CERTIFIED FORENSIC LOAN AUDITORS, LLC

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Forensic Audit Report

Prepared for: Audit Recipient

Borrower(s): Lance Cassino

Property: 13883 S. Wamblee Valley Rd.; Conifer, CO 80433

June 19, 2012

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June 19, 2012

Certified Forensic Auditors Services
13101 West Washington Blvd., Suite140
Los Angeles, CA 90066

Re: Forensic Audit for Mr. Lance Cassino
Loan #: 1210505017

Dear Audit Recipient:

The loan transaction for the above-referenced borrower/property has been audited[1] for violations of the Truth in Lending Act [15 U.S.C. §1601] ("TILA"), the Real Estate Settlement Procedures Act [12 U.S.C. §2601] ("RESPA"), and to the extent applicable, violations of other state and federal laws discussed below.

This report was based exclusively on the documentation provided. It also required that we make reasonable assumptions respecting disclosures and certain loan terms that, if erroneous, may result in material differences between our findings and the loan's actual compliance with applicable regulatory requirements. While we believe that our assumptions provide a reasonable basis for the review results, we make no representations or warranties respecting the appropriateness of our assumptions, the completeness of the information considered, or the accuracy of the findings.

The contents of this report are being provided with the understanding that we are not providing legal advice, nor do we have any relationship, contractual or otherwise, with anyone other than the recipient. We do not, in providing this report, accept or assume responsibility for any other purpose.

Sincerely,

Shatara Perkins

Shatara Perkins

Senior Certified Forensic Loan Auditor

CERTIFIED FORENSIC LOAN AUDITORS
13101 West Washington Blvd., Suite 140
Los Angeles CA 90066
310-432-6304

[1] Please note that a complete mortgage servicing audit (i.e., audit for RESPA and/or breach of contract violations for the entire servicing history of the loan) is not included in this audit; QWR recommended before such audit can be accomplished.

INTRODUCTION

Interested Parties:

ORIGINAL MORTGAGE LENDER/TABLE FUNDER:	ESCROW/TITLE:	MORTGAGE NOMINEE/BENEFICIARY:
Community Mortgage Group Inc. 1745 Shea Ctr. Dr. #270 Highland Ranch, CO 80129	Security Title Guaranty Co. 1333 W. 120th Ave. #208 Westminister, CO 80234	MERS 102282-1210505017-8 Mortgage Electronic Registration Systems, Inc. P.O. Box 2026 Flint, MI 48051
MORTGAGE BROKER:	**MORTGAGE TRUSTEE:**	**SECURITIZATION:**
Retail loan	TBD	Likely See discussion below.

Documents Provided for Review:

1st	2nd	
		Loan Application (Form 1003) MISSING
		Loan Commitment Letter MISSING
		Good Faith Estimate MISSING
X		Truth in Lending Disclosure Statement
X		(3-Day) Notice of Right to Cancel (may not find with purchase money loans)
X		HUD-1 (or HUD-1A) Settlement Statement
X		Note (with Addendums)
X		Deed of Trust (with Riders) MISSING RIDERS
		Underwriting and Transmittal Summary (Form 1008) MISSING
		Appraisal Report MISSING
		RESPA servicing disclosure MISSING
		Hazard Insurance disclosure MISSING
		Credit score disclosure MISSING
		Lender's Closing Instructions MISSING
		Affiliated Business Arrangement Disclosure MISSING
NA		I/O and/or Neg-Am disclosure
NA		ARM disclosure
X		Itemization of Amount Finance Disclosure
		2 Year W-2's or Tax Returns MISSING
		Current Mortgage statement within the last 30 days MISSING

REPORT SUMMARY

Total Potential TILA Violations (see p. 17): 4

Total Potential RESPA Violations (see p. 19): 2

Total Predatory Lending Violations: (see p. 20):2

CLAIM	CONCLUSION	DETAILS
Underwriting		See p. 14.
TILA APR Tolerance Test		See pp. 17-18.
TILA Finance Charge Test		See pp. 17-18.
TILA Right of Rescission		See pp. 17-18.
Predatory Indicators		See p. 20.
Discrimination*	**POSSIBLE**	See discussion at p. 22.
Fraud*	**POSSIBLE**	See discussion at p. 23.
Other State/Common Law Claims*	**POSSIBLE**	See discussion at p. 25-35.

*(Probability of Violations Ratings: No Evidence or Possible)

Auditor's Summary:

The borrower refinanced the property with Community Mortgage Group, Inc. The interest rate is 5.75%; the amount of interest paid into the loan is $424,949.78. The difference of $232,340.74; goes to the fiduciary as a profit; this is highly predatory on the behalf of the lender.

There were pertinent documents that were missing from the loan transaction which can reflect negatively on the fiduciary agent if they cannot prove that they have the documents in their possession. The GFE, the loan application, the appraisal, RESPA and riders are missing.

There is a lack of due diligence on behalf of the underwriter. The borrowers income was not calculated using the worst case rate to qualify the borrower. This situation ensures that the borrower will experience Extreme Payment Shock because the income of the borrower was not calculated for a decline of income, or increase of personal liabilities. Predatory Lending, Unfair Business Practices – Deceptive Business Acts -are all possible violations of this loan! A QWR is requested on this file to solidify the negligence on the behalf of the lender.

SUMMARY OF LOAN TERMS

The **essential loan terms** were found to be as follows:

Type of Loan:	REFINANCE
Loan Document Date:	SEPTEMBER 26, 2005
Amount of Loans:	$200,000
Appraised Value / Sales Price and LTV:	TBD
Originating Lender:	COMMUNITY MORTGAGE GROUP INC.
Loan Broker:	RETAIL LOAN
Current Servicer:	TBD
Current Note Holder:	LIKELY SECURITIZED
1st Note (ARM) Terms:	
Initial Fixed Rate:	5.75%
Term of Initial Rate:	360 MONTHS
Initial Payment:	$1,167.15
Payment Feature:	30/30
Index Measure:	NA
Index Rate:	NA
Margin:	NA
Fully Indexed Rate:	NA
Min/Max Rate:	NA
TILA disclosed APR:	6.301%
Total Closing Costs:	$9,680.19
Total "Closing Costs" %:	.048%
Prepayment Penalty:	TBD
Unsecured Debt Paid off by Refinance:	TBD
Loan Origination Fees:	$2,000
Loan Discount Fees:	$2,000
Total Broker Fees:	NA
2nd Note (Fixed) Terms:	
Fixed Rate:	
Term of Loan:	
Payment Feature:	
TILA disclosed APR:	
Total Closing Costs:	

FINANCIAL & UNDERWRITING ANALYSIS

Underwriting Standards

The purpose of an underwriter is to determine whether the borrowers can qualify for a loan and if the borrowers have the ability to repay the loan. This determination of the ability to repay a loan is based upon employment and income in large measure, which is proved by getting pay stubs, 1040's, W-2's and a Verification of Employment and Income on the borrowers.

If an underwriter has evaluated the loan properly, then there should be no question of the ability of the borrower to repay the loan. Debt ratios will have been evaluated, credit reviewed and a proper determination of risk made in relation to the loan amount. Approvals and denials would be made based upon a realistic likelihood of repayment.

Automated Underwriting Systems

The underwriter's role in approving loans has been delegated to a support role in the past decade. Automated Underwriting Systems became the normal approval method. An underwriter or even a loan officer would simply input the data and the Automated System would give an approval or denial. Any documents requested would be gathered and then loan documents drawn and signed.

