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Leverage: State Enforcement Actions in the Wake of the Robo-Sign Scandal

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LEVERAGE: STATE ENFORCEMENT ACTIONS IN THE WAKE OF THE ROBO-SIGN SCANDAL

Raymond H. Brescia

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LEVERAGE: STATE ENFORCEMENT ACTIONS IN THE WAKE OF THE ROBO-SIGN SCANDAL

Raymond H. Brescia[*]

I. INTRODUCTION

In the fall of 2010, the revelations that tens of thousands of foreclosure filings across the nation were likely fraudulent—if not outright criminal—sparked a nation-wide investigation by all fifty state attorneys general to assess the extent of the scandal and its potential impacts, but also to consider likely legal and policy responses to such behavior. One of the tools at the state attorneys general's disposal that might rein in this behavior includes each state's Unfair and Deceptive Acts and Practices (UDAP) laws. Such laws typically prohibit "unfair" and "deceptive" practices, which are described loosely in these laws, and often give consumers, as well as state attorneys general, the ability to bring affirmative litigation to rein in practices that violate their provisions. They are often drafted with less specificity than other laws, and give litigants and the courts a certain degree of leeway in mapping out their contours in response to evolving market practices. In this way, UDAP laws serve a critical consumer protection function by filling in gaps in the law where other, more targeted laws might not cover practices that have a harmful impact on consumers. Since their inception, UDAP laws have been used to rein in abusive practices in such areas as used car sales, telemarketing and even the sale of tobacco products. This article explores the availability of UDAP laws and the remedies they provide to rein in the range of practices revealed in the so-called "Robo-Sign Scandal." It concludes that such practices—the false affidavits, reckless claims, and improper notarizations—all violate the essence of most state UDAP laws; accordingly, the remedies available under such laws may be wielded by state attorneys general to halt abusive foreclosure practices throughout the nation. What is more, UDAP actions in light of robo-sign abuses could help chart a path towards a more robust mortgage modification regime, one that would result in principal reductions. In the end, such strategies offer the clearest path out of the current foreclosure crisis.

This paper is divided into seven sections. Sections two and three provide overviews, respectively, of the present state of the foreclosure scandal as well as state UDAP laws generally. The fourth section discusses the use of state UDAP laws to combat predatory lending in the last decade. The fifth analyzes the prospects for applying UDAP laws and remedies to improprieties in the foreclosure process itself. Section six discusses a potential barrier to the use of the UDAP laws

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in the foreclosure context: namely, the threat of federal pre-emption of such UDAP laws and enforcement actions.

II. THE ROBO-SIGN SCANDAL.

In late September 2010, fact-finding processes in several foreclosure cases revealed rampant fraud in the manner in which many banks handled those and many other foreclosures.[1] The most egregious example of such fraud could be found in what has come to be known as "robo-signing": the use of surrogates to sign foreclosure paperwork.[2] In many instances, the fraud goes much deeper, however, revealing fundamental problems with the claims of many banks in tens of thousands of foreclosure cases. These revelations raise doubts about whether these banks even have the right to foreclose on borrowers where such banks have difficulty proving that they are a party to the mortgages that underlie the foreclosure actions in question.[3] In order to explain these problems, a brief description of the mortgage origination, securitization, and foreclosure processes is in order.

A. Background: Mortgages, Foreclosures, and Recording Acts.

When a borrower takes out a mortgage to purchase a property, he or she makes a promise to the bank that the mortgage loan will be paid back, and typically "secures" that loan by pledging the property purchased as collateral for the loan.[4] If the borrower defaults on the loan, the bank can seek to take back the collateral securing that loan: the home. In nearly half of U.S. states, banks seeking to foreclose on a property for the borrower's failure to maintain his or her obligations on the loan must go through the courts to seek a court order to foreclose on the property.[5] This process, which dates back hundreds of years, is known as the

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1. On the origins of the underlying events that revealed the practices that have come to be known as the Robo-Sign Scandal, see David Streitfeld, *From a Maine House, a National Foreclosure Freeze*, N.Y. TIMES, Oct. 14, 2010, at A1, *available at* http://www.nytimes.com/2010/10/15/business/15maine.html.

2. For a description of robo-signing practices, see CONG. OVERSIGHT PANEL, NOVEMBER OVERSIGHT REPORT: EXAMINING THE CONSEQUENCES OF MORTGAGE IRREGULARITIES FOR FINANCIAL STABILITY AND FORECLOSURE MITIGATION 9 (2010) [hereinafter CONG. OVERSIGHT PANEL], *available at* http://cybercemetery.unt.edu/archive/cop/20110402010313/http://cop.senate.gov/documents/cop-111610-report.pdf.

3. *See* Rod S. Dubitsky, *Foreclosure Flaws Trigger New Round of Uncertainty*, PIMCO ADVISORY (Jan. 2011), http://www.pimco.com/Pages/ForeclosureFlawsTriggerNewRoundofUncertainty.aspx.

4. *See* DAVID SIROTA, ESSENTIALS OF REAL ESTATE FINANCE 111 (2003) (stating "[i]n exchange for a certain consideration, usually a sum of money, a mortgagor will pledge property as collateral to back up the promise to repay a mortgage.").

5. John Carney, *A Primer on the Foreclosure Crisis*, CNBC.COM (Oct. 11, 2010), http://www.cnbc.com/id/39617381/A_Primer_On_The_Foreclosure_Crisis (noting that "[t]wenty-three states . . . require banks to go to court to get a foreclosure order. These are the 'judicial states.'"). *See also* CONG. OVERSIGHT PANEL, *supra* note 2, at 12 n.17 (stating that "[t]wenty-two states require judicial oversight of foreclosure proceedings."). *But see* JOHN RAO & GEOFF WALSH, NAT'L CONSUMER LAW CTR., FORECLOSING A DREAM: STATE LAWS DEPRIVE HOMEOWNERS OF BASIC PROTECTIONS 12 (2009), *available at* http://www.nclc.org/images/pdf/foreclosure_mortgage/state_laws/foreclosing-dream-report.pdf (placing the number of non-judicial foreclosure states at 31, including the District of Columbia, leaving only 20 "judicial states"). According to Rao and Walsh, the non-

process of foreclosure, an ancient remedy which "foreclosed" the borrower's right of "redemption": the right to satisfy the mortgage.[6] Over the years, in the "judicial foreclosure states," when a borrower is in default and the lender wishes to take back the collateral, pursuing a court order that will transfer title in the property to the lender is the exclusive remedy available to lenders to enforce the provisions of the mortgage agreement.[7]

In the thirty states that permit "non-judicial foreclosures," a court order is not required to reclaim title to the property through foreclosure.[8] The lender simply gives notice to the borrower that it intends to foreclose on the property.[9] Title to the property is typically auctioned to a third party and the transfer of the interest in the property brings with it a right to seek a court order to remove the borrower from the home, if he or she has not voluntarily vacated the premises.[10]

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judicial foreclosure states are: Alabama, Alaska, Arkansas, Arizona, California, Georgia, Hawaii, Idaho, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Mexico, Oklahoma, Oregon, Rhode Island, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, West Virginia, Wyoming, and the District of Columbia. By implication, the "judicial states" would be: Colorado, Connecticut, Delaware, Florida, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, New Jersey, New York, North Carolina, North Dakota, Ohio, Pennsylvania, South Carolina, Vermont, and Wisconsin.

6. Traditionally, this right of redemption was a right a borrower could exercise even after he or she lost the property to the lender and the lender sold it to a third party. By exercising the right of redemption, the borrower could often regain the property, and evict the new purchaser, simply by paying off the debt. The right to "foreclose the right of redemption" arose as a lender's equitable remedy to prevent the borrower from coming back later to claim the property. By obtaining a court order foreclosing the right of redemption, the lender, and any subsequent purchaser, was able to make certain that a sale of the property would not be challenged later by the borrower seeking to reclaim the property by paying off the debt. For an overview of the history of foreclosure law, see GRANT S. NELSON & DALE A. WHITMAN, REAL ESTATE FINANCE LAW 7-10 (4th ed. 2001); Michael H. Schill, *An Economic Analysis of Mortgagor Protection Laws*, 77 VA. L. REV. 489 (1991).

7. *See* Carney, *supra* note 5.

8. *See* RAO, *supra* note 5, at 11 (stating that "in thirty states and the District of Columbia, homeowners can lose their homes with no court oversight over the process and without an opportunity to be heard.").

9. *Id.* (stating that in the non-judicial foreclosure states "foreclosures are accomplished by the mortgage holder's exercise of the 'power of sale' contained in the mortgage or deed of trust. The mortgage holder does not need to initiate a court proceeding to foreclose and the homeowner has no clear access to a court hearing. The holder typically only needs to send a notice of sale to the homeowner, place a legal advertisement in a local newspaper, and hire an auctioneer to sell the property on the scheduled sale date.")

10. *See*, *e.g.*, Molly F. Jacobson-Greany, *Setting Aside Nonjudicial Foreclosure Sales: Extending the Rule to Cover Both Intrinsic and Extrinsic Fraud or Unfairness*, 23 EMORY BANKR. DEV. J. 139, 149 (2006) ("The auctioneer generally sells the property to the highest bidder….Sometimes, the highest bidder may (1) take immediate possession of the premises upon full payment of the purchase price; or (2) obtain an order for immediate possession from the court."); Grant S. Nelson & Dale A. Whitman, *Reforming Foreclosure: The Uniform Nonjudicial Foreclosure Act*, 53 DUKE L.J. 1399, 1507 (2004) ("Once foreclosure has occurred, sale purchasers sometimes have difficulty obtaining physical possession of the real estate from those whose rights the foreclosure has terminated…. [I]f foreclosure is nonjudicial, the purchaser faces a dilemma when possession is not surrendered voluntarily. Self-help, peaceable or otherwise, generally may not be used to acquire possession."). *See also*, Rao, *supra* note 5, at 12 ("After the auctioneer's hammer falls in most states, the sale itself is final and cannot be undone…. Only after the foreclosure sale is there a court proceeding in these states to remove a homeowner who does not voluntarily vacate, but by then it is usually too late to contest the sale.").

