Given this obvious difference between the two cases, one questions CHA's decision to include *Talley*. CHA may have cited *Talley* because the Seventh Circuit rejected the pro se plaintiff's FHA claim, concluding that "being unlawfully discriminated against on the basis of his criminal record had no arguable basis in the laws cited by the applicant," including the FHA.[40] Advocates, however, should not mistake the appellate court's language as commentary on the viability of using the FHA to challenge criminal records screening policies. The plaintiff in *Talley* sought to bring a claim of discrimination on the basis of disability, not race. He failed to tie his arrests and convictions to a disability.[41] *Talley*'s relevance to future race-based disparate impact claims under the FHA, therefore, is likely limited.

Ultimately, the appellate court accepted Mr. Landers' testimony that he did not engage in criminal activity for two reasons. First, the dismissal of all of his criminal charges corroborated his claim that his arrests arose from his homelessness rather than any criminal activity. Second, CHA offered no evidence to rebut his testimony, meaning that it could not satisfy a preponderance of the evidence standard.[42] Without any evidence of criminal activity, therefore, the court found that CHA wrongly denied admission to Mr. Landers because he did not pose a threat to the health, safety and welfare of the public housing community.[43]

Conclusion

Although the appellate court did not address the fair housing arguments, the *Landers* opinion offers important building blocks for advocates who bring these challenges in the future. Arrests, the court held, cannot be used unless they are verifiable and substantiated.[44] The court recognized that arrests alone are not a reliable indicator of criminal activity and noted the limited, permissible use of arrest information in criminal proceedings, such as for impeachment and in sentencing hearings.[45] The *Landers* opinion will be especially helpful in FHA litigation to show that relying on arrests in the absence of convictions does nothing to further a PHA's interest in promoting safety in public housing. The *Landers* court, in essence, called for a narrowly tailored policy that actually examines—rather than simply presumes—whether arrests prove past criminal activity. Once PHAs like CHA answer this call, only then will they achieve their goal of safer public housing communities. ■

[40] *Talley*, 13 F.3d at 1034-35.
[41] *Id.* at 1034.
[42] *Landers*, 2010 WL 3718028, at *4-*5.
[43] *Id.* at *7.
[44] *Id.* at *4.
[45] *Id.* at *6-7.

Advocates Secure Victory for Minnesota Homeowner in Equity Stripping Case*

In *Gustafson v. Smith*, a Minnesota court awarded a homeowner title to her home free and clear of a mortgage after almost two years of litigation challenging an equity stripping scheme.[1] Plaintiff Sandra Gustafson was at risk of losing her home to foreclosure after a job loss. Recognizing that Ms. Gustafson's home had over $125,000 of equity in it, a now-defunct company called Midwest Equity Consultants, Inc. promised to "save her home" and "repair her credit." Ms. Gustafson ultimately became the victim of an elaborate equity stripping scheme and was an eviction notice away from losing her home and her equity. Fortunately, Ms. Gustafson sought assistance from the Foreclosure Relief Law Project, which quickly recognized the scheme for what it was—a real estate transaction set up to strip the plaintiff of her equity while appearing to "save" the home.

Although victory in *Gustafson* was primarily rooted in state statutory violations, the legal theories used in the case can be applied in any jurisdiction. This article describes the Foreclosure Relief Law Project's legal strategy and the theory that ultimately won the case at trial.

Equity Stripping 101

Equity stripping schemes target homeowners who have substantial equity in their properties, but who are at risk of losing their entire properties to foreclosure. The homeowner signs over ownership rights to an investor with a subsequent reconveyance of a lesser property interest back to the homeowner and a promise that the homeowner can fully repurchase her property at a later date.

Typically, a homeowner at risk of losing her home is approached by a "foreclosure consultant" who promises to help her save her home and repair her credit. The foreclosure consultant convinces the homeowner to sell her property to an investor. The sale of the property to the investor results in a large portion of the homeowner's liquidated equity being deposited into an "escrow" account. The money in this escrow account is set aside to make payments to the investors on behalf of the homeowner

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[1] Gustafson v. Smith, No. 02-CV-09-682, was litigated in Anoka County District Court. Attorneys Jane N. Bowman and Mark R. Ireland represented Ms. Gustafson.

pursuant to the terms of the homeowner's new contract with the investor. Once this account is drained, the homeowner is to find her own financing, repay the investor the purchase price of property, and live happily ever after.

More often than not, the homeowner is unable to secure traditional financing and defaults on her contract with the investor. Since the investor is the title holder of the property, the investor simply cancels the contract with the homeowner and serves her with eviction papers. Once the eviction is complete, the investor now owns a property for a significantly reduced price and has collected monthly payments from the now-evicted homeowner for the past year or two.