The real issue with the automated systems is that they were not designed to be the "final word" in approval. The system approval was designed to be a guide, a preliminary approval and nothing more. After approval was received, the underwriter would then be expected to extensively review the file, closely examining the documents for final approval.

DISCUSSION: Borrower's financial status at the time of the loan is taken from the loan application. An analysis of borrower's financial status at the time of the loan reveals the following: **The following figures are based on the information from the Loan Application and have not been verified.**

Gross Monthly Income		Mortgage Payment (PITI)	Other Monthly Debt	Total Monthly Debt	Debt-to-income ratio
STATED		$1,167.15	TBD	TBD	TBD

CONCLUSION: Normal underwriting practices include analysis for a 28/36% debt-to-income ratio. During 2003 to 2006, subprime lending involved higher DTI ratios, from 33/38% to 38/50%. **Lender's underwriting standard for this loan far exceeded normal underwriting practices for normal and subprime loans. The Lender/Broker has a fiduciary duty not to put the borrower is HARMS WAY and by approving this loan, the Lender/Broker had put him in HARMS W AY!**

I was unable to review the credit report, income/employment documentation to verify the debt/income ratios. The purpose of an underwriter is to determine whether the borrowers can qualify for a loan and if the borrowers have the ability to repay the loan. This determination of the ability to repay a loan is based upon employment and income in large measure, which is proved by getting pay stubs, 1040's, W-2's and a Verification of Employment and Income on the borrowers. If an underwriter has evaluated the loan properly, then there should be no question of the ability of the borrower to repay the loan. Debt ratios will have been evaluated, credit reviewed and a proper determination of risk made in relation to the loan amount. Approvals and denials would be made based upon a realistic likelihood of repayment. There was no determination of the borrower to repay the loan, with complete disregard for the Guidance Letters issued by Federal Agencies and even Federal and State Law. This disregard for the borrower leads to the potential for legal action under many different legal statutes, UDAP laws, and common law principles.

Underwriting Standards:

The income used to approve this loan was stated by the borrower. The lender used a stated income product for approval based on the value of the collateral used as the security for the loan. Typically, such credit is underwritten predominantly on the basis of the liquidation value of the collateral, without regard to the borrower's ability to service and repay the loan according to its terms absent resorting to that collateral. When a loan has been made based on the foreclosure value of the collateral, rather than on a determination that the borrower has the capacity to make the scheduled payments under the terms of the loan, based on the borrower's current and expected income, current obligations, employment status, and other relevant financial resources, the lender is effectively counting on its ability to seize the borrower's equity in the collateral to satisfy the obligation and to recover the typically high fees associated with such credit. Not surprisingly, such credits experience foreclosure rates higher than normal.

<u>The failure to adequately underwrite this loan could be actionable under:</u> Rescission Law for Fraud, Mistake, Undue Influence, Breach, Illegality Causes of Action could include:

- **Lack of due diligence by the lender in approving the loan.**
- **Lack of Good Faith and Fair Dealings by the Lender.**
- **Fiduciary Duty by the lender for doing a loan where it could lead to default.**
- **Unconscionability by the lender for doing the loan.**

Risk layering is the concept of borrowers having multiple elements of risk in any one loan. Risk would be greater as the different factors that lenders should be concerned about were found in each loan. The more layers of risk, the greater the likelihood of default. Layers of risk in this loan include….

Risk factors for the loan:

1. **Stated income**
2. **High Debt to income Ratios (POSSIBLE)**
3. **Discounted Rate**
4. **Lack of due diligence in underwriting**
5. **High LTV(POSSIBLE)**
6. **Equity Leveraging**
7. **Payment Shock**
8. **Less than adequate reserves verified**

TRUTH IN LENDING ACT ANALYSIS

APPLICATION: The TILA applies because the transaction involves the extension of credit to a consumer for personal, family or household purposes that is subject to a finance charge and/or payable by written agreement in more than four installments. 15 U.S.C. §§ 1601-1666j.

Pass	Fail			
X		Notice of Right to Cancel (2 copies per borrower; filled out completely). 12 C.F.R. § 226.23(b).		
X		TIL Disclosure Statement provided. 12 C.F.R. §§ 226.17, 226.18.		
X		Payment Schedule correctly identified on TIL. 12 C.F.R. §§ 226.18(g), (h).		
	X	Interest rate consistent and properly disclosed: Loan app-GFE-Commitment-TIL; variable rate. 12 CFR § 226.17-18. MISSING GFE AND COMMITMENT		
	X	Delivered good faith estimates of disclosures (preliminary TILDS) within 3 days of loan application. 12 C.F.R. §§ 226.19(a). NO EVIDENCE IN FILE		
NA		"Consumer Handbook on Adjustable Rate Mortgages" (CHARM) provided within 3 days of application. [Or equivalent disclosure - see 12 CFR § 226.19(b)].		
NA		Interest-only payment feature adequately disclosed. 15 U.S.C. §§ 1638, 12 C.F.R. § 226.17-18.		
NA		Negative-amortization payment feature adequately disclosed. 15 U.S.C. §§ 1638, 12 C.F.R. § 226.17-18.		
X		Itemization of amount financed. 12 C.F.R. § 226.18(c).[RESPA-GFE may be substituted]		
	X	Property/Hazard Insurance disclosure provided (choice by consumer). 12 C.F.R. § 226.4(d)(2). NO EVIDENCE IN FILE		
N/A		Prepayment Penalty disclosed. 12 C.F.R. § 226.18(k).		
		APR Calculation See Note 1 below for further discussion.	1^{ST} Lien Result Disclosed:5.75% vs. Actual: 6.301% Difference = <. .551% >	2^{ND} Lien Result Disclosed: vs. Actual: Difference = <. >
		Finance Charge Calculation See Note 2 below for further discussion.	1^{ST} Lien Result Disclosed: $200,000 vs. Actual: $192,609.24 Difference = <$ 7,390.76>	2^{ND} Lien Result Disclosed: vs. Actual: Difference = <$>
	X	All disclosures accurately reflect the legal obligation between the parties; 15 U.S.C. §§ 1638, 12 C.F.R. § 226.17(c).		

Total Potential TILA Violations: 4

FURTHER RECOMMENDATIONS: None at this time.

POTENTIAL REMEDIES FOR VIOLATIONS: Where a material disclosure was not given or inaccurate (APR, finance charge, amount financed, payment schedule, or total of payments), or consumer was not provided with proper notice of right to cancel, the right of rescission is extended to 3 years.

Statutory (up to $2000) and actual damages, as well as attorney's fees, may also be available for the violations noted.

TILA NOTATIONS

Under the Truth in Lending Act ("TILA"), rescission rights arise when: (1) the transaction is a consumer credit transaction; (2) in which a non-purchase lien or security interest is or will be placed; and (3) on the consumer's principal dwelling. In a rescindable transaction, each consumer must be given a copy of the TILA disclosure statement with all "material" information correctly disclosed and notice of a three-day right to rescind. If these material disclosures are not properly provided, the three-day right to rescind is extended until one of the following events occurs: (1) all materials disclosures are correctly given and a new three day notice of cancellation, (2) the expiration of three years after consummation of the transaction; (3) the transfer of all of the consumer's interest in the property; or (4) the sale of the property. All persons entitled to rescind under TILA must receive two copies of the rescission notice rights and one copy of the material disclosures at or before closing. The notice of rescission must provide the following information: (1) the retention or the acquisition of a security interest in the consumer's principal dwelling; (2) the consumer's right to rescind; (3) how to exercise the right to rescind with a form for that purpose, designating the address of the creditor's place of business; (4) the effects of rescission; and (5) the date the rescission period expires.

