

**MBA REGULATORY COMPLIANCE CONFERENCE  
JW MARRIOTT HOTEL  
WASHINGTON, DC  
SEPTEMBER 23-25, 2007**

***Federal Regulators and Alphabet Soup Panel***

***Monday, September 24, 9:30 a.m. to 11:00 a.m.***

***RESPA and TILA Issues Roundtable***

***Tuesday, September 25, 9:45 a.m. to 11:00 a.m.***

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**I. RESPA**

**A. Scope**

1. RESPA applies to federally related mortgage loans.
2. The term “federally related mortgage loans” is broadly defined to include:
  - a. First lien purchase money loans.
  - b. First lien refinance loans.
  - c. Junior lien loans, including home equity credit lines.
    - i. Home equity credit lines are exempt from various RESPA requirements.

**B. Section 8 Background**

1. RESPA Section 8 prohibits referral fees.

- a. A “referral” includes any oral or written action directed to a person that has the effect of affirmatively influencing the selection by any person of a settlement service provider.
2. RESPA Section 8 also prohibits the splitting of a settlement service fee, other than for services provided.
3. RESPA Section 8 does not prohibit payments to any person that reflect the reasonable value of services, goods or facilities provided by the person.
4. HUD interprets the RESPA fee splitting prohibition to prohibit all unearned fees, including but not limited to cases in which:
  - a. Two or more persons split a fee for settlement services, any portion of which is unearned.
  - b. One settlement service provider marks-up the cost of services performed or goods provided by another settlement service provider without providing additional actual, necessary and distinct services, goods or facilities to justify the additional charge.
  - c. One service provider charges the consumer a fee where no, nominal or duplicative work is done, or the fee is in excess of the reasonable value of goods or facilities provided or the services actually performed. This commonly is referred to as “overcharging.”
5. Until recently, United States Circuit Courts of Appeals rejected HUD’s position on overcharges. The Courts are divided on HUD’s position regarding mark-ups.
  - a. Overcharges
    - i. No Circuit Court of Appeal had found that an overcharge could violate Section 8(b), until an August 6, 2007 decision by the Second Circuit Court of Appeals in *Cohen v. JP Morgan Chase & Co. et al.*, --F.3d --, 2007 WL 2231106 (2d Cir. 2007).
    - ii. The decision distinguishes a prior decision of the Second Circuit in *Kruse v. Wells Fargo Home Mortgage, Inc.*, 383 F.3d 49 (2d Cir. 2004). In *Kruse* the Second Circuit rejected the contention that the amount by which a fee or charge for a service exceeds the reasonable value of the service is the portion, split or percentage of the charge that is other than for services rendered and, thus, in violation of Section 8(b). Based on *Kruse*, it appeared that the

Second Circuit rejected the overcharge theory of HUD's position of fee splits.

- iii. In *Cohen*, the Second Circuit addressed allegations by the plaintiff that Chase provided no services for a \$225 post closing fee imposed on the plaintiff. The Court stated that *Kruse* invalidated only part of HUD's overcharge theory—the part providing that Section 8(b) prohibits a fee that exceeds the reasonable value of goods or facilities provided or the services actually performed.
  - A. The Second Circuit explained that HUD's position on fees that exceed the reasonable value of goods effectively imposed price controls on settlement fees and was contrary to the plain meaning of Section 8(b).
  - B. Finding the Section 8(b) language prohibiting “any portion, split, or percentage of any charge” to be ambiguous, the Second Circuit deferred to HUD's position that a single settlement service provider that charges a fee for which no, nominal or duplicative work is done violates Section 8(b).

b. Mark-ups

- i. The Fourth, Seventh and Eighth Circuit Courts of Appeals have found that mark-ups do not violate the fee splitting prohibition.
- ii. The Second and Third Circuit Courts of Appeals have found that the mark-ups violate the fee splitting prohibition, if not supported by services.
  - A. *Santiago v. GMAC Mortgage*, No. 02-4048 (E.D. Pa.). In a 2005 decision, the Third Circuit accepted HUD's position that mark-ups can violate RESPA Section 8(b), rejected HUD's position that overcharges can violate RESPA Section 8(b), and remanded the case to the district court for further proceedings. On August 7, 2007 the district court approved a settlement agreement providing for a settlement fund of \$650,000, with \$325,000 going to the 81,981 class members and \$325,000 going to the plaintiff's attorneys.
- iii. The Eleventh Circuit, although ruling for the defendants in a case, noted that a single settlement service provider can violate the fee splitting prohibition and, thus, appeared to indicate that mark-ups violate the fee splitting prohibition if not supported by services.

- iv. The Seventh Circuit also found that an impermissible fee split may exist when both the lender and the closing agent imposed a release fee on the borrower.
- c. States Within The Jurisdiction of the Courts of Appeals:
  - i. Second Circuit: Connecticut, New York and Vermont.
  - ii. Third Circuit: Delaware, New Jersey, Pennsylvania and the Virgin Islands.
  - iii. Fourth Circuit: Maryland, North Carolina, South Carolina, Virginia and West Virginia.
  - iv. Seventh Circuit: Illinois, Indiana and Wisconsin.
  - v. Eighth Circuit: Arkansas, Iowa, Minnesota, Missouri, Nebraska, North Dakota and South Dakota.
  - vi. Eleventh Circuit: Alabama, Florida and Georgia.
- 6. Related TILA Issue.
  - a. Under the Truth in Lending Act and Regulation Z, in a mortgage loan transaction certain fees are excluded from the finance charge if they are bona fide and reasonable in amount.
  - b. The fees include credit report fees, appraisal fees, loan-related document preparation fees and title examination fees.
  - c. If a party marks-up one of the fees, does the entire fee still qualify for exclusion from the finance charge? Is the fee still reasonable?
- 7. Related State Law Issues.
  - a. States typically limit the fees that may be imposed on a borrower, and various state regulators take the position that a mortgage company may pass on to a consumer only the actual charge imposed by a third party service provider.
  - b. States also have unfair and deceptive practice and related laws. Disclosing to a consumer that a third party charge is higher than that actual charge presents issues under such laws.

- c. In September 2006 a California appellate court, in the case of *McKell v. Washington Mutual, Inc.*, 2006 WL 2664130 (Cal.App. 2 Dist.), addressed alleged mark-ups of third party fees by a lender.
  - i. The court determined that the borrowers properly alleged claims under the California Unfair Competition Law (UCL) in challenging the lender's imposition of charges for third party services that exceeded the actual cost of the services, with no indication to the borrowers of such mark-ups.
  - ii. Specifically, the court determined that the challenged conduct may constitute a deceptive practice within the meaning of the UCL, would be an unfair business practice under the UCL, and would be an unlawful business practice under the UCL.
  - iii. The unlawful business practice determination is based on the court's conclusion that the mark-up practice would violate RESPA. Thus, the California court sided with the federal appellate courts that believe mark-ups violate RESPA Section 8.

### **C. RESPA Reform or Déjà Vu All Over Again**

#### **1. RESPA Reform Announcement**

- a. On August 31, President Bush announced a new RESPA reform proposal will be issued this Fall.
  - i. The proposal must be submitted for review to the Office of Management and Budget before it can be officially released for public comment.
- b. Apparently, the proposal will:
  - i. Promote comparative shopping by consumers for the best loan terms.
  - ii. Provide clearer disclosures.
  - iii. Limit settlement cost increases.
  - iv. Require fee disclosure.

2. HUD's Previous Efforts
  - a. HUD issued a RESPA reform proposal in July 2002 and withdrew the proposal in March 2004 in the face of opposition and comments from various fronts, including Congress, federal government agencies, industry groups and consumer groups.
  - b. HUD kicked off a second round of RESPA reform in June 2005 by announcing it would hold a series of roundtables.
  - c. MBA directly or through its members attended each of the seven roundtables.
  - d. MBA also formed the RESPA at Ready Task Force to address RESPA reform.
3. RESPA at Ready Task Force
  - a. Threshold determination: Should HUD elect to forgo reform at this time?
    - i. The market is evolving and reforming itself.
    - ii. HUD may wish to consider allowing the market to continue to operate, innovate and simplify the mortgage process under the current rules.
    - iii. Under the current rules, competition and innovation in the mortgage market are resulting in greater transparency and lower costs to consumers.
    - iv. Regulatory changes will require significant and costly changes by the industry, and require consumer education.
      - A. The related costs ultimately will be borne by consumers.
4. MBA 2006 Proposal For Consideration if HUD Will Move Forward With Reform
  - a. If HUD determines there is a need to revise the current rules, then three Options developed by the RESPA at Ready Task Force are available for consideration.
  - b. A central theme of the Options is that any reform should be accompanied by regulatory relief.
  - c. Option 1 focuses on revising the Good Faith Estimate and HUD-1.

- d. Option 2 includes Option 1, and adds tolerances for lender and mortgage broker charges, along with limited Section 8 exemptions.
  - e. Option 3 includes Options 1 and 2, and adds tolerances for all major settlement charges, except government charges and prepaid charges, and includes an additional Section 8 exemption.
5. Option 1
- a. Good Faith Estimate. The form would be revised to provide as follows:
    - i. At the top, the GFE would:
      - A. Include a brief statement describing the document.
      - B. Provide that the estimate is based on information provided by the consumer.
      - C. Provide that additional information would be required to determine if the consumer and property qualifies for the loan.
    - ii. The basic loan characteristics, such as amount and term, would be set forth.
    - iii. The proposed interest rate, points, APR and monthly payment would be disclosed.
    - iv. The estimated charges would be disclosed in nine main categories instead of being itemized individually:
      - A. Lender charges.
      - B. Mortgage broker charges.
      - C. Credit report, property valuation and inspection charges.
      - D. Title charges.
      - E. Government, recording and transfer charges.
      - F. Interest and mortgage insurance charges.
      - G. Taxes, flood and hazard insurance charges.

- H. Escrow charges and reserves.
  - I. Other loan settlement charges, such as life of loan flood and tax services.
- v. The charges that are included in the APR calculation would be noted.
  - vi. The POC items would be shown as a lump-sum and deducted from the total charges to show the estimated amount due at closing.
  - vii. Consistent with the current rule, the GFE would disclose estimated compensation to be paid by the lender to the mortgage broker, but with an explanation.
    - A. You may recall that the FTC tested with consumers the method of disclosing lender-paid mortgage broker compensation that HUD included in its original reform proposal.
    - B. The FTC found that under the proposed disclosure method, consumers often could not determine whether a retail or wholesale loan was cheaper, and in various cases incorrectly concluded that the brokered loan was more expensive.
    - C. Under Option 1, the GFE would state that brokers must disclose lender-paid compensation, and that to compare loans the consumer should focus on the interest rate, points and settlement charges, and not lender-paid broker compensation.
- b. HUD-1.
    - i. Like the GFE, the HUD-1 would set forth the actual loan charges in nine main categories instead of itemizing each charge.
    - ii. This would provide for an easy comparison of the estimated charges in the GFE and the actual charges in the HUD-1.
  - c. Other Matters:
    - i. The Special Information Booklet would be revised to reflect the new forms.

- ii. HUD would need to consult with the Federal Reserve Board for TILA coordination purposes.
  - iii. The Option recommends that HUD preempt state laws that would conflict with the streamlined disclosure method.
- 6. Option 2
  - a. The Good Faith Estimate and HUD-1 would be the same as with Option 1.
  - b. Tolerances:
    - i. Tolerances would be added.
    - ii. Except for discount points, the lender charges and the broker charges each could vary by no more than 2%, as long as:
      - A. The borrower and property qualify for the loan; and
      - B. The borrower does not request a change in the loan described in the GFE.
  - c. The Good Faith Estimate would be open for acceptance for a minimum period of 5 calendar days.
  - d. Limited Section 8 Exemptions:
    - i. Lenders and mortgage brokers would be entitled to a limited Section 8 exception for average-cost pricing of their own charges and other categories of costs on the GFE, provided that:
      - A. The tolerances were not exceeded; and
      - B. The charges for each of the cost categories are generally (that is, more than 80%) attributable to the sub-items of costs described in the category.
    - ii. Lenders and mortgage brokers also would be entitled to an exemption from Section 8(b) with regard to mark-ups of third party costs, as long as the charges in each cost category are disclosed and the tolerances are not exceeded.

- e. Non-Judicial Corrective Action
  - i. If the lender's or broker's charges exceeded the 2% tolerance, the lender or broker, as applicable, could take non-judicial corrective action by repaying any overage.
    - A. If the lender or broker did not repay the overage in a certain period of time, the amount required to correct the error would increase.