Once property is used as collateral to secure loans, there is a heightened risk that conflicting claims will arise over the right to title of the property. Disputes can occur at practically every step of the process: whether the borrower is in default, which would trigger the lender's right to foreclose; whether the lender properly foreclosed on the property by following the appropriate procedures for doing so; whether a third-party purchasing the property out of foreclosure had a right to do so, to name just a few. Over the years, important legal protections have been put in place to minimize, to the fullest extent possible, the risk that conflicting claims to the property will arise.[11] One of the most important of these protections is that in many jurisdictions a lender must maintain, in its possession, the original loan documents to prove that he or she has the right to foreclose on the property.[12] Without such evidence of authority to foreclose, multiple parties could claim the right to foreclose, making it unclear to a borrower who he or she should pay to maintain his or her mortgage obligations.[13] Furthermore, prospective third-party purchasers of properties after foreclosure might purchase such properties from parties that do not have the right to foreclose upon and sell such properties.[14] Multiple parties could claim title: the borrower, who might protest that he or she is current on his or her mortgage; the lender who possesses the original mortgage documents; a third-party purchaser, claiming he or she purchased the property from a party claiming to have had the right to sell it.[15]

Another important mechanism for protecting the rightful claims of lenders, borrowers, and third-parties is the manner through which each state requires anyone with an interest in property to notify appropriate authorities of that interest by recording evidence of that interest in a central, publicly accessible location or through some electronic, publicly searchable database.[16] These property recording systems, typically administered at the local level, serve as central access points for anyone who may wish to purchase property to determine who claims an interest in the property he or she wishes to buy.[17] Research at the local level will reveal the presence of property law claims so that one can purchase property with confidence that no one with a conflicting claim will come forward later to challenge the

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11. *See* Schill, *supra* note 6, at 492.

12. Kenneth M. DeLashmutt, *Does the Lender Have the "Original" Note in Hand?*, BANK FRAUD VICTIM CENTER, http://mortgage-home-loan-bank-fraud.com/articles/stop_foreclosure.htm (last visited Oct. 14, 2011). *See also High Court's Low Opinion of Foreclosure Process*, WHERE'S OUR MONEY? (Jan. 11, 2011), http://www.wheresourmoney.org/?p=1318.

13. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 5.

14. *Id.* (stating that "if [clear and uncontested property rights] are called into question . . . . Borrowers who have already suffered foreclosure may seek to regain title to their homes and force any new owners to move out. Would-be buyers and sellers could find themselves in limbo, unable to know with any certainty whether they can safely buy or sell a home.").

15. *Id.* For a comparison of judicial and non-judicial foreclosure processes, see Georgina W. Kwan, *Mortgagor Protection Laws: A Proposal for Mortgage Foreclosure Reform in Hawai'i*, 24 HAW. L. REV. 245, 253-257 (2001).

16. New York City's ACRIS database is one example of an online, searchable database that tracks interests in real property located within that city. *See New York City's Automated City Register Information System*, NYC.GOV, http://www.nyc.gov/html/dof/html/jump/acris.shtml (last visited Oct. 28, 2011).

17. Bill Bronchik, *The Property Recording System*, REICLUB.COM, http://reiclub.com/articles/property-recording-system (last visited Oct. 14, 2011).

purchase because the seller of the property did not have the legal right to sell it. As the following discussion shows, practices in the mortgage market over the last decade mean these protections are more important, not less. This phenomenon makes the problems revealed in the present scandal even more troublesome.[18]

B. The Modern Mortgage Market and the Rise of Securitization.

The modern mortgage market does not resemble the picture painted of it in the film "It's a Wonderful Life." There, the venerable Bailey Building & Loan used depositors' funds to make mortgage loans to local borrowers. As Jimmy Stewart's George Bailey intones when he faces his depositors who have gathered and are making a run on the institution, seeking to withdraw their savings: "the money's not here, it's in Joe's house, that's right next to yours, and in the Kennedy house and Mrs. Maicklin's house and a hundred others."[19] This quaint approach to community banking is now all but extinct. For the most part, gone are the days when a local lender makes mortgage loans in its local community and keeps such loans on its books for the duration of those loans. During the height of the subprime mortgage mania of the last decade, "originate to securitize" was the widespread practice, changing the rules of the game, and leading to many of the present problems exposed by the Robo-Sign Scandal.[20]

For decades, banks engaged in mortgage lending faced a liquidity problem.[21] They would have funds to lend to prospective borrowers, but those funds would be tied up in long-term, fixed rate loans once they committed those funds to a loan.[22] While the business of banking may have been boring and slow moving, it certainly could lead to steady, if not fantastic, profits. In the 1970s, a new model arose that promised to revolutionize mortgage finance, although it would not grow in popularity until the late 1990s.[23] Under this approach, known as mortgage

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18. The facts revealed in the Robo-Sign Scandal raise the specter that it may take years to work through the apparent defects in title of many of the entities claiming to hold mortgages on individual properties and of anyone who has purchased property from such entities. This process will inevitably raise transaction costs associated with proving title to land so that owners can use such property to secure capital and, should they wish, alienate it freely. Such a process can hamper economic development considerably. As Hernando de Soto argues, a functioning system of property titling is often what distinguishes functioning and dynamic economies from ones that are stagnant. HERNANDO DE SOTO, THE MYSTERY OF CAPITAL: WHY CAPITALISM TRIUMPHED IN THE WEST AND FAILS EVERYWHERE ELSE 39-68 (2000).

19. IT'S A WONDERFUL LIFE (Liberty Films 1946).

20. In 2008, then Securities and Exchange Commissioner Christopher Cox argued that the "originate to securitize" model was at the heart of the financial crisis because of the incentives such an approach created: "When mortgage lending changed from originate-to-hold to originate-to-securitize, an important market discipline was lost. The lenders no longer had to worry about the future losses on the loans, because they had already cashed out." *The Role of Federal Regulators: Lessons from the Credit Crisis for the Future of Regulation, Hearing Before the H. Comm. on Oversight and Gov't Reform*, 110th Cong. 26 (2008).

21. KENNETH W. EDWARDS, YOUR SUCCESSFUL REAL ESTATE CAREER 98 (2007).

22. *Id.* (stating that "[i]n the past, lenders were badly burned when changing economic circumstances forced them to start paying more for their money while their assets were tied up in long term, low-yielding real estate loans.").

23. Arturo Estrella, *Securitization and the Efficacy of Monetary Policy*, 8 FED. RES. BANK OF N.Y. ECON. POL'Y REV. 1, 3, 5 (2002), *available at* http://ftp.ny.frb.org/research/epr/02v08n1/0205estr.pdf.

securitization, lenders could convert the future income stream they could generate from the promise of mortgage payments into a present cash payoff.[24] Other institutions, typically investment banks, would purchase the right to collect the future income streams from loan originators by purchasing the mortgage from that originator.[25] The investment bank would then bundle mortgages, representing the income streams they would generate, into investment vehicles.[26] Those investment banks would then sell the right to collect those future income streams to other investors.[27] With securitization, lenders could generate profits not from the payments they would receive from the borrowers over the length of the loans they made to such borrowers, but, rather, from the fees they could collect from the investment banks for selling the loans to those banks.[28]

With the growth of mortgage securitization, the business model of many mortgage lenders would evolve over time.[29] Their main focus would change from assessing the quality of a prospective borrower and the likelihood that he or she would pay back a loan over time, to calculating the fees the lender could collect by selling loans to investment banks.[30] Given the short-term gains mortgage lenders could reap from selling such loans as quickly as possible to those banks, the quantity of loans the lender could sell was more important than the quality of such loans: i.e., total loan volume was more important than the likelihood that any particular borrower would pay back his or her loan.[31]

But mortgage securitization would not take root as a widespread practice in the mortgage industry until the early 2000s, when global events would whet the appetite of investors for mortgage-backed securities.[32] In the aftermath of the tragic events of September 11, 2001, and the recession that followed, the Federal Reserve slashed interest rates on U.S. Treasury securities in order to spur investment and prevent a complete investor retreat to the safety of those securities.[33] Investors looked for other investment vehicles, and mortgage-backed securities seemed to fit that bill: they held out the promise of solid returns on investment and the underlying securities earned a "AAA" rating from credit ratings agencies (i.e., typically the highest grade those ratings agencies assign).[34] What is

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24. *Id.* at 3. *See generally* Kurt Eggert, *The Great Collapse: How Securitization Caused the Subprime Meltdown*, 41 CONN. L. REV. 1257 (2009) (providing an overview of the securitization process and its role in the financial crisis).

25. Eggert, *supra* note 24, at 1259.

26. *Id.* at 1266.

27. *Id.*

28. *See* SIMON JOHNSON & JAMES KWAK, 13 BANKERS: THE WALL STREET TAKEOVER AND THE NEXT FINANCIAL MELTDOWN 76 (2010) (providing a description of the role of the fee structure in the securitization process and its relation to loan volume); MARK ZANDI, FINANCIAL SHOCK: A 360º LOOK AT THE SUBPRIME MORTGAGE IMPLOSION, AND HOW TO AVOID THE NEXT FINANCIAL CRISIS 95 (2009) (same).

29. *See* Eggert, *supra* note 24, at 1264-68.

30. ZANDI, *supra* note 28, at 95-96; Eggert, *supra* note 24, at 1268.

31. *See* Eggert, *supra* note 24, at 1268 (discussing the impact of securitization on the mortgage market).

32. DANIEL GROSS, DUMB MONEY: HOW OUR GREATEST FINANCIAL MINDS BANKRUPTED THE NATION 13–20 (2009).

33. *Id.*

34. *See* JOHNSON & KWAK, *supra* note 28, at 131.

more, this appetite for mortgage-backed securities coincided with the rise of a number of other phenomena. First, "innovations" in mortgage products began to take hold, and the dominance of the market by the standard 30-year fixed rate mortgage gave way to a slew of new mortgage products: adjustable rate mortgages; higher-interest mortgages; and more exotic products, like no documentation loans, interest only loans, and negative amortizing loans.[35] These non-standardized products were used to bring non-traditional borrowers into the mortgage market: i.e., borrowers with lower credit scores; with little history with credit; with lower, less regular incomes; and with few assets.[36] Although many touted the benefits of homeownership,[37] expanding the pool of prospective borrowers ultimately served one larger end: creating more mortgages to securitize, which would lead to more fees for originators, mortgage brokers, investment banks, and the credit ratings agencies that assessed the investment quality of the mortgage-backed securities at the center of the fee-generating chain.[38]

C. Drawing a Line from Securitization to the Robo-Sign Scandal.

In retrospect, the connection between securitization and the Robo-Sign Scandal appears quite clear. During the height of the subprime mortgage market, the business model of mortgage lenders—those entities that originate mortgages—was one built on quick resale of their product, not long-term "curation": a more traditional approach that included cultivating borrowers for a relationship that extended through the life of the loan.[39] As economist Joseph Stiglitz[40] and FDIC Chair Sheila Bair[41] both assert, one of the chief causes of the collapse of the mortgage market in the United States was the breakdown of this traditional borrower-lender relationship. With a focus on the quantity of the loans they could generate, and not their quality, that quality dropped considerably, particularly in the later years of the housing bubble.[42] Lenders sought a continuous stream of borrowers, creating innovative lending products to bring down traditional barriers

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35. Allan N. Krinsman, *Subprime Mortgage Meltdown: How did it Happen and How will it End*, 13 J. STRUCTURED FIN., no. 2, 2007, at 13-15 (describing lowering of underwriting criteria and creation of exotic loan products).