1. Annual Percentage Rate Tolerances and Right of Rescission

An APR deviation is a material violation permitting the right of rescission **if**: (a) it was a refinance, (b) within 3 years of the transaction, and (c) outside the tolerances set forth below.

12 CFR § 226.22(a)(2) provides: "As a general rule, the annual percentage rate shall be considered accurate **if** it is not more than 1/8 of 1 (.125%) percentage point above or below the annual percentage rate determined in accordance with paragraph (a)(1) of this section." Under 12 CFR 226.22(a)(3): "In an irregular transaction, the annual percentage rate shall be considered accurate if it is not more than 1/4 of 1 (.25%) percentage point above or below the annual percentage rate determined in accordance with paragraph (a)(1) of this section."

2. Finance Charge Tolerances and Right of Rescission

12 CFR § 226.18(d) requires the disclosure of the finance charge amount. For purposes of "mortgage loans," 12 CFR § 226.18(d)(1) provides: "In a transaction secured by real property or a dwelling, the disclosed finance charge and other disclosures affected by the disclosed finance charge (including the amount financed and the annual percentage rate) shall be treated as accurate if the amount disclosed as the finance charge: (i) is understated by no more than $100; or (ii) is greater than the amount required to be disclosed." Statutory and actual damages are available for this violation.

A finance charge deviation is a material violation permitting the right of rescission **if**: (a) it was a refinance, (b) within 3 years of the transaction, and (c) outside the tolerances set forth below.

12 CFR § 226.23(g) provides: "Tolerances for accuracy.--(1) One-half of 1 percent tolerance. Except as provided in paragraphs (g)(2) and (h)(2) of this section, the finance charge and other disclosures affected by the finance charge (such as the amount financed and the annual percentage rate) shall be considered accurate for purposes of this section if the disclosed finance charge: (i) is understated by no more than ½ of 1 percent of the face amount of the note or $100, whichever is greater; or (ii) is greater than the amount required to be disclosed. (2) One percent tolerance. In a refinancing of a residential mortgage transaction with a new creditor (other than a transaction covered by § 226.32), if there is no new advance and no consolidation of existing loans, the finance charge and other disclosures affected by the finance charge (such as the amount financed and the annual percentage rate) shall be considered accurate for purposes of this section if the disclosed finance charge: (i) is understated by no more than 1 percent of the face amount of the note or $100, whichever is greater; or (ii) is greater than the amount required to be disclosed."

15 U.S.C. §1635(i) also provides: "Rescission Rights In Foreclosure.--(2) Tolerance For Disclosures.--Notwithstanding section 106(f), and subject to the time period provided in subsection (f), for the purposes of exercising any rescission rights after the initiation of any judicial or non judicial foreclosure process on the principal dwelling of the obligor securing an extension of credit, the disclosure of the finance charge and other disclosures affected by any finance charge shall be treated as being accurate for purposes of this section if the amount disclosed as the finance charge does not vary from the actual finance charge by more than $35 or is greater than the amount required to be disclosed under this title."

HOEPA ANALYSIS

APPLICATION: Neither statute like applies as the estimated APR [~xx] would not exceed 8% over the comparable yield on Treasury securities [~10], nor do the "total points and fees" exceed 8% or 6%, respectively, of the loan amount. **Discussion: N/A**

REAL ESTATE SETTLEMENT PROCEDURES ACT ANALYSIS

APPLICATION: The RESPA applies because lender regularly extends federally related mortgage loans aggregating more than $1 million per year, and intended for the purchase of a one- to four-family residential property. 12 U.S.C. §§ 2601-2617.

Pass	Fail	
X		Informed borrower of intention to transfer the servicing of the loan and/or failed to inform the borrower of the actual transfer within fifteen (15) days before the effective date of the transfer. 24 C.F.R. § 3500.21.
X		Did not require deposit of funds in escrow in excess of the statutorily permitted amounts. 24 C.F.R. § 3500.17.
NA		Purchase Money: Provided the Special Information Booklet explaining the settlement costs within three (3) business days after consumer submitted loan application. 24 C.F.R. § 3500.6.
	X	No fees charged for preparation of the settlement statement, escrow account statement, and/or the TILA disclosure statement. 24 C.F.R. § 3500.12. $240.00
X		Disclosed all affiliated business arrangements. 24 C.F.R. § 3500.15.
X		Did not give, provide or receive a hidden fee or thing of value for the referral of settlement business, including but not limited to, kickbacks, hidden referral fees, and/or yield spread premiums. 24 C.F.R. § 3500.14.
	X	Properly and timely paid for property taxes, insurance and other charges for which Defendants are collecting within an escrow impound account; or other servicing violations. 24 C.F.R. § 3500.17. NO EVIDENCE IN FILE
X		HUD-1 provided at closing (or 1 day before if requested) and accurate. 24 C.F.R. § 3500.8(b).
X		No fees charged in excess of the reasonable value of goods provided and/or services rendered.
NA		Purchase Money: Seller did not impose use of particular service provider. 24 C.F.R. § 3500.16.

Total Potential RESPA Violations: 2

FURTHER RECOMMENDATIONS: QWR/discovery re mortgage servicing for potential servicing violations or breach of contract.

POTENTIAL REMEDIES FOR VIOLATIONS: Actual damages, statutory (up to $1000 if show pattern and practice), and treble damages for excessive portion of fees (below), plus attorney's fees and costs for violations noted.

The following are **suspect or excessive closing costs/fees** that may be actionable for treble damages pursuant to 12 U.S.C. §2607:

PREDATORY LOAN INDICATORS

"Predatory lending" is a general term used to describe unfair, deceptive, or fraudulent practices of lenders during the loan origination process. Predatory lending is often a combination of several factors that can only be evaluated in the context of the overall lending transaction. Typically, no single factor can be relied upon to consider it a predatory loan.

A large number of agencies and consumer organizations recognize predatory lending, including, for example, the Department of Housing and Urban Development, Federal Deposit Insurance Corporation, National Consumer Law Center, Pennsylvania Department of Real Estate, Fannie Mae, National Association of Consumer Advocates, Association of Community Organizations for Reform Now, National Home Equity Mortgage Association, and Center for Responsible Lending.

The predatory lending factors present in the subject transaction were found to be as follows:

Pass	Fail	
TBD		Solicitation for refinance.
N/A		Mortgage broker and corresponding lender involved.
TBD		Borrower was a minority and/or the transaction was conducted in a foreign language.
TBD		Loan-to-value ratio above 80%. MISSING APPRAISAL
	X	Debt-to-income ratio above 28/36%. STATED
NA		Teaser rate involved.
X		Interest rate on 1st was more than 2 points above: 6.08% (2.77 margin) [average US 5/1 ARM rate] or 6.4% [average 30-year fixed]. (*source*: Freddie Mac 1/2003-12/2006)
TBD		Excessive Closing Costs/Fees.
X		Prepayment Penalty.
NA		Interest-Only Payments.
NA		Negative Amortization Payments.
TBD		Broker Compensation >2% (including yield spread premium).
TBD		Loan Flipping – refinance within 3 years of previous loan.
NA		Balloon Payments.
TBD		Unsecured Debt Shifted to Secured (i.e., credit cards).
NA		Unnecessary insurance and other products offered in closing.
X		Mandatory arbitration clause in Note.
TBD		Bait & Switch – e.g., borrower initially offered lower rate than final Note.
	X	Other unfair, deceptive, or fraudulent practices in transaction.

