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Good Cop, Bad Cop: Market Competitors, UDAP Consumer Protection Laws, and the U.S. Mortgage Crisis

James J. Pulliam

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State unfair or deceptive acts or practices statutes (UDAPs) offer consumers broad protections against abusive business activity. However, although UDAPs could have been used to combat predatory lending during the housing bubble, the laws generally failed to detour the predatory lending that fueled the mortgage crisis. One reason that UDAPs did not play a bigger role in litigating against predatory lending is that states limit or deny UDAP standing for business competitors. Because businesses often lack a transactional nexus with other competitor businesses in their marketplaces, this Article argues that UDAPs should provide businesses with representative standing free of an injury-in-fact requirement. This reform would allow businesses that suffer a diminished capacity to compete when their competitors act in unfair ways to engage in industry self-policing by using UDAPs to litigate against abusive business practices in their marketplaces.

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I. INTRODUCTION

From 1993 to 2007, Fremont Investment & Loan ("Fremont"),[1] was one of the most pervasive subprime[2] lenders in the Commonwealth of Massachusetts.[3] Between January 2004 and March 2007, Fremont originated 14,578 owner-occupied home mortgages in the state.[4] The majority of these loans were subprime, and nearly all of them were quickly unloaded on the secondary market.[5] More importantly, these loans were not designed to foster stable homeownership.[6] By the end of 2007, fewer than 2,000 Fremont-originated Massachusetts loans remained in existence—the rest having ended through refinance, sale, or foreclosure.[7] Of the remaining 2,000 mortgages, nearly a quarter were in default.[8]

After more than 6,500 Massachusetts family homes were lost to foreclosure,[9] the state's Attorney General finally took action.[10] In

1. Chartered in California, Fremont originated residential mortgages nationwide. Amended Brief of Defendant-Appellant Fremont Investment & Loan at 5–6, Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548 (Mass. 2008) (No. 10258), 2008 WL 4296889 [hereinafter Amended Brief of Fremont]; Brief of the Commonwealth of Massachusetts at 8–9, Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548 (Mass. 2008) (No. 10258), 2008 WL 4448973 [hereinafter Brief of Commonwealth]. In March 2007, Fremont exited the home-loan business after settling federal claims of unsound and illegal lending practices. Brief of Commonwealth, *supra*, at 9; Amended Brief of Fremont, *supra*, at 6 n.3. In June 2008, Fremont filed for bankruptcy. *Fremont Inv. & Loan*, 897 N.E.2d at 548 n.1.

2. For an explanation of the differences between prime and subprime lenders, see note 76 and accompanying text, *infra*.

3. *Fremont Inv. & Loan*, 897 N.E.2d at 550–52; CHRISTOPHER L. FOOTE ET AL., FED. RESERVE BANK OF BOSTON, SUBPRIME FACTS: WHAT (WE THINK) WE KNOW ABOUT THE SUBPRIME CRISIS AND WHAT WE DON'T 13 (2008); Kimberly Blanton, *Subprime Lender Sued Under Predator Law; AG Accuses Fremont of 'Worst Practices,'* BOSTON GLOBE, Oct. 6, 2007, at C10.

4. *Fremont Inv. & Loan*, 897 N.E.2d at 551.

5. *Id.* at 551–52 & n.7.

6. *See, e.g.*, Barbara Crutchfield George et al., *The Opaque and Under-Regulated Hedge Fund Industry: Victim or Culprit in the Subprime Mortgage Crisis?*, 5 N.Y.U. J. L. & BUS. 359, 391–96 (2009).

7. Brief of Commonwealth, *supra* note 1, at 13–14.

8. *Id.*

9. Kimberly Blanton, *Ex-Fremont Pair Offer Inside Look at Lender: Aggressive Sales Tactics, Brokers Cited in State Fraud Suit*, BOSTON GLOBE, Jan. 17, 2008, at D1.

10. *See* Complaint at 1, Commonwealth v. H & R Block, Inc., No. 2008-2474 (Mass. Super. Ct. Jan. 3, 2008), 2008 WL 6008126; Complaint at 1, Commonwealth v. Fremont Inv. & Loan, No. 07-4373-F (Mass. Super. Ct. Oct. 4, 2007), 2007 WL 5180872; William M. Bulkeley, *Goldman Settles Subprime Inquiry—Bank's Agreement with Massachusetts Requires Relief of*

Commonwealth v. Fremont Investment & Loan,[11] the Attorney General brought suit against Fremont, alleging that its lending practices violated Massachusetts's unfair and deceptive acts or practices statute.[12] In ruling against Fremont, the Massachusetts Supreme Court affirmed the trial court's grant of injunctive relief enjoining the foreclosure of Fremont loans with certain characteristics that "doomed [the mortgages] to foreclosure."[13]

The Massachusetts law at issue in *Fremont Investment & Loan*[14] is one example of state unfair or deceptive acts or practices statutes (UDAPs) that are designed to protect consumers and business competitors from unfair business activity.[15] However, these statutes proved ineffective during the recent mortgage crisis, because they failed to sufficiently deter the widespread predatory lending that harmed individual borrowers and contributed to the excessive speculation and risky lending that caused the broader financial meltdown.[16] While the application of Massachusetts's UDAP in *Fremont Investment & Loan* prevented imminent foreclosure for some homeowners,[17] its overall effectiveness was too limited to halt the spread of foreclosures that led to the broader economic crisis.[18]

$60 Million, WALL ST. J., May 12, 2009, at C3 (detailing a 2009 settlement between Massachusetts and Goldman Sachs for securitizing unfair loans).

11. Commonwealth v. Fremont Inv. & Loan, No. 07-4373-BLS1, 2008 WL 517279 (Mass. Super. Ct. 2008), *aff'd*, 897 N.E.2d 548 (Mass. 2008).

12. *Id.* at *1.

13. Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548, 554 (Mass. 2008); *Fremont Inv. & Loan*, 2008 WL 517279, at *1, *10; *see also infra* Part II.C (discussing the court's decision in more detail).

14. MASS. GEN. LAWS ch. 93A, § 2 (2006).

15. *See, e.g.*, Michael Flynn & Karen Slater, *All We Are Saying Is Give Business a Chance: The Application of State UDAP Statutes to Business-to-Business Transactions*, 15 LOY. CONSUMER L. REV. 81, 81–82 (2003); Note, *Toward Greater Equality in Business Transactions: A Proposal to Extend the Little FTC Acts to Small Businesses*, 96 HARV. L. REV. 1621, 1623–24 (1983) [hereinafter *Toward Greater Equality*].

16. *See infra* Part III.A. *See generally* DEAN BAKER, FALSE PROFITS: RECOVERING FROM THE BUBBLE ECONOMY (2010) (discussing the causes and scope of the financial crisis); RICHARD A. POSNER, THE FAILURE OF CAPITALISM: THE CRISIS OF '08 AND THE DESCENT INTO DEPRESSION (2009) (analyzing the origins of the current recession, and critiquing the government and economic response); Prentiss Cox, *The Importance of Deceptive Practice Enforcement in Financial Institution Regulation*, 30 PACE L. REV. 279 (2009) (positing that stronger enforcement of consumer protection laws should be part of a restructured financial regulatory system).

17. The Fremont Investment & Loan injunction was issued on February 25, 2008 and remained in place through the appellate process. *Fremont Inv. & Loan*, 897 N.E.2d at 553–55; *Fremont Inv. & Loan*, 2008 WL 2312648, at *1. In 2009, Fremont settled with the Massachusetts

Given that state UDAP statutes give courts broad authority to protect consumers from the unfair or deceptive tactics employed in predatory lending, why did they fail to stop the abusive business practices that contributed to the mortgage crisis? One reason is that relatively few plaintiffs successfully utilized UDAPs to challenge the rise of risky and predatory lending in the years leading up to the mortgage crisis.[19] This failure to litigate was due in part to the fact that most UDAPs either limit or omit standing for a group of potential plaintiffs who are arguably in the best position to make effective and efficient use of UDAP claims—business competitors.[20]

By using California's Unfair Competition Law (UCL)[21] as a model through which to evaluate UDAP shortcomings, it is evident that mortgage-market competitors[22] were in the best position to successfully use UDAPs to police their own marketplaces through litigation. Compared to individual consumers and public law offices[23] (the two groups most frequently conferred with UDAP standing) market competitors (1) are better able to quickly and accurately identify and advocate against unfair business practices; (2) are invested in securing stable and successful marketplaces, rather than just remedying past wrongs; and (3) collectively have more resources

Attorney General for $10 million in damages, penalties, and costs. *See* Jennifer Levitz, *Fremont General Settles Deceptive-Loans Case*, WALL ST. J., June 10, 2009, at C4.

18. *See* JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., THE STATE OF THE NATION'S HOUSING 2009, at 2 (2009).

19. *See, e.g.*, Cox, *supra* note 16, at 293–96 (surveying examples of successful state attorney general litigation against predatory lending); *infra* Part III.A.

20. Flynn & Slater, *supra* note 15, at 87–89 (2003); D. Wes Sullenger, *Only We Can Save You: When and Why Non-Consumer Businesses Have Standing to Sue Business Competitors Under the Tennessee Consumer Protection Act*, 35 U. MEM. L. REV. 485, 490–93 (2005); *Toward Greater Equality*, *supra* note 15, at 1621, 1626–28; *see also* JONATHAN SHELDON & CAROLYN L. CARTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES § 2.1.8, at 15–21 (6th ed. 2004) (explaining how issues of statutory interpretation determine whether a transaction is a "consumer transaction" for the purposes of UDAP standing).

21. CAL. BUS. & PROF. CODE §§ 17200–17210 (West 2006).

22. The terms "market competitors" and "business competitors" refer to the different businesses that make up an industry. In the context of the mortgage market, market competitors would include, for example, businesses engaged in lending, brokering loans, and appraising.

23. "Public law offices" refers to the offices of state attorneys general, county counsels, district attorneys, city attorneys, and other state officials with authority to pursue UDAP litigation. *See* ROBERT C. FELLMETH, CAL. LAW REVISION COMM'N, CALIFORNIA'S UNFAIR COMPETITION ACT: CONUNDRUMS AND CONFUSIONS 1 (1995). Because UDAPs vary from state to state, this general term is used to represent the public enforcement provisions of these statutes. *See* SHELDON & CARTER, *supra* note 20, §§ 10.2–10.7, at 931–64.

to prosecute litigation.[24] This Article therefore contends that UDAPs could have been more successful at preventing the pervasive predatory lending that contributed to the mortgage crisis if the statutes had provided broader standing for market competitors.

Part II provides background on UDAP statutes, the mortgage crisis, and predatory lending. Part III shows that while state UDAPs can have positive regulatory effects on financial markets, they generally limit standing for businesses in a harmful way. Part IV offers a proposal for enhancing the effectiveness of UDAPs by reforming UDAP standing for business litigants despite potential limitations from state constitutions[25] and federal preemption.[26] Part V concludes that the relaxation of standing requirements for businesses would better equip UDAPs to achieve their statutory purpose of preventing unfair business activity.

II. MORTGAGES, CONSUMER PROTECTION, AND THE CRISIS

The recent collapse of the housing market has caused the worst recession since the Great Depression,[27] and predatory lending was a key contributor to the crisis.[28] Although various federal and state statutes protect consumers from predatory lending in theory, these regulations have generally failed to do so in practice.[29] Designed to

24. *See infra* Part IV.C.1.

25. *See infra* note 204 and accompanying text.

26. Federal preemption of state efforts to regulate the mortgage industry is an ongoing and controversial issue. *See* Watters v. Wachovia Bank, N.A., 550 U.S. 1, 6–7 (2007); *see also* Keith R. Fisher, *Toward a Basal Tenth Amendment: A Riposte to National Bank Preemption of State Consumer Protection Laws*, 29 HARV. J.L. & PUB. POL'Y 981, 984–86 (2006) ("Early in 2004, [the Office of the Comptroller of the Currency], . . . promulgated regulations purporting to preempt all state laws that 'obstruct, impair, or condition a national bank's ability to fully exercise' its federally granted powers. Even more controversially, the preemption applies whether a national bank exercises such powers directly or through one or more state chartered operating subsidiaries."); G. Marcus Cole, *Protecting Consumers from Consumer Protection:* Watters v. Wachovia Bank, 2007 CATO SUP. CT. REV. 251, 251–53 (2007) ("[T]he issue in *Watters v. Wachovia Bank* is actually a policy choice disguised as a doctrinal one. The real issue is whether given our national credit markets, states should have extensive authority to impose cumbersome, expensive, and, indeed, irrational regulation on operating subsidiaries of a national bank."). However, current congressional proposals are exploring the curtailment of preemption in this area as part of the federal legislative response to the mortgage crisis. *See* Consumer Financial Protection Agency Act of 2009, H.R. 3126, 111th Cong. § 141 (2009).

27. *See, e.g.*, POSNER, *supra* note 16, at vii.

28. Cox, *supra* note 16, at 279.

29. *See, e.g.*, Rayth T. Myers, Comment, *Foreclosing on the Subprime Loan Crisis: Why Current Regulations Are Flawed and What Is Needed to Stop Another Crisis from Occurring*, 87 OR. L. REV. 311, 323–40 (2008).

combat any type of abusive business practice, state UDAPs offer an alternative mechanism to regulate the mortgage market.[30]

A. UDAPs and the UCL

UDAPs are foundational consumer protection laws that grew out of the 1914 Federal Trade Commission Act (the "FTC Act").[31] In prohibiting "unfair or deceptive acts or practices,"[32] Congress intentionally framed the FTC Act's language in broad terms so that courts could develop and refine definitions of "unfair or deceptive practices."[33] Nonetheless, Congress limited the FTC Act's effectiveness by restricting its enforcement to the Federal Trade Commission (FTC)[34]: there is no private right of action, and there is no public right of action for state or local governments.[35]

In the 1960s, the perceived inadequacies of common-law claims and FTC regulation led states to enact UDAPs to provide a cause of action against unfair business practices.[36] As a result, all fifty states now provide UDAP authority to their public law offices to investigate and enjoin unfair or deceptive business practices[37] and

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30. Jessica Fogel, Comment, *State Consumer Protection Statutes: An Alternative Approach to Solving the Problem of Predatory Mortgage Lending*, 28 SEATTLE U. L. REV. 435, 459–65 (2005).

31. Federal Trade Commission Act of 1914, Pub. L. No. 63-203, § 5, 38 Stat. 717 (1914) (codified as amended at 15 U.S.C. §§ 41–58 (2006)); Sullenger, *supra* note 20, at 489–93. The FTC Act itself can be traced to common-law claims brought by market competitors for unfair competition based on "trademark or trade name infringement." WILLIAM L. STERN, BUS. & PROF. C. § 17200 PRACTICE ch. 2-A (2010); Wesley J. Howard, Note, *Former Civil Code Section 3369: A Study in Judicial Interpretation*, 30 HASTINGS L.J. 705, 706–13 (1978).

32. *See* Wheeler-Lea Act of 1938, Pub. L. No. 75-447, § 3, 52 Stat. 111 (1938) (codified as amended at 15 U.S.C. §§ 41–58 (2006)) (amending the FTC Act of 1914). The 1914 Act originally prohibited "unfair methods of competition in commerce." Federal Trade Commission Act of 1914, Pub. L. No. 63-203, § 5, 38 Stat. 717 (1914).

