



**WEINER
BRODSKY
SIDMAN
KIDER PC**

Litigation Update: Developments in Fair Lending, RESPA, and Fraud

MITCHEL H. KIDER

WEINER BRODSKY SIDMAN KIDER

September 24, 2007

FAIR LENDING

- **NCRC HUD Complaints Alleging Discrimination in Lending Policies**
 - Cases challenging lenders' policies of not lending on row houses
 - Cases challenging lenders' policies of not issuing loans secured by property located on American Indian Reservations
 - HUD has settled several cases containing these allegations, complaints continue to be filed
- **State Attorneys General Investigations**
 - Fair lending issue: Do brokers and lenders pressure appraisers to inflate property values in order to make loans?
- **Government Initiatives**
 - Feds Issue Final Statement on Subprime Mortgage Lending (June 2007)
 - Sets forth lending standards to insure borrowers obtain loans they can afford to repay
 - State Regulators issue parallel statement
 - New HUD Office – Fair Lending Division
 - Purpose: to review mortgage lending practices nationwide and investigate allegations of discrimination

- **Civil Litigation**
 - American Indian Reservation Loans:
 - A novel action by a borrower asserts Fair Housing Act claims against a lender in connection with its policy of not issuing loans secured by property on American Indian Reservations
 - Discrimination based on language:
Coelho v. Alliance Mortgage Banking Corp. (D.N.J.)
 - In a case where a borrower claimed that he was discriminated against in his loan transaction because he did not speak English, the court rejected the mortgage broker's claim that "language minorities" are not a protected class under New Jersey's anti-discrimination law, denying the broker's motion to dismiss
 - Discrimination based on neighborhood :
Anderson v. Wachovia Mortgage Corp. (D. Del.)
 - Plaintiffs previously obtained loans to purchase homes in racially mixed or predominantly white neighborhoods
 - When plaintiffs later attempted to purchase homes in "white" neighborhoods, they filed suit, claiming that the lenders imposed different, more stringent requirements on them
 - The Court has denied the lender's motion to dismiss
 - "Systematic, Institutionalized Racism":
NAACP v. Ameriquest Mortgage Co. (C.D. Cal.)
 - NAACP filed this putative class action against 14 of the largest subprime lenders, alleging racism in making mortgage loans
 - NAACP alleges that "systematic, institutionalized racism" results in African Americans paying higher mortgage rates than similarly situated white borrowers

- Consumer Protection Laws as alternative outlet for fair lending claims
 - Attractive to plaintiffs who want to avoid federal court jurisdiction
 - Plaintiffs have had varying degrees of success
 - Example: *Green v. Branch Banking & Trust Co.* (N.C. App.): Lending money to poorly qualified borrower did not constitute an unfair and deceptive trade practice

RESPA

- **Flat-fee Pricing: Does it violate RESPA?**
 - *Price v. Landsafe Credit, Inc.* (S.D. Ga.) holds “No”
 - Facts: The lender charged a credit report provider a flat fee for credit reports, only where the applicant ultimately received a loan. The fee did not vary depending on the number of credit reports provided
 - Holding: “Free” credit reports for non-borrower applicants was not a “kickback” from the provider to the lender
 - Case on appeal to the Eleventh Circuit
- **Unearned Fees: Must they be divided to give rise to a Section 8(b) claim?**
 - The Second Circuit joins the debate: *Cohen v. JP Morgan Chase & Co.*
 - Facts: Plaintiff challenged a “post-closing fee,” for which she claims her lender provided no services
 - Holding: The court denied the lender’s motion to dismiss. Holding that the statute was ambiguous, the court deferred to HUD’s policy statement, which advises that a single service provider violates Section 8(b) by charging unearned, nominal, duplicative fees
- **Seminal *Santiago v. GMAC Mortgage Case Settles***
 - Following the Third Circuit’s decision that RESPA Section 8 does not provide a cause of action for overcharges, only for markups, the case was remanded to the district court. The parties have since settled their claims
 - Pursuant to the settlement agreement, approved by the court, GMAC will create a settlement fund of \$650,000
 - \$325,000 will be disbursed among the 81,981 class members; class members will receive between \$2 and \$14.40
 - The remaining \$325,000 will go to attorney’s fees and costs, a fraction of the amount expended

- **Yield Spread Premiums**
 - *Culpepper IV*: The Eleventh Circuit’s Final Installment
 - Likely the final gasp for the first major YSP case, which began more than 10 years ago
 - The court reversed its position in *Culpepper III*
 - Based on HUD Statement of Policy 2001-1, the court affirmed decertification of the class, holding that legality of a YSP must be examined in light of each specific claim, a fact incompatible with class certification
 - YSP Range Disclosures:
 - Although Regulation X contemplates that disclosures may be set forth as a range, some states require disclosure of a specific dollar amount
 - Creative Litigation: Consumer Protection Laws as Vehicles for “RESPA” Claims
 - Increasing trend to present as state law action claims that are, at their heart, RESPA claims
 - Advantages to litigants include:
 - Longer statutes of limitations
 - More expansive remedies (generally including treble damages and/or attorney’s fees)
 - Avoidance of federal court

