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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA – EASTERN DIVISION

KRISTA RAILEY, individually, and
on behalf of all others similarly
situated,

Plaintiff,

v.

PENTAGON FEDERAL CREDIT
UNION,

Defendant.

Case No.:

CLASS ACTION COMPLAINT

DEMAND FOR JURY TRIAL

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1 are required to disclose to borrowers, among other items, applicable interest rates,
2 including any discounts, notices of interest rate adjustments, and the timeline for
3 repayment, so that borrowers are fully informed of the costs and conditions of a
4 mortgage.

5 7. Defendant’s mortgage products are strictly regulated by federal
6 disclosure requirements under the Truth-In-Lending-Act (“TILA”), implemented
7 by Regulation Z. 12 C.F.R. §1026.1 *et seq.*

8 8. The Consumer Financial Protection Bureau has opined that preferred
9 rate mortgage products offered to a creditor’s employees are considered variable
10 rate mortgage products if the offered rate is contingent upon continued
11 employment with the creditor employer.¹

12 9. PenFed Loan Estimate and Closing Disclosures (“Loan Disclosure
13 Documents”) are presumptive form documents issued at the outset of a mortgage
14 transaction and a few days prior to the closing of a mortgage financing transaction.
15 The Loan Disclosure Documents are presumptively structured to be consistent with
16 and abide by the disclosure requirements of TILA.

17 10. Among other terms, the PenFed Loan Disclosure Documents set forth
18 the loan amount, interest rate, loan term, purpose of the loan, whether a fixed or
19 variable loan product is presented, and loan type. Exhibits A, B.

20 11. Under TILA, PenFed is statutorily required to disclose through its
21 Loan Disclosure Documents to its preferred rate employee borrowers, among other
22 items, whether its mortgage loans are variable, what conditions would trigger a
23 change to the applicable interest rate, and amount of time required for notice of a
24 change in rate.

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26 ¹ See Consumer Financial Protection Bureau (“CFPB”) Comment for 12 C.F.R. § 1026.19(b)-5i(B) at
27 <https://www.consumerfinance.gov/rules-policy/regulations/1026/interp-19/#19-b-Interp-5-i> (last accessed
28 on December 5, 2022)

1 **PARTIES**

2 19. Plaintiff Krista Railey is a resident of Canyon Lake, California and
3 has resided in Riverside County during the relevant time period.

4 20. Defendant Pentagon Federal Credit Union is a national credit union
5 headquartered in McLean, Virginia. Defendant regularly conducts business in this
6 District, including the marketing and issuance of residential mortgage services and
7 mortgage finance products such as the one issued to Plaintiff.

8 **FACTUAL ALLEGATIONS**

9 **PenFed Issues Preferred Rate Mortgage Agreements To Its Employees**

10 21. PenFed offered to Plaintiff and other employees of PenFed a preferred
11 rate mortgage product whereby a discount was applied to the standard mortgage
12 rate that would otherwise have applied but for the borrower's status as an
13 employee of PenFed.

14 22. The discounted mortgage rate offered by PenFed to its employees
15 would only apply while PenFed actively employed its employee borrowers. Thus, a
16 PenFed employee who had obtained a preferred rate mortgage product through
17 PenFed would stand to lose the applicable discount upon termination of
18 employment with PenFed.

19 23. As such, what was presented by PenFed as a preferred fixed rate
20 mortgage product was actually a variable preferred mortgage rate product.

21 24. Although PenFed's preferred rate mortgage product may be
22 considered an employee benefit to its employees, PenFed is still obligated to
23 follow all disclosure requirements promulgated under TILA and Regulation Z to
24 ensure its employee borrowers are made fully aware of the costs and variability of
25 the mortgage product they obtain from PenFed consistent with applicable
26 timeframes before the closing of the mortgage transaction as established in TILA.
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1 **TILA Protects Borrowers Against Unlawful Mortgage Rate Changes**

2 25. TILA, and its implementing statute, Regulation Z, collectively
3 require lenders to timely disclose critical components of a mortgage product
4 offered to its borrowers. The timing component of TILA ensures borrowers can
5 fully assess and evaluate the total projected costs of the mortgage product prior to
6 the closing of the mortgage transaction.

7 26. Regulation Z requires specific disclosures for variable-rate mortgage
8 transactions if the applicable annual percentage rate may increase on a mortgage
9 transaction that has a term greater than one year. 12 C.F.R. §1026.19(b)

10 27. Regulation Z sets forth particular disclosure requirements concerning
11 the variability of the applicable interest rate that must be provided for variable-rate
12 mortgage products presented to borrowers. These disclosure requirements include,
13 but are not limited to, the following pertinent subsections of 12 C.F.R.

