

JOURNAL of LAW REFORM ONLINE

COMMENT

NOTICE IS NOT ENOUGH: WHY TILA REQUIRES MORE THAN A LETTER OF INTENT

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The federal Truth in Lending Act¹ (TILA) provides borrowers with protections and remedies against certain actions by lenders. TILA allows, in some circumstances, a borrower to rescind a loan from a lender within a three-year period from when the loan is made. However, a circuit split has developed regarding how the right to rescind must be exercised. Of the circuits that have considered this question, some require a lawsuit to be filed within the three-year period to rescind the loan.² Other circuits have held that providing notice of the intent to rescind the loan within the three-year period is sufficient to rescind the loan, even if a lawsuit is not filed until beyond the three-year time limit.³ This Comment argues that in order to rescind the loan, courts should require that an actual lawsuit be filed before the three-year period expires.

TILA was enacted to ensure that borrowers could make informed decisions about consumer loans.⁴ In fact, TILA is one of the most powerful tools that borrowers have to protect themselves from predatory and unscrupulous lenders.⁵ To ensure that lenders comply with TILA's disclosure requirements, TILA grants borrowers a limited right to rescind a loan secured by the borrower's residence if the lender fails to make the required disclosures.⁶ This incentivizes lenders to follow the requirements

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1. Truth in Lending Act, 15 U.S.C. §§ 1601-1667f (2006).

2. See, e.g., *McOmie-Gray v. Bank of Am. Home Loans*, 667 F.3d 1325 (9th Cir. 2012), *Rosenfield v. HSBC Bank, USA*, 681 F.3d 1172 (10th Cir. 2012).

3. See, e.g., *Gilbert v. Residential Funding LLC*, 678 F.3d 271 (4th Cir. 2012).

4. Michael Sabet, Comment, *Slamming the Door in the Consumer's Face: Courts' Inadequate Enforcement of TILA Disclosure Violations and the False Hope of a Foreclosure Defense*, 115 PENN ST. L. REV. 183, 185 (2010).

5. Kimberley Ayer, Note, *Striking a Balance: When to Extend the Right to Rescind Under TILA*, 85 ST. JOHN'S L. REV. 261, 262 (2011).

6. *McOmie-Gray*, 667 F.3d at 1327.

of the Act. Under TILA, a borrower has a three-day period following the consummation of the loan to exercise their right to rescind.⁷ However, when a lender fails to provide the required disclosures to the borrower, TILA provides that the time for rescission is extended for three years or until the property is sold, whichever is earlier.⁸ This three-year period is a statute of repose that governs “the life of the underlying right” to rescind.⁹ The right to rescind is completely extinguished at the end of the three-year period.¹⁰

Although the right to rescind is clearly established by the statute, a circuit split regarding the proper way and time to exercise this right has developed in the circuits that have addressed this issue. In the Ninth and Tenth Circuits, a borrower must actually file a lawsuit to enforce the borrower’s right to rescind within the three-year statute of repose.¹¹ If the lawsuit is not filed within the three-year period, the right to rescind is lost.¹² But in the Fourth Circuit, the right is preserved beyond the three-year period if the borrower provides notice to the lender that the borrower intends to rescind the loan.¹³ An actual lawsuit does not need to be filed within the three-year period.¹⁴

Resolution of this divergence depends on either a United States Supreme Court ruling or congressional action to clarify the procedural aspects of the rescission provision of TILA. In the interim, the split has implications for lenders, borrowers, and the mortgage industry. Lenders are more likely to receive from borrowers rescission notices that purport to preserve the right to

7. 15 U.S.C. § 1635(a) (2006).

8. 15 U.S.C. § 1635(f) (2006).

9. *Beach v. Ocwen Fed. Bank*, 523 U.S. 410, 417 (1998).