Total Predatory Indicators: 2

PREDATORY LOAN ANALYSIS

Predatory Lending

The terms “abusive lending” or “predatory lending” are most frequently defined by reference to a variety of lending practices. Although it is generally necessary to consider the totality of the circumstances to assess whether a loan is predatory, ***a fundamental characteristic of predatory lending is the aggressive marketing of credit to prospective borrowers who simply cannot afford the credit on the terms being offered.***

While such disregard of basic principles of loan underwriting lies at the heart of predatory lending, a variety of other practices may also accompany the marketing of such credit.
Some Predatory Lending practices found in this loan:

Targeting
Targeting inappropriate or excessively expensive credit products to older borrowers, to persons who are not financially sophisticated or who may be otherwise vulnerable to abusive practices, and to persons who could qualify for mainstream credit products and terms.

Loan Flipping & Equity Stripping
Repeated refinancing of borrowers into loans that have no tangible benefit to the borrower. Can be the same lender or different ones. Loans and refinances whereby equity is removed from the home through repeated refinances, consolidation of short term debt into long term debt, negative amortization or interest only loans whereby payments are not reducing principle, high fees and interest rates. Eventually, borrower cannot refinance due to lack of equity.

High Debt Ratios
This is the practice of approving loans with high debt ratios, usually 50% or more, without determining the true ability of the borrower to repay the loan. Can often be seen with Prime borrowers approved through the Automated Underwriting Systems.

High Loan to Value loans

Loans offered to a borrower having little or no equity in the home. Usually adjustable rate mortgages that the borrower will not be able to refinance out of when the rate adjusts due to lack of equity.

Stated or No Income/No Assets

Is based on a loan application that is inappropriate for the borrower. For instance, the use of a stated-income loan application from an employed individual who has or can obtain pay stubs, W-2 forms and tax returns.

Lack of Due Diligence in Underwriting

Is underwritten without due diligence by the party originating the loan. No realistic means test for determining the ability to repay the loan. Lack of documentation of income or assets, job verification. Usually with Stated Income or No documentation loans, but can apply to full documentation loans.

Inappropriate Loan Programs

Is materially more expensive in terms of fees, charges and/or interest rates than alternative financing for which the borrower qualifies. Can include prime borrowers who are placed into subprime loans, negative or interest only loans. Loan terms whereby the borrower can never realistically repay the loan.

POTENTIAL ADDITIONAL CLAIMS ANALYSIS

(Probability of Violations Ratings: No Evidence or Possible)

Note: Federal laws may preempt certain state claims.

Equal Credit Opportunity Act (discrimination) – ***Possible***

The Equal Credit Opportunity Act provides at Sec. 202.1 – Authority, scope and purpose:

> (b) Purpose. The purpose of this regulation is to promote the availability of credit to all creditworthy applicants without regard to race, color, religion, national origin, sex, marital status, or age (provided the applicant has the capacity to contract); to the fact that all or part of the applicant's income derives from a public assistance program; or to the fact that the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The regulation prohibits creditor practices that discriminate on the basis of any of these factors. The regulation also requires creditors to notify applicants of action taken on their applications; to report credit history in the names of both spouses on an account; to retain records of credit applications; to collect information about the applicant's race and other personal characteristics in applications for certain dwelling-related loans; and to provide applicants with copies of appraisal reports used in connection with credit transactions.

Additionally, at Sec. 202.4 – General Rule Prohibiting Discrimination:

> 1. Scope of section. The general rule stated in Sec. 202.4 covers all dealings, without exception, between an applicant and a creditor, whether or not addressed by other provisions of the regulation. Other sections of the regulation identify specific practices that the Board has decided are impermissible because they could result in credit discrimination on a basis prohibited by the act. The general rule covers, for example, application procedures, criteria used to evaluate creditworthiness, administration of accounts, and treatment of delinquent or slow accounts. Thus, whether or not specifically prohibited elsewhere in the regulation, a credit practice that treats applicants differently on a prohibited basis violates the law because it violates the general rule. Disparate treatment on a prohibited basis is illegal whether or not it results from a conscious intent to discriminate. Disparate treatment would be found, for example, where a creditor requires a minority applicant to provide greater documentation to obtain a loan than a similarly situated nonminority applicant. Disparate treatment also would be found where a creditor waives or relaxes credit standards for a nonminority applicant but not for a similarly situated minority applicant. Treating applicants differently on a prohibited basis is unlawful if the creditor lacks a legitimate nondiscriminatory reason for its action, or if the asserted reason is found to be a pretext for discrimination.

DISCUSSION: No direct evidence of discrimination, but lender may be less than favorable than those offered to non-minorities: recommend investigation into borrowers credit, income etc.

Fraud – ***Possible***

Deceit is defined in Civ. Code §§1709 and 1710, and fraud is defined in Civ. Code §§1572 (actual fraud) and 1573 (constructive fraud). Liability for actual fraud under Civ. Code §1572 is limited to acts committed by or with the connivance of a party to a contract with the intent to deceive another party to the contract and induce that party to enter into the contract.[2]

DISCUSSION: It appears the lender approved the loan based on STATED income and no assets verification. The lender has a fiduciary responsibility to the borrower to perform their due diligence before extending credit. However, the lender did NOT perform their due diligence by confirming the borrower's ability to make his monthly payments over the lifetime of the loan. Recommend investigation into the loan programs presented to the borrower from the beginning of the transaction.

Fraud in the factum

Fraud in the Factum is a type of fraud where misrepresentation causes one to enter a transaction without accurately realizing the risks, duties, or obligations incurred. Black's Law Dictionary (2nd Pocket ed. 2001 pg. 293). This can be when the maker or drawer of a negotiable instrument, such as a promissory note or check, is induced to sign the instrument without a reasonable opportunity to learn of its fraudulent character or essential terms. Determination of whether an act constitutes fraud in the factum depends

