

STATE OF MINNESOTA

DISTRICT COURT

COUNTY OF ANOKA

TENTH JUDICIAL DISTRICT

Sandra L. Gustafson,

Case File No. 02-CV-09-682

Case Type: Civil, Quiet Title

Plaintiff,

vs.

**PLAINTIFF'S MEMORANDUM IN
SUPPORT OF PARTIAL SUMMARY
JUDGMENT REGARDING COUNT XI**

Brian J. Smith,
Midwest Equity Consultants, Inc.,
Bradley R. Pederson,
Amy L. Pederson,
Lake Elmo Bank
Defendants.

INTRODUCTION

This motion for partial summary judgment is to void the lien on Ms. Gustafson's home based upon a loan between Lake Elmo Bank and equity strippers, Bradley Pederson and Amy Pederson. As found by this Court on August 25, 2009, the lien was filed in direct violation of Minnesota's anti-equity stripping laws. The Court further voided the underlying contracts between the equity strippers and Ms. Gustafson. Therefore, Defendants Bradley Pederson and Amy Pederson have no property interest to offer as collateral for their loan from Lake Elmo Bank, and the voiding of the Lake Elmo Bank-Pederson security interest is the logical next step to unwinding this illegal transaction. Lake Elmo Bank should not and does not have the right to foreclose on Ms. Gustafson and evict her from her home of seventeen years, based upon a security interest that she did not sign and that is rooted in a voided transaction.

IDENTIFICATION OF DOCUMENTS

Plaintiff relies on the following documents in support of her motion for summary judgment:

1. Order and Memorandum of Law in Support of Order regarding the above-captioned matter. Second Bowman Affidavit (“Bowman Affidavit”), ¶ 2, Exhibit A.
2. Plaintiff Gustafson also incorporates by reference the factual basis for her motion for Partial Summary Judgment filed on April 28, 2009. Specifically, the Affidavit of Jane N. Bowman dated April 28, 2009.

RECITAL OF UNDISPUTED FACTS

The facts in this case are similar to a typical equity-stripping scheme, and, for the purposes of this motion, the facts are not in dispute. This Court has already identified and outlined the undisputed facts in its Order, dated August 25, 2009. Bowman Affidavit ¶ 2, Ex A. Specifically, this Court held that in the spring of 2007, Plaintiff Gustafson became delinquent on her monthly mortgage payments. Bowman Aff. ¶ 2, Ex A at p. 3. A sheriff’s sale occurred in August 2007, and the property was sold for approximately \$90,156. *Id.* During the time that Ms. Gustafson was delinquent on her payments, she became acquainted with Defendant Brian J. Smith (“Smith”) and Defendant Midwest Equity Consultants (“MWE”) who informed her that they could help her regain ownership of her home. *Id.* On September 6, 2007, Ms. Gustafson, Smith (an employee of MWE) and MWE entered into a “consulting contract” whereby Smith and MWE would assess Ms. Gustafson’s equity position, find a suitable investor to purchase her property, resell it to Ms. Gustafson on a contract for deed, and arrange for the closing. *Id.*

Defendants Smith arranged for Bradley and Amy Pederson to purchase the home and lease it back to Plaintiff on a contract for deed. *Id.* The Contract for Deed was signed by the

Pedersons and Ms. Gustafson on September 6, 2007. *Id.* The transaction included the following terms: Ms. Gustafson sold her property to Defendants Pederson for \$140,000, \$90,156 of the sale proceeds redeemed the property from the sheriff's sale; \$24,956 of the proceeds were placed into an escrow account for future monthly payments on the contract for deed (\$1,664.33 per month for 15 months for interest, taxes, insurance only at 12.5%); \$11,000 of the proceeds went to Defendant MWE for fees and services; \$7,722.73 of the proceeds were to be placed in a separate escrow for purposes of repairing Ms. Gustafson's credit; \$5,305 of the sale proceeds went to covering closing costs; the remaining \$850 went to Ms. Gustafson. *Id.* At the end of the contract for deed, Ms. Gustafson was responsible for paying off the remaining balance of \$140,000. *Id.*

Also on September 6, 2007, Defendants Pederson mortgaged the subject property with Lake Elmo Bank at 8.25% financing. *Id.* After receiving monthly payment from the Plaintiff and after making their mortgage payment to Lake Elmo Bank, the Pedersons kept the difference, earning a monthly profit of approximately \$500.00. *Id.*

On August 25, 2009, this Court granted Plaintiff's motion for partial summary judgment.

The Court held that:

- a. The property was illegally encumbered, meaning that the lien between Lake Elmo Bank and the Pedersons was recorded with Anoka County, on September 6, 2007. This Court held that "[s]uch an encumbrance clearly violates §325N.17(f)." *Id.*
- b. There was no separate written contract between Ms. Gustafson and Mr. and Mrs. Pederson outlining the entire agreement as required under Minn. Stat. § 325N.11. Bowman Aff. ¶ 2, Ex A at p. 6.