33. STERN, *supra* note 31, at ch. 3-A.

34. *See, e.g.*, ABA, FTC PRACTICE AND PROCEDURE MANUAL 11–56 (2007).

35. *See, e.g.*, MICHAEL M. GREENFIELD, CONSUMER LAW: A GUIDE FOR THOSE WHO REPRESENT SELLERS, LENDERS, AND CONSUMERS 63–64 (1995); FELLMETH, *supra* note 23, at 5–6; *see also* Holloway v. Bristol-Myers Corp. 485 F.2d 986, 987, 1002 (D.C. Cir. 1973) ("[P]rivate actions to vindicate rights asserted under the Federal Trade Commission Act may not be maintained."); Carlson v. Coca-Cola Co., 483 F.2d 279, 280–81 (9th Cir. 1973) ("The protection against unfair trade practices afforded by the [FTC] Act vests initial remedial power solely in the Federal Trade Commission.").

36. *Toward Greater Equality*, *supra* note 15, at 1625–26 (stating that there are three principal policy rationales behind the adoption of the Little FTC Acts: (1) to rectify an "imbalance of power in the marketplace"; (2) to "make litigating small claims economical"; and (3) to further the effective enforcement of the law through the provision of a private remedy).

37. SHELDON & CARTER, *supra* note 20, § 1.1, at 1.

forty-nine of those states also include a private right of action for such claims.[38] While they vary greatly in structure,[39] UDAPs are generally patterned after similar model codes.[40]

California's UDAP, the UCL, provides an example of a typical structure for a UDAP.[41] The UCL prohibits "any unlawful, unfair or fraudulent business act or practice."[42] To prevail, a UCL plaintiff must prove the following: (1) the defendant was engaged in a business act or practice;[43] and (2) the alleged conduct was (a) unlawful, (b) unfair, or (c) fraudulent.[44] UCL cases tasked with defining a "business act or practice" have typically applied the term to a broad range of conduct so as to give effect to the statutory scheme's broad remedial purpose.[45] Similarly, a single act is sufficient to violate the UCL.[46] Generally, a pattern of conduct is relevant only when a court fashions remedial relief.[47]

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38. Prentiss Cox, *Goliath Has the Slingshot: Public Benefit and Private Enforcement of Minnesota Consumer Protection Laws*, 33 WM. MITCHELL L. REV. 163, 167 (2006). Iowa is the only state that omits a UDAP private right of action. *Id.*; SHELDON & CARTER, *supra* note 20, §§ 7.2.1–7.2.2, at 659–61.

39. *See generally* SHELDON & CARTER, *supra* note 20, §§ 1.1–1.2, at 1–2 (providing a 1000+-page treatise on the nuances of UDAP schemes, and the depth of their jurisprudence).

40. Cox, *supra* note 38, at 166–67 (describing the four model codes and categorizing them as (1) "general statutory fraud laws" or (2) "topical laws that regulate specific types of consumer transactions"). Reliance on these model codes led many states to enact multiple UDAP schemes. *See* Fogel, *supra* note 30, at 454. This Article focuses on general statutory fraud laws like California's UCL. *See* CAL. BUS. & PROF. CODE §§ 17200–17210 (West 2006).

41. However, despite sharing similar characteristics with other UDAPs, the UCL's history is related to the FTC Act, but largely independent of the 1960s model codes. *See* FELLMETH, *supra* note 23, at 2–15; STERN, *supra* note 31, at ch. 2-B–2-F; Howard, *supra* note 31, at 715–21.

42. CAL. BUS. & PROF. CODE § 17200 (West 2006); STERN, *supra* note 31, at ch. 2-F.

43. STERN, *supra* note 31, at ch. 3-D–3-E.

44. Kasky v. Nike, Inc., 45 P.3d 243, 249 (Cal. 2002); Joshua D. Taylor, Note, *Why the Increasing Role of Public Policy in California's Unfair Competition Law Is a Slippery Step in the Wrong Direction*, 52 HASTINGS L.J. 1131, 1133–35 (2001). The UCL also prohibits "[u]nfair, deceptive, untrue or misleading advertising" and "[a]ny act prohibited by [California Business & Professions Code] §§ 17500–17577.5," but these latter two wrongs are duplicative of conduct prohibited under the three primary provisions. STERN, *supra* note 31, at ch. 3-C (alteration and emphasis omitted); Sharon J. Arkin, *The Unfair Competition Law After Proposition 64: Changing the Consumer Protection Landscape*, 32 W. ST. U. L. REV. 155, 157–63 (2005).

45. STERN, *supra* note 31, at ch. 3-D.

46. *See* CAL. BUS. & PROF. CODE § 17200; STERN, *supra* note 31, at ch. 3-E.

47. *See* CAL. BUS. & PROF. CODE § 17204; STERN, *supra* note 31, at ch. 3-E.

The UCL provides standing for both public law offices and private parties.[48] However, private plaintiffs must show that they have "suffered [an] injury in fact and . . . lost money or property as a result of the unfair competition."[49] This injury-in-fact requirement limits standing to those consumers or businesses that are directly harmed by the unlawful conduct, preventing individuals from bringing suit on behalf of a different injured party.[50] If UCL standing requirements are satisfied and litigation is successful, a private plaintiff's potential remedies are limited to equitable relief.[51] Thus, while restitution and injunctive relief are available, traditional damages are not.[52] Further, while not specifically provided for in the statutory scheme, successful plaintiffs may recover attorney's fees if the litigation furthers an important public interest.[53]

Like many other UDAPs, the UCL prohibits three types of conduct: unlawful, unfair, and fraudulent.[54] The first type of conduct for which the UCL creates a cause of action is "unlawful" conduct.[55] This general prohibition of illegal business practices means that a plaintiff can bring or "borrow" a UCL claim where the defendant's conduct violates some other law.[56] Under this provision, proof of the

48. The UCL empowers various public law offices with enforcement authority, including: (1) the Attorney General; (2) district attorneys; and (3) any city attorney representing a city with a population that exceeds 750,000. CAL. BUS. & PROF. CODE § 17204.

49. *Id.*

50. *See infra* Part III.C.

51. Arkin, *supra* note 44, at 164–65. Many UDAPs do provide for monetary damage awards in various forms. Although forty-nine states are uniform in providing for a UDAP private right of action, they are substantially inconsistent in their treatment of available statutory remedies for UDAP violations. *See generally* SHELDON & CARTER, *supra* note 20, §§ 8.1–8.2, at 737–39 (surveying various statutory approaches for remedying UDAP violations); DEE PRIDGEN, CONSUMER PROTECTION AND THE LAW §§ 6.1–6.34 (2d ed. 2003) (same).

52. STERN, *supra* note 31, at ch. 8-A.

53. *See* CAL. CIV. PROC. CODE § 1021.5 (West 2010) (establishing four criteria under California law for evaluating an appropriate shift of attorney's fees in the public's interest); *see also* STERN, *supra* note 31, at ch. 8-A (examining the different theories by which a successful UCL plaintiff can recover attorney's fees). Nationally, in UDAP litigation, "the prevailing plaintiff is normally entitled to an award of reasonable fees and costs." PRIDGEN, *supra* note 51, §§ 6.17–6.27; *see also* SHELDON & CARTER, *supra* note 20, § 8.8, at 796–834 (providing a national overview of UDAP attorney's fees provisions).

54. These clauses are disjunctive. For example, "lawful" conduct can still be unfair or fraudulent, and therefore illegal under the UCL. *See* STERN, *supra* note 31, at ch. 3-G.

55. CAL. BUS. & PROF. CODE § 17200 (West 2006); STERN, *supra* note 31, at ch. 3-F.

56. *See* STERN, *supra* note 31, at ch. 3-F.

violation of the borrowed law thus becomes a per se UCL violation.[57] For example, a plaintiff can formulate a UCL claim based on a defendant's violation of a federal statute and regulation, an FTC guideline or opinion, a state statute and regulation, a local ordinance, judicial precedent, or perhaps a law of another jurisdiction.[58]

The second type of conduct for which the UCL creates a cause of action is "unfair" conduct.[59] This provision allows courts to find a business activity unfair, "even if [it is] not specifically proscribed by some other law."[60] Like the language of the FTC Act, the UCL language was intentionally left broad by the legislature in order to provide courts with the greatest ability and discretion to define prohibited conduct.[61]

The third type of conduct for which the UCL creates a cause of action is "fraudulent" business conduct.[62] The term "fraudulent" has been interpreted to mean business activity that is likely to deceive the public.[63] While application of this fraudulent-conduct restriction is most frequently found in the context of false advertising,[64] UCL claims for fraudulent practices need not involve advertising or false statements.[65]

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57. *See generally* SHELDON & CARTER, *supra* note 20, §§ 3.2.6–3.2.7, at 120–29 (surveying jurisdictional approaches to UDAP prohibition of unlawful conduct).

58. STERN, *supra* note 31, at ch. 3-F. A successful UDAP "unlawful" claim can unlock several advantages that may be unavailable under the borrowed law. *See id.* at ch. 7-A; SHELDON & CARTER, *supra* note 20, § 3.2.7.1, at 121.

59. CAL. BUS. & PROF. CODE § 17200; *see also* SHELDON & CARTER, *supra* note 20, § 3.3.4.3, at 131 ("Over thirty UDAP statutes prohibit unfair practices and about ten UDAP statutes proscribe unconscionable acts. Neither of these standards is precisely defined. Instead they are expansive evolving concepts that can be used to challenge novel forms of consumer abuse.").

60. Cel-Tech Commc'ns, Inc. v. L.A. Cellular Tel. Co., 973 P.2d 527, 540 (Cal. 2002).

61. STERN, *supra* note 31, at ch. 3-G ("One advantage to plaintiffs in including an 'unfairness' claim is that [the UCL's] prohibition of 'unfair' practices sometimes can be used to stretch statutory prohibitions beyond their express or technical limits.").

62. CAL. BUS. & PROF. CODE § 17200.

63. *See* Comm. on Children's Television, Inc. v. Gen. Foods Corp., 673 P.2d 660, 668 (Cal. 1983). In contrast to common-law fraud claims, under the UCL "a plaintiff can prove a *prima facie* case that a business practice is 'fraudulent' without having to prove intent, scienter, actual reliance, or damage. Even actual deception is not required." STERN, *supra* note 31, at ch. 3-H; *see also* SHELDON & CARTER, *supra* note 20, § 4.2.3.1, at 144 (describing the elements of common-law fraud).

64. Arkin, *supra* note 44, at 161–63.

65. *See, e.g.*, Allied Grape Growers v. Bronco Wine Co., 249 Cal. Rptr. 872, 882–85 (Ct. App. 1988); STERN, *supra* note 31, at ch. 3-H.

B. Federal and State Mortgage Regulations Proved Ineffective at Mitigating Predatory Lending

The current mortgage crisis is the result of a housing bubble that began in the late 1990s and early 2000s.[66] After American home sales, ownership, and construction peaked in 2006—all hitting or nearing historic highs[67]—prices dropped and the bubble burst.[68] A $10 trillion industry in 1995,[69] the housing market saw nearly $6 trillion in home equity evaporate.[70] As the national foreclosure rate tripled,[71] the crisis spread to the financial markets,[72] resulting in a "$5.3 trillion plunge in the real value of stocks and mutual funds."[73] Roughly 6 million Americans lost their jobs, while an additional 11 million were underemployed or had stopped looking for work.[74] As the severity of these consequences demonstrates, effective regulation of home-mortgage lending is of critical importance.

1. Predatory Lending

A mortgage is a contract that conveys an interest in a piece of land from a borrower to a lender as security for payment of a debt.[75] Generally, home loans are either "prime" or "subprime."[76] Although

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66. *See* BAKER, *supra* note 16, at 17–26, 33–34.

67. *Id.* at 19–21, 26, 31 (noting how this growth occurred without corresponding increases in income and population—the two demand factors that have historically driven increases in home prices).

68. *Id.* at 35; JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 1.

69. BAKER, *supra* note 16, at 18.

70. *See id.* at 35; JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 9.

71. JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 1–2.

72. *See* BAKER, *supra* note 16, at 33; JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 2, 9.

73. JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 13.

74. *Id.* at 2 (citing statistics as of April 2009).

75. MARGARET C. JASPER, HOME MORTGAGE LAW PRIMER 5 (2000).

76. *See, e.g.*, Todd J. Zywicki & Joseph D. Adamson, *The Law and Economics of Subprime Lending*, 80 U. COLO. L. REV. 1, 5–9 (2009). Prime loans offer a uniform low interest rate and are issued only to borrowers with sufficiently high credit scores. *See* Baher Azmy, *Squaring the Predatory Lending Circle: A Case for States as Laboratories of Experimentation*, 57 FLA. L. REV. 295, 304 (2005). In contrast, subprime mortgages "are loans with higher interest rates . . . designed for borrowers with impaired credit or who do not otherwise qualify for loans in the conventional prime market." Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255, 1261 (2002). During the housing bubble, Alt-A mortgages, which fit somewhere in between prime and subprime loans, also developed as a significant source of risky lending. *See* Lauren E. Willis, *Will the Mortgage*

the mortgage crisis is often tied to abuses in the subprime market,[77] subprime and predatory loans are not always coextensive products.[78] Rather, for the purposes of UDAP litigation, the focus is on "predatory lending," a term that collectively represents unfair practices in the mortgage market.[79]

Predatory lending can occur at any stage of the lending process. A typical borrower is obliged to interact with a mortgage broker, an appraiser, a lender, and a servicer in a complex transaction involving hundreds of thousands of dollars.[80] When this transactional complexity is paired with several layers of convoluted federal and state regulations,[81] even the most rational actors can struggle to identify unfair practices.[82] Thus it is extremely difficult to uniformly define and identify the abusive business practices that contributed to the mortgage crisis.[83]

In general, a mortgage can be predatory through either substantive or procedural unfairness (unfair terms versus unfair sales tactics).[84] Predatory loans are substantively unfair when they are either (1) "overpriced" or (2) "overly risky."[85] First, a loan is overpriced when a borrower receives a loan with a higher interest

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Market Correct? How Households and Communities Would Fare If Risk Were Priced Well, 41 CONN. L. REV. 1177, 1214 & nn.137–39 (2009).

77. *See* BAKER, *supra* note 16, at 26–33.

78. Azmy, *supra* note 76, at 303–04; Engel & McCoy, *supra* note 76, at 1261; *cf.* SONIA GARRISON ET AL., CTR. FOR RESPONSIBLE LENDING, CONTINUED DECAY AND SHAKY REPAIRS: THE STATE OF SUBPRIME LOANS TODAY 3 (2009) (arguing that the subprime market has ultimately resulted in a loss of wealth and a net decline in homeownership); Alan M. White, *Deleveraging the American Homeowner: The Failure of 2008 Voluntary Mortgage Contract Modifications*, 41 CONN. L. REV. 1107, 1109 (2009) (positing that subprime mortgages "triggered the broader credit crisis").

79. *See* Azmy, *supra* note 76, at 297–300; Engel & McCoy, *supra* note 76, at 1259–60; Lauren E. Willis, *Decisionmaking and the Limits of Disclosure: The Problem of Predatory Lending: Price*, 65 MD. L. REV. 707, 738–41 (2006).