[2] *See also*, the traditional elements of fraud are frequently more difficult to establish than a deception claim under an Unfair Deceptive Acts and Practices (UDAP) statute. However, in some instances fraud causes of action can be used quite effectively. *People Trust & Saving Bank v. Humphrey*, 451 N.E. 2d 1104 (Ind. Ct. App. 1983). In this case, the consumers went to their own bank for a home construction loan. The bank promised them a "good loan" at a 9.5% rate. That was merely the initial rate. The permanent financing was actually a variable rate loan and included a clause that allowed the bank to demand full payment at their discretion. The court held that "when parties to a contract have prior understanding about the contract terms, and the party responsible for drafting the contract includes contrary terms and then allows the other party to sign it without informing him of the changes, the drafter's conduct is fraudulent." The court in Humphrey dismissed the lender's foreclosure, reformed the contract by deleting the demand and variable rate clauses, and awarded $1000 actual and $40,000 punitive damages.; *Greene v. Gibraltar Mortgage Investment Corp*, 488 F. Supp. 177 (D.D.C. 1980), 839 F.2d 680 (D.C. Cir. 1980). This was another misrepresentation case. The court found the failure to disclose an unconscionably high broker fee and the lender's charging of interest on that fee to be a misrepresentation. The lender also falsely represented the loan amount and claimed to offer a market interest rate. Accordingly, the court voided the promissory note and deed of trust and permanently enjoined foreclosure proceedings; *Mahaffe v. Investors National Security*, 747 P.2d 890 (Nev. 1987).
This case involved a common home improvement fraud. The borrowers were promised home insulation which would cut fuel consumption in half, the borrower's home would be used for promotional purposes, and the total cost would be $5300. work was begun before the 3 day cooling off period, but never completed; what was done was done improperly. The contractors induced the borrowers to sign a completion certificate despite the incomplete work by threatening them with "skyrocketing interest rates" and "troubles." The assignee tried to foreclose but the Nevada Supreme Court found the contract to be null and void because of the fraudulent inducement and failure of consideration on the contractor's part; *First Charter National Bank v. Ross*, 29 Conn. App. 667, 617 A.2d 909 (1992). fraud may also be available as a defense when a borrower is tricked by a family member into signing mortgage documents. In this case a wife was allowed to assert fraud as a special defense to foreclosure action when her husband had given her loan documents to sign with the signature page on top, had discouraged her from looking at the documents, and had told her that the documents had nothing to do with their home. The court ruled that the defense of fraud was not barred by the general rule that a person has a duty to read what they sign and that notice of the content of signed documents is imputed. The court said the official rule does not apply when there is fraud and only applies if nothing is said to mislead the person signing. It should be noted, however, that some courts have refused to invalidate a mortgage when the fraud was committed by a party other than the lender and the lender was not involved in or aware of the fraud. *Family First Fed. Sav. Bank v. De Vincentis*, 284 N.J. Super. 503, 665 A.2d 1119 (1995).

upon consideration of “all relevant factors.” Fraud in the factum usually voids the instrument under state law and is a real defense against even an holder in due course.

<u>Other State/Common Law Claims-</u> ***<u>Possible</u>***

<u>Breach of Contract</u>

Need to evaluate entire mortgage-servicing history for breach of contract – QWR RECOMMENDATION.

[Statute of Limitations of 4 years, CCP §337 – may be subject to equitable tolling.]

<u>Breach of Implied Covenant of Good Faith and Fair Dealing</u>

The law provides that in every contract, there is an implied duty of good faith and fair dealing between the parties. This implied covenant imposes the requirement “that neither party will do anything, which will injure the right of the other to receive the benefits of the agreement.”

<u>Breach of Fiduciary Duty</u>

In certain situations, courts have implicitly recognized imposing fiduciary duties on lenders based on policy grounds. For instance, a lender may be considered a fiduciary when it “takes control” of the borrower, or when “moral, social, personal, or domestic” relationships are shown to exist between the parties. (Cases cited in American Bar Association – Business Tort Litigation (2d Ed.) Further, when the lender undertakes to perform a task on behalf of the borrower, then it is likely that the lender has made itself a fiduciary for the borrower, based on the law of agency.

Often times, when a loan officer or mortgage broker is helping to arrange a loan for a borrower, that loan officer/mortgage broker is, in reality, acting as the agent for both the lender and borrower.

The fiduciary duty of the lender is a responsibility to perform their own diligence to determine if a customer is being placed in a loan that is legal, properly disclosed, is the best loan for the consumer given their financial circumstance and affordable over the life of the loan if present financial positions hold steady**. If the <u>lender knew or should have known that the Borrower has a likelihood of defaulting on this loan, he/she has a fiduciary duty to the borrower to not place them in that loan (in harm’s way).</u>**

When a loan transaction occurs, any missteps in the loan transaction process can lead to dire consequences for the borrower. It is for this reason that the law should impose more liberally a fiduciary relationship between borrower and lender, especially in the residential home loan marketplace where the average borrower is not as sophisticated as the lender. If fiduciary relationships were more liberally imposed, we would likely see lenders implementing more safeguards before underwriting a loan.

If the lender is aware that the borrowers would be better off with another type of loan that the lender offers, they have violated their duty to the consumers and such act of deception would be likely be considered fraud on the consumer and predatory.

►Brokers owe a fiduciary duty to borrowers.

►Liability potential for lender may exist if borrower can prove either that: (1) a "special relationship or circumstance" existed, (2) the lender "directly ordered, authorized or participated in" the broker's tortious conduct, or (3) that broker acted as lender's agent for the transaction.

DISCUSSION: Summary of Underwriting Decision by Auditor

Examiner has reviewed the approval process of this loan. I find that the underwriting process was flawed in that it did not take into consideration the likelihood of inflated income on the loan application. No consideration of the ability of the borrower to repay this loan with a realistic means test has been made. This is especially true when the adjustment of the interest rate is taken into consideration. The borrowers signed a 4506-T Income Tax Disclosure form and an IRS form8821. These forms allow the lender to check the income of the borrowers. Failure to do so was a lack of due diligence on the part of the lender regarding underwriting standards and the ability to repay the loan, suggestive that they knew the income was overstated and if it came back as being overstated, the lender would have to declined the loan. (Other areas of applicability regarding the 4506-T could be considered breach of the lenders contractual duty to conduct the transaction in good faith and through fair dealing; gross negligence, or breach of fiduciary duty as a licensed professional under their lending license if applicable.)

Unjust Enrichment

Unjust enrichment is a general equitable principle that no person should be allowed to profit at another's expense without making restitution for the reasonable value of any property, services, or other benefits that have been unfairly received and retained. The elements to prove this claim are threefold. First, the plaintiff must have provided the defendant with something of value while expecting compensation in return. Second, the defendant must have acknowledged, accepted, and benefited from whatever the plaintiff provided. Third, the plaintiff must show that it would be inequitable or unconscionable for the defendant to enjoy the benefit of the plaintiff's actions without paying for it

Unconscionability

The court has the power to refuse to enforce a contract or a clause in a contract that is unconscionable when made.

The common law contract defense of unconscionability could be applied to stop a foreclosure when either the mortgage terms are unreasonably favorable to the lender or certain aspects of the transaction render it unconscionable.[3]

[3] *In re Maxwell*, 281 B.R. 101 (Bankr. D. Mass. 2002); *Hager v. American Gen. Fin. Inc.*, 37 F.Supp. 2d 778 (1999). For example, a Connecticut court found a second mortgage contract to be unconscionable based on the facts that:

Civil Conspiracy

A civil conspiracy or collusion is an agreement between two or more parties to deprive a third party of legal rights or deceive a third party to obtain an illegal objective.

Unfair/Deceptive Practice – Business & Professions Code §17200, §17500

Business & Professions Code §17200 provides:

> *… unfair competition shall mean and include any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by Chapter 1 (commencing with Section 17500) of Part 3 of Division 7 of the Business and Professions Code.*

Violations of other statutes and laws also violate §17200. (See *McKell v. Washington Mut., Inc.* (2006) 142 Cal.App.4th 1457).

[Statute of Limitations of 4 years, B&P §17208 – may be subject to equitable tolling.]

OTHER CLAIMS & RECOMMENDED LEGAL RESEARCH

Note: Federal laws may preempt certain state claims.

Fair Debt Collection Practices Act (Fed. & State)

The FDCPA, 15 U.S.C. § 1692 et seq., a United States statute added in 1978 as Title VIII of the Consumer Credit Protection Act, broadly defines a debt collector as “any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another.” The Act prohibits certain types of "abusive and deceptive" conduct when attempting to collect debts.

