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The (Un)informed Use of Credit: The Need To Clarify Consumers' Right Of Rescission Under The Truth In Lending Act

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THE (UN)INFORMED USE OF CREDIT: THE NEED TO CLARIFY CONSUMERS' RIGHT OF RESCISSION UNDER THE TRUTH IN LENDING ACT

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Currently, over 1 million properties in the United States are in some stage of foreclosure. Although foreclosure rates have decreased in recent years, they remain significantly higher than pre-lending-crisis rates, revealing that foreclosure is relatively commonplace in the current housing market. As such, consumers increasingly rely on consumer protection laws to provide security against the threat of foreclosure and unfair credit practices. The Federal Truth in Lending Act (TILA) was enacted to assure meaningful disclosure of credit and finance terms in consumer credit transactions. Among the various remedies available under TILA, consumers have the right to rescind the entire credit transaction if the lender fails to make certain disclosures. Section 1635(f) provides that a consumer must exercise his or her right to rescind within three years of the loan's consummation, or the right expires. Thus, the question becomes: how does a consumer exercise his or her right to rescind under TILA? According to the Ninth and Tenth Circuit Courts of Appeal, a consumer must file an action for rescission to exercise his or her right to rescind under Section 1635(f). On the other hand, the Fourth Circuit, relying largely on the Federal Reserve Board's regulations to TILA, held that a consumer exercises his or her right to rescind merely by sending notice to the lender within the statutory three-year period. This Note explores the split of authority on consumers' right to rescind under TILA and ultimately proposes that the Fourth Circuit's holding be reversed by the Supreme Court of the United States.

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I. INTRODUCTION

Imagine a scenario in which a mortgage lender receives a fax just hours before a foreclosure sale, informing the lender that the borrower—the previous owner of the foreclosed residence—is rescinding the initial loan because certain required disclosures were absent from the loan documents. As a result, the lender is now obligated to reconvey the deed of trust and return all fees and interest payments the borrower made on the loan.[1] Can the borrower lawfully rescind the contract in this situation? Yes. As this Note highlights below, consumers may rescind specific contracts within three years of their consummation under the Truth in Lending Act (TILA) if the lender fails to disclose certain required information.[2]

Now imagine that the lender, having knowledge that such an action is possible up to three years after the initial loan's consummation, has planned accordingly and held the foreclosure sale two months after the statutory three-year period has passed. This time, the original borrower files an action to rescind the initial loan for the same reason. The case goes to trial and the court rules in favor of the borrower. Has the court decided correctly here? Can the borrower lawfully rescind the agreement *after* the statutory three-year period has run? The Supreme Court, in *Beach v. Ocwen Federal Bank*,[3] appeared to answer this question in the negative.[4] However, recent circuit court decisions have signified a split of authority regarding the temporal life of consumers' rescission rights, making the answer to the question posed above contingent upon the federal jurisdiction in which the action arises.

In 2012, the Fourth Circuit held that a consumer could bring a rescission action after TILA's three-year period, as long as the consumer delivered sufficient notice of rescission to the lender within the statutory time frame.[5] In contrast, the Ninth[6] and Tenth[7]

1. *See* 15 U.S.C. § 1635(b) (2006).

2. *See infra* Part II.B.

3. 523 U.S. 410 (1998). "[T]he Act permits no federal right to rescind, defensively or otherwise, after the 3-year period of § 1635(f) has run." *Id.* at 419.

4. *See id.* at 410 ("A borrower may not assert the § 1635 right to rescind . . . after § 1635(f)'s 3-year period has run.").

5. *Id.* at 278.

Circuits have each declared that a consumer must exercise his or her right to rescind by filing suit within three years of the loan's consummation, or that right is completely extinguished. Although circuit splits are commonplace in American jurisprudence,[8] the split of authority examined in this Note, in the context of a depressed and unstable housing market, significantly threatens the basic foundations[9] of TILA and its supplemental regulations by establishing indefinite and variable constraints on consumer rescission rights.[10]

Currently, over 1 million properties in the United States are in some stage of foreclosure.[11] In fact, in August 2014 alone, one in every 1126 housing units nationwide received a foreclosure filing.[12] Although foreclosure rates have decreased in recent years, they remain significantly higher than pre-lending-crisis rates,[13] revealing the relative commonplace of foreclosure in the current housing market. As such, while consumers grapple with the decision of whether they should enter into a mortgage loan transaction, "one of the most complex financial transactions of a consumer's life,"[14] they increasingly rely on consumer protection laws, such as TILA, to provide security against the threat of foreclosure and unfair credit practices.[15] Specifically, TILA permits consumers to rescind certain credit transactions within statutorily defined timeframes.[16] However,

6. Miguel v. Country Funding Corp., 309 F.3d 1161, 1164–65 (9th Cir. 2002).

7. Rosenfield v. HSBC Bank, USA, 681 F.3d 1172, 1182 (10th Cir. 2012).

8. Mary Garvey Algero, *A Step in the Right Direction: Reducing Intercircuit Conflicts by Strengthening the Value of Federal Appellate Court Decisions*, 70 TENN. L. REV. 605, 605–06 (2003).

9. *See infra* Part II.A.

10. *See infra* Parts III.B–C, IV.B.1–2.

11. *See National Real Estate Trends & Market Info*, REALTYTRAC, http://www.realtytrac.com/statsandtrends (last visited Oct. 12, 2014) (defining "some stage of foreclosure" as including default, auction, or bank owned).

12. *See National Real Estate Trends*, REALTYTRAC, http://www.realtytrac.com/trendcenter/trend.html (last visited Oct. 12, 2014) ("The foreclosure rate is calculated by dividing the total housing units in the state (based on the most recent estimate from the U.S. Census bureau) by the total number of properties that received foreclosure filings during the month (using most recent monthly data available), and that number is expressed as a ratio.").

13. *See* Marcy Gordon, *US Foreclosure Filings Hit 5-year Low in September*, HUFFINGTON POST (Oct. 11, 2012, 7:26 AM), http://www.huffingtonpost.com/huff-wires/20121011/us-foreclosure-rates/.

14. Lea Krivinskas Shepard, *It's All About the Principal: Preserving Consumers' Right of Rescission Under the Truth in Lending Act*, 89 N.C. L. REV. 171, 171 (2010).

15. *See id.* at 188–89.

16. *See infra* Part II.B.

the split of authority regarding the temporal life of that right threatens not only to undermine many of the central goals of TILA[17] but also to hinder economic growth and stability.[18]

Part II of this Note explores the current state of the law, beginning with a discussion of TILA's history and the congressional intent behind TILA's passage. It then provides an overview of the right of rescission, both at common law and under TILA and its accompanying regulations. Finally, Part II summarizes the relevant case law, including the Supreme Court's holding in *Beach*, the Tenth Circuit's decision in *Rosenfield v. HSBC Bank, USA*,[19] and the Fourth Circuit's contrasting opinion in *Gilbert v. Residential Funding, LLC*.[20]

Part III of this Note examines the primary problems with the current state of the law regarding consumers' rescission rights. The split of authority has weakened federal TILA regulations and presented various interpretive issues for consumers, lenders, and judges alike.[21] The differing interpretations of TILA and its regulations weaken basic foundations of consumer protection legislation, including consumer leverage, lender protection, and economic stability.[22]

Part IV of this Note proposes a judicial solution to the split of authority. Specifically, the Supreme Court should invalidate the Fourth Circuit's holding in *Gilbert* and expressly uphold the decisions in *Beach* and the Ninth and Tenth circuits.[23] In support of this proposal, Part IV engages in a prototypical plain language analysis of the applicable statutes and regulations, applies the judicial precedent in *Beach*, and examines various policy considerations.

Finally, Part V justifies the proposal by arguing that it supports the congressional intent behind TILA's passage, promotes economic certainty and stability, and preserves statutory consumer leverage.

Ultimately, this Note seeks to provide a tangible and principled solution to a current and significant problem. As discussed below,

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17. *See infra* Part III.A–B.
18. *See infra* Part III.C.
19. 681 F.3d 1172 (10th Cir. 2012).
20. 678 F.3d 271 (4th Cir. 2012).
21. *See infra* Part III.A.
22. *See infra* Part III.B–C.
23. *See Rosenfield*, 681 F.3d 1172; Miguel v. Country Funding Corp., 309 F.3d 1161 (9th Cir. 2002).

TILA, with its accompanying administrative regulations, comprises the paramount consumer protection directive. However, the legal status quo, represented by a split of authority, ultimately hinders TILA's consumer protection purpose by reducing consumer leverage and injecting uncertainty into an already uncertain and fragile lending market. By invalidating the Fourth Circuit's decision in *Gilbert*, as this Note proposes, the Supreme Court can clearly identify the temporal boundary of the right of rescission under TILA and, as a result, support and adhere to Congress's original intent, protect consumer leverage, and promote economic strength and stability.

II. BACKGROUND

To understand the current state of consumer rescission rights, it is necessary to discuss the federal statutory provisions that define and limit these rights, the supplemental administrative regulations that clarify and expand upon these federal provisions, and the judicial interpretations of both the provisions and regulations. The first section discusses the origin and basic premise behind Congress's first major foray into consumer protection, TILA. The second section examines the specific rescission provisions of TILA and the Federal Reserve Board's (the "Board") accompanying regulations (collectively known as "Regulation Z"). Finally, the remaining sections summarize significant case law addressing the right to rescind under TILA, including the Supreme Court's decision in *Beach*, the Tenth Circuit's opinion in *Rosenfield*, and the Fourth Circuit's opinion in *Gilbert*.