80. *See* JASPER, *supra* note 75, at 49–64; The Mortgage Professor's Website, Mortgage Glossary, http://www.mtgprofessor.com/glossary.htm (last visited Aug. 8, 2010).

81. *See, e.g.*, Cox, *supra* note 16, at 283–86; Christopher L. Peterson, *Predatory Structured Finance*, 28 CARDOZO L. REV. 2185, 2225–32 (2007).

82. *See, e.g.*, Willis, *supra* note 79, at 749–54.

83. *Id.* at 735–36.

84. Azmy, *supra* note 76, at 332–43.

85. Willis, *supra* note 79, at 735–36.

rate than one for which the borrower is otherwise qualified.[86] This happens when lenders give high-risk, high-cost subprime loans to borrowers who are eligible for low-risk, low-cost prime loans, or when lenders give subprime borrowers higher-risk, higher-cost subprime loans than they are otherwise eligible to receive.[87] For example, one way in which a lender can overprice a loan is through the use of yield-spread premiums—kickbacks from lenders to brokers for selling borrowers higher-cost loans.[88] Second, substantively predatory loans are overly risky if they create a heightened risk of foreclosure relative to other available alternatives.[89] An example of an overly risky loan term is an excessive prepayment penalty that can be used to trap a borrower in a loan with other abusive terms.[90]

Procedurally predatory loans are abusive not only because they can result in overpriced or overly risky loans, but also because they may (1) originate from fraudulent lending practices; (2) lack transparency in outlining the terms of the mortgage; or (3) waive the borrower's rights against the lender.[91] First, the most obvious form of

86. *Id.* at 736 ("An overpriced loan is priced higher than otherwise comparable loans that were available on the market to the borrower and at a greater savings than the tangible search costs that the borrower would have incurred by price shopping.").

87. *Id.*

88. *See Mortgage Lending Reform: A Comprehensive Review of the American Mortgage System: Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Servs.*, 111th Cong. 2 (2009) (testimony of Julia Gordon, Senior Counsel, Center for Responsible Lending) [hereinafter *Hearing*], *available at* http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/gordon-testimony-3-11-09-final.pdf. Yield-spread premiums theoretically allow a borrower to defer a mortgage broker's loan origination costs by spreading the fees over the life of the loan in the form of a higher annual percentage rate (APR). However, in practice, they create perverse incentives for mortgage brokers to steer borrowers into higher-cost loans in exchange for substantial payments from the lender. *Id.*; *see also* Howell E. Jackson & Laurie Burlingame, *Kickbacks or Compensation: The Case of Yield Spread Premiums*, 12 STAN. J.L. BUS. & FIN. 289, 308–12 (2007) (summarizing the various arguments in defense of and against yield spread premiums).

89. Willis, *supra* note 79, at 736 ("Overly risky loans are loans that leave the borrower in the position of such a risk of default and loss of equity in the home that the loan itself is financially unwise and would not have been taken but for exploitation of borrower vulnerabilities.").

90. *See Hearing*, *supra* note 88, at 2. Prepayment penalties are theoretically used by lenders to ensure recovery of loan origination costs if a borrower prematurely ends a loan through repayment or refinance. *See, e.g.*, Robert K. Baldwin, *Prepayment Penalties: A Survey and Suggestion*, 40 VAND. L. REV. 409, 414–19 (1987). However, in the context of the mortgage crisis, prepayment penalties that were higher or longer than justified by the loan's origination costs were used to exact harmful rents from borrowers forced to refinance out of abusive loans. Azmy, *supra* note 76, at 339–40; *Hearing*, *supra* note 88.

91. Engel & McCoy, *supra* note 76, at 1260.

predatory lending is fraudulent lending, which can take any number of forms.[92] Second, even if a loan is not fraudulent and complies with all legal requirements, it can still lack transparency by, for instance, hiding fees through "loopholes that hinder effective disclosure."[93] Finally, some loans may require borrowers to "waive meaningful legal redress" by agreeing to mandatory arbitration or waiving class-action rights.[94]

2. Federal and State Mortgage Market Regulations

Against this backdrop of prime, subprime, and predatory loans, federal and state mortgage regulations tried—and largely failed—to protect consumers from the abusive lending practices that fueled the mortgage crisis.[95] Consumer protection laws focused on home-loan origination can be broadly categorized into two groups: (1) disclosure requirements, and (2) substantive regulation of loan terms.[96]

a. Disclosure requirements

On the federal level, disclosure-requirement regulations are codified under the Truth in Lending Act (TILA)[97] and the Real Estate Settlement Procedures Act (RESPA).[98] Enacted in 1968,[99] TILA seeks "to assure [the] meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit."[100]

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92. *Id.* at 1267–68 ("The most notorious deceptions include fraudulent disclosures, failures to disclose information as required by law, bait-and-switch tactics, and loans made in collusion with home-repair scams.").

93. *Id.* at 1268–70 (noting that these exceptions include, for example, "fees for credit reports, appraisals, inspections by lenders, flood certifications, document preparation, title searches, and title insurance, as well as notary fees, recording fees, and government taxes").

94. *Id.* at 1260, 1270.

95. *See* Azmy, *supra* note 76, at 345; Fogel, *supra* note 30, at 436; Willis, *supra* note 79, at 714.

96. Cox, *supra* note 16, at 283.

97. 15 U.S.C. §§ 1601–1667f (2006).

98. 12 U.S.C. §§ 2601–2617 (2006).

99. Truth in Lending Act, Pub. L. 90-321, 82 Stat. 146 (1968) (codified as amended at 15 U.S.C. §§ 1601–1667f).

100. 15 U.S.C. § 1601(a).

TILA's primary mechanism requires that mortgage interest rates and costs be expressed as an annual percentage rate (APR) term.[101]

In 1974, Congress passed RESPA to supplement TILA.[102] RESPA aims to prevent excessive costs and unfair practices in mortgage closings.[103] RESPA's primary disclosure mechanism is the good faith estimate (GFE), which must be provided by lenders and mortgage brokers within three days of a borrower's submission of a mortgage application.[104] The GFE is intended to inform borrowers of "the nature and costs of real estate services."[105]

However, disclosure regimes like TILA and RESPA are often criticized as being ineffective because they fail to educate consumers and ignore the substantive terms of mortgage lending.[106] Moreover, as the severity of the mortgage crisis demonstrates, these disclosure regimes did not successfully regulate the mortgage market.

b. Substantive regulation of loan terms

Substantive regulation of mortgage terms occurs at both the federal and state levels.[107] At the federal level, the 1994 Home Ownership and Equity Protection Act (HOEPA)[108] was a response to predatory lending and was intended to protect vulnerable subprime borrowers through both additional disclosure requirements and substantive protections from abusive loan terms.[109] On the substantive side, HOEPA "designates a special class of nonpurchase, closed-end 'high-cost' loans and prohibits lenders originating them

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101. Jeffrey A. Payne, *Class Retreat from Mass Deceit: Assessing Class-Action Compatibility with Truth in Lending Act Rescission*, 43 LOY. L.A. L. REV. 1207, 1212 (2010); Willis, *supra* note 79, at 744.

102. *See* Real Estate Settlement Procedures Act of 1974, Pub. L. No. 93-533, 88 Stat. 1724 (1974) (codified as amended at 12 U.S.C. §§ 2601–2617 (2006)); Willis, *supra* note 79, at 744.

103. *See* Willis, *supra* note 79, at 744.

104. *See id.* at 745.

105. Peterson, *supra* note 81, at 2226. The GFE must be provided by lenders and mortgage brokers within three days of a borrower's submission of a mortgage application. 24 C.F.R. § 3500.7 (2010).

106. *See, e.g.*, Willis, *supra* note 79, at 749–54, 789–96 ("Even if all borrowers met the mildly bounded decisionmaker model envisioned by the law, price shopping for home loans would be extremely difficult in the subprime marketplace because the timing of the disclosures is late, the information given is incomplete, and borrowers lack the financial literacy needed to use the information provided.").

107. *See* Cox, *supra* note 16, at 285–86.

108. Pub. L. No. 103-325, 108 Stat. 2190 (1994) (amending 15 U.S.C. §§ 1639–1648 (2006)).

109. Willis, *supra* note 79, at 746–47.

from employing specific loan terms or practices."[110] Following the enactment of HOEPA, states also began to combat predatory lending through their own substantive restrictions on abusive loan terms.[111] These laws are commonly referred to as "mini-HOEPAs."[112] Beginning with North Carolina in 1999, nearly thirty states have enacted mini-HOEPAs.[113] Because these schemes vary greatly from state to state, their impact on restricting predatory lending is inconsistent and is best evaluated on the state level.[114]

Like the federal disclosure regimes, however, statutes regulating the substantive terms of mortgages failed to protect consumers from lending abuses. While some states' mini-HOEPAs proved effective at limiting the severity of the mortgage crisis on a local level,[115] they generally fell short. Rather, the complexity of modern mortgage products and the frequency with which the market changes[116] allows lenders to comply with HOEPA and mini-HOEPA laws while still crafting abusive predatory loans.[117]

C. Fremont Investment & Loan *Shows How the Broad Unfairness Standard Makes UDAPs an Effective Alternative Through Which to Regulate the Mortgage Market*

Fremont Investment & Loan demonstrates how the flexible UDAP unfairness standard can successfully be applied to loans that

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110. Azmy, *supra* note 76, at 352–53 ("HOEPA protections apply if a loan meets one of two high-cost loan triggers: (i) the APR exceeds by eight percent the yield on Treasury securities of comparable maturity for first-lien loans, or above ten percent for subordinate lien loans . . . ; or (ii) the total of all the loan's points and fees exceeds eight percent of the loan total or $400 (adjusted for inflation), whichever is greater."). In 2009, the Federal Reserve Board implemented new regulations strengthening HOEPA. *See* Alan H. Scheiner, *State Subprime Lending Litigation and Federal Preemption: Toward a National Standard*, 30 PACE L. REV. 253, 263–65 (2009).

111. *See* Azmy, *supra* note 76, at 364–72.

112. *See* RAPHAEL W. BOSTIC ET AL., JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., THE IMPACT OF STATE ANTI-PREDATORY LENDING LAWS: POLICY IMPLICATIONS AND INSIGHTS 1 (2008).

113. *See* Azmy, *supra* note 76, at 361–62.

114. *See* BOSTIC ET AL., *supra* note 112, at 1. *See generally* Azmy, *supra* note 76, at 361–62 (surveying and critiquing mini-HOEPAs).

115. *See, e.g.*, Azmy, *supra* note 76, at 361–62.

116. For example, subprime lending and the securitization of mortgages are relatively recent phenomena. *See, e.g.*, Sally Pittman, *ARMS, But No Legs to Stand On: "Subprime" Solutions Plague the Subprime Mortgage Crisis*, 40 TEX. TECH L. REV. 1089, 1097–98 (2008).

117. *See, e.g.*, Fogel, *supra* note 30, at 454–59.

do not violate TILA, RESPA, HOEPA, or mini-HOEPAs despite being highly abusive and predatory. Because it made aggressive use of the securities market to sell its loans, Fremont was largely insulated from exposure to borrower default.[118] Consequently, the company's lending standards changed to reflect that reality, and the company began aggressively marketing its loans to unqualified homebuyers. Some examples of the company's sales tactics included the following: "roll[ing] out special offers to people with poor credit ratings"; "target[ing] expensive housing markets, such as California, Massachusetts, and New York, because mortgages there generated larger commissions for the brokers"; and using brokers that were "lazy, uneducated, or inexperienced" to sell stated-income loans in low-income neighborhoods.[119]

These lax lending standards were used to sell loans to unqualified borrowers:

> One such borrower was Patricia Sujballi, who in May 2006 purchased a two-family home in Dorchester. Fremont gave her a subprime loan for $529,000, even though she had just moved out of a homeless shelter, was unemployed, and her husband earned around $32,000 a year. . . . Sujballi's home was foreclosed on June 15[, 2007], and on Tuesday, the mother of two received a 72-hour notice to move out. Sujballi said she faces being homeless again. [The Massachusetts Attorney General's] action against Fremont, she said, "is too late for me."[120]

Although Fremont's loans complied with disclosure regimes and federal and state statutes that substantively regulate high-cost loan terms, the trial court in *Fremont Investment & Loan* still found that

118. Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548, 551–52 & n.6 (Mass. 2008). For example, in July 2007, Fremont owned only 290 loans out of the roughly 3,000 Fremont-originated Massachusetts loans still in existence. *Id.* at 551 & n.6; *see also* Brief of Commonwealth, *supra* note 1, at 6 ("Although Fremont typically sold the vast majority of its loans to the secondary market, Fremont continued to service many of the loans it originated, that is, Fremont collected monthly payments and otherwise administered the loans."). However, Fremont continued to service, but no longer own, nearly 2,200 of these loans. *Fremont Inv. & Loan*, 897 N.E.2d at 551 & n.6.

119. Blanton, *supra* note 9.

120. Kimberly Blanton, *2,200 to Get Reprieves on Foreclosures: Facing Threat of a Suit, Subprime Lender to Let State Review Mortgages*, BOSTON GLOBE, July 12, 2007, at D1.

many of the loans were unfair under the Massachusetts UDAP.[121] Specifically, the court found that the combination of four loan characteristics made these loans destined to fail from the moment of origination:

> 1. The loan is an [adjustable-rate mortgage] with an introductory period of three years or less; 2. The loan has an introductory or teaser rate for the initial period that is at least 3 percent lower than the fully indexed rate; 3. The borrower has a debt-to-income ratio that would have exceeded 50 percent if the lender's underwriters had measured the debt, not by the debt due under the teaser rate, but by the debt due under the fully indexed rate; and 4. The loan-to-value ratio is 100 percent *or* the loan carries a substantial prepayment penalty *or* a prepayment penalty that extends beyond the introductory period.[122]

Notably, the court concluded that Massachusetts's mini-HOEPA dictated this result.[123] Although Fremont's lending practices did not violate the letter of the law, they fell "within the 'penumbra' of [the mini-HOEPA's] concept of unfairness" because the mini-HOEPA treated "a high cost mortgage loan . . . as structurally unfair . . . if the lender reasonably believed at the time the loan was issued that the borrower would be unable to make the scheduled payments."[124]

III. UDAPS FAILED TO RESTRICT THE PREDATORY LENDING THAT CAUSED THE U.S. MORTGAGE CRISIS

As demonstrated by *Fremont Investment & Loan*,[125] UDAPs protect against mortgage abuses in a way that consumer protection statutes like disclosure regimes and substantive term restrictions cannot. Unlike RESPA, TILA, HOEPA, and mini-HOEPAs, the UDAP "unfairness" standard goes beyond mere statutory compliance to evaluate the substantive terms and procedural process of a

121. Commonwealth v. Fremont Inv. & Loan, No. 07-4373-BLS1, 2008 WL 517279, at *9–16 (Mass. Super. Ct. Feb. 26, 2008).

122. *Id.* at *11.

123. *Id.* at *10–11.

124. *Id.* at *11.

125. 897 N.E.2d 548 (Mass. 2008).

mortgage practice on a flexible and more individualized basis.[126] Nonetheless, the explosion of predatory lending and the subsequent financial crisis indicate that UDAPs also failed to protect consumers from mortgage-market abuses.[127] Despite suffering injury from the unfair practices of their competitors, other businesses in the mortgage market largely lacked standing to initiate UDAP litigation.

