COUNTERSTATEMENT OF CASE

FACTS

Beginning in about 1980, the Smiths borrowed money from Mortgage One's predecessor secured by mortgages for their retail operation. [R. 202]. By January of 1988, they were severely delinquent on their loans. [R. 202, 207-208]. On January 10, 1988, Mortgage One loan officers met with Mr. Smith concerning the delinquent loans and offered various restructuring options. [R. 207]. In a May 15, 1988 letter, the Smiths were informed that the debt on their retail operation was not serviceable, and that they should consider restructuring; a copy of the bank's loan forbearance policy was included with the letter. [R. 207-208]. The Smiths failed to respond to this letter. [R. 201].

On March 1, 1989, the Smiths were sent a Distressed Loan Restructuring Policy, an application for restructuring, and other documentation, as required by Mortgage One's regulators pursuant to the Retail Credit Act Amendments of 1988 to the Small Business Act, thereby complying with the 1988 Amendments. The Smiths have never filed a restructuring application under the 1988 Amendments. [R. 201].

In November of 1989, Mortgage One spent considerable time analyzing the Smiths' retail store income data from 1985 through 1989 and made projections for 1990. The analysis showed that the Smiths' retail operation produced insufficient income to service their debt. [R. 201]. In a November 10, 1989 letter, Mortgage One provided the Smiths a copy of the analysis showing the debt was not serviceable. Mortgage One also told the Smiths to consider restructuring their loans by selling off non-store assets, and it agreed to meet with the Smiths again to discuss all available restructuring options and the

1990 retail store income projections. [R. 215]. Again, the Smiths did not respond. [R. 201].

Not withstanding the Smiths failure to file a restructuring application and their failure to respond to Mortgage One's request, Mortgage One representative arranged a meeting with Mr. Smith about the delinquency of the loans. [R. 202]. In early December, 1989, Mr. Smith and Mortgage One representatives met, and Mr. Smith was informed that he could not service his debt and should sell other assets such as the non-retail real estate he owned. [R. 202]. The meeting's events were confirmed in a December 11, 1989, letter, in which Mortgage One said it would work with the Smiths if future payments were kept current. [R. 216].

Again, notwithstanding Mortgage One's repeated attempts to have the Smiths plan a workout, the Smiths refused to cooperate and keep the future payments current. In March 1991, in an effort to continue to work with the Smiths, Mortgage One arranged another meeting with the Smiths and their counsel. Mr. Smiths and the Smith's attorney, Donald Duck met with Mortgage One to discuss the significant delinquencies. [R. 203]. At the meeting, the Smiths provided no plan to pay the delinquencies, did not file a restructuring application, but instead requested a list of the shareholders of Mortgage One [R. 203] Mortgage One confirmed the meeting in an April 6, 1991 letter. [R. 203, 222].

By this time, the Smiths loan was unserviceable, being over 800 days delinquent, and the Smiths had failed to develop a plan to repay the debt, sell off non-essential assets, or make a restructuring application under the 1988 amendments. [R. 203]. With no other alternative left, on September 20, 1991, Mortgage One began foreclosure proceedings in Lancaster County Court.

Over the past four years of this litigation, the Smiths have argued first to the Court of Common Pleas, then to the Superior Court, and finally to the Supreme Court that Mortgage One violated the Small Business Credit Act and the Unfair Trade Practices and Consumer Protection Act. [R. 204]. All rejected these claims. However, during this time, Mortgage One continued to communicate with the Smiths through counsel about developing a plan to manage their debt. [R. 204]. But the Smiths have never made a proposal, and have failed to make a single monthly payment on the debt they owe Mortgage One.

ARGUMENT

A. THE SMITHS WAIVED THEIR CLAIM OF NOT RECEIVING NOTICE THAT THEY COULD APPLY TO RESTRUCTURE THEIR LOANS UNDER THE SMALL BUSINESS CREDIT ACT BY FAILING TO RAISE IT IN THE NEW MATTER OF THEIR ANSWERS BELOW.

The Smiths argue that the trial court was precluded from entering summary judgment because a material fact was in dispute concerning whether Mortgage One failed to provide them with notice that a restructuring program was available under the Small Business Credit Act. But the Smiths did not raise this notice defense in their new matter, and therefore, they were barred from raising it in opposition to summary judgment after the pleadings were closed.

