members of the American Bar Association Section of Business Law – Committee on Consumer Financial Services – Predatory Lending Task Force designed and launched a website called “safeborrowing.com”. The website was created to assist both homebuyers and to assist attorneys representing clients with the financing of their home.

- a. The website was updated in 2004 by including additional practical on-line resources to assist attorneys and the general public and those persons involved with housing and financial-related programs to develop financial literacy information for homeowners and future homeowners.
- b. Plans to expand the website include adding links to other financial literacy websites with reciprocal links to Safeborrowing.com and provide

interactive capability to answer questions. A financial literacy component is also planned for auto financing.

- c. A nationwide network of Committee members and other experts is being established to speak to community and other organizations on consumer financial literacy issues together with developing suitable materials for the presentations.
- d. The Committee intends to work with the newly established federal Financial Literacy Education Commission.

### **Bibliography & Website Links:**

Minnesota Mortgage Foreclosure Prevention Association - <http://www.mmfpa.org/>

Don't Borrow Trouble – Minnesota - <http://www.dontborrowtroublemn.org/>

Center for Responsible Lending - <http://www.responsiblelending.org/index.cfm>

Safeborrowing.com - The American Bar Association – Business Law Section – Consumer Financial Services Committee - <http://www.safeborrowing.com/>

Minnesota Attorney General's website on Home Equity Stripping - <http://www.ag.state.mn.us/consumer/housing/HomeEquityStripping/HomeEquityStripping.htm>

1. *Preserving Homeownership: Community Development Implications of the New Mortgage Market*, a Report Prepared by Neighborhood Housing Services of Chicago, March 25, 2004.
2. Stark, *Become a Hero to a Family in Need: Lenders Beware*, Probate & Property, Vol. 18, No. 4.
3. Nicols, *Home Alone: Home Mortgage Foreclosure Rescue Scams and Theft of Equity*, Journal of Affordable Housing, Vol. 11, No. 3, (Spring 2002)

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