# Current Developments

# in

# Lender Liability Law

## Web Conference Series



FOLEY

FOLEY & LARDNER LLP

# Lender Liability Consumer Claims Part I

## Truth in Lending Act
## Fair Debt Collection Practices Act


Christi R. Adams

Michael C. Lueder

William J. McKenna

# Definition

- “Lender liability” defines a group of causes of action borrowers sometimes bring against their lenders. These claims include breach of contract, fraud, bad faith, duress, and tortious interference. They also include actions based on statutes such as RICO, RESPA, TILA, FDCPA, FCRA and State Unfair and Deceptive Practices Acts.

# The Truth in Lending Act

- The purpose of TILA is “to assure meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit . . .” 15 U.S.C. § 1601.

# The Truth in Lending Act

- TILA generally applies:
  - if the business extending credit does so regularly;
  - the credit is subject to a finance charge, or is payable in more than four installments; and
  - the credit is primarily for personal, family, or household purposes.  Reg. Z, 12 C.F.R. § 226.1(c)(1).

# The Truth in Lending Act

- TILA contains an exemption for loans that exceed $25,000, but this exemption does not apply if the loan is secured by real estate or the principal dwelling of the borrower.  15 U.S.C. § 1603(3).

# TILA and Regulation Z

- TILA and Regulation Z require disclosure of 10 essential pieces of information in relation to every loan to which they apply. 12 C.F.R. § 226.18.
  - The creditor's identity.
  - The amount being financed.

# TILA and Regulation Z (continued)

- Itemization of the amount financed or notice that such itemization is available.
- The finance charge expressed as a dollar amount.
- The finance charge expressed as an annual percentage rate.
- Details regarding the number, amount, and timing of payments.

# TILA and Regulation Z (continued)

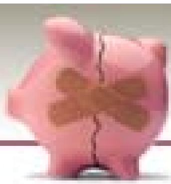
- The total amount of all payments.
- Any provisions for late fees, prepayment penalties, or nonpayment provisions.
- The fact that the lender is receiving a security interest.
- The fact that the loan might be assumed by another creditor in residential mortgage transactions.

# TILA Initial Disclosures

- TILA requires that these initial disclosures be made prior to the extension of credit. 15 U.S.C. 1637(a). The disclosures are therefore typically found as a part of the credit application and/or the terms and conditions associated with a credit account (i.e. cardholder agreement).

# TILA Periodic Disclosures

- Separately TILA requires periodic disclosures if there is an existing balance on the account. 15 U.S.C. 1637(b). These disclosures are typically made on the monthly statement of account. Certain monthly disclosures are required to be presented in a certain format. We typically refer to this disclosure format as the Schumer Box.



# Representative Recent TILA Claims

- TILA claims are generally highly technical and often are based upon ambiguities in existing regulations or Federal Reserve Board commentary
- TILA claims are limited only by the ingenuity of borrowers' counsel

# Representative Recent TILA Claims (continued)

– Examples of Lender Actions claimed to violate TILA

- Failure to provide prior written notice to borrower of increased interest rate due to borrower's balance exceeding applicable credit limits
  - This particular claim has been raised in numerous courts across the country and has resulted in recent conflicting judicial decisions. *McCoy v. Chase Manhattan Bank, USA*, 06CV5380 (9th Cir. 2009); *Swanson v. Bank of America*, 08CV3322 (7th Cir. 2009).

# Representative Recent TILA Claims (continued)

- Failure to send credit card billing statements to estate of deceased card holder
  - This claim was rejected on the ground that TILA only requires periodic statements be furnished to a "natural person." *Hess v. Citibank*, 459 F.3d 837 (8th Cir. 2006).
- Using the Regulation Z Model Form appropriate for refinancing with a new lender when the original lender actually provided the refinancing
  - Claim rejected on the theory that using the wrong form does not automatically violate TILA so long as the form used was not confusing and clearly stated the right to rescission. *Santos-Rodriquez v. Doral Mortgage Corp.*, 485 F.3d 12 (Ist Cir. 2007)

# Representative Recent TILA Claims (continued)

- Lender failed to immediately and unconditionally release its mortgage upon receipt of a notice of cancellation rather than conditioning rescission on borrowers actual tender of loan proceeds
  - Courts split on this but most say unconditional rescission is inappropriate unless borrower shows ability to tender loan proceeds. *See e.g. American Mortgage Network, Inc. v. Shelton*, 486 F.3d 815 (4th Cir. 2007).
- Negative amortization resulting from minimum payment on option ARM loan not properly disclosed.
  - These claims are getting a lot of traction where mere "possibility" of negative amortization is disclosed when the reality is it will occur. *Monaco v. Bear Stearns Residential Mortgage Corp.*, 554 F. Supp. 2d 1034 C.D. Cal. 2008.