A. Consumer Protection Codified: The Truth in Lending Act

TILA, a progeny of President Lyndon Johnson's "Great Society" ideals,[24] is a strict liability statute that requires credit lenders to clearly and accurately disclose certain terms and

24. Shepard, *supra* note 14, at 184; *see also* LYNDON B. JOHNSON, *Remarks at the University of Michigan (May 22, 1964)*, *in* 1 PUBLIC PAPERS OF THE PRESIDENTS OF THE UNITED STATES: LYNDON B. JOHNSON 1963–64 704, 704–07, *available at* http://coursesa.matrix.msu.edu/~hst306/documents/great.html (discussing the erosion of community bonds, poverty, urban decay, and inadequate education).

conditions to consumers in credit transactions.[25] Its passage in 1968 "marked the birth of modern consumer legislative activism"[26] and resulted in a wave of subsequent federal and state consumer credit protection laws.[27] Prior to TILA's enactment, the consumer credit landscape suffered from a debilitating combination of deregulation and preemption of state consumer laws by weak federal legislation.[28] For example, consumers often found it difficult or impossible to shop for credit, because unsupervised creditors used various methods of calculating interest and determining which additional charges would be included in the interest rate, resulting in vague and multifarious interest calculations across the lending market.[29] Furthermore, according to Senator Paul H. Douglas, creditors often

> compound[ed] the camouflaging of credit by loading on all sorts of extraneous fees, such as exorbitant fees for credit life insurance, excessive fees for credit investigation, and all sorts of loan processing fees . . . so that any percentage rate quoted [was] completely meaningless and deceptive.[30]

Finally, consumer confusion was further aggravated by the fact that creditors often buried essential information in legalese and fine print.[31]

Congress enacted TILA to protect consumers from "inaccurate and unfair credit" practices,[32] "increase transparency" in the credit markets, and promote the "informed use of credit."[33] The statute applies to virtually all forms of consumer credit transactions—from credit card plans to small loans to home mortgages.[34] Essentially, the

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25. *See* RALPH J. ROHNER & FRED H. MILLER, TRUTH IN LENDING 2 (Supp. 2009).

26. ELIZABETH RENUART & KATHLEEN KEEST, NAT'L CONSUMER LAW CTR., TRUTH IN LENDING § 1.2.1, at 4 (6th ed. 2007).

27. *See id.* ("Subsequently, Truth in Lending became just one of several titles in the Consumer Credit Protection Act which encompasses much of the other federal consumer legislation which followed. Some states now have enacted their own truth in lending acts or similar consumer credit disclosure laws."); ROHNER & MILLER, *supra* note 25, at 1 ("[I]t explored new territory, and other federal consumer credit laws followed in its path.").

28. *See* RENUART & KEEST, *supra* note 26, at 2; Shepard, *supra* note 14, at 184.

29. *See* RENUART & KEEST, *supra* note 26, at 1.

30. 109 CONG. REC. 2029 (1963) (statement of Sen. Douglas).

31. RENUART & KEEST, *supra* note 26, at 2.

32. 15 U.S.C. § 1601(a) (2006).

33. Shepard, *supra* note 14, at 185 (quoting 15 U.S.C. § 1601(a)).

34. ROHNER & MILLER, *supra* note 25, at 2; *see also* Shepard, *supra* note 14, at 185–86 ("TILA's application is broad-ranging from open-end credit transactions like credit card and home equity loans to closed-end transactions like car loans and mortgages.").

provisions of TILA apply whenever a creditor[35] offers or extends credit, subject to a finance charge,[36] to a consumer[37] for personal, family, or household purposes.[38] As a disclosure statute, TILA primarily requires creditors to disclose the true cost of credit prior to the consummation of the credit transaction by using standardized terminology established by the act itself and by the Board.[39] The cost of credit at its most basic level includes the "finance charge"[40]—the total dollar cost of credit—and the "annual percentage rate"[41]—"the annualized simple interest rate of that finance charge."[42] However, Congress has appended numerous other terms to the cost of credit, terms that often do not affect the actual cost, such as default charges and security interests.[43] In addition, the statute also contains numerous regulatory provisions to prevent substantive abuses by creditors that cannot be fully addressed through mandatory disclosures alone.[44] Thus, notwithstanding TILA's conception as a pure disclosure statute, it has functioned, for all intents and purposes, as a comprehensive consumer credit protection statute.[45]

35. 12 C.F.R. § 226.2(a)(17) (2013) ("Creditor means: A person who regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments (not including a down payment), and to whom the obligation is initially payable, either on the face of the note or contract, or by agreement when there is no note or contract.").

36. *Id.* § 226.4(a) ("The finance charge is the cost of consumer credit as a dollar amount. It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.").

37. *Id.* § 226.2(a)(11) ("Consumer means a cardholder or natural person to whom consumer credit is offered or extended. However, for purposes of rescission . . . the term also includes a natural person in whose principal dwelling a security interest is or will be retained or acquired, if that person's ownership interest in the dwelling is or will be subject to the security interest.").

38. Shepard, *supra* note 14, at 185–86.

39. RENUART & KEEST, *supra* note 26, at 4–5.

40. 12 C.F.R. § 226.4(a) (defining "finance charge").

41. *Id.* § 226.14(a) (defining "annual percentage rate").

42. ROHNER & MILLER, *supra* note 25, at 3.

43. *Id.*

44. *See id.* at 2 ("[T]he Act includes qualified or absolute prohibitions on prepayment penalties, balloon payments, increases in interest upon default, negative amortization, prepaid payments, extending credit without adequate consideration of repayment ability, and direct lender to contractor payments in certain high rate/high fee residential mortgages; limitations on acceleration and changes in terms in home equity plans and reverse mortgages; and limitations on the liability of a cardholder for unauthorized use and on the ability of a card issue to enforce payment if there is a valid defense to payment.").

45. *Id.*

Since its enactment in 1968, TILA has been amended and revised several times.[46] One notable revision occurred in 1980 when President Jimmy Carter signed the Depository Institutions Deregulation and Monetary Control Act of 1980, which included the Truth in Lending Simplification Act (the "Simplification Act").[47] The Simplification Act, unlike previous amendments that merely clarified technical terms, changed the basic philosophy of TILA.[48] The revised TILA trimmed much of the unnecessary and confusing disclosure requirements and retained only the information Congress deemed useful to a consumer's credit decisions.[49] For example, an itemized disclosure of the amount financed was no longer required, because the resulting complexity could often make it more difficult for a consumer to detect inaccurate disclosures.[50] TILA again saw substantial change in 1994 as a result of the predatory lending crisis.[51] Congress amended TILA by passing the Home Ownership and Equity Protection Act, which enhanced certain disclosure requirements for statutorily defined "high cost" mortgages exceeding certain price-threshold triggers.[52] Finally, most recently, in response to the subprime mortgage crisis, the Board added a new category of "higher-priced mortgage loans" subject to heightened disclosure requirements by the Board's regulations.[53]

Although TILA has been amended and supplemented various times over the past four decades, it has retained its original consumer protection initiative by providing borrowers with the tools and information necessary to make informed credit decisions.

B. A Consumer's Controversial Sword: TILA's Right of Rescission

TILA provides consumers with access to a variety of remedies when creditors violate various provisions of the statute.[54] Expectedly, consumers may bring an action for actual and statutory damages,

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46. *Id.* at 1.
47. RENUART & KEEST, *supra* note 26, at 5.
48. *Id.*
49. *See id.*
50. *Id.*
51. Shepard, *supra* note 14, at 187.
52. *Id.*
53. *Id.* at 187–88.
54. *See* 15 U.S.C. § 1640 (2006).

correction of billing errors and reporting errors, crediting of payments, costs, and reasonable attorney's fees.[55] However, TILA provides an even more potent remedy to consumers for violations of certain disclosure provisions—rescission.[56]

At its most basic level, rescission is a legal remedy, sought unilaterally or mutually, that returns the parties of a contract to their pre-contractual positions by discharging both parties of their obligations.[57] At common law, a borrower seeking to rescind a loan on the basis of the lender's fraudulent misrepresentation had to prove the following elements: "(1) a representation, (2) its falsity, (3) its materiality, (4) the [lender's] knowledge of the representation's falsity or ignorance of its truth (scienter), and (5) the borrower's justifiable reliance on the representation."[58] In addition, the borrower was also required to bring the rescission action within a "reasonable time"[59] after the transaction and take the first steps in restoring the lender to the status quo ante.[60] However, during the 1960s, many states began to adopt laws that granted consumers a right to cancel certain kinds of consumer contracts that were thought to be especially prone to fraud and predatory practices within established "cooling-off periods."[61] Eventually, Congress borrowed from these state cooling-off periods, which permit a consumer to unilaterally withdraw from a contractual relationship within a statutorily defined timeframe, and incorporated this rescission mechanism into TILA.[62]

However, the statutory right of rescission is not unlimited. Under § 1635(a), the right of rescission extends only to transactions involving non-purchase-money mortgages on consumer dwellings.[63] In other words, if, as part of a credit transaction other than for the purchase of a home, the creditor acquires or retains a security interest

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55. *See id.*; RENUART & KEEST, *supra* note 26, at 379; Shepard, *supra* note 14, at 186.