To make matters worse, the foreclosure consultants who put these deals together stand only to gain. These consultants typically charge hefty fees from closing as a result of their "services," and at no time have their names or credit on the line.

The Facts in *Gustafson*

As is typical in an equity stripping scheme, Ms. Gustafson, who had owned her property for almost 20 years, was in foreclosure as the result of a recent job loss. Since she had been in the property for so long, she had a significant amount of equity in it. Her property was worth about $215,000, while she owed only $81,000 on the mortgage.

After receiving a flyer in the mail from a company called Midwest Equity Consultants, Inc. (MWE), Ms. Gustafson contacted MWE for assistance as it promised to "save her home," and "repair her credit." MWE promised to find an investor that would purchase Ms. Gustafson's home and simultaneously sell it back to her on a contract for deed.

As promised, investors were found and in September 2007, Ms. Gustafson signed a quitclaim deed assigning title to her property to the investors. Ms. Gustafson sold her property to the investors for $140,000: $90,156 of the sale proceeds redeemed the property from the sheriff's sale, $25,000 was placed in a separate escrow account for future monthly payments on the contract for deed, $11,000 went to MWE for "services," $7,722 was to be placed in another escrow for the purpose of repairing Ms. Gustafson's credit, $5,305 was for closing costs, and the remaining $850 went to Ms. Gustafson.

At the same time, the parties signed a contract for deed whereby Ms. Gustafson would make monthly payments of $1,664 for 15 months. At the end of the 15 months, Ms. Gustafson would be responsible for finding her own financing to repurchase the property for its previous $140,000 sale price to the investors.

To purchase the property, the investors obtained financing from a local bank. The terms of the investors' mortgage with the local bank were $140,000 for 15 months at 8.5% interest, meaning that with each monthly payment, the investors would take in about $1,664 and pay the bank about $1,075 per month, keeping the difference.

After the transaction, MWE failed to assist with any credit repair, despite retaining $7,722 to do so. In addition, at the end of the 15 months—after Ms. Gustafson's separate $25,000 escrow to make the monthly payments was drained—she was in no better position to obtain financing of $140,000 on her own. As discovery would later indicate, the investors were contemplating an eviction action.

Using Minnesota's Laws Combating Equity Stripping

Assisting a homeowner by purchasing her property, and then subsequently reconveying a lesser interest back, is *not* illegal in Minnesota. Indeed, the procedures for conducting this type of transaction are outlined in Minnesota Statutes Section 325N.[2] However, thanks to laws combating equity stripping that were updated in 2007, those who legally complete these transactions will not make much money.[3] This abides by the public policy reason for permitting such transactions: Minnesota wants to allow people to assist homeowners in times of need while prohibiting those same people from exploiting financially vulnerable homeowners.

The rest of this article describes the step-by-step strategy the Foreclosure Relief Law Project used in Ms. Gustafson's case.

Step 1: Declare the Transaction Void

Without a clear roadmap from previous cases, the Foreclosure Relief Law Project litigated Ms. Gustafson's case bit by bit, rather than asking the court to void the transaction and award the house to Ms. Gustafson free and clear of a mortgage all at once—an action that the court likely would not have taken seriously. Ms. Gustafson's first motion was simply to declare that foreclosure consultants MWE and the investors violated the law when they conducted the transaction.[4]

In her motion, Ms. Gustafson identified six statutory violations that were easily affirmed by the court on a motion for summary judgment. For example, in any equity stripping deal (the statute calls it a "foreclosure reconveyance transaction"), the homeowner must receive a five-day notice of a right to cancel from the investors. Ms. Gustafson did not. Further, the law states that investors cannot convey any interest in the property during the five-day cancellation period. The investors sold the property back to Ms. Gustafson on the same day she

[2]MINN. STAT. § 325N *et seq.* (2010). Chapter 325 is Minnesota's consumer protection statute.

[3]The primary drafter of the updated laws combating equity stripping was University of Minnesota professor Prentiss Cox, with lobbying support from Legal Services Advocacy Project attorney Ron Elwood. The bill authors were State Senator Ellen Anderson and State Representative Andy Westerberg.

[4]Damages were not raised or alleged at this point.

transferred it to the investors. The court held that MWE and the investors violated various sections of Minnesota's laws against equity stripping and reserved the amount of damages for these violations for trial. The court went even further in finding that "[w]here a contract violates the law or public policy the contract is void"[5] and that it was "compelled to find this contract void as against public policy."