36. *See id.*

37. *See generally* ALYSSA KATZ, OUR LOT: HOW REAL ESTATE CAME TO OWN US (2009) (describing efforts by elected officials to promote homeownership in the United States).

38. *See* ZANDI, *supra* note 28, at 95 (discussing the role of the mortgage originators' compensation structure in the securitization process and its impact on the mortgage market); Krinsman, *supra* note 35, at 13 (providing an overview of the expansion of the subprime mortgage market in the 2000s).

39. Arva Rice, *Subprime Lenders Could Have Learned a Thing or Two From New York*, THE HUFFINGTON POST, Dec. 12, 2007, http://www.huffingtonpost.com/arva-rice/subprime-lenders-could-ha_b_76538.html (stating "[s]o why have we succeeded where others failed? Well, for one reason, because we based our business model on opportunity, not failure.").

40. *See* JOSEPH E. STIGLITZ, FREEFALL: AMERICA, FREE MARKETS, AND THE SINKING OF THE WORLD ECONOMY 14 (2010).

41. Sheila C. Blair, Chairman, Fed. Deposit Ins. Corp., Address before the U.S. House of Representatives Committee on Financial Services: Possible Responses to Rising Mortgage Foreclosures (Apr. 17,2007) (transcript available at http://www.fdic.gov/news/news/speeches/archives/2007/chairman/ spapr1707.html).

42. *See*, Krinsman, *supra* note 35, at 14-15 (describing the lowering of underwriting criteria to expand the pool of mortgage borrowers).

that kept potential customers from taking out loans.[43] This fed not only the lenders' own appetite for the fees selling those mortgages could generate, but also the desire of investors to increase their holdings in mortgage-backed securities (not to mention the interest of those investors who wanted to "short" the housing market—generate securities, particularly ones that might underperform, so that they could bet they would fail through the purchase of "Credit Default Swap" insurance to protect against such failure).[44]

But this focus on quantity not quality lies at the heart of the Robo-Sign Scandal in many less obvious ways. First, as these mortgages were packaged, sold and re-sold on the secondary mortgage market, buyers and sellers of those mortgages were often overwhelmed with the sheer volume of mortgages they needed to process and the speed with which those mortgages changed hands.[45] As a result, in the securitization process, not all transactions were properly documented and recorded, and bank personnel often failed to secure and maintain original documents throughout the course of these transactions.[46] Second, once millions of mortgages went into default, servicers and lenders charged with foreclosing on those mortgages were overwhelmed with the sheer volume of mortgages that needed some form of action taken due to borrower delinquency.[47] As a result, we now know that in tens of thousands, if not hundreds of thousands of instances, institutions seeking to foreclose on mortgages failed to follow basic procedural rules for filing papers in foreclosure actions; it is this failure that lies at the heart of the Robo-Sign Scandal.[48]

The acts underlying this scandal include the following: In documents submitted to courts where foreclosure actions were being pursued, sworn affidavits contained a range of potentially false and/or frivolous allegations. These documents, signed under oath, included allegations that the bank official or the employee of a loan servicer who signed the affidavit: (1) reviewed essential documents related to the case, (2) could attest that the borrower was in default, and (3) could make representations that the plaintiff in the case (the lender, servicer or other entity claiming an interest in the mortgage) had the right to pursue the foreclosure of the property securing the mortgage allegedly in default. These

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43. *Id.*

44. *See* MICHAEL LEWIS, THE BIG SHORT: INSIDE THE DOOMSDAY MACHINE 28 (2010) (discussing the role of investors "shorting" the housing market).

45. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 7, 9-11.

46. *See* Gretchen Morgenson, *Trying to Put a Price on Bank Errors*, N.Y. TIMES, Nov. 20, 2010, at BU1, *available at* http://www.nytimes.com/2010/11/21/business/21gret.html?pagewanted=all.

47. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 7, 9-11 (stating that bank "employees were having trouble keeping up with the crush of foreclosures.").

48. *See id.* at 9. The report outlines one example:

> In a June 7, 2010, deposition, Jeffrey Stephan, who worked for GMAC Mortgage as a "limited signing officer," testified that he signed 400 documents each day. In at least some cases, he signed affidavits without reading them and without a notary present. . . . Similarly, [Bank of America was] faced with revelations that robo-signers had signed tens of thousands of foreclosure documents without actually verifying the information in them . . . .

Id. at 11-12 (footnote omitted).

affidavits were then purportedly notarized in the presence of a notary public.[49] As the following discussion shows, in many cases, virtually every aspect of these affidavits was defective.

First, the affiants (the individuals signing the affidavits), signing these documents on behalf of his or her employer (the plaintiff in the case), often did not review any documents in the case prior to signing the affidavit.[50] Second, even if the affiant did review records related to the case, the records related to borrower payment history were often incomplete or inaccurate.[51] Third, the affiant had no way of proving that his or her employer had the original documents in its possession to prove that the plaintiff had the right to bring the action.[52] Fourth, the affiant, in all too many instances, simply did not sign the affidavit personally: this task was often delegated to other employees who, themselves, had no knowledge of the contents of the affidavit and forged the signature of the person whose name appeared on it.[53] Finally, just as the affidavits were forged in many instances, the individuals serving as notaries public often did not witness the signature of the affiant, despite acknowledging such signature and certifying them for filing with a court.[54] These affidavits, with all of these fatal defects, were then filed in courts throughout the country in support of claims that foreclosure actions should go forward.[55]

Despite the wide-spread nature of this scandal, for the most part, courts have yet to mete out penalties for these activities.[56] At present, the attorneys general of

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49. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 11 n.12; Brady Dennis, *Robo-Signer Played Quiet Role in Huge Number of Foreclosures*, WASH. POST, Sept. 22, 2010, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/09/22/AR2010092206650.html (describing the acts and practices that have come to be known as robo-signing); Gretchen Morgenson, *Flawed Paperwork Aggravates a Foreclosure Crisis*, N.Y. TIMES, Oct. 3, 2010, at A1, *available at* http://www.nytimes.com/2010/10/04/business/04mortgage.html?pagewanted=all..

50. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 9 (stating that employees were signing hundreds of documents each day without verifying information contained within).

51. *See* Carrick Mollenkamp, *Probe Targets Foreclosure Paperwork*, WALL ST. J., Oct. 13, 2010, *available at* http://online.wsj.com/article/SB10001424052748704164004575548580189204898.html.

52. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 48 (discussing a 2007 study that showed "mortgage companies who filed claims to be paid in bankruptcy cases of homeowners did not attach a copy of the note to 40% of their claims.").

53. *Id.* at 7 (stating "[e]mployees . . . have testified that they signed, and in some cases backdated, thousands of documents attesting to personal knowledge of facts about the mortgage and the property that they did not actually know to be true.").

54. *See* David Streitfeld & Gretchen Morgenson, *Foreclosure Furor Rises; Many Call for a Freeze*, N.Y. TIMES, Oct. 5, 2010, at B1, *available at* http://www.nytimes.com/2010/10/06/business/06mortgage.html?_r=2& ref=your-money.

55. *See* CONG. OVERSIGHT PANEL, *supra* note 2, at 11-12. The extent to which similar practices infected foreclosure actions in non-judicial foreclosure states is still unknown. Hopefully, the attorney general investigation will reveal whether such practices spread into those states as well. As the *Ibanez* case, discussed *infra*, reveals, however, defects in a foreclosing mortgagee's title can have an impact in non-judicial foreclose states as well by raising questions about the validity of title of subsequent purchasers who buy property from those mortgagees after foreclosure.

56. Even before the facts concerning robo-signing came to light, conscientious judges handling foreclosure actions noted the inability of at least some mortgagees to establish their standing to sue in foreclosure actions because they were unable to prove that they held an interest in the properties that were the subject of the actions. *See, e.g.*, *In re* Foreclosure Cases, 2007 U.S. Dist. Lexis 84011 (N.D. Ohio Oct. 31, 2007) (dismissing foreclosure actions for plaintiffs' failure to establish their ownership

all fifty states are conducting an investigation into the abuses described above. [57] But what remedies, if any, are available to such public officials for these practices?

First and foremost, many of these acts involved criminal conduct. Affidavits must be signed under oath and under the penalties of perjury. Those penalties in many states are criminal in nature. That allegations were made with no basis in fact (e.g., that an affiant had reviewed bank records, when he or she had not); that documents were forged; that signatures were improperly notarized: all of these acts open the participants in this course of conduct to criminal prosecution. Moreover, the filing of such fraudulent documents that contain blatant misrepresentations, omissions, and errors may have consumer protection implications as well. The remainder of this paper addresses this issue: did robo-sign practices expose lenders, mortgage servicers, and other entities responsible for such acts to civil liability under state consumer protections laws?

III. STATE CONSUMER PROTECTION THROUGH "UDAP" LAWS.

All fifty states and the District of Columbia have some statutory ban on unfair or deceptive practices in trade or commerce.[58] Many of these Unfair and Deceptive Acts and Practices (UDAP) laws were adopted in the 1970s and early 1980s as states sought new tools to protect consumers from abusive business practices.[59] These laws are modeled on the Federal Trade Commission Act (FTCA), which Congress passed in 1914 and makes unlawful "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce."[60] These state UDAP statutes are often referred to as "little FTC Acts," and provide a wide array of tools to consumers and state attorneys general to combat unfair and deceptive business practices. One of the limitations of the FTCA is that it is typically only enforced by the U.S. Federal Trade Commission. Unlike the FTCA, however, all state UDAP statutes grant consumers a private right of action to enforce their provisions[61] and state attorneys general also have standing to bring actions alleging UDAP violations.[62]

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interest in the underlying mortgages); HSBC Bank USA, N.A. v. Yeasmin, No. 50927U, slip op. at *6 (N.Y. App. Div. May 24, 2010) (finding arguments of counsel regarding plaintiff's right to foreclose "so incredible, outrageous, ludicrous and disingenuous that they should have been authored by the late Rod Serling, creator of the famous science-fiction television series, *The Twilight Zone*."). *See also* Raymond H. Brescia, *Beyond Balls and Strikes: Towards a Problem-Solving Ethic in Foreclosure Proceedings*, 59 CASE W. RES. L. REV. 305, 345 n.144 (2009) (collecting early cases).