56. *See* 15 U.S.C. § 1635(a) (2006).

57. *See* BLACK'S LAW DICTIONARY 1420 (9th ed. 2009).

58. Shepard, *supra* note 14, at 188 (citing W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 105, at 728 (5th ed. 1984)).

59. *See* Warner v. Denis, 933 P.2d 1372, 1385 (Haw. Ct. App. 1997) (holding that "[t]he right of rescission must be exercised within a reasonable time after the default of the other party").

60. *See* Shepard, *supra* note 14, at 188–89 ("[T]he borrower had to return the loan proceeds to the lender before the court would require the lender to terminate its security interest in the borrower's home and return accrued interest and fees.").

61. ROHNER & MILLER, *supra* note 25, at 10.

62. *See id.*

63. *See* 15 U.S.C. § 1635(a) (2006).

in the consumer's principal dwelling, the consumer may rescind the transaction during the statutory cooling-off period.[64] TILA provides consumers with a three-day period "to reflect on the wisdom and desirability of the contract and on the risk of possible loss of the home."[65] Within the three-day period, the consumer is free to rescind any consummated agreement for any reason.[66] However, if the creditor fails to disclose, or improperly discloses important TILA requirements, and the homeowner does not sell the home, the right of rescission may extend to three years.[67] The specific temporal life of the right of rescission is governed by § 1635(f), which states that "an obligor's right of rescission shall expire three years after the date of consummation of the transaction or upon the sale of the property, whichever occurs first."[68] Problems arise when courts, interpreting and applying the language of § 1635(f) and the Board's Regulation Z,[69] apply different meanings to the phrase "exercise of right,"[70] resulting in a right to rescind that may be "exercised" beyond the statutory three-year period in some circuits[71] but not in others.[72] Thus, it is no surprise that the consumer's right to rescind was the most heavily litigated TILA issue of 2012.[73]

C. "The Fed" Weighs In: The Federal Reserve Board's Regulation Z

Early on, Congress recognized that the oversight of consumer credit is complex, arduous, and generally beyond the legislature's

64. Shepard, *supra* note 14, at 186.

65. *Id.* (quoting RALPH J. ROHNER & FRED H. MILLER, TRUTH IN LENDING ¶ 8.01[1], at 598 (Robert A. Cook et al. eds., 2000)).

66. ROHNER & MILLER, *supra* note 25, at 10.

67. *See* 15 U.S.C. § 1645; Shepard, *supra* note 14, at 187 ("The consumer's three-day rescission right extends to three years if the creditor fails to provide the consumer with a notice describing the rescission right or with material information about the loan, including the APR, finance charge, amount financed, total number of payments, and payment schedule.").

68. 15 U.S.C. § 1635(f).

69. *See* 12 C.F.R. § 226.23 (2008), *invalidated by In re* Smith-Pena, 484 B.R. 512 (Bankr. D. Mass. 2013).

70. *See id.* § 226.23(a)(2) ("To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram, or other means of written communication.").

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

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

73. Arthur Axelson & Richard Vance, *Truth in Lending Update—2011*, 67 BUS. LAW. 541, 549 (2012).

administrative capacity.[74] Therefore, Congress delegated broad authority to the Board to implement, clarify, and expand upon[75] TILA's provisions.[76] The Board responded by implementing a comprehensive set of TILA rules and regulations, collectively known as Regulation Z, which have been in effect since July 1, 1969.[77] The Board amended Regulation Z numerous times between 1969 and 1981 to reflect the Board's own determination to clarify, modify, or expand the rules.[78] In 1981, Regulation Z was completely rewritten to embody changes mandated by the Simplification Act and to streamline the remaining provisions where no substantive changes were necessary.[79] For the purposes of this article, "Regulation Z" will stand for the 1981 revised version of the Board's regulations.

Regulation Z is indispensable in dealing with TILA provisions because the Board is able, under Congress's express authorization, to modify, expand and refine the provisions mandated in TILA.[80] For example, Regulation Z may provide options or may require disclosures not specifically mentioned in the statutory framework of TILA.[81] As such, Regulation Z is considered to be *the truth in lending law* in most[82] operational aspects.[83]

The Board's answer to the uncertainties surrounding the three-year rescission period under § 1635(f) can be found in 12 C.F.R. § 226.23(a)(2), which states: "[t]o exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram, or other means of written communication."[84] Nevertheless, continued

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74. *See* Ford Motor Credit Co. v. Milhollin, 444 U.S. 555, 559 (1980) ("Because of their complexity and variety, however, credit transactions defy exhaustive regulation by a single statute."); RENUART & KEEST, *supra* note 26, at 13.

75. *See* ROHNER & MILLER, *supra* note 25, at 30 ("This is not presumptuous action by the Board, but rather is consistent with Congress' expressed authorization that the Board should have the power to adjust the ground rules as it believes necessary or proper to achieve the purposes of the Act or to prevent circumvention or evasion of the Act's provisions.").

76. RENUART & KEEST, *supra* note 26, at 13; ROHNER & MILLER, *supra* note 25, at 29.

77. RENUART & KEEST, *supra* note 26, at 13.

78. ROHNER & MILLER, *supra* note 25, at 29.

79. *Id.*

80. *Id.* at 30.

81. *Id.*

82. *See id.* ("Nonetheless because on occasion the Board has been found to have exceeded its authority, it is important to determine if that may be the case with respect to a given issue."); *see, e.g.*, *In re* Stanley, 315 B.R. 602, 615 (Bankr. D. Kan. 2004) (holding that 12 C.F.R. § 226.23(d)(4) (2008) is not a permissible interpretation of 15 U.S.C. § 1635(b) (2010)).

83. ROHNER & MILLER, *supra* note 25, at 30.

84. 12 C.F.R. § 226.23(a)(2) (2008).

litigation has resulted in a split of authority regarding the interpretation of § 1635(f) and Regulation Z—that is, "whether the borrower must file a lawsuit within three years after the consummation of a loan transaction to exercise her right to rescind, or whether the borrower need only assert the right to rescind through a written notice within the three-year period."[85]

In the following sections, this Note will discuss recent Supreme Court holdings and two conflicting circuit court opinions regarding the interpretation and application of § 1635(f) and Regulation Z.

D. *The Supreme Court Addresses Rescission:* Beach v. Ocwen Federal Bank

David and Linda Beach refinanced their Florida home in 1986 with a loan from Great Western Bank.[86] After the Beaches stopped making payments in 1991, Great Western initiated a foreclosure proceeding.[87] The Beaches acknowledged their default but raised an affirmative defense, alleging that Great Western failed to make disclosures required by TILA and thus, the Beaches argued, they had a defensive right under § 1635(f) to rescind the mortgage agreement.[88]

Justice Souter, writing for a unanimous U.S. Supreme Court, held that the Beaches' recoupment defense was barred because TILA "permits no federal right to rescind, defensively or otherwise, after the 3-year period of § 1635(f) has run."[89] The Court expressly concluded that the three-year period of § 1635(f) did not operate as a statute of limitations governing the institution of a suit, but rather as a statute of repose governing the underlying right of rescission.[90] In analyzing the congressional intent behind TILA, the Court concluded that the inclusion of recoupment language in § 1640(e)[91] and its

85. Gilbert v. Residential Funding LLC, 678 F.3d 271, 276 (4th Cir. 2012).
86. Beach v. Ocwen Fed. Bank, 523 U.S. 410, 413 (1998).
87. *Id.*
88. *Id.* at 413–14.
89. *Id.* at 419.
90. *Id.* at 410.
91. Subsection (e) reads that the 1-year limit on actions for damages "does not bar a person from asserting a violation of this subchapter in an action to collect the debt which was brought more than one year from the date of the occurrence of the violation as a matter of defense by recoupment or set-off in such action, except as otherwise provided by State law."

simultaneous absence in § 1635(f) proved that Congress ultimately did not intend to provide the same kind of flexibility in rescission claims as it did in claims for damages.[92] However, the Court acknowledged that a borrower might have hope of recoupment outside of the three-year statutory period under state law.[93]

The Court's holding in *Beach* clearly established that TILA does not permit any federal right to rescind *defensively* after the three-year period of § 1635(f) has run.[94] However, *Beach* left some important issues unresolved.[95] The first issue is how § 1635(f) should be interpreted with respect to affirmative, as opposed to defensive, actions of rescission. Second, and related to the first, is the issue of how a borrower actually exercises his or her right to rescind under § 1635(f) and Regulation Z. The following circuit court decisions address these issues.

E. The Tenth Circuit Concurs: Rosenfield v. HSBC Bank

In *Rosenfield v. HSBC Bank, USA*, Jean Rosenfield refinanced an existing loan on her home on November 3, 2006.[96] That "loan was subsequently sold or assigned to HSBC Bank."[97] Believing that the original lender had violated several federal statutes, including TILA, Rosenfield sent a notice of rescission letter to the lender on September 9, 2008.[98] Convinced that she had legally rescinded the transaction, Rosenfield ceased paying her mortgage.[99] As a result, HSBC instituted a foreclosure proceeding against her on July 9, 2009.[100] On December 21, 2009, more than three years after the loan transaction, Rosenfield sued HSBC, asserting claims for relief based on her alleged right to rescind the loan under § 1635(f).[101]

Id. at 417–18 (citing 15 U.S.C. § 1640(e) (2010)).

