

TILA and FCRA: 2007 Litigation Update

Richard E. Gottlieb
Dykema

May 7, 2007

Mortgage Bankers Association

Outline

- 1. TILA Litigation Developments
- 2. FCRA Litigation Developments

Part One: Truth in Lending Litigation Update

- First Circuit holds that TILA prohibits class action rescissions but district court within 7th Circuit rules to the contrary
- Seventh Circuit now expected to rule on same issue
- Three appellate courts approve of “rescission damages” concept notwithstanding plain language of the statute

Class Actions under TILA

- Under 15 USC § 1640, plaintiffs may pursue class actions for damages
- Maximum liability is \$500,000
- TILA is silent with respect to class actions for rescission (the rescission provision makes no reference to it)
- Notwithstanding the cap, the theoretical damages for rescission class actions could annihilate many a lender.

Plaintiffs Bar Has Longed Attempted to Pursue Rescission Class Actions

- Challenges date back to earliest years of TILA
- Districts courts have broadly been split on the issue (earliest cases rejected the concept)
- Most courts recognize personal nature of remedy
- Until recently, the more prevalent trend was to allow class actions seeking a “declaration” that borrowers had the right to rescind

McKenna v. First Horizon (1st Cir. Jan. 29, 2007)

- Decision below: D. Mass. certifies class action for rescission
- First Circuit:
 - Rescission is private remedy not amenable to class treatment
 - Based on statutory scheme, including \$500,000 statutory cap, Congress must have intended rescission to be totally unavailable as a class remedy

Andrews v. Chevy Chase Bank (ED Wis. Jan. 16, 2007)

- District court concludes that Option ARM disclosures violated TILA because, among other things, they did not clearly disclose the APR and variable rate feature.
- Court concludes that case may be certified as a class action seeking judicial declaration that borrowers had a right of rescission
- Case has been appealed to 7th Circuit. MBA and others have filed amicus briefs urging reversal

Is there a right to “rescission damages”?

- TILA nowhere addresses the question whether a borrower may rescind a loan **AFTER** the loan has been paid off.
- What is there left to rescind after the borrower pays off the loan?
- TILA allows for right of rescission, and **NOT** to damages equal to the value of a rescission if requested after the loan is refinanced or paid.

Barrett v JP Morgan Chase Bank (6th Cir. Apr. 18, 2006):

- 6th Circuit reverses district court ruling that rejected rescission damages.
- Neither TILA nor Reg Z, says court, provide that act of refinancing extinguishes an unexpired right to rescind.
- Indeed, right to rescind allows for right to recover fees in addition to release of the security interest.

Two Other Decisions worth noting

- *Handy v. Anchor Mortgage*, 464 F3d 760 (7th Cir. 2006): Court agrees with “well-reasoned opinion” of *Barrett*
- *Pacific Shore Funding v. Lozo*, 138 Cal App 4th 1342 (Cal. App. 2d Dist. 2006): likewise follows *Barrett*. Even after paying off loan, borrowers still have something to rescind, *i.e.*, interest, fees, penalties and charges paid by the borrower.

Part Two:

FCRA Litigation Developments

- The Supreme Court prepares to resolve a split among appellate courts concerning the “willfulness” standard under FCRA
- The courts deal a death blow to FCRA “adverse action” and “clear and conspicuous” disclosure private actions
- Courts come to their senses in the “firm offer of credit” litigation plague

Fair Credit Reporting Act, 15 USC § 1681 et seq.

- Enacted primarily to monitor and regulate use and disclosure of consumer data by credit bureaus (CRA's)
- Among others things:
 - CRA's must have a "permissible purpose" before releasing consumer information
 - Lenders must provide "adverse action" notices to persons who are denied credit or receive lesser credit terms because of information in their credit reports

Willful Violations

- 15 USC § 1681n allows for recovery of statutory damages of \$100 to \$1000 for willful noncompliance with the statute
- Traditional view: willfulness requires knowing violation of the statute
- But Ninth Circuit, in *Reynolds v. Hartford Financial Services*, 435 F3d 1081 (9th Cir. 2006) held that “reckless disregard” was sufficient.

