

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

CASE NO. 01-21920

PENNY R. NUNN,

Debtors.

DECISION & ORDER

PENNY R. NUNN,

Plaintiffs,

v.

AP #01-2104

IMC MORTGAGE COMPANY,

Defendants.

BACKGROUND

On May 17, 2001, Penny R. Nunn (the "Debtor") filed a petition initiating a Chapter 13 case. On the Schedules and Statements required to be filed by Section 521 and Rule 1007, the Debtor indicated that: (1) IMC Mortgage Company ("IMC") held a September 28, 1998 mortgage on her residence at 82 Catherine Street, Hornell, New York (the "IMC Mortgage"); (2) the IMC Mortgage had an outstanding balance of \$26,534.91; (3) in January 2001, IMC commenced a mortgage foreclosure action; (4) her total unsecured debt was \$1,169.55; (5) her monthly gross income as a librarian was \$548.75; and (6) she would commence an action to have the Court permit her to rescind the IMC Mortgage

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because the transaction had violated various Federal and New York State statutes.

On June 26, 2001, the Debtor, by her attorneys, Southern Tier Legal Services, commenced an Adversary Proceeding against IMC. The Complaint in the Adversary Proceeding alleged that: (1) the IMC Mortgage loan transaction (the "Loan Transaction") violated various Federal and New York State statutes, which should result in the Court entering an Order: (a) rescinding or canceling the IMC Mortgage; (b) canceling all finance charges due on the IMC Mortgage; and (c) requiring the refund of all finance charges previously paid; (2) the IMC Mortgage was a covered loan under the Home Ownership and Equity Protection Act, 15 U.S.C. § 1639 ("HOEPA"), as the total points and fees exceeded eight percent (8%) of the amount financed; (3) IMC had failed to provide the Debtor with the three-business-day notice required by HOEPA Section 1639(a)(1) (the "HOEPA Notice"); and (4) both the direct mortgage broker fee of \$1,437.50, paid by the Debtor at the time the IMC Mortgage loan was entered into, as well as an indirect mortgage broker fee of \$750.00 paid by IMC (the "Indirect Fee"), should be included in the eight percent (8%) points and fees trigger.

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In its Answer and at a pretrial conference conducted by the Court, IMC asserted that the Loan Transaction was not covered by HOEPA because the Indirect Fee was not required to be included in the eight percent (8%) points and fees trigger.

On February 25, 2002, the Debtor filed a Motion for Partial Summary Judgment and a Brief (collectively, the "Motion for Summary Judgment") in connection with its HOEPA cause of action only, which asserted that: (1) if the Indirect Fee was required to be included for purposes of HOEPA Section 1602(aa)(1)(B),¹ total points and fees exceeded eight percent (8%) of the total

¹ HOEPA Section 1602(aa)(1) provides that:

A mortgage referred to in this subsection means a consumer credit transaction that is secured by the consumer's principal dwelling, other than a residential mortgage transaction, a reverse mortgage transaction, or a transaction under an open end credit plan, if -

(A) the annual percentage rate at consummation of the transaction will exceed by more than 10 percentage points the yield on Treasury securities having comparable periods of maturity on the fifteenth day of the month immediately preceding the month in which the application for the extension of credit is received by the creditor; or

(B) the total points and fees payable by the consumer at or before closing will exceed the greater of -

- (i) 8 percent of the total loan amount; or
- (ii) \$400.

15 U.S.C. § 1602(aa)(1) (2002).

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loan amount, making the Loan Transaction a covered loan; (2) if the Loan Transaction was a covered loan, IMC was required to give the Debtor the HOEPA Notice, which it failed to do; (3) even though the Indirect Fee was paid to the broker by IMC, it should be found to have been payable by the Debtor because: (a) on August 10, 1998, prior to the September 28, 1998 IMC Mortgage closing, the Debtor executed a Mortgage Loan Origination Agreement with the mortgage broker (the "Origination Agreement"), under which she agreed to finance a portion of the broker's compensation by agreeing to pay a higher interest rate on the loan to be obtained by the broker than would otherwise be available;² (4) a Borrower's Broker Fee Affidavit (the "Fee Affidavit"), executed by the Debtor at the IMC Mortgage closing, indicated in part that, "To the extent the Broker Compensation was paid by the lender, we may be indirectly paying that portion of the Broker Compensation through a higher interest rate on our loan"; (5) even though the Loan Transaction was a covered

² The Origination Agreement read in part that:

"You understand that you have a choice of paying more of our compensation 'Broker Compensation' at closing and receiving a lower interest rate on your loan, or of financing all or a portion of the Broker Compensation by way of a higher interest rate on your loan, allowing the lender to pay to us all or a portion of the Broker Compensation."

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transaction because the total points and fees exceeded eight percent (8%), IMC failed to give the HOEPA Notice which must: (a) be in conspicuous type-size; (b) set forth the basic terms of the loan; (c) advise the borrower that there is no obligation to proceed with the loan; and (d) advise the borrower that if the borrower proceeds with the loan and defaults, the borrower could lose their home; (6) because of IMC's failure to give the HOEPA Notice, a material disclosure, the Debtor was permitted by law to rescind the Loan Transaction within three years; and (7) within the three-year period a June 15, 2001 rescission notice was mailed on behalf of the Debtor to IMC Mortgage and on June 26, 2001 this Adversary Proceeding seeking rescission was commenced.

On March 15, 2002, IMC interposed a Brief (the "IMC Brief") in Opposition to the Motion for Summary Judgment, which asserted that even though 12 CFR Section 226.32³ provided that all

³ Section 226.32 Requirements for certain closed-end home mortgages, provides, in part, that:

(a) Coverage.