7. Option 3

- a. Option 3 would include all the changes in Option 1 and Option 2.
- b. Additional Tolerance:
  - i. There would be a 10% tolerance for a third-party costs and title costs, as long as:
    - A. The borrower and property qualify for the loan; and
    - B. The borrower does not request a change in the loan described in the GFE.
  - ii. Government charges and prepaid charges would not be included in the tolerance.
- c. Additional Section 8 Exemption:
  - i. There would be a limited Section 8 exemption for lenders, mortgage brokers and other settlement service providers to permit volume discount arrangements.
    - A. As long as the charges in each cost category are within the tolerances, volume discounts would be permissible, whether or not the charges in the categories are greater than the volume costs negotiated.

**D. Enforcement Trend**

- 1. Parties Who Can Enforce Section 8 Kickback and Fee Split Prohibitions
  - a. HUD.
  - b. The Attorney General or Insurance Commissioner of a state.

- c. Private parties.
2. Time Period to Enforce
    - a. Three years from the violation for HUD and the Attorney General or Insurance Commissioner of a state.
    - b. One year from the violation for private parties.
      - i. Private parties may argue that a violation was concealed and that the running of one year time period should be “tolled,” or delayed.
  3. Numbers—Potential Enforcement Parties
    - a. HUD.
 

Total number in 2007: 1.
    - b. State Attorney Generals and Insurance Commissioners.
 

Total number in 2007: 100.
    - c. Law Firms With 2 or More Lawyers (according to the ABA).
 

Total number in 2000: Over 47,500.
    - d. Lawyers (according to the ABA).
 

Total number in 2006: Over 1.1 million.
  4. Numbers—Enforcement
    1. HUD.
 

From 2001 to 2006 HUD entered into 46 RESPA Section 8 settlements that were made public on its website.
    2. States.
 

Historically, RESPA Section 8 has not been a priority for states, but states now are focusing more on RESPA and related state laws, especially with regard to title companies.
    3. Private Lawsuits.

Don't ask.

5. Litigation Trend

- a. In the 1990s plaintiffs' attorneys found and fell in love with the settlement service industry.
- b. Initially cases brought against industry members took aim at "nuts and bolts" issues under federal law, such as:
  - i. Claims that escrow accounts were not handled in accordance with RESPA.
  - ii. Claims that yield spread premiums paid by lenders to mortgage brokers were illegal kickbacks or referral fees under RESPA Section 8.
  - iii. Claims that the exclusion of certain fees from the finance charge violated the Truth in Lending Act.
- c. The nature of cases brought against settlement service industry members has changed over time.
  - i. State law claims are now often added to RESPA claims, or may be made in lieu of RESPA claims.
    - A. State laws often have longer statutes of limitations than the one-year period for private RESPA Section 8 lawsuits.
    - B. States often have laws that prohibit unfair and deceptive practices, which provide for generalized claims that certain conduct was unfair or deceptive.
  - ii. As the plaintiffs' bar has become more familiar with the settlement service industry, it is now challenging broader types of arrangements and conduct, such as affiliated business arrangements and marketing arrangements.

## **D. Recent Agency Settlements**

### **1. Referrals Conditioned on Things of Value**

- a. February 2007 HUD Settlement With Fidelity National Title Insurance Company (Fidelity). Relates to Settlement Discussed Below With Longford Homes of New Mexico, Inc. (Longford).
  - i. HUD states that it initiated an investigation of settlement service practices in the Albuquerque, NM market to determine, among other things, whether Fidelity's marketing arrangement with Longford, a homebuilder, complied with RESPA Section 8(a).
  - ii. HUD alleges that Fidelity provided prepaid "just sold" and "just listed" postal cards and listing agreements to real estate agents at no cost or below market cost, and gave other things of value to Longford in exchange for the referral of real estate settlement service business. HUD alleges that the other things of value included a prepaid postage meter, a periodic subsidy to cover Longford marketing expenses, retail store gift certificates, event tickets, and funds to cover the costs of dinners for Longford employees.
  - iii. Fidelity states that it does not agree with HUD's determinations, and the agreement provides that it does not constitute an admission of liability or fault on the part of Fidelity.
  - iv. Fidelity agreed to charge real estate settlement service providers fair market value for Fidelity's printing and other communication services, and with joint advertising to charge each provider whose goods or services are advertised its share of the advertising cost in direct proportion to its prominence in the advertising. Fidelity also agreed to pay \$68,635 to the United States.
- b. February 2007 HUD Settlement With Longford Homes of New Mexico, Inc. (Longford). Relates to Settlement Discussed Above With Fidelity National Title Insurance Company (Fidelity).
  - i. Longford is a homebuilder. HUD alleges that from 1999 to 2005 Longford received things of value in exchange for referrals of business to Fidelity. Specifically, HUD alleges that Longford accepted \$25,000 annually from Fidelity to pay for or be reimbursed for promotional expenditures, and that portions of the payments were used to provide Longford with a postage meter that had \$6,430 of prepaid postage (of which \$1,541 was used),

underwrite the costs of grand opening promotional events, provide Longford employees and customers with retail store gift certificates, lottery tickets and event tickets, subsidize the costs of dinners for real estate agents and Longford employees, and underwrite homeowner/customer seminars conducted by Longford.

- ii. Longford denies HUD's allegations. Longford also represents that its relationship with Fidelity was terminated as soon as possible upon the discovery that the arrangement could possibly violate RESPA, and that it has taken strict steps to ensure that no other similar action is engaged in by Longford or its agents. The agreement provides that it does not constitute an admission of liability or fault on the part of Longford.
  - iii. Longford agrees to not to enter into any agreements or arrangements through which Longford would accept from Fidelity or any other title insurance company gifts, opportunities or other things of value in return for the referral of title insurance business. Longford also agrees to pay \$20,700 to the United States.
- c. November 2005 HUD Settlement With 1-800 East-West Mortgage Company (East-West), with the FDIC as a signatory to the Settlement.
- i. East-West is a wholly-owned subsidiary of Commerce Bank & Trust Co. in Worcester, Massachusetts, and provides mortgage loan services in or about Massachusetts and the greater New England area.
  - ii. HUD and FDIC allege that East-West received, requested and/or was reimbursed for:
    - A. Tickets and premium seating to Boston Red Sox baseball games from settlement service providers in exchange for the referral of business.
    - B. Tickets and premium seating to New England Patriots football games from settlement service providers in exchange for the referral of business.
    - C. Restaurant gift certificates from settlement service providers in exchange for the referral of business.
    - D. Payment for charitable galas and other special events with the New England Patriots from settlement service providers in exchange for the referral of business.



- e. June 2006 HUD Settlement With R. Norman Peters and his law firm Peters & Sowydra (collectively “Peters”).
  - i. Relates to November 2005 Settlement With 1-800 East-West Mortgage Company (East-West).
  - ii. East-West provides mortgage loan services in or about Massachusetts and the greater New England area, and Peters served as a closing attorney for East-West.
  - iii. HUD alleges that Peters paid for and/or subsidized the purchase of tickets and premium seating to Boston Red Sox baseball games, tickets to a special event with the New England Patriots, and restaurant gift certificates for East-West, and lunch for all East-West employees, in return for the referral of business.
  - iv. HUD also alleges that Peters violated RESPA and/or aided and abetted others in violation of RESPA with respect to the alleged practices.
  - v. Peters denies that any payments or things of value provided to East-West were pursuant to any agreement or understanding that business would be referred.
  - vi. Peters agreed to pay \$7,500 to the United States.
  - vii. Peters agreed to cooperate with any HUD investigations of any settlement service providers who provided kickbacks or other things of value to East-West.

## **2. Affiliated Business Arrangements**

- a. January 2007 Consent Order With First American Title Insurance Company (First American). Both HUD and Minnesota Department of Commerce (Department) Are Parties.
  - i. The Consent Order addresses joint venture title companies operating in Minnesota. HUD and the Department allege that First American formed 35 joint venture title companies, retained a 20% interest in each company, and that the remaining 80% interest in the companies was held by various parties consisting of real estate agents, real estate brokerage firms, mortgage brokers, loan officers, builders or developers (the “Other Parties”).

- ii. HUD and the Department also allege that (A) the Other Parties and their associates were encouraged to direct their customers to a joint venture for closing and title services, (B) the title services of the joint ventures were not marketed to the general public or persons not related to the Other Parties, (C) the Other Parties' typical investment was \$500 per share, (D) if sufficient funds from operations were available, the Other Parties would receive quarterly distributions from the joint venture in which they invested, (E) First American managed the joint ventures without compensation for such services, (F) First American would hire, train and terminate employees of the joint ventures and directly supervise employees, (G) at times, certain of the joint ventures shared employees, and (H) certain of the joint ventures shared office space, supplies and equipment.
- iii. HUD and the Department state their position that First American committed certain violations of Minnesota insurance law and RESPA. Among other claims, HUD and the Department specifically state that: (A) First American created and controlled joint ventures that were not bona fide settlement service providers within the meaning of RESPA and, as a result, HUD and the Department contend that First American's distributions of the joint ventures' profits to the Other Parties violated RESPA and Minnesota law, and (B) First American, through the joint ventures, failed as the supervising agent to either completely or accurately disclose its affiliated business arrangement, and that this violated Minnesota law and failed to meet the requirements of the affiliated business arrangement exception.
- iv. First American contends that it operated the joint ventures in accordance with RESPA and Minnesota law.
- v. The Consent Order provides that it is an informal settlement of the allegations and that there have been no hearings, findings of fact or conclusions of law with respect to the allegations.
- vi. First American agreed to undertake an internal review of its rates with the objective of simplifying and clarifying them.
- vii. First American agreed to make available to the Department web-ready content for use by the Department on its website, including a Minnesota schedule of rates and rate calculator (that First American would update), a primer explaining title insurance and its role in real estate transactions, FAQs answering the most common questions consumers might have about title insurance,

and contact information for First American personnel in Minnesota available to answer consumer questions. First American also agreed to certain additional consumer education efforts.

- viii. First American agreed to pay a civil penalty of \$500,000 to the State of Minnesota.
- b. March 2007 Consent Order With American Residential Mortgage, LP (American). Both HUD and Minnesota Department of Commerce (Department) Are Parties.
- i. HUD and the Department allege that American failed to disclose its affiliated business arrangement with a title company in four files reviewed by the Department involving referrals to the company, in violation of RESPA.
  - ii. American agreed to cease and desist from further violations of RESPA, and to pay a civil penalty of \$5,000 to the State of Minnesota.
- c. March 2007 Consent Order With Gibraltar Title Agency, LLC (Gibraltar) and other parties (with Gibraltar, the “Respondents”). Both HUD and Minnesota Department of Commerce (Department) Are Parties.
- i. HUD and the Department allege that Gibraltar’s website incorrectly indicates that it is “an independent agency, unaffiliated with any lender, builder or real estate broker,” that the Respondents paid things of value for lender referrals of business, and that in certain instances Respondents failed to disclose their affiliated business arrangement with lenders in violation of RESPA and Minnesota law.
  - ii. The Respondents agreed to cease and desist from operating any further affiliated business arrangements that are not in compliance with Minnesota law and/or RESPA, and to surrender producer licenses for certain of the Respondents.
  - iii. The Respondents also agreed to reimburse \$100,000 to customers of certain of the Respondents that had processed a closing transaction originated by an affiliated business, and Gibraltar agreed to pay a civil penalty of \$10,000 to the State of Minnesota.

### 3. Title Reinsurance

a. In 2006 HUD entered into six separate settlement agreements in which it alleged that captive reinsurance companies were formed by parties in a position to refer title insurance business, and that title underwriters reinsured title insurance policies with the captive companies as a means to impermissibly provide a thing of value in return for the referral of title insurance business.

i. The settlement agreements are with:

A. AHT Reinsurance, Inc. and M.D.C. Holdings, Inc. (April 2006).

B. Chesapeake Title Reinsurance Company, Inc. and CitiMortgage, Inc. (July 2006).

C. WL Homes LLC, dba John Laing Homes (July 2006).

D. Shea Homes Limited Partnership and related entities and Shea Insurance Services, Inc. (September 2006).

E. William Lyon Homes and Duxford Title Reinsurance, Inc. (September 2006).

F. Fulton Homes Corporation and Fulton Homes Sales Corporation (October 2006).

ii. The settlement agreements are similar in nature, and provide for payments by the parties ranging from \$150,000 to \$950,000.

iii. By way of example, the settlement agreement with Fulton Homes Corporation and Fulton Homes Sales Corporation (collectively "Fulton Homes") provides as follows:

A. Fulton Homes builds homes in Arizona. HUD alleges that Fulton Homes refers homebuyers to certain companies for title insurance. HUD also alleges that on or about February 1, 2004, Fulton Homes joined as a participant in First American Homebuilders Reinsurance Company (FAHRC), a captive title reinsurance company that reinsures certain title insurance business.

