
Nontraditional Mortgages – Nontraditional Litigation?

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Do New Products or Practices Bring Waves Of New Cases?

Yes

- Mortgage brokers
- ARMs
- AfBAs
- Servicing fees

No

- Nonprime lending
- Outsourcing
- AUS
- Internet/website origination activity

Will Nontraditional Mortgages Spawn Litigation?

- High public visibility
- Controversy
- Questionable practices by some in industry
- Jury appeal, or confusion
- Significant risk of loss for individual consumers

Key Areas of Litigation Focus

■ Advertising/marketing

□ Misleading statements

- *FTC v. Chase Financial Funding, Inc., et als.*, Case No. 04-549 (C.D. Cal.)

■ Disclosures

□ TILA

□ Entire body of what consumer receives

Key Areas of Litigation Focus

- Underwriting
- Substantive terms
 - Interest only ARMs
 - Pay option ARMs
- Servicing

Claims In Search Of A Legal Theory

- Traditional magnets for suits may not provide ready remedy for controversial practices
 - TILA (including HOEPA)
 - RESPA
 - Common law
- Debate about “suitability” standard shows there is no clear standard today

So How Will Suits Arise?

- Suits probably will be filed with *traditional* theories
 - Safest approach – less of a stretch for the judge
 - Lazyman’s approach
- Two types to watch for
 - Suits to remedy the symptom (foreclosure), not the underlying cause (allegedly bad loan)
 - Suits filed about unrelated problem, which was discovered because the consumer complained about a nontraditional loan

Implications – What Traditional Litigation Looms?

- TILA – rescission remedies severe
 - **But** *McKenna v. First Horizon*, 475 F.3d 418 (1st Cir. 2007) (no TILA rescission class actions allowed)
- UDAP challenges
- Foreclosure and bankruptcy class actions

Possible Nontraditional Theories About Nontraditional Mortgages

■ Unconscionability

- Terms that are excessively one-sided, with an element of unfair bargaining
- Examples:
 - *In re Maxwell*, 281 B.R. 101 (D. Mass.)
 - *United Companies Lending, Inc. v. Sargeant*, 20 F. Supp.2d 192 (D. Mass. 1998)
 - *Besta v. Beneficial Loan Co. of Iowa*, 855 F.2d 532 (8th Cir. 1988)

Possible Nontraditional Theories About Nontraditional Mortgages

- UDAP - “Unfairness”
 - S&H test (405 U.S. 233 (1972))
 - Offends public policy
 - Immoral, unethical, oppressive or unscrupulous
 - Substantial and unavoidable consumer injury
- UDAP - terms that may be confusing to average or reasonable consumer
 - Very short term “teaser” rates
 - *Andrews v. Chevy Chase Bank, FSB*, Case No. 05-454 (E.D. Wis.)

Possible Nontraditional Theories About Nontraditional Mortgages

- Fraudulent sales and marketing practices
 - Consumer confusion exacerbated by excessive disclosures, unsuitable TILA documents
- Breach of fiduciary duty
 - Broker loans – California, NY
- Unjust enrichment
- Aiding and abetting, agency
 - *In re First Alliance Mortgage Co.*, 471 F.3d 977 (9th Cir. 2007)

Can These Be Made Into Class Actions?

- Many theories are borrower-specific, not necessarily subject to class treatment
- Risks remain
 - “Policies” are at the heart of the cases
 - Even fraud can be certified in proper case
 - Certification is discretionary
 - Having to fight the class can be almost as bad as getting certified

So What Should You Do About It?

- Review the “entire” package of what consumers receive – consider additional disclosures
- Be diligent about overall compliance
- Follow advice from the panel!

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