A. Public Law Offices and Individual Consumers Were Not Sufficiently Successful as UDAP Plaintiffs to Effectively Deter Predatory Lending

When compared to the scope of lending abuses committed during the housing bubble,[128] UDAP litigation, as evidenced through available precedent, was relatively sparse.[129] Although there are some examples of the successful use of UDAPs to combat predatory lending, a survey of the available record suggests that UDAPs, as currently structured, do not effectively protect consumers. Rather, despite access to these powerful consumer protection laws, public

126. *See generally* Cox, *supra* note 16, at 283–86 (explaining how UDAPs differ from objective disclosure requirements and substantive restrictions on loan terms because the analysis is subjective); Fogel, *supra* note 30, at 454–56 (arguing that, in addition to the flexible unfairness standard, UDAPs are an important alternative to anti-predatory lending regulations because they usually provide for a private rights of action, a longer statute of limitations, and attorney's fees).

127. *See supra* Part II.B.

128. Back in 2001, when the housing bubble was in its infancy, predatory lending was estimated to cost U.S. borrowers $9.1 billion annually. *See* ERIC STEIN, CTR. FOR RESPONSIBLE LENDING, QUANTIFYING THE ECONOMIC COSTS OF PREDATORY LENDING 2 (2001), www.selegal.org/Cost%20of%20Predatory%20Lending.pdf. This was before the subprime mortgage market ballooned from less than 10 percent of new mortgage originations to nearly a quarter. *See Preserving the American Dream: Predatory Lending Practices and Home Foreclosures: Hearing Before the S. Comm. on Banking, Housing and Urban Affairs*, 110th Cong. (2007) (testimony of Martin Eakes, CEO, Ctr. for Responsible Lending), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=9e054bb1-667c-4b47-888b-bbdd795346d1; SONIA GARRISON ET AL., CTR. FOR RESPONSIBLE LENDING, CONTINUED DECAY AND SHAKY REPAIRS: THE STATE OF SUBPRIME LOANS TODAY 3 (2009), http://www.responsiblelending.org/mortgage-lending/research-analysis/continued_decay_and_shaky_repairs.pdf.

129. For example, a search of two Westlaw databases that compile California verdicts, judgments, and settlements reveals that since 2000 there are only seventy-seven such UCL dispositions on record. *See* Westlaw, Search Results, http://www.westlaw.com (search VS-CA-JV and LRPCA-JV databases for "(bus! /5 prof! /5 1720* 1721*) & da(aft 1999)") (last searched Mar. 17, 2010). Of these seventy-seven dispositions, only a single disposition references either "mortgage" or "home loan." *See* Westlaw, Search Results, http://www.westlaw.com (search VS-CA-JV and LRPCA-JV databases for "(mortgage "home loan") & (bus! /5 prof! /5 1720* 1721*) & da(aft 1999)") (last searched Mar. 17, 2010). That case, *1601 McCarthy Boulevard, LLC v. GMAC Commercial Mortgage Corp.*, No. CGC-03-425848, 2005 WL 517619 (Cal. Super. Ct. Jan. 26, 2005), involved a dispute over a commercial mortgage. *Id.* at *2.

law offices and individual plaintiffs appear to have not aggressively prosecuted UDAP litigation until the dramatic rise in foreclosures caught the nation's attention.

A few state attorneys general utilized UDAPs to combat predatory lending before the mortgage crisis hit in 2007.[130] In 1998, for example, several state attorneys general initiated UDAP litigation against First Alliance Mortgage Company (FAMCO) that ultimately led to a settlement of $525 million.[131] The abuses alleged in the FAMCO matter foreshadow the predatory lending practices that fueled the housing bubble. FAMCO was accused of originating—often without borrower knowledge—"extraordinarily high cost loans . . . , with fees regularly exceeding 20% of the principal amount," and "'teaser rate' adjustable rate mortgages that would increase at an average of more than 2%, even if rates remained stable."[132]

While, like Fremont, FAMCO ultimately filed for bankruptcy, the settlement is significant because it "could [have] serve[d] as a roadmap for the problems that lay ahead in the surging subprime mortgage market."[133] However, there appear to be only a few other examples of high-profile successful state attorney general UDAP litigation against predatory lenders.[134] The point thus remains that public law offices were not sufficiently successful at using UDAPs to deter the predatory lending that caused the mortgage crisis.

As for private-party UDAP litigation, the record indicates that while there were some individual success stories during the housing bubble, private litigants did not pursue UDAP claims against predatory lending en masse until after the mortgage crisis hit.

130. *See generally* Cox, *supra* note 16, at 293–297 (arguing that, "before the mortgage crisis became apparent," "the only public agencies that systematically attempted to attack problems in subprime mortgage lending were a few state attorneys general . . . who brought actions alleging UDAP violations").

131. *Id.* at 293–95.

132. *Id.* at 294 (citations omitted).

133. *Id.* at 294–95.

134. *See, e.g., id.* at 295–96 (discussing a 2004 to 2006 multi-state enforcement action against Ameriquest Mortgage Corporation that resulted in a $325 million settlement); Gretchen Morgenson, *Countrywide to Set Aside $8.4 Billion in Loan Aid*, N.Y. TIMES, Oct. 6 2008, at B1 (discussing a more recent multi-state enforcement action against Countrywide Financial). The Countrywide matter was initiated in 2008 by California and Illinois after the mortgage crisis had already arrived. *See California Sues Countrywide over Lending*, N.Y. TIMES, June 26, 2008, at C11. Within a few months, Countrywide settled with eleven states for $8.4 billion. Morgenson, *supra*.

California precedent offering insight into the types of predatory-lending abuses targeted by UCL claims includes *In re First Alliance Mortgage Co.*[135] and *McKell v. Washington Mutual, Inc.*[136] In *First Alliance*, mortgagors of a bankrupt mortgage company brought class-action claims against an investment bank, Lehman Brothers, Inc., alleging fraud and UCL violations for aiding and abetting the mortgage company's predatory lending practices.[137] The lender, First Alliance Mortgage Co., was accused of using deception to sell high-cost mortgages to vulnerable borrowers who had "built up substantial equity in their homes."[138] The plaintiffs ultimately prevailed on their common-law fraud claim.[139]

In *McKell*, another UCL class action, borrowers alleged that a lender's mortgage practices were unlawful, unfair, and fraudulent.[140] The borrowers accused Washington Mutual, Inc. of "overcharging plaintiffs for underwriting, tax services, and wire transfer fees in conjunction with home loans."[141] After the trial court's dismissal of the complaint on demurrer, the appellate court held that the plaintiffs had successfully stated a claim for fraudulent and unfair business practices in violation of the UCL.[142] Moreover, the plaintiffs' unlawful-conduct claim under the UCL, borrowing from the defendant's alleged violations of RESPA,[143] was not preempted.[144]

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135. 471 F.3d 977 (9th Cir. 2006).

136. 49 Cal. Rptr. 3d 227 (Ct. App. 2006).

137. *First Alliance*, 471 F.3d at 983.

138. *Id.* at 984–85 ("First Alliance originated, sold and serviced residential mortgage loans in the subprime market through a network of retail branches located throughout the country, utilizing a marketing methodology designed to target individuals who had built up substantial equity in their homes, many of whom were senior citizens. Through telemarketing efforts, First Alliance employees would set up appointments for what they described as in-house appraisals with targeted prospective borrowers. Following the appraisals, loan officers would employ a standardized sales presentation to persuade borrowers to take out loans with high interest rates and hidden high origination fees or 'points' and other 'junk' fees, of which the borrowers were largely unaware. The key to the fraud was that loan officers would point to the 'amount financed' and represent it as the 'loan amount,' disregarding other charges that increased the total amount borne by the borrowers.").

139. *Id.* at 1009–10. Despite satisfying the elements for a UCL violation, the appellate court held that the UCL claim failed because the UCL's available remedies—injunctive relief and restitution—could only be recovered from the lender, and not from Lehman Brothers on an aiding and abetting theory. *Id.*

140. *McKell*, 49 Cal. Rptr. 3d at 234.

141. *Id.*

142. *Id.* at 256.

143. *Supra* notes 58–62 and accompanying text.

Despite these success stories, relatively little UCL litigation targeted predatory lending during the housing bubble. For example, a search of California state and federal cases for UCL mortgage litigation in the eight years between the beginning of 2000 and the end of 2007 returns sixty-seven results—just over eight opinions per year on average.[145] Considering the scope of abuse and the depth of the resulting crisis, it is apparent that private litigants were unable to deter predatory-lending abuses during the housing bubble. Moreover, the limited amount of litigation was almost entirely citizen-driven—businesses did not initiate any mortgage-related UDAP litigation alleging predatory lending practices.[146]

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144. *McKell*, 49 Cal. Rptr. 3d at 236.

145. *See* Westlaw, Search Results, http://www.westlaw.com (search CA-CS-ALL database for "atleast5(mortgage) atleast5("home loan") & (bus! /5 prof! /5 1720* 1721*) & da(aft 1999 & bef 2008)") (last searched Apr. 9, 2010) (showing eighty-six results). In order to avoid irrelevant hits, the search requires that a disposition mention either "mortgage" or "home loan" at least five times. Of the eighty-six hits, nineteen do not directly involve mortgage issues. *See* In re Wells Fargo Home Mortgage Overtime Pay Litig., 527 F. Supp. 2d 1053 (N.D. Cal. 2007); In re Wells Fargo Home Mortgage Overtime Pay Litig., No. MDL 06-1770 MHP, 2007 WL 3045995 (N.D. Cal. Oct. 18, 2007); Woo v. Home Loan Group, L.P., No. 07-CV-0202-H (POR), 2007 WL 6624925 (S.D. Cal. Jul. 27, 2007); FTC v. Optin Global, Inc., No. C05-1502 SC, 2005 WL 1027108 (N.D. Cal. Apr. 13, 2005); Barnett v. Wash. Mut. Bank, FA, No. C 03-00753 CRB, 2004 WL 1753400 (N.D. Cal. Aug. 5, 2004); People v. Beaumont Inv., Ltd., 3 Cal. Rptr. 3d 429 (Ct. App. 2003); Cal. Hous. Fin. Agency v. Hanover/Cal. Mgmt. & Accounting Ctr., Inc., 56 Cal. Rptr. 3d 92 (Ct. App. 2007); Vargas v. Countrywide Home Loans, No. H030802, 2007 WL 4100158 (Cal. Ct. App. Nov. 19, 2007); Cal. Hous. Fin. Agency v. Hanover/Cal. Mgmt. and Accounting Ctr., Inc., No. G034968, 2006 WL 3096029 (Cal. Ct. App. Nov. 2, 2006); Cebular v. Cooper Arms Homeowner Ass'n, 47 Cal. Rptr. 3d 666 (Ct. App. 2006); WFS Fin., Inc. v. Superior Ct., 44 Cal. Rptr. 3d 561 (Ct. App. 2006); Oakland v. Rice, No. B176390, 2005 WL 2882831 (Cal. Ct. App. Nov. 3, 2005); Wagh v. Metris Dir., Inc., No. A103161, 2005 WL 1253940 (Cal. Ct. App. May 27, 2005); Garcia v. Mortgage Inv. Corp., No. B175195, 2005 WL 714038 (Cal. Ct. App. Mar. 30, 2005); Shaw Indus., Inc. v. Superior Ct., No. B167878, 2003 WL 22995267 (Cal. Ct. App. Dec. 22, 2003); Nat'l Notary Ass'n v. U.S. Notary, No. D038278, 2002 WL 1265555 (Cal. Ct. App. June 7, 2002); Wershba v. Apple Computer, Inc., 110 Cal. Rptr. 2d 145 (Ct. App. 2001); Wershba v. Apple Computer, Inc., 107 Cal. Rptr. 2d 220 (Ct. App. 2001); Schwartz v. Vista Intern. Corp., No. 822404-4, 2003 WL 1870370 (Cal. Super. Ct. Apr. 7, 2003).

146. *See* Westlaw, Search Results, http://www.westlaw.com (search CA-CS-ALL database for "atleast5(mortgage) atleast5("home loan") & (bus! /5 prof! /5 1720* 1721*) & da(aft 1999 & bef 2008)") (last searched Apr. 9, 2010) (showing eighty-six results). Of the eighty-six results, there are ten business-to-business dispute dispositions, none of which involve a challenge to a predatory lending practice. *See* Standfacts Credit Services, Inc. v. Experian Information Solutions, Inc., 405 F.Supp.2d 1141 (C.D. Cal. 2007); Family Home & Finance Ctr., Inc. v. Fed. Home Loan Mortgage Corp., 461 F.Supp.2d 1188 (C.D. Cal. 2006); Calyx Techs., Inc. v. Ellie Mae, Inc., No. C 04-1640 SI, 2005 WL 2036918 (N.D. Cal. 2005); Resource Lenders, Inc. v. Source Solutions, Inc., 404 F.Supp.2d 1232 (E.D. Cal. 2005); Golden West Financial v. WMA Mortgage Services, No. C 02-05727 CRB, 2003 WL 1343019 (N.D. Cal. 2003); PMI Mortgage Ins. Co. v. American Int. Specialty Lines Ins. Co., No. C-02-1774 PJH, 2002 WL 32065867 (N.D. Cal. 2002); CTX Mortgage Co. v. Rodriguez, No. G036120, 2007 WL 512755 (Cal. Ct. App. 2007); Am. Interbanc Mortgage, LLC v. E-Lenders Report Card, Inc., No D042546, 2005

After the mortgage crisis hit, there was a dramatic increase in the amount of private-party UCL mortgage litigation. The number of UCL cases quickly ballooned from roughly eight per year to well over one hundred per year between 2008 and 2010.[147] Like the timing issue at play in *Fremont Investment & Loan*, this substantial increase in UCL mortgage litigation apparently resulted from the record numbers of foreclosures and their associated individual and collective harms.[148]

In sum, this brief survey of UDAP mortgage precedent permits three general conclusions: (1) despite a unique ability to combat novel forms of predatory lending, there was not a substantial amount of UDAP litigation between 2000 and 2008; (2) public law offices and individual consumers typically act in a reactionary fashion, generally litigating only when past harms manifest themselves in a more direct way; and (3) businesses in the mortgage industry did not pursue UDAP litigation against predatory lending.

B. Businesses in the Mortgage Market Were Harmed by the Bad Practices of Their Competitors

In addition to inflicting direct harm on consumers, predatory lending imposes a significant secondary harm on honest businesses in the mortgage industry by reducing their capacity to compete. Lenders, appraisers, and mortgage brokers who did not engage in unfair or deceptive practices were placed at a competitive disadvantage in attracting market share vis-à-vis those firms that did engage in predatory lending.

WL 615838 (Cal. Ct. App. 2005); Am. Interbanc Mortgage, LLC v. Bankrate, Inc., Nos. G032166, G032344, 2004 WL 1922508 (Cal. Ct. App. 2004); CBSK Fin. Group, Inc. v. Novastar Mortgage, Inc., No. B173210, 2004 WL 2757200 (Cal. Ct. App. 2004).

