Assignee Liability: Through the Minefield

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I. Introduction

Consumer credit transactions, from retail installment contracts, to mortgages, to automobile leases, to credit cards, often generate assignments. The recipients of assignments -- those who assume rights and obligations from the original creditors -- often face a minefield of state and federal laws which may trigger liability. This paper contrasts various liability possibilities which assignees may face in these situations.

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II. **Limitation On Assignee Liability**[4]

The protection conferred by the limitation on assignee liability in Section 1641(a) of the Truth In Lending Act (TILA)[5] is a bulwark that prevents consumer disputes with the original creditors from affecting the rights of their assignees to enforce contractual obligations. But it may potentially be undermined in several situations.

The TILA was enacted "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair billing and credit card practices."[6] Significantly, however, Congress deliberately limited assignee liability when it amended the Act in the early 1980s to provide as follows in 15 U.S.C. section 1641(a):

> Except as otherwise specifically provided in this subchapter, any civil action for a violation of this subchapter or proceeding under Section 1607 of this title which may be brought against a creditor may be maintained against any assignee of such creditor only if the violation for which such action or proceeding is brought is apparent on the face of the disclosure statement, except where the assignment was involuntary.

In enacting these amendments, Congress expressed its purpose as narrowing "considerably the potential scope of assignee liability," to "make[e] compliance easier for creditors" and to limit civil liability for statutory penalties for only significant violations.[7]

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[4] See generally Mark E. Dapier, Eugene J. Kelley, Jr., John L. Ropiequet, and Christopher S. Naveja, *Assignee Liability Under the TILA: Is the Conduit Theory Really Dead?*, 54 Consumer Fin. L.Q. Rep. 242 (2000), reprinted in Rohner & Miller, Truth in Lending ¶ 12.06[1] (2006 Supp.).

[5] 15 U.S.C. § 1641(a).

[6] 15 U.S.C. § 1601(a).

[7] Ramadan v. Chase Manhattan Corp., 229 F.3d 194, 200 (3d Cir. 2000), citing S. Rep. No. 96-73 (1979), reprinted in 1980 U.S.C.C.A.N. 10,236, 10,281.

Beginning in 1998, an unbroken line of U.S. Court of Appeals and district court decisions has recognized that assignees are liable for the TILA disclosure violations of the creditors who originated the credit transactions only where the violations are "apparent on the face" of the documents assigned.[8] The policy behind these decisions was succinctly stated in *Irby-Greene v. M.O.R., Inc.*:

> This limit on assignee liability is sensible, as a duty to inquire beyond the assigned documents would impede commerce, which depends upon the established practice of assigning commercial paper at a discount to financial institutions. In general, assignees are not in a position to know whether a given price was set in violation of TILA, as assignees often are not present at the transaction (which may have occurred much earlier than the assignment), do not participate in the negotiation, and may not be aware of a seller's mode of conducting business. Assignees are in a position to examine the documents assigned for irregularities, and they usually make pricing decisions based on those documents. Thus, 15 U.S.C. § 1641(a) "enable[s] an assignee to know with [a reasonable degree of] certainty upon receipt of assigned documents whether it would be subject to possible liability for the actions of the vendor."[9]

Despite this firmly established law, however, the limitation on assignee liability is not always absolute. An assignee may lose the protection of Section 1641(a) when other laws intervene. Assignees should always beware of such "mines" lurking under the surface of consumer credit transactions.

[8] Taylor v. Quality Hyundai, Inc., 150 F.3d 689, 695 (7th Cir. 1998); Walker v. Wallace Auto Sales, Inc., 155 F.3d 927, 936 (7th Cir. 1998); Ellis v. General Motors Acceptance Corp., 160 F.3d 703, 709 (11th Cir. 1998); Green v. Levis Motors, Inc., 179 F.3d 286, 295 (5th Cir.), *cert. denied*, 520 U.S. 1020 (1999); Balderos v. City Chevrolet, Buick & Geo, Inc., 214 F.3d 849, 853 (7th Cir. 2000); *Ramadan*, 229 F.3d at 198; Irby-Greene v. M.O.R., Inc., 79 F. Supp. 2d 630, 633-34 (E.D. Va. 2000); Knapp v. AmeriCredit Financial Services, Inc., 245 F. Supp. 2d 841, 848 (S.D.W. Va. 2003); Coleman v. General Motors Acceptance Corp., 196 F.R.D. 315 (M.D. Tenn. 2000).

[9] 79 F. Supp. 2d at 634.

III. The Mines

A. Consumer Leasing Act

The federal Consumer Leasing Act (CLA)[10] was enacted in 1976 as an amendment to the TILA. Like the TILA, "the CLA is a disclosure rather than a regulatory statute."[11] The CLA broadens the reach of the TILA and applies to all leases for the use of personal property having a term exceeding four months that have a "total contractual obligation not exceeding $25,000."[12]

As it did when it passed the TILA, Congress delegated to the Federal Reserve Board (FRB) the task of drafting regulations with respect to the CLA, giving it the authority to "update and clarify the requirements and definitions application to lease disclosures."[13] Those regulations are collectively referred to as Regulation M. The regulations, along with the FRB Staff Commentary on Regulation M, are codified at 12 C.F.R. section 213.

The FRB Staff Commentary states that "an assignee may be a lessor for the purposes of the regulation in circumstances *where the assignee has substantial involvement in the lease transaction*."[14] Thus, the assignee can lose the protection of the limitation on assignee liability in Ssction 1641(a) where it is directly involved, in certain circumstances.

The interplay between Regulation M and section 1641(a) was brought into sharp focus in *Kennedy v. BMW Financial Services, N.A.*[15] There, the plaintiff was a lessee

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[10] 15 U.S.C. § 1667 *et seq*.
[11] Turner v. General Motors Acceptance Corp., 180 F.3d 451, 454 (2d Cir. 1999).
[12] 15 U.S.C. § 1667(1).
[13] 15 U.S.C. § 1667f(a)(1).
[14] 12 C.F.R. § 213.2(h), Supp. I (emphasis supplied).
[15] 363 F. Supp. 2d 110 (D. Conn. 2005).

who had entered into a motor vehicle lease agreement with an auto dealer which assigned the least to BMW Financial Services (BMW). He alleged that the lease agreement was inaccurate on several points, claiming: (1) the agreement overstated the title, registration, and license fees due on the automobile (resulting in an increased total payment); and (2) BMW miscalculated the excess mileage and sales tax at lease termination. Based on these inaccuracies, the plaintiff alleged that BMW violated the CLA. BMW claimed that it was immune from liability under the CLA because, as an assignee of the original lessor, its liability was limited by section 1641(a).