- c. The contract for deed does not include a notice of cancellation, nor any statement informing Ms. Gustafson that she had five (5) days to cancel the contract in violation of Minn. Stat. § 325N.13-14. *Id.*
- d. The contract for deed does not state when the fair market value of the home would be assessed in violation of Minn. Stat. § 325N.17(b)(2)(ii). *Id.*
- e. As it relates to Defendants Smith and Midwest Equity, the record shows that Smith and Midwest Equity violated Minnesota's Foreclosure Consultant Statute, §§ 325N.01-09, by collecting compensation before completing all promised services; inducing Plaintiff to enter into a contract in violation of state law; and by retaining funds for purposes of restoring Plaintiff's credit and failing to repair as promised. *Id.* at 8.

LEGAL ARGUMENT

I. THIS COURT SHOULD VOID THE SECURITY INTEREST BETWEEN LAKE ELMO BANK AND THE EQUITY STRIPPERS RELATED TO MS. PEDERSON'S HOME.

Ms. Gustafson's motion for partial summary judgment to void the security interest in her home is appropriate, since the lien was filed in direct violation of Minnesota's anti-equity stripping laws and enforcing the lien is against public policy since the underlying transaction was voided by this Court. Summary judgment is appropriate where there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. MINN. R. CIV. P. 56.03 (2008). See *Hinricks v. Farmers Co-op. Grain & Seed Ass'n*, 333 N.W.2d 639 (Minn. 1983). A material fact that will preclude issuance of a summary judgment is one that "will affect the result or outcome of the case depending on its resolution." *Zappa v. Fahey*, 245 N.W.2d 258, 259-60 (Minn. 1976).

A party moving for summary judgment has the burden of showing that there are no genuine issues as to any material facts; “the nonmoving party has the benefit of that view of the evidence which is most favorable to him.” *Sauter v. Sauter*, 70 N.W.2d 351, 353 (Minn. 1955). Where affidavits are submitted in support of a motion for summary judgment, the nonmoving party cannot simply rely on general statements in a complaint; the “adverse party must present specific facts showing a genuine issue for trial. . .” *Ahlm v. Rooney*, 143 N.W.2d 65, 68 (Minn. 1966).

Here, the Plaintiff is entitled to a summary judgment motion. As set forth in more detail below, this motion should be granted for two reasons. First, the lien was illegally recorded and is a direct result of an illegal transaction that is contrary to the public interest. Second, the underlying transaction is void, meaning that Mr. and Mrs. Pederson have no interest in Ms. Gustafson’s property to provide as collateral for the loan.

A. The Security Interest Is Void Because It Was Granted In Violation Of State Law And Against Public Policy

The lien on Ms. Gustafson’s property was recorded in violation of Minnesota law and should be declared void. Minnesota Courts have long recognized that in order to hold a valid security interest on property, the security interest transaction must comport with state law. *See Missouri, Kansas & Texas Trust Co. v. Krumseig*, 172 U.S. 351, 355 (U.S. 1899). In other words, if the underlying transaction is illegal or the security interest is recorded against a property in violation of the law, then that security interest is void. *Id.* Similarly, courts have long held that if a contract is void because it offends public policy, it is unenforceable. *See Perkins v. Hegg*, 212 Minn. 377, 3 N.W.2d 671 (1942). In this case, the security interest between the

Pedersons and Lake Elmo Bank is void for both reasons. The security interest or lien was recorded in direct violation of Minnesota statute, and the underlying transaction itself was illegal.

1. The Security Interest Is Void Because It Was Illegally Recorded Against Ms. Gustafson's Home.

In the Plaintiff's motion filed on April 28, 2009, the Plaintiff moved for partial summary judgment related to Defendants Smith, Midwest Equity, and the Pedersons. This Court granted Plaintiff's motion. Specifically, the Court held that Defendants Smith, Midwest Equity, and the Pedersons violated Minnesota's Anti-Equity Stripping laws. More importantly for this motion, however, was that this Court held that Defendants Pederson had also violated Minnesota's ban on transferring or encumbering the property in foreclosure before the time has elapsed during which the homeowner could cancel the transaction.

Minnesota law, in part, states:

A foreclosure purchaser shall not . . . do any of the following until the time during which the foreclosed homeowner may cancel the transaction has fully elapsed: . . .
(3) transfer or encumber or purport to transfer or encumber any interest in the residence in foreclosure to any third party. . .

Minn. Stat. 325N(f)(3) (2007)(emphasis added).

After taking the record into consideration, this Court found the Defendants Pederson had encumbered the property, by attaching a mortgage or lien on the property, in violation of Minn. Stat. 325N(f)(3) (2007). Specifically, this Court held:

Having reviewed the record, the Court finds that the parties executed a series of documents on September 6, 2007, including a contract for deed, a consulting contract, warranty deed, a mortgage from Bradley and Amy Pederson to Lake Elmo Bank and the corresponding promissory note. The record does not contain any separate written contract between Plaintiff and Defendants Pederson outlining the entire agreement of the parties as required under §325N.11. The contract doe feed does not include a notice of cancellation, nor any statement informing Plaintiff that she has five (5) days to cancel the contract. The contract for deed

does not state when the fair market value of the home would be assessed¹. **Finally, the record clearly establishes that the Pedersons encumbered the subject property on September 6, 2007, when they executed a mortgage and promissory note with Lake Elmo Bank. Such an encumbrance clearly violates §325N.17(f).**

Bowman Aff. ¶ 2, Ex A at 6. (emphasis added).