147. Using the same search terms but different years, a search of UCL state and federal precedent from 2008 to 2010 returns 224 results. Westlaw, Search Results, http://www.westlaw.com (search CA-CS-ALL database for "atleast5(mortgage) atleast5("home loan") & (bus! /5 prof! /5 1720* 1721*) & da(aft 2007 & bef 2010)") (last searched Apr. 9, 2010).

148. *See* JOINT CTR. FOR HOUS. STUDIES OF HARVARD UNIV., *supra* note 18, at 19–20 (noting that four states—California, Arizona, Nevada, and Florida—accounted for "a stunning 61 percent of the growth in foreclosures nationwide.")

1. Lenders

Predatory lending by unscrupulous firms harmed other lenders by depriving them of the ability to issue fair mortgages with competitive interest rates to borrowers purchasing affordable homes at sustainable prices. Substantively unfair predatory lending through subprime and Alt-A mortgages[149] like those at issue in *Fremont* resulted in attractive but ultimately overpriced mortgages—loans that were doomed to fail.[150] By allowing consumers to borrow more,[151] predatory lenders lured borrowers away from competitor lenders that refused to match the substantively unfair terms. Such schemes ultimately led to higher interest rates, loss of borrower equity extracted through frequent refinancing, and—eventually—foreclosure.[152]

These predatory lenders also fueled the housing bubble by putting borrowers in homes that they simply could not afford.[153] While some borrowers were unable to afford a residential property at any price level, the more likely result was that otherwise creditworthy borrowers were continually lured into homes outside of their price range. By originating unsustainable and unfair loans on overvalued homes, predatory lenders like Fremont also harmed competitors who could otherwise have profited by selling fair mortgages at uninflated prices.

2. Appraisers

Another example of harm to market competitors involves appraisal inflation, an example of procedurally unfair predatory lending. A home appraiser overvaluing a property allows a borrower to borrow more and a lender to lend more, thereby allowing a mortgage broker to make a larger commission.[154] Because appraisers generally develop local expertise and operate within a limited geographic area, they are only in direct competition with a finite

149. *Supra* note 76 and accompanying text.

150. *See* Commonwealth v. Fremont Inv. & Loan, 897 N.E.2d 548, 552–54 (Mass. 2008).

151. *See id.* at 552–53.

152. *See* Azmy, *supra* note 76, at 335–37.

153. *See* Brief of Commonwealth, *supra* note 1, at 9–14.

154. *See* J. Kevin Murray, *Issues in Appraisal Regulation: A Crack in the Foundation of the Mortgage Lending Process*, 43 LOY. L.A. L. REV. 1301, 1314 (2010).

number of other appraisers.[155] This competition is enhanced by the structure of the appraisal process, which tacitly incentivizes mortgage brokers and lenders to work exclusively with appraisers that deliver desirable appraisals, regardless of accuracy.[156]

During the housing bubble, brokers and lenders funneled work to appraisers who were willing to inflate their appraisals and away from appraisers who refused to engage in this unfair conduct.[157] Again, while ultimately imposing direct harms on individual consumers who bought or borrowed against overpriced homes, there were clear secondary harms imposed on honest business actors. When true property values were later revealed, borrowers ended up underwater; when these borrowers faced foreclosure, investors ended up with insufficient collateral on the loans. Honest appraisers could have helped to prevent the bubble; instead, they lost business due to the unfair or deceptive practices of their competitors.

3. Mortgage Brokers

In the mortgage-broker sub-industry, a popular technique for profiting from unfair or deceptive trade practices has been the lowballing of both GFEs of settlement costs and TILA estimates of mortgage costs. Under this bait-and-switch scheme, mortgage brokers give borrowers RESPA-mandated GFEs and TILA-mandated disclosures containing artificially low closing costs and loan price figures soon after the borrower has applied for the home loan.[158] However, when the borrower arrives at the loan closing table, the settlement costs and loan terms are greatly inflated compared to the prior GFEs.[159] By then it is often too late for borrowers to pull out

155. *See id.* at 1315.

156. Although paid by borrowers, appraisers are selected by mortgage brokers or lenders. *Id.* at 1316. These brokers or lenders are in turn paid only when a mortgage application results in the origination of a home loan. *See id.* at 1314.

157. *See id.* at 1313. The effects of this unfair practice were magnified by the localized nature of the appraisal industry. *See id.* at 1315.

158. *See* Testimony of Patricia McCoy, Federal Reserve Board, Building Sustainable Homeownership: Responsible Lending and Informed Consumer Choice Public Meeting 155 (June 7, 2006), http://www.federalreserve.gov/events/publichearings/hoepa/2006/20060711/transcript.pdf.

159. *See id.* ("[T]he prices on subprime loans often turned out to be a moving target. A lender or broker might have the customer apply for one type of loan, price A, say a fixed rate loan; changed the loan during underwriting to an adjustable rate mortgage, price B; and then finally

because of the inflexible timeline associated with the purchase of a home or because the borrower has already committed the home's equity through a refinance.[160] Other borrowers, having already looked at the estimates to ensure that the closing costs and loan terms were reasonable, simply do not realize that the operative terms of the agreement have changed.

Bait-and-switch tactics with GFEs and TILA disclosures trick borrowers into accepting unfavorable loan terms and deprive them of the opportunity to search for mortgage brokers who present accurate estimates of costs.[161] Because brokers are often paid in the form of commissions for originated loans, brokers using bait-and-switch techniques benefit from presenting unrealistically low costs to lure borrowers away from brokers offering estimates with higher but more accurate closing costs. Again, while the borrower suffers a direct harm through fraudulent higher costs, honest brokers suffer an indirect harm from a diminished capacity to compete with other brokers who employ the lowball technique.

C. UDAPs Limit Standing for Market Competitors

Businesses did not pursue UDAP litigation against other mortgage-market actors largely because UDAPs limit or omit standing for these parties. Because the U.S. Constitution does not set forth a standing requirement for state courts,[162] state legislatures have discretion—within the limits of their state constitutions[163]—to tailor standing requirements to the policy considerations behind specific statutory causes of action.[164] Standing to sue in state court on a

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change the loan at closing to something different at price C, say an interest only mortgage. Often, the effect is bait and switch.").

160. *See* Willis, *supra* note 79, at 749–50.

161. *See id.* (citing a study that found that nearly 85 percent of borrowers end up with closing costs higher than those quoted in their GFEs).

162. *See* U.S. CONST. art. III, § 2, cl. 1; William A. Fletcher, *The "Case or Controversy" Requirement in State Court Adjudication of Federal Questions*, 78 CAL. L. REV. 263, 263–64 (1990).

163. While state courts are not bound by the Article III standing doctrine, Asarco Inc. v. Kadish, 490 U.S. 605, 617 (1989), some states have elected to impose similar constitutional constraints. *See* Helen Hershkoff, *State Courts and the "Passive Virtues": Rethinking the Judicial Function*, 114 HARV. L. REV. 1833, 1834–42, 1852–59 (2001).

164. *See, e.g.*, CAL. CIV. PROC. CODE § 367 (West 2010) (showing an example of statutory enactment of a standing provision of general applicability); *see also* Hershkoff, *supra* note 163, at 1834–42, 1852–59 ("The source of standing rules varies from state to state, as does their content."); Sullenger, *supra* note 20, at 488 ("When a statute creates a cause of action and

UDAP theory is thus dictated by two related authorities: (1) the background standing doctrine in that state's courts, whether predicated on the state's constitution or a standing statute of general applicability; and (2) any standing provisions in the state UDAP itself. Federal standing law is largely irrelevant to the UDAP-standing calculus because a UDAP plaintiff seeking a more relaxed standing provision can pursue the claim in state court.[165]

1. UDAP Business-Standing Provisions

With respect to business plaintiffs, UDAP standing provisions generally fall within one of five categories: (1) no private right of action; (2) a private right of action for persons but not businesses; (3) a private right of action for consumers, including businesses when businesses act as consumers;[166] (4) a private right of action for persons and businesses; and (5) a private right of action for persons and businesses with no injury-in-fact requirement.[167] States in the first two categories deny UDAP standing to businesses altogether.[168] States in the third and fourth categories confer businesses with UDAP standing but impose a threshold injury-in-fact requirement that significantly restricts the businesses' ability to exercise this right.[169] These restrictions reduce the deterrent effect of UDAPs by largely eliminating businesses as potential UDAP plaintiffs.[170] No

designates who may bring an action, the issue of standing is interwoven with that of subject matter jurisdiction." (quoting *Osborn v. Marr*, 127 S.W.3d 737, 740 (Tenn. 2004))).

165. *See* Catherine L. Rivard, *Federal Court Standing in Unfair Competition Law Litigation*, 24 L.A. LAW. 16, 17 (Mar. 2001). If a state UDAP claim is removed to federal court, it would have to be remanded back to state court if the plaintiff does not satisfy federal standing requirements. *Id.* at 16. Moreover, a state-court UDAP plaintiff can still pursue related federal claims despite lacking independent federal-court standing. *See* Fletcher, *supra* note 162, at 303.

166. Businesses act like individual consumers only when they buy goods and services from other businesses. *See, e.g.*, Flynn & Slater, *supra* note 15, at 84, 87–88.

167. *See generally* SHELDON & CARTER, *supra* note 20, § 2.4.5, at 89–96, § 7.2.1, at 659–60, §§ 7.5.2.1–7.5.2.3, at 673–76 (describing the different limitations imposed on businesses as potential UDAP plaintiffs); Flynn & Slater, *supra* note 15, at 87–93 (categorizing UDAP approaches to business standing on a state-by-state basis); *Toward Greater Equality*, *supra* note 15, at 1634–40 (surveying UDAP business-standing restrictions nationally, and arguing that states should extend UDAP coverage to include small businesses).

168. SHELDON & CARTER, *supra* note 20, §§ 7.2.1–7.2.3, at 659–61. States in the second category limit private-party UDAP standing to non-business individual consumers. *See Toward Greater Equality*, *supra* note 15, at 1625.

169. *See infra* Part III.C.2.c.

170. *See infra* Part IV.

state currently employs the liberal UDAP standing found in category five—representative standing.[171]

2. The Evolution of Standing Under the UCL

The story of UDAP standing in California illustrates the significance of the categorical distinctions between different UDAP business-standing provisions. Because California's constitution is silent on the issue of standing,[172] the state legislature elected to enact a standing provision of general applicability: "Every action must be prosecuted in the name of the real party in interest, except as otherwise provided by statute."[173]

a. Pre-Proposition 64 UCL standing

Prior to 2004, the California legislature made just such a statutory standing exception for the UCL.[174] Rather than require a real party in interest, the UCL provided private-party plaintiff standing for "any board, officer, person, corporation or association or by any person acting for the interests of itself, its members or the general public."[175] Generally referred to as "representative" or "private attorney general" standing, this type of relaxed standing provision allowed any party to bring a UCL claim in state court on behalf of the general public.[176] In particular, representative standing

171. *See* SHELDON & CARTER, *supra* note 20, § 7.5.2.3, at 675–76; STERN, *supra* note 31, at ch. 7-A.

172. *See* CAL. CONST. art. III, § 6.

173. CAL. CIV. PROC. CODE § 367 (West 2010).

174. *See* CAL. BUS. & PROF. CODE § 17200 et seq. (West 2004); *see also* STERN, *supra* note 31, at ch. 2-D (reviewing the various legislative amendments to the UCL from 1933 to 2004).

175. CAL. BUS. & PROF. CODE § 17535 (West 2004) (amended 2004); Fellmeth, *supra* note 23, at 1 ("[T]he [UCL] provides that any person who files is a party allowed to represent the injunctive/restitutionary interests of all who may be injured—historically or prospectively."). In 2004 the statute was amended when voters passed Proposition 64 to read, in relevant part, as follows:

> Actions . . . under this section may be prosecuted by the Attorney General or any district attorney, county counsel, city attorney, or city prosecutor in this state in the name of the people of the State of California upon their own complaint or upon the complaint of any board, officer, person, corporation or association or by any person who has suffered injury in fact and has lost money or property as a result of a violation of this chapter.

CAL. BUS. & PROF. CODE § 17535 (West 2004).

176. *See, e.g.*, STERN, *supra* note 31, at ch. 7-A. One commentator labeled the UCL's former representative-standing provision as the "nonclass class" because "literally anyone can sue and seek restitution on behalf of the public without having to meet the standards of a true class

did not require a "transactional nexus" between the plaintiff's harm and the wrongful conduct at issue.[177] Rather, a plaintiff could be a "complete stranger to the transaction."[178]

With no restrictions on standing, the pre-2004 UCL empowered business competitors to pursue UCL claims against other businesses guilty of "unlawful," "unfair," or "fraudulent" conduct.[179] For example, in *Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.*,[180] a maker of mobile phones brought suit against a mobile-phone service provider alleging that the service provider's below-cost sale of mobile phones constituted unfair competition.[181] While the opinion focused on defining the type of conduct that violates the UCL unfairness standard in the context of a competitor suit,[182] the facts illustrate how representative UCL standing facilitated business-competitor litigation. Because the parties were not doing business together, it would have been difficult for the plaintiff to show an injury-in-fact from a transactional nexus to the defendant's conduct. Instead, representative standing allowed the plaintiff to sue for injury in the form of a diminished capacity to compete.[183]

While there is some UCL business-competitor precedent,[184] the overall body of UCL law is relatively thin. This partly results from a

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action." *Id.* at ch. 7-B. Another commentator facetiously remarked that "[a]ll [§ 17200] seems to require is that the plaintiff actually be standing." Eliot G. Disner & Noah E. Jussim, *So Unfair and Foul: The Scandals Involving the Unscrupulous Application of the Private Attorney General Provision of the Unfair Competition Act Cry Out for a Sensible Solution*, 26 L.A. LAW. 42, 44 (Nov. 2003).

177. *See* STERN, *supra* note 31, at ch. 7-A. This differs from Article III standing limitations, which require that the plaintiff be injured by the defendant's violation of the law. *See generally* Brian Stern, *An Argument Against Imposing the Federal "Case or Controversy" Requirement on State Courts*, 69 N.Y.U. L. REV. 77, 80–83 (1994) (describing Article III standing requirements).

178. STERN, *supra* note 31, at ch. 7-A.

179. *See* Christopher W. Arledge, *Standing Under the Unfair Competition Law Is Unlikely to Exist for Competitors*, 50 ORANGE COUNTY LAW. 51, 51–52 (Sept. 2008); STERN, *supra* note 31, at ch. 7-A.

180. Cel-Tech Commc'ns, Inc. v. L.A. Cellular Tel. Co., 973 P.2d 527 (Cal. 1999).

181. *Id.* at 532–33.

182. *See id.* at 532–34.

183. *See, e.g.*, MAI Sys. Corp. v. UIPS, 856 F. Supp. 538, 540 (N.D. Cal. 1994) (holding that a business competitor lacked Article III federal-court standing to pursue a representative UCL claim).