The *Kennedy* court began by examining the definition of a "lessor" under the CLA, which is "a person who is regularly engaging in leasing, offering to lease, or arranging to lease under a consumer lease."[16] Regulation M, the court pointed out, defines an arranger of a lease as one "has knowledge of the lease terms and participates in the preparation of the contact documents required in connection with the lease."[17] The FRB Staff Commentary also states that "an assignee *may* be a lessor for the purposes of the regulation in circumstances where the assignee has substantial involvement in the lease transaction."[18]

The *Kennedy* court noted that BMW's use of section 1641(a) as a defense in the leasing context was an essentially an issue of first impression. While the plaintiff argued that section 1641(a) was inapplicable in the CLA context, the court disagreed:

> The CLA itself is enforced through the larger statutory scheme of TILA. 15 U.S.C. [section] 1667(d) of the CLA, discussing the civil liability of lessors, specifically states that the "grounds for maintenance of [a civil] action" is provided by "[15 U.S.C. section] 1640 of [TILA]." Section 1641,

[16] 15 U.S.C. § 1667(4).
[17] 363 F. Supp. 2d at 115, *quoting* 12 C.F.R. § 213.2(h), Supp. I.
[18] *Id.* at 115 (emphasis in original).

> obviously, directly follows 15 U.S.C. [section] 1640, and limits what claims under the former Section may be pursued against assignees. There is nothing to suggest that, in the context of consumer leases, a lessee may avail himself of the remedies provided by TILA through [section] 1640 but ignore the restrictions of [section] 1641(a).[19]

The court went on to cite the FRB Staff Commentary as support for its holding that Section 1641(a) does not by its terms exclude lease assignees:

> Nor does the staff commentary to Regulation M, to which courts must defer in interpreting the CLA, suggest that lease assignees are excluded from the protections of [section] 1641(a). That commentary says that assignees who are substantially involved in lease arrangements *may* be considered lessors for purposes of regulation. *See* 12 C.F.R. [section] 213.4(h), Supp. I. That language implies both that it is not *mandatory* for substantially involved assignees to be treated as such, and that assignees less involved in lease arrangements should not be considered lessors.[20]

Having concluded that BMW could avail itself of the section 1641(a) defense in the lease context, the court then examined BMW's level of participation to determine if it merited holding BMW liable. As to the miscalculation of the amount due for title, registration, and licensing, the court found that BMW was "shielded from liability on these violations as an assignee, as BMW did not calculate these figure and any errors in calculations were not apparent on the face of the lease."[21] In reaching this conclusion, the court relied on *Taylor v. Quality Hyundai*[22] and emphasized that BMW merely provided the forms to the dealer. There was no evidence of *any* involvement by BMW in calculating those fees, much less any evidence of the "substantial involvement" required by the Commentary to trigger assignee liability. Accordingly, because the

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[19] 363 F. Supp. 2d at 116.
[20] *Id.* (emphasis in original).
[21] *Id.* at 117.
[22] 150 F.3d 689 (7th Cir. 1998)

miscalculations were not apparent on the face of the assigned documents, the court held that section 1641(a) shielded BMW from liability on that charge.[23]

As to the miscalculation of excess mileage fees and sales tax at lease termination, however, the court found that BMW did indeed participate at such a level as to warrant treating it as a lessor for Regulation M purposes. BMW "participates in setting the mileage allowance and excess mileage charges for vehicle leases that it assumes from a dealer," and "at the time of lease termination (when these fees are calculated), BMW was the only lessor."[24] Nevertheless, plaintiff's failure to plead this claim led the court to grant summary judgment dismissing it.[25]

B. <u>Credit Cards</u>

A similar theory was advanced unsuccessfully to try to circumvent the limitation on assignee liability in *Neff v. Capital Acquisitions & Management Co.*[26] The plaintiffs there asserted that a purchaser of credit card debt from the original creditor was liable under the TILA as a "creditor" for failure to issue monthly billing statements. Plaintiff Neff had fallen behind on his credit card payments to Citibank. His account was sold as delinquent to Capital One. In 1997, a collection agency sent him a letter stating that his balance was $1,133 but that he could settle by paying $536. Neff paid the amount with a money order marked "payment in full."

For the next five years, Neff did not receive any monthly billing statements, and assumed that his Citibank debt was satisfied. But in 2002, he received a letter from Capital Acquisitions & Management Company ("CAMCO"), an assignee of Capital One

[23] *Kennedy*, 363 F. Supp. 2d at 119.
[24] *Id*.
[25] *Id.* at 120.
[26] 353 F.3d 1118 (7th Cir. 2003).

which had purchased his account, informing him that he owed $2,835.32. The other plaintiff in the case was similarly situated, claiming that although he settled his account, he received a letter from CAMCO years later demanding he satisfy a debt of $7,000.