92. *Id.* at 418.

93. *See id.*

94. *See id.* at 419.

95. *See* Elwin Griffith, *Searching For the Truth in Lending: Identifying Some Problems in the Truth in Lending Act and Regulation Z*, 52 BAYLOR L. REV. 265, 350 (2000).

96. 681 F.3d 1172, 1175 (10th Cir. 2012).

97. *Id.* at 1176.

98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

The court held that written notice of rescission was "not enough for a consumer to invoke her right to rescission under TILA."[102] The court reasoned that, "consistent with *Beach*, TILA establishes a *right of action* that is *generally* redressable only when a party seeks recognition of it by invoking the power of the courts."[103] Thus, the court held, it is the filing of an action in court, not mere notice, that is required to invoke the right of rescission under § 1635(f).[104] The court further opined that notice of rescission is a necessary, but not sufficient, condition for the exercise of the TILA right of rescission.[105]

Thus, *Rosenfield* closely mirrored the analysis and holding in *Beach*, emphasizing that consumers must file an action of rescission to properly exercise their right to rescind under § 1635(f) and Regulation Z.[106]

F. The Fourth Circuit Paves a New Path: Gilbert v. Residential Funding, LLC

In *Gilbert v. Residential Funding, LLC*, Rex and Daniela Gilbert executed a note to refinance an existing lien on their home on May 5, 2006.[107] Residential Funding, LLC, eventually acquired the interest.[108] The Gilberts defaulted on the loan in 2008 and, facing foreclosure, wrote a letter dated April 5, 2009 to the mortgage lender providing notice that the Gilberts were rescinding the transaction based on alleged TILA violations.[109] After the foreclosure proceeding had been resolved against the Gilberts, and while their appeal was pending, the Gilberts filed suit on September 14, 2009, against Residential Funding, LLC, seeking to rescind the May 5, 2006 loan.[110]

The court acknowledged that there was a "split of authority as to whether the borrower must file a lawsuit within three years after the consummation of a loan transaction to exercise her right to rescind,

102. *Id.* at 1182.
103. *Id.* at 1183 (footnote omitted).
104. *Rosenfield*, 681 F.3d at 1183.
105. *Id.* at 1185.
106. *Id.* at 1183.
107. 678 F.3d 271, 274 (4th Cir. 2012).
108. *Id.*
109. *Id.*
110. *Id.* at 274–75.

or whether the borrower need only to assert the right to rescind through a written notice within the three-year period."[111] Relying on a plain language analysis of § 1635(f) and Regulation Z,[112] the court held that "a borrower exercises her right to rescission by merely communicating in writing to her creditor her intention to rescind."[113] The court continued that courts "must not conflate the issue of whether a borrower has exercised her right to rescind with the issue of whether the rescission has, in fact, been completed and the contract voided."[114]

Further, the court stated that the Supreme Court in *Beach* failed to address the "proper method of exercising a right to rescind or the timely exercise of that right."[115] Rather, the Supreme Court, according to *Gilbert*, held that § 1635(f) extinguished the foundational right for the claim, not that a borrower is required to "file a claim for the invocation of that right."[116]

The Fourth Circuit's singular holding in *Gilbert* is significant because it challenges the previously uniform interpretations of *Beach*, § 1635(f), and Regulation Z found in *Rosenfield* and similarly decided circuit court opinions.[117] Thus, until or unless the Supreme Court strikes down *Gilbert*, Congress amends § 1635(f), or the Board amends Regulation Z, the current conflicting interpretations of TILA's rescission provision will remain valid law in their respective

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111. *Id.* at 276.

112. *Id.* at 277.

> Taking the plain meaning of these texts, and assuming that the words say what they mean and mean what they say, we come to the conclusion that the Gilberts exercised their right to rescind with the April 5, 2009, letter. Simply stated, neither 15 U.S.C. § 1635(f) nor Regulation Z says anything about the filing of a lawsuit, and we refuse to graft such a requirement upon them.

Id.

113. *Id.*

114. *Id.*

115. *Id.* at 278.

116. *Id.*

117. *See also* McOmie-Gray v. Bank of Am. Home Loans, 667 F.3d 1325, 1328 (9th Cir. 2012) ("[U]nder the case law of this court and the Supreme Court, rescission suits must be brought within three years from the consummation of the loan, regardless whether notice of rescission is delivered within that three-year period."); Miguel v. Country Funding Corp., 309 F.3d 1161, 1164–65 (9th Cir. 2002) (citations omitted) ("[S]ection 1635(f) represents an 'absolute limitation on rescission actions' which bars any claims filed more than three years after the consummation of the transaction. Therefore, § 1635(f) is a statute of repose, depriving the courts of subject matter jurisdiction when a § 1635 claim is brought outside the three-year limitation period.").

jurisdictions. As a result, the current state of the law will remain burdened with inconsistency and uncertainty.

III. THE STATUS QUO FAVORS NO ONE: A CRITIQUE OF THE CURRENT LAW

The current state of the law, discussed above, disfavors consumers by potentially weakening their statutory right to rescind[118] and increasing economic uncertainty in a frail market.[119] The following sections address the problems arising from the current split of authority, including the judicial weakening of the Board's regulation, the dilution of consumers' statutory leverage, and the economic risks of preserving the status quo.

A. The Circuits Disagree: How Regulation Z Fails to Clarify Section 1635(f)

As discussed above, § 1635(f) provides that consumers may rescind certain loan transactions up to three years after consummation of the loan.[120] Even before venturing into the issues and uncertainties surrounding the interpretation of the provision, one can imagine complications arising from such a lengthy rescission period. For example, a three-year rescission period complicates any attempt to return parties to their pre-transaction states when the property has significantly depreciated in value.[121] In addition, consumers are able to rescind upon discovering a defect in the disclosure, even if the discovery comes after related or unrelated complications with the loan arise.[122] However, Congress accounted for these potential consequences and included § 1635(f) in TILA because encumbering the family home via a credit transaction is a major decision that deserves serious reflection absent creditor pressure.[123] Thus, it appears that Congress's intent to encourage the "informed use of credit"[124] by consumers trumped the foreseeable complications attributable to the statutory three-year rescission

118. *See infra* Part V.B.
119. *See infra* Part V.C.
120. *See* 15 U.S.C. § 1635(f) (2006); 12 C.F.R. § 226.23(2)–(3) (2008).
121. *See* Shepard, *supra* note 14, at 189–90 ("[T]he borrower therefore is unable to finance her tender obligation by selling her home or refinancing the mortgage.").
122. *Id.* at 190.
123. RENUART & KEEST, *supra* note 26, at 401.
124. *See* 15 U.S.C. § 1601(a).

period in § 1635(f). But, what if that three-year period was not actually three years? More broadly, are there currently any procedures or guidelines in place to address the inevitable interpretive questions arising from the statutory language and construction of § 1635(f)?

The latter question can be answered in the affirmative. Congress delegated expansive authority to the Board "to elaborate and expand the legal framework governing commerce in credit."[125] In fact, congressional intent reveals a "decided preference for resolving interpretive issues by uniform administrative decision, rather than piecemeal through litigation."[126] While it is clear that courts often further legislative goals by filling gaps in the wake of congressional silence,[127] the Supreme Court has expressly concluded that "judges ought to refrain from substituting their own interstitial lawmaking for that of the Federal Reserve, so long as the latter's lawmaking is not irrational."[128]

In fact, administrative agencies are generally better suited to engage in the interpretation of legislative statutes.[129] Interpretation often involves a highly intricate "empirical process that entails investigation into consumer psychology and . . . presupposes broad experience with credit practices."[130] Courts that attempt to interpret legislative purpose, without deference to an administrative agency like the Board, are said to be "embarking upon a voyage without a compass."[131] Hence, great deference should be afforded to the Board and "absent some obvious repugnance to the statute, the . . . regulation implementing [TILA] should be accepted by the courts."[132]

However, the circuit courts that have encountered § 1635(f) interpretive issues have disagreed about the deference given to the language in Regulation Z.[133] This lack of judicial consensus,

125. Ford Motor Credit Co. v. Milhollin, 444 U.S. 555, 559–60 (1980).

126. *Id.* at 568.

127. *Id.* at 565.

128. *Id.* at 568; *see* Gilbert v. Residential Funding, LLC, 678 F.3d 271, 277 (4th Cir. 2012) (citing Anderson Bros. Ford v. Valencia, 452 U.S. 205, 219 (1981)).

129. *Milhollin*, 444 U.S. at 569.

130. *Id.* at 568–69.

131. *Id.* at 568.

132. *Anderson Bros. Ford*, 452 U.S. at 219.

