



MBA Regulatory Conference— Litigation Risk for Mortgage Lending Laws

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Goals of Presentation

- To Look at Several Laws from Litigation Perspective—
 - Fair Credit Reporting Act (FCRA)
 - Home Mortgage Disclosure Act (HMDA)
 - Equal Credit Opportunity Act (ECOA)
 - Fair Housing Act (FHA)
- To Understand the Legal Risk That Arises from Compliance Failure
 - Administrative Enforcement
 - Civil Litigation



Initial Perspectives

- Your Charter Form Matters
 - Federal Preemption May be Available
 - Transactional Preemption
 - Chartering Preemption
- State Laws Can be Applied as Hammers
 - “Mirror Image” Statutes May Carry Greater Damage Potential
 - UDAP-Type Statutes May Apply if a Federal Law is Violated



Initial Perspectives

- Consumer Groups are Sophisticated
- Liability Provisions are Traps for the Unwary
- Legislative Compromises Frequently Result in Liability Provisions that are Downplayed
- Today's Courts are Hesitant to Absolve Lenders From Liability



Why Are We Concerned About Litigation?

- Litigation is a Cost of Doing Business
- Individual Lawsuits Can Act as a Governor for Unfair or Illegal Lending Practices
- Class Action Exposure May be Significant
 - An Organized Plaintiff's Bar "Franchises" Lawsuits
- Every Decade an "End of the World Lawsuit"
- Reputational Risk
- Enormous Costs Resulting From Minor Violations



Fair Credit Reporting Act

- A Useful Case Study Supporting Compliance
- The FCRA's Liability Provision is Bifurcated—
 - Actual Damages for Negligent Violations
 - \$100 to \$1000 Statutory Damages for “Willful” Violations—Per Violation



The Firm Offer of Credit Saga

- The FCRA Protects Consumer's Privacy Rights From Unsolicited Offers of Credit
- An Exception is the "Firm Offer" of Credit Exception
 - Relatively Easy to Do in the Credit Card Arena
 - More Complicated in Mortgage Lending



The Firm Offer of Credit Saga

- Courts Decided that the Industry's Compliance With the "Firm Offer" Requirements of the FCRA Provision was Wrong
 - Plaintiffs' Bar Alleged Violations Were Willful
 - Damages Estimated in the Billions or Trillions?
- Over 250 Class Action Lawsuits Filed
 - This Decade's End-of-the-World Lawsuit
- What is Willfulness in the Civil Law Context?



Safeco Insurance v. Burr

- Decided by the Supreme Court in June Under the “Insurance Prong” of the Adverse Action Provision of the FCRA
- Technically Determined that an Initial Underwriting of Insurance Could Constitute Adverse Action if a Credit Report is Used
- More Importantly—*Safeco* Addressed the Willfulness Standard in FCRA



Safeco Insurance v. Burr

- Willfulness Includes Reckless Behavior
 - An Objective Standard
 - Not a Subjective Standard
- Reckless Disregard of a Statute Requires—
 - A Violation of a Statute Based Upon an Erroneous Reading or Interpretation
 - Substantially Greater Risk of Violating the Statute than the Risk Associated with Being Merely Careless



Compliance Procedures And Process Are Essential

- FCRA Violations Are Potentially Severe if Willful
 - Lack of Agency Guidance
 - No Reliable Judicial Precedent
 - Complex FCRA Compliance Obligations
- Staying Current is Critical



ECOA, The FHA And HMDA

- 2002 Amendments to Regulation C
 - Required Reporting of Limited Pricing Data
 - Assembled and Released by the FRB Each September
 - Anxiously Anticipated by Consumer Groups



The Public HMDA Data Supports The Mortgage Industry—But...

- Mortgage Lending is Conducted on a Racially and Ethnically Neutral Basis
- The Public Data Has Not Resulted in Massive Lawsuits
- The Federal Regulators Have Not Stopped Reviewing Lenders' Fair Lending Performance
- The Consumer Groups Have Retrenched in Their Litigation Tactics



Administrative Fair Lending Enforcement

- The FRB Performs a Screening for Outliers
 - Last Year 270 Lenders Were Identified
 - Each Federal Agency Provided With the List
 - Each Banking Agency Can Refer to the DOJ
 - The DOJ Has Initiated Its Own Investigations



Administrative Investigations

- Extremely Expensive and Resource Draining—
 - Outside Experts Needed
 - Econometric Data Required
 - Never-Ending
 - Stressful
 - Senior Management Not Happy
 - At Best an Opaque Process



Private Party Enforcement

- The ECOA and FHA Provide Plaintiffs Significant Procedural Rights—
 - Complaints Can Be Made to HUD
 - Lawsuits Can Be Filed Directly
 - The Government Does All of the Discovery
 - Settlements Go to the Consumer Groups



Recent Private Party Claims

- Redlining
- Product Redlining
- Predatory Lending



Proving Fair Lending Claims

- Disparate Treatment
- Disparate Impact
- Accusations Count More Than Actual Proof
 - Atlanta Constitution
 - Boston FED Report
 - Chevy Chase Federal
- Reputation Risk Is Paramount Concern
- The Technical Legal Requirements Are at Best Uncertain



Use of Counsel

- Section 1818(x) of the FDIA Act
 - Preserves All Privileges
 - Protects Sensitive Data Provided to State and Federal Banking Regulators
 - Should Always be Considered When Sensitive Litigation Material Data is Requested as Part of an Investigation or Examination