The plaintiffs charged that by not sending monthly billing statements, CAMCO violated the TILA. The trial court dismissed this claim on motion. The Seventh Circuit affirmed, reasoning that the "normal rule" that the assignee assumes the duties of the assigning party does not apply to obligations under the TILA because the TILA and Regulation Z specifically address the obligations of assignees. Any liability would have to be within the TILA framework.[27]

Although the plaintiffs claimed that CAMCO was a "creditor" so as not to trigger the application of Section 1641(a), the Seventh Circuit did not agree. The actions of the assignee did not bring it within the definition of "creditor" under the TILA since it only purchased credit card accounts.[28]

C. HOEPA[29]

For standard mortgage transactions, as discussed above, the assignee is only liable for violations that are apparent on the face of the disclosure statement. However, the "apparency" protection of the TILA does not apply to assignees of loans which come under the purview of the Home Ownership Equity Protection Act, (HOEPA).[30] The HOEPA comes into play if the APR is more than 10 points over the applicable Treasury security rate (the "APR trigger") or the points and fees paid by the consumer are more

[27] *Id.* at 1121.
[28] *Id.*
[29] See generally Eugene J. Kelley, Jr., John L. Ropiequet, and Anna-Katrina S. Christakis, *An Overview of HOEPA, Old and New*, 59 Consumer Fin. L.Q. Rep. 203 (2005), reprinted in Rohner & Miller, Truth in Lending ¶ 12.06[3] (2006 Supp.).
[30] 15 U.S.C. § 1641(d).

than the greater of 8% of the principal amount of the loan or $400 (the "points and fees trigger").[31] If either of these tests is met, special disclosures must be made and a series of statutory prohibitions will apply.[32]

The limitation on assignee liability under section 1641(a) of the TILA also does not apply to HOEPA loans. Under section 1641(d), an assignee is subject to all claims and defenses that the consumer could assert with respect to that mortgage against the 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 this subchapter, the itemization of the amount financed, and other disclosure of disbursements that the mortgage" is a mortgage subject to HOEPA. Likewise, the consumer's right of rescission survives assignment, and can be asserted against any assignee of the obligation.[33]

In *Mason v. Fieldstone Mortgage Co.*,[34] the assignee argued that it was a holder in due course and therefore could not be held liable because the plaintiff's fraud claim was not a claim "with respect to" the mortgage. Citing the "plain language" of section 1641(d)(1), the court simply stated: "I find that it is."[35] Similarly, in two other cases dealing with assignee liability, the courts found that the "unmistakable effect" of section 1641(d) was to eliminate holder in due course defenses for HOEPA mortgages.[36]

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[31] 15 U.S.C. § 1602(aa).
[32] 15 U.S.C. § 1639.
[33] 15 U.S.C. § 1641(c).
[34] 2000 WL 1643589 (N.D. Ill. 2000).
[35] *Id.* at *4.
[36] Vandenbroeck v. Contimortgage Corp., 53 F. Supp. 2d 965, 968 (W.D. Mich. 1999); In re Murray, 239 B.R. 728 (E.D. Pa. 1999).

More recently, in *Durham v. The Loan Store, Inc.*,[37] the court held that two successive assignees of a HOEPA mortgage could be held liable for the original mortgagee's HOEPA violations. The plaintiff alleged that the original creditor exceeded the HOEPA threshold and that inclusion of a HOEPA Notice to Assignee made it apparent on the face of the document that it was subject to the HOEPA. The assignees therefore had no protection from assignee liability under section 1641(a).[38]

D. <u>The ECOA</u>

Claims of race discrimination violative of the Equal Credit Opportunity Act (ECOA)[39] have made use of the broader definition of "creditor" in the ECOA, which includes "any person who regularly extends, renews, or continues credit; any person who regularly arranges for the extension, renewal, or continuation of credit; *or any assignee of an original creditor who participates in the decision to extend, renew, or continue credit*,"[40] to avoid the limitation on assignee liability in section 1641(a) of the TILA. Assignees often meet this definition by participating in the decision to extend credit when they agree to accept an assignment at the same time that the TILA "creditor" extends credit.

The assignee can be excluded from the ECOA definition of "creditor" and avoid liability for discriminatory acts or practices by the person who deals directly with the consumer under Regulation B only if it did not know or have reasonable notice of the

[37] 2005 WL 2420389 (N.D. Ill. Sept. 30, 2005).
[38] *Id.* at *7.
[39] 15 U.S.C. § 1691 *et seq*.
[40] 15 U.S.C. § 1691a(e) (emphasis supplied). This is sometimes referred to as the "multiple creditor rule," which references multiple creditors while recognizing that a subsequent creditor who purchases a credit contract (*e.g.*, an assignee) is not a "creditor" under the ECOA (though possibly a creditor for other purposes) unless the subsequent creditor participated in the transaction originating the credit contract. *See also* Regulation B, § 202.2(1); *infra* this text at note 41.

original creditor's discrimination before it accepted the assignment.[41] Although this would appear on its face not too difficult to establish under most circumstances, the "effects test" referred in a footnote to Regulation B[42] has proven to be quite a challenge to assignees.

Many class actions have been filed in recent years against deep-pocket assignees of automobile retail installment contracts which do not even name the auto dealers who allegedly discriminated against the protected classes as defendants. All of the reported cases have now been settled for large amounts of fees to the plaintiffs' attorneys and benefits of more dubious value to the class members. Unfortunately, because they have been settled rather than litigated to a conclusion, these cases give little guidance as to what the ECOA really requires of assignees.

This subject and the ramifications for future litigation against assignees are discussed at length in two recent articles by one of your authors.[43]

E.. FTC Holder Rule[44]

1. Federal Holder Rule Cases

The FTC Holder Rule[45] requires that the following language be included in at least ten point bold type in all consumer retail installment contracts:

NOTICE

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[41] 12 CFR § 202.2(1). This is sometimes called the "multiple creditor" rule.
[42] 12 CFR § 202.6(a), footnote 2.
[43] John L. Ropiequet and Nathan O. Lundby, "APR Split Class Actions Under the Equal Credit Opportunity Act: The End Of History?", 61 Cons. Fin. L.Q. Rep. 49 (2007); John L. Ropiequet and Nathan O. Lundby, "Dealer Rate Participation Class Actions Under the ECOA: Have We Reached the End of the Road?", 62 Bus. Law. __ (Feb. 2007).
[44] See generally Mark E. Dapier, Eugene J. Kelley, Jr., John L. Ropiequet, and Christopher S. Naveja, *Assignee Liability Under the TILA: Is the Conduit Theory Really Dead?*, 54 Consumer Fin. L.Q. Rep. 242 (2000), reprinted in Rohner & Miller, Truth in Lending ¶ 12.06[4] (2006 Supp.).
[45] 16 C.F.R. § 433.2.