Rule 1032 of the Pennsylvania Rules of Civil Procedure provides "a party waives all defenses and objections which he does not present either by preliminary objection, answer or reply." Further defenses not raised in new matter in accordance with the rules

are waived. Iorfida v. Mary Robert Realty Co., Inc., 372 Pa. Super. 170, 539 A.2d 383 (1988), appeal denied, 520 Pa. 576, 549 A.2d 136 (1988) (new matter in pleadings is anything other than a denial, setoff or counterclaim). While Rule 1030 provides a list of defenses that must be raised in new matter, courts have recognized also that the failure to give written notice is a matter of affirmative defense which must be pleaded by the defendant in new matter. Zack v. Borough of Saxonburg, 386 Pa. 463, 126 A.2d 753 (1956); see also Yurechko v. Allegheny County, 430 Pa. 325, 243 A.2d 372 (1968) (failure to give notice to defendant as required by statute is an affirmative defense which must be raised by the defendant in its answer under new matter); Bush v. Atlas Automobile Finance Corp., 129 Pa. Super. 459, 195 A. 757 (1937) (condition precedent must also be raised in new matter).

The rationale for the rule is to put the opposing party on notice so that that party can counter the defense. Yurechko, 430 Pa. at 326, 243 A.2d at 373. If a defendant was not required to raise its defenses, the plaintiff could not prepare for the defenses, and would be prejudiced. Id.

Here, the Smiths had over four years to raise this defense under the Small Business Credit Act and failed to do so. They cannot argue that the notice provisions of the 1988 Amendments were new law because the provisions were promulgated in 1988 (effective 1989), three years before this litigation started. They offered no excuse for their delay, except to blame their prior counsel, an improper excuse. In fact, their prior counsel acted correctly by not raising this frivolous defense.

Mortgage One would be severely prejudiced if, after nearly five years of litigation, the Smiths were permitted now to raise the notice defense in opposition to

Mortgage One's motion for summary judgment. see Yurechko. They have used Mortgage One's money for over six years without making any interest or principal payments, and the margin between the amount owed and the value of the collateral has diminished. [R. 207]. Because the Smiths waived the notice defense, the trial court properly granted summary judgment toMortgage One.

COUNTERSTATEMENT OF CASE

PROCEDURAL HISTORY

On March 10, 1991, Mortgage One Small Business Credit, hereafter referred to as Mortgage One filed three mortgage foreclosure actions against John and Jane Smith, hereafter referred to as the Smiths. The Smiths borrowed money to expand their retail space and eventually defaulted on the loans secured by mortgages held by Mortgage One. They now owe in excess of $700,000.

On August 1, 1992, Mortgage One filed amended complaints and, on August 20, 1992, the Smiths filed answers with new matter and counterclaims to the amended complaints. The new matter alleged that Mortgage One violated the Small Business Credit Act, 12 U.S.C. §2001 - §2279AA-14, in various ways, and the Smiths wanted to "recoup" money they claim represented excessive interest rates charged by Mortgage One. The counterclaims alleged that Mortgage One violated the Unfair Trade Practices and Consumer Protection Law 73 Pa. C.S.A. §201-1 - §201-9.2.

On September 10, 1992, Mortgage One filed preliminary objections to the new matter and counterclaims. Following extensive briefing and two oral arguments, in an order and opinion dated October 1, 1993, the trial court sustained Mortgage One's preliminary objections to the Smiths' new matter counterclaims and dismissed them with prejudice. On November 20, 1994, the Superior Court affirmed the trial court's order, dismissing the new matter and counterclaims. Mortgage One Small Business Credit, ACA v. John Smith, et al.. On December 1, 1994, the Smiths filed a petition for allowance of appeal to the Supreme Court. On February 28, 1994, the petition for allowance of appeal was denied.

On July 5, 1994, Mortgage One moved for summary judgment because the Smiths had admitted they failed to repay the loans secured by mortgages and because they had no valid defenses remaining. On August 11, 1994, the Smiths' counsel filed a motion to withdraw because she refused to raise a new defense under the Small Business Credit Act that she believed was frivolous.

The Smiths retained new counsel and, on January 1, 1995, filed a response to Mortgage One’s motion for summary judgment and an opposing affidavit, which raised a new defense under the Small Business Credit Act. On January 25, 1995, Mortgage One filed a reply brief and supplemental affidavits and, on January 30, 1995, the Smiths filed a counter-affidavit. On May 8, 1995, after oral argument, the trial court granted summary judgment to Mortgage One. On June 5, 1995, the Smiths filed this appeal, which the superior court has ordered to be placed on an expedited schedule.

