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Right of Rescission after Jesinoski v Countrywide

A few weeks ago I notified you about the denouement of the Supreme Court's granting of certiorari on April 28, 2014 to decide whether, as held by the Eight Circuit, a borrower must file a lawsuit to exercise and preserve the TILA rescission right within three years of consummating the loan, or whether simply providing written notice of rescission is sufficient to do so. I have followed this litigation virtually from its inception, given the considerable implications for creditors. [736 F.3d 1134 (8th Cir. 2013)]

My White Paper on this matter can be found HERE and HERE. It was published on September 2, 2014 and entitled, "TILA versus TILA: Rescission by Notice or Lawsuit." My analysis of the Supreme Court's ruling, issued on January 13, 2015, was published on the same date as the ruling. You can read it HERE and HERE. In a unanimous opinion, the Supreme Court held that providing a notice of rescission within the three-year period is timely and sufficient to trigger rescission within the meaning of 15 USC § 1635(f), the operative statute.

The notion that the borrower would have to sue in order to effectuate rescission simply had no traction because, as the court noted, nothing in the applicable section of TILA requires the borrower to sue in order to exercise the right of rescission, and nothing in Section 1635(f) changed this conclusion, because that section tells borrowers "*when* the right to rescind must be exercised, [but] says nothing about *how* that right is exercised". (Emphasis in Original)

Personally, I thought the defendant, Countrywide, had a non-argument, when it allowed for only requiring written notice of rescission within the first three days after the loan closing, pursuant to Section 1635(a), accepting that the written notice was sufficient to rescind a loan within three years after the closing, but, and this is a big BUT, only if the parties agreed that the lender failed to make the required disclosures. Thus, Countrywide argued that if the parties disputed the adequacy of the lender's disclosures, the written notice would not suffice and a lawsuit was required. I thought this was some pretty fancy footwork on the part of defendant's counsel, and the Supreme Court certainly rejected this puffed out stretch of an argument. To quote the ruling: "Section 1635(a) nowhere suggests a distinction between disputed and undisputed rescissions, much less that a lawsuit would be required for the latter."

Since the ruling, I have been asked several questions regarding certain aspects of the Supreme Court's findings and its impact on creditors. In this essay, I consolidate my thinking on this subject, with a view to considering the actual and potential issues arising from the ruling.

I think there are a few outcomes of the decision. But first permit me to offer a thumbnail overview of the issue itself.

Creditors must notify borrowers in writing that borrowers have three business days to rescind the credit transaction by providing written notice of their intent to do so to the creditor. [§ 1635(a)] This right of rescission procedure is well known. Indeed, given any consumer credit transaction that results in the creditor retaining or acquiring a security interest in the borrower's principal dwelling, the right of rescission is mandatory. By 'consumer credit transaction', I mean to include subordinate mortgage loans and refinance mortgage loans wherein borrowers receive additional credit.

If a creditor fails to provide the written disclosure, or provide inadequate written disclosure, the borrower's rescission rights are extended to three years after the loan was originated. [§ 1635(f)]

The Supreme Court was asked to decide whether borrowers are required to provide a notice of intent to rescind, or affirmatively sue the creditor to effectuate the rescission rights within the three year limitation period. [Jesinoski, 135 S. Ct. 790, 790 (2015)] The decision reached by the Supreme Court was that the plain language of the statute (*supra*) requires only the former, stating that "[t]he language of the statute leaves no doubt that rescission is effected when the borrower notifies the creditor of his intention to rescind." [Idem at 792]

The defendant's gambit was to use the equitable principle in common law for rescission. Under common law, the equitable principle is that borrowers must be able show that they can tender the property received at origination back to the creditor before being permitted to rescind the loan. Specifically, rescission traditionally requires either that the rescinding party return what was received before a rescission could be effectuated (rescission at law) or else that a court must affirmatively decree rescission (rescission in equity). The Supreme Court's position, however, was that this principle cannot be applied to interpret the TILA rescission regime. [Idem at 793]

Countrywide's argument fell flat when it argued that Congress could not have intended to eliminate both of these long-standing common law requirements and allow a borrower to rescind a loan simply by writing to its lender. Furthermore, the defendant advanced a counterfactual conundrum which hypothesized that allowing rescission in this manner would simply encourage frivolous claims from borrowers. But the Supreme Court had the last word: "The clear import of §1635(a) is that a borrower need only provide written notice to a lender in order to exercise his right to rescind. To the extent §1635(b) alters the traditional process for unwinding such a unilaterally rescinded transaction, this is simply a case in which statutory law modifies common-law practice."