> **ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.**

By its terms, this language would appear on its face to allow a consumer to assert all claims and defenses to which the original creditor was subject against the assignee as well. This seeming conflict between the FTC Holder Rule, which would permit an assignee to be held liable to the consumer, and section 1641(a), which would preclude such liability, was firmly resolved in favor of limiting liability by the same cases which recognized the limitation, starting with *Taylor v. Quality Hyundai, Inc.*[46] That case held that the holder in due course language cannot override the limitation on assignee liability in section 1641(a):

> The plaintiffs initially argued that the TILA actually has nothing to do with the assignee's liability in these cases, because they are bound under the terms of the contracts they accepted, wholly apart from the statute. . . . In our view, however, this misconstrues the effect of the Holder Notice insofar as it governs TILA-based claims.
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> The Holder Notice, even though contained within the contract, was not the subject of bargaining between the parties, and indeed could not have been. It is part of the contract by force of law, and it must be read in light of other laws that modify its reach. [citation omitted] We therefore reject the plaintiffs' contract-based effort to side-step [section] 1641(a).[47]

[46] 150 F.3d 689 (7th Cir. 1998).
[47] *Id.* at 693.

2. Holder Rule Cases Under State Law

This holding in *Taylor* was followed in numerous other cases each time that they considered the limitation on assignee liability under TILA in section 1641(a).[48] However, many state court decisions which were decided prior to the seminal *Taylor* decision applied the FTC Holder Rule contract language without considering the limitation on assignee liability in TILA section 1641(a). For example, the Alabama court in *Eachen v. Scott Housing Systems, Inc.*[49] was faced with the issue of whether mobile home buyers could sue both the mobile home manufacturer and the finance company to which their retail installment contract was assigned for breach of warranty. Instead of relying on section 1641(a) to defend the TILA issue, the finance company argued that the FTC Holder Rule does not provide a basis for making a claim directly against the assignee, but rather only applies if the plaintiff were defending a suit filed against it by the assignee. The *Eachen* court rejected this argument, holding that the FTC Holder Rule language imposed liability on the finance company because it was a subsequent holder of the contract.[50] Similar rulings were handed down in many state courts[51] and federal courts[52] in the years preceeding the *Taylor* decision. However, these cases were called into question by the courts' failure to consider the impact of TILA section 1641(a), especially after *Taylor*.

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[48] Walker v. Wallace Auto Sales, Inc., 155 F.3d 927, 935 (7th Cir. 1998); Ellis v. General Motors Acceptance Corp., 160 F.3d 703, 709 (11th Cir. 1998); Green v. Lewis Motors, Inc., 179 F.3d 286, 295 (5th Cir.), *cert. denied*, 520 U.S. 1020 (1999); Ramadan v. Chase Manhattan Corp., 229 F.3d 194, 199 (3d Cir. 2000); Balderos v. City Chevrolet, Buick & Geo, Inc. 214 F.3d 849, 853 (7th Cir. 2000); Irby-Greene v. M.O.R., Inc., 79 F. Supp. 2d 630, 635-36 (E.D. Va. 2000).
[49] 630 F. Supp. 162 (N.D. Ala. 1986).
[50] *Id*. at 164-65.
[51] See, e.g., Bendix Home Systems v. Jessop, 644 P.2d 843 (Alaska 1982); Jefferson Bank & Trust v. Stamatiou, 384 So. 2d 388 (La. 1980); Thomas v. Ford Motor Credit Corp., 48 Md. App. 617, 429 A.2d 277 (1981); Hardeman v. Wheels, Inc., 56 Ohio App. 3d 142, 565 N.E.2d 849 (1988).
[52] See, e.g., Perry v. Household Retail Services, Inc., 953 F. Supp 1370, 1375-76 (M.D. Ala. 1996); Mayberry v. Said, 911 F. Supp. 1393, 1402-03 (D. Kan. 1995); Cox v. First National Bank of Cincinnati, 633 F. Supp. 236, 239 (S.D. Ohio 1986).

Following the federal decisions in *Taylor* and numerous other cases subsequently confirming *Taylor*, there still remained the issue of whether the same rule would be applied to state law claims. This issue was carefully analyzed by the Illinois Supreme Court in an important decision, *Jackson v. South Holland Dodge, Inc.*[53] In addition to following *Taylor* on the issue of whether the limitation on assignee liability in section 1641(a) affected liability under state laws, discussed below at Part III.F., the court addressed whether the FTC Holder Rule language nevertheless imposed liability on a subsequent holder of the contract. Noting that all of the federal courts that had addressed the issue rejected that argument, the *Jackson* court likewise found that the FTC Holder Rule language could not impose liability.[54]

Nonetheless, the treatment of the FTC Holder Rule in subsequent cases, both state and federal has not been consistent. For example, in *Alexiou v. Brad Benson Mitsubishi*,[55] a federal district court followed *Ramadan* and held that the New Jersey state law Holder Rule was expressly preempted by TILA section 1641(a) and therefore the state law could not impose liability on an assignee for state law claims under the New Jersey Consumer Fraud Act,[56] breach of contract or money paid by an estate.[57]

On the other hand, in *Cavette v. MasterCard Int'l, Inc.*,[58] a federal district court completely ignored the issue of federal preemption of conflicting state law under TILA. At issue was whether plaintiff's claim, that MasterCard's failure to disclose its currency

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[53] 197 Ill. 2d 39, 755 N.E.2d 462 (2001).
[54] *Id*. at 53-55, 755 N.E.2d at 471-72, citing *Taylor*, 150 F.3d at 692-93; *Ellis,* 160 F.3d at 708-09; *Greene,* 179 F.3d at 296.
[55] 127 F. Supp. 2d 557 (D.N.J. 2000).
[56] N.J. Stat. Ann. § 56:8-1 *et seq.*
[57] 127 F. Supp. 2d at 564-65.
[58] 282 F. Supp. 2d 813, 819 (N.D. Tenn. 2003).

conversion fee violated the Tennessee Consumer Protection Act,[59] was in conflict with the disclosure requirements of the TILA, which included no duty to disclose such information. The court found that no federal question jurisdiction was present under the artful pleading doctrine and remanded the case to state court without reviewing the TILA's requirements for open-end credit disclosures or federal preemption issues.