133. *Compare Gilbert*, 678 F.3d at 277 (assuming that the words in Regulation Z say what they mean and mean what they say; that a borrower exercises her right of rescission by sending

combined with the absence of a Federal Reserve Board Staff opinion applying Regulation Z's notice requirement to § 1635(f), creates uncertainty with respect to the deference afforded to, and the interpretation of, Regulation Z for consumers, lenders, and judges. In turn, the resulting lack of clarity could lead to a more hesitant mortgage and lending market, harming the economic interests of both lenders and borrowers.[134]

B. Rescission Diluted: How the Split in Authority Harms Consumer Leverage

Borrowers are generally unsophisticated actors who possess comparatively less leverage in loan negotiations than their more sophisticated lending counterparts.[135] The resulting disparity in bargaining power often leads to borrower vulnerability.[136] Thus, TILA's rescission provisions "shift[] significant leverage from lenders to borrowers in setting forth a strict liability remedy that substantially liberalizes the steps needed to unwind a mortgage transaction under the common law."[137] At least one commentator has argued that the statutory right of rescission in § 1635(f) is the singular source of borrower leverage in a tumultuous legal and economic environment.[138]

Since rescission is such an important "weapon in the arsenal of consumer advocates,"[139] the current uncertainty regarding its

notice), *with* Rosenfield v. HSBC Bank, 681 F.3d 1172, 1185 (10th Cir. 2012) (interpreting the language of Regulation Z to mean that notice is a necessary predicate to the act of exercising the right, but not sufficient in itself), *and* McOmie-Gray v. Bank of Am. Home Loans, 667 F.3d 1325, 1327 (9th Cir. 2012) (holding that the language of Regulation Z indicates that notice merely advances a claim seeking rescission, but does not exercise a borrower's right of rescission).

134. Congress intended to establish a fixed and limited repose period in § 1635(f) to ensure commercial certainty. *Rosenfield*, 681 F.3d at 1187. Without a firm and established time period for solidifying the legal relationship between lenders and borrowers, the "economic best interests of the public as a whole" could be upset. *Id.* at 1186.

135. RENUART & KEEST, *supra* note 26, at 12; *see In re* Hunter, 400 B.R. 651, 656–57 (Bankr. N.D. Ill. 2009) (citing Velazquez v. Home Am. Credit, Inc., 254 F. Supp. 2d 1043, 1045 (N.D. Ill. 2003)); Shepard, *supra* note 15, at 192.

136. Shepard, *supra* note 14, at 192.

137. *Id.*

138. *Id.* at 172.

139. Major Lescault, *The Truth in Lending Act Means What It Says—You Only Have Three Years to Rescind*, Aug. 1998 ARMY LAW. 28, 30.

application could prove harmful to borrowers' leverage.[140] Therefore, even though the process of rescission is undoubtedly vague in other respects,[141] certainty as to the availability of a borrower's right to rescind is necessary to preserve the borrower's limited leverage.

C. "Cloudy Titles": The Negative Economic Ramifications of the Status Quo

On the other hand, banks and other lenders must be "protected from the possibility that a foreclosed home could have a 'cloudy title' because of a delayed rescission claim by a borrower."[142] A title is "clouded" when a consumer can rescind a loan transaction after the property is disposed of in a foreclosure sale or the interest is subsequently assigned to a third party.[143] However, such post-foreclosure rescission is generally infeasible because foreclosed real estate is often purchased by innocent third parties, making it virtually impossible for the creditor to return the consumer to his or her pre-contractual position[144] unless the innocent purchaser is divested of his or her right in the real estate.[145] The possibility that an innocent, bona fide third party purchaser could be divested of his or her right to property purchased at a foreclosure sale will certainly reduce the marketability of such property.[146]

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140. *See infra* Part V.C; *see also* Griffith, *supra* note 95, at 350 (noting that if TILA permits no federal right of rescission after the expiration of the thee-year period, borrowers must look to state law for remedies in this context).

141. Neither TILA nor Regulation Z "set forth any technical requirements that govern the language a consumer must use when requesting a rescission." Sam v. Am. Home Mortg. Servicing, No. CIV. S-09-2177, 2010 WL 761228, at *3 (E.D. Cal. Mar. 3, 2010).

142. Rosenfield v. HSBC Bank, 681 F.3d 1172, 1177 (10th Cir. 2012).

143. *See* 15 U.S.C. § 1635(i)(1) (2006) ("[A]fter the initiation of any judicial or nonjudicial foreclosure process on the primary dwelling of an obligor securing an extension of credit, the obligor shall have a right to rescind the transaction equivalent to other rescission rights by this section."); 15 U.S.C. § 1641(c) (2006) ("Any consumer who has the right to rescind a transaction under section 1635 of this title may rescind the transaction as against any assignee of the obligation."); Jones v. Saxon Mortg., Inc., 537 F.3d 320, 327 (4th Cir. 1998).

144. *See* 15 U.S.C. § 1635(b) ("[T]he creditor shall return to the boligor [sic] any money or property given as earnest money, downpayment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction.").

145. *Jones*, 537 F.3d at 327.

146. *See id.*; *see also* 15 U.S.C. § 1641(c) ("Any consumer who has the right to rescind a transaction under section 1635 of this title may rescind the transaction as against any assignee of the obligation.").

Therefore, certainty as to a consumer's right of rescission is necessary to protect the marketability of real estate purchased via foreclosure, and as a corollary, the economic interests of banks and other lenders.

IV. PROPOSAL

In an effort to adhere to the congressional intent behind TILA and promote economic certainty, the Supreme Court should strike down the Fourth Circuit's holding in *Gilbert* and expressly declare that consumers must initiate an action for rescission within the three-year statutory period to effectively exercise their right to rescind under § 1635(f) and Regulation Z.[147] The following analysis supports this proposal by examining the plain language of various provisions in TILA and Regulation Z, applying the applicable precedent in *Beach*, explaining the significance of § 1635(f) as a statute of repose, and weighing various policy considerations.

A. Start at the Source: A Plain Language Analysis of TILA and Regulation Z

Under § 1635(f), "[a]n obligor's right of rescission shall expire three years after the date of consummation of the transaction or upon the sale of the property, whichever occurs first."[148] In an effort to clarify § 1635(f), Regulation Z states that "[t]o exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication."[149]

Significantly, neither § 1635(f) nor Regulation Z mentions a suit's commencement.[150] Hence, according to some courts, TILA does not require a consumer to file an action seeking rescission to

147. Alternatively, Congress could amend § 1635(f) to expressly require the filing of a rescission suit within three years of consummation of the loan or the Federal Reserve Board could amend Regulation Z to clarify that notice is necessary, but not sufficient to exercise the right to rescind under § 1635(f). However, because the effect of amended legislation and regulation on case law interpreting such legislation or regulation is ambiguous, this Note does not address these alternatives but acknowledges that they may also achieve the goals in the analysis of the proposal. For an in-depth discussion on precedent, see generally Mary Massaron Ross, *An Advocate's Toolbox: Techniques to Help Appellate Lawyers Evaluate Precedent and Craft Analytically Precise Arguments*, 81 MICH. BUS. L.J. 24 (2002).

148. 15 U.S.C. § 1635(f).

149. 12 C.F.R. § 226.23(a)(2) (2008).

150. *See* Beach v. Ocwen Fed. Bank, 523 U.S. 410, 417 (1998); Gilbert v. Residential Funding, LLC, 678 F.3d 271, 278 (4th Cir. 2012); *In re* Hunter, 400 B.R. 651, 659 (Bankr. N.D. Ill. 2009).

exercise the right to rescind but requires only that notice be given to the creditor.[151] In other words, there is a difference between the underlying right of rescission, exercised by notice pursuant to Regulation Z,[152] and the effectuation of that rescission, accomplished through legal action.[153] Thus, under this plain language analysis of § 1635(f), when a consumer timely notifies her creditor of her intention to rescind the loan, § 1635 will not limit her ability to subsequently file suit to enforce that right.[154]

However, the analysis above, adopted by the Fourth Circuit in *Gilbert*,[155] misconstrues the underlying right of rescission. Instead, § 1635(f) represents an "absolute limitation,"[156] which "permits no federal right to rescind, defensively *or otherwise*, after the 3-year period of § 1635(f) has run."[157] According to the Supreme Court in *Beach*, § 1635(f)'s "uncompromising statement that the borrower's right 'shall expire' with the running of time manifests a congressional intent to extinguish completely the right of rescission at the end of the 3-year period."[158] Importantly, the court noted, § 1635(f) establishes a right of action that is "*generally* redressable only when a party seeks recognition of it by invoking the power of the courts."[159] Thus, mere notice will only signify the consumer's intent to rescind rather than actually invoke his or her underlying

151. *See Gilbert*, 678 F.3d at 278; Leonard v. Bank of Am., No. 10-C-0814, 2012 WL 3001266, at *6 (E.D. Wis. July 23, 2012); *In re Hunter*, 400 B.R. at 659.

152. "To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication." 12 C.F.R. § 226.23(a)(2) (2013).

153. *See Gilbert*, 678 F.3d at 277.

154. *In re Hunter*, 400 B.R. at 662; *see also* RENUART & KEEST, *supra* note 26, at 403 ("The three-year period limits only the consumer's right to rescind, not the consumer's right to seek judicial enforcement of the rescission.").

155. *See Gilbert*, 678 F.3d at 277–78.