Now, as I see it, there are several outcomes of this decision.

- Borrowers preserve their TILA rescission claims by merely notifying their creditors in writing of their intent to rescind within the applicable three-year time period.

  Outcome: Creditors could see some increase of rescission notices and will continue to see distressed borrowers allege TILA rescission claims, in some instances commencing such claims many years after rescission notices are received.

- If a creditor disputes a borrower's rescission notice, it is an open question as to when the borrower must file suit to enforce the right of rescission.

  Outcome A: It is possible that the limitations period could be indefinite, as long as the borrower timely provides the rescission notice.

  Outcome B: As the CFPB posited in Sherzer v. Homestar Mortgage Services, the general TILA one-year statute of limitations [in 15 USC § 1640(e)] may begin to run from the date the borrower sent the rescission notice. [707 F.3d 255, 266 n. 8 (3rd Cir. 2013)]

- Creditors will need to reevaluate their responses to borrower rescission notices that they intend to dispute.

  Outcome: Creditors must consider the cost of disputing the rescission attempt against the potentially added cost and complexity of rescinding a loan many years after origination, since the procedures of rescission generally require creditors to return all funds received from the borrower and to terminate security interests - even if borrowers are unable to return any funds they received at origination. In other words, the costs to creditors will be far higher over time as rescission takes place from the date of the loan. [12 USC 1635(b)]

- A lender has twenty days to determine whether the rescission notice is valid or whether it is going to seek a declaratory judgment in court that would block the rescission based on the theory that it provided sufficient disclosures.

  Outcome: Creditors may consider retaining a security interest in the mortgage or give up its rights to get repaid. This means going through records from mortgages from commencement of origination.

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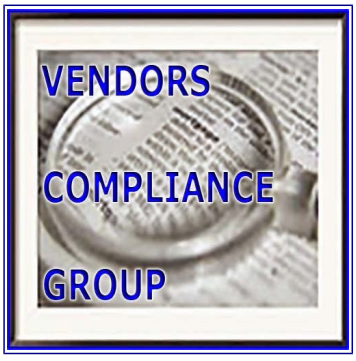

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Outcome B: Creditors may consider having a blanket policy of challenging all such rescission notifications in order to protect their interests, by seeking a declaratory judgment that there was no disclosure violation.

- Repayment of principal is going to be a contested area in the future. The Supreme Court did not address the question of what happens when the borrower does not return the principal. In a rescission a lender is supposed to return any points and fees that a borrower paid on a mortgage, release its senior secured lien, and be repaid the principal amount of the loan.

  Outcome: A reading of the decision is that, due to recsission, a creditor may be left without a return of the principal and without any claim against the borrower. It is relatively easy to predict that future litigation will center on who owes whom what - and when whatever it is that must be repaid will be repaid!

After Jesinoski, lenders face questions of how to handle rescission notices received more than three days after the close of a transaction. For instance, what if the lender disagrees with the borrower's assertion that the lender failed to provide the requisite disclosures, and thus rescission should not be available? Does the lender still have to release the mortgage? Can (or must) a lender file suit within 20 days of receipt of such a letter to protect its interest? What internal policies and procedures will the Consumer Financial Protection Bureau be looking for lenders to establish? Presumably, lower courts will answer these questions. In the meantime, creditors should revisit their right of rescission policies and procedures, with a view of ascertaining that they reflect the Jesinoski ruling.

Labels: Consumer Financial Protection, Jesinoski v. Countrywide, TILA, Truth in Lending Act

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