- The defendant had limited knowledge of English, was uneducated and did not read very well;
- The defendant’s financial situation made it apparent she could not reasonably expect to repay the mortgage;
- At the closing, the defendant was not represented by an attorney and was rushed by plaintiff’s attorney to sign the loan document;
- The defendant was not informed until the last minute that, as a condition of credit, she was required to pay one year’s interest in advance and there was an absence of meaningful choice on the part of the defendant; and
- In addition, the court found that the contract was substantively unconscionable, because it contained a large balloon payment that the borrower had no means of paying, and that the borrower had no reasonable opportunity to understand the terms of the contract. *FamilyFin. Servc. V. Pencer*, 677 A.2d 479, (Conn. Ct. App. 1996); and *Emigrant Mortg., Co., Inc., v. D’Angostino*, 896 A.2d 814 (Conn. App. Ct. 2006).

Case Law

In *Saxon vs. Hillery*, CA, Dec 2008, Contra Costa County Superior Court, an action by Saxon to foreclose on a property by lawsuit was dismissed due to lack of legal standing. This was because the Note and the Deed of Trust were "owned" by separate entities. The Court ruled that when the Note and Deed of Trust were separated, the enforceability of the Note was negated until rejoined. This can be an effective defense in foreclosure actions.

If the mortgage (or the deed of trust) is not a legally enforceable instrument then there can be no valid foreclosure. *In re Hudson*, 642 S.E. 2d 485 (N.C. Ct. App. 2007). A deed or mortgage that is forged is presumptively invalid. *Ex Parte Floyd*, 796 So. 2d 303 (Ala. 2001). As a result, forgery of a mortgage is generally an absolute defense to foreclosure. Similarly, where a deed has been forged and the new title holder then encumbers the property, courts have held both the deed and the mortgages are null. *Flagstar v. Gibbons*, 367 Ark. 225 (2006).

The validity of security instruments in some community property states may require both spouses to execute instruments encumbering a homestead. For example, under Wisconsin law, a court found that a mortgage on a married couple's homestead that was not signed by both spouses was void as to both spouses, regardless of their respective ownership interests. *In re Larson*, 346 B.R. 486 (Bankr. E.D. Wis. 2006). The failure to follow the formal requisites in acknowledging deeds and mortgages may also result in a void instrument. Many deed and mortgage fraud cases involve situations in which the person whom the notary certified as having appeared did not, in fact, appear.

In re Fisher, 320 B.R. 52 (E.D. Pa. 2005). In fraudulent mortgage cases, borrowers are often instructed to sign a stack of documents that are then taken elsewhere for notarization. *Goldone Credit Corp. v. Hardy*, 503 So. 2d 1227 (Ala. Civ. App. 1987). Alternatively, improper notarization may result from the taking of an actual acknowledgment from an imposter, incompetent person, or over the telephone. Regardless, of the reason for the defective acknowledgment, practitioners should investigate whether such defects may render the instrument invalid.

UCC Provisions

UCC 3-309. ENFORCEMENT OF LOST, DESTROYED, OR STOLEN INSTRUMENT. 9. ENFORCEMENT OF LOST, DESTROYED, OR STOLEN INSTRUMENT.

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

(b) A person seeking enforcement of an instrument under subsection (a) must prove the terms of the instrument and the person's right to enforce the instrument.

§ 3-301. PERSON ENTITLED TO ENFORCE INSTRUMENT.

"Person entitled to enforce" an instrument means (i) the holder of the instrument, (ii) a non-holder in possession of the instrument who has the rights of a holder, or (iii) a person not in possession of the instrument who is entitled to enforce the instrument pursuant to Section 3-309 or 3-418(d). A person may be a person entitled to enforce the instrument even though the person is not the owner of the instrument or is in wrongful possession of the instrument.

2. HOLDER IN DUE COURSE.

(a) Subject to subsection (c) and Section 3-106(d), "holder in due course" means the holder of an instrument if:

(2) the holder took the instrument (i) for value, (ii) in good faith, (iii) without notice that the instrument is overdue or has been dishonored or that there is an uncured default with respect to payment of another instrument issued as part of the same series, (iv) without notice that the instrument contains an unauthorized signature or has been altered, (v) without notice of any claim to the instrument described in Section 3-306, and (vi) without notice that any party has a defense or claim in recoupment described in Section 3-305(a).

§ 3-305. DEFENSES AND CLAIMS OF RECOUPMENT.

(a) Except as otherwise provided in this section, the right to enforce the obligation of a party to pay an instrument is subject to the following:

(1) a defense of the obligor based on (i) infancy of the obligor to the extent it is a defense to a simple contract, (ii) duress, lack of legal capacity, or illegality of the transaction which, under other law, nullifies the obligation of the obligor, (iii) fraud that induced the obligor to sign the instrument with neither knowledge nor reasonable opportunity to learn of its character or its essential terms, or (iv) discharge of the obligor in insolvency proceedings;

(c) Except as stated in subsection (d), in an action to enforce the obligation of a party to pay the instrument, the obligor may not assert against the person entitled to enforce the instrument a defense, claim in recoupment, or claim to the instrument (Section 3-306) of another person, but the other person's claim to the instrument may be asserted by the obligor if the other person is joined in the action and personally asserts the claim against the person entitled to enforce the instrument. An obligor is not obliged to pay the instrument if the person seeking enforcement of the instrument does not have rights of a holder in due course and the obligor proves that the instrument is a lost or stolen instrument.

§ 3-305. TRANSFER OF INSTRUMENT: RIGHTS ACQUIRED BY TRANSFER

(a) Transfer of an instrument, whether or not the transfer is a negotiation, vests in the transferee any right of the transferor to enforce the instrument, including any right as a holder in due course, <u>but the transferee cannot acquire rights of a holder in due course by a transfer, directly or indirectly, from a holder in due course if the transferee engaged in fraud or illegality affecting the instrument.</u>

<u>Case Law</u>

Pacific Concrete F.C.U. V. Kauanoe, 62 Haw. 334, 614 P.2d 936 (1980),

GE Capital Hawaii, Inc. v. Yonenaka, 25 P.3d 807, 96 Hawaii 32, (Hawaii App 2001),

Fooks v. Norwich Housing Authority, 28 Conn. L. Rptr. 371, (Conn. Super.2000), and

Town of Brookfield v. Candlewood Shores Estates, Inc. 513 A.2d 1218, 201 Conn.1 (1986).

Solon v. Godbole, 163 Ill. App. 3d 845, 114 Ill. Dec. 890, 516 N. E.2d 1045 (3Dist. 1987).

Staff Mortgage. & Inv. Corp., 550 F.2d 1228 (9th Cir 1977). "Under the Uniform Commercial Code, the only notice sufficient to inform all interested parties that a security interest in instruments has been perfected is actual possession by the secured party, his agent or bailee.

§ 46.2. Proper conduct of lending and brokering in the mortgage loan business.

(a) *Advertising*. A licensee may not engage in false or misleading advertising.

(b) *Disclosures to applicant*. On a form prescribed by the Department, a licensee who takes an application shall disclose the following to the applicant:

(1) If the lender providing the loan will escrow the applicable property taxes and hazard insurance.

(2) If the licensee is a lender with the ability to directly lock-in a loan interest rate.

(3) Whether the loan contains a variable interest rate or balloon payment feature.

(4) Whether the loan includes a prepayment penalty.

(5) Whether the loan has a negative amortization feature.

(c) *Timing and issuance of disclosure form*. A licensee issuing the disclosure form required by subsection (b) shall sign and date the disclosure form and deliver or place in the mail the disclosure form within 3 business days after the application is received or prepared by the licensee.