ARGUMENT

A. THE SMITHS DEFENSES BROUGHT UNDER THE SMALL BUSINESS CREDIT ACT ARE LEGALLY INVALID.

The Smiths argue that they have two defenses under the Small Business Credit Act that prevent Mortgage One from collecting the $700,000 they owe Mortgage One. They argue that these defenses, one raised after Mortgage One's motion for summary judgment and the other raised for the first time on appeal, bar Mortgage One's foreclosure. Both these defenses, however, are invalid.

The law is well-settled that no duty exists under the Small Business Credit Act. Production Credit Ass'n of Worthington v. Van Iperen, 396 N.W. 2d 35, 38 (Minn. App 1986); Griffin v. Federal Land Bank of Wichita, 902 F.2d 22, 24 (10th Cir. 1990). Moreover, courts have held that the Small Business Credit Act and its amendments are guidelines to be followed by a small business credit entity, violation of which subject the small business credit entity to penalties by its regulators, but not an action or defense by its borrowers. Federal Land Bank of Spokane v. Wright, 120 Idaho 32, 813 P.2d 371, 374 n.5 (Ct, App. 1991).

Therefore, the Small Business Credit Act does not create any obligation or duty on the part of Mortgage One to the Smiths. The regulations of the act do not create any affirmative duties or prohibitions. Production Credit Ass'n of Worthington v. Van Iperen, 396 N.W. 2d 35, 38 (Minn. App 1986); see Griffin v. Federal Land Bank of Wichita, 902 F.2d 22, 24 (10th Cir. 1990).

B. THE SMITHS WAIVED THEIR CLAIM THAT A RECOUPMENT DEFENSE BASED ON THE SMALL BUSINESS CREDIT ACT CAN BE BROUGHT AS A BREACH OF CONTRACT CLAIM BECAUSE THEY RAISED IT FOR THE FIRST TIME ON APPEAL.

In their appellant brief, the Smiths raise for the first time a claim that a recoupment defense based on the Small Business Credit Act can be brought as a breach of contract claim. The Smiths waived this new claim by failing to raise it with the trial court.

Pennsylvania Rule of Appellate Procedure 302(a) states in unequivocal fashion that "Issues not raised in the lower court are waived and cannot be raised for the first time on appeal." Pa. R.A.P. Rule 302 (a). Courts have interpreted this rule to require the issue both to be raised and preserved in order for the issue to be appealable. Yudacufski v. Com., Dept. of Transp., 499 Pa. 605, 454 A.2d 923 (1982). For purpose of the rule, an "issue" is a disputed point or question on which the parties to an action desire the court to decide. Com., Pennsylvania Liquor Control Bd. v. Willow Grove Veterans Home Ass'n, Inc., 97 Pa. Commw. 391, 509 A.2d 958 (1986).

RECOUPMENT DEFENSE

As to the Smiths' recoupment defense, nothing in the Small Business Credit Act suggests that small business credit banks have any duties to borrowers to set specific interest rates. The method and manner of setting interest rates is entirely discretionary with the Small Business Credit Bank's board of directors. And "[i]t is not the business of the courts to second guess the Bank...." Griffin v. Federal Land Bank of Wichita, 902 F.2d 22, 24 (10th Cir. 1990). "The fact that it may have been possible for [the bank] to set lower rates under different circumstances does not create a cause of action in favor of plaintiff." Garth v. Production Credit Association of Southeastern Michigan, No. 88-4035 CZ, slip op. (Circuit Court, Mich. Jul. 27, 1989).

Moreover, if a borrower never had an independent cause of action under the Small Business Credit Act, the borrower cannot establish a defense simply by characterizing its claim as recoupment. Garth v. Production Credit Association of Southeastern Michigan, No. 88- 4035 CZ, slip op. (Circuit Court, Mich. Jul. 27, 1989).