57. Diana Olick, *State AG Robosigning Settlement Brewing*, CNBC (Nov. 16, 2010, 7:06PM), *available at* http://www.cnbc.com/id/40220735/State_AG_Robosigning_Settlement_Brewing.

58. CAROLYN L. CARTER, CONSUMER PROTECTION IN THE STATES: A 50 STATE REPORT ON UNFAIR AND DECEPTIVE ACTS AND PRACTICES STATUTES 5 (2009), *available at* http://www.nclc.org/images/pdf/car_sales/UDAP_Report_Feb09.pdf.

59. *Id.* at 5-6.

60. 15 U.S.C. § 45(a)(1) (2006).

61. *See* CAROLYN CARTER & JONATHAN SHELDON, UNFAIR AND DECEPTIVE ACTS AND PRACTICES §§ 7.2.1-7.2.2 (7th ed. 2008) (providing a general discussion of private rights of action under different states' UDAP provisions). Until recently, all states' UDAP laws except Iowa's granted individuals a private right of action to sue for violations of those laws. In 2009, the Iowa legislature amended that state's statute to permit such private rights of action. 2009 IOWA LEGIS. SERV. Ch. 167 (West).

62. *See* CARTER, *supra* note 58, at 6.

The FTCA and its state cousins are broad and remedial in nature, and prohibit conduct in general terms rather than drawing strict lines and giving clear guidance about what is outlawed and what is not.[63] When Congress first passed the FTCA, it recognized the limitations of drafting overly specific provisions given the shifting nature of unfair and deceptive conduct and the impossibility of spelling out every type of behavior the FTCA would prohibit:

> It is impossible to frame definitions which embrace all unfair practices. There is no limit to human inventiveness in this field. Even if all known unfair practices were specifically defined and prohibited, it would be at once necessary to begin over again. If Congress were to adopt the method of definition, it would undertake an endless task.[64]

Consistent with this approach, while some state statutes specifically describe the acts that can constitutes violations of those states' UDAP statutes,[65] many of these laws contain general prohibitions against unfair or deceptive practices.[66] With the goal of adapting to changing practices in the market, they contain specific clauses that describe some acts as unfair or deceptive, but also include "catch all" provisions that rein in any conduct that could be construed as unfair or deceptive.[67] As a further example of the deep connections between state laws and the FTCA, many states specifically incorporate interpretations of the FTCA into the judicial treatment and interpretation of their own UDAP statutes.[68]

In 2002, the U.S. Office of the Comptroller of the Currency (OCC) issued a guidance letter on unfair and deceptive mortgage practices in which it re-stated Federal Trade Commission interpretations of the meaning of the key components of the FTCA.[69] The OCC laid out the basic elements of claims arising under the FTCA and UDAP statutes as follows:

For an act to qualify as a "deceptive" practice, the following must occur:

- There is a representation, omission, act or practice that is likely to mislead.
- The act or practice would be deceptive from the perspective of a reasonable consumer.

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63. *See, e.g.*, VT. STAT. ANN. tit. 9, § 2453(a) (providing simply that "[u]nfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are hereby declared unlawful.").

64. H.R. Rep. No. 63-1142 (1914).

65. *See, e.g.*, Michigan Consumer Protection Act, MICH. COMP. LAWS § 445.903 (2011) (outlining thirty-two specific grounds that violate the act).

66. *See supra* note 63 and accompanying text. For a comprehensive overview of UDAP laws, see CARTER & SHELDON, *supra* note 61.

67. For example, the Kansas Consumer Protection Act defines "deceptive acts and practices" as "include[ing], but … not limited to," a series of specifically enumerated acts. KAN. STAT. ANN. § 50-626(b) (2009).

68. *See, e.g.*, MASS. GEN. LAWS ch. 93A, § 2(b) (2011) (expressing intent of state legislature that courts interpreting state statute should be guided by interpretations of the FTCA).

69. JULIE L. WILLIAMS & EMORY W. RUSHTON, OFFICE OF THE COMPTROLLER OF CURRENCY, OCC ADVISORY LETTER: GUIDANCE ON UNFAIR OR DECEPTIVE ACTS OR PRACTICES 3-6 (Mar. 22, 2002), *available at* http://www.occ.gov/static/news-issuances/memos-advisory-letters/2002/advisory-letter-2002-3.pdf.

- The representation, omission, act, or practice is material.[70]

In terms of "unfair" practices, those occur when the following are present:

- The practice causes substantial consumer injury.
- The injury is not outweighed by benefits to the consumer or to competition.
- The injury caused by the practice is one that consumers could not reasonably have avoided.[71]

Not only are UDAP statutes to be interpreted broadly, the remedies available to UDAP litigants are varied in scope and powerful. Unlike the FTCA, private individuals in most states have a right to bring an action under UDAP statutes, while the attorneys general of every state have the authority to bring actions under their respective UDAP statutes. Since this paper focuses on those enforcement powers of attorneys general only, the following discussion highlights the remedies available in such cases.[72] Where an attorney general pursues a UDAP violation in the courts, the remedies he or she may pursue often include the following: the imposition of statutorily created civil penalties and fines; the assessment of damages suffered by victims of the defendant as a result of violations of UDAP provisions, often awarded in the form of restitution; the award of punitive damages in some instances; the grant of costs and, at times, attorneys' fees to successful litigants; and the issuance of injunctions against unfair and deceptive practices.[73]

Apart from establishing the basic elements of a UDAP claim—that a particular act is either deceptive or unfair—and determining the appropriate and available remedies to seek, when assessing whether conduct related to a foreclosure of a mortgage might come within the reach of a particular state's UDAP statute, litigants face several additional questions. First, is a loan servicer or other entity involved in carrying out the foreclosure an entity covered by a relevant UDAP statute? Second, does a particular state's UDAP laws apply to mortgage transactions: that is, whether a credit transaction such as a mortgage is a "good" or a "service" where a particular state's UDAP statute covers only the sale of goods and services?[74] Third, does a particular state's UDAP law cover "post-transaction" activities like debt collection, as opposed to applying only to unfair and deceptive practices in the marketing or consummation of a sale of goods or services? As to

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70. *Id.* at 3-4.

71. *Id.* at 4-5.

72. As in the tobacco litigation of the 1990s, state attorneys general, if they pool their resources, may be able to offset the strategic advantages that many defense counsel may enjoy when compared to the resources available to the attorneys of private, individual litigants. For an overview of the history of tobacco litigation and the role played by the state attorneys general in that litigation, see Frank J. Vandall, *The Legal Theory and the Visionaries that Led to the Proposed $368.5 Billion Tobacco Settlement*, 27 SW. U. L. REV. 473 (1998). Similarly, state attorneys general can avoid sticky problems of proof that individual litigants may face, like showing reliance by a particular consumer on a particular fraudulent communication. Gary L. Wilson & Jason A. Gillmer, *Minnesota's Tobacco Case: Recovering Damages Without Individual Proof of Reliance Under Minnesota's Consumer Protection Statutes,* 25 WM. MITCHELL L. REV. 567 (1999) (discussing the litigation advantages of public attorneys general).

73. *See* CARTER & SHELDON, *supra* note 61, at app. A.

74. Stafford v. Cross Country Bank, 262 F. Supp. 2d 776, 792 (W.D. Ky 2003) (holding that not only under Kentucky's UDAP statute does extending a mortgage qualify as the sale of a service but also that "nearly every state court deciding this question in similar contexts has also reached this outcome.").

this question, many states' laws expressly include such post-transaction activities within the range of conduct they cover.[75]

Although there are many similarities among the various states' UDAP statutes, there are also many differences and variations. Some prohibit only "deceptive" acts, as opposed to deceptive and "unfair" acts.[76] Some statutes specifically exempt certain types of financial institutions from their coverage.[77] In order to assess whether a particular state's UDAP law prohibits any particular acts in any specific jurisdictions, state attorneys general, advocates, and defense counsel will have to review their own state's statutes for the specific limitations that apply to particular acts and actors within that state.[78]

Despite these variations, many states have used UDAP laws to attack questionable mortgage market practices in the courts. The following section surveys a number of cases in which state UDAP laws have been used against subprime mortgage lenders. Attorneys general from nearly every state have attempted to use UDAP remedies to rein in and rectify some of the worst abuses seen in the mortgage market during its heyday over the last decade. Following this next section, Section V, *infra.,* looks at the specific application of different UDAP statutes to unfair or deceptive practices related to foreclosures to assess whether the acts that have come to be known as the Robo-Sign Scandal might qualify as actionable conduct under UDAP laws.

IV. APPLICATION OF UDAP LAWS TO MORTGAGES.

Across the nation, state attorneys general have filed a number of high profile actions under state UDAP laws and other consumer protection statutes against lenders active in the subprime mortgage market over the last decade. Several high profile cases have resulted in sweeping settlements that resulted in the payment of penalties and attorneys fees, and forced lenders to reform their lending practices. Many of these settlements involved high price tags for the defendant-lenders, and many included remedial programs to help generate mortgage modifications and

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75. *See, e.g.*, OHIO REV. CODE ANN. § 1345.02(A) (West 2007) ("No supplier shall commit an unfair or deceptive act or practice in connection with a consumer transaction. Such an unfair or deceptive act or practice by *a supplier violates this section whether it occurs before, during, or after the transaction."*)(emphasis added); CARTER & SHELDON, *supra* note 61, at § 2.2.3.

76. For example, Arizona's Consumer Fraud Act applies to deceptive acts, but not ones that are unfair. The express terms of the act provide as follows:

> The act, use or employment by any person of any deception, deceptive act or practice, fraud, false pretense, false promise, misrepresentation, or concealment, suppression or omission of any material fact with intent that others rely upon such concealment, suppression or omission, in connection with the sale or advertisement of any merchandise whether or not any person has in fact been misled, deceived or damaged thereby, is declared to be an unlawful practice.

ARIZ. REV. STAT. ANN. § 44-1522(A) (2007).

77. *See, e.g.*, Virginia Consumer Protection Act, VA. CODE ANN. §59.1-199(D) (2011). Other states with similar exemptions include: Louisiana, Michigan, New Hampshire, and Rhode Island. *See* CARTER, *supra* note 58, at 14.

78. It is beyond the scope of this article to determine in any specific instance whether any discrete robo-sign practice, by any particular actor, is a violation of any given state's UDAP laws. Instead, I have attempted to identify those interpretations of and precedents under various states' UDAP laws to show that robo-sign practices appear to fall under such prohibitions generally.

offer relief to borrowers saddled with predatory loans.

