

Top 10 Things That Will Get You Sued in a Residential Mortgage Transaction

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Our Goals

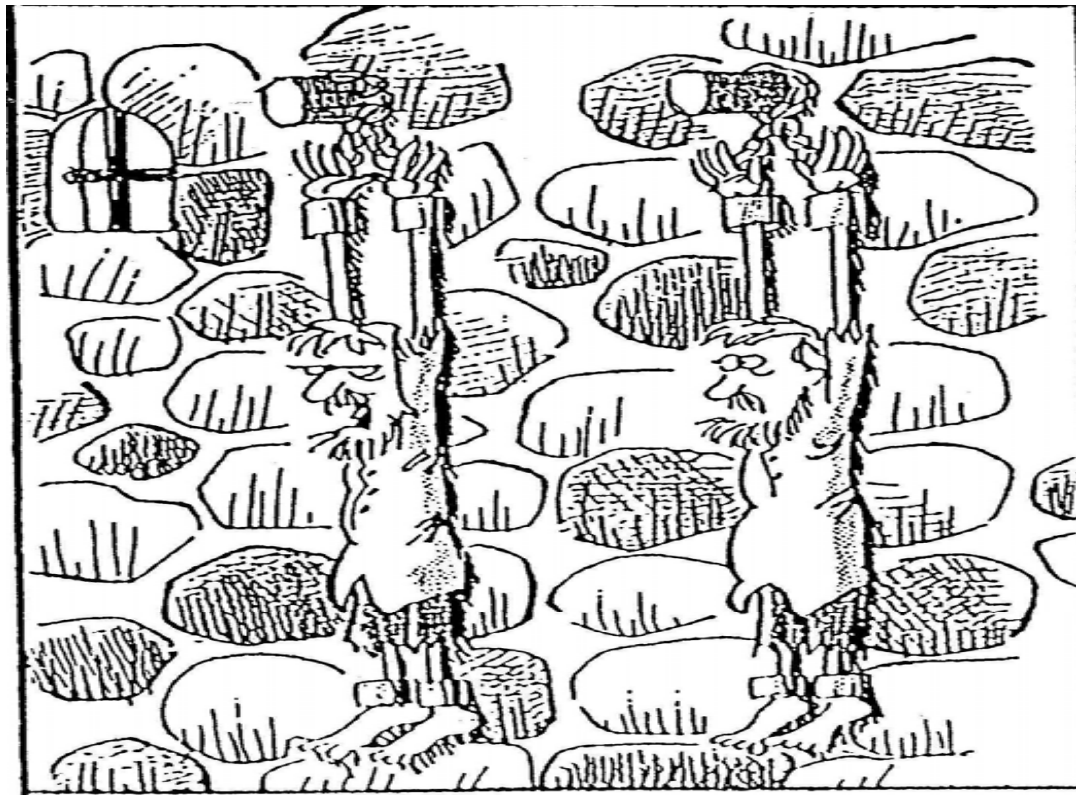
- Identify areas of litigation risk
- Avoid attention from plaintiffs lawyers and regulators
- Share “Best Practices”
- Learn from the mistakes of others
- Anticipate what’s coming
- Avoid hiring. . . me!

Overview

- People sue because they are frustrated.
- Residential mortgage industry is closely regulated by federal and state governments.
- It's the lawyers – not the clients – who figure out the technical reasons in the complaint.
- Common sense and a strong, well distributed procedures manual help to avoid most problems.
- Compliance training and testing is key and potential defenses.