184. *See, e.g.*, Sw. Marine, Inc. v. Triple A Machine Shop, Inc., 720 F. Supp. 805 (N.D. Cal. 1989) (holding that the plaintiff was entitled to equitable relief such as restitution but could not recover punitive damages); Korea Supply Co. v. Lockheed Martin Corp., 63 P.2d 937 (Cal. 2003) (concluding that disgorgement of profits is not a proper remedy in an individual action under the UCL); AICCO, Inc. v. Ins. Co. of N. Am., 45 P.3d 24 (Cal. 2001) (holding that insurance

general lack of published UDAP opinions because few UDAP matters proceed to trial.[185] However, the universe of UCL remedial options also significantly restricted representative competitor UCL claims.[186] Because UCL claims are limited to equitable relief, only the most aggrieved businesses—those suffering a significant financial loss from a competitor's unlawful conduct—were motivated to bring suit to secure injunctive relief and restitution. Financially successful businesses were not motivated to risk costly litigation by filing suit under the UCL where the potential for monetary recovery was limited to recovery of attorney's fees. The UCL therefore tempered broad representative standing with limited remedial provisions that served to disincentivize such litigation.[187]

b. Proposition 64

Long disfavored by some in the state's business community, the UCL's broad standing provision faced intense criticism after a series of scandals emerged in which plaintiffs' attorneys were accused of subverting the statute's purpose. These attorneys sued small businesses under the UCL and entered into cash settlements for personal gain; they neither enjoined the alleged unlawful, unfair, or fraudulent practices nor made any serious attempts to compensate injured consumers or entities.[188] The uproar caused by these scandals provided UCL opponents with an opportunity to limit the scope of the law by eliminating the representative standing provision.[189]

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companies had standing to sue industry competitors for violation of the UCL and were not required to allege anti-competitive conduct); Saunders v. Superior Ct., 33 Cal. Rptr. 2d 438 (Cal. Ct. App. 1994) (overturning the superior court's dismissal on demurrer of a certified shorthand reporter's suit against industry competitors alleging unfair business practices); Allied Grape Growers v. Bronco Wine Co., 249 Cal. Rptr. 872 (Cal. Ct. App. 1988) (holding that a grape crusher's practices toward a cooperative of grape growers violated the UCL).

185. *See* SHELDON & CARTER, *supra* note 20, § 3.4.3.1, at 134; *see also supra* Part III.A (surveying UCL mortgage precedent).

186. *See* Arkin, *supra* note 44, at 164–65.

187. *See id.*

188. *See, e.g.*, Disner & Jussim, *supra* note 176, at 42–44 (describing the fallout from the California Attorney General's 2004 investigations into two law firms for ethical violations associated with "egregious and excessive enforcement" the UCL). *But see* Jacquetta Lannan, Comment, *Saving 17200: An Analysis of Proposition 64*, 46 SANTA CLARA L. REV. 451, 460–61 (2006) (arguing that, despite these examples of UCL facilitated ethics violations, "[t]he lawyers in those cases filed actions that theoretically were legally sound").

189. *See id.* at 468 ("The tort reformers began a powerful campaign, backed in part by small businesses. The largest contributors to the campaign, however, were large corporations who had

On November 2, 2004, California voters passed Proposition 64.[190] The proposition amended the UCL's standing provision by requiring that private-party plaintiffs "ha[ve] suffered [an] injury in fact and . . . lost money or property as a result of [the] unfair competition."[191] Among its eight "Findings and Declarations of Purpose," the Proposition stated that "[i]t is the intent of the California voters in enacting this Act that only the California Attorney General and local public officials be authorized to file and prosecute actions on behalf of the general public."[192]

c. Post-Proposition 64 UCL standing

Proposition 64 took immediate effect, eliminating representative standing in UCL cases pending in both trial and appellate courts.[193] Although the arguments advanced in favor of the initiative were generally inapplicable to UCL business plaintiffs,[194] the reform had a significant impact on business-to-business UCL litigation.[195] Under the post-Proposition 64 UCL standing provision, a business plaintiff in California must demonstrate that as a result of the defendant's

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previously been sued under the UCL. The money was poured into a televised campaign that bombarded voters with stories of small business owners being bullied by unethical and unscrupulous lawyers.").

190. Californians for Disability Rights v. Mervyn's LLC, 138 P.3d 207 (Cal. 2006). California Proposition 64 is now codified in scattered sections of CAL. BUS. & PROF. CODE § 17000 et seq. (West 2008).

191. *See* CAL. BUS. & PROF. CODE § 17204; STERN, *supra* note 31, at ch. 2-D. Proposition 64 made other changes to the UCL scheme including, for example, a requirement that civil penalties recovered by public law offices be used exclusively to further the enforcement of California consumer protection laws. STERN, *supra* note 31, at ch. 2-D.

192. CAL. SEC'Y OF STATE, *supra* note 191, at 109. Other declarations included statements that the UCL was "being misused by some private attorneys" to file "frivolous lawsuits—as a means of generating attorneys' fees without creating a corresponding public benefit," and "without any accountability to the public [or] adequate court supervision," and that "[f]rivolous [UCL] lawsuits clog our courts and cost taxpayers . . . California jobs and economic prosperity." *Id.* At the time, one commentator remarked that Proposition 64 was "an over-fix consisting of a very bad public policy that will soon cause its own harm." Lannan, *supra* note 188, at 470 (alterations omitted).

193. *See* Californians for Disability Rights v. Mervyn's LLC, 138 P.3d 207, 212–13 (Cal. 2006); *see also* Benjamin M. Weiss & Michael A. Geibelson, *Life After 64: Two Cases Under Review by the California Supreme Court Will Determine the Contours of Future Litigation Under the UCL*, 31 L.A. LAW 39, 40–44 (Sept. 2008) (discussing other issues left unresolved by Proposition 64's amendments, including whether causation is now required and how substantial a plaintiff's injury must be).

194. *See infra* Part IV.B.3.

195. *See* Arledge, *supra* note 179, at 55.

unfair competition it suffered an injury-in-fact in the form of lost money or property.[196] A business will usually only be able to satisfy this standing requirement when there is a transactional nexus with another business from the buying or selling of goods or services.[197] Businesses seeking to sue competitors based on a diminished capacity to compete are now denied standing under Proposition 64's amendments.[198]

In the context of the mortgage market, however, it is at least plausible that a business could have post-Proposition 64 UCL standing in a suit against a competitor, even in the absence of a clear transactional nexus.[199] For example, if a plaintiff lender alleged that another lender used unlawful or unfair practices to cause a borrower to refinance one of the plaintiff lender's mortgages, the plaintiff lender may be able to show an injury-in-fact—a loss of money—and causation. Nonetheless, it is still safe to say that the post-Proposition 64 UCL generally prohibits business-competitor litigation.

California is hardly alone in precluding businesses from pursuing UCL claims against competitors whose unlawful, unfair, or fraudulent conduct harms both the business and the consuming public.[200] Most states provide businesses with UDAP standing only when they can show an injury-in-fact.[201] The remaining states do not treat businesses as potential UDAP plaintiffs at all.[202]

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196. *Id.* at 54–55 (arguing that Proposition 64 imposes a standing requirement on UCL claims that is more burdensome than Article III standing).

197. Arledge, *supra* note 179.

198. *See id.* at 55 ("The typical UCL action between competitors involves one competitor suing the other for allegedly engaging in unlawful, unfair, or fraudulent business activities, and the plaintiff often alleges that it has lost business opportunities or profits as a result. Under the old version of the UCL, such a plaintiff would probably not be able to seek restitution of the allegedly lost profits . . . , such a plaintiff rarely will have had possession of or an ownership interest in the lost profits sufficient to give rise to restitution—but the plaintiff would be able to seek injunctive relief against the competitor. But after Proposition 64, even injunctive relief may be precluded."). *But see* Sybersound Records, Inc. v. UAV Corp., 517 F.3d 1137, 1151–53 (9th Cir. 2008) (rejecting a UCL claim between business competitors on grounds unrelated to standing).

199. Of course, mortgage-market businesses continue to have UCL standing where there is a clear transactional nexus with the defendant's conduct. *See, e.g.*, CTX Mortgage Co v. Rodriguez, No. G036120, 2007 WL 512755, at *1 (Cal. Ct. App. Feb. 20, 2007) (adjudicating a mortgage lender's allegations of "a massive loan fraud land-flipping scheme" on statute of limitations grounds).

200. *See* Arledge, *supra* note 179, at 55.

201. Flynn & Slater, *supra* note 15, at 87–93; *Toward Greater Equality*, *supra* note 15, at 1634–36. However, unlike California, several of these states further limit UDAP standing by

IV. STATES SHOULD PROVIDE REPRESENTATIVE UDAP STANDING FOR MARKET COMPETITORS

By now, it should be apparent that state UDAP business-standing provisions are inconsistent and routinely fluctuate due to legislative amendments or judicial reinterpretation.[203] Under the current UDAP business-standing approach, however, businesses were legally ill-equipped to deter the unlawful, unfair, and fraudulent predatory lending that permeated the home loan industry. Because business competitors would make effective use of these strong and flexible statutory devices to deter and combat abusive business practices, they should be granted representative UDAP standing, an amendment that would also benefit consumers by furthering the public policy interests that underlie UDAPs.

A. State UDAP Statutes Should Be Amended to Provide Broad Standing for Market Competitors

Whether through UDAP amendment or the enactment of a distinct statutory scheme,[204] states should provide the necessary legal

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requiring a business to demonstrate a significant public interest in the litigation. *See* SHELDON & CARTER, *supra* note 20, § 7.5.3, at 682–93.

202. *See, e.g.*, Flynn & Slater, *supra* note 15, at 87–93.

203. *See generally* Arledge, *supra* note 179 (discussing the effect of Proposition 64 on California's UCL); Edward X. Clinton, Jr., *Business Standing Under the Illinois Consumer Fraud Act: An Attempt to Resolve the Confusion*, 17 N. ILL. U. L. REV. 71 (1996) (examining conflicting judicial standards under the Illinois Consumer Fraud and Deceptive Business Practices Act); Cox, *supra* note 38 (critiquing the private right of action under Minnesota consumer protection law following an important judicial decision); Flynn & Slater, *supra* note 15, at 87–93 (analyzing the ability of one business to sue another under state UDAP statutes); Sullenger, *supra* note 20 (arguing for business standing under the Tennessee Consumer Protection Act); Charlotte E. Thomas, *The Quicksand of Private Actions Under the Pennsylvania Unfair Trade Practices Act: Strict Liability, Treble Damages, and Six Years to Sue*, 102 DICK. L. REV. 1 (1997) (arguing that Pennsylvania courts have employed too liberal of an interpretation of that state's Unfair Trade Practices and Consumer Protection Law); *Toward Greater Equality*, *supra* note 15 (surveying state approaches to UDAP business standing).

204. A primary obstacle to this proposal is the legislative challenge associated with revising UDAPs on a state-by-state basis. Some states have standing restrictions that would first require constitutional amendment in order to permit UDAP standing reform. *See* Hershkoff, *supra* note 163, at 1852–59. Other state legislatures are free to tailor their UDAP standing restrictions as they see fit. *See id.* In California, legislative reform of a voter-approved ballot proposition must be consistent with the enacted proposition's language. *See* CAL. CONST. art. 2, § 10(c). If UCL reform cannot be drafted in a manner authorized by Proposition 64, another voter-approved measure would be necessary. *See, e.g.*, Franchise Tax Board v. Cory, 145 Cal. Rptr. 819, 822 (Ct. App. 1978); J. E. Macy, Annotation, *Power of Legislative Body to Amend, Repeal, or Abrogate Initiative or Referendum Measure, or to Enact Measure Defeated on Referendum*, 33 A.L.R.2d 1118 (2009); 42 AM. JUR. 2D *Initiative and Referendum* § 52 (2009). While this would be a

tools to empower market competitors to enjoin and deter unfair business practices. This Article proposes the following four reforms: (1) business competitors should have representative UDAP standing; (2) representative standing should be tethered to a public-interest requirement; (3) UDAP remedial provisions should be expanded for business plaintiffs; and (4) settlements of competitor UDAP claims should be public and require judicial approval.

1. Representative Market-Competitor UDAP Standing

As a first step, state UDAPs should provide standing for businesses.[205] Because businesses generally only suffer a conjectural injury in the form of a diminished capacity to compete, most businesses lack a transactional nexus with the wrongful conduct of their business competitors.[206] As such, businesses usually lack standing to pursue UDAP claims against other businesses.[207] This lack of standing unnecessarily handicaps a business's ability to influence conduct in its marketplace through UDAP litigation.[208] Therefore, if businesses are to enhance the deterrent effect of UDAPs as additional potential plaintiffs, UDAP standing for businesses must be representative in form—omitting the traditional injury-in-fact requirement.[209]

Representative UDAP standing for businesses would enable market competitors to use UDAPs to efficiently and effectively

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daunting task, the California legislature could initiate the process by placing the proposal on the ballot. *See* CAL. CONST. art. 2, § 10.

205. *See supra* Part III.C.1.

206. *See supra* Part III.C.2.c.

207. *See supra* Part III.C.2.c.

208. *See infra* Part IV.B.

209. *See generally infra* Part IV.C.1; William B. Rubenstein, *On What a "Private Attorney General" Is—And Why It Matters*, 57 VAND. L. REV. 2129 (2004) (discussing the legal concept and various applications of representative standing). Presumably, the collective rationale behind this proposal is also applicable to industry trade associations if such groups are viewed as a collection of individual competitors. Because they also generally lack standing under the injury-in-fact standard, *see* Standfacts Credit Servs. v. Experian Info. Solutions, Inc., Nos. SA CV 04-0358 DOC (PKWx), SA CV 04-1055 DOC (PJWx), 2006 WL 4941834, at *2 (C.D. Cal. 2006) (dismissing a trade association's post-Proposition 64 UCL claim for lack of standing), trade associations represent an additional group that merits evaluation for the provision of representative UDAP standing. In the context of the mortgage market, for example, trade associations representing appraisers or mortgage brokers may have been more valuable as potential UDAP plaintiffs than individual businesses because the fragmented nature of those two sub-industries makes effective business-to-business litigation more problematic.

police their own marketplaces.[210] Nonetheless, representative UDAP standing for market competitors should supplement, not replace, traditional standing requirements. Rather, businesses should be able to plead either injury-in-fact standing through a showing of a transactional nexus, or representative standing through a showing of a market-competition nexus. Requiring representative business plaintiffs to demonstrate that they are in actual competition with a defendant would ensure that these business plaintiffs have a tangible interest in the outcome of the litigation, which in turn would help prevent the type of attorney's fees–driven litigation that led to the passage of Proposition 64.[211]

2. A Public-Interest Requirement

To promote the consumer-protection purpose underlying UDAPs and prevent businesses from abusing broad standing provisions, UDAPs should require prospective market-competitor plaintiffs to identify a public interest that their UDAP litigation would advance.[212] Under this scheme, business plaintiffs could gain either traditional UDAP standing (by alleging an injury-in-fact) or representative standing (by demonstrating a public interest in the outcome of the litigation).

A public-interest requirement could be instrumental in preventing businesses from abusing a liberal standing provision to harm competitors. In the business-to-business litigation context, a business can use litigation in many unscrupulous ways. For example, a larger competitor could try to drive a smaller competitor out of business with oppressive litigation costs. A business could also utilize litigation to try to acquire a competitor's trade secrets through discovery disclosures. Although a public-interest requirement would

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210. *See* Flynn & Slater, *supra* note 15, at 97; *see also infra* Part IV.C.1 (discussing some of the potential strengths of businesses as UDAP plaintiffs).