In one of the first of these settlements, in 2006, Ameriquest, which was at the time the nation's largest subprime lender, resolved actions filed by forty-nine states and the District of Columbia alleging that the lender and its affiliates engaged in unfair and deceptive practices in the origination of subprime loans.[79] Through the settlement, Ameriquest agreed to reform its lending practices and to pay $325 million in damages.[80] This payment included restitution to consumers, compensation to the attorneys general for the cost of bringing the action, and funding for consumer education.[81]

Following the Ameriquest settlement, in 2007, the Attorney General of Massachusetts, Martha Coakley, filed a lawsuit against Fremont General Corporation (Fremont), a California-based subprime lender that had a large portfolio of subprime loans in the Bay State.[82] After an FDIC investigation revealed that Fremont had engaged in predatory lending practices, Coakley's office reached an agreement with the bank as to how it would handle foreclosures in the state.[83] When the agreement was unsuccessful in preventing the foreclosure of loans Coakley's office considered predatory in nature, she filed suit in Massachusetts state court, seeking an injunction under the state's UDAP law that would prevent Fremont from foreclosing on any loan that had questionable features.[84]

The heart of the accusations against Fremont included that the bank lured borrowers into Adjustable Rate Mortgage (ARM) loans without taking into account those borrowers' ability to repay the loans once the interest reset and that it offered 100% financing options, with the expectation that the borrower could refinance the loan (with a prepayment penalty) after a few years.[85] The trial court issued an injunction preventing Fremont from foreclosing on any loan deemed "presumptively unfair," without first giving notice to the attorney general's office and getting approval from the court.[86] The highest court in Massachusetts, in affirming the lower court's injunction, summarized Fremont's practices as follows:

> [L]oans were made in the understanding that they would have to be refinanced before the end of the introductory period. Fremont suggested in oral argument that the loans were underwritten in the expectation, reasonable at the time, that housing prices would improve during the introductory loan term, and thus could be

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79. E. Scott Reckard, *Ameriquest Settles Claims: Accused of Misleading Borrowers with Credit Problems, the Mortgage Company Will Overhaul Its Lending Practices and Pay $325 Million*, L.A. Times, Jan. 21, 2006, *available at* http://articles.latimes.com/2006/jan/21/business/fi-ameriquest21.

80. *Id.*

81. *Id.*

82. *See* Press Release, Office of Mass. Attorney Gen. Martha Coakley, Attorney General Martha Coakley Reaches $10 Million Settlement with Subprime Lender Fremont Investment and Loan (June 9, 2009) [hereinafter Press Release], *available at* http://www.mass.gov/?pageID=cagopressrelease&L=1&L0=Home&sid=Cago&b=pressrelease&f=2009_06_09_fremont_agreement&csid=Cago.

83. *Id.*

84. *Id.*

85. *Id.*

86. The terms of the trial court's injunction can be found in the lower court's decision. Commonwealth v. Fremont Inv. & Loan, No. 07-4373-BL51, 2008 Mass. Super. LEXIS 46, at *47-50 (Mass. Super. Ct. Feb. 25, 2008), *aff'd*, 897 N.E.2d 548 (Mass. 2008).

> refinanced before the higher payments began. However, it was unreasonable, and unfair to the borrower, for Fremont to structure its loans on such unsupportable optimism.[87]

Ultimately, the Massachusetts Supreme Judicial Court upheld the lower court's injunction, forcing Fremont to give the requisite pre-foreclosure notice to Coakley's office and to seek court approval of any foreclosure on a loan deemed presumptively unfair.[88] The goal of these notice/approval mechanisms was to improve the chances that Fremont would renegotiate the terms of predatory loans by bringing the attorney general's office and the bank to the negotiating table any time a delinquent loan had questionable features.[89] The parties reached a settlement of the litigation in June of 2009 through which Fremont paid $10 million to Coakley's office to be used in part to assist borrowers and made permanent the terms of the trial court's injunction, barring Fremont from foreclosing on properties without the consent of either the attorney general or the court.[90]

In a series of similar cases, with broader application—and an even higher price tag—Bank of America settled a group of lawsuits filed by 11 different attorneys general from across the country for the predatory acts of its subsidiary, Countrywide, which occurred prior to that lender's purchase by Bank of America.[91] Many of these actions included claims under the different states' UDAP laws, as well as common law fraud claims.[92] In October 2008, Bank of America settled these actions for a record $8.4 billion.[93] These billions were to be used for direct loan relief to an estimated 400,000 borrowers nationwide.[94] In addition, under the agreement, Bank of America must attempt to modify mortgages to give borrowers more favorable and affordable terms, including principal reduction where appropriate.[95] Through the settlement the bank is also supposed to provide financial assistance to families so that they can relocate if they do not appear able

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87. Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548, 558 (Mass. 2008).

88. *Id.* at 559-62.

89. *See* Press Release, *supra* note 82.

90. *Id.*

91. *See* Gretchen Morgenson, *Countrywide to Set Aside $8.4 Billion in Loan Aid,* NY TIMES, October 5, 2008, *available at* http://www.nytimes.com/2008/10/06/business/worldbusiness/06iht-06countrywide.16713621.html.

92. *E.g.,* Complaint, California v. Countrywide Fin. Corp., No. LC081846 (Cal. Super. Ct. June 24, 2008), *available at* http://ag.ca.gov/cms_attachments/press/pdfs/n1582_draft_cwide_complaint2.pdf (alleging violations of California Business and Professionals Code section 17500 (prohibiting making or disseminating untrue or misleading statements) and section 17200 (prohibiting unfair competition)); Complaint, Connecticut v. Countrywide Fin. Corp., No. 1207 (Conn. Super. Ct Aug. 5, 2008), *available at* http://www.ct.gov/ag/lib/ag/consumers/countrywidelawsuit.pdf (alleging a violation of the Connecticut Unfair Trade Practices Act); Complaint, Illinois v. Countrywide Fin. Corp., No. 08CH22994 (Cook County Cir. Ct. June 25, 2008), *available at* http://www.ag.state.il.us/pressroom/2008_06/countrywide_complaint.pdf (alleging violations of Illinois' Consumer Fraud and Deceptive Practices Act); Complaint, Office of the Att'y Gen., Dep't of Legal Affairs, Florida v. Countrywide Fin. Corp., No. 08 30105 03 (Fla. Cir. Ct. June 30, 2008), *available at* http://myfloridalegal.com/webfiles.nsf/WF/MRAY-7G5G7L/$file/CountrywideComplaint.pdf (alleging a violation of Florida's Deceptive and Unfair Trade Practices Act).

93. Morgenson, *supra* note 91.

94. *Id.*

95. *Id.*

to afford a loan even on more favorable terms.[96] The agreement also requires borrowers assisted through the modification or relocation program to sign a general release, relieving Bank of America and Countrywide from any future liability for illegality in the terms of the original mortgages written by Countrywide.[97]

As I have argued elsewhere, these cases and others suggest that litigation in the wake of the financial crisis, and the foreclosure crisis that has followed it, possesses features that fit it within the category of cases known as "mass torts."[98] In the mass torts context, litigation can be used to bring sweeping relief to a wide range of victims through procedural mechanisms that can facilitate global settlements of complex social problems.[99] Deborah Hensler has identified some of the key features of this category of cases as follows: numerosity, commonality, interdependence of case values, controversy over causation, emotional or political heat, and higher than average claim rates.[100] Other important hallmarks of mass torts litigation include aggregating techniques for adjudicating questions of liability, causation and damages, as well as mechanisms for compensating plaintiffs through settlement;[101] and collaboration among attorneys on both sides of the litigation, including sharing information about claim values, relevant evidence, discovery strategy, and litigation strategy.[102]

To the extent that the acts underlying the Robo-Sign Scandal, and those efforts that may be used to rectify the harm emanating from it, may fit under the rubric of the mass torts paradigm, state attorneys general may pursue litigation and can use their authority under state UDAP laws to promote meaningful mortgage relief for borrowers whose properties have been swept up in the scandal.[103] The tools at the disposal of state attorneys general in the wake of the Robo-Sign Scandal—namely,

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96. *Id.*

97. *See* People v. Countrywide Fin. Corp., No. LC081846, at 20 (Cal. Super. Ct. Oct. 20, 2008), *available at* http://ag.ca.gov/cms_attachments /press/pdf/n1618_cw_judgment.pdf.

98. See, Raymond H. Brescia, *Tainted Loans: the Value of a Mass Torts Approach in Subprime Mortgage Litigation*, 78 U. CIN. L. REV. 1, 13 (2009).

99. *See id.* at 13-17.

100. Deborah R. Hensler, *A Glass Half Full, a Glass Half Empty: The Use of Alternative Dispute Resolution in Mass Personal Injury Litigation*, 73 TEX. L. REV. 1587, 1596 (1995).

101. Brescia, *supra* note 98, at 14. *See also* Judith Resnik, *From "Cases" to "Litigation,"* 54 LAW & CONTEMP. PROBS. 5, 25–40 (1991) (providing an overview of aggregative techniques).

102. *See* Byron G. Stier, *Resolving the Class Action Crisis: Mass Tort Litigation as Network*, 2005 UTAH L. REV. 863, 893 (2005) (describing the benefits of collaboration among counsel in mass torts litigation). The state attorneys general have instituted just this type of collaborative effort, as the offices of all fifty state attorneys general are working together to investigate robo-sign practices and consider the law enforcement response. *See* Press Release, Nat'l Ass'n of Attorneys General, 50 States Sign Mortgage Foreclosure Joint Statement (October 13, 2010), *available at* http://www.naag.org/joint-statement-of-the-mortgage-foreclosure-multistate-group.php.

103. Litigation by state attorneys general certainly fits under the mass torts umbrella; the massive litigation filed by a majority of the state attorneys general in the 1990s against the tobacco industry is a paradigmatic example of a mass tort dispute. *See* Howard M. Erichson, *The End of The Defendant Advantage in Tobacco Litigation*, 26 WM. & MARY ENVTL. L. & POL'Y REV. 123, 135-36 (2001) (noting that state attorneys general have entered "the fray" in mass torts litigation on the plaintiffs' side); Wendy E. Wagner, *Rough Justice and the Attorney General Litigation*, 33 GA. L. REV. 935, 961-62 (1999) (noting that litigation led by state attorneys general has been "uniquely successful" against tobacco manufacturers); ROBERT L. RABIN, REGULATING TOBACCO 177 (Robert L. Rabin & Stephen D. Sugarman eds., 2001) (describing role of attorneys general in tobacco litigation).

for our purposes here, state UDAP laws—place such law enforcement officials at the nexus of a wide-ranging series of fraudulent acts. Such acts have tainted foreclosure processes throughout the nation and raise questions about the legitimacy of title claims in tens of thousands, if not millions, of cases. Mass torts litigation, with its aggregating techniques and its ability to achieve global settlements in complex disputes, is particularly suited to address the actions at the heart of the Robo-Sign Scandal. As the next section argues, by pursuing UDAP claims (or perhaps just raising the threat of such claims), state attorneys general can generate positive social ends in the wake of the scandal, including a reduction in the social cost of the foreclosure crisis.