In *Psensky v. American Honda Finance Corp.,*[60] the New Jersey Superior Court, Appellate Division, overruled an earlier decision[61] where a lower court had held that while TILA section 1641(a) applies to TILA claims, it did not apply to claims under the New Jersey Consumer Fraud Act.[62] The *Psensky* court held that in the absence of an allegation that the defendant assignee actively participated in wrongdoing by the original creditor, an auto dealer, so that only a failure to disclose was present, the assignee's compliance with the TILA was "a complete defense to the state claims."[63]

A similar ruling was issued in *Vickers v. Interstate Dodge, Inc.*[64] In Vickers, the trial court had found both the original creditor, again an auto dealer, and its assignee liable on a claim that the dealer had forged plaintiff's initials on an option to purchase credit life insurance. On appeal, the Louisiana Court of Appeals followed *Ramadan* and *Alexiou* in finding that the definition of "creditor" and "extender of credit" under a state statute could not extend liability to an assignee in contravention of TILA section 1641(a) of the TILA, and that the FTC Holder Rule language in the contract also could not extend liability.[65]

[59] Tenn. Code Ann. § 47-18-101 *et seq.*
[60] 378 N.J. Super. 221, 875 A.2d 290 (2005).
[61] Scott v. Mayflower Home Improvement Corp., 363 N.J. Super. 145, 831 A.2d 564 (2001).
[62] N.J. Stat. Ann. § 56:8-1 *et seq.*
[63] 378 N.J. Super. at 231, 875 A.2d at 296, citing *Jackson*.
[64] 882 So. 2d 1236 (La. App. 2005).
[65] *Id.* at 1243.

One commentator has recently recommended that consumers rely on the FTC Holder Rule language to seek redress against both original creditors and assignees for any type of claim that they may have.[66] He advocates this since the language since the FTC Holder Notice language is designed to make all subsequent assignees "stand in the shoes of the seller."[67] However, in support he cited pre-*Taylor* cases and cases involving rescission, a special circumstance discussed below in Part III.G. He did not discuss *Taylor* and the cases following it. Such arguments may sway courts that are unfamiliar with the now well-settled rule that the TILA section 1641(a) limitation on assignee liability trumps the FTC Holder Rule language.

This approach to the issue may have influenced the court in the recent case of *Glovier v Barton Homes, LLC*[68] to find that no federal question was presented in a situation similar to that presented in *Cavette*. The *Glovier* case had been removed to federal court on the ground that plaintiff's claim under the FTC Holder Rule presented a claim arising under federal law. The *Glovier* court ruled that bringing breach of contract and other state law claims against an assignee pursuant to the FTC Holder Rule language did not create federal question jurisdiction since the FTC Holder Rule does not create a federal private right of action.[69] As in *Cavette*, the *Glovier* court gave no consideration to whether the claims implicated the limitation on assignee liability in TILA section 1641(a). Whether the issue will be raised after remand to state court remains to be seen.

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[66] David A. Szwak, *The FTC "Holder" Rule*, 60 Consumer Fin. L.Q. Rep. 361 (2006).
[67] *Id*. at 364, citing FTC Guidelines, 41 Fed. Reg. 20,022, 20,023 (May 14, 1976).
[68] 2006 U.S. Dist. Lexis 65215 (W.D. La. Sept. 13, 3006).
[69] *Id*. at *5-7.

F. **<u>State UDAP Laws</u>**[70]

The FTC Holder Rule cases deal with the question of whether a consumer's claims against the original creditor are preserved or extinguished upon assignment of the credit instrument. If the claims are preserved, they can be asserted against the assignee. If they are extinguished by the assignment, they cannot be. Such claims may involve the question of whether disclosures required by the TILA have been given by the original creditor.

As discussed above, under section 1641(a), TILA disclosure claims may not be asserted against an assignee unless they are "apparent on the face" of the disclosure statement. A related and significant question is whether the original creditor may have done something underhanded or fraudulent that may subject it to liability under a state Uniform Deceptive Acts and Practices (UDAP) statute but which cannot be determined simply by looking at the face of the documentation being assigned. Can such claims be brought against an assignee under the UDAP statute, or does the limitation on assignee liability in TILA section 1641(a) also absolve an assignee of liability for such claims?

This was the question that faced the Illinois Supreme Court in *Jackson v. South Holland Dodge, Inc.*[71] At issue was whether an assignee could be held liable under the Illinois Consumer Fraud Act[72] where the auto dealer violated the TILA by failing to disclose that it retained part of the price being paid for an extended warranty instead of entering the full amount of the purchase price as an "amount paid to others" in the TILA disclosure statement. This would present a TILA violation on the part of the dealer, but

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[70] See generally Eugene J. Kelley, Jr. and John L. Ropiequet, *Assignee Liability Under State Law After* Jackson v. South Holland Dodge, 56 Consumer Fin. L.Q. Rep. 16 (2002), reprinted in Rohner & Miller, Truth in Lending ¶ 12.06[5] (2006 Supp.).
[71] 197 Ill. 2d 39, 755 N.E.2d 462 (2001).
[72] 815 ILCS 501/1 *et seq.*

under federal circuit court of appeals decisions, an assignee who purchased the retail installment contract from the dealer could not be liable under the TILA because the violation was not apparent on the face of the disclosure statement.