10. *Id.*

11. *See McOmie-Grey v. Bank of Am.*, 667 F.3d 1325, 1327–28 (9th Cir. 2012) (holding that rescission is not automatic upon borrower’s mere notice of rescission, and the borrower cannot raise the right to rescind after the three-year period has run); *Rosenfield v. HSBC Bank, USA*, 681 F.3d 1172, 1188 (10th Cir. 2012) (concluding that a borrower’s notice to bank is insufficient to exercise or preserve a borrower’s right to rescind a loan transaction under TILA, and TILA established a right of action that must be exercised by invoking the power of the courts.).

12. *Rosenfield*, 681 F.3d at 1188.

13. *See Gilbert v. Residential Funding LLC*, 678 F.3d 271, 278 (4th Cir. 2012) (holding that borrowers effectively exercised their right to rescind under TILA by sending notices of rescission to lenders even though the borrowers did not file suit until more than three years after the consummation of the loan).

14. *Id.*

rescind even if a lawsuit is not filed within three years. Given that asserting an intention to rescind is without cost (unlike a lawsuit), it's likely that lenders will receive more of these notices in an attempt by borrowers to influence restructuring and foreclosure negotiations by threatening full rescission, even beyond the three-year period. Consequently, depending on the jurisdiction in which a suit is ultimately brought, this notice may be effective. In those cases, lenders cannot be certain that a loan transaction is final even after the three-year statute of repose has expired. Such practice will likely add monitoring and response costs to loans, which may ultimately be passed on to the borrower in the form of higher fees or interest rates.¹⁵The circuit split also creates unnecessary uncertainty for borrowers. Borrowers must investigate the governing law in their jurisdiction and ensure that the right to rescission is not lost if a suit is not filed within three years. As borrowers are often less informed and sophisticated than lenders, such uncertainty may place a burden and inequity upon these individuals.

The approach taken by the Ninth and Tenth Circuits requiring a lawsuit to be filed within three years is the best resolution of this circuit split. Such a rule provides the clearest notice to the lender that the borrower is seeking to enforce the legal right to rescind. This rule also encourages a borrower to sue only if the borrower has a non-frivolous claim for rescission, rather than allowing the borrower to give mere notice of rescission to influence negotiations between the two parties. As this "notice" would not be governed by the same rules that govern legal actions, including rules that provide sanctions for frivolous lawsuits,¹⁶ there is less of an incentive for borrowers to assess the merits of their claims before seeking to rescind. Requiring a lawsuit to be filed within three years also provides more certainty to lenders and borrowers on the status of the rescission claim, and ultimately reduces the cost to borrowers of dealing with these claims. These cost savings may be passed on to consumers, thus improving the lending

15. *Rosenfield*, 681 F.3d at 1885 (10th Cir. 2012) (explaining that circumstances could change in the period between when notice is given of the intent to rescind and the consummation of the judicial action to rescind which would make the rescission "costly and difficult." These additional costs would likely ultimately be borne by borrowers.)

16. *See, e.g.*, FED. R. CIV. P. 11.

climate for those in need of secured capital.¹⁷

Finally, this rule maintains the policy purposes of a statute of repose. Potential defendants are insured repose after the lapse of time.¹⁸ A strict limit “encourages prompt assertion of claims to allow full and fair litigation of the issues” while evidence, documentation, and witnesses are more recent and available.¹⁹ “Thus, the private interests of potential defendants are served” in resolving claims filed within the time period, “while public interests are served as well by keeping stale litigation out of the courts, barring inefficient use of limited public resources.”²⁰ The certainty and efficiency that this outcome promotes is both embodied by the governing law and is an equitable resolution for both lenders and borrowers.

17. David Smith & Gregg Stevens, *The Impact of TILA on the Debtor-Creditor Relationship*, 61 CONSUMER FIN. L. Q. REP. 296, 299 (2007) (explaining that “creditors inevitably seek to cover the costs and legal risks,” which has “contributed to overall higher costs” to consumers).

18. Daniel Rothstein, Comment, *Truth in Lending: The Right to Rescind and the Statute of Limitations*, 14 PACE L. REV. 633, 640 (1994).

19. *Id.*

20. *Id.*