V. Application of UDAP Laws and Remedies to the Foreclosure Process.

This next section addresses two questions: first, whether state UDAP laws have been applied to practices related to foreclosure proceedings themselves; and, second, whether UDAP remedies offer creative and effective responses to not just the Robo-Sign abuses in particular, but also the problem of delinquent and underwater mortgages in general.

A. The Application of UDAP Laws to Foreclosures.

A range of practices fall under state UDAP laws. One of those practices is debt collection. Courts routinely consider practices related to foreclosures as practices worthy of review under the rubric of state UDAP laws. Courts have also recognized questionable servicer and lender actions related to the foreclosure process itself as giving rise to a UDAP claim.

The leading case in this area, *Smith v. Commercial Banking Corp.*,[104] was a bankruptcy proceeding filed in federal bankruptcy court in Pennsylvania. There, the Third Circuit Court of Appeals construed Pennsylvania's UDAP statute to find that deceptive practices undertaken during the course of carrying out a foreclosure gave rise to claims under that state's UDAP laws.[105] The appellate court found that the bank had engaged in two practices that justified such claims: first, the bank had knowingly served its foreclosure papers at the borrower's former residence; and, second, it had sent out a 30-day notice of intent to foreclose on the borrower, but began the foreclosure process before the expiration of the 30-day time period set forth in the notice and required by state law.[106] The court found as follows:

> Although the failure properly to serve the foreclosure complaint may not by itself be an unfair practice, here we have considerably more. Fidelity's conduct effectively deprived Smith both of an opportunity to cure the default before imposing additional and unnecessary costs and expenses on her, and of her opportunity to defend in court. We hold that such conduct is "unfair" in the most basic sense of the word and fraudulent within the meaning of the UDAP.[107]

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104. 866 F.2d 576 (3d Cir. 1988).
105. *Id.* at 585-86.
106. *Id.* at 586.
107. *Id.* at 584-85.

Similarly, in an action filed in federal court in Massachusetts, the court in *Morse v. Mutual Federal Savings & Loan Association of Whitman*[108] found a violation of that state's UDAP law where a lender engaged in a series of acts that ultimately led to the commencement of an unjustified foreclosure on a home mortgage loan.[109] There, the lender and borrowers had engaged in a series of transactions, and the lender had taken action against the borrowers for their apparent failure to maintain sufficient funds in a checking account to cover their expenses in running a small business.[110] When the borrowers tried to tender payment on their mortgage in a proper and timely manner, the lender refused such payment, froze their personal checking account and improperly commenced a foreclosure action on their home mortgage.[111] The jury found for the plaintiff-borrowers on their state UDAP claims, and the court endorsed that finding as follows:

> Improperly freezing the [checking] account, without notice . . . led to excess interest charges, and also may have led, ultimately, to a reduction in [plaintiff's] credit sales. The wrongful institution of foreclosure proceedings, if nothing else, resulted in unjustified charges by defendant of its costs and attorney's fees. Finally, defendant's refusal to allow refinancing through [a second] bank denied plaintiffs the use of a sum of money well in excess of their mortgage with defendant. . . .[112]

The court found that all of these acts fell within the scope of Massachusetts's UDAP law.[113]

Similarly, in *Hart v. GMAC Mortgage Corp.*,[114] a case arising out of bankruptcy court in Massachusetts, the court there found that a pattern of lender activity in a foreclosure action gave rise to a claim under that state's UDAP law.[115] There, the lender commenced a foreclose action after misapplying the payments the borrower had made to the lender and sending conflicting correspondence to the borrower about his level of indebtedness and whether he was even in default (partly because different units within the bank were not communicating effectively and the bank's computer system was not accessible to all units of the bank dealing with the borrower).[116] The court concluded that these actions constituted unfair trade practices in violation of the Massachusetts UDAP law.[117] It awarded the borrower a range of relief, including attorney's fees for the cost associated with filing a bankruptcy petition, an injunction, and an order directing the bank to communicate with credit reporting agencies to advise them that the borrower was not in foreclosure on the mortgage loan.[118]

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108. 536 F. Supp. 1271 (D. Mass. 1982).
109. *Id.* at 1281-82.
110. *Id.* at 1275-76.
111. *Id.* at 1276.
112. *Id.* at 1281-82.
113. *Id.*
114. 246 B.R. 709 (Bankr. Mass. 2000).
115. *Id.* at 733-35.
116. *Id.* at 713-21.
117. *Id.* at 734.
118. *Id.* at 736-37.

Finally, in *Flenniken v. Longview Bank & Trust Co.*,[119] the Supreme Court of Texas found that a bank that had purchased a mortgage note from a third party lender could be liable to the borrower under that law for violations of that state's UDAP laws.[120] The third party, a contractor, had agreed to construct a residence for the borrowers, who, in exchange, executed a mechanic's lien naming the contractor as the payee.[121] The contractor both sold the loan note to the bank and completed only about twenty percent of the repairs, even after drawing down the bulk of the loan proceeds.[122] The purchasing bank, in turn, went ahead and foreclosed on the property even though the work was not completed.[123] The Texas Supreme Court upheld the trial court's finding that the act of foreclosing on the property when the repairs were not completed was itself a violation of the state's UDAP laws, even if carried out by the bank, which was not responsible for the fact that the work was not completed on the home.[124]

As these cases make clear, unfair and deceptive practices carried out in the foreclosure setting itself can give rise to claims that a foreclosing entity violated a state's UDAP laws. As made apparent through the revelations from the Robo-Sign Scandal, lenders, servicers, and other entities processing foreclosure filings engaged in a range of deceptive acts, all of which would qualify as acts violating the key provisions of UDAP laws: filing false and misleading affidavits, forging and improperly notarizing those affidavits, and making claims that they had the authority to foreclose on mortgages when, at least in some instances, they possessed neither the ability to prove such claims or even the knowledge to assert them. If such acts violate a particular state's UDAP laws, what remedies might litigants pursuing UDAP claims seek? The following discussion addresses these and other questions.

B. The Use of UDAP Remedies to Promote Loan Modifications.

Given the broad and remedial nature of UDAP laws, the filing of fraudulent affidavits qualifies as a deceptive act under most states' definition of the term under their respective UDAP provisions. State attorneys general can thus pursue a range of remedies under their respective UDAP statutes, where such remedies are available, including civil penalties, restitution and injunctions. In addition, the actual damages to borrowers wrongfully foreclosed upon would seem quite substantial, especially if they lost equity in their home or were rendered homeless

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119. 661 S.W.2d 705 (Tex. 1984).

120. *Id.* at 707.

121. *Id.* at 706.

122. *Id.*

123. *Id.*

124. *Id.* at 707-08. In contrast, the Louisiana Supreme Court found that there could be no violation of that state's UDAP law where the challenged foreclosure was not contrary to law. Levine v. First Nat'l Bank, 948 So. 2d 1051, 1066 (La. 2006). In reaching this conclusion, the court did not find that foreclosure practices were beyond the reach of the UDAP laws, just that the foreclosure challenged in that action was not improper or unlawful, thus it could not be unfair or deceptive. *Id.* at 1058, 1066. The court there also ruled that the grounds that gave rise to the foreclosure emanated from mortgage provisions that were consistent with federal law, thus any argument that such provisions themselves violated state law would be pre-empted by the federal law in question. *Id.* at 1066. For a discussion of federal pre-emption of state mortgage laws, see *infra* Part VI.

as a result of a foreclosure in which a lender or servicer engaged in UDAP violations in carrying out that foreclosure. Given the high stakes at risk when deceptive practices are utilized in the foreclosure process, the threat of substantial civil penalties and punitive damages, as well as injunctions preventing foreclosures from going ahead when tainted by robo-sign practices, is considerable. At the end of the day, however, the prospect of a resolution to such claims that minimizes the threat of substantial penalties or injunctions barring foreclosures from taking place, or unwinding foreclosures already completed, should be enough to get lenders and servicers to the negotiating table to bring about solutions to the Robo-Sign Scandal that are more acceptable to borrowers, lenders, servicers and investors alike.

Apart from resolving such defects, the best solution to the broader foreclosure crisis is principal reduction: i.e., bringing outstanding debt in line with home values.[125] This both reduces the monthly payments borrowers must make and strengthens incentives to continue to make those payments by restoring the prospect of borrower equity in the home. The threat of significant penalties and injunctions through state UDAP laws for the abuses evident in the Robo-Sign Scandal may be just the type of leverage needed to convince interested parties that such principal reductions are a more palatable resolution to UDAP enforcement actions than allowing them to drag out in the courts, where litigants may obtain more costly awards and more sweeping remedies.[126]

Such principal write-downs would not be unprecedented in the UDAP enforcement context. In both the *Fremont* litigation and the Countrywide/Bank of America settlements discussed above,[127] UDAP prosecutions were used as leverage

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125. STIGLITZ, *supra* note 40, at 100 (calling mortgage principal reduction "the best option for the country."). One of the strongest critiques of mortgage modification programs during the current crisis is that they rarely result in a reduction of the principal of the underlying mortgage to bring it more into line with the value of the property in question. *See* David Indiviglio, *Only 0.1% of Government Mortgage Modifications Cut Principal?*, THE ATLANTIC, June 24, 1010, *available at* http://www.theatlantic.com/business/archive/2010/06/only-01-of-government-mortgage-modifications-cut-principal/58685/ ("[o]ne of the chief criticisms of the government's Home Affordable Mortgage Program (HAMP) is that it hasn't been doing enough to convince underwater homeowners to rework their loans. The key to doing that is principal modifications."). *See also* OFFICE OF THE COMPTROLLER OF THE CURRENCY AND THE U.S. DEPT. OF THE TREASURY, OCC AND OTS MORTGAGE METRICS REPORT: DISCLOSURE OF NATIONAL BANK AND FEDERAL THRIFT MORTGAGE LOAN DATA 27 (2010), *available at* http://www.ots.treas.gov/_files/482142.pdf (noting just 0.1% of mortgages modified permanently in the first quarter of 2010 through the Home Affordable Modification Program resulted in principal reduction).