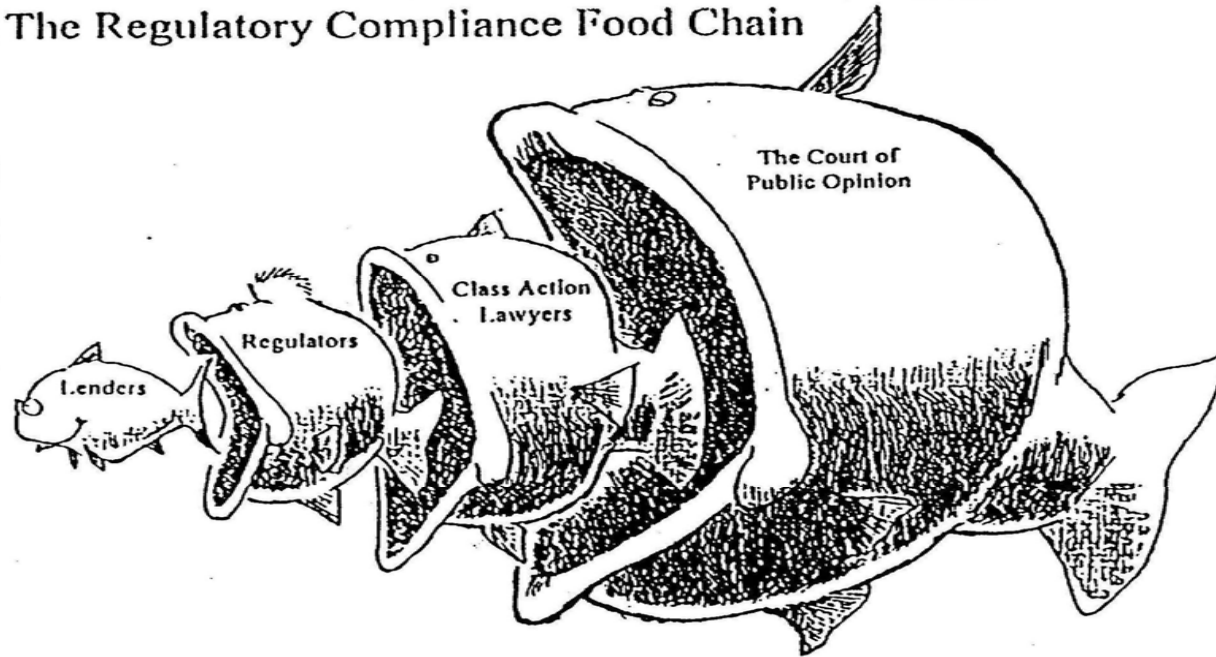
Who Is Looking Over Your Shoulder

- State departments of banking
- State attorneys general
- HUD
- Consumer lawyers
- Class action lawyers
- Title companies
- Wholesale loan purchasers/investors
- Fannie and Freddie
- Federal banking agencies
- Federal Trade Commission
- The press



"So,...do you still believe the examiners
are only here to help?"

The Regulatory Compliance Food Chain



The Top Ten List

10. Early Payment Default

- Borrower's failure to make first payment is red flag that other problems may exist
- EPD means heightened scrutiny by secondary market purchasers
- Telltale fraud signal
- Avoid EPD through proper underwriting and loan processing
- Due diligence in the selection of brokers, closers and other settlement service providers also helps

10. Early Payment Default (cont'd)

- Title insurance provides protection from some fraud problems
- Adopt tough TPO repurchase obligations

9. Rescission Notices in Refinance Transaction

- Federal Truth in Lending Act requires that “each” person with an interest in the mortgaged property receive TWO COPIES of the Rescission Notice.
- Two co-borrowers (husband and wife) must get FOUR COPIES of Notice.
- If there’s one borrower, but two names on the mortgage, both must get two copies of the Notice.
- Notices must be filled in with proper dates (three business days).

9. Rescission Notices in Refinance Transaction (cont'd)

- Most abused law in all of mortgage land.
- TILA allows them to rescind the mortgage for up to three years.
- Claim can be brought against assignees of original lender.
- He said/she said.

9. Rescission Notices in Refinance Transaction (cont'd)

- Paper the file to prove compliance.
- Written procedures.
- Distribute and explain procedures.
- Provide clear, explicit closing instructions.
- Helps to get affidavit from closing agent as part of closing package.
- Hold them liable.