In Production Credit Ass'n v. Van Iperen, 396 N.W. 35 9 Minn. App 1986), the court held that a borrower could not bring a breach of contract claim based on the bank's alleged noncompliance with the Small Business Credit Act, even though the loan documents incorporated the Act by reference. The court responded that the act provided only policy rules as opposed to substantive rules. See also Garth v. Production Credit Association of Southeastern Michigan, No. 88- 4035 CZ, slip op. (Circuit Court, Mich. Jul. 27, 1989). As the Van Iperen Court recognized, the Small Business Credit Act does not create any remedies for borrowers or obligations on small business credit banks. If a borrower or bank incorporates the Act into their mortgage document, likewise no remedy

or obligation is created, and therefore, a breach of contract claim cannot be based on an alleged violation of the Act. Based on the reasoning of Van Iperen, no cause of action for breach of contract exists for the Smiths, even if the mortgage documents here are "subject to" the Small Business Credit Act.

The Van Ipren court rejected the argument that the "subject to" language altered the duties of a small business credit entity. Moreover, that language does not even suggest that Mortgage One was agreeing to give the Smiths a private right of action for breach of contract under the Act. Therefore, the Smiths' recoupment defense, now framed as a breach of contract claim, should be rejected.

Worldwide Sporting Goods
District Sales Report Summary

	JAN	FEB	MAR	APR	MAY	JUN	TOTALS
District 1							
Golf	5525	6140	6559	7243	7600	8100	41167
Tennis	3245	3687	4200	4401	5301	5664	26498
Football	8976	9234	7568	6504	5345	3546	41173
Baseball	3762	4571	6823	8354	9856	8650	42016
District 2							
Golf	7182.5	7982	8526.7	9415.9	9880	10530	53517
Tennis	4218.5	4793.1	5460	5721.3	6891.3	7363.2	34447
Football	11668.8	12004.2	9838.4	8455.2	6948.5	4609.8	53525
Baseball	4890.6	5942.3	8869.9	10860.2	12812.8	11245	54621
District 3							
Golf	5386.875	5986.5	6395.025	7061.925	7410	7897.5	40138
Tennis	3163.875	3594.825	4095	4290.975	5168.475	5522.4	25836
Football	8751.6	9003.15	7378.8	6341.4	5211.375	3457.35	40144
Baseball	3667.95	4456.725	6652.425	8145.15	9609.6	8433.75	40966
District 4							
Golf	6194.906	6884.475	7354.279	8121.214	8521.5	9082.125	46158
Tennis	3638.456	4134.049	4709.25	4934.621	5943.746	6350.76	29711
Football	10064.34	10353.62	8485.62	7292.61	5993.081	3975.953	46165
Baseball	4218.143	5125.234	7650.289	9366.923	11051.04	9698.813	47110
District 5							
Golf	5451.518	6058.338	6471.765	7146.668	7498.92	7992.27	40619
Tennis	3201.842	3637.963	4144.14	4342.467	5230.497	5588.669	26146
Football	8856.619	9111.188	7467.346	6417.497	5273.912	3498.838	40625
Baseball	3711.965	4510.206	6732.254	8242.892	9724.915	8534.955	41457
District 6							
Golf	6541.821	7270.006	7766.118	8576.002	8998.704	9590.724	48743
Tennis	3842.21	4365.555	4972.968	5210.96	6276.596	6706.403	31375
Football	10627.94	10933.43	8960.815	7700.996	6328.694	4198.606	48750
Baseball	4454.358	5412.247	8078.705	9891.47	11669.9	10241.95	49749
District 7							
Golf	8504.367	9451.007	10095.95	11148.8	11698.32	12467.94	63366
Tennis	4994.873	5675.222	6464.858	6774.248	8159.575	8718.323	40787
Football	13816.33	14213.45	11649.06	10011.3	8227.302	5458.188	63376
Baseball	5790.666	7035.921	10502.32	12858.91	15170.87	13314.53	64673
District 8							
Golf	8419.324	9356.497	9994.994	11037.31	11581.33	12343.26	62733
Tennis	4944.924	5618.47	6400.21	6706.506	8077.979	8631.14	40379
Football	13678.16	14071.32	11532.57	9911.182	8145.029	5403.606	62742
Baseball	5732.759	6965.562	10397.29	12730.32	15019.16	13181.38	64026