126. Another point of contention in foreclosure litigation is the fact that a portion of properties impacted by the present foreclosure crisis are also a part of the Mortgage Electronic Registration System (MERS), which has come under a degree of scrutiny by courts and litigants recently. *See, e.g.*, *In re* Agard, No. 810-77338-reg, slip op. at 35-37 (Bankr. E.D.N.Y. Feb. 10, 2011) (rejecting ability of MERS to assign mortgage); Landmark Nat'l Bank v. Kesler, 216 P.3d 158 (Kan. 2010) (same). To resolve such questions, mortgagees may face similar demands as those that may be made of them to settle robo-sign disputes. For a discussion of the MERS system, see Christopher L. Peterson, *Predatory Structured Finance*, 28 CARDOZO L. REV. 2185, 2212-13 (2007). For a discussion of the standing of MERS in foreclosure actions, see Christopher L. Peterson, *Foreclosure, Subprime Lending and the Mortgage Electronic Registration System*, 78 U. CIN. L. REV. 1359, 1375-86 (2010). A further discussion of MERS is beyond the scope of this article, however.

127. *See supra* Part IV. As this article goes to print, at least with respect to many of the state attorneys general and most of the largest banks, a settlement of charges over the Robo-Sign scandal, one

to promote mortgage modifications, which could include principal reductions where appropriate. Getting banks to the settlement table through the pursuit of UDAP actions for robo-sign abuses could be a primary goal of such actions. Should lenders and servicers wish to defend those actions on the merits, and risk judicial intervention that might translate into tens of thousands of dollars in penalties and punitive damages in each case, such would be their right. At the same time, a sensible response to such actions by the institutions caught up in the Robo-Sign Scandal would be to consider more robust foreclosure mitigation strategies, including meaningful principal write-downs and reductions. State attorneys general should not hesitate to pursue UDAP remedies for robo-sign abuses and, at the same time, they should be willing to discuss resolution of UDAP cases in ways that can help bring about mortgage principal reductions for borrowers that need such assistance.

Furthermore, to the extent the investigation of robo-sign practices may expose deeper problems with title, failing to address these problems in a comprehensive way may mean that questions about title may linger, and costly litigation may ensue, for years to come, even in non-judicial foreclosure states. An example of what may unfold over the coming years was made apparent in the recent decision out of Massachusetts in which a bank's title to property seized after foreclosure was called into question, and its ability to sell such property after that foreclosure was rejected by the state's highest court.

In *U.S. Bank National Ass'n v. Ibanez*,[128] the Massachusetts Supreme Judicial Court found that in two consolidated cases the failure on the part of two foreclosing banks to prove they had an interest in two mortgages meant that their non-judicial foreclosures of the affected properties were defective.[129] The dispute over the rights of the respective parties in the underlying properties arose in quiet title actions filed by the foreclosing banks.[130] The plaintiff banks had pursued an affirmative action to ensure that there were no questions clouding their title to the underlying properties.[131] The court rejected the banks' claims, saying they had not proven that they had the right to foreclose on the properties in the first place, and voided the foreclosures.[132] As is apparent from this case, disputes such as these can arise in both judicial and non-judicial foreclosure states (Massachusetts is among the latter group). Unresolved real and perceived defects in title will likely create a burdensome drag on the alienation of property moving forward, as was the case in *Ibanez*. The investigation into and potential litigation surrounding robo-sign practices may also serve to clear up these kinds of disputes by developing an effective mechanism for resolving such disputes.

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that would involve principal reductions for up to one million borrowers, appears imminent. Gregory Korte and Julie Schmit, *HUD Secretary: Mortgage settlement deal "very close,"* USA TODAY, January 19, 2012. http://www.usatoday.com/money/economy/housing/story/2012-01-18/mortgage-settlement/526533821/1.

128. 458 Mass. 637 (2011).

129. *Id.* at 638.

130. *Id.* at 638-39.

131. *Id.*

132. *Id.* at 650-52.

VI. FEDERAL PRE-EMPTION OF STATE UDAP LAWS: A POTENTIAL BARRIER TO THE APPLICATION OF UDAP LAWS TO THE FORECLOSURE CONTEXT.

Even in situations where robo-sign practices are found to violate a particular state's UDAP laws, there is still one more question that needs to be answered about the viability of UDAP claims in the wake of the Robo-Sign Scandal: whether a particular state's UDAP laws are pre-empted by federal banking laws with respect to federally chartered financial institutions.[133] As the following discussion shows, while this question is a legitimate one, it would appear that the scope of federal pre-emption is not so broad as to encompass and displace the authority of state attorneys general to bring enforcement actions under state UDAP laws to address abusive foreclosure practices.

To the extent national banks[134] are caught up in the Robo-Sign Scandal, one issue that may arise in the investigation of this scandal is the extent to which federal law, most notably the National Bank Act, may pre-empt the ability of state attorneys general to enforce state UDAP laws. For example, Bank of America is both a nationally chartered financial institution, which is organized under the National Bank Act and supervised by the U.S. Office of the Comptroller of the Currency (OCC), as well as the nation's largest servicer of existing mortgage loans.[135] Federally chartered banks like Bank of America may raise as a defense to any UDAP actions whether the fact that they are "national" banks pre-empts the

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133. It is also possible that defendants facing claims that robo-sign practices violate a particular state's UDAP laws may raise several other arguments. First, that actions filed in federal court under diversity jurisdiction and charging UDAP violations in the course of foreclosure proceedings may run afoul of the *Rooker-Feldman* doctrine. This doctrine holds that federal district courts should not review the actions of state courts. *See* District of Columbia Court of Appeals v. Feldman, 460 U.S. 462, 479 (1983). For an overview of the *Rooker-Feldman* doctrine, see Susan Bandes, *The Rooker-Feldman Doctrine: Evaluating Its Jurisdictional Status,* 74 NOTRE DAME L. REV. 1175 (1999). A second, and similar, argument defendants may raise involves abstention: that is, asking a federal court to abstain from adjudicating UDAP claims where the prosecution of such claims may interfere with pending state court proceedings (here, foreclosure actions of the underlying mortgages). *See* Younger v. Harris, 401 U.S. 37 (1971). For an overview of the *Younger* abstention doctrine, see ERWIN CHEMERINSKY, FEDERAL JURISDICTION 819-65 (5th ed. 2007). In both instances, the UDAP claims would have to be adjudicated in federal court and the plaintiffs in those cases would have to seek an injunction against any pending foreclosure actions for either potential defense to apply. Because these questions are beyond the scope of this article, I will not address them here.

134. "National banks" are banks organized under the federal National Bank Act, 12 U.S.C. § 21 (2006), and regulated by the Office of the Comptroller of the Currency under the Act. Many of the largest banks, like Bank of America, JPMorgan Chase, and Citigroup are national banks. *See* OFFICE OF THE COMPTROLLER OF THE CURRENCY, LIST OF NATIONAL BANKS AND FEDERAL BRANCHES AND AGENCIES ACTIVE AS OF 06/30/2011, *available at* http://www.occ.treas.gov/topics/licensing/national-bank-lists/bank-list-national-by-name-v2.pdf. Many subprime lenders, on the contrary, were mortgage lenders not given federal charters and generally not overseen by federal banking regulators. *See* David D. Troutt, *Disappearing Neighbors*, 123 HARV. L. REV. 21, 23 (2010) (describing the environments in which subprime lenders operated as "regulatory antimarkets, beyond the reach of federal and state regulators and without the safeguards protecting capital investment in what became 'prime' neighborhoods.").

135. *See* E. Scott Reckard, *Bank of America to Increase Loan Modification Staffing*, L.A. TIMES, Dec. 4, 2010, at B2, *available at* http://articles.latimes.com/2010/dec/04/business/la-fi-bofa-loanmods-20101204 (noting Bank of America's status as the largest servicer of home loans in the nation after it purchased Countrywide Financial Corp. in 2008).

application of state law to their foreclosure practices. In sweeping actions over the last fifteen years, both the OCC and the U.S. Office of Thrift Supervision (OTS) issued opinions and regulations that attempted to prevent state legislatures and state attorneys general from enforcing state laws against nationally chartered banks and thrifts.[136] For the most part, these agencies were successful in preventing state-based, anti-predatory laws from applying to federally chartered banks and thrifts, even if those banks provided services within the states in which those laws applied.[137] In a 2007 decision of the U.S. Supreme Court, *Watters v. Wachovia Bank, N.A.*,[138] the pre-emptive effect of federal laws was upheld, not just against federally chartered banks themselves, but also to the extent those laws applied to shield the subsidiaries of these banks from the application of many state banking laws.[139] Due to the anti-regulatory philosophy of the Bush Administration,[140] state attorneys general, and state laws they enforced, were often the last line of defense against predatory lenders. But the pre-emptive effect of OCC and OTS regulations restricted the ability of these laws and state law enforcement officials to rein in the predatory practices of federally chartered banks at the height of the subprime mortgage frenzy of the last decade. In the words of one state attorney general, the Supreme Court decision endorsing a broad view of pre-emption "'took 50 sheriffs off the beat at a time when lending was becoming the Wild West.'"[141]

While the Dodd-Frank legislation scales back the extent of federal pre-emption of state laws, the effect of such changes did not go into effect until July of 2011,[142] and such changes are only prospective: they do not apply retroactively. But the fact that the changes to federal pre-emption of state banking laws did not go into

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136. After passage of the Dodd-Frank financial reform legislation over the summer, the responsibilities of the OTS will be transferred to the OCC. *See Hearings on the Dodd-Frank Wall Street Reform and Consumer Protection Act Before the S. Comm. On Banking, Housing, and Urban Affairs*, 111th Cong. 4 (2010) (statement of John Walsh, Acting Comptroller of the Currency).

137. *See, e.g.*, Arthur E. Wilmarth, Jr., *The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services*, 36 J. Corp. L. 893, 909 (2011) ("In contrast to the half-hearted measures taken by federal regulators, many states passed laws and brought enforcement actions to combat predatory lending. However, the OCC and the OTS responded to those initiatives by preempting the states' authority to enforce state consumer protection laws against national banks, federal thrifts, and their subsidiaries and agents."); Adam J. Levitin, *Hydraulic Regulation: Regulating Credit Markets Upstream,* 26 Yale J. on Reg. 143, 150-51 (2009) ("Beginning in the 1970s, however, as banks began to engage in large-scale interstate consumer lending, courts began to hold that state consumer-protection laws were preempted as applied to federally chartered financial institutions."); Alan H. Scheiner, *State Subprime Lending Litigation and Federal Preemption: Toward A National Standard*, 30 Pace L. Rev. 253, 268 (2009) ("Numerous courts of appeals have held that state laws or regulations similar to subprime lending laws--such as those prohibiting certain practices in consumer lending--are inapplicable to national banks on the basis of the OCC regulation (or a similar Office of Thrift Supervision ("OTS") regulator)….").