211. *See supra* Part III.C.2.b. To precisely define a "market competitor," legislatures may find themselves evaluating the substantiality of competitive business relationships in countless contexts and confronting difficult definitional questions (for example, whether the parties need to be providing the same good or service, or whether they need only be in the same industry). As a result, state legislatures may be better off articulating a balancing test—the potential benefits of business-to-business UDAP litigation against the potential for abuse when the competitive relationship is distant or de minimis—to guide the judiciary in building a workable definition through case law.

212. *See generally* SHELDON & CARTER, *supra* note 20, § 7.5.3, at 682–93 (reviewing the various approaches to UDAP public-interest requirements).

not completely eliminate the possibility of abuse, it would make UDAP litigation more likely to benefit the broader community while limiting its potential as a competitive tool for businesses.

Like the remedial limitations imposed by California's pre-Proposition 64 UCL,[213] a public-interest requirement would moderate the potential costs of a broad business-standing provision. Some jurisdictions already require businesses to demonstrate the promotion of a public interest to obtain UDAP private-party standing;[214] however, these jurisdictions impose this requirement in addition to the threshold injury-in-fact standing requirement, not in its place. This Article suggests that it is more appropriate to require a business competitor to demonstrate an injury-in-fact for traditional standing in ordinary business disputes and a public interest where a business seeks to utilize representative standing.

However, courts must strike the right balance between gate-keeping and facilitating self-regulatory UDAP competitor litigation. Rather than enforcing standing requirements rigidly, courts should approach the question of standing with flexibility and a broad view of the substantive merits, purpose, and potential effects of the litigation.[215] For example, a court could look to a variety of factors to determine whether the requirement is satisfied: (1) the number of consumers impacted by the abusive practice; (2) the magnitude of the defendant's interaction with the public; (3) the sophistication and bargaining power of the parties involved; (4) the harm, or lack thereof, that the practice has caused in the past; (5) the likelihood that the practice will recur; (6) the isolated or systematic character of the practice; (7) the practice's violation of or compliance with statutes promoting the public interest; and (8) the practice's relation to a consumer transaction or a private dispute.[216]

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213. *See supra* III.C.2.a.

214. *See, e.g.*, Ly v. Nystrom, 615 N.W.2d 302, 312–14 (Minn. 2000) (imposing a public-interest requirement on all private-party plaintiffs under Minnesota's UDAP); Hall v. Walter, 969 P.2d 224, 234–36 (Colo. 1998) (finding that businesses have standing under Colorado's UDAP only if they can show a significant public interest). As of 2004, eight states imposed a public-interest requirement. SHELDON & CARTER, *supra* note 20, § 7.5.3, at 682–93.

215. For example, Washington and Minnesota impose a burdensome public-interest requirement that is difficult to satisfy. *See* SHELDON & CARTER, *supra* note 20, §§ 7.5.3.2–7.5.3.3, at 685–88; Cox, *supra* note 38, at 163.

216. *See* SHELDON & CARTER, *supra* note 20, § 7.5.3, at 682–93.

3. Remedies That Deter Unfair Business Practices

UDAP remedies available in competitor cases should deter abusive business practices and incentivize self-regulatory UDAP competitor litigation. Like standing provisions, remedies should take into account the difference between the two types of potential competitor plaintiffs: (1) businesses that have suffered an injury-in-fact; and (2) those that have suffered a conjectural injury from a diminished capacity to compete.

Presumably businesses that have suffered an injury-in-fact from a competitor's wrongful conduct are primarily motivated to litigate to enjoin the competitor's unfair practices. The potential recovery of damages and attorney's fees would remain as secondary considerations. Because such businesses have suffered an injury-in-fact, a provision for bare compensatory damages would sufficiently motivate and compensate these types of plaintiffs. If more remedial flexibility is sought, jurisdictions could increase potential compensation by making multiple or punitive damages available where a defendant's conduct is particularly egregious or intentional.[217]

By contrast, businesses that have been injured in the form of a diminished capacity to compete in their marketplaces have different motivations to litigate. Because these plaintiffs have not suffered a legally recognized injury such that they are entitled to sue for compensatory damages, their potential recovery is limited to injunctive relief and attorney's fees. While enjoining a defendant's wrongful conduct and potentially recovering for attorney's fees are desirable remedies, the risk of loss from the costs of litigation—coupled with the lack of a tangible impact on the company's bottom line—would likely be sufficient to discourage such self-regulatory UDAP litigation.

To limit these risks, it thus becomes necessary to pair representative market-competitor UDAP standing with the potential for a monetary recovery. Enhanced remedial provisions would strengthen UDAPs by (1) reinforcing the overall deterrent effect of

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217. Multiple or treble damage provisions permit or require a court to multiply an "actual damage award, under specified conditions, . . . usually by three." They are available under "[a]bout half of all UDAP statutes." SHELDON & CARTER, *supra* note 20, § 8.4.2, at 756–69. Punitive damages are available to remedy UDAP violations in at least twelve states. *Id.* § 8.4.3.1, at 769–70.

the statutes, and (2) better incentivizing industry self-regulation through UDAP litigation. Provisions for multiple or punitive damages would be the best way to accomplish this result. However, these statutory damage multipliers cannot exist in isolation; instead, they must be tied to an existing monetary award. Because representative market-competitor plaintiffs lack injuries meriting compensatory damages by definition, another mechanism must provide a baseline award upon which to build multiple or punitive damages.

One way to create such a baseline monetary award is by creating a statutory minimum-damages provision.[218] Such a provision could award a successful UDAP plaintiff either a fixed amount or an amount within a specified range. However, the fixed damages option is problematic in the context of UDAP litigation because potential UDAP business plaintiffs and defendants range from small businesses to the largest corporations. Fixed statutory minimum damages would have to be set at a level that would be largely ineffective at motivating or deterring large-business defendants so as not to overburden small-business defendants.

This problem could be solved by awarding statutory minimum damages as a percentage instead of a dollar amount.[219] A fixed percentage approach would tailor a UDAP's statutory minimum damages to the size of the business by awarding a successful plaintiff a proportion of the defendant's annual revenue rather than a fixed amount or range. A more precise—and perhaps more appropriate—approach would provide for a percentage recovery from the revenue of the specific product or service line in which the abusive activity has occurred rather than tying an award to the company's overall revenue.

Under this scheme, traditional business UDAP plaintiffs with an injury-in-fact could secure injunctive relief, attorney's fees, and

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218. Minimum-damages provisions require a court to award a specified amount to a successful plaintiff regardless of proof of actual damage. *Id.* at 754. They are designed to "encourage private litigation" by increasing the incentive for plaintiffs to sue when their actual damages are minor and by eliminating the need to prove actual damages. *Id.* at 754–55. Approximately half of the states provide statutory minimum damages, which range from $25 to $5,000 per violation, to private plaintiffs who prove a UDAP injury. *Id.* at 754.

219. *See* Payne, *supra* note 101, at 1216 & nn.35–37 (discussing how damages for violating TILA are capped at 1 percent of a defendant's net worth so as to balance the interests of small and large businesses).

compensatory damages. If a defendant's conduct is particularly egregious, a court could also award multiple or punitive damages. In contrast, representative business UDAP plaintiffs could recover injunctive relief, attorney's fees, and a statutory minimum damages award tied to the defendant's revenue. If a defendant's conduct is sufficiently egregious or intentional, multiple or punitive damages awards would be available to enhance the statutory minimum damages, thereby increasing the UDAP's deterrent effect while creating an incentive for business competitors to act as litigant-regulators.

4. Public Settlements

The potential for UDAP abuse by representative business plaintiffs could also be limited by requiring that any settlement of business-to-business UDAP litigation be both public in nature and judicially approved.[220] First, requiring judicial approval and public knowledge of settlements in UDAP suits would help to ensure that litigation actually benefits the public.[221] Like the attorneys who allegedly abused California's UCL to extort attorney's fees from small businesses, representative business UDAP plaintiffs could secure a financial windfall from a settlement with a competitor without enjoining the defendant's harmful practices to create a public benefit.[222] Requiring judicially sanctioned settlements would ensure that injunctive relief is issued to promote the public interest.[223] Representative competitor UDAP standing could thus curb bad business practices rather than serving as a vehicle for litigation abuse.

220. *See* Christopher R. Drahozal & Laura J. Hines, *Secret Settlement Restrictions and Unintended Consequences*, 54 U. KAN. L. REV. 1457 (2006) (discussing the pros and cons of secret settlement restrictions, including their effectiveness and their economic impact). While jurisdictional approaches vary, public-settlement provisions generally seek to prevent secret settlements by voiding confidentiality clauses in settlement contracts. *Id.* at 1458–59, 1476. Efforts to prohibit secrecy in litigation gained traction in the 1980s and 1990s after secret settlements of individual mass-tort claims prevented others from learning of the potential for harm or the existence of a claim. *Id.* at 1457–58 (discussing recent examples including the Firestone/Bridgestone tires matter that contributed to at least 148 deaths, and widespread allegations against the Catholic Church of sexual abuse by priests).

221. *See* Blanca Fromm, Comment, *Bringing Settlement out of the Shadows: Information About Settlement in an Age of Confidentiality*, 48 UCLA L. REV. 663, 664–66, 701–07 (2001).

222. *See* Lannan, *supra* note 188, at 476–77 (arguing that Proposition 64 would have been unnecessary if the UCL had required judicial approval of settlements).

223. Disner & Jussim, *supra* note 176, at 44.

Second, a public-settlement requirement in business-to-business UDAP litigation would prevent duplicative litigation against the same defendant. A primary criticism of California's pre-Proposition 64 UCL was that different representative litigants could pursue duplicative UCL actions, burdening defendants with multiple claims stemming from the same conduct.[224] Judicially sanctioned public settlements would prevent this inequitable result in representative-standing cases at least in part by creating a res judicata effect to protect defendants from duplicative lawsuits.[225]

Criticism of public-settlement provisions as ineffective and counterproductive generally presumes that both plaintiffs and defendants share a financial interest in secret settlements.[226] In the context of representative business-to-business UDAP litigation, however, it is less likely that a plaintiff and a defendant would share this motivation. While a business plaintiff is motivated to maximize its financial windfall and a business defendant is motivated to limit its loss, a business plaintiff would also benefit in a more tangible way than an individual plaintiff from the injunctive relief and harmful publicity that could result from the judicial enforcement of a public settlement.

B. Public Policy Supports the Provision of Representative UDAP Standing for Market Competitors

Conferring representative UDAP standing upon business competitors would advance substantial public policy interests, namely promoting industry self-regulation and discouraging a "race to the bottom." Moreover, policy-based criticisms of general

224. *See id.* at 42–44; Lannan, *supra* note 188, at 462–63; *see also* SHELDON & CARTER, *supra* note 20, § 7.2.1, at 659–60, § 7.7.8, at 719 (describing how duplicative UDAP claims can be brought by both a private litigant and a public law office).

225. *See* FELLMETH, *supra* note 23, at 1–2 & nn.4–6. Other potential advantages of public settlements in the context of representative business UDAP standing could include: (1) preventing sellout settlements, whereby the plaintiff business elects to join the defendant business in the bad activity; and (2) providing a greater opportunity for the media to publicize the settlement and educate consumers about the specific practice at issue. *See infra* Part IV.B.2

226. *See* Drahozal & Hines, *supra* note 220, at 1459 (arguing that plaintiffs generally have a significant financial interest in secret settlements because a defendant is incentivized to pay more to an individual plaintiff, for example, in order to prevent other potential plaintiffs from discovering the past conduct); *cf.* Richard A. Zitrin, *The Laudable South Carolina Court Rules Must Be Broadened*, 55 S.C. L. REV. 883, 884–94 (2004). *But see* Scott A. Moss, *Illuminating Secrecy: A New Economic Analysis of Confidential Settlements*, 105 MICH. L. REV. 867, 909–12 (2007).

representative UDAP standing do not apply with equal force to business-competitor litigation.

1. Empowering Industry Self-Regulation

From a broad policy perspective, it makes little sense to authorize government and consumer UDAP litigation without also providing business competitors with the legal tools to facilitate self-regulation.[227] Part of the original purpose of the UDAP private right of action was to supplement the ineffectiveness and limited resources of the government by expanding the pool of potential unfair business practice regulators beyond the FTC to state public law offices and private-party litigants.[228] The provision of representative standing for businesses is thus consistent with this general goal of enhancing the overall effectiveness of consumer protection laws.[229] Including businesses in the pool of potential UDAP plaintiffs benefits both the consuming public and the plaintiff-competitor by increasing the number of UDAP enforcers, thereby enhancing the deterrent effect of the statute.[230]

Moreover, the provision of representative UDAP standing for market competitors fits with the basic socioeconomic principle that government should only regulate where the industry at issue has first failed to satisfactorily self-regulate.[231] UDAPs currently provide state public law offices and individual consumers with plenary authority to redress unfair business activity,[232] but deny industry actors an opportunity to police their own marketplaces.[233] Not only is this contrary to common sense, but it also ignores the benefits of reducing strain on public law offices by partially reallocating the

227. *See* Flynn & Slater, *supra* note 15, at 97; *Toward Greater Equality*, *supra* note 15, at 1640.

228. Fogel, *supra* note 30, at 455–56.

229. *See supra* notes 31–40 and accompanying text.

230. Notably, this proposal also reconnects UDAPs with the common-law trademark claims that provided the original framework for FTC and UDAP jurisprudence. *See* Howard, *supra* note 31, at 706–13. Ironically, these historical common-law claims only permitted litigation between competitors and did not recognize standing for government or consumer claimants. *See* STERN, *supra* note 31, at ch. 2-A.

231. *See* PRIDGEN, *supra* note 51, § 6.2 ("[T]he private right of action [is] a marketplace solution to a marketplace problem.").

232. *See* SHELDON & CARTER, *supra* note 20, § 1.1, at 1.

233. *See supra* Part III.C.

burden of UDAP enforcement to better incorporate private actors.[234] Rather than handicapping businesses as potential UDAP plaintiffs, the law should empower businesses to take more responsibility in protecting both consumers and the integrity of their respective industries.

2. Avoiding a Race to the Bottom

If businesses are not provided with the legal tools necessary to combat unfair or unlawful conduct, market forces compel them to keep pace with bad industry actors.[235] For example, a business that is unable to initiate UDAP litigation against a competitor's unfair business activity risks going out of business if it fails to adjust its own business practices to incorporate the profitable wrongful conduct.[236] Conversely, if market competitors are provided with broad standing to combat wrongful conduct but fail to effectively use these legal tools, society is more justified in holding an entire industry accountable for the actions of individual entities.

There is at least some evidence that a race to the bottom among mortgage businesses contributed to the growth of predatory lending. In the context of the securitization market, competition from industry actors helped drive Fannie Mae and Freddie Mac into the subprime market.[237]

> Fannie and Freddie did eventually relax their standards and get into the nonprime market, but they were motivated to do so by the need to preserve market share.
>
> Fannie and Freddie began entering the nonprime market in 2005, after losing almost half of their market share to private issuers of mortgage-backed securities. Their decision to enter this market was a response to competitive pressures from the investment banks . . . .[238]

234. *See, e.g.*, PRIDGEN, *supra* note 51, § 6.2.