14 §1026.19(b)(2) addressing variable-rate mortgages:

- 15
- 16 (i) The fact that the interest rate, payment, or term of the loan can
 change.
 - 17 (vii) Any rules relating to changes in the index, interest rate, payment
18 amount, and outstanding loan balance, including, for example, an
19 explanation of interest rate or payment limitations, negative
 amortization, and interest rate carryover.
 - 20 (xi) The type of information that will be provided in notices of
21 adjustments and the timing of such notices.

22 28. Regulation Z further requires certain information about the loan be
23 delivered or mailed to the borrower in the form of a good faith estimate within
24 three days of the creditor's receipt of the mortgage loan application. 12 C.F.R.
25 §1026.19(e)(iii), *et seq.*

26 29. Under 12 C.F.R. §1026.37, the required contents of the good faith
27 estimate presented to the borrower by the creditor include, but are not limited to, a
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1 description of the loan product as an adjustable, step, or fixed rate product ²; and
2 loan terms disclosing the applicable interest rate at consummation and any
3 adjustments that may be made after consummation.³

4 30. Under 12 C.F.R. § 1026.38, the required contents of the closing
5 disclosures include, but are not limited to, certain disclosures made as part of the
6 good faith estimate, such as the description of the loan product ⁴ and loan terms
7 expressing the applicable interest rate and any adjustments that may be made after
8 consummation.⁵

9 31. The Official CFPB Staff Commentary to 12 C.F.R. §1026.19(b), *et*
10 *seq.* provides a pointed example of how a preferred rate mortgage offered to an
11 employee by an employer creditor is presumptively considered a variable-rate
12 transaction:

13 **Examples of Variable-Rate Transactions**

14 i. The following transactions, if they have a term greater than one
15 year and are secured by the consumer's principal dwelling,
16 constitute variable-rate transactions subject to the disclosure
requirements of § 1026.19(b).

17 B. Preferred-rate loans where the terms of the legal obligation
18 provide that the initial underlying rate is fixed but will increase
19 upon the occurrence of some event, ***such as an employee leaving***
20 ***the employ of the creditor, and the note reflects the preferred***
21 ***rate.*** The disclosures under §§ 1026.19(b)(1) and 1026.19(b)(2)(v),
(viii), (ix), and (xii) are not applicable to such loans.

22 (emphasis added)

26 ² 12 C.F.R. §1026.37(a)(10)(i)

27 ³ 12 C.F.R. §1026.37(b)(6)

28 ⁴ 12 C.F.R. § 1026.38(a)(5)(iii)

⁵ 12 C.F.R. § 1026.38(b)

1 *See Official Interpretation of 12 C.F.R. §1026.19(b) Certain Variable Rate*
2 *Transactions* ⁶

3 **PenFed Unlawfully Adjusted The Rate On Plaintiff's Mortgage**

4 32. Plaintiff applied for and subsequently obtained a purchase mortgage
5 from Defendant on or around December 8, 2021. The preferred rate mortgage was
6 issued in the amount of \$575,000 and was secured by her primary residence in
7 Canyon Lake, California. *See Exhibit A.*

8 33. In contrast to the fixed interest rate of 2.75% mortgage consistently
9 presented and disclosed in the PenFed Loan Disclosure Documents, Defendant
10 inserted a supplemental addendum on the December 8, 2021 closing date of
11 Plaintiff's mortgage transaction notifying Plaintiff that her preferred rate mortgage
12 was contingent upon continued employment with PenFed. In its notice, Defendant
13 disclosed an "Employee Rate Discount" applied to Plaintiff's mortgage rate as
14 follows:

15
16 **EMPLOYEE RATE DISCOUNT**

17 I/we acknowledge a loan rate discount has been granted to the PenFed
18 Employee/Borrower on my Note/Agreement in accordance with
19 PenFed's policies and procedures. I/we understand and agree I/we will
20 be in default upon the PenFed Employee/Borrower's separation from
21 PenFed employment either by resignation or termination, or if the
22 loan becomes 60 days or more delinquent. In those events of default,
23 the loan rate discount applicable to the loan will be rescinded and
24 the loan rate will revert to the regular loan rate in effect at the time the
25 loan was granted for the type of loan obtained for fixed-rate loans. For
26 variable-rate loans, in those events of default, the loan rate discount
27 applicable to the loan will be rescinded and the loan rate will revert to
28 the regular loan rate in effect at the time the discount is rescinded.
I/we further understand and agree the rate discount and the terms and

⁶ <https://www.consumerfinance.gov/rules-policy/regulations/1026/19/#19-b-Interp-5> (last
accessed on December 5, 2022)

1 conditions are made in accordance with and subject to applicable law,
2 and PenFed's policy and procedure for Employee loan rate discounts
3 as may be amended from time to time in PenFed's sole discretion.
4 All other terms and conditions of the Note/Agreement remain in full
5 force and effect.

6 *See Exhibit C.*

7 34. Putting aside Defendant's failure to disclose the