Drawing on its earlier decision in *Lanier v. Associates Finance, Inc.*,[73] the *Jackson* court found that the assignee fully complied with its TILA obligations by purchasing a contract that had no TILA disclosure violations apparent on its face.[74] The court further found that holding an assignee liable under the Consumer Fraud Act where the TILA exempted it from liability would violate the state's public policy because:

> If an assignee were liable under the Consumer Fraud Act, though exempted from liability under TILA, it would impose disclosure requirements on assignees beyond those mandated by federal law. This would frustrate the overarching reasons put forth by Congress in enacting the assignee exemption, i.e., to narrow assignee liability, to make compliance easier for creditors and to eliminate confusion as to the responsibilities of assignees. [citation omitted] Thus, we conclude that an assignee is not responsible for the misrepresentations made by the dealer to the consumer outside of reviewing the face of the assigned document for apparent defects. Accordingly, we will follow *Lanier* and hold that compliance with the disclosure requirements of TILA is a defense to the Consumer Fraud Act claim against Chrysler in this case.[75]

As mentioned above at Part III.E.2., this holding in *Jackson* was followed in New Jersey in *Psensky v. American Honda Finance Corp.*,[76] overruling the earlier decision in *Scott v. Mayflower Home Improvement Corp.*[77] The *Psensky* court agreed that absent some allegation that the assignee actively participated in wrongdoing by the dealer that

[73] 114 Ill. 2d 1, 499 N.E.2d 440 (1986).
[74] 197 Ill. 2d at 47-48, 755 N.E.2d at 468, citing *Taylor*, 150 F.3d at 691, 694; *Ramadan*, 229 F.3d at 197, 203; *Greene*, 179 F.3d at 295-96; *Ellis*, 160 F.3d at 709-10.
[75] *Id*. at 49-50, 755 N.E.2d at 469.
[76] 378 N.J. Super. 221, 875 A.2d 290 (2005).
[77] 363 N.J. Super 145, 831 A.2d 564 (2001).

assigned the contract to it, so only a failure to disclose was present, there could be no liability, adopting the rationale of *Jackson.*[78]

The same result occurred in California in *Silvas v. E*Trade Mortgage Corp.*[79] In Silvas, the plaintiffs claimed that the defendant mortgage lender failed to rescind the transaction after receiving a proper notice of rescission and violated the TILA in other respects. They failed to file suit within the one-year statute of limitations provided by the TILA, so they sued only under Sections 17200 and 17500 of the California Unfair Competition Law (UCL),[80] which had a four-year statute. The mortgage lender asserted that allowing plaintiffs to prosecute claims under the California statute when their claims would be barred by the TILA conflicted with the TILA's federal regulatory scheme. Thus, the state law claims should be preempted. The *Silvas* court agreed that UCL claims could not be brought where TILA claims were barred because to allow such claims would amount to conflicting state regulation of the defendant's activities where federal law and banking regulations occupy the entire field.[81]

The *Silvas* court distinguished a recent California state court decision, *Smith v. Wells Fargo Bank, N.A.,*[82] because the *Smith* court dealt with "a different, narrower, preemption regulation, and it also did not apply field preemption principles."[83] *Smith* involved UCL claims concerning fees for ATM and check card overdrafts. The *Silvas* court stated that *Smith* only involved a predicate act of violating federal disclosure requirements, but did "*not* involve or seek to impose any *state* law *limitation* or other

[78] 378 N.J. Super. 221, 231, 875 A.2d 290, 296, citing *Jackson.*
[79] 421 F. Supp. 2d 1315 (S.D. Cal. 2006).
[80] Cal. Bus. & Prof. Code §§ 17200, 17500.
[81] 421 F. Supp. 2d at 1320, citing 12 C.F.R. § 560.2.
[82] 135 Cal. App. 4th 1463, 38 Cal. Rptr. 3d 653 (2005).
[83] 421 F. Supp. 2d at 1320-21.

state requirement regarding disclosure."[84] Its ruling therefore did not conflict with federal regulations or implicate federal preemption of the state law causes of action.

Under these cases and others, it is clear that the limitation on assignee liability in section 1641(a) applies to bar state law claims if the liability is merely derivative of the original creditor's wrongful act against the consumer. For example, the Illinois Supreme Court ruled in *Zekman v. Direct American Marketers, Inc.*[85] that there is no derivative liability under the state UDAP statute for the act of a person who directly defrauded a consumer, even if the person knowingly received the benefit of the other's fraud.[86] Derivative UDAP liability has also been rejected elsewhere.[87]

If, however, the assignee can be found to have participated "directly" in the claimed wrongdoing, a UDAP claim may still be possible. For example, in *Knapp v. AmeriCredit Financial Services, Inc.*,[88] it was alleged that the assignee's branch manager conspired with an auto dealer to create false documents and to hide a finance charge in the vehicle price stated on the retail installment contract. This would make it directly rather than derivatively liable for a UDAP violation. The court accordingly did not dismiss the UDAP claim against the assignee, although it did dismiss the claims brought against it under the TILA.[89]

This issue was addressed more recently in *Cazares v. Pacific Shore Funding*.[90] The *Cazares* plaintiffs sued a mortgage broker and its assignees under the UCL for TILA and HOEPA violations, alleging that the assignees participated directly in the

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[84] 135 Cal. App. 4th at 1482 (emphasis in original).
[85] 182 Ill. 2d 359, 695 N.E.2d 853 (1998).
[86] *Id.* at 369, 695 N.E.2d at 859.
[87] See, e.g., Home Savings Ass'n v. Guerra, 733 S.W.2d 134, 136 (Tex. 1987); Harvey v. Ford Motor Credit Co., 8 S.W.3d 273, 275 (Tenn. App. 1999).
[88] 245 F. Supp. 2d 841 (S.D.W. Va. 2003).
[89] *Id*. at 851-52.
[90] 2006 WL 149106 (C.D. Cal. Jan. 3, 2006).

broker's loan transactions by dictating the mortgage broker's loan terms, financing the loans issued by the broker and paying a premium for including prepayment penalty provisions that violated the HOEPA prohibition on such terms in high cost mortgage loans. The court agreed that "secondary liability cannot be imposed under the UCL," but found that these allegations of the assignees' direct involvement in wrongful conduct were sufficient to state a claim under the UCL.[91]

The *Knapp* plaintiffs also asserted that the assignee was liable for the dealer's alleged violation of the West Virginia usury law.[92] Although the court found that there was no usury violation,[93] such a claim could clearly have created liability for both the dealer and the assignee if it had merit since the TILA does not preempt this type of state regulation. Under Section 1610(a)(1),[94] the TILA only preempts state laws that are "inconsistent with the provisions of the Act and then only to the extent of the inconsistency." Since the TILA does not regulate interest rates, this is one type of state law claim that can clearly be brought against an assignee as well as the original creditor.[95]

G. <u>Rescission</u>

1. <u>Introduction</u>

Where a plaintiff claims a right to rescind a credit transaction, the rules change. This is true in two different respects. First, the FTC Holder Rule language will be given