B. HUD states its position that (1) it is a violation of RESPA Section 8(a) to accept a thing of value in the form of any

opportunity to participate in money-making captive title reinsurance arrangements in return for the referral of settlement service business to primary title insurance companies, and (2) any captive title reinsurance arrangements in which payments to the reinsurer are not bona fide and exceed the value of the reinsurance would violate RESPA Section 8.

- C. HUD further states that (1) in its view there is almost never any bona fide need or business purpose for title reinsurance on a single family residence, especially from an entity or an affiliate of an entity that is in a position to refer business to the primary title insurer, and (2) when there is a history of little or no claims paid or the premium payments to the captive reinsurer far exceed the risk borne by the reinsurer, there is strong evidence that there is an arrangement constructed for the purpose of payment of referral fees or other things of value in violation of RESPA Section 8.
- D. Fulton Homes states its position that (1) it participated in a captive title reinsurance program through FAHRC in good faith reliance on HUD's regulations, guidelines and interpretations of RESPA, including its 1997 and 2004 letters regarding reinsurance, and in compliance with applicable law, and (2) its participation was in compliance with applicable law and that its share of premiums received did not exceed the value of reinsurance provided and risk assumed.
- E. Fulton Homes represents that (1) title reinsurance was only extended in Arizona and (2) no new title reinsurance business was written after January 31, 2005.
- F. HUD made no finding of RESPA violations and noted that Fulton Homes cooperated with HUD.
- G. Fulton Homes agreed not to enter into any future captive title reinsurance arrangements, and to cease writing new captive title reinsurance business, but is not prohibited from conduct permitted by any changes to RESPA law or new HUD policy statements. Fulton Homes also agreed to pay \$150,000 to the United States.
- H. The agreement may not be construed as preventing Fulton Homes from unwinding the captive title reinsurance

arrangements, including without limitation the ceding of risk and/or premium to one or more third parties under terms and conditions that differ from the terms and conditions under which such risk and/or premium was obtained. Additionally, HUD will not consider such unwinding undertaken in conjunction with the agreement to be in violation of RESPA, provided that the unwinding does not involve an agreement or understanding for the referral of future settlement service business.

- b. There are various state settlements regarding captive title insurance arrangements, including a January 2007 Stipulation and Waiver—California Department of Insurance Settlement (the “Department”), First American Title Insurance Company and First American Title Company (collectively “First American”).
  - i. The Department states that it received complaints alleging illegal rebating activities by First American.
  - ii. Based on an examination of First American activities between February 2005 and February 2006, the Department alleges that during such time period First American (A) made cash payments to settlement service providers for the referral of title insurance business, (B) paid business support expenses, unrelated to the business of title insurance, of persons covered by California Insurance Code Section 12404 (12404 persons), which prohibits certain rebates and inducements for the placement or referral of title business, (C) paid the accommodations of and entertainment expenses for 12404 persons that were unrelated to the business of title insurance, (D) provided gifts, gift certificates, gift cards, and miscellaneous gifts and merchandise to 12404 persons as an inducement for the referral and placement of title business, (E) paid the food and beverage expenses of 12404 persons unrelated to the business of title insurance, and (F) paid the transportation expenses of 12404 persons unrelated to the business of title insurance.
  - iii. First American agreed to (A) cease activities that may be in violation of specific Insurance Code provisions, (B) comply with Insurance Code section 12404 regarding illegal rebates and inducements, (C) cease certain marketing activities, (D) have an officer review, monitor and certify compliance with the anti-rebate provisions of the Insurance Code with respect to the company’s business dealings with Frontier Homes, Inc., and (E) have an officer review, monitor and certify compliance with the anti-rebate

provisions of the Insurance Code with respect to the company's homebuilders division.

- iv. First American also agreed to pay (A) \$9,949,500 as a penalty, (B) \$45,500 for reimbursement of costs, and (C) \$5,000 for failure to comply with a prior order of the Department.

## E. LITIGATION

### 1. Yield Spread Premium

- a. *Culpepper v. Irwin Mortgage Corp.*, 491 F.3rd 1260 (11th Cir. July 2, 2007)—*Culpepper IV*.
  - i. This case challenging yield spread premiums began in the 1990s, and there have been three prior decisions by the United States Court of Appeals for the Eleventh Circuit. The fourth decision by the Court may finally lay this case to rest.
  - ii. In *Culpepper III*, the Eleventh Circuit certified a class and, in so doing, held that a lender must not show simply that a mortgage broker who received a yield spread premium performed some services; the lender must show that the services performed were directly tied to the yield spread premium. The Court relied on HUD's 1999-1 Statement of Policy, although the Court believed the Statement of Policy was ambiguous.
  - iii. Following *Culpepper III*, HUD issued Statement of Policy 2001-1 to clarify its position on yield spread premiums. In particular, HUD stated that each case involving a yield spread premium must be assessed based on the specific factual circumstances to determine if a yield spread premium was paid for services performed, and that the total compensation received by a broker should be measured against the total services performed by the broker.
  - iv. Based on the 2001 Statement of Policy, in *Culpepper IV* the Eleventh Circuit held that to assess the permissibility of a yield spread premium under RESPA Section 8(a), the Court first must examine if any compensable services were performed by the mortgage broker and, if so, the Court then must examine whether the total compensation received by the broker was reasonable in light of the services performed. There is no need for any services to be linked directly to the yield spread premium.

- v. The Eleventh Circuit rejected the plaintiffs' claims that (A) the absence of a reduction in their up-front closing costs as a result of the yield spread premium is sufficient to establish that the total compensation was unreasonable, and (B) broker compensation in excess of 1% of the loan amount is *per se* unreasonable.
  - vi. The Eleventh Circuit affirmed the district court's order that the lender was entitled to summary judgment, because the borrowers failed to present any evidence that the fees paid to the broker were "unreasonable in light of the total array of services performed." The Court further affirmed the district court's order decertifying a class, based on HUD's position in Statement of Policy 2001-1 that the legality of a yield spread premium must be assessed in light of the specific facts and circumstances of each individual borrower's transaction.
- b. ***Clifford v. FMF Capital, LLC***, 2007 WL 1701816 (W.D. Mich. June 11, 2007).
- i. The district court held that the mortgage broker, who received \$1,500 in origination fees and a \$1,200 YSP on a \$62,000 loan, violated Section 8(a) by accepting a YSP from the lender that was neither reasonable in amount nor related to actual goods or services. In granting the plaintiff's motion for summary judgment, the court held that the only "services" provided by the broker were consulting with the borrower, completing an application for a fixed rate conventional loan, completing a second falsified application for an adjustable rate mortgage that erroneously stated that the borrower was employed, and obtaining one sole lending offer for the borrower.
  - ii. Note that the court started its opinion by stating "The crooks in prison wear (orange jump suits) are easy to spot. Those in business wear are not; though they do no less harm to their unsuspecting victims."
- c. While RESPA clearly provides for the disclosure of the amount or range of charges in a Good Faith Estimate, some state regulators take the position that a yield spread premium must be disclosed as a specific dollar amount.

## 2. Builder Cases

The plaintiffs' bar has filed multiple putative class action lawsuits in various federal district courts alleging that homebuilders violated RESPA Sections 8(a) and 8(b) by requiring the use of the homebuilders' affiliated mortgage lending companies and title companies. In these suits, all brought by the same syndicate of law firms, the homebuilders offered discounts and rebates on home sales prices, upgrade packages, or closing costs on the condition that the homebuyers use the affiliates' settlement services. The homebuilders' disclosures to the buyers indicated that they were free to use a service provider of their choice. The plaintiff buyers contend that the offered incentives constitute a "required use," that precludes the homebuilders and their affiliates from relying on the RESPA Section 8(c)(4) affiliated business arrangement exemption. The homebuilders have argued on motions to dismiss that the buyers lack standing to sue because they have not alleged they paid any inflated settlement charges and, further, that the offering of the aforementioned types of discounts and rebates does not constitute a "required use" under Regulation X.

## 3. Flat-Fee Pricing

- a. *Price v. Landsafe Credit, Inc.*, 2006 WL 3791391 (S. D. Ga. Dec. 22, 2006).
  - i. The district court granted summary judgment for the defendants, holding that RESPA Section 8(a) does not prohibit companies from adopting a flat-fee pricing structure to recoup expenses of credit reports. The lender obtained credit reports from an affiliate. The affiliate charged the lender \$35 per transaction for credit reports if the loan closed, regardless of the number of credit reports provided. No fee was charged if the loan did not close.
  - ii. The plaintiffs claimed that by providing free credit reports for loans that did not close, the affiliate was providing a thing of value in return for the referral of credit report business in violation of the RESPA Section 8(a) referral fee prohibition. The court rejected this argument, holding that the business charge for overhead – including the cost of investigating potential borrowers' credit – was legitimate. The court compared the charge to charges for mortgage insurance that are passed through to borrowers, even though, in the court's view, the service does not benefit borrowers directly. The court considered its decision to be consistent with a prior decision of the United States Court of Appeals for the Ninth Circuit regarding the reasonableness of flat-fee price structures (*Lane v. Residential Funding Corp.*, 323 F.3d 739 (9th Cir. 2003).)

- ii. The plaintiffs have appealed to the United States Court of Appeals for the Eleventh Circuit, where oral argument was held on August 2, 2007. Meanwhile, similar suits are cropping up in other jurisdictions. How the Eleventh Circuit resolves the appeal may dictate how many additional attempts there may be to seek recovery under this theory and whether the industry will face another circuit split.
- iii. MBA has proposed a revision to RESPA Section 8 that would permit average-cost pricing.

#### **4. Sham Affiliated Business Arrangement Cases**

- a. *Jackson, Secretary of HUD v. Property I.D. Corp. et al.*, United States District Court for the Central District of California, CV 07-03372. Filed May 2007.
  - i. HUD filed the case against Property I.D. Corp. (Property I.D.) and other parties alleging that Property I.D. formed “sham” joint ventures with various real estate brokerage entities to funnel kickbacks to the entities in return for the referral of settlement service business, and for Property I.D. and the entities to split unearned fees.
  - ii. Property I.D. provides Natural Hazard Disclosure Reports, which are required in California. A key element in the case will be whether providing such reports is in fact a settlement service under RESPA.
  - iii. The day before HUD filed its complaint, Property I.D. filed a complaint against HUD in the same court seeking declaratory relief in connection with a HUD investigation of Property I.D. that was commenced in 2005.
    - A. Property I.D. sought a determination that by providing Natural Hazard Disclosure Reports, it does not render a settlement service that is covered by RESPA.
    - B. Property I.D. also sought a determination that RESPA Section 8 does not entitle HUD to seek disgorgement or restitution of funds in connection with seeking to enjoin a Section 8 violation. HUD maintains it can seek such disgorgement or restitution.

- C. Property I.D. further sought a determination that the definition of settlement services is unconstitutionally vague, and that if HUD is entitled to seek disgorgement or restitution, then RESPA is unconstitutional because it authorizes excessive penalties and violates due process.
  - iv. In July 2007, based on a prior order of the court, Property I.D. agreed to the dismissal of its suit without prejudice.
  - v. The judge handling the case also is handling the *Berger* case discussed below, which contains similar claims and was filed by a private party in 2005.
- b. ***Carter v. Welles-Bowen Realty et al.***, 493. F.Supp.2d 921 (N.D. Ohio 2007).

Plaintiffs' Attorneys: Murray & Murray.

- i. The named plaintiffs filed the case as a class action against Welles-Bowen Realty, Inc. (WB Realty), Welles Bowen Title Agency, LLC (WB Title), Welles Bowen Investors, LLC, Welles Bowen Mortgage, Inc., Fidelity National Financial, Inc. (Fidelity) and Chicago Title Insurance Company (Chicago).
- ii. The plaintiffs asserted that WB Realty, Fidelity and Chicago created WB Title as a sham affiliated business arrangement to provide kickbacks and other improper or illegal payments to WB Realty in exchange for referrals of settlement work to Chicago Title in violation of RESPA.
- iii. The court dismissed the case in May 2007. The court determined that the plaintiffs lacked standing to bring a RESPA Section 8 claim because they did not allege that they paid inflated charges for title insurance or settlement services, or that they suffered any other concrete injury.
- iv. The court rejected the plaintiffs' position that RESPA Section 8 provides for treble damages of the entire settlement fee, and determined that correct damages formula is three times the overcharge. The plaintiffs did not allege any overcharge and, thus, were not entitled to damages. Note different interpretations by courts of the damages available under RESPA Section 8 are discussed below—see the *Berger* and *Yates* cases and a statement by the court in the *Pettrey* case.

- c. ***Berger et al. v. Property I.D. Corp. et al.***, United States District Court of the Central District of California, CV 05-5373. Filed July 2005.

Plaintiffs' Attorneys: Lieff, Cabraser, Heimann & Bernstein, LLP. Among others.