156. McOmie-Gray v. Bank of Am. Home Loans, 667 F.3d 1325, 1329 (9th Cir. 2012); Miguel v. Country Funding Corp., 309 F.3d 1161, 1164 (9th Cir. 2002); King v. California, 784 F.2d 910, 913 (9th Cir. 1986).

157. Beach v. Ocwen Fed. Bank, 523 U.S. 410, 419 (1998) (emphasis added).

158. *Id.* at 410 (quoting 15 U.S.C. § 1635(f) (2006)).

159. Rosenfield v. HSBC Bank, 681 F.3d 1172, 1183 (10th Cir. 2012); *see also McOmie-Gray*, 667 F.3d at 1327 ("Rescission is not automatic upon a borrower's mere notice of rescission . . . . Instead, where a lender fails to comply with § 1635(b), the statute and regulations contemplate that a borrower, who by sending notice of rescission has 'advanced a claim seeking rescission,' will seek a determination that rescission is proper." (quoting Large v. Conseco Fin. Servicing Corp., 292 F.3d 49, 55 (1st Cir. 2002))).

right of rescission. It follows then that a consumer must file an action in court to invoke her right of rescission under TILA.[160]

When a statute fundamentally limits a litigant's ability to file an action, it is said to be a "statute of repose."[161] "Unlike a statute of limitation, which regulates [the availability of] remedies, a statute of repose regulates [the underlying] rights and 'operates as a statutory bar independent of the actions (or inaction) of the litigants.'"[162] In other words, under a statute of repose, similar to § 1635(f), the right to relief (in this case to rescind the loan transaction) is completely extinguished when the relevant time period expires.[163]

Furthermore, in reading the plain language of Regulation Z[164] in combination with § 1635(f)'s repose language,[165] it is apparent that these regulations suggest that notice is only a "*necessary* predicate act to the ultimate exercise of the right,"[166] rather than a *sufficient* act constituting the exercise of the right.

Therefore, in reading both § 1635(f) and Regulation Z under a plain language standard, consumers must actually bring an action for rescission within the three-year statutory period under § 1635(f) to exercise their right of rescission.[167] Regulation Z clearly makes notice a necessary component of exercising the right of rescission, however, notice is not a sufficient condition to exercise such a right.[168] If the consumer fails to bring an action within the three-year period, his or her right of rescission will be extinguished.[169]

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160. *Rosenfield*, 681 F.3d at 1183; *McOmie-Gray*, 667 F.3d at 1329; *see* Barry v. Countrywide Home Loans, F.S.B., No. 10-cv-1525, 2011 WL 441508, at *3 (D. Colo. Feb. 8, 2011).

161. *Rosenfield*, 681 F.3d at 1182–83.

162. Sobieniak v. BAC Home Loans Servicing, LP, 835 F. Supp. 2d 705, 710 (D. Minn. 2011) (quoting Nesladek v. Ford Motor Co., 46 F.3d 734, 737 (8th Cir. 1995)).

163. *See* Margiolies v. Deason, 464 F.3d 547, 551 (5th Cir. 2006).

164. "To exercise the right to rescind, the consumer shall notify the creditor of the rescission by mail, telegram or other means of written communication." 12 C.F.R. § 226.23(a)(2) (2013).

165. "An obligor's right of rescission *shall expire* three years after the date of consummation of the transaction or upon the sale of the property, whichever occurs first." 15 U.S.C. § 1635(f) (2006) (emphasis added).

166. *Rosenfield*, 681 F.3d at 1185.

167. *See id.*

168. *See id.*

169. *See id.* at 1181 (citing Beach v. Ocwen Fed. Bank, 523 U.S. 410, 419 (1998)); McOmie-Gray v. Bank of Am. Home Loans, 667 F.3d 1325, 1329 (9th Cir. 2012).

B. *The Real World: Examining Various Policy Considerations*

When interpreting the meaning of a statute, courts should explore the underlying concerns embodied in the statute, the intent of the legislature in drafting the statute, and the potential social and economic policy arguments in favor of differing interpretations. In the following sections, this Note argues that the proposal not only adheres to Congress's original intent in drafting TILA and, more specifically, § 1635(f), but also supports sound economic policy.

1. Promoting Economic Stability

TILA's basic premise is to promote certainty in the lending marketplace to enable consumers and lenders to make knowledgeable decisions regarding credit transactions.[170] However, the intended certainty quickly erodes to uncertainty when titles become "clouded"[171] through ambiguous interpretations of § 1635(f) and Regulation Z. As discussed above, the Fourth Circuit's decision in *Gilbert* established that a consumer, having provided sufficient notice of rescission to the lender within three years of discovering certain violations of TILA, may file a suit of rescission against the lender after the statutory three-year period found in § 1635(f) has run.[172] The court in *Gilbert* then analogized the filing of an action of rescission to an action for damages under § 1640(e)[173] for a violation of § 1635(b),[174] thus limiting the rescission-tolling period to one year.[175] However, the plain terms of § 1635(b)[176] suggest that a

170. Jonathan Landers & Ralph Rohner, *A Functional Analysis of Truth in Lending*, 26 UCLA L. REV. 711, 713 (1979).

171. *See supra* Part III.C.

172. *See* Gilbert v. Residential Funding LLC, 678 F.3d 271, 278 (4th Cir. 2012); *In re* Hunter, 400 B.R. 651, 661–62 (Bankr. N.D. IL 2009); *see also* Johnson v. Long Beach Mortg. Loan Trust 2001–04, 451 F. Supp. 2d 16, 39–41 (D.D.C. 2006) (holding that an action seeking rescission must be filed within one year of the date in which the lender refuses to effectuate rescission); *In re* Ralls, 230 B.R. 508, 512 (Bankr. E.D. Penn. 1999) (allowing a rescission suit where notice was sent within the three-year period and suit began less than one year after the lender refused to effectuate the rescission).

173. "Any action under this section may be brought in any United States district court, or in any other court of competent jurisdiction, within one year from the date of the occurrence of the violation." 15 U.S.C. § 1640(e) (2006).

174. "Within 20 days after receipt of a notice of rescission, the creditor shall return to the obligor any money or property given as earnest money, downpayment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction." 15 U.S.C. § 1635(b).

175. *Gilbert*, 678 F.3d at 278–79.

176. *See infra* note 179 and accompanying text.

reaction by the creditor—such as returning any money or property, or taking any action necessary to terminate any security interest created under the transaction—is necessary to effectuate the rescission.[177] Without a reaction by the creditor, there can be no mutual recognition of rescission.[178] It must follow then that a creditor's failure to respond to a consumer's notice of rescission would not be considered a failure to act under § 1635(b) because unilateral notification cannot be construed as exercising the right to void a loan contract.[179] Therefore, under the holding in *Gilbert*, a consumer could provide notice to a lender within the statutory three-year period and proceed to sit on his or her rescission rights for an indeterminate amount of time.[180] By allowing consumers to indefinitely toll the rescission period,[181] the time period for solidifying the legal relationship between lenders and consumers expands beyond any statutory boundaries, thus "upset[ting] the economic best interests of the public as a whole."[182]

The indirect enlargement of the congressionally established three-year period could also spawn a multitude of "cloudy titles."[183] According to § 1641(c), "[a]ny consumer who has the right to rescind a transaction under section 1635 of this title may rescind the transaction as against any assignee of the obligation."[184] Furthermore, § 1635(i) states, "after the initiation of any judicial or nonjudicial foreclosure process on the primary dwelling of an obligor securing an extension of credit, the obligor shall have a right to rescind the transaction equivalent to other rescission rights provided by this section."[185] Thus, allowing a consumer to indefinitely extend the three-year period of rescission, or to extend it for any amount of time past the established three-year period, would put innocent bona fide purchasers and transferees of certain titles at risk of facing

177. Rosenfield v. HSBC Bank, 681 F.3d 1172, 1187 n.11 (10th Cir. 2012).
178. *Id.*
179. *See id.* (quoting Am. Mortgage Network, Inc. v. Shelton, 486 F.3d 815, 821 (4th Cir. 2007)).
180. *Id.*
181. Sobieniak v. BAC Home Loans Servicing, LP, 835 F. Supp. 2d 705, 711 (D. Minn. 2011).
182. *See Rosenfield*, 681 F.3d at 1186 (alteration in original) (quoting Jones v. Saxon Mortg., Inc., 537 F.3d 320, 327 (4th Cir. 1998)).
183. *See id.* at 1187.
184. 15 U.S.C. § 1641(c) (2006).
185. 15 U.S.C. § 1635(i) (2006).

a delayed rescission claim by the original consumer via §§ 1641(c) and 1635(f).[186] This possibility would therefore create uncertainty in the chain of title of real estate purchased from foreclosure sales,[187] essentially defeating the intent to promote commercial-certainty that led Congress to establish the three-year repose period in the first place.[188] Therefore, to further the congressional goal of commercial-certainty, reduce the risk of "clouded titles," and promote the best economic interests of the public, § 1635(f) and Regulation Z must establish a strict three-year period during which consumers can bring a suit of rescission.