It's Important to Build Strong Working Relationships With Your Regulators

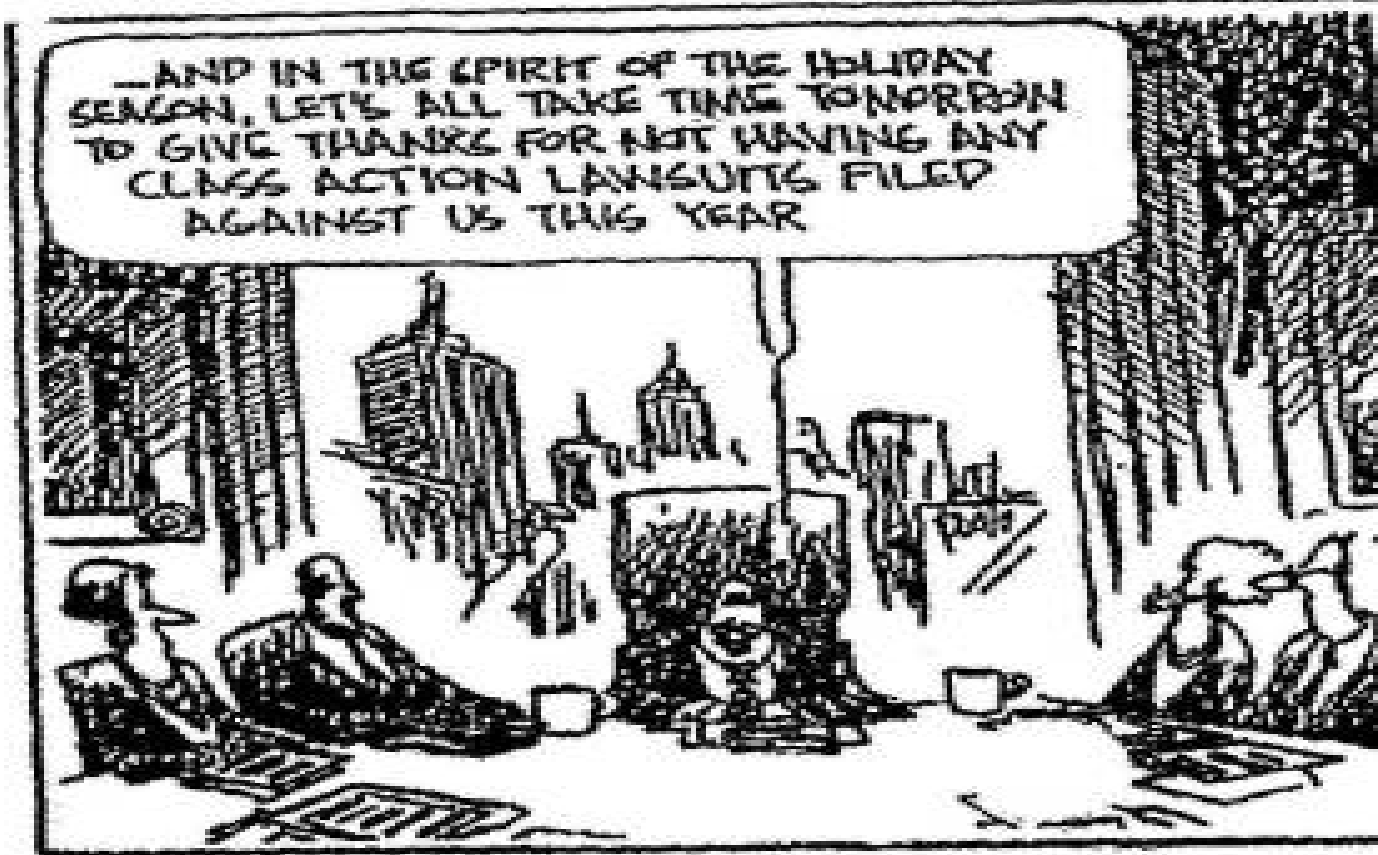
8. Prescreen Solicitations; Firm Offers of Credit

- Solicitation letter required disclosures.
- Is offer meaningful?
- Identify on paper underwriting criteria and credit factors used in prescreen.

7. Exotic Loan Products

- Borrowers focus on monthly payment amount.
- Unsophisticated borrowers may not understand alternative mortgage credit terms like balloon, ARMs, negative amortization, or “interest only” loans.
- Loan officers and brokers may be unable to explain accurately.
- When payments go up, borrowers say, “Nobody told me!” They go to a lawyer.
- New products require strong disclosures and quality customer and TPO relations.

