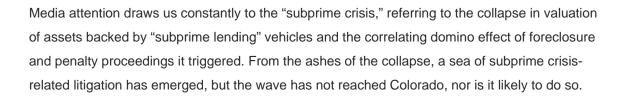
Subprime lending crisis brings little litigation to Colorado

Colorado has seen fewer than 10 subprime-related lawsuits

By Jennifer Weddle, as originally published on www.cobizmag.com

Question: What are the likely Colorado litigation consequences of the "subprime crisis"?

Answer: Investor arbitrations.



"Subprime lending" is a financial term describing the provision of credit – including mortgages, auto loans and credit cards – to borrowers who do not meet prime underwriting guidelines, with greater risk of default.

Many hundreds of subprime-related suits have been filed over the last two years, including over 150 securities lawsuits against companies like Citigroup and Merrill Lynch, dozens of class actions, and hundreds of individual investor complaints. Subprime lenders have also been targeted with allegations that they engaged in deceptive or unfair trade practices. Most of these high-stakes suits have been filed in New York federal courts. In just one of these cases, last month, Merrill Lunch agreed to pay \$475 million to settle class-action securities fraud claims that accused the investment bank of deceiving its shareholders by overstating the value of its portfolio of subprime-mortgage-backed securities.

In contrast, Colorado has seen fewer than 10 individual, subprime-related lawsuits, mostly in federal court and involving much smaller universes of damages. The sweeping investor claims that have been the hallmark of the national litigation have been absent in Colorado. Rather, the Colorado suits have generally involved 'fringe' issues, such as risk insurance and loan repurchase agreements between firms. This is not surprising, given Colorado's geographic distance from the country's financial centers and its relatively high percentage of community banks with much lesser participation in subprime mortgage lending and collateralized mortgage-backed securities. Most Colorado businesses were simply less entangled in subprime activity than their national counter-parts. Those Colorado lenders that have faced allegations related to



subprime lending activity, such as Countrywide Financial Corp., have generally engaged in litigation – in Countrywide's case, with the state – and settled relatively quickly. For instance, in a Feb. 3 settlement, Countrywide will make nearly \$6 million available to Colorado borrowers and to the state and assist its borrowers in with fast-track loan modification.

That pattern is likely to continue. While there already is and will likely still be significant Colorado derivative litigation activity associated with the bursting of the housing market bubble, most of Colorado's subprime-crisis litigation activity is likely to take the form of investor arbitrations. Many Colorado companies had supported and marketed subprime-backed securities, even just as smaller holdings of larger investment vehicles, and may face legal and financial exposure as result.

As is common in economic downturns, investors facing significant account losses will take their brokerage firms and financial advisers to arbitration before the Financial Industry Regulatory Authority (FINRA), the largest independent regulator for all securities firms doing business in the U. S. These complaints are likely to allege claims premised on: (a) suitability (resting on allegations that investments are inappropriate for the objectives, age or sophistication of the investor) and (b) diversification (alleging failure to diversify accounts and/or over-weighting of mortgage-backed securities).

In most instances, investors will have agreed in their new account documents to bring any claims in FINRA arbitration and forego opportunities to litigate in federal or state courts or to participate in class actions. Similarly, consumers seeking to bring claims against subprime credit card issuers will be subject to arbitration clauses contained in their credit agreements or mailed later with monthly bills as contracts of adhesion. Both sorts of arbitration agreements are highly likely to be enforced by Colorado courts because, under the Federal Arbitration Act, arbitration agreements are valid and enforceable in the same manner as other contracts. Plaintiffs might challenge arbitration provisions on ground of unconscionability or vagueness, but those arguments are not often successful. Consequently, most of Colorado's subprime-related litigation will probably take place behind closed arbitration doors and/or settle early.

Therefore, from a litigation perspective, the subprime crisis in Colorado is more of a "subprime whimper." What should not be discounted, however, is the level of personal crisis many Coloradoans may face as a result of the debacle – dealing with foreclosures and penalties.

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