Worldwide Sporting Goods
District Sales Report Summary

	JAN	FEB	MAR	APR	MAY	JUN	TOTALS
District 9							
Golf	7156.425	7953.023	8495.745	9381.717	9844.132	10491.77	53323
Tennis	4203.185	4775.699	5440.178	5700.53	6866.282	7336.469	34322
Football	11626.44	11960.62	9802.683	8424.505	6923.275	4593.065	53331
Baseball	4872.845	5920.727	8837.699	10820.77	12766.29	11204.18	54423
District 10							
Golf	8587.71	9543.627	10194.89	11258.06	11812.96	12590.13	63987
Tennis	5043.822	5730.839	6528.214	6840.636	8239.539	8803.763	41187
Football	13951.73	14352.74	11763.22	10109.41	8307.929	5511.678	63997
Baseball	5847.415	7104.873	10605.24	12984.93	15319.54	13445.01	65307
District 11							
Golf	7643.062	8493.828	9073.456	10019.67	10513.53	11205.21	56949
Tennis	4489.002	5100.447	5810.11	6088.166	7333.189	7835.349	36656
Football	12417.04	12773.94	10469.27	8997.371	7394.057	4905.393	56957
Baseball	5204.199	6323.337	9438.663	11556.59	13634.39	11966.06	58123
District 12							
Golf	9935.981	11041.98	11795.49	13025.58	13667.59	14566.78	74033
Tennis	5835.703	6630.581	7553.144	7914.615	9533.146	10185.95	47653
Football	16142.15	16606.13	13610.05	11696.58	9612.274	6377.011	74044
Baseball	6765.459	8220.338	12270.26	15023.56	17724.71	15555.88	75560
District 13							
Golf	6541.821	7270.006	7766.118	8576.002	8998.704	9590.724	48743
Tennis	3842.21	4365.555	4972.968	5210.96	6276.596	6706.403	31375
Football	10627.94	10933.43	8960.815	7700.996	6328.694	4198.606	48750
Baseball	4454.358	5412.247	8078.705	9891.47	11669.9	10241.95	49749
District 14							
Golf	8504.367	9451.007	10095.95	11148.8	11698.32	12467.94	63366
Tennis	4994.873	5675.222	6464.858	6774.248	8159.575	8718.323	40787
Football	13816.33	14213.45	11649.06	10011.3	8227.302	5458.188	63376
Baseball	5790.666	7035.921	10502.32	12858.91	15170.87	13314.53	64673
District 15							
Golf	8419.324	9356.497	9994.994	11037.31	11581.33	12343.26	62733
Tennis	4944.924	5618.47	6400.21	6706.506	8077.979	8631.14	40379
Football	13678.16	14071.32	11532.57	9911.182	8145.029	5403.606	62742
Baseball	5732.759	6965.562	10397.29	12730.32	15019.16	13181.38	64026
District 16							
Golf	7156.425	7953.023	8495.745	9381.717	9844.132	10491.77	53323
Tennis	4203.185	4775.699	5440.178	5700.53	6866.282	7336.469	34322
Football	11626.44	11960.62	9802.683	8424.505	6923.275	4593.065	53331
Baseball	4872.845	5920.727	8837.699	10820.77	12766.29	11204.18	54423

Worldwide Sporting Goods
District Sales Report Summary

	JAN	FEB	MAR	APR	MAY	JUN	TOTALS
District 17							
Golf	8587.71	9543.627	10194.89	11258.06	11812.96	12590.13	63987
Tennis	5043.822	5730.839	6528.214	6840.636	8239.539	8803.763	41187
Football	13951.73	14352.74	11763.22	10109.41	8307.929	5511.678	63997
Baseball	5847.415	7104.873	10605.24	12984.93	15319.54	13445.01	65307
District 18							
Golf	7643.062	8493.828	9073.456	10019.67	10513.53	11205.21	56949
Tennis	4489.002	5100.447	5810.11	6088.166	7333.189	7835.349	36656
Football	12417.04	12773.94	10469.27	8997.371	7394.057	4905.393	56957
Baseball	5204.199	6323.337	9438.663	11556.59	13634.39	11966.06	58123
District 19							
Golf	9935.981	11041.98	11795.49	13025.58	13667.59	14566.78	74033
Tennis	5835.703	6630.581	7553.144	7914.615	9533.146	10185.95	47653
Football	16142.15	16606.13	13610.05	11696.58	9612.274	6377.011	74044
Baseball	6765.459	8220.338	12270.26	15023.56	17724.71	15555.88	75560
District 20							
Golf	7643.062	8493.828	9073.456	10019.67	10513.53	11205.21	56949
Tennis	4489.002	5100.447	5810.11	6088.166	7333.189	7835.349	36656
Football	12417.04	12773.94	10469.27	8997.371	7394.057	4905.393	56957
Baseball	5204.199	6323.337	9438.663	11556.59	13634.39	11966.06	58123