# Remedies

- Individual Action
  1. Actual damages.
  2. Twice the amount of the finance charge up to $2000.
  3. Attorneys’ fees.
  4. Rescission.
- Class Action
  1. Not more than $500,000 or 1 percent of the net worth of the creditor, whichever is the less.
  2. Probably no rescission.

# TILA Defenses

- The Truth in Lending disclosure statement
- Statute of limitations
- Parol evidence bar

# TILA Defenses

- The TILDS itself
  - The federal government mandates certain disclosures which are arguably confusing.

# TILA Defenses

- Statute of Limitations
  - Many cases are dismissed on Statute of Limitations basis. All TILA actions for damages must be brought within one year of the alleged violation. 15 U.S.C. § 1640(e). Actions for rescission based on improper material disclosure must be brought within three years after the date of consummation of the transaction. 15 U.S.C. § 1635(f).

# TILA Defenses

- Parol evidence bar
- Borrowers cannot introduce evidence of oral representations that contradict written Truth in Lending disclosures. *Gray v. First Century Bank*, 547 F. Supp. 2d 815, (E.D. Tenn. 2008).
- Parol evidence argument is hard to make if the disclosures or note are ambiguous.

# Assignee Liability

- Assignee is liable if a TILA violation is apparent on the face of the disclosure statement.  15 U.S.C. § 1641(a).
- Assignee is liable for all TILA violations if the loan is a HOEPA loan.  15 U.S.C. § 1641(d).
- A servicer of a consumer obligation is not an assignee of the obligation for purposes of TILA unless the servicer is or was the owner of the obligation. 15 U.S.C. § 1641(f).

# Fair Debt Collection Practices Act

– The Fair Debt Collection Practices Act (FDCPA), 15 U.S.C. § 1692, et seq., regulates how a "debt collector" must conduct itself when it attempts to collect a "debt" from a "consumer." The FDCPA offers significant protections to consumer debtors and restricts debt collectors' collection efforts in a variety of ways.

# Fair Debt Collection Practices Act

- A "debt collector" is a person the "principal purpose" of whose business is the collection of debts or a person who "regularly" collects debts on behalf of others. 15 U.S.C. § 1692a(6).
- State law definitions may differ.

# Key Exclusions

- There are several key exclusions from the statutory definition of "debt collector" that may be applicable to financial institutions:
  - an officer or employee of a creditor who, in the name of the creditor, collects debts for such party;
  - a person collecting or attempting to collect a debt owed to itself;
  - a person collecting a debt due another party, as long as such collection occurs only in isolated instances;

# Key Exclusions (continued)

- a person that collects a debt not in default when obtained;
- a person that collects a debt that it originated and sold into the secondary market even though it services the debt, e.g., mortgages and student loans;
- a person that collects a debt incidental to a bona fide fiduciary relationship or escrow arrangement; or
- a person that collects a debt on behalf of another person to whom it is related by common ownership or control as long as it does so only for those persons to whom it is so related. 15 U.S.C. § 1692a(6).

# Key Exclusions (continued)

– The principal FDCPA litigation involving financial institutions relates to the relationship between financial institutions and affiliated service organizations responsible for collecting defaulted consumer debt, particularly credit card debt.

# Common Claims

- Current Common Claims:
  - Attempts to collect attorneys fees where such fees are not permitted by federal or state law.
  - Misrepresenting the proper owners of mortgage at the time foreclosures actions are filed. (Filing before assignment.)
  - Passing on to borrowers improper or excessive costs for service of process, broker price opinions, property inspections, title reports and the like.
  - Contacting debtors directly when they are members of a putative class.

# Common Claims (continued)

- We often see FDCPA claims in conjunction with FCRA claims. The Plaintiff's allege that the financial institution may be held liable under the FDCPA if it knew the debt was not legitimate at the time it referred the debt for collection. For example, in identity theft cases the Plaintiff alleges that he or she informed the lender that he or she was the victim of identity theft and did not authorize the extension of credit; therefore the Lender knew the debt was not owed when it sold the debt obligation or referred it for collection.

# Remedies

- Individual Action
  1. Actual damages.
  2. Statutory damages up to $1000.
  3. Attorneys’ fees.

- Class Action
  1. Not more than $500,000 or 1 percent of the net worth of the creditor, whichever is the less.