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In A Putative Class Action, The Third Circuit Holds That A Plaintiff Must Show Detrimental Reliance On Improper Loan Disclosure Statements To Obtain Actual Damages Under The Truth In Lending Act

By Shannon Petersen

On December 31, 2009, the Third Circuit held that a borrower must prove detrimental reliance to obtain actual damages for a violation of the federal Truth in Lending Act ("TILA"). *See Vallies v. Sky Bank,* ---F.3d---, 2009 WL 5154473 (3rd Cir. 2009).

Under TILA, the federal government requires that lenders make certain disclosures to borrowers about the terms of their loans before lending them money. TILA claims are at the epicenter of the mortgage litigation crises. Over the past two years, TILA claims, including class action claims, have flooded the state and federal courts. Most of these claims involve allegations that some technical TILA disclosure violation has occurred.

Though not a mortgage case, the allegations of the borrower in *Vallies v. Sky Bank* are typical. The plaintiff alleged that the finance charge statement made by the bank for an auto loan was misleading in that it did not include $395 representing the amount of the debt cancellation insurance, which the plaintiff alleged should have been included in the finance charge statement under TILA. The district court granted summary judgment in favor of the bank because the borrower had failed to show that (1) he had read the TILA disclosure statement pertaining to finance charges, (2) he had understood the finance charges being disclosed, (3) had the disclosure been accurate by including an additional $395, he would have sought better terms or foregone the loan, and (4) if he had sought better terms, he would have obtained them.

The Third Circuit declined to state the specific facts or circumstances that constitute detrimental reliance under TILA, but affirmed the decision of the district court that detrimental reliance must be shown and had not been shown here. In so holding, the Third Circuit relied on the language of

TILA itself, which provides for both actual damages and statutory damages. According to the Third Circuit, to obtain actual damages, a plaintiff must show causation by showing that he or she relied on a misleading or improper loan disclosure statement to his or her detriment. In contrast, to obtain statutory damages, a plaintiff must only show that a violation of TILA has occurred. (For class action suits, statutory damages under TILA are capped at the lesser of $500,000 or 1% of the defendant's net worth.).

In reaching its decision, the Third Circuit considered but rejected as irrelevant the concerns of some legal commentators, who have noted that under a detrimental reliance standard actual damages for TILA loan disclosure violations may be difficult to prove. The court also disregarded the fact that "detrimental reliance may create obstacles for class certification because of the individualized fact-specific nature of the reliance inquiry." The court distinguished other case law, holding that detrimental reliance under TILA is not necessary, on the grounds that those cases involved claims for statutory damages, not actual damages, under TILA.

Finally, the Third Circuit noted that it joined the holding of every other circuit court that has addressed the issue, including the First, Fifth, Sixth, Eighth, and Ninth Circuits. *Citing United States v. Petroff-5 Kline*, 557 F.3d 285, 297 (6th Cir. 2009) ("[A]ctual damages require a showing of detrimental reliance."); *McDonald v. Checks-N-Advance, Inc. (In re Ferrell)*, 539 F.3d 1186, 1192 (9th Cir. 2008) (finding no valid basis to overturn the rule of *In re Smith* requiring a showing of detrimental reliance to establish actual damages); *Gold Country Lenders v. Smith (In re Smith)*, 289 F.3d 1155, 1157 (9th Cir. 2002) ("Wejoin with other circuits and hold that in order to receive actual damages for a TILA violation . . . a borrower must establish detrimental reliance."); *Turner v. Beneficial Corp.*, 242 F.3d 1023, 1028 (11th Cir. 2001) (en banc) ("We hold that detrimental reliance is an element of a TILA claim for actual damages . . . ."); *Perrone v. Gen. Motors Acceptance Corp.*, 232 F.3d 433, 434–40 (5th Cir. 2000) (holding that detrimental reliance is an element of a claim for actual damages); *Peters v. Jim Lupient Oldsmobile Co.*, 220 F.3d 915, 917 (8th Cir. 2000)(requiring a showing of proximate causation and adopting a four-prong reliance test for establishing actual damages); *Bizier v. Globe Fin. Servs., Inc.*, 654 F.2d 1, 4 (1st Cir. 1981) (noting *in dicta* the need to show causation for an award of actual damages "in addition to a threshold showing of a violation of a TILA requirement").

Under this law, it is not enough, as plaintiffs in TILA cases often do, to allege that a TILA loan disclosure violation has occurred. Instead, a plaintiff must also allege and prove that he or she relied on the misleading or improper statement and as a result of this reliance suffered actual damage. This recent decision of the Third Circuit also emphasizes the difficulty of certifying a class action for actual damages under TILA. Even where the named plaintiff has detrimentally relied on an improper loan disclosure statement, such reliance can rarely be universally inferred for other, unnamed class members. Instead, to determining detrimental reliance usually requires an individual inquiry about whether the class member read the disclosure statement, understood it, and relied on it to his or her detriment. For this reason, such cases are very difficult to certify for class treatment. *See, e.g., Stout v. J.D. Byrider*, 228 F.3d 709, 718 (6th Cir. 2000) (affirming the denial of class certification based on the need for individualized assessment of whether "each putative class member relied upon false representations or failures to disclose" under TILA).