GEICO v. Edo; Safeco v. Burr

- Supreme Court accepted certiorari to resolve the split in the Circuits concerning willfulness standard
- Also should resolve question whether “adverse action” notices are required even if the lender or insurer merely fails to offer the consumer the best possible rate because of the absence of credit data. Ninth Circuit, in *Reynolds*, concluded that notices were required.

Fearless prediction

- The Supremes will conclude:
 - (1) that there is no adverse action notice requirement unless the lender or insurer increases the quoted insurance rates or credit terms because of information in the credit report; and
 - (2) that willfulness requires a knowing violation of the law or, at a minimum, willful blindness of a known legal standard

Adverse action: no more private rights of action?

- Eff. 12/1/04, Fair and Accurate Credit Transactions Act (FACTA) amendments effectively negated private rights of action for violations of 15 USC § 1681m
- Among other things, that provision addresses “adverse action” notice requirements and obligation to provide “clear and conspicuous” disclosures of “firm offer” mailers.

“Firm Offer of Credit” Developments

- 7th Circuit has further amplified on its misunderstood *Cole v. US Capital* decision
- District courts outside and within the 7th Circuit reject view that all material terms of the offer must be in the mailer itself
- District courts are likewise beginning to grant summary judgment on “willfulness” in the absence of objective evidence of knowing violation

Background: *Cole v. US Capital*

- 7th Circuit decision from 2004
- Concluded that “firm offers” must have sufficient value to justify invasion of privacy
- Court reversed dismissal of suit because the mailer, on its face, lacked sufficient terms to determine whether it met “firm offer” requirements

Cole leads to a litigation explosion

- Well over 300 putative class actions
- In 2005, courts broadly refused to dismiss most suits at pleading stage
- Also, courts routinely certified classes by the dozens
- Widespread concern last year that suits could lead to annihilating damages

Murray v. GMAC Mortgage (7th Cir. 2006)

- Court ambiguously suggests that court need only look at “four corners of the offer” to determine whether it meets FCRA requirements
- Did court mean to state that a mailer violates FCRA if it lacks all material terms in the mailer?
- Or does this phrase refer to the entire “offer,” including follow-up communications?

Perry v. First National Bank (7th Cir. 2006)

- Affirms dismissal of credit card “firm offer” case, and affirms lack of private action for “clear and conspicuous” claims
- Distills *Cole* to require three things:
 - 1. That the mailer advise consumers the offer will be honored;
 - 2. That terms be adequately disclosed; and
 - 3. That the amount of credit have sufficient value.

The Tide Begins to Turn

- Several district court decisions outside the Seventh Circuit distinguish or openly reject the *Cole* line of decisions
- District courts within the Seventh Circuit begin to distinguish *Cole*, *Murray* and *Perry* on the facts
- Most credit card “firm offer” cases get dismissed at pleading stage based on *Murray* four corners test

Bruce v. Keybank (ND Ind. Dec. 15, 2006)

- First district court decision anywhere to grant summary judgment to mortgage lender on “willfulness” in “firm offer” case
- Concludes that issue can be resolved on summary judgment where there is no “smoking gun” evidence that lender knowingly and intentionally violated the law

Cavin v. Home Loan Center (ND Ill. 2007)

- First district court decision within Seventh Circuit to grant summary judgment to mortgage lender where mailer lacks material terms
- Rejects any reading of *Cole* or *Perry* to require such disclosures
- Grants summary judgment to mortgage lender because mortgage offers must be tailored to the individual consumer

So where do we go from here?

- *GEICO/Safeco* should make it more difficult for plaintiffs to prevail in FCRA class action litigation
- Most lenders have taken the corrective action needed to avoid future liability
- Class actions will begin to settle on an individual basis as courts increasingly reject these suits in droves

Thanks!

Richard Gottlieb

Dykema

rgottlieb@dykema.com