(d) *Required redisclosures*. A licensee who has issued the disclosure form required by subsection (b) shall issue an updated disclosure form at the time the licensee knows or reasonably should know that the initial disclosure form is inaccurate.

(e) *Applicant acknowledgment and retention of disclosure form*. A licensee shall require an applicant to sign and date the disclosure form required by subsections (b) and (d) within 10 business days after delivery or mailing and retain the original executed disclosure form in the applicant's loan file.

(f) *Duplication*. A licensee broker taking an application is not required to provide the disclosure form required by subsections (b) and (d) if the lender making the loan elects to provide the required disclosure form in accordance with this section.

(g) *Evaluation of applicant ability to repay*.

(1) A licensee may not offer a loan without having reasonably determined, based on the documents and information provided under this subsection, that the applicant will have the ability to repay the loan in accordance with the loan terms and conditions by final maturity at the fully indexed rate, assuming a fully amortized repayment schedule.

(2) In performing an analysis to determine whether an applicant will have the ability to repay an offered loan, a licensee shall consider, verify and document:

(i) The income of the applicant.

(ii) The fixed expenses of the applicant.

(3) When performing the income verification required by paragraph (2), a licensee is only required to verify the income that the applicant chooses to rely upon to repay the offered loan.

(4) In performing an evaluation of an applicant's ability to repay, a licensee may consider and document supplemental information provided by the applicant in addition to income that demonstrates that the applicant has the ability to repay the offered loan, provided that the supplemental information is reasonably related to an applicant's ability to repay.

(5) A licensee may not primarily rely upon the sale or refinancing of an applicant's collateral in determining an applicant's ability to repay an offered loan.

(6) All records, worksheets and supporting documentation used in the licensee's ability to repay analysis shall be maintained in the applicant's loan file.

(7) In determining an applicant's ability to repay an offered loan under this subsection, a licensee may not ignore facts or circumstances that it knows or reasonably should know which would indicate that an applicant does not have the ability to repay the offered loan.

(8) An applicant may be presumed to have the ability to repay an offered loan if the offered loan has one of the following characteristics:

(i) Is insured by the Federal Housing Administration.

(ii) Is guaranteed by the United States Department of Veterans Affairs.

(iii) Is originated or approved for purchase by the Pennsylvania Housing Finance Agency.

(iv) Is the subject of a written finding by a United States Department of Housing and Urban Development approved counseling agency that there is a reasonable expectation that the borrower will be able to repay the offered loan.

(9) For an offered loan with a balloon payment, a licensee:

(i) May consider the sale or refinance of the applicant's collateral when evaluating an applicant's ability to make the balloon payment.

(ii) Shall base the fully amortized payment schedule on the full term the borrower chooses when calculating the amortization period for a loan containing a borrower option for an extended amortization period.

(iii) Shall consider the due date of the balloon payment and if there is a reasonable expectation the applicant will have sufficient equity in the property to make the balloon payment through a sale or refinance of the residence.

(h) *Reverse mortgages*. A licensee offering or making a reverse mortgage to an applicant is not required to comply with subsections (b), (g), (i) and (j)(3).

(i) *Material changes and ability to repay*. If there is a material change after a licensee has performed the ability to repay calculation required by subsection (g), a licensee shall immediately:

(1) Send a notice to the applicant disclosing the material change and that the material change may affect the applicant's ability to repay the offered loan, if the licensee is a broker.

(2) Perform another ability to repay analysis in accordance with subsection (g), if the licensee is a lender.

(j) *Loan transaction prohibitions*. A licensee may not:

(1) Advise or imply to an applicant that the applicant's income is not relevant to the loan transaction.

(2) Recommend or imply that an applicant default on any existing contract or financial obligation.

(3) Advise or induce an applicant to refinance an existing loan or otherwise enter into a new financial obligation without performing the ability to repay analysis required by subsection (g).

(4) Offer to the applicant a covered loan without advising the applicant that the applicant qualifies for a loan other than a covered loan, if an applicant qualifies for a loan offered by the licensee.

(5) Advise or imply that an applicant should ignore any required disclosures or suggest that a document or the execution of any document is unimportant or of no consequence.

(6) Direct, encourage, permit or otherwise be involved with the improper execution of any document, including:

(i) Requesting or allowing an applicant to sign documents that contain blank spaces where material information regarding the loan transaction is required.

(ii) Permitting the execution of documents where signatures are required to be witnessed without the witnesses being physically present.

(iii) Permitting someone other than the required signatory to execute a document unless otherwise authorized by law.

(7) Knowingly submit or permit or encourage an applicant or third party to submit, false or misleading information, or information that the licensee reasonably should know is false or misleading, to any party to a loan transaction.

(8) Improperly influence, or attempt to improperly influence:

(i) An appraiser by committing any act or omission that is intended to:

(A) Compromise the independent judgment of an appraiser.

(B) Ensure that an appraisal matches a requested or target value.

(ii) Any other entity related to the mortgage loan business, such as notaries, title companies, real estate agents, builders and sellers of properties.

(9) Obtain hazard insurance required for a loan for an applicant at loan consummation without providing the applicant with the opportunity to secure or provide evidence of the applicant's own hazard insurance.

(10) Pay compensation to or receive compensation from, contract with, or employ any person engaged in the mortgage loan business who is not licensed or otherwise exempt from licensure.

(k) *Loan funding*.

(1) A licensee lender may not refuse or fail to fund a consummated loan, other than when an applicant rescinds the loan in accordance with 12 CFR 226.15 or 226.23 (relating to the right of rescission), as applicable except as provided in paragraph (4).

(2) A licensee lender shall fund a consummated loan in a reasonable time period after consummation of the loan or in accordance with any commitment or agreement with the

applicant; provided that, if an applicant has a right of rescission under 12 CFR 226.15 or 226.23, a licensee lender is not required to fund a consummated loan in accordance with this subsection until after the applicable rescission period has ended.

(3) A licensee shall disburse loan funds to third parties in accordance with any commitment or agreement with the applicant.

(4) Any postclosing underwriting or quality control review conducted by a licensee lender after the consummation of a loan may not delay the funding of a loan or result in a failure or refusal to fund the loan in accordance with this subsection unless the applicant has committed fraud against the licensee, which may be raised as an affirmative defense in any proceeding brought by the Department based upon a violation of this subsection.

(5) Nothing in this subsection relieves or limits the liability of a licensee against a claim of a borrower based upon a licensee's refusal or failure to fund a loan based upon an allegation of consumer fraud.

(l) *Licensee responsibility to provide documents*. Upon request, a licensee shall provide to an applicant or authorized representative of an applicant, unless prohibited by Federal or State law, copies or originals of the documents associated with a loan that an applicant has paid for or signed, such as loan applications, appraisals, surveys, loan documents, disclosures and any fee agreement executed by the applicant and the licensee, to the extent the documents are in the licensee's possession.

(m) *Payoff statement or statement of mortgage reinstatement*. A licensee lender that holds or services a loan shall provide a borrower with payoff statements or statements of mortgage reinstatement, as applicable, for the borrower's loan within 7 business days of receipt of a written request by a borrower or a person authorized by the borrower.

§ 46.3. Enforcement.

(a) *Violations*. Violations of this chapter shall be violations of the Mortgage Act and CDCA, as applicable.