[91] *Id.* at *9.
[92] W. Va. Code § 46A-3-101 *et seq.*
[93] 245 F. Supp. 2d at 850-51.
[94] 15 U.S.C. § 1610(a)(1). See also 12 C.F.R. § 226.28(a)(1).
[95] For a discussion of federal preemption of usury laws with respect to mortgage lending, see John L. Ropiequet and Eugene J. Kelley, Jr., *Usury Strikes Back: Recent Developments Under the Illinois Interest Act*, 59 Consumer Fin. L.Q. Rep. 118 (2005); John L. Ropiequet and Eugene J. Kelley, Jr., *Usury Revisited: The Illinois Supreme Court Rights the Balance in Mortgage Lending*, 60 Consumer Fin. L.Q. Rep. 133 (2006).

effect against an assignee where the consumer seeks to rescind the transaction after receiving "little or nothing of value." Second, mortgage borrowers are given a statutory right to rescind which is made expressly effective against all assignees under the TILA.[96] Both types of rescission have been the subject of substantial litigation.

2. Consumer Received No Value

In the *Taylor* decision, the court stated that it was not interpreting the limitation of assignee liability in section 1641(a) in such a way as to make the FTC Holder Rule a nullity. It took note of a line of cases providing that where the consumer has received "little or nothing of value," there is a common law right to rescind the transaction. The court therefore held:

> As a legally required part of every consumer financing contract, the Holder Notice continues to perform an important function even in the contracts between the plaintiffs and their respective assignees. If the cars turn out to be lemons and they assert a right to withhold payment against the sellers, they may also assert the same right against the assignees.[97]

This ruling followed from earlier case law which held that the Holder Rule language allowed a consumer to pursue affirmative claims, as opposed to mounting a defense, "only if the seller's breach was so substantial that rescission and restitution were justified under applicable state law principles."[98]

Claims for rescission outside of the mortgage finance arena are unusual, since TILA plaintiffs typically seek only actual or statutory damages. Occasionally, a TILA claim will be coupled with a claim under the Odometer Act.[99] For example, the plaintiff

[96] 15 U.S.C. § 1641(c).
[97] 150 F.3d at 693.
[98] Mount v. LaSalle Bank Lake View, 926 F. Supp. 759, 763-64 (N.D. Ill. 1996).
[99] 49 U.S.C. § 32705.

in *Irby-Greene v. M.O.R., Inc.*[100] claimed that a 40,000 mile odometer discrepancy entitled her to rescission and restitution. While the court dismissed the TILA claim against the assignee, it did not dismiss the Odometer Act claim against it, although it did cast doubt on whether such discrepancy could entitle the plaintiff to rescission in a decision on the merits of the case.[101] Similar rulings have been issued in a few other cases.[102]

3. <u>TILA Statutory Rescission Rights</u>

The TILA permits a mortgage borrower to rescind the transaction for three business days after the transaction is consummated or delivery of the disclosures required by the TILA, whichever is later.[103] If, however, the creditor fails to provide the required disclosures or fails to make them clearly and conspicuously, as the TILA requires, the right to rescind does not expire until three years after the consummation of the transaction or the sale of the property, whichever occurs first.[104] A failure to comply with these requirements can create substantial difficulty for mortgage lenders.

For example, in *Hammox v. Heartland Home Finance, Inc.*,[105] the plaintiffs sought to rescind the mortgage loan because they allegedly did not receive the requisite two copies of the disclosure statement, even though they had signed a document indicating that they had received them. The court dismissed their claim for actual and statutory damages against the assignee because such a violation was not "apparent on

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[100] 79 F. Supp. 2d 630 (E.D. Va. 2000).
[101] *Id*. at 636 & n. 22.
[102] See, e.g., Crews v. Altavista Motors, Inc., 65 F. Supp. 2d 388, 390 (W.D. Va. 1999); Bogges v. Lewis Raines Motors, Inc., 20 F. Supp. 2d 979 (S.D.W. Va. 1998).
[103] 15 U.S.C. § 1635(a).
[104] 15 U.S.C. § 1635(f).
[105] 2005 WL 1130347 (E.D. Tenn. May 13, 2005).

the face" of the document that was assigned.[106] However, since their signature on the document only created a "rebuttable presumption of delivery," which they might be able to disprove at trial, the court did not dismiss their rescission claim.[107] In another case, *Oscar v. Bank One*,[108] signing the disclosure statement at the loan closing was sufficient for the court to grant summary judgment dismissing the plaintiffs' rescission claim since it was not rebutted.

The issue of damages in connection with a rescission claim arose again in *Belini v. Washington Mutual Bank, F.A.*[109] In that case, the plaintiffs sent the assignee bank a notice of rescission which asserted that the mortgage was subject to the HOEPA but the original creditor had not made the disclosures that the HOEPA required. When the bank failed to return any of plaintiffs' payments or to terminate its security interest, the plaintiffs sought damages for the monies that were not returned as well as rescission. The trial court found that the damage claims were barred by the TILA's one-year statute of limitations and that they could not rescind because of an exception in the TILA with respect to their state.

The First Circuit U.S. Court of Appeals reversed. It found that the one-year statute of limitations under TILA section 1640 began to run from the "date of the occurrence of the violation," which was the date when the plaintiffs sent their rescission notice, not the earlier date when the loan closed. The plaintiffs' claims for damages for

[106] *Id.* at *1.
[107] *Id.* at *2.
[108] 2006 WL 401853 (E.D. Pa. Feb. 17, 2006).
[109] 412 F.3d 17 (1st Cir. 2005).

failure to comply with the rescission notice therefore were not barred.[110] The court also found that there was no basis to deny plaintiffs the right to rescind the transaction.[111]

In three recent cases, courts have found that the statutory right to rescind, when extended beyond the initial three-day period by failure to make timely disclosures, will survive refinancing. An early case in the Ninth Circuit U.S. Court of Appeals, *King v. State of California*,[112] held that rescission was not possible when a mortgage has been refinanced because once the mortgage has been paid off, there is nothing left to rescind. The Sixth Circuit U.S. Court of Appeals took a fresh look at this issue in *Barrett v. JP Morgan Chase Bank, N.A.*[113] After noting a split in the district court decisions subsequent to *King*, some following it,[114] some not,[115] the *Barrett* court emphasized the mandatory nature of the TILA requirement that the right to rescind be disclosed in finding that rescission rights survive refinancing:

> To the extent banks wish to avoid a three-year window for bringing rescission claims, the Act offers them a fail-safe way of doing so: satisfy the disclosure requirements.[116]

The *Barrett* court cautioned that there had still been no determination on the merits "whether the bank failed to make the required *material* disclosures or failed to disclose adequately the Barretts' right to rescind, which are the types of disclosure errors that must be present to trigger the three-year right of rescission."[117]

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[110] *Id.* at 25.
[111] *Id.* at 27.
[112] 784 F.2d 910, 913 (9th Cir. 1986).
[113] 445 F.3d 874 (6th Cir. 2006).
[114] See, e.g., Jenkins v. Mercantile Mortgage Co., 231 F. Supp. 2d 737, 745-46 (N.D. Ill. 2002); Coleman v. Equicredit Corp. of America, 2002 WL 88750 at *2 (N.D. Ill. 2002).
[115] See, e.g., McIntosh v. Irwin Union Bank & Trust Co., 215 F.R.D. 26, 30 (D. Mass. 2003); Payton v. New Century Mortgage Corp., 2003 WL 22349118 at *2 & n. 1 (N.D. Ill. 2003); Pulphus v. Sullivan, 2003 WL 1964333 at *17 (N.D. Ill. 2003).
[116] *Id.* at 881-82.
[117] *Id*. at 882. (emphasis in original).

Just nine days later, the California Court of Appeal declined to follow the Ninth Circuit decision in *King* and instead followed *Barrett* in *Pacific Shore Funding v. Lozo,*[118] citing the *King* court's lack of analysis and its failure to support its decision by referring to the language of the TILA and Regulation Z, which contain "an enumerated list of events that cut off rescission rights -- and do not include the payment in full of the loan as one of those events."[119] The *Pacific Shore* court also distinguished *King* because unlike the facts there, the *Lozo* plaintiffs continued to hold title subject to a security interest, so that "something does remain to be rescinded in this case."[120]

Finally, the Seventh Circuit U.S. Court of Appeals followed *Barrett* in *Handy v. Anchor Mortgage Corp.*[121] In that case, the original mortgage lender provided two conflicting forms notifying the borrower of her right to rescind. The trial court dismissed the case on the basis that either one of the forms would have given her notice of her rescission rights. The Seventh Circuit reversed because although one of the forms was the correct one and gave her notice that the entire loan could be rescinded, the other form, which was not the correct one for the transaction, suggested that she could only rescind the additional amount being refinanced, $5,500 out of the entire $80,500 loan. This was legally insufficient to give the requisite notice of right to rescind.[122] The court noted that "TILA does not easily forgive 'technical' errors."[123] With respect to the argument that because the loan had been paid off, rescission was not an available

[118] 138 Cal. App. 4th 1342, 42 Cal. Rptr. 3d 283 (2006).
[119] *Id.* at 1353, 42 Cal. Rptr. 3d at 290, citing McIntosh v. Irwin Union Bank & Trust Co., 215 F.R.D. 26, 31 (D. Mass. 2003).
[120] *Id.* at 1353-54, 42 Cal. Rptr. 3d at 290.
[121] 464 F.3d 760 (7th Cir. 2006).
[122] *Id.* at *10.
[123] *Id.*, citing Cowen v. Bank United of Texas, FSB, 70 F.3d 937, 941 (7th Cir. 1995) ("hypertechnicality reigns" in TILA cases).

remedy, the court followed *Barrett* because there is a right to rescind the transaction, not merely a right to rescind the security interest.[124]

On the other hand, and despite the "technical errors" admonition in *Handy*, the courts have not always shown an eagerness to find in favor of rescission claims where they are based on mere technicalities. In *Mills v. EquiCredit Corp.*,[125] the plaintiffs asserted that the defendant's use of an incorrect disclosure form was a material misdisclosure that triggered the extension of their right to rescind beyond the three-day period. The Sixth Circuit rejected this argument and affirmed dismissal of their TILA claims because they received actual notice of their right to rescind, as the TILA requires, even if an incorrect form was used. However, in *Rollins v. Drive-1 of Norfolk, Inc.*,[126] the court found that the FTC Holder Rule language in the mortgage documents formed the basis for an affirmative claim for rescission against the assignee even where the plaintiff failed to plead a claim for rescission, so long as sufficient facts were pleaded to justify it.

IV. Conclusion

The limitation on assignee liability in TILA section 1641(a) has withstood many attacks. It continues to afford broad and meaningful protection to all assignees.

But there are exceptions, and these can create a minefield of risks for assignees. The CLA allows an assignee to have the status of a "lessor," analogous to the "creditor" under the TILA, where there has been substantial involvement in the lease transaction. And, while an attack on assignee protection was rejected in a credit card case, the protection provided by section 1641(a) is not available where HOEPA is involved.

[124] *Id.* at *13, citing *Barrett*, 445 F.3d at 878.
[125] 172 Fed. Appx. 652 (6th Cir. Feb. 24, 2006).
[126] 2006 U.S. Dist. Lexis 61197 (E.D. Va. Aug. 29, 2006).

There is potential exposure in an ECOA setting as well, although the parameters of the multiple creditors rule and Regulation B "effects" have never been settled in this context.

Section 1641(a) protection has survived claims under the FTC Holder Rule that do not involve rescission, but there is always the danger that courts which are not made aware of the relevant federal case law will fail to recognize that protection. Claims under other state laws may also circumvent the protection. Finally, rescission claims, while often difficult to substantiate, may have vitality since they present yet another exception to section 1641(a) protection.

So, assignees must walk carefully in this minefield. Direct participation in the original creditor's operations can and does lead to liability. It should be avoided wherever possible, because it may sufficiently entangle the assignee to confer joint liability under one of the situations discussed above. Never take your protection from assignee liability under section 1641(a) for granted.

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