...AND IN THE SPIRIT OF THE HOLIDAY SEASON, LET'S ALL TAKE TIME TOMORROW TO GIVE THANKS FOR NOT HAVING ANY CLASS ACTION LAWSUITS FILED AGAINST US THIS YEAR



6. Bad Appraisals

- Over-appraised properties mean under-secured lenders.
- Claims against originating lender by secondary market purchaser.
- Fannie and Freddy review appraisals when loans suffer EPD or go to foreclosure – may lead to repurchase or indemnity request against loan seller.
- No good deed goes unpunished, borrower lawsuits claiming, “You lent me too much money!”

6. Bad Appraisals (cont'd)

- “Predatory Lending” theory – lending based on obtaining maximum amount that borrower can possibly pay.
- Review appraisals.
- Representation and warranty re: multiple appraisals.

5. Referral Fees

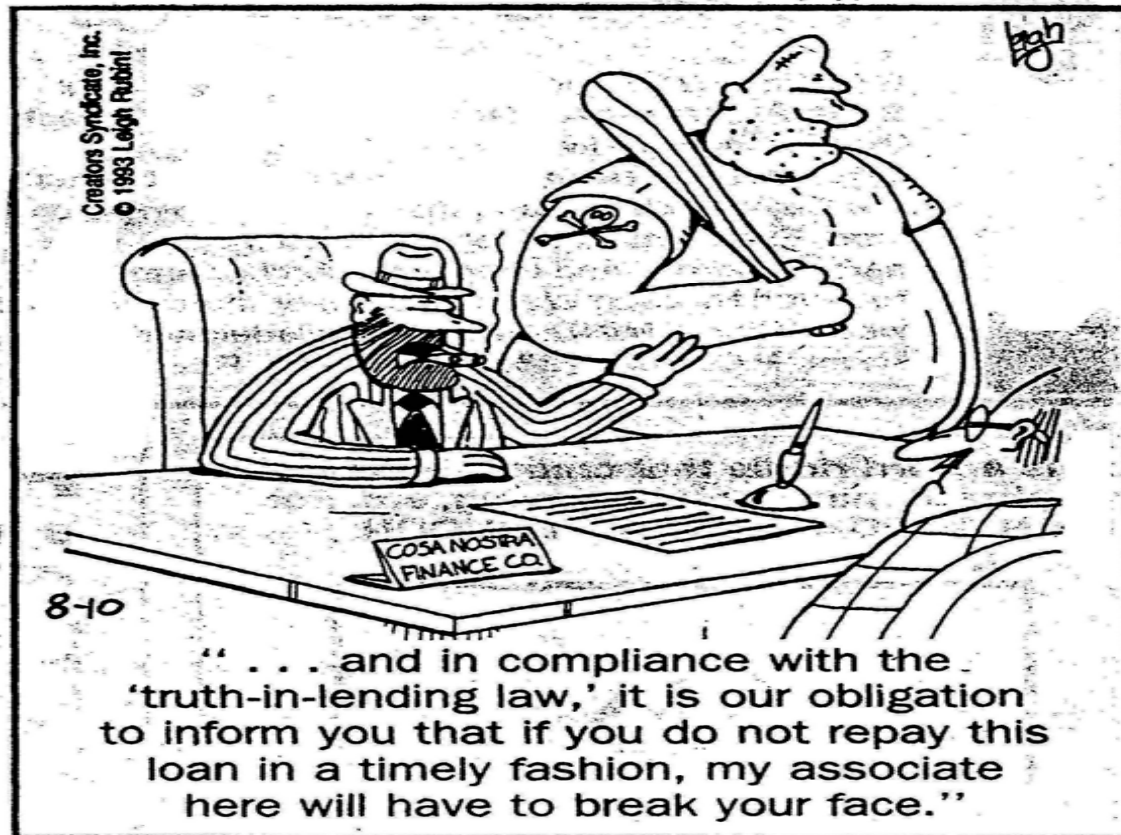
- Real Estate Settlement Procedures Act (RESPA)
- State mini-RESPA laws.
- Illegal under RESPA to pay or receive a fee, kickback or anything of value for referral of business.
- Very broad definitions of kickback and thing of value.
- It's a crime – fines, imprisonment.

5. Referral Fees (cont'd)

- Private lawsuit to get three times the charge.
- HUD and some courts hold that markup of third-party service is RESPA violation.
- Poorly constructed joint ventures; excellent documentation – bad facts on the ground.