(b) *Interpretation of chapter*. If a loan is made in good faith in conformity with an interpretation of this chapter by the Department or the courts of this Commonwealth, a penalty for a violation of this chapter will not apply, notwithstanding that after the loan is consummated, the interpretation, rule or regulation is amended, rescinded or determined by a judicial or other authority to be invalid for any reason.

§ 48.3. Dishonest, fraudulent, illegal, unfair or unethical, or negligent or incompetent practices or conduct in the mortgage loan business.

The following paragraphs provide guidance as to what the Department will consider when reviewing licensee conduct for dishonest, fraudulent or illegal practices or conduct in any business, unfair or unethical practices or conduct in connection with the mortgage loan business and negligence or incompetence in performing any act for which a licensee is required to hold a license under the act and examples of these kinds of activities within the context of the mortgage loan business. The examples listed under each paragraph are for illustrative purposes only and do not limit or otherwise alter the Department's discretion or the applicability of the guidance contained in each paragraph to all licensees.

(1) A dishonest practice or conduct is characterized by a lack of truth, honesty or trustworthiness, or is deceptive or implies a willful perversion of the truth to deceive, cheat, or defraud.

Example A: In the process of obtaining a mortgage loan for a consumer, a mortgage originator employed by a mortgage broker discloses to the consumer in the Good Faith Estimate that the mortgage broker's fee for the transaction will be $1,000, although the mortgage originator knows that the fee will be much higher. There are no material changes to the loan prior to closing. The consumer appears at the loan closing and discovers when reviewing the HUD-1 settlement sheet that the mortgage broker's fee is $3,000.

Example B: A consumer tells a mortgage originator employed by a mortgage broker that she seeks a fixed-rate mortgage loan without a prepayment penalty that has an interest rate within a certain range. The mortgage originator knows that the consumer does not qualify for such a fixed-rate mortgage loan, but does not inform the consumer of that fact. Additionally, in all legally-required disclosures it is indicated that the consumer is getting a fixed-rate loan without a prepayment penalty. However, when the consumer arrives at the loan closing, the mortgage loan that is offered is a variable-rate loan with a prepayment penalty.

Example C: A mortgage loan correspondent designs and issues targeted loan solicitations that purposefully appear to come from Federal or State government agencies or consumers' existing lenders, or both.

(2) A fraudulent practice or conduct is characterized by deceit or trickery, an intentional perversion of the truth to induce another to part with something of value or to surrender a legal right, or an act of deceiving or misrepresenting. Fraud also includes any other definition of fraud under applicable law.

Example A: A mortgage originator employed by a mortgage broker has promised a certain low-rate mortgage loan to a consumer. However, the consumer does not have the minimum debt-to-income ratio set by the lender preferred by the mortgage originator's employer to qualify for the lowest-rate mortgage loan offered. Therefore, the mortgage originator changes the W-2 statement of the consumer to reflect a higher income for the consumer without the consumer's knowledge, and then submits the documentation to the lender.

Example B: An employee of a mortgage lender contacts a real estate appraiser with a request to perform an appraisal and informs the appraiser that the sale price of the property is $150,000. The employee knows that the property will not appraise for that amount, but promises the appraiser future business if the appraiser ‘‘can make the deal work.’’ The mortgage loan is closed by the mortgage lender based upon the appraisal report showing the value of the property as $150,000.

Example C: A consumer seeks a particular mortgage loan from a mortgage broker but does not have sufficient income or assets to obtain the specified product offered by one of the mortgage broker’s lenders. After the mortgage broker explains the problem to the consumer, the consumer tells the mortgage broker he forgot to mention previously that he makes double his previously-stated income based upon a side business. The consumer later provides documentation to the mortgage broker regarding the additional income. The mortgage broker, although suspicious of the sudden change in the consumer’s circumstances, does not question the consumer on the additional income and submits a loan application including the additional income to the lender. The mortgage loan is closed by the lender and the lender later discovers that the purported additional income never existed.

(3) An illegal practice or conduct is characterized as not according to or authorized by law.

Example A: A mortgage broker fails to provide a consumer with a good faith estimate within 3 business days of receiving the consumer’s mortgage loan application as required by the Real Estate Settlement Procedures Act of 1974 (12 U.S.C.A. § § 2601—2617) in a situation where the lender has not rejected the application within 3 days.

Example B: A mortgage loan correspondent fails to implement a plan to safeguard confidential consumer information as required by the Gramm-Leach-Bliley Act and the Federal Trade Commission’s Privacy and Safeguards Rules.

Example C: A mortgage lender advertises an interest rate without conspicuously disclosing the annual percentage rate and identifying the qualification terms, as required by the Truth-in-Lending Act (15 U.S.C.A. § § 1601—1667f).

(4) An unfair practice or conduct is characterized as being marked by injustice, partiality or deception or being inequitable in business dealings. An unethical practice or conduct is characterized as not conforming with the moral norms or standards followed in the mortgage loan business or profession.

Example A: A consumer tells a mortgage originator employed by a mortgage broker that he seeks a $30,000 fixed-rate home equity loan on a house that the consumer has advised the mortgage originator he intends to remain in permanently. Although the mortgage originator’s employer is able to provide the requested loan, the mortgage originator ‘‘steers’’ the consumer to variable-rate products with balloon payment features for which the mortgage originator’s employer, and thus the mortgage originator, will receive higher compensation than with a traditional fixed-rate home equity loan.

Example B: A lender has an agreement with a mortgage broker to provide qualified consumers a certain interest rate. The mortgage broker then tells a consumer who qualifies for the certain interest rate that the interest rate is locked in with the lender; however, the consumer was not asked by the mortgage broker or lender to sign a lock-in agreement with the lender. The lender later informs the mortgage broker that the lender is not going to honor the agreement between the mortgage broker and the lender to provide certain interest rates. Therefore, the mortgage broker is unable to offer the consumer a mortgage loan with the promised interest rate and the consumer has no written lock-in agreement to enforce against the lender.

Example C: A mortgage lender enters into a lock-in agreement with a consumer. During the lock-in period, interest rates rise. The mortgage lender decides to delay closing until the lock-in agreement with the consumer expires, thus causing the consumer to lose his locked-in interest rate and forcing the consumer to accept a mortgage loan with a higher interest rate.

(5) Negligence in performing any act for which the licensee is required to hold a license under the act is characterized by the definition of negligence as used by the courts of this Commonwealth. Incompetence in performing any act for which the licensee is required to hold a license under the act is characterized as inadequate or unsuitable for a particular purpose, or lacking the qualities needed for effective action.

Example A: A mortgage originator employed by a mortgage lender takes mortgage loan applications from consumers on behalf of the licensee, but then leaves the company. The mortgage lender fails to follow up on the former employee's application files. A consumer assumes that his mortgage loan is being processed by the mortgage lender until he contacts the mortgage lender as the closing date on his home purchase approaches. The mortgage lender realizes the error but is unable to provide the applied-for mortgage loan in time for the closing date.

Example B: A mortgage broker routinely fails to timely forward information received from consumers that was requested by the lenders and which is necessary to meet lenders' underwriting criteria. As closing approaches, the lenders receive the consumers' information and determine that the consumers do not qualify for the loans promised by the mortgage broker, thereby causing the consumers to delay closings or obtain different loans, or both.

Example C: A mortgage lender consistently fails to file mortgage satisfaction pieces, thereby repeatedly causing consumers to have to send notices to satisfy to the mortgage lender to get the mortgage lender to issue mortgage satisfaction pieces regarding the consumers' paid-off mortgage loan obligations