(1) Except as provided in paragraph (a)(2) of this section, the requirements of this section apply to a consumer credit transaction that is secured by the consumer's principal dwelling, and in which...

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compensation paid to mortgage brokers is to be included in the eight percent (8%) total points and fees trigger:⁴ (1) it still must be compensation payable by the consumer; and (2) the Federal Reserve System Board of Governors Official Staff Commentary to the Section has clarified that the only broker fees to be included in the eight percent trigger are those paid directly by the consumer.

DISCUSSION

(ii) The total points and fees payable by the consumer at or before loan closing will exceed the greater of 8 percent of the total loan amount, or \$400;...

(b) Definitions. For purposes of this subpart, the following definitions apply.

(1) For purposes of paragraph (a)(1)(ii) of this section, points and fees mean:

(ii) All compensation paid to mortgage brokers[.]

12 CFR § 226.32 (2002).

⁴ "Commentary section 226.32(b)(1)(ii) - 1. Mortgage broker fees. In determining 'points and fees' for purposes of this section, compensation paid by a consumer to a mortgage broker (directly or through the creditor for delivery to the broker) is included in the calculation whether or not the amount is disclosed as a finance charge. **Mortgage broker fees that are not paid by the consumer are not included. Broker fees already included in the calculation as finance charges under Sec. 226.32(b)(1)(i) need not be counted again under Sec. 226.32(b)(1)(ii).** [Comp. At paragraph 1942.] [Federal Reserve Board Comment 32(b)(1)(ii) - 1, as added effective April 1, 1996, compliance mandatory October 1, 1996; 61 F.R. 14952.] [Emphasis added]"

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Neither party has been able to provide the Court with a published or unpublished decision where a Court has addressed the issue of whether an indirect broker fee paid by the mortgagee in a transaction similar to the Loan Transaction must be included in the eight percent (8%) points and fees trigger, and, it is not as clear to this Court, as it apparently is to IMC, that: (1) the Official Staff Commentary set forth at footnote 4, above; or (2) Section 6.09(b)(II) of the Truth in Lending treatise of Rohner and Miller,⁵ which it filed with the Court on March 21, 2002, make it clear that such an indirect fee is not included.

⁵ The Truth in Lending treatise states, in part, that:

[ii] Mortgage broker compensation. For purposes of the "eight percent test," compensation paid to mortgage brokers is limited to all amounts paid by the consumer to a mortgage broker and would include amounts paid in cash to the broker, as well as those that are financed by the creditor and paid out of the loan proceeds. Amounts paid to a mortgage broker by a secondary market source should not be included in calculating mortgage broker compensation. Thus, a service release fee, a yield spread premium, or other fees that are commonly paid to brokers in table-funded mortgage loan transactions should be excluded from this calculation. Fees paid to a broker who acts as the creditor in originating the loan would also be excluded. Broker fees already included in the finance charge under Regulation Z section 226.32(b)(1)(i) need not be counted again under Regulation Z section 226.32(b)(1)(ii).

Ralph J. Rohner & Fred H. Miller, Truth in Lending § 6.09(2)(b)(ii) (Robert A. Cook et al. eds. (2000)).

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I find that for purposes of HOEPA Section 1602(aa)(1)(B)(i) the Indirect Fee was not required to be included in the eight percent (8%) points and fees trigger, for the following reasons:

(1) although it is clear that the Debtor agreed in the Origination Agreement to indirectly pay any indirect broker fee through a higher interest rate loan, the applicable HOEPA section does not say total points and fees "paid" by the consumer, or directly or indirectly paid, as it could have, rather, it says "payable" by the consumer; (2) the Debtor entered into the Origination Agreement with the mortgage broker prior to: (a) the broker negotiating for any particular mortgage on behalf of the Debtor, including the IMC Mortgage; and (b) any broker fee being earned and payable by the Debtor; (3) once the Debtor entered into the Origination Agreement, which provided that she would pay part of the broker fee directly and the balance would be paid by the mortgagee because she had agreed to a higher interest rate loan and authorized and directed the mortgage broker to only negotiate and obtain such a higher interest rate interest loan where an indirect mortgage broker fee would be paid by the mortgagee, the Debtor was never then or ultimately contractually liable to pay the entire mortgage broker fee, and, therefore, the portion of the broker fee paid

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by IMC was never "payable" by the Debtor; (4) the payment of the Indirect Fee was always fully disclosed to the Debtor, both before and at the time of the IMC Mortgage closing, by the: (a) Origination Agreement; (b) HUD-1 closing statement, prepared, delivered to and signed by the Debtor at the IMC Mortgage closing, where she was represented by counsel; and (c) Fee Affidavit, executed by the Debtor when she was represented by counsel, who notarized the affidavit; (5) rescission of the IMC Mortgage and cancellation of the finance charges is an extraordinary remedy, which, although available under HOEPA, should not be enforced unless the facts, circumstances and evidence presented clearly warrant such a drastic remedy; and (6) in this case, where all of the parties were aware of the Indirect Fee, which was fully disclosed and directed to be paid by the Debtor who was represented by counsel, and was never "payable" by the Debtor, the extraordinary remedy of rescission does not appear warranted.

CONCLUSION

The Motion for Summary Judgment is, in all respects, denied, and the Debtor's HOEPA cause of action is dismissed. This Adversary Proceeding shall be recalled on the Court's June 19,

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2002 Trial Calendar, unless the matter is appealed by the Debtor, in which case the Court will enter an appropriate Order when any appeals have become final.

IT IS SO ORDERED.

HON. JOHN C. NINFO, II
CHIEF U.S. BANKRUPTCY JUDGE

Dated: May 9, 2002