The investors made two arguments against Ms. Gustafson's motion. First, they argued that since she did not complete the terms of the ill-fated contract for deed, she breached the terms of the contract. The investors requested that she relinquish the property or find financing to complete the contract. Second, the investors argued that Ms. Gustafson had a fiduciary duty to the investors and that any errors in the contract should be construed against her rather than the investors. However, the court found it unnecessary to determine whether or what type of agency relationship existed between Ms. Gustafson and MWE because the consumer protection duties imposed through Minnesota's laws combating equity stripping were imposed upon purchasers, not upon the seller or any agent. Further, the court found that the burden was on the investors to comply with the statutes. With this favorable ruling, the investors were barred from raising any breach of contract counterclaim. They were also without any legal leverage to force Ms. Gustafson to make mortgage, rent or other types of payments.

Step 2: Void the Security Interest

Until this point, the financing bank—which is not held liable under Minnesota law, but nonetheless has an interest in the outcome—was fairly quiet. It was not interested in the outcome of the case, as long as it was repaid its $140,000 loan by someone. With the goal of unwinding the transaction one step at a time, Ms. Gustafson next moved to void the underlying mortgage.[6] Ms. Gustafson argued that a mortgage cannot stand when it is based upon a real estate transaction that was voided as against state statute and public policy.

Building upon its previous ruling, the court stated that since the mortgage was recorded in violation of state law (i.e. the mortgage encumbered the property before Ms. Gustafson's five-day cancellation period had expired), it was void. Furthermore, the court held that since the terms of the statute were violated, and since the statute is a consumer protection statute, the mortgage was also void because it violated public policy.

This time, the bank raised a defense: ratification. It argued that Ms. Gustafson ratified the mortgage by accepting and using the funds provided to her at closing to repurchase her home and used her equity to make 15 months of payments. Notwithstanding the absurdity of this argument—alleging that a homeowner ratifies an equity stripping transaction when she complies with the terms of the transaction *before* she realizes it is illegal—the court ruled against the lender on a different basis. Only voidable contracts may be ratified.[7] In its previous order, the Court declared the transaction void, not voidable. The court found "that [the] Plaintiff did not, and legally could not, ratify the Mortgage by her actions following the execution of the Mortgage."

Step 3: Hold the Equity Strippers Accountable

With the investors unable to enforce any contract against Ms. Gustafson, and with the financing bank unable to enforce its mortgage, the only issue remaining for trial was whether the investors and the bank had an unjust enrichment claim against Ms. Gustafson. The bank made clear that it intended to ask the court to grant it an equitable trust or other equitable legal remedy to force Ms. Gustafson to repay the bank the funds used to redeem the property.

At the bench trial,[8] Ms. Gustafson called three witnesses: herself, one investor and a representative from the bank. Ms. Gustafson walked the court through her foreclosure, the enticement by MWE to help her save her home and the real estate transaction. She also talked about her embarrassment and shame during her foreclosure, which prevented her from asking for help elsewhere.

The investor walked the court through his understanding of the transaction, which did not differ from the terms of the documents. In sum, the investor stood to gain from the transaction either way—if Ms. Gustafson could refinance, the investor took home about $600 per month for 15 months, and if Ms. Gustafson could not refinance, then the investor purchased a $215,000 property for $140,000. He could and would have evicted Ms. Gustafson, resold the property and stripped her of her equity.

A representative from the financing bank testified last. His testimony was not remarkable, but it also was not entirely common in an equity stripping transaction given that the financing bank knew exactly what was going on.[9] The bank financed the transaction—in discovery, its representative admitted to financing other similar transactions with MWE—with its eyes wide open. Introduced into evidence was an attorney's opinion drafted for MWE

[5]Citing Barna, Guzy & Steffen, Ltd. v. Beens, 541 N.W. 2d 354, 356 (Minn. Ct. App. 1995).

[6]Ms. Gustafson's briefs did not address the validity of the accompanying note signed by the investors as mortgagors and the financing bank as mortgagee.

[7]Spartz v. Rimnac, 208 N.W.2d 764, 767 (Minn. 1973) (quoting 17 Am. Jur. 2d Contracts § 7).

[8]Ms. Gustafson initially requested a jury trial, but the court determined that matters of equity did not allow for a jury trial.

[9]A defense available to mortgagees is bona fide purchaser status. If a bank can show that it reasonably did not know about the illegal and void as against public policy nature of the transaction, its mortgage and lien position could be protected. Since the bank in this instance was clearly aware of the transaction, it did not raise this defense.

explaining what a "foreclosure reconveyance transaction" was and what a "foreclosure consultant" and a "foreclosure purchaser" must do to comply with Minnesota's prohibitions on equity stripping.