2. Preserving Consumer Leverage

As discussed above, the average consumer generally possesses comparatively less leverage in a loan transaction than his or her more sophisticated lending counterparts.[189] Some commentators, examining this reality, have argued that the right of rescission is the singular source of consumer leverage in a damaged housing market[190] and essentially levels the playing field by reducing the disparity in bargaining power that exists between consumers and lenders.[191] In addition, as one court noted, lenders can enjoy ultimate protection against rescission claims under TILA by simply complying with the statutory disclosure provisions.[192] Therefore, under the *Gilbert* reasoning, holding that notice is insufficient to exercise the consumer's right of rescission would unfairly reward

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186. *See Rosenfield*, 681 F.3d at 1187 n.11.

187. *See Jones*, 537 F.3d at 327 ("[A]llowing tolling under § 1635(f) and permitting a party to rescind after a foreclosure sale would create uncertainty in any chain of title of real estate purchased from a foreclosure sale.").

188. *Rosenfield*, 681 F.3d at 1187.

189. *See* RENUART & KEEST, *supra* note 26, at 12; *see also In re Hunter*, 400 B.R. 651, 656–57 (Bankr. N.D. Ill. 2009) ("'The point of giving the consumer an absolute right to rescission is to place the consumer in a much stronger bargaining position than he enjoys under the traditional rules of rescission . . . .'" (quoting Velazquez v. Home Am. Credit, Inc., 254 F. Supp. 2d. 1043, 1045 (N.D. Ill. 2003))); Shepard, *supra* note 14, at 192 ("TILA is designed to protect borrowers who, relative to lenders, are unsophisticated actors who possess less leverage in loan negotiations.").

190. Shepard, *supra* note 14, at 172.

191. Lescault, *supra* note 139, at 30 (stating that with the proliferations of the home-equity market, TILA rescission rights have become an important weapon in the arsenal of consumer advocates).

192. Lippner v. Deutsche Nat'l Trust Co., 544 F. Supp. 2d 695, 702 (N.D. Ill. 2008).

creditors for failing to respond to a consumer's notice of rescission under § 1635(b).[193]

However, contrary to the belief that consumers suffer from a grand disparity in bargaining power, borrowers in fact enjoy a wealth of leverage with respect to rescission. This calls into question the need for courts to extend the congressionally established three-year rescission period through judicial interpretation. First, courts will generally view facts in the light most favorable to consumers in TILA rescission claims and presume that the lenders did not make the required disclosures.[194] As a result, in a rescission action, courts require only that the consumer produce enough evidence necessary to rebut the presumption of disclosure under TILA and thus withstand a motion for summary judgment.[195] Ultimately, this non-arduous responsibility allows consumers to extend their rescission rights from three days to three years with relative ease under § 1635(f) and Regulation Z.[196]

In addition, Congress and the Board, whether intentionally or unintentionally, omitted any technical requirements governing the language a consumer must use when notifying the creditor that the consumer intends to rescind the contract.[197] As a result, the vague statutory definition of required notice essentially prevents creditors

193. *In re Hunter*, 400 B.R. at 662; *see also* Gilbert v. Residential Funding LLC, 678 F.3d 271, 277 (4th Cir. 2012) ("[A] borrower exercises her right of rescission by merely communicating in writing to her creditor her intention to rescind. To complete the rescission and void the contract, however, more is required. Either the creditor must 'acknowledge[ ] that the right of rescission is available' . . . or the borrower must file a lawsuit." (quoting Am. Mortg. Network, Inc. v. Shelton, 486 F.3d 815, 821 (4th Cir. 2007))).

194. Barry v. Countrywide Home Loans, F.S.B., No. 10-cv-1525, 2011 WL 441508, at *2 (D. Colo. Feb. 8, 2011); *see also* Adamson v. Multi Cmty. Diversified Servs., 514 F.3d 1136, 1145 (10th Cir. 2008) ("In considering a motion for summary judgment, this court draws all reasonable inferences in favor of the nonmoving party.").

195. *See* Cappuccio v. Prime Capital Funding LLC, 649 F.3d 180, 189 (3d Cir. 2011) ("[T]he quantum of evidence needed to 'burst' the presumption's 'bubble' under Rule 301 is also minimal, given that 'the presumption's only effect is to require the party [contesting it] to produce enough evidence substantiating [the presumed fact's absence] to withstand a motion for summary judgment or judgment as a matter of law on the issue.'" (quoting McCann v. Newman Irrevocable Trust, 458 F.3d 281, 288 (3d Cir. 2006))).

196. *See* 12 C.F.R. § 226.23(a)(3) (2013) ("The consumer may exercise the right to rescind until midnight of the third business day following consummation . . . . If the required notice or material disclosures are not delivered, the right to rescind shall expire 3 years after consummation . . . .").

197. Sam v. Am. Home Mortg. Servicing, No. CIV. S-09-2177, 2010 WL 761228 at *3 (E.D. Cal. Mar. 3, 2010).

from attacking the substance of a rescission notice, providing added protection for unsophisticated consumers.[198]

In sum, the Supreme Court should invalidate the holding in *Beach* because it violates sound economic policy and gratuitously broadens consumer leverage at the expense of lender protection. In the following section, this Note proves that this proposal upholds the original congressional intent behind TILA, promotes increased economic strength and stability, and preserves consumer leverage in credit transactions.

V. JUSTIFICATION OF PROPOSAL

As discussed in Part III of this Note, the current split of authority is problematic to both consumer interests and economic stability. In response, this Note proposed above that the Supreme Court should strike down the Fourth Circuit's holding in *Gilbert*.[199] In the following sections, this Note will justify that proposal by providing that it supports and embraces the original congressional intent behind TILA and furthers economic policy and consumer interest considerations.

A. Congress Would Approve: How the Proposal Satisfies Congressional Intent

Congress enacted TILA to provide consumers with tangible protection in credit transactions[200] through increased transparency[201] and the promotion of the "informed use of credit."[202] According to Congress, the "informed use of credit" would also enhance economic stabilization and "competition among the various financial institutions and other firms engaged in the extension of consumer credit."[203] However, as discussed above, the existing state of the law, encapsulated in a circuit split, fails to achieve this legislative intent.[204] For how can consumers be "informed" if their own rights

198. *See id.* ("Defendants contend that a notice of rescission must be unequivocal. . . . [However,] neither TILA and Regulation Z, which implements TILA, set forth any technical requirements that govern the language a consumer must use when requesting a rescission.").

199. *See supra* Part IV.

200. 15 U.S.C. § 1601(a) (2006).

201. Shepard, *supra* note 14, at 185.

202. 15 U.S.C. § 1601(a).

203. *Id.*

204. *See supra* Part III.

are indefinite and ill expounded? Similarly, how can economic stabilization and competition be enhanced when some jurisdictions allow consumers to indefinitely toll certain rights,[205] while others restrict those very same rights to statutorily defined periods?[206] As noted in *Rosenfield*, allowing any uncertainty with respect to the statutory three-year rescission period would "run counter to the commercial-certainty concerns of Congress (recognized in *Beach*) that led Congress to establish the fixed and limited repose period of § 1635(f) in the first place."[207]

Striking down *Gilbert*, as this Note proposes, would adhere to Congress's intent to both protect consumers and promote economic certainty. The consumer would retain the right to rescind the contract within the statutory three-year period, thus preserving an essential part of the protective scheme of TILA. In addition, confining the consumer's rescission rights to the statutory language of § 1635(f), by holding that a consumer must actually bring suit for rescission within the statutory three-year period, would eliminate the possibility that an innocent third-party purchaser of real estate or assignee of a mortgage could be divested of her interest after the statutory three-year period has run.[208] In turn, the confinement of rescission rights to the statutory three-year period would promote economic certainty in the lending market, and thus, prevent a foreseeable reduction in the marketability of property secured by mortgages and interests in mortgages. Clearly, the preservation of the marketability of property and interests in mortgages sustain the best economic interests of both lenders and consumers.[209] Therefore, striking down *Gilbert* is

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

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

207. *Rosenfield*, 681 F.3d at 1187.

208. *See* Jones v. Saxon Mortg., Inc., 537 F.3d 320, 327 (4th Cir. 1998); *see also* 15 U.S.C. § 1635(i) (2006) (explaining the obligor's right to rescind the transaction after the initiation of judicial or nonjudicial foreclosure proceedings); 15 U.S.C. § 1641(c) (2006) (explaining that any consumer that has a right to rescind under § 1635 may rescind the transaction as against any assignee of the obligation).

209. *See Jones*, 537 F.3d at 327 ("Given these differences between statutes of limitations and statutes of repose, it is understandable that a statute of limitations is tolled by a defendant's fraudulent concealment. To disallow tolling when a defendant has fraudulently concealed an injury would permit a defendant to use a device, that was created out of considerations of fairness, inequitably. Similarly, it is easy to understand why a statute of repose is typically an absolute time limit beyond which liability no longer exists and is not tolled for any reason. To permit tolling of a statute of repose would upset the economic best interests of the public as a whole." (citations omitted)).

consistent with the legislature's intent to protect consumers while simultaneously promoting economic certainty.

B. Removing the Clouds: How the Proposal Promotes Economic Certainty

The holding in *Gilbert* effectively permits consumers to indefinitely toll their rescission rights, potentially resulting in economic uncertainty, "clouded titles," and reduced marketability of foreclosed real estate.[210] However, the Supreme Court possesses the authority to circumscribe these latent economic risks by striking down *Gilbert* and expressly upholding *Rosenfield* and *Beach*. As this Note has proposed, the Court should exercise this authority in an attempt to restore economic certainty to the consumer credit marketplace.