4. Forgery

- Some give in to temptation to forge a signature on that additional disclosure; “no harm done” syndrome.
- Use a notary correctly.
- Forgery makes bad situation, where there is a missing signature on a document, and makes it worse.
- Many mistakes can be fixed by going back to the borrowers and getting them to sign new disclosures.
- State investigations.
- Compare signatures on multiple documents.



3. Bogus Rate Locks

- Commitment *vs.* rate lock.
- Verbal promises of “rate lock” lead to borrower disappointment, when lender fails to honor unwritten “commitment”.
- Borrowers not informed of lock expiration date.
- Disclose in writing the rate, the terms, and the duration of the rate lock.
- Then process the loan promptly, before rate lock expires.
- Misleading advertising.
- Lock in with investor *vs.* consumer rate lock.

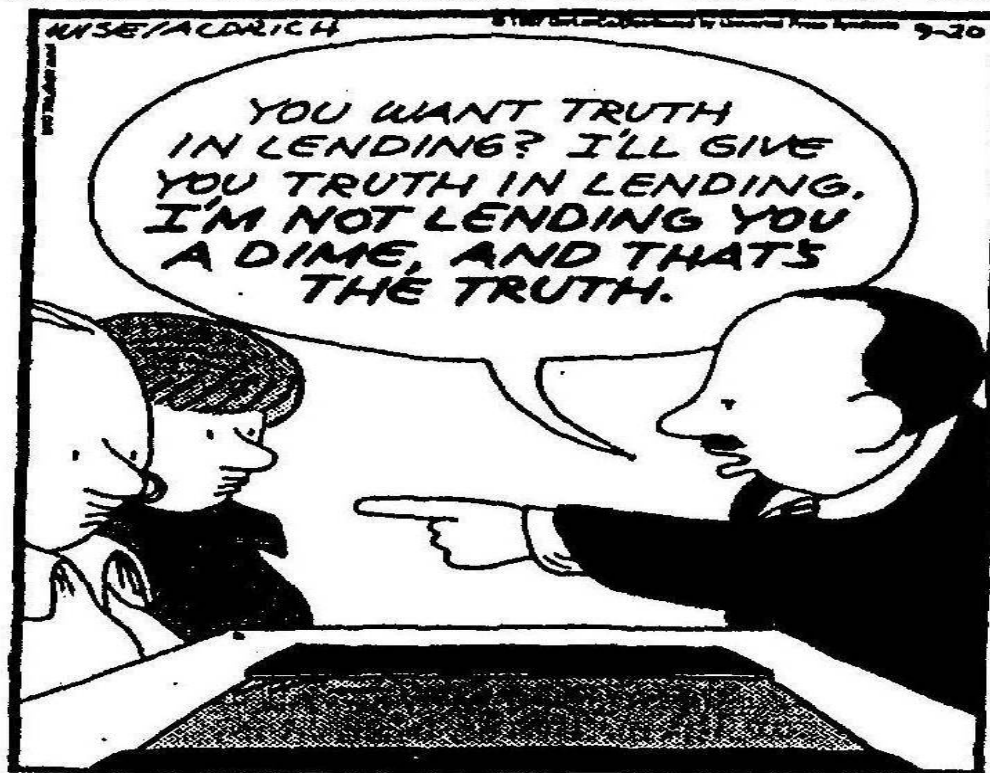
2. “Adverse Action” Notices

- ECOA and FCRA require lender to notify borrower in writing of rejection, the acceptance or counteroffer, and credit report information.
- If loan is rejected or counteroffer is not accepted, then lender must send adverse action notice.
- Failure to do so = \$100 to \$1,000 statutory penalty, plus.

1. Inflated Settlement Fees

- Appraisal charges
- Document preparation fees
- Settlement charges
- Credit report charges
- Title search
- Flood search
- In-house attorney's fees
- Unreasonable charges must be included in the TILA finance charge
- Can be basis for rescission
- Can convert loan into high cost HOEPA loan or violation of state predatory lending laws

REAL LIFE ADVENTURES



Summary

10. Early payment default
9. Rescission Notices
8. Prescreen solicitations
7. Exotic Loan Products
6. Bad appraisals
5. Referral Fees
4. Bad Appraisals
3. Bogus Rate Locks
2. Adverse Action Notices
1. Inflated Settlement Charges