- i. The named plaintiffs filed the case as a class action against Property I.D. Corp. (Property I.D.) and other parties. Property I.D. provides Natural Hazard Disclosure Reports, which are required in California.
- ii. The plaintiffs assert that certain real estate brokers formed joint ventures with Property I.D. cover up kickbacks or referral fees from Property I.D. to the real estate brokers in violation of RESPA.
- iii. The defendants filed various motions to dismiss. With respect to the RESPA claims, the defendants asserted that the RESPA Section 8 damages section permits recovery only to the extent that the fee paid by the plaintiffs was an overcharge, and that because the plaintiffs fail to allege an overcharge the RESPA claims should be dismissed. The defendants cited the *Carter* case discussed above to support their position.
- iv. On August 17, 2007, the court denied defendants' motions to dismiss the RESPA and other claims. The court held that by providing for damages equal to three times the charge for the settlement services "involved in the violation," a defendant is liable for three times the full charge for the specific services provided in connection with the RESPA Section 8 violation. The court went on to reject the defendant's argument that only the "illegal" portion of fee paid for each service involved in the violation is subject to the trebling provisions of RESPA. The court, thus, disagrees with the position of the court in *Carter* discussed above.

- d. ***Yates et al. v. All American Abstract Company, Inc. et al.***, United States District Court for the Eastern District of Pennsylvania, 2:06-cv-02174. Filed May 2006.

Plaintiffs' Attorneys: Quinn, Gordon & Wolf and Donald Searles.

- i. The named plaintiff filed the case as a class action against All American Abstract Company, Inc. (All American), Leo T. White, Philadelphia Federal Credit Union (PFCU), PFCU Services, LLC (PFCU Services) and PFCU Abstract, LLC (PFCU Abstract).

- ii. The plaintiff asserts that All American encouraged and assisted PFCU and PFCU Services to set up a sham affiliated business arrangement, PFCU Abstract, as a way to pay referral fees and kickbacks to PFCU and PFCU Services in violation of RESPA.
  - iii. Initially, the case was suspended in August 2006 pending mediation, and a motion to dismiss was filed in December 2006. In denying the defendants' motion to dismiss the RESPA claims, the court held that the plaintiff may seek three times the amount she paid for the settlement services, regardless of whether she paid a mark-up for the services. The defendants contended that the plaintiff could not receive as damages more than three times the amount of the alleged mark-up.
  - iv. Currently the parties are conducting discovery and the plaintiff's motion for class certification is due in October 2007.
- e. ***Benway et al. v. Resource Real Estate Services, LLC et al.***, United States District Court for the District of Maryland, WMN-05-03250. Filed October 2005.

Plaintiffs' Attorneys: Quinn, Gordon & Wolf.

- i. The named plaintiffs filed the case as a class action against Resource Real Estate Services LLC (Resource), Access One Mortgage Group (Access) and Clipper City Settlement Services, Inc. (Clipper).
- ii. The plaintiffs assert that Resource encourages and assists mortgage brokers, including Access, to set up sham affiliated business arrangements, such as Clipper, to pay referrals fees and kickbacks for referrals of title services in violation of RESPA and Maryland law.
- iii. The court granted the plaintiffs' motion to certify a class in October 2006.
- iv. The court denied the plaintiffs' attempt to have the class include consumers whose transactions had occurred within three years of the case filing. The plaintiffs asserted that the three-year period was appropriate because their civil conspiracy claim under Maryland law was governed by the general three year statute of limitations in Maryland. The court concluded that the one-year statute of limitations under RESPA was the appropriate time

period, because the civil conspiracy claim was based on the asserted violation of RESPA.

- f. ***Pettrey v. Enterprise Title Agency, Inc. et al.***, United States District Court for the Eastern Division of the Northern District of Ohio, 1:05-cv-1504. Filed May 2005.

Plaintiffs' Attorneys: Fair Housing Law Clinic; Richard Gordon, Quinn, Gordon & Wolf.

- i. The named plaintiffs filed this case as a class action against Enterprise Title Agency (Enterprise), First USA Title Agency, LP (First USA), John DeSantis and John Doe(s).
- ii. The plaintiffs assert that Enterprise set up sham affiliated business arrangements, such as First USA, with real estate agents, such as Mr. DeSantis, as a way to allow real estate agents to earn fees for referrals of title and closing work, under the guise of a return on an investment, in violation of RESPA.
- iii. The court denied the plaintiffs' motion for class certification in December 2006. In connection with addressing the class certification issue, the court noted that damages under RESPA Section 8 are based on the total amount paid for the settlement services
- iv. The court denied the plaintiffs' motion to reconsider the class certification decision in March 2007.

## **5. Marketing Arrangement Case**

- a. ***Shahan et al. v. Tower City Title Agency, Inc. et al.***, United States District Court for the Northern District of Ohio, 1:05-cv-01983. Filed August 2005.

Plaintiffs' Attorneys: Quinn, Gordon & Wolf.

- i. The plaintiffs allege that the defendants Tower City Title Agency, Inc. and Tower City Title Agency, LLC entered into "marketing agreements" with mortgage brokers who were in a position to send title and escrow business to the defendants, and that the defendants paid referral fees to mortgage brokers that were disguised as "promotional fees" under the marketing agreement in violation of RESPA.

- ii. The court preliminarily accepted a settlement agreement in January 2007, and approved the settlement in April 2007.
- iii. The settlement agreement provides that the defendants will (A) enter into a consent order prohibiting the use of marketing agreements or otherwise prohibiting the making of payments to any mortgage broker, lender or other person pursuant to any agreement or understanding that settlement service business shall be referred to any person, and (B) pay \$900,000 into a settlement fund, plus any unpaid balance of an insurance policy available to the defendants that may exist at the time of final approval of the settlement.

## 6. Mark-Up Related Cases

- a. *Wooley et al. v. Countrywide Home Loans, Inc. et al.*, United States District Court for the Southern District of Alabama, 1:06-cv-00835. Filed December 2006.

Plaintiffs' Attorneys: Earl Underwood; George Irvine, Stone, Granade & Crosby; Kenneth Reimer.

- i. The named plaintiffs filed the case as a class action against Countrywide Home Loans, Inc. (Countrywide), First Franklin Financial Corporation (First Franklin), First National Financial Title Services of Alabama, Inc. (First National) and Fidelity National Title Insurance Company (Fidelity National).
- ii. The plaintiffs assert that the title insurance premium that they were charged exceeded the maximum allowed premium set by the Alabama Department of Insurance, and that the premium was marked-up and split by First National and Fidelity National in violation of RESPA.
- iii. The plaintiffs assert that the Truth in Lending Act disclosure provided by First Franklin violated the act by failing to include the amount of the title insurance premium, and that First Franklin, as the lender, and Countrywide, as the assignee of the loan, are both liable for the violation.
- iv. In March 2007 the court granted a joint motion to dismiss the lawsuit without prejudice.

- b. *Dempsey v. Swafford Settlement Services, Inc.*, United States District Court for the Southern District of Alabama, 1:06-cv-00754. Filed November 2006.

Plaintiffs' Attorneys: Earl Underwood; George Irvine; Kenneth Reimer.

- i. The named plaintiff filed the case as a class action against Swafford Settlement Services, Inc. (Swafford).
- ii. The plaintiff asserts that Swafford marked-up third party settlement service costs in violation of RESPA.
- iii. The case is stayed pending resolution of issue of liability insurance coverage for the plaintiff's claims.

- c. *Lemley et al. v. Liberty Title Insurance Company, LLC et al.*, United States District Court for the Northern District of Alabama, 7:06-cv-02076. Filed October 2006.

Plaintiffs' Attorneys: Earl Underwood; George Irvine, Stone, Granade & Crosby; Kenneth Reimer; Milton Brown, Jr.; Knox McLaney, McLaney & Associates.

- i. The named plaintiffs filed the case as a class action against Liberty Title Insurance Company, LLC and First American Title Insurance Company.
- ii. The plaintiffs assert that the defendants marked-up third party settlement service costs in violation of RESPA.
- iii. Specifically, the plaintiffs assert that they were charged (A) amounts for a title search, title examination, and recording costs that exceeded the actual third party costs, and (B) an amount for title insurance that exceeded the rate approved by the Alabama Department of Insurance.
- iv. A motion to dismiss is pending.
- v. With regard to the challenge to the amount charge to title insurance, certain of the plaintiffs' attorneys were involved in another case in which same claims was raised. While the plaintiffs alleged that by charging more than filed rate the title insurance company marked-up the title insurance charge in violation of RESPA Section 8(b), the title company was successful in having the case dismissed on the grounds that the plaintiffs were alleging

an overcharge that does not violate RESPA Section 8(b). *Morrisette v. NovaStar Home Mortgage, Inc.*, 484 F.Supp.2d 1227 (S.D. Ala. Apr. 19, 2007).

## 7. Fiduciary Duty Case

- a. *Grady et al. v. Burnet Realty Inc. dba Coldwell Banker Burnet*, District Court for the Fourth Judicial District of Minnesota. Filed February 2007.

Plaintiffs' Attorneys: Zimmerman Reed; University of Minnesota Law School Consumer Protection Clinic; Crowder Teske.

- i. The named plaintiffs filed the case as a class action against Burnet Realty (Burnet).
- ii. The case is not based on RESPA Section 8, likely because the underlying real estate transaction for the named plaintiffs occurred in 2003, which is well outside the one year statute of limitations.
- iii. The plaintiffs assert that they retained the real estate brokerage services of Burnet as a buyer broker in connection with the purchase of a residence, and that Burnet referred them to an affiliate, Burnet Title, for title insurance and closing services.
- iv. The plaintiffs assert that they paid Burnet fees and premiums for the title insurance and services provided, and that:
  - A. The fees charged were higher than the fees charged by other providers in the same market for the same or comparable title insurance and closing services.
  - B. The fees and charges are among the highest, if not the highest, in the State of Minnesota.
  - C. Burnet knew that there were lower priced alternatives to Burnet Title for the same or comparable goods and services.
- v. The plaintiffs also assert that Burnet did not disclose material facts related to the referral of the plaintiffs to Burnet. Specifically, the plaintiffs assert that Burnet did not disclose:
  - A. The availability of lower priced providers of title insurance and closing services.
  - B. That Burnet Title has some of the highest fees and rates for title insurance and closing services in Minnesota.

- C. That it pressures and trains its sales associates to steer clients to Burnet Title for title insurance and closing services.
  - D. That it provides financial incentives to its sales associates to steer clients to Burnet Title for title insurance and closing services.
- vi. The plaintiffs claim that Burnet owed the plaintiffs and the other asserted class members fiduciary duties under Minnesota statutes and common law, and that Burnet breached those duties by virtue of the asserted conduct set forth above.
  - vii. The plaintiffs also claim that Burnet's failure to disclose to its clients all material facts regarding its arrangements for title insurance and closing services for the clients constitutes a fraud, misrepresentation or deceptive practice under the Minnesota Consumer Fraud Act.
  - viii. The class that the plaintiffs seek to represent consists of Minnesota citizens who during the six years before the complaint was filed:
    - A. Were the purchaser in a residential real estate transaction in the counties of Hennepin, Ramsey, Scott, Anoka, Washington, Dakota or Carver;
    - B. Entered into a buyer representation or listing contract with Burnet for buyer's representation, seller's representation or dual representation;
    - C. Were referred to Burnet Title; and
    - D. Paid for the goods, insurance and/or services provided by Burnet Title.
  - ix. A class certification hearing is scheduled for November 2007.

## II. TRUTH IN LENDING ACT

### A. LITIGATION

#### 1. Availability of Rescission in a Class Action

- a. *Andrews v. Chevy Chase Bank, FSB*, 2007 WL 112568 (E.D. Wisconsin, January 16, 2007).