235. FELLMETH, *supra* note 23, at 15–17.

236. *See id.*

237. BAKER, *supra* note 16, at 29–30 ("Fannie Mae and Freddie Mac are government-created companies established to promote a secondary mortgage market by buying mortgages from the banks who issued them. Both were largely run as private companies prior to the crisis, and continue[] to fill this public purpose . . . .").

238. *Id.*

Fannie Mae and Freddie Mac's unwise decision to enter the subprime market is only one example of the competitive race to the bottom that drove increasingly risky and more abusive business practices during the housing bubble. Rather than having their hands tied by their lack of UDAP standing, businesses should be challenged to maintain lawful, fair, and competitive marketplaces.

3. Policy Arguments Advanced Against Representative UDAP Standing Do Not Readily Apply to Market Competitors

Finally, the arguments in favor of the Proposition-64 UCL reforms are not readily applicable to imposing standing restrictions on businesses. Proposition 64 advocates argued that representative standing led to "shake down" lawsuits without corresponding public benefits.[239] In such lawsuits, plaintiffs' attorneys were accused of bringing meritless UDAP claims against small businesses solely to extort settlement dollars.[240]

However, providing limited representative standing for market competitors would not permit such manipulation of the system if market-competitor plaintiffs were required to have a nexus with the defendant's wrongful conduct as a competitor in the same industry.[241] A nexus also creates a stronger connection between market-competitor suits and a corresponding public benefit[242]—a connection that is furthered by requiring that a representative standing business plaintiff demonstrate a public interest in the outcome of the litigation.[243]

239. Cal. Legis. Serv. Prop. 64 (2004); *see also* Disner & Jussim, *supra* note 176, at 43–45 ("The profiteering by some lawyers using Section 17200 to file actions that were needless and redundant because public enforcement agencies have already acted has highlighted other ethical problems surrounding the Unfair Competition Act.").

240. Disner & Jussim, *supra* note 176, at 42.

241. A plaintiff that is a true business competitor—not just a plaintiffs' attorney—is invested in gaining more than attorney's fees. *See id.* at 42–46.

242. Businesses presumably want to enjoin the wrongful conduct and not just recover damages and attorney's fees. Coupling this desire for injunctive relief with the deterrent effect of damages awards would further restrict unfair conduct, creating an even greater public benefit.

243. *See* Hall v. Walter, 969 P.2d 224, 234–37 (Colo. 1998); SHELDON & CARTER, *supra* note 20, §§ 8.5–8.6, at 782–90.

C. Market-Competitor UDAP Standing Could Have Made a Difference

In addition to the aforementioned policy considerations, there are practical benefits to market competitors functioning as UDAP plaintiffs. These advantages place businesses in a strong position to show a court how a novel or established business practice violates a UDAP's unfairness standard. When balancing the competing interests involved in this proposed expansion of UDAP standing, the benefits outweigh the more limited potential costs of this reform.

1. Benefits of Representative Competitor Standing

UDAP schemes are less effective when market competitors are denied representative standing because market competitors are ideally positioned to promote fair business practices through UDAP litigation. Compared to other potential plaintiffs with UDAP standing—namely public law offices and individual consumers—businesses have: (a) more marketplace expertise; (b) greater permanence as industry stakeholders; and (c) more substantial financial resources.

a. Marketplace expertise

Market competitors should have broad standing to pursue UDAP claims against unscrupulous businesses because they have the knowledge to identify—and advocate against—unfair business practices. Unlike government attorneys and private plaintiffs, market competitors are true experts in their respective industries and should know what constitutes fair business activity in the marketplace. Businesses are also better equipped to discover unfair competition because they are industry insiders.[244] Individual consumers, on the

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244. Collectively referred to as "competitive intelligence," many small and large businesses actively engage in gathering and analyzing intelligence information about their competitors' products and customers. *See* Linda K. Stevens, *Trade Secrets and Inevitable Disclosure*, 36 TORT & INS. L.J. 917, 940 (2001); Neil King Jr. & Jess Bravin, *Call It Mission Impossible Inc.—Corporate-Spying Firms Thrive*, WALL ST. J., July 3, 2000, at B1. Distinguishable from illegal intelligence gathering or industrial espionage, competitive intelligence involves acquiring information through legal means. Robert C. Van Arnam, Comment, *Business War: Economic Espionage in the United States and the European Union and the Need for Greater Trade Secret Protection*, 27 N.C. J. INT'L L. & COM. REG. 95, 133 & n.262 (2001) (citation omitted); Paulette Thomas, *Breakaway (A Special Report): The Entreprenurial Life—Intelligent Intelligence: Information on Rivals, Suppliers and Clients Can Keep a Business Alive; But Knowing What to Look for and How to Look Is Vital*, WALL ST. J., Dec. 7, 1998, at 29.

other hand, usually learn about an unfair business practice only after they realize that they have been injured, and, even then, their knowledge is limited to their own experiences. Public law offices are similarly constrained because their own channels for the discovery of bad business practices are often limited to individual consumer complaints.[245]

Moreover, market competitors are more likely to stop practices before they harm the broader public because they can identify abuse sooner.[246] These advantages are particularly pertinent in the context of the flexible UDAP unfairness standard because an effective advocate can further a UDAP's statutory purpose of adapting to and enjoining novel forms of bad business practices.[247]

b. Competitors as marketplace stakeholders

Market competitors should be empowered to make effective use of UDAPs because they are, at least theoretically, financially

245. *See, e.g.*, Mass.Gov, Consumer Affairs and Business Regulation, Official Website of the Office of Consumer Affairs & Business Regulation (OCABR), *How to Resolve a Consumer Problem*, http://www.mass.gov/?pageID=ocamodulechunk&L=2&L0=Home&L1=Consumer&sid=Eoca&b=terminalcontent&f=resolve_a_problem&csid=Eoca (last visited Aug. 18, 2010); Andrew M. Cuomo, New York State Attorney General, Consumer Frauds Bureau, *Filing a Consumer Complaint*, http://www.ag.ny.gov/bureaus/consumer_frauds/filing_a_consumer_complaint.html (last visited Aug. 18, 2010). Because they are not experts in an industry, individual consumers and public law offices generally have to educate themselves about the particular market to better recognize questionable conduct. The average consumer's lack of sufficient legal knowledge to understand that an unreasonable term in a contract may actually constitute an unfair business practice is particularly relevant in the context of UDAP litigation.

246. *See* Neil Gunningham & Joseph Rees, *Industry Self-Regulation: An Institutional Perspective*, 19 L. & POL. 363, 363 (1997) ("[T]here is growing evidence of a range of circumstances where self-regulation (either alone, or more commonly, in conjunction with other policy instruments) can be a remarkably effective and efficient means of social control."); Debra A. Valentine, General Counsel, Federal Trade Commission, Industry Self-Regulation and Antitrust Enforcement: An Evolving Relationship, Remarks Before the Interdisciplinary Center Herzlia, the Arison School of Business, and the Israeli Antitrust Authority Seminar on New Developments in Antitrust Policy (May 24, 1998), *available at* http://www.ftc.gov/speeches/other/dvisraelspeech.shtm (discussing ways in which the FTC has aided private-industry actors with industry self-regulation).

247. Indeed, a primary criticism of UDAPs in general is that the unfairness standard is too vague, such that compliance is overly burdensome. *See, e.g.*, J.R. Franke & D.A. Ballam, *New Applications of Consumer Protection Law: Judicial Activism or Legislative Directive?*, 32 SANTA CLARA L. REV. 347, 348–49 (1992) (concluding that, despite some examples of novel applications of UDAPs, courts are not "abusing their authority by interpreting [UDAPs] more broadly than envisioned by the legislatures"); Thomas, *supra* note 203, at 32 (suggesting that, with UDAPs, courts "must be cautious not to interpret away the legislature's written word"). However, bringing businesses to the table to help define the contours of unfair or deceptive practices is one way to mitigate this criticism.

invested in securing a vibrant marketplace in their respective industries. While a UDAP's consumer-protection purpose appears to conflict with a business's primary function in furthering its own financial success, these seemingly divergent interests can both be served by representative market-competitor standing. If a competitor is operating in an unfair or deceptive fashion, a direct harm is inflicted upon its customers;[248] however, a significant, indirect harm is also imposed on that business's competitors that have suffered injury from a lost opportunity to compete.[249] As such, a market competitor arguably has a greater incentive to bring UDAP litigation because its viability depends on the health of the market in which it participates; for consumers and public law offices, however, a particular business's set of UDAP violations is only one among many concerns.

c. *Financial resources*

Relative to individual consumers and taxpayer-funded state public law offices, market competitors are well positioned to make effective use of UDAPs because they collectively have the most resources with which to litigate.[250] While this proposition undoubtedly varies by plaintiff and industry, businesses generally have more resources to devote to litigation than do individuals.[251] Because litigation poses significant financial risk, however, it is important to mitigate this risk as much as possible through strong remedial provisions—monetary remedies that would incentivize industry self-regulation while deterring unfair business practices.[252]

2. Costs of Representative Competitor Standing

Despite the value added from employing businesses as aggressive, self-regulatory UDAP litigants, expansion of UDAP standing is not without cost. In the context of business-to-business litigation, the primary drawbacks include indirect harms to

248. *See Toward Greater Equality*, *supra* note 15, at 1631–32.

249. *Id.*

250. *See* Lannan, *supra* note 188, at 476; Fogel, *supra* note 30, at 455–56.

251. *Toward Greater Equality*, *supra* note 15, at 1626 ("Unscrupulous merchants know that federal and state government agencies can monitor and detect only a small fraction of the deceptive or fraudulent practices occurring in the marketplace.").

252. *See supra* Part IV.A.3.

consumers through a reduced access to credit and the potential for litigation abuse.[253]

a. Indirect harm to consumers

Critics often argue that consumer protection laws actually hurt the groups they seek to protect by reducing access to credit or driving up prices.[254] This argument is readily applicable to UDAP market-competitor standing because increased litigation may drive up costs for consumers and lead to new restrictions on business practices.[255] Despite these theoretical costs to consumers, erring on the side of broader consumer protection offers greater benefits than the questionable extension of credit. After all, the liberal access to credit in the years leading up to the mortgage crisis did not result in a corresponding increase in homeownership rates.[256] It must therefore be asked whether business practices that ultimately hurt consumers are even worth protecting.[257] Simply stated, some credit is not in consumers' best interest, so not every extension of credit merits protection.[258]

b. The potential for litigation abuse

Critics could also argue that representative UDAP market-competitor standing would both revive the same abuses that led to the passage of Proposition 64 and create entirely new opportunities for abuse.[259] However, the requirements of (1) an actual business-competitor plaintiff, (2) a demonstration of a significant public

253. Several articles have explored more general criticisms of UDAPs. *See, e.g.*, Franke & Ballam, *supra* note 247, at 348–49, 366–425 (1992) (evaluating claims of abuse in judicial interpretation of UDAPs); Thomas, *supra* note 203, at 1–10, 17–23, 30–32 (arguing that Pennsylvania's courts should rein in application of that state's UDAPs through, for example, strict construction of standing limitations). While more limited, other sources have offered criticisms of businesses as potential UDAP plaintiffs. *See, e.g.*, *Toward Greater Equality*, *supra* note 15, at 1627–39 (noting, for example, that businesses have greater bargaining power, less of an incentive to defraud other businesses, and little need to create a deterrent effect).

254. *See, e.g.*, Cole, *supra* note 26, at 264–72.

255. *Id.* 272–75.

256. Willis, *supra* note 79, at 731–32.

257. *See* Azmy, *supra* note 76, at 308–11.

258. *See generally* Willis, *supra* note 76, at 1184–99, 1230–55 (deconstructing the economic model imputed to consumers engaged in home-loan borrowing).

259. *See* Disner & Jussim, *supra* note 176, at 42–46; Lannan, *supra* note 188, at 460–65, 471–79.

interest, and (3) judicially approved settlements, would go far to prevent the pre-Proposition 64 problems with representative standing. As for potential new abuses from unscrupulous competitor claims seeking only to obtain trade secret information or harass small businesses, these problems are common to all litigation[260] and should be remedied through judicial sanctions and early summary judgment motions.

3. Weighing Costs and Benefits

It is impossible to prove that representative UDAP standing for businesses would have helped prevent the mortgage crisis, but there are some indications that it could have had a positive effect. First, structured mortgage regulations like TILA, RESPA, and HOEPA failed to prevent lending abuses because the complicated nature of these statutes allowed abusive lenders to find ways to originate otherwise legal loans with unfair terms and procedures. Second, as *Fremont Investment & Loan* shows, UDAPs can play an effective role in regulating the mortgage market because the unfairness standard gives courts the flexibility to find business practices unfair even where they do not violate the law. Third, as the severity of the mortgage crisis demonstrates, UDAPs, despite their inherent benefits, failed to prevent the mortgage crisis because such claims were not brought in sufficient numbers and were not sufficiently successful.

Fourth, while consumers suffered a primary harm from predatory lending practices, businesses suffered secondary harms from lost market share because of a diminished capacity to compete. Fifth, UDAPs prevent businesses from pursuing UDAP litigation against competitors that are acting unfairly. Sixth, when the harmful conduct of a competitor results in a diminished capacity to compete, a business generally must choose between joining in the profitable but harmful conduct or bringing suit to enjoin its competitor's bad acts. Seventh, it is good public policy to facilitate industry self-regulation before inviting government intervention and consumer litigation. Finally, policy arguments advanced against representative

260. *See* BILL MCINTURFF & LORI WEIGEL, PUBLIC OPINION STRATEGIES, 2010 VOTERS' VIEWS ON LAWSUITS (2010), *available at* http://www.instituteforlegalreform.com/images/stories/documents/pdf/research/2010electionsurveykeyfindings.pdf.

UDAP standing are not applicable in the context of business-to-business litigation.

The inherent benefits of representative UDAP standing for businesses are therefore likely to outweigh its potential costs. This Article proposes a practical method, supported by good policy, through which to stop bad business practices by enhancing the deterrent effect of UDAPs. Arguably, conferring representative UDAP standing on market competitors would not have prevented the mortgage crisis. Market competitors may have avoided litigation and instead joined in profitable predatory lending practices. Nevertheless, by precluding mortgage-industry actors from pursuing other options through UDAP litigation, the law inadvertently pushed businesses toward predatory lending. At the very least, the law should be structured to give businesses a choice between joining in harmful conduct and trying to prevent it.

V. CONCLUSION

By providing an expansive cause of action, state UDAP statutes serve a critical function in deterring and curbing unfair or deceptive business practices. However, a UDAP's effectiveness in protecting consumers and promoting lawful business activity is partly a product of the statute's standing provisions and available remedies.[261] Of potential plaintiffs, market competitors are well positioned with industry expertise, commitment to the marketplace, and sufficient resources to utilize UDAP statutes to police their own marketplaces.

Amending UDAPs to provide representative standing for business plaintiffs—free of an injury-in-fact requirement—would allow these groups greater freedom to make efficient and effective use of UDAPs to self-regulate their own industries. Including tailored remedial provisions would further empower business competitors to take the lead in preventing unfair and unlawful business activities like the predatory lending that contributed to the mortgage crisis. As the risky lending at issue in *Fremont Investment & Loan* shows,[262] the bad practices of one business actor can cause widespread harm to both its business competitors and the general public.

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261. *See* Sullenger, *supra* note 20, at 488.

262. *See supra* Part II.C.