The legal rule -- if a security interest placed on property violates state law, then it is void -- is long-standing. *See Missouri, Kansas & Texas Trust Co. v. Krumseig*, 172 U.S. 351, 355 (U.S. 1899) (voiding a mortgage because it violated usury laws). Similarly, at the federal level, if a mortgage violates the Truth In Lending Act, the borrower has the option to rescind the mortgage loan, which cancels the note and extinguishes the security interest. *See* 15 U.S.C. §§ 1601, *et seq.*

Here, the Defendants Pederson and Lake Elmo Bank recorded a security interest on the property in violation of Minnesota's equity stripping laws. Since the security interest was placed on the property in direct violation of state law, it is void.

2. The Security Interest Is Unenforceable Because It Violates Public Policy

The contracts and documents that were executed in violation of Minnesota law and in furtherance of the equity scheme are unenforceable as against public policy. Courts retain an inherent right to hold contracts or other agreements unenforceable if they violate public policy and an established societal interest. *See Perkins v. Hegg*, 212 Minn. 377, 3 N.W.2d 671 (1942) (holding that contracts, the subject, operation, or tendency of which violates public policy or the established interest of society, are not enforceable); *See also Independent School Dist v. Loberg Plumbing & Heating Co.*, 266 Minn. 426, 123 N.W.2d 793 (1963) (holding that if a contract

¹ These are references to other statutory violations the Court found the Defendants Pederson to have violated in the foreclosure reconveyance transaction.

transgresses the law or contravenes public policy, it is void); *Equitable Holding Co. v. Equitable Bldg. & Loan Ass'n*, 202 Minn. 529 (Minn. 1938) (holding that since the building contract did not violate public policy, it was enforceable).

Furthermore, courts have held that a contract will not be enforced, if it is incidentally or indirectly connected with an illegal transaction. See *Brubaker v. Hi-Banks Resort Corp*, 415 N.W.2d 680 (Minn. Ct. App. 1987) (holding that because a contract was neither illegally made nor involved illegal action in its performance was enforceable). In other words, if the party seeking enforcement requires the aid of an illegal transaction to make out his case, the contract is unenforceable. *Id.*

In this case, there is little question that enforcing the various agreements executed by Defendants are contrary to public policy. Indeed, in the Court's previous ruling, the Court identified the various documents that enabled the equity stripping scheme to occur. These documents included the contract for deed, warranty deed, consulting contract, as well as the mortgage loan and note between the Pedersons and Lake Elmo Bank. All of the documents identified by the Court are dependent upon one another to have any affect. The Court voided the Contract for Deed transaction as against public policy, and now Plaintiffs' simply ask the Court to continue to unwind the transaction and void the security interest between the equity strippers and Lake Elmo Bank. It does not make any sense to allow Lake Elmo Bank to foreclose and evict Ms. Gustafson, based upon a contract rooted and based on other voided agreements. Since Defendant Lake Elmo Bank's mortgage on the property directly stems from an illegal contract, this Court should similarly unwind the security interest in the same manner it unwound the contract for deed.

B. The Security Interest Is Void Because The Pedersons Did Not Have Any Legal Interest To Convey

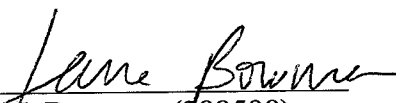
The security interest, or mortgage lien, filed against Ms. Gustafson's home is void because Defendants Pederson did not have any interest in the property to mortgage. A person cannot convey a greater interest than what they legally own. *In re Estate of Van Den Boom*, 590 N.W.2d 350, 353 (Minn. Ct. App. 1999)(holding that "one can only convey what one has"); *Bank Midwest v. Lipetzky*, 674 N.W.2d 176 (Minn. 2004)(holding that the mortgage was invalid as against bank because bank had constructive knowledge the mortgagors did not have legal right to mortgage the property).

Since the transaction giving the Defendants the right to encumber the property was voided, the Defendants Pederson had no interest in the property to offer as collateral for a mortgage loan. Since a property owner cannot convey a greater interest than what that property owner has, Defendant Lake Elmo Bank's lien is invalid. As a result, this Court should void the Pederson-Lake Elmo Bank security interest.

CONCLUSION

For the above-mentioned reasons, the Plaintiff respectfully requests this Court grant her Motion for Partial Summary Judgment.

Dated: Nov. 11, 2009

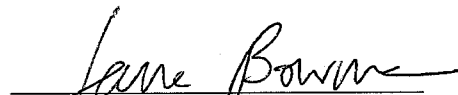

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ACKNOWLEDGMENT

The undersigned hereby acknowledges that costs, disbursements, and reasonable attorney and witness fees may be awarded, pursuant to Minn. Stat. § 549.21, subd. 2, to the party against whom the allegations in this motion are asserted.

Dated: Nov. 10, 2009



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