- i. Borrowers alleged that the lender: (A) failed to properly disclose the payment schedule because the schedule did not reflect that the required payments were due monthly; (B) did not clearly disclose the APR and variable rate feature, based in part on disclosures reflecting a note rate of 1.950% and a five year fixed period that applied to the payment and not the rate; (C) added information to the TILA disclosure that was not directly related to the information required to be disclosed (i.e., the initial discounted interest rate of 1.950% set forth as the note rate); and (D) failed to properly disclose the possibility of negative amortization.
  - ii. The federal district court agreed with the first three allegations and determined that the loan was rescindable because of the violations. The court further determined that this matter was appropriate for class certification, finding nothing in the language of the TILA that precludes the use of the class action mechanism to obtain a judicial declaration of whether a TILA error entitles each member of the class individually to seek rescission.
  - iii. The MBA and other industry trade groups have filed an amici curiae brief requesting that the United States Court of Appeals for the Seventh Circuit overturn the class certification. Arguments are scheduled for September 26, 2007.
  - iv. *Andrews v. Chevy Chase, FSB*, 2007 WL 1556537 (E.D. Wisconsin, May 25, 2007).
    - A. Although the class certification ruling is on appeal to the Seventh Circuit, the plaintiffs filed a motion with the district court for a determination of whether the filing of the class action tolled the running of the extended three-year rescission period.
    - B. The court indicated that the three-year rescission period is a statute of repose rather than a statute of limitations, and that while equitable tolling does not apply to statutes of repose, legal tolling does.
    - C. The court determined that the filing of the class action by the plaintiffs tolled the three-year period to rescind for all the class members.
- b. *LaLiberte v. Pacific Mercantile Bank*, 147 Cal. App. 4th 1 (4th Dist. Cal., January 25, 2007)

- i. The borrowers filed suit alleging that the exclusion of \$450 in closing fees from the Truth in Lending disclosures with each of their loans violated the TILA, and later amended the complaint to include class allegations, including the right to rescind on a class basis.
  - ii. The California appellate court held that rescission is a personal remedy under the TILA and should not be given class treatment. The court found it difficult to believe that Congress would carefully balance the deterrent effects of class actions under the TILA against the potential harm to businesses in the context of statutory damages, and yet allow class action rescission to proceed without any safeguard. The court also noted that with 100 class members, the lender could face the loss of over \$37 million in security if rescission were allowed on a class basis.
  - iii. The borrowers filed a petition for certiorari on August 7, 2007.
- c. ***McKenna v. First Horizon Home Loan Corp.***, 475 F.3d 418 (1st Cir., January 29, 2007).
- i. The borrowers filed suit alleging that the lender inaccurately disclosed information pertaining to their rescission rights and had failed to appropriately respond to their requests for rescission in violation of the TILA and its Massachusetts counterpart, the Massachusetts Consumer Credit Cost Disclosure Act (MCCCDCA). The borrowers asserted that the violations entitled them to statutory damages and rescission, and sought a declaration that any class member who so elected could rescind.
  - ii. The United States Court of Appeals for the First Circuit reversed the district court's 2006 decision certifying class treatment of the rescission claim, finding class certification is not available for rescission claims, whether direct or declaratory, under the TILA or the MCCCDCA. The First Circuit stated that the rescission process is intended to be private, with the creditor and debtor working out the logistics of a given rescission.
  - iii. In addressing the express cap on statutory damages for class actions and the absence of any express class action provision in connection with rescission, the First Circuit stated that "Congress either may have intended rescission to be totally unavailable as a class remedy in the TILA milieu or it may have intended rescission class actions to be available unrestrainedly in TILA cases, not

subject to any special limiting conditions. We find the first alternative to be much more likely.”

- d. ***In re Ameriquest Mortgage Co. Mortgage Lending Practices Litigation***, 2007 WL 1202544 (N.D. Illinois April 23, 2007).
  - i. In a class action the plaintiffs sought a declaration that the members of the class involving claims that the defendants failed to provide material TILA disclosures have the right to rescind their loan transactions. The defendants moved to dismiss the on the basis that rescission is not susceptible to class relief.
  - ii. The court disagreed with the decision of the United States Court of Appeals for the First Circuit in *McKenna* discussed above, finding that nothing in the TILA precludes declaratory relief authorizing class members to individually request rescission when they are legally entitled to do so.
- e. ***Murry v. America’s Mortgage Banc, Inc.***, 2006 WL 1647531 (N.D. Ill. June 5, 2006).
  - i. The court denied a plaintiff’s motion to certify a class with regard to a rescission claim based on grounds specific to the case. The issue of whether or not a rescission claim may proceed on a class action basis was not addressed.
  - ii. The case settled on March 12, 2007.

## **2. Right to Rescind After Loan Pay-Off**

- a. ***Barrett v. JP Morgan Chase Bank, N.A.***, 445 F.3d 874 (6th Cir., April 18, 2006).
  - i. The borrowers refinanced their mortgage with Bank One in May 2000 and again in January 2001. In May 2001, the borrowers refinanced the loan with another lender, and Bank One released its security interest in their home. The borrowers requested that the Bank One loans be rescinded based on alleged TILA violations. Bank One responded that because both loans were refinanced, and the security interest released, there was nothing left to rescind.
  - ii. The district court agreed with Bank One, but the United States Court of Appeals for the Sixth Circuit reversed. The Sixth Circuit stated that nothing in the TILA or its implementing regulations provides that the act of refinancing extinguishes an unexpired right

to rescind, and that the right to rescind gives consumers the right to recover fees in addition to the right to the release of the security interest.

b. ***Handy v. Anchor Mortgage Corp.***, 464 F.3d 760 (7th Cir., September 29, 2006).

i. The borrower obtained a refinance mortgage loan from Anchor Mortgage and was provided with five copies of a notice of right to cancel. Four of the notices followed the Federal Reserve Board's H-9 model form (refinancing with original creditor) and one followed model form H-8 (general). The H-8 form was the correct form for the transaction. The borrower sought to rescind the transaction two years later on the basis that the rescission notices were not clear and conspicuous. While the case was pending, the borrower died and the administrator of her estate was allowed to substitute as plaintiff.

ii. The district court denied the rescission claim on the grounds that if the borrower wanted to rescind following the closing, she could have used either of the forms to do so. The United States Court of Appeals for the Seventh Circuit disagreed, finding that the provision of two versions of the rescission notice violated the clear and conspicuous notice requirement, especially with regard to the effects of rescission.

A. See the discussion below regarding the *Santos-Rodriguez* case what rejects *Handy* with regard to the use of the incorrect form of notice.

iii. The lender argued that rescission was inappropriate, and maybe even impossible, because the estate of the borrower had recently repaid the loan. The Seventh Circuit agreed with the "well-reasoned opinion" of the Sixth Circuit in *Barrett* and held that even though the loan had been paid in full, a transaction containing a TILA violation is rescindable even after the loan is paid off.

c. ***Pacific Shore Funding v. Lozo***, 138 Cal. App. 4th 1342 (2d Dist. Cal., Apr. 27, 2006).

i. The borrowers obtained a refinance loan subject to the Home Ownership and Equity Protection Act (HOEPA). Almost two years later the borrowers refinanced the loan. The borrowers then attempted to rescind the first loan on the grounds that the rescission notice did not include the date of the transaction or the

deadline for rescission, and that lender failed to comply with the HOEPA pre-closing disclosure requirements.

- ii. The borrowers filed suit after the lender rejected the rescission demand, and the trial court, following the decision of the United States Court of Appeals for the Ninth Circuit in the 1986 case *King v. State of Cal.*, denied the claim on the grounds that once a loan is refinanced there is nothing left to rescind. The appellate court declined to follow *King*, and instead followed *Barrett* and other cases in holding that the right to rescind survived the refinance of the loan. The court noted that the borrowers still had something to rescind, namely the interest, fees, penalties and charges paid under the first loan.
- iii. A motion for review was denied on July 19, 2006.

### 3. Other Rescission Issues

- a. *American Mortgage Network, Inc. v. Shelton*, 486 F.3d 815 (4th Cir. May 14, 2007).
  - i. The borrower obtained a refinance loan from the lender. About a month after the loan closing, the borrower received documents from the lender noting an error in the original TILA disclosure, and including a new TILA disclosure and notice of right to cancel. Believing there to be various discrepancies with the documents, the borrower rescinded the loan.
  - ii. Within 20 days of receipt of the notice of cancellation, the lender confirmed that it was prepared to unwind the transaction, upon receipt of confirmation from the borrower that he was prepared to return the net loan proceeds. The borrower offered to sell the house to the lender. The lender declined the offer and asserted that the offer did not constitute a proper tender.
  - iii. The borrower's counsel asserted that the lender was required under the TILA to release its security interest on the house immediately without a specific agreement on the borrower's part to return the net loan proceeds. The lender disagreed. After the borrower obtained new counsel, the counsel asserted that the lender had forfeited the loan proceeds by refusing to unconditionally release its security interest within 20 days of cancellation of the loan as required by the TILA. The lender then filed suit seeking a modification of the TILA rescission procedures and an order declaring its full compliance with the TILA.

- iv. The district court granted the lender's motion for summary judgment. The United States Circuit Court of Appeals for the Fourth Circuit affirmed the district court's decision. The Fourth Circuit stated that the borrower claims "the right to simply walk away with a windfall of \$313,468 without any further obligation. This construction [of the TILA rescission section] not only offends traditional notions of equity, but misinterprets the procedural requirements of [the section]."
  - v. The Fourth Circuit stated that the equitable goal of rescission under the TILA is to restore the parties to the "status quo ante." The court further stated it adopted the majority view of reviewing courts that unilateral notification of cancellation does not automatically void the loan contract.
- b. *In re Groat*, 369 B.R. 413 (8th Cir. Bankruptcy, May 24, 2007).
- i. A loan to the borrower was closed on September 5, 2002, and the notice of right to cancel identified the rescission deadline as September 10, 2001 instead of September 10, 2002. The borrower notified the lender in July 2005 that based on defects, including the incorrect date, he was rescinding the loan. The borrower also alleged that once he tendered the rescission notice, the rescission was automatic, and the lender would have to file a declaratory judgment action to challenge the rescission.
  - ii. With regard to the claim that rescission is automatic, among other findings that are particular to the facts of the case, the Eighth Circuit noted that it has previously held that rescission is not automatic and that a court may condition rescission on the borrower's return of the principal.
  - iii. With regard to the date error in the notice of right to cancel, the bankruptcy court determined that that error did not trigger the extended three-year rescission period. The Eighth Circuit stated that the TILA provides a safe harbor for unintentional violations that result from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error. The court noted the procedures used by the lender's attorney to prepare a notice of right to cancel, and agreed with the bankruptcy court that the error fell within the safe harbor. The court stated that from the vantage point of the hypothetical average consumer, the defect was not misleading because anyone reading the document would

know that the cancellation deadline could not have passed a year before the document was even executed.

- c. *Santos-Rodriguez v. Doral Mortgage Corp.*, 485 F.3d 12 (1st Circuit, April 19, 2007).
- i. Plaintiffs obtained loans from the lender and asserted that they were entitled to rescind during the extended three-year rescission period because the lender (A) provided a notice of right to cancel based on the model H-8 form for a new lender refinancing instead of the model H-9 form for a same lender refinancing, and (B) the notice of right to cancel did not adequately explain the effects of rescinding a same lender refinancing. The district court granted the lender's motion to dismiss. The United States Court of Appeals for the First Circuit affirmed the dismissal of the plaintiffs' claims.
  - ii. With regard to the claim that the wrong model notice was used, the First Circuit stated that the TILA and Regulation Z do not require exclusive use of the model forms and that, therefore, the alleged failure to provide the appropriate model form is not a per se violation.
  - iii. With regard to the claim that the notice did not adequately explain the effects of rescinding a same lender refinancing, the First Circuit first addressed the plaintiffs' argument as to why the notice was misleading. The plaintiffs claimed that the notice did not disclose that if a same lender refinance transaction is rescinded, the original loan is not cancelled, the lender retains the security interest under the original loan, and the borrower reverts to paying off the original loan. The plaintiffs also asserted that a consumer would be less willing to rescind a same lender refinance loan if he or she believed that doing so would require immediate repayment of the original loan.
  - iv. The First Circuit concluded that the lender had clearly and conspicuously informed the plaintiffs of their rescission right and the effects thereof in compliance with Regulation Z. The court stated that, from the vantage point of the hypothetical average consumer, because the plaintiffs were told clearly and conspicuously that rescission would operate as to their pending refinance transaction, any conclusions that they might have drawn from that disclosure about their previously existing mortgage were unreasonable. The First Circuit declined to follow *Handy*, discussed above, noting the facts in that case were very different,

and that *Handy* “adopts a hyper-technical compliance requirement, a position we have rejected.”

- d. *In re Nutase*, 2007 WL 1704392 (Bankruptcy, D. Maryland, June 11, 2007).
- i. The plaintiffs obtained a refinance loan from a lender that closed on January 5, 2005. The notice of right to cancel received by the plaintiffs correctly identified midnight on January 8, 2005 as the time that the right to rescind expired. On January 10 at 5:18 p.m. the plaintiffs sent a handwritten notice by facsimile to the lender advising that they wished to cancel the loan, and they dated the notice January 8. They also sent the notice by Federal Express for overnight delivery, and this notice was received by the lender on January 11.
  - ii. The lender had disbursed the loan on January 10, and did not honor the rescission request. The plaintiffs argued that the three-day rescission period was extended because the lender failed to wait to disburse the loan proceeds until the time that it would have received a notice that was timely mailed.
  - iii. The court stated that a lender “is required to delay performance for a reasonable period after expiration of the rescission period to allow for delivery of a mailed notice of rescission.” Note, the actual language of Regulation Z provides that the lender should not perform “until the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded.”
  - iv. The court rejected the plaintiffs’ interpretation of the delay of performance provision. The court stated that the plain reading of the TILA is that a consumer is given three business days to rescind the transaction, and the lender’s failure to delay performance is of no consequence if the right to rescind has expired and the lender has not acted in such a way as to thwart the consumer’s right to rescind.
  - v. The court did not rule on whether the lender had or had not delayed performance for an appropriate period, and stated that had the lender delayed performance until the rescission notice was received, the lender would not have been required to honor the notice because the notice was not sent timely.
- e. *Antanuos v. First National Bank of Arizona*, 2007 WL 1378543 (E.D. Virginia, May 7, 2007).