At the end of an otherwise uneventful bench trial, Ms. Gustafson moved for a directed verdict based upon the legal theory that if a party has an adequate remedy at law, that party is barred from seeking a remedy in equity.[10] Since the bank still had a valid note (although the mortgage had been voided), it could recover from the investors, signors on the note. Counsel for the bank stated that since the investors could file for bankruptcy on the now-unsecured note, it was not an adequate remedy.

Almost immediately, the court ruled in favor of Ms. Gustafson, holding that there was an adequate remedy at law (i.e. the note), and the bank must use that remedy to collect on its debt. The bank therefore was barred from seeking a remedy in equity. The court was unequivocal in its ruling: Ms. Gustafson owned the property free and clear of a mortgage, and if the bank wanted to collect on its debt, it must collect from the investors.

Afterthoughts

Although the *Gustafson* decision almost certainly will be appealed, it provides a road map for attorneys nationwide who are seeking to assist homeowners who have been scammed out of their equity by "foreclosure consultants," and "investors." The decision also places the burden on those that took the risk—investors and banks that finance illegal transactions that are doomed to fail, leaving homeowners without their homes or their equity. ■

[10]Ms. Gustafson also noted several other threshold defenses, which were never addressed since the trial was decided on her motion for a directed verdict. Those defenses were: (1) a party cannot invoke equity merely because it has made a bad bargain, Cady v. Bush, 283 Minn. 105 (1969); (2) a party who seeks equity must come to court with clean hands, Hamilton v. Wood, 55 Minn. 482, 57 N.W. 208 (1893); and (3) an action for unjust enrichment does not hold if the defendants fail to provide any evidence of fraudulent or illegal acts by the plaintiff, Custom Design Studio v. Chloe Inc., 584 N.W.2d 430 (Minn. Ct. App. 1998); Schumacher v. Schumacher, 627 N.W.2d 725, 729 (2001) (quoting First Nat'l Bank of St. Paul v. Ramier, 311 N.W.2d 502, 504 (Minn. 1981); ServiceMaster of St. Cloud v. GAB Business Services, Inc., 544 N.W.2d 302, 306 (Minn. 1996).

Advocates Win Partial Summary Judgment in Tax Credit Siting Case

State housing finance agencies are responsible for approving or rejecting the location of housing built using Low-Income Housing Tax Credits (LIHTC). In Texas, and likely many other states, LIHTC housing is disproportionately located in areas with a high concentration of both poverty and people of color. Seeking redress for this practice, the Inclusive Communities Project (ICP) filed suit against the Texas Department of Housing and Community Affairs (TDHCA). On September 28, 2010, a federal court found that ICP established a prima facie case of racial discrimination against TDHCA and granted partial summary judgment in its favor.[1]

Background

ICP assists low-income families, primarily African-American, in finding housing in high-opportunity, racially integrated areas. In its initial complaint, filed on March 28, 2008, ICP alleged that TDHCA had violated the Fair Housing Act (FHA), the Equal Protection Clause of the Fourteenth Amendment, and 42 U.S.C. § 1982. ICP asserted that TDHCA (1) used race as a consideration in siting LIHTC properties; and (2) disproportionately allocated tax credits in areas primarily comprised of people of color while denying credits in predominantly Caucasian neighborhoods, thus making housing unavailable based on race, color and national origin.[2] In December 2008, ICP survived a motion to dismiss filed by TDHCA, which had alleged that the organization lacked standing and had failed to join necessary parties.[3]

Claims

In its September 2010 order, the court addressed several motions filed by both parties. ICP had moved for partial summary judgment regarding its standing to bring its claims and its establishment of a prima facie case of racial discrimination based on the discriminatory pattern of TDHCA's siting of LIHTC units. TDHCA had moved for judgment on the pleadings and summary judgment, claiming that ICP lacked standing and was not entitled to relief on the merits.

[1]Inclusive Communities Project v. Texas Dep't. of Hous. & Cmty. Affairs, 2010 WL 3766714 (N.D. Tex. Sept. 28, 2010) [hereinafter ICP II].
[2]Compl., Inclusive Communities Project v. Texas Dep't. of Hous. & Cmty. Affairs, No. 08cv0546 (N.D. Tex. Mar. 8, 2008).
[3]Inclusive Communities Project v. Texas Dep't. of Hous. & Cmty. Affairs, 2008 WL 5191935 (N.D. Tex. Dec. 11, 2008) [hereinafter ICP I]. For background information see NHLP, *Fair Housing Tax Credit Case Survives Motion to Dismiss*, 39 Hous. L. Bull. 1, 10 (Jan. 2009) and NHLP, *Texas Group Files Suit Alleging LIHTC Program Perpetuates Segregation*, 38 Hous. L. Bull 135, 146 (July 2008).