138. 550 U.S. 1 (2007).

139. *See id.* at 20-21.

140. Admittedly, the OTS's pre-emptive regulations were adopted under President Clinton, but they were not enforced aggressively until 2003.

141. Jo Becker, *White House Philosophy Stoked Mortgage Bonfire*, N.Y. TIMES, Dec. 21, 2008, at A1, *available at* http://www.nytimes.com/2008/12/21/business/21admin.html?pagewanted=all.

142. Designated Transfer Date, 75 Fed. Reg. 57252 (Sept. 20, 2010) (Treasury Secretary's setting of the "transfer date" of responsibilities to the Consumer Financial Protection Bureau, which is also the date the new pre-emption rules take effect).

effect until the summer of 2011 does not end the debate in terms of pre-emption and state UDAP laws. In fact, in June of 2009, the Supreme Court narrowed its prior ruling on pre-emption, and issued its decision in the case of *Cuomo v. Clearinghouse Ass'n.*[143] That decision upheld the power of state attorneys general to bring enforcement actions against federally chartered banks under state law.[144] This power was framed in contrast to those entities' inability to regulate federally chartered banks and thrifts in terms of their banking practices per se.[145] In *Clearinghouse*, the Court found that a state attorney general does not have "visitorial" powers over a national bank, that is: it cannot inspect bank records or carry out the particular functions of a bank regulator when that bank is a national bank carrying out powers expressly granted it from the national government.[146] At the same time, banks, whether they are national banks or not, engage in a range of practices that *are* covered by state law alone, like state civil rights statutes. The Court held that an attorney general may bring judicial actions that seek to enforce such laws, regardless of the status of the bank as a national bank.[147] This ruling has important implications in the UDAP setting, as the following discussion shows.

At the same time, for the purposes of pursing claims against those banks involved in the Robo-Sign Scandal that might claim pre-emption under either OCC or OTS regulations still in effect, such pre-emption does not appear to impact the types of practices brought into question in this scandal. Pre-emption is often invoked to prevent state regulation of federally chartered banks and thrifts in terms of the powers they carry out pursuant to their federal charters. But state laws of general application, which are not directed towards federally chartered institutions in a discriminatory way—for example, by giving state chartered institutions a leg up on their federal counterparts—fall outside the scope of pre-empting laws and regulations. As the Supreme Court in *Watters* made clear: "Federally chartered banks are subject to state laws of general application in their daily business to the extent such laws do not conflict with the letter or the general purposes of the [National Bank Act]."[148]

Moreover, consistent with protecting state authority to regulate in areas traditionally left to the states, laws related to property, contract and tort are generally preserved regardless of pre-emption. This is particularly germane to any discussion of the Robo-Sign Scandal, where the actions of servicers and other foreclosing entities (to the extent they might be able to invoke federal pre-emption based on their status as affiliates of federally chartered institutions), are largely within an area of law typically left to the states, regardless of the status of the financial institution: i.e., state real property law. Foreclosure processes are traditionally found in state laws, and there is no federal law of foreclosure. In fact, the regulation that gave rise to the claims of OTS-regulated thrifts that they were exempt from state banking laws expressly exempts from preemption those state laws that "incidentally" affect the operations of OTS-regulated entities and are

143. 129 S. Ct. 2710 (2009).
144. *Id.* at 2721-22.
145. *Id.* at 2720.
146. *Id.* at 2721.
147. *Id*. at 2721-22.
148. Watters v. Wachovia Bank, N.A., 550 U.S. 1, 11 (2007).

more traditionally relegated to state law, such as contract, tort, criminal law, and real property law.[149] Similarly, the OCC's pre-emption regulations do not apply to state laws pertaining to contract, the "right to collect debts," the acquisition and transfer of property, and any other law that only "incidentally" affects a national bank's lending activities.[150]

In one case in which the question of the scope of federal pre-emption of state UDAP laws figured prominently, the court, the federal district court for the Northern District of California, found that the manner in which a federally chartered bank handled mortgage payments was not exempt from the reach of California's UDAP statute, regardless of the fact that the financial institution had a federal charter.[151] In *Jefferson v. Chase Home Finance,* the court concluded as follows:

> The core of each of Plaintiff's causes of action is the claim that Chase misrepresented how it would credit prepayments to Plaintiff's account. Plaintiff also contends that Chase's systematic breach of the promises about how it would credit prepayments is an unfair business practice under the [California UDAP statute] . . . Plaintiff does not claim that California consumer protection laws require Chase to service or process loans, include specific content in its disclosures, or handle repayment of loans in any particular manner-requirements that would be preempted. *See* 12 C.F.R. §34.4 (a). Instead Plaintiff claims that the laws require Chase to refrain from misrepresenting the manner in which it *does* service loans. The core issue in this case will be not whether or when Chase is permitted to place payments in suspense accounts, but whether Chase misrepresented to customers what it would do with their payments.
>
> The duty to refrain from misrepresentation falls on all businesses. It does not target or regulate banking or lending, and it only incidentally affects the exercise of banks' real estate lending powers. Chase has not articulated any way that enforcing state laws prohibiting misrepresentation to consumers would interfere with a bank's nationwide operation or "obstruct, impair or condition" its ability to engage in real estate lending any more than those laws impair the operation of any business.[152]

As the decision in *Jefferson* holds, regulating the representations the lender in question made about how it serviced the plaintiff's loan—i.e., its disclosures about how it credited payments—is not pre-empted by the force of federal laws designed to ensure that state laws do not discriminate against federally chartered institutions or interfere with the manner in which the federal government regulates them. Holding federally chartered institutions to a duty of care that all businesses in a state must meet does not constitute an interference with essential federal rights.

In the wake of the Robo-Sign Scandal, to permit enforcement of state UDAP laws by applying them to the foreclosure practices of lenders and loan servicers, even when those entities are federally chartered institutions or their subsidiaries, preserves the state's traditional authority over its laws concerning real property.

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149. 12 C.F.R. § 560.2(c) (2011).

150. 12 C.F.R. § 34.34 (b) (2011).

151. Jefferson v. Chase Home Fin., No. C06-6510 TEH, 2008 WL 1883484, at *13-14 (N.D. Cal. April 29, 2008).

152. *Id.* at *12-13.

This area of law is one that has historically been exempt from the pre-emptive effect of federal banking laws, evidence of which is apparent from the OCC and OTS regulations, which, carve out exceptions for these laws from pre-emption. To the extent federally chartered institutions and their subsidiaries have engaged in deceptive practices in terms of the tactics they have used in pursuing foreclosures, federal preemption should not be a barrier to state enforcement of UDAP laws against such tactics.[153]

Moreover, even if a court were to find that certain regulatory functions of state attorneys general might be curtailed by federal preemption with certain entities, the ability of those offices to bring enforcement actions under those same laws would appear to have been preserved by the Supreme Court's decision in *Cuomo v. Clearinghouse Ass'n*, discussed above.[154] The meaning of the *Clearinghouse* case is still to be determined. In any event, it preserves the ability of state attorneys general to bring enforcement actions against even federally chartered institutions. A question remains, though: do enforcement actions under state UDAP laws fall within the powers of an attorney general's office authorized in *Clearinghouse*? If so, even if the laws themselves may be pre-empted to the extent a regulatory body seeks to use them to carry out mere regulatory oversight of a federally chartered institution, the *Clearinghouse* decision seems to suggest that pre-emption would not limit the ability of state attorneys general to bring state enforcement actions under those same laws.

Apart from this potential dispute over the meaning of the Supreme Court's decision in the *Clearinghouse* case, with respect to federal pre-emption of any enforcement actions directed towards federally chartered institutions and their subsidiaries under state UDAP laws, the following facts remain. First, financial institutions that are not regulated by the OCC or the OTS would not be able to raise pre-emption as a defense. Second, even federally chartered banks and thrifts would have to show that the application of the UDAP laws as they relate to foreclosure processes and the collection of debts are being applied in a discriminatory fashion in terms of federal banks and thrifts. Finally, in order to invoke pre-emption as a defense, such institutions would have to show that such laws are not within the scope of laws traditionally enforced by the states, such as state laws related to real property, contracts, and torts. As a result, it is unlikely that federal pre-emption of state UDAP laws is a significant barrier to enforcement actions brought to rein in the practices evident in the Robo-Sign Scandal.

VII. CONCLUSION

The Robo-Sign Scandal has exposed deep flaws in the practices of many mortgage lenders and mortgage servicers. These flaws expose those entities to liability under many states' consumer protection laws, notably the collection of state statutes considered UDAP laws. These UDAP laws are broad in their reach and offer litigants pursuing claims under them a range of remedies, from restitution to injunctions. The threat of litigation from lawsuits under these statutes is real,

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153. Of course, those institutions that do not qualify as federally chartered institutions would not be able to claim federal preemption of state UDAP laws.

154. *See supra* notes 143-47 and accompanying text.

and the pressure to settle such actions in the wake of admissions of abusive foreclosure practices will be strong. State attorneys general pursuing such claims, and wielding such threats can work with lenders and servicers to come to sensible solutions that not only root out abusive practices, but help reform the mortgage market. There is no better place to start in this road to reform than working with lenders to write down and forgive mortgage principal. This will help align borrower debt with the assets that secure that debt. Short of such settlements, financial institutions face the prospect of stiff penalties, multiple damage claims and injunctions preventing them from bringing tainted foreclosure actions. Aligning borrower debt to home values will help re-align and balance incentives, reducing the risk of foreclosure for hundreds of thousands of borrowers. Such a re-alignment will also help stabilize the mortgage market by reducing the number of mortgages in the foreclosure pipeline and slowing the flow of properties entering the mortgage market at reduced, post-foreclosure prices. Once supply slows, demand will rise, as will prices.

The state attorneys general have an opportunity, through strategic use of their UDAP enforcement powers, to pursue claims that foreclosure practices ran roughshod over consumer protection laws and the laws that govern those foreclosures. This opportunity can give rise to critical advances in stabilizing home prices and the mortgage market, and reduce volatility in those prices and markets. State law enforcement officials should not hesitate to pursue these claims and utilize all tools at their disposal to move from scandal to settlement, and uncertainty to resolution.