Striking down *Gilbert* would prevent consumers from unilaterally and indirectly enlarging the congressionally established rescission period.[211] Under *Rosenfield*, consumers must bring suit for rescission within three years after the date of consummation,[212] or earlier if the property was sold.[213] Thus, both lenders and consumers, knowing that a rescission claim could be brought no later than three years after consummation, would be able to structure their respective affairs accordingly, thereby reducing the risk of economic uncertainty, "clouded titles," and diminishing real estate marketability. For example, a lender that fails to disclose certain information required by TILA would know, under this Note's proposed invalidation of *Gilbert*, that the original consumer could rescind the contract no later than three years after the date of consummation.[214] Thus, the lender, and other potential actors in the marketplace, could consciously avoid assignment or acquisition of loans burdened by possible rescission claims, thereby reducing the risk of third parties obtaining interest in the loan or property subject to potential divestment[215] and preserving the marketability of such

210. *See supra* Part III.C.

211. *See Rosenfield*, 681 F.3d at 1187.

212. *Id.* (citing McOmie-Gray v. Bank of Am. Home Loans, 667 F.3d 1325 (9th Cir. 2012)).

213. *See* 15 U.S.C. § 1635(f) (2006).

214. *See supra* Part IV.

215. *See* Jones v. Saxon Mortg., Inc., 537 F.3d 320, 327 (4th Cir. 1998); *see also* 15 U.S.C. § 1635(i)(1) ("[A]fter the initiation of any judicial or nonjudicial foreclosure process on the primary dwelling of an obligor securing an extension of credit, the obligor shall have a right to

property.[216] Similarly, as discussed in further detail below,[217] consumers would benefit from a strict repose interpretation of § 1635(f) and Regulation Z because their decision to rescind must involve a calculation of whether they are able to tender the required obligations to the lender upon rescission.[218] If consumers know that rescission is prohibited beyond a set date, the required market foresight is reduced, making the calculation simpler and more precise. Hence, consumers can more accurately predict the economic consequences of rescission and, as a result, make an "informed" decision.[219]

In addition, invalidating *Gilbert* would clarify and elucidate the process of exercising legally effective rescission.[220] *Gilbert* suggests that sending notice is sufficient to exercise rescission under § 1635(f) and Regulation Z.[221] *Gilbert* then goes on to apply a one-year statute of limitations from the date of the TILA violation for bringing a suit for rescission under § 1640(e).[222] However, other courts, including the Supreme Court, have refused to apply the Fourth Circuit's § 1640(e) test and have held that declaring notice of rescission as sufficient to exercise the right of rescission under § 1635(f) *indefinitely* tolls the rescission period.[223] It follows then that under *Gilbert*, a consensus among the judiciary regarding the post-notice limitation period is necessary to clearly and accurately define consumers' rescission rights. Currently, that consensus does not exist. By striking down *Gilbert* and upholding the principles in *Beach* and *Rosenfield*, the Court would determinatively define the rescission process as consisting of a necessary, but insufficient notice

rescind the transaction equivalent to other rescission rights provided by this section . . . ."); 15 U.S.C. § 1641(c) (2006) ("Any consumer who has the right to rescind a transaction under section 1635 of this title may rescind the transaction as against any assignee of the obligation.").

216. *See Jones*, 537 F.3d at 327.

217. *See infra* Part V.C.

218. *See* 15 U.S.C. § 1635(b) (2006).

219. *See* 15 U.S.C. § 1601(a) (2006).

220. *See* Rosenfield v. HSBC Bank, 681 F.3d 1172, 1188 (10th Cir. 2012) ("[N]otice, by itself, is not sufficient to exercise (or preserve) a consumer's right of rescission under TILA. The commencement of a lawsuit within the three-year TILA repose period [is] required.").

221. Gilbert v. Residential Funding LLC, 678 F.3d 271, 277 (4th Cir. 2012).

222. "Any action under this section may be brought in any United States district court, or in any other court of competent jurisdiction, within one year from the date of the occurrence of the violation." 15 U.S.C. § 1640(e) (2006); *see Gilbert*, 678 F.3d at 278–79.

223. *See* Beach v. Ocwen Fed. Bank, 523 U.S. 410, 417–19 (1998); *Rosenfield*, 681 F.3d at 1186–87; Sobieniak v. BAC Home Loans Servicing, LP, 835 F. Supp. 2d 705, 711 (D. Minn. 2011).

requirement, followed by a necessary and sufficient suit for rescission within the three-year statutory period.[224]

In conclusion, by invalidating *Gilbert*, the Supreme Court can enhance economic certainty, reduce the risk of "clouded titles," and clarify the process and requirements of consumer rescission.

C. A Consumer's Friend: How the Proposal Protects Consumers

As discussed above, consumers generally possess less leverage in loan negotiations than their lending counterparts.[225] Nonetheless, as a result of Congress's inclusion of § 1635(f) in TILA,[226] which substantially liberalized the steps necessary to unwind loan transactions, TILA has shifted a significant amount of leverage from lenders to consumers.[227] However, the added leverage from the rescission provisions is only palpable if the application of § 1635(f) is unambiguous. For example, when a consumer rescinds a loan agreement under TILA, he or she generally refinances his or her mortgage or sells his or her home and uses the proceeds from one of these transactions to return the lender to the status quo ante per the statutory requirements in § 1635(b).[228] But in today's depressed housing market, many consumers cannot afford to immediately tender their obligations upon rescission because the value of their homes has significantly decreased between the time the consumer refinanced the mortgage and when he or she sought rescission under § 1635(f), meaning that neither refinancing, nor the sale of his or her

224. *See Rosenfield*, 681 F.3d at 1188.

225. *See supra* Part III.B.

226.

> TILA's legislative history provides little guidance as to the precise reasons Congress created the rescission remedy. It is clear that Congress intended to protect homeowners from abuse by dishonest home improvement contractors who made questionable "home improvements" financed by loans secured by borrowers' homes. Beyond this articulated concern, however, courts and the Federal Reserve Board have little information about rescission's precise origins.

Shepard, *supra* note 14, at 191–92 (citations omitted).

227. *Id.* at 192.

228. *See* 15 U.S.C. § 1635(b) (2006) ("Within 20 days after receipt of a notice of rescission, the creditor shall return to the obligor any money or property given as earnest money, downpayment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction. . . . Upon the performance of the creditor's obligations under this section, the obligor shall tender the property to the creditor, except that if return of the property in kind would be impracticable or inequitable, the obligor shall tender its reasonable value.").

home, will cover the consumer's tender obligations.[229] Therefore, if the three-year period for rescission in § 1635(f) is extended indefinitely or for an additional year under § 1640(e), as in *Gilbert*, consumers risk losing the ability to tender their obligations upon rescission by sitting on their rights too long. Consumers must "fish or cut bait"—and an unquestionable and definite repose period would set a final "cut bait" point with which to base the decision of whether to rescind. If consumers knew that they had only three years to exercise their right to rescind a contract and thereby be forced to tender any obligation necessary to return the lender to the status quo ante, consumers would then be able to make an informed decision whether to rescind—and when to rescind—based on the current and forecasted market information. Thus, a strict three-year statutory limit on the right of rescission is necessary to protect consumers' leverage from their own potential misinformation or miscalculation. With a hardline three-year limit on the right to rescind, consumers can plan accordingly and do not run the risk of stretching their rescission rights passed the three-year period in hopes of economic rebound, only to find further market depression, thus preventing the consumer from tendering their obligations in full per § 1635(b) and ultimately leading to dismissal of the rescission claim.[230]

In conclusion, the proposal laid out above supports the original congressional intent behind the passage of TILA, promotes a stable economic environment, and preserves and protects consumer leverage in credit transactions.

VI. CONCLUSION

The split of authority regarding consumers' right to rescind credit transactions under TILA presents substantial risks to the underlying objectives of the consumer protection legislation. If the

229.

> Although courts have the equitable authority to modify consumers' tender obligations by allowing consumers to repay the net loan proceeds in installments, most courts have treated consumers' repayment obligations in an all-or-nothing fashion: consumers are required to tender in full immediately or within a short time, or their rescission claims are eventually dismissed.

Shepard, *supra* note 14, at 198.

230. "[I]f the court finds that 'the borrower cannot comply with [her] rescission obligations no matter what,' a court can dismiss the rescission action before deciding whether the defendants committed a material disclosure error." Shepard, *supra* note 14, at 201 (quoting Yamamoto v. Bank of N.Y., 329 F.3d 1167, 1173 (9th Cir. 2003)).

holding in *Gilbert* is allowed to survive as good law, consumers will suffer the worst of the consequences. They will be forced to participate in an unpredictable and instable lending marketplace, with the looming risk of foreclosure weighing on them, and with weakened and ill-defined rights providing unsatisfactory protection from unfair credit practices and foreclosure. The Supreme Court needs to invalidate *Gilbert* and consolidate judicial consensus by upholding *Rosenfield* and *Beach*. In doing so, as this Note has put forth, the Court would support the congressional intent underlying TILA and Regulation Z, prevent economic uncertainty and instability, and preserve the necessary leverage and rights of consumers.