- **Plaintiffs' Bar Asserting Claims Traditionally Brought as HUD Enforcement Actions**
 - Increasing trend, includes claims based on sham affiliated business arrangements and sham affiliated marketing arrangement cases
- **Required Use: Homebuilder Cases**
 - Facts: Plaintiffs allege that the homebuilder offers discounts and rebates on home prices, upgrade packages, or closing costs if the buyer uses the affiliate's settlement services. The buyer is informed that he is free to choose any service provider
 - Issue: Does offering discounts and rebates constitute a “required use” under Regulation X?
- **When is Compliance with RESPA not Enough?**
 - *Grady v. Burnet Realty Inc.*
 - Facts: Plaintiffs assert that their real estate broker referred them to its affiliate for title insurance and settlement services, despite the fact the affiliate charged higher prices for those services than other providers. Plaintiffs assert that the broker had a duty to inform them of these “material facts” and that a RESPA-compliant affiliated business disclosure is not sufficient to satisfy this duty
 - Requested standard: “fully disclose all material facts known to [the broker] which might affect the clients’ rights or interest, without ambiguity or reservation”

- **Calculation of Damages: What amount is subject to trebling under RESPA Section 8?**
 - Issue One: What damages are recoverable?
 - *Berger v. Property I.D. Corp.* (C.D. Cal.)
 - Facts: Plaintiffs claim real estate brokers and providers of Natural Hazard Disclosure Reports created LLCs to cover up kickbacks to the real estate brokers
 - Holding: The specific service(s) involved in the violation are subject to the damages provisions of RESPA. The court rejected the argument that only the “illegal” portion of a settlement charge paid is subject to RESPA’s trebling provisions
 - Other courts have held that only the “illegal” portion – i.e. the inflated amount – is subject to trebling
 - Issue Two: If no “inflated charge” was paid, does the plaintiff have standing?
 - *Carter v. Welles-Bowen* (N.D. Ohio):
 - Facts: Plaintiffs allege that a realty company, settlement agent, and other entities created a title company to provide kickbacks to the realty company in exchange for referrals of settlement work.
 - Holding: Plaintiffs lacked standing because they did not allege they paid inflated charges for title insurance
 - Case on appeal to the Sixth Circuit

- **HUD Enforcement Actions**

- Since 2001, HUD has entered into about 50 public settlement agreements concerning alleged RESPA violations
- Focus of HUD Actions:
 - Sham affiliated business arrangements:
 - Actions typically involve title agents
 - Example of settlement: In January 2007, HUD joined with Minnesota Department of Commerce to address joint venture title companies. One involved title company agreed to pay \$500,000 in civil penalties to the state
 - Captive title reinsurance
 - HUD entered into six settlements in 2006
 - Settling parties paid from \$150,000 to \$950,000
 - Various states have also negotiated settlement with title insurers
 - Referrals conditioned on payments of a thing of value
 - Trend – HUD is now seeking enforcement against both the recipient of the thing of value and the provider of the thing of value
 - Example of settlement: In related February 2007 settlements, a title company paid over \$68,000, and a builder paid over \$20,000, in connection with allegations by HUD that the title company provided things of value to the builder for referrals

- Test Case: *Jackson v. Property I.D.* (C.D. Cal.):
 - May 2007 action by Secretary of HUD, alleging unlawful affiliated business arrangement
 - HUD's claims parallel the claims brought by private party in *Berger*
 - Case may test HUD's theory that RESPA contemplates the remedy of disgorgement of profits

FRAUD

- **Borrower Fraud**
 - Stated-Income/Stated-Asset and No-Doc Loans
 - Are borrowers really qualified for the loans they seek?
 - Some borrowers are seeking damages from lenders even though they made material misrepresentations regarding their income on their loan applications
 - Foreclosure Workout Schemes
 - Some original homeowners who accepted foreclosure rescue are now suing the lenders making loans under their purchase agreements.
 - Example: *Phifer v. Home Saver Consulting Corp.* (E.D.N.Y.): Court denied motion to dismiss aiding-and-abetting-of-fraud claim against lender, who was represented at the closing, where misrepresentations were made in furtherance of the scheme to deprive the homeowner of title.
 - State legislation:
 - Some states have implemented rescission statutes to “undo” foreclosure rescue transactions
 - Some states have created statutory penalties for fraudulent acts of foreclosure consultants
 - Mortgage brokers’ roles in foreclosure rescue schemes are gaining increased media attention, may lead to increased litigation
- **Seller Fraud – Cash back at closing not disclosed on HUD-1**

- **Title Company/Settlement Agent Fraud**
 - Examples: Failing to verify earnest money/down payments made; converting funds for own use; creating “fake” HUD-1 settlement statements; failing to ensure timely recordation of deeds, mortgages
 - *IndyMac Bank F.S.B. v. National Settlement Agency* (S.D.N.Y.): Lender suing settlement agent for conversion of funds that should have been distributed out of loan proceeds. Four transactions are involved, more than \$2.4M allegedly converted
- **Appraiser Fraud**
 - Pushed Values
 - Lack of objectivity can make it difficult for lenders to discern where appraisers have inflated values
 - Increasing litigation by lenders seeking damages from appraisers and brokers based on faulty appraisals
 - Identity Theft: Impostors posing as appraisers/ using their electronic signatures
 - Lenders’ Responsibility for Appraisals – Attorney General Investigations
 - NY AG investigating brokers/lenders for allegedly pressuring appraisers to inflate property values
 - Ohio and Colorado AGs conducting similar investigations