- i. The plaintiffs obtained a refinance loan on commercial rental property, and at the closing received the notice of right to cancel. The plaintiffs asserted that they properly rescinded the loan, and filed suit when the lender did not agree to the alleged rescission.
  - ii. The plaintiffs acknowledged that they did not have a right to rescind under the TILA because the security property was not their principal dwelling. The plaintiffs argued that because the lender provided them with the notice of right to cancel, legal principles of waiver and estoppel prohibited the lender from claiming that they did not have the right to rescind.
  - iii. The court determined that the plaintiffs did not have the right to rescind simply because the lender provided them with the notice of right to cancel. Although noting that the provision was not directly on point, the court cited the portion of the Regulation Z Commentary regarding the business loan exemption that provides that if some question exists as to the primary purpose of a credit extension, the creditor is, of course, free to make the TILA disclosures, and the fact that the disclosures are made under such circumstances is not controlling on the question of whether the transaction is exempt from the TILA.
  - iv. The court stated it is reasonable that in some circumstances a creditor may not know whether its security interest constitutes the debtor's principal dwelling or not, and that a creditor may provide a debtor with notice of the right to rescind, even if no such right exists in fact because the property is not the debtor's principal dwelling. In such a case, the disclosure is not controlling on whether the transaction is exempt.
  - v. It appears as if the court read the TILA exemption for credit transactions exceeding \$25,000 to exempt mortgage loans over \$25,000 that are secured by real estate that is not the primary dwelling of the borrower. The exemption provides that the TILA does not apply to "An extension of credit not secured by real property, or by personal property used or expected to be used as the principal dwelling of the consumer, in which the amount financed exceeds \$25,000 or in which there is an express written commitment to extend credit in excess of \$25,000."
- f. *Saygnarath v. BNC Mortgage, Inc.*, 2007 WL 1141495 (D. Minnesota, April 17, 2007).

- i. The court addressed the plaintiffs' motion for a temporary restraining order to enjoin execution of an eviction order. Thus, the court's decision was in the context of whether the plaintiffs were likely to succeed on the merits of the case.
  - ii. The plaintiffs obtained a loan from the lender in August 2005 and, after defaulting, the loan was foreclosed, with the lender obtaining the property at the foreclosure sale in June 2006. The plaintiffs filed suit in August 2006 asserting TILA violations and claiming the right to rescind. The plaintiffs also asserted that they had sent a rescission letter. The letter was never produced, although the plaintiffs' counsel conceded that the letter was sent after the foreclosure sale.
  - iii. The court determined that because the right to rescind based on a TILA violation expires three years after consummation, upon transfer of all of the consumer's interest in the property or upon sale of the property, whichever first occurs, the right expired upon the foreclosure sale. (The court noted that the plaintiffs did not exercise their six-month redemption right.)
- g. ***Bills v. BNC Mortgage, Inc.***, 2006 WL 3227887 (N.D. Illinois, November 3, 2006).
- i. The borrower, who was married, obtained a refinance loan. The borrower's wife did not attend the closing, or receive or sign any documents, as the borrower was the sole owner of the property and sole borrower. The couple later sought to rescind the loan on the grounds that the wife had not received a notice of the right to cancel. The couple argued that the wife was a consumer entitled to receive the notice of the right to cancel because she held homestead rights in the property.
  - ii. Based on other cases, the district court determined that under Illinois law homestead rights are merely rights of possession and do not rise to the level of an ownership interest and, therefore, the wife was not a consumer entitled to receive a notice of the right to rescind. The court granted the defendant's motion to dismiss.
- h. ***Bills v. BNC Mortgage, Inc.***, 2007 WL 1438371 (N.D. Illinois, May 11, 2007).
- i. The plaintiffs in the first *Bills* case discussed above filed an amended complaint. Among other motions by the defendants, the

servicer of the loan (which never owned the loan) filed a motion to dismiss the complaint with respect to it.

- ii. The court noted that at least three courts in the district had previously ruled that a current servicer of a loan should not be dismissed in a suit for rescission because the servicer is a necessary defendant under Federal Rules of Civil Procedure. The prior courts noted that dismissing the servicer could impair the borrower's ability to fully protect his or her interest because the servicer could improperly report to credit bureaus or foreclose on the loan.
  - iii. The court disagreed with the prior decisions. Noting a statement by another a court that a servicer's interest automatically ceases upon rescission, the court stated that any concern that the servicer might thereafter engage in improper reporting to the credit agencies or attempt to foreclose a rescinded loan is purely speculative and does not warrant retaining the servicer as a defendant.
- i. ***Bank of New York v. Conway***, 916 A.2d 130 (Superior Court of Connecticut, December 13, 2006).
    - i. A married couple obtained a refinance loan that was closed on March 22, 2000. The named defendant-borrower signed the note, but did not sign the mortgage as he did not have any ownership interest in the property at the time of closing. On March 27, 2000, the borrowers signed and returned a document certifying that they had not exercised the right to rescind. On March 28, 2000, the borrower who owned the property executed a quitclaim deed that conveyed the property to herself and her husband. The husband then added his signature to the mortgage. After the borrowers defaulted, they were sent a demand letter. In response, the husband returned a notice of the right to cancel seeking to rescind the loan. A foreclosure action was commenced and the note holder moved for summary judgment.
    - ii. The borrowers asserted that the signing of the mortgage by the husband after closing constituted a separate transaction that entitled him to receive a separate notice of the right to cancel. As special defenses the borrowers asserted that the loan was rescinded, that the lender had failed to follow the rescission procedures, and that the lender had failed to disclose an \$80 recording fee and had padded a \$475 appraisal fee. The note holder claimed that the assertions regarding the fees were false.

- iii. The court determined that the husband's signing of the mortgage did not constitute a separate transaction that triggered the right to receive a notice of the right to cancel. With regard to the borrower's special defenses based on the recording and appraisal fees, although the facts were in dispute, the court, following prior state court decisions, determined that even if the allegations were true the right to foreclose would not be defeated. The court stated that violations of the TILA's disclosure provisions are not valid special defenses in a mortgage foreclosure action because such violations do not relate to the validity of the note or mortgage, but rather relate to the conduct of the lienholder.
  
- j. *Palmer v. Champion Mortgage*, 465 F.3d 24 (1st Cir., September 29, 2006).
  - i. The borrower obtained a debt consolidation loan that was closed on March 28, 2003. On that date the borrower signed the loan documents, TILA disclosure statement and settlement statement, but did not receive copies of the documents. In early April the borrower received by mail copies of the closing documents, and the notice of the right to cancel. The notice provided that the borrower had the right to cancel within three business days of the last to occur of (A) the date of the transaction, which was stated to be March 28, 2003, (B) the date of receipt of the TILA disclosures or (C) date of receipt of the cancellation notice. The notice also provided that to cancel, the cancellation notice must be sent no later than April 1, 2003 or midnight of the third business day following the latest of the three listed events. In August of 2004 the borrower attempted to rescind the transaction, and the lender did not respond. The borrower then filed suit claiming that the inclusion in the cancellation notice of the April 1 deadline was confusing and entitled her to a continuing right to rescind.
  
  - ii. The district court granted the lender's motion to dismiss. Citing other cases, the United States Court of Appeals for the First Circuit stated that the court must refrain from crediting the plaintiff's bald assertions, unsupported conclusions and opprobrious epithets, and that courts must evaluate the adequacy of TILA disclosures from the vantage point of a hypothetical average consumer, which the court described as a consumer who is neither particularly sophisticated nor particularly dense. The First Circuit stated that it failed to see how any reasonable consumer would be drawn to the April 1 deadline without grasping the twice-repeated alternate deadlines, and affirmed the dismissal of the case.

- k. *Moore v. Cycon Enterprises, Inc.*, 2007 WL 475202 (W.D. Michigan, February 9, 2007).
  - i. The borrowers rescinded a mortgage transaction under the TILA. At issue was whether borrowers were required to tender the full original principal loan amount or the principal loan amount less the loan origination fee, underwriting fee and settlement fee that the borrowers financed.
  - ii. The court noted that the TILA and Regulation Z provide that upon rescission, a consumer is not liable for any amount, including any finance charge. The court held that the borrowers were not required to pay any charges related to the transaction, even if such fees were financed by the lender. Thus, the borrowers were required to return the principal, less the amount of the fees that were financed.
- l. *Tucker v. Beneficial Mortgage Company*, 437 F.Supp.2d 584 (E.D. Virginia, July 7, 2006).
  - i. In October 2003, the borrowers joined a class action settlement with the lender that was negotiated by the Virginia Attorney General. The settlement released the lender from liability for “all civil claims and causes of action...whether known or unknown.” In September 2004, the borrowers attempted to rescind their loan with lender based on alleged TILA and HOEPA violations. The court found that because borrowers joined in the class action settlement, they were barred from rescinding the loan.

#### **4. Payoff Fees**

- a. *McAnaney v. Astoria Financial Corp.*, 2006 WL 2689621 (E.D.N.Y., September 19, 2006).
  - i. Three married couples obtained loans made or acquired by the defendant. In connection with the payoff of their loans, the couples assert that they received a letter from the defendant demanding fees such as an attorney document preparation fee, a facsimile fee and a recording fee. The couples brought a class action against the defendant challenging the fees.
  - ii. The district court noted that the defendant used Fannie Mae/Freddie Mac uniform instruments that provided there would be no prepayment penalties or fees, and that the TILA disclosures

did not disclose the disputed fees as prepayment penalties or finance charges. The court granted the motion of the couples to certify a class.

## 5. Reissue Rate

- a. *In re Glauser*, 365 B.R. 531 (Bankruptcy, E.D. Pennsylvania, April 3, 2007).
  - i. The plaintiffs obtained a refinance loan from the lender and were charged for title insurance at the basic rate. The plaintiffs then filed an adversary proceeding claiming that because they already had a title insurance policy, they should have been charged the lower reissue rate and, as a result, the charge for title insurance was unreasonable and should have been included in the finance charge.
  - ii. The parties in the case agreed that the Manual of Title Insurance Rating Bureau of Pennsylvania in effect at the time the loan was made established the prevailing rates and, thus, the “reasonable” rates for purposes of the proceeding. However, the parties disagreed on which rate was applicable. The basic rate paid by the plaintiffs was \$1,178.75, and the reissue rate was \$848.70.
  - ii. The court determined that the lender was not provided with any documents evidencing that title insurance was obtained in the existing loan transaction, and rejected the claim by the plaintiff that the mere knowledge of an existing mortgage loan was sufficient to put the lender on notice that a title policy might exist.
  - iii. The court held that the plaintiffs failed to meet the burden of demonstrating (A) that the lender knew or should have known of the existence of the title policy, or (B) that a condition to qualify for the reinsurance rate (the insurance of the identical premises) was satisfied.

## 6. Assignee Liability

- a. *Parker v. Potter*, 2007 WL 465560 (11th Cir., February 14, 2007).
  - i. The United States Court of Appeals for the Eleventh Circuit held that the right to rescind applies against assignees, as well as creditors, even if a violation of the TILA is not apparent on the face of the documents.

- b. ***Bills v. BNC Mortgage, Inc.***, 2007 WL 1438371 (N.D. Illinois, May 11, 2007).
  - i. This case also is addressed above with regard to rescission issues.
  - ii. The plaintiffs filed suit against their mortgage lender, the assignee of their loan and the assignee's servicer seeking rescission of their loan and damages. The defendant assignee moved for summary judgment on the grounds that it can be liable for damages under the TILA only if the alleged violation was apparent on the face of the disclosure documents provided to the assignee's servicer. The plaintiffs did not dispute this point, but argued that the assignee was liable for statutory damages for its own failure to rescind their loan after receiving a notice of cancellation.
  - iii. The court agreed with a prior case in the same district and held that an assignee cannot be held liable for failing to comply with a notice of rescission when the underlying basis for the rescission is a disclosure violation that is not apparent on the face of the disclosure statements.
- c. ***Miranda v. Universal Financial Group, Inc.***, 459 F.Supp.2d 760 (N.D. Illinois, November 7, 2006).
  - i. The borrower brought an action for rescission against the lender, two former assignees and the current note holder. The former assignees argued that they no longer had the power to rescind the loan, and that they should be dismissed from the litigation. The court held that a borrower may exercise the right to rescind against any assignees, including former assignees, and declined to dismiss the former assignees.
  - ii. The case was dismissed on May 1, 2007 pursuant to a settlement.

## 7. Business Purpose

- a. ***Cashmere Valley Bank v. Brender***, 146 P.3d 928 (Supreme Court of Washington, November 16, 2006).
  - i. In 1993 the borrower consolidated approximately \$203,000 of business loans with the lender, and obtained an additional \$150,000 to settle a divorce and obtain his wife's interest in an orchard and shake mill. The borrower signed an agreement representing and warranting that the new loan primarily was for business purposes. The loan was renewed in 1996, and the lender

obtained additional security in the borrower's mobile home. In 1999 the borrower obtained additional funds, and in 2001 the 1996 and 1999 loans were consolidated into one loan. The borrower defaulted on the 2001 loan and the lender commenced foreclosure. The borrower asserted defenses and counterclaims including a violation of the TILA. The central issue was whether the 2001 loan was exempt from the TILA on the grounds that it was primarily for a business purposes.

- ii. The Supreme Court of Washington noted the analysis of the Court of Appeals, in which the lower court identified the following three approaches by which courts assess the purpose of a loan: (A) the original purpose approach, pursuant to which a court will assess the original character and predominating purpose of the loan, (B) the all circumstances approach, pursuant to which the court undertakes a factual analysis, and (C) the quantitative approach, pursuant to which the court looks to whether the borrower used the majority of the loan proceeds for a commercial or consumer purpose.
- iii. The Court of Appeals selected the quantitative method for the case, and the Supreme Court agreed that such method was appropriate (noting that it was not opining on whether the quantitative method is appropriate for use outside the circumstances of the particular case). The \$150,000 obtained by the borrower to settle his divorce and obtain his wife's interest in an orchard and shake mill was considered at trial to be for a consumer purpose. The Supreme Court noted that bank did not object to this characterization, even though it appeared as if the proceeds were used to obtain business assets. The court concluded that, even if the \$150,000 was considered to be used for consumer purposes, the majority of the funds still were used for an exempt purpose and, therefore, the loan was not subject to the TILA.

## 8. Security Interest Disclosure

- a. *Carye v. Long Beach Mortgage Company*, 470 F.Supp.2d 3 (D. Massachusetts, January 22, 2007).
  - i. The lender required the borrower to sign a 1-4 Family Rider, adding to the property description, among other items, "goods of every nature whatsoever now or hereafter located in, on, or used, or intended to be used in connection with the Property...." The borrower argued that the Rider created a security interest that should have been disclosed as part of the TILA disclosures. The

lender countered that the Rider created only incidental interests that are excluded from the definition of a security interest. The court denied the lender's motion to dismiss, stating that it "cannot conclude that the only reasonable interpretation of the Rider is that it creates only incidental interests that cannot be disclosed."

## **B. REGULATORY**

### **1. CHARM Booklet**

- a. A revised Booklet was issued by the Federal Reserve Board (Board) in December 2006. The prior version was issued in May 2005.
- b. The revised Booklet may be used now, and must be used no later than October 1, 2007.
- c. Revisions to the Booklet include:
  - i. An upfront summary of key points, referred to by the Board as "core message," with references to where the points are addressed in the Booklet.
  - ii. A mortgage shopping worksheet that is an expanded version of the mortgage checklist and appears in the front of the Booklet.
  - iii. A greater focus on the potential for payment shock.
  - iv. A highlighted statement that loans are available through lenders and brokers, and that brokers are not required to find the best deal for the consumer unless they are acting as the consumer's agent.
  - v. A highlighted statement that with no-doc or low-doc loans, the lender does not require proof of income, but the consumer usually will have to pay a higher interest rate or extra fees.
  - vi. A highlighted statement that the payment amounts used in the examples do not include taxes, insurance, condominium or HOA fees, or similar items that can be a significant part of the monthly payment.
  - vii. Specific discussions regarding:
    - A. Hybrid ARMs.
    - B. Interest-only ARMs.

C. Payment-option ARMs.

viii. A Consumer Cautions section that addresses:

A. Loans with initial discounted interest rates.

B. Payment shock that can result when initial discounted rates are adjusted.

C. Negative amortization in greater detail, including the potential for significantly higher payments.

D. The potential for home prices not to increase sufficiently, or to decrease, and that this may make it difficult for the consumer to refinance.

E. Prepayment penalties and conversion fees.

F. Graduated-payment or stepped-rate loans.

**2. Interest-Only Mortgage Payments and Payment-Option ARMs—Are They for You?**

a. A new Booklet issued by Federal Financial Institution Examination Council members in November 2006 for consumers. Not a required disclosure.

b. Addresses interest-only ARMs and payment-option ARMs, and refers consumers to the CHARM Booklet for additional information.

**3. HOEPA Points and Fees Trigger**

a. Under the Home Ownership and Equity Protection Act, in addition to the applicable annual percentage rate trigger, the requirements of the Act are triggered if the points and fees exceed the greater of a specific dollar amount that is adjusted annually or 8% of the “total loan amount”.

b. The Board adjusted the dollar amount for points and fees test from \$547 for 2007 to \$561 for 2008. (August 7, 2007 *Federal Register* notice.)

**4. Regulation Z—Bankruptcy Act Changes/Other Open-End Changes**

a. Background

- i. In December 2004 the Board published an advanced notice of proposed rulemaking to commence a comprehensive review of the open-end credit rules under Regulation Z. (December 8, 2004 *Federal Register*.)
  - ii. On April 20, 2005 the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was signed into law.
    - A. The Act includes amendments to the TILA, both open-end and closed-end provisions.
    - B. The Board is required to adopt regulations to implement the amendments.
  - iii. In October 2005 the Board published a second advanced notice of proposed rulemaking regarding the open-end credit rules, and advised that it will include the changes regarding open-end credit that are required by the Act in the Board's overall review of the Regulation Z open-end credit provisions. (October 17, 2005 *Federal Register*.)
  - iv. On June 14, 2007 the Board published in the *Federal Register* a proposed rule to revise the open-end credit rules and implement the Bankruptcy Act changes. Comments are due by October 12, 2007.
- b. Bankruptcy Act Changes.
- i. Minimum payment warning (open-end).
  - ii. Introductory rate offers (open-end, credit card).
  - iii. Credit card Internet solicitations (open-end, credit card).
  - iv. Late fee disclosure (open-end).
  - v. Tax deductibility warning with high loan-to-value mortgage credit (open- and closed-end).
  - vi. Account termination restriction (open-end).

- c. Minimum Payment Warning.
  - i. Pursuant to the minimum payment warning requirement, periodic billing statements for open-end accounts will need to include in a prominent location on the front of the statements:
    - A. A warning that making only the minimum payment will increase the interest the consumer pays and the time it takes to repay the balance.
    - B. A hypothetical example of how long it would take to pay off a specified balance if only minimum payments are made.
    - C. A toll-free telephone number that the consumer may call to obtain an estimate of the time it would take to repay their actual account balance.
  - ii. To standardize the information provided to consumers through the toll-free telephone number, the Board is required by the Act to prepare tables that illustrate the approximate number of months it would take to repay an outstanding balance if the consumer pays only the minimum monthly payment and if no other advances are made.
  - iii. With regard to the toll-free telephone number:
    - A. The Board must establish and maintain for up to a 24-month period a toll-free number for use by customers of depository institutions having assets of \$250 million or less.
    - B. Other depository institutions must establish their own toll-free number or use a third party.
    - C. The FTC must establish a toll-free number for use by customers of non-depository institutions.
  - iv. Exception: If through a toll-free number a creditor provides the actual number of months that it will take the consumer to repay the outstanding balance (rather than an estimate):
    - A. The hypothetical example is not required to be included in the periodic statement.

- B. The warning and toll-free number must be disclosed in the periodic statement, but do not have to be on the front of the statement.
- v. The Board can exempt one or more types of open-end accounts from some or all of the minimum payment warning requirements.
  - A. The Board requested comment on whether it should exempt open-end accounts and credit extensions with a fixed repayment period, such as certain home equity lines of credit, from all of the requirements, or only the requirement to disclose the hypothetical example and toll-free number.
  - B. The Board noted that the requirements may not be suitable for reverse mortgage transactions.
- vi. The Board proposes to implement the minimum payment warning concept only for credit card issuers. Additionally, among other exemptions, home equity plans would not be subject to the requirement.
  - A. The general rule would require the disclosure in periodic statements of the warning regarding making periodic statements, the hypothetical example of how long it would take to pay off the balance by making only the minimum payment, and a toll free number that the consumer could use to obtain an estimate of the time it would take to pay off his or her balance.
  - B. Creditors would be exempt from the general rule requirements if they, at their option:
    - 1. Established and maintained a toll free telephone number that consumers could use to obtain the actual time to repay the balance, and included in periodic statements a minimum payment warning that set forth the toll free number; or
    - 2. Simply included the actual repayment information in their periodic statements.
    - 3. In either case, creditors could rely on guidance provided by the Board to determine the time period to repay the balance that is disclosed to the consumer.

- C. Although the Board is required by the Act to prepare tables to help creditors prepare the repayment estimates, the proposal sets forth guidance, including a minimum payment calculation formula, that creditors may follow to prepare the estimates. The approach taken by the Board would provide for consumers calling a toll free number, entering information on their account based on prompts, and then receiving the repayment estimate.
- d. Late Fee Disclosure.
  - i. The Act requires that with open-end plans creditors must provide additional disclosures on periodic statements if a late payment fee will be imposed for failure to make a payment on or before the due date.
  - ii. The Act provides that the periodic statement must disclose clearly and conspicuously:
    - A. The date on which the payment is due or, if different, the earliest date on which a late payment fee may be charged.
    - B. The amount of the late payment fee that may be imposed if payment is made after the applicable date.
  - iii. In the June 2007 release, the Board proposes that the periodic statement for an open-end (not home-secured) plan:
    - A. Set forth on its front side the payment due date.
      - 1. If the cut-off time for application of payments is before 5 p.m., the cut-off time in close proximity to the due date.
    - B. Set forth on its front side the amount of the late payment fee and the penalty APR that could be triggered by a late payment, in close proximity to the due date.
- e. Tax Deductibility Warning With High Loan-to-Value Mortgage Credit.
  - i. For credit, both open-end and closed-end, secured by a consumer's principal dwelling, creditors must provide additional disclosures if the credit amount will or may exceed the fair market value of the dwelling.

- ii. With advertisements that are disseminated in paper form to the public or through the Internet (but not radio or television), the advertisements must include a clear and conspicuous statement that:
  - A. The interest on the portion of the credit extension that is greater than the fair market value of the dwelling is not tax deductible for Federal income tax purposes.
  - B. The consumer should consult a tax advisor for further information regarding the deductibility of the interest and charges.
- iii. Credit applications for open-end credit must include a statement that interest on the portion of the credit extension that is greater than the fair market value of the dwelling is not tax deductible for Federal income tax purposes (and continue to include a statement that the consumer consult a tax advisor, which was required before the Act).
- iv. Credit applications for closed-end credit must include a clear and conspicuous statement that:
  - A. The interest on the portion of the credit extension that is greater than the fair market value of the dwelling is not tax deductible for Federal income tax purposes.
  - B. The consumer should consult a tax advisor for further information regarding the deductibility of the interest and charges.
- v. In the June 2007 release, the Board advises that because this requirement of the Act relates to home-secured credit, the Board is not proposing revisions to Regulation Z to implement the requirement, and anticipates implementing the requirement in connection with an upcoming review of Regulation Z requirements for mortgage transactions.
- f. Account Termination Restriction.
  - i. A creditor may not terminate an open-end credit plan before its expiration date solely because the consumer has not incurred finance charges on the account.

- ii. A creditor would not be prohibited from terminating an account that was inactive for three or more consecutive months.
- iii. In the June 2007 release, the Board proposes to implement the prohibition using language similar to that contained in the Act. The proposal would define an account as being “inactive” if no credit has been extended, such as by purchase, cash advance or balance transfer, and the account has no outstanding balance.

## **5. Federal Reserve Board Hearings**

- a. The Home Ownership Equity Protection Act (HOEPA) requires the Board to periodically hold public hearings on the home equity lending market and the adequacy of existing regulatory and legislative provisions for protecting the interests of consumers, particularly low income consumers.
- b. The Board held hearings in 2000, which focused on predatory lending and the ability of the Board to use its regulatory authority to address abusive lending practices.
  - i. The hearings led to amendments of the Regulation Z provisions governing HOEPA loans that were adopted in December 2001, with compliance becoming mandatory in October 2002 (the “2002 revisions”).
  - ii. Among other changes, the 2002 revisions:
    - A. Lowered the APR trigger for first lien loans from 10 to 8 percentage points above the yield on Treasury securities with comparable maturities.
    - B. Required (1) the inclusion in the points and fees test of premiums or other charges for credit life, accident, health or loss-of-income insurance, or debt-cancellation coverage and (2) the deduction from the loan principal of such premiums and charges for purposes of computing the total loan amount in cases in which the premiums and charges are financed.
    - C. Added the prohibition against creditors, assignees or servicers of a HOEPA loan refinancing the loan within the first year following origination, unless the refinancing is in the borrower’s interest.

- D. Added a presumption that a creditor engages in a pattern or practice of making HOEPA loans based on the consumer's collateral without regard to the consumer's repayment ability (which constitutes a violation of HOEPA) if the creditor engages in a pattern or practice of making HOEPA loans without verifying and documenting the consumer's ability to repay.
- c. Pursuant to the public hearing requirement, in the Summer of 2006 the Board held hearings in Chicago, Philadelphia, San Francisco and Atlanta.
    - i. The Board also invited the submission of written comments.
    - ii. Parties submitting comments included the MBA, industry members and consumer groups.
  - d. The four main objectives of the Board were to:
    - i. Gather views on the effectiveness of the 2002 revisions in protecting consumers and the impact of the revisions on the availability of credit in the higher-cost portion of the subprime market.
    - ii. Gather information that will assist the Board's review of Regulation Z, particularly the rules governing home mortgage loans.
    - iii. Identify matters for which the Board or other entities can develop educational materials to help consumers make informed choices about mortgage loans.
    - iv. Help identify matters for which additional research about the mortgage lending market would be beneficial.
  - e. The Board identified the following as topics to be addressed:
    - i. The impact of HOEPA rules and state and local predatory lending laws on predatory lending. The Board invited comment on:
      - A. Whether the 2002 revisions were effective in curtailing predatory lending practices, the impact of the revisions on the availability of subprime credit, whether other abusive practices emerged since the revisions, and whether certain provisions were particularly effective, or particularly likely to negatively affect credit availability.

- B. The impact of state and local predatory lending laws on curbing abusive practices, whether the laws have adversely affected the access of consumers to legitimate subprime lending, whether certain provisions were particularly effective, or particularly likely to negatively affect credit availability.
  - C. What efforts since the 2002 revisions to educate consumers about predatory lending have been successful, and what is needed to help such efforts succeed.
  - D. Whether the existing HOEPA disclosures required by Regulation Z should be changed to improve the understanding by consumers of high-cost loan products and, if so, in what way.
- ii. Nontraditional mortgage products—interest only and payment options ARMs. The Board invited comment on:
- A. Whether consumers have sufficient information from disclosures and advertisements about nontraditional mortgage products to understand the risks, such as payment increases and negative amortization, associated with the products.
  - B. Whether any disclosures required by Regulation Z should be eliminated or modified because they are confusing to consumers, unduly burdensome to creditors, or are simply not relevant to nontraditional mortgage products, and whether the current required disclosures present information about nontraditional mortgage products in an understandable manner.
  - C. Whether some Regulation Z disclosures should be provided earlier in the mortgage shopping and application process to aid consumers' understanding of key credit terms and costs.
- iii. Nontraditional mortgage products—reverse mortgages. The Board invited comment on:
- A. Whether current Regulation Z disclosures are adequate to inform consumers about the costs of reverse mortgages and to ensure that they understand the terms of the product.

- B. Whether counseling under the HUD reverse mortgage program has been effective in educating consumers about reverse mortgages and in preventing abuses from occurring.
  - C. With regard to reverse mortgages that are not made under the HUD program, whether counseling is offered to applicants, whether the borrowers have difficulty understanding the loan terms or encounter other difficulties, and whether the lenders employ alternate disclosure approaches that are proven to be effective.
- iv. Informed consumer choice in the subprime market. The Board invited comment on:
- A. How do consumers who get higher-priced loans shop for the loans, and how do the consumers select a particular lender?
  - B. What do consumers understand about the role of mortgage brokers in offering mortgage products, and has their understanding been furthered by state-required mortgage broker disclosures?
  - C. What strategies have been helpful in educating consumers about their options in the mortgage market, and what efforts are needed to help educate consumers about the mortgage credit process and how to shop and compare loan terms and fees?
  - D. What are some of the “best practices” that lenders, mortgage brokers, consumer advocates and community development groups have employed to help consumers understand the mortgage market and their loan choices?
  - E. What explains the differences in borrowing patterns among racial and ethnic groups, how much are patterns attributable to differences in credit history and other underwriting factors such as loan-to-value ratio, and what other factors may explain these patterns?
- f. On June 14, 2007 the Board held an additional hearing.
- i. The hearing focused on how the Board may use its authority under Section 129(1)(2) of TILA (which sets forth requirements for

HOEPA loans) to address concerns about abusive lending practices in the mortgage market, including the subprime mortgage market.

- ii. The Board intended to gather information to evaluate whether it can address issues about predatory lending in a way that preserves incentives for responsible lenders to provide credit to borrowers, particularly subprime borrowers.
- iii. The Board sought comment on whether it should use its rulemaking authority to address concerns about the following loan terms or practices:
  - A. Prepayment penalties. The Board solicited comment on the following issues:
    - 1. Should prepayment penalties be restricted? For example, should prepayment penalties that extend beyond the first adjustment period on an adjustable rate mortgage loan be prohibited?
    - 2. Would enhanced disclosure of prepayment penalties help address concerns about abuses?
    - 3. How would a prohibition or restriction on prepayment penalties affect consumers and the type and terms of credit offered?
  - B. Escrows for taxes and insurance on subprime loans. The Board solicited comment on the following issues:
    - 1. Should escrows for taxes and insurance be required for subprime mortgage loans? If escrows were to be required, should consumers be permitted to “opt out” of escrows?
    - 2. Should lenders be required to disclose the absence of escrow to consumers and, if so, at what point during a transaction? Should lenders be required to disclose an estimate of the consumer’s tax and insurance obligations?
    - 3. How would escrow requirements affect consumers and the type and terms of credit offered?

C. “Stated income” or “low doc” loans. The Board solicited comment on the following issues:

1. Should stated income or low doc loans be prohibited for certain loans, such as loans to subprime borrowers?
2. Should stated income or low doc loans be prohibited for higher-risk loans, for example loans with high loan-to-value ratios?
3. How would a restriction on stated income or low doc loans affect consumers and the type and terms of credit offered?

D. Unaffordable loans. The Board solicited comment on the following issues:

1. Should lenders be required to underwrite all loans based on the fully-indexed rate and fully amortizing payments?
2. Should there be a rebuttable presumption that a loan is unaffordable if the borrower’s debt-to-income ratio exceeds 50% at loan origination?
3. Are there specific consumer disclosures that would help address concerns about unaffordable loans?
4. How would such provisions affect consumers and the type and terms of credit offered?

g. Under HOEPA, the Board has the authority to:

- i. Except specific mortgage products or categories of mortgage loans from certain HOEPA requirements. (TILA Section 129(1)(1).)
- ii. Prohibit acts or practices in connection with any mortgage loans that the Board finds to be unfair, deceptive, or designed to evade HOEPA. (TILA Section 129(1)(2).)
- iii. Prohibit acts or practices in connection with refinance mortgage loans that the Board finds to be associated with abusive lending practices, or that are otherwise not in the interest of the borrower. (TILA Section 129(1)(2).)

- h. If the Board decides to adopt rules under TILA Section 129(1)(2) applicable to all loans, and not just HOEPA loans, there are significant issues.
  - i. Damages.
    - A. For mortgage loans, the general damages provisions of TILA provide for actual damages and statutory damages of not less than \$200 nor more than \$2,000, with a class action cap on statutory damages of the lesser of \$500,000 or 1% of the net worth of the creditor.
    - B. For HOEPA loans, there is a special damages provision that provides for an amount equal to the sum of all finance charges and fees paid by the consumer, unless the creditor demonstrates that the failure to comply with HOEPA is not material. Thus, for HOEPA loans the damages provision is equivalent to a rescission.
    - C. The special damages provision applies “in the case of a failure to comply with any requirement under section 129”. If the Board adopts rules under its HOEPA authority in Section 129 that apply to all mortgage loans, and not just HOEPA loans, would the rules be a requirement under Section 129?
  - ii. Rescission.
    - A. Any mortgage loan “that contains a provision prohibited by [Section 129] shall be deemed a failure to deliver the material disclosures required under” the TILA for purposes of the rescission right. Could a requirement regarding loan terms adopted under Section 129 that applies to all mortgage loans be deemed a provision prohibited by Section 129, thus creating another ground for rescission?
  - iii. Assignee Liability.
    - A. Under the general assignee liability provision of TILA for mortgage loans, an assignee is liable for a violation of the TILA by the original creditor if the violation is apparent on the face of the disclosure statement provided in connection with the loan pursuant to the TILA. A violation is apparent on the face of the disclosure if:

1. The disclosure can be determined to be incomplete or inaccurate by a comparison among the disclosure statement, any itemization of the amount financed, the note or any other disclosure of disbursement, or
  2. The disclosure statement does not use the terms or the format required to be used by the TILA.
- B. For HOEPA loans, an assignee is subject to all claims and defenses with respect to the loan that the consumer could assert against the original creditor, unless the assignee demonstrates by a preponderance of the evidence that a reasonable person exercising ordinary due diligence could not determine, based on the documentation required by the TILA, the itemization of amount financed, and other disclosure of disbursements that the loan was a HOEPA loan. The relief available to the consumer against the assignee may not exceed:
1. With respect to actions based on a violation of the TILA, the amount permitted under the special damages provision for HOEPA loans.
  2. With respect to all other causes of action, the sum of the amount of all remaining indebtedness, and the total amount paid by the consumer in connection with the transaction.
- C. The HOEPA assignee liability provision applies “to “[a]ny person who purchases or is otherwise assigned a mortgage referred to in section 103(aa)” of the TILA. A mortgage referred to in section 103(aa) is defined as a mortgage that meets the annual percentage rate trigger and/or the points and fees trigger. Thus it appears that the HOEPA assignee liability provisions should apply to only HOEPA loans.
- iv. In its comments to the Board, the MBA recommended that if the Board determines that new disclosures are required, it should use its authority under TILA Section 105(a), and not 129(1), to adopt the disclosures.

## 6. **FTC Warnings on Advertisements**

- a. The Federal Trade Commission (FTC) announced on September 11, 2007 that it is advising more than 200 advertisers and media outlets that some mortgage ads are potentially deceptive under the FTC Act or in violation of the Truth in Lending Act (TILA).
- b. The FTC advises that the ads were identified in June during a nationwide review that focused on claims for very low monthly payment amounts or interest rates, without adequate disclosure of other important terms. The FTC noted as an example that some ads touted rates as low as 1%, but failed to disclose adequately:
  - i. That the stated rate was a “payment rate” and not the interest rate that applied only during the loan’s initial period.
  - ii. That low advertised payments applied for only a short period.
  - iii. The Annual Percentage Rate for the loan.
- c. The FTC letter to mortgage companies advises, among other things, that:
  - i. “We read at least one of your mortgage advertisements as part of a multi-media review of mortgage advertising.”
  - ii. “We have not determined whether your company is in violation of the law. However, we urge you to review your practices to ensure that they comply with the law. We have preserved your advertisement for future reference. By sending you this notice, we do not waive the right of the Commission to take action against you based on past or future law violations.”

## 7. **Electronic Disclosures**

- a. History
  - i. The Board issued an interim final Regulation Z rules regarding electronic disclosures in March 2001.
    - A. The Board provided for a mandatory compliance date of October 1, 2001.
    - B. Similar interim final rules were issued for Regulations B, E, M and DD.

- ii. The Board lifted the mandatory compliance date in August 2001.
- b. Current proposal
  - i. The Board published a new proposed rule in the *Federal Register* on April 30, 2007.
    - A. Similar proposed rules were issued for Regulations B, E, M and DD.
  - ii. The Board proposes to remove the interim rules for electronic communications that are set forth in Regulation Z Section 226.36, including the 90 day availability requirement for electronic documents.
  - iii. The Board also proposes:
    - A. Allowing certain disclosures to be made electronically without regard to the federal E-Sign requirements, including:
      - 1. Regulation Z Section 226.5b home equity plan disclosures.
      - 2. Regulation Z Section 226.19(b) adjustable rate mortgage disclosures.
    - B. Requiring that the 226.5b and 226.19(b) disclosures be provided electronically on or with electronic home equity plan applications and electronic adjustable rate mortgage loan applications, respectively.
    - C. Including the concept from the interim final rules that only one “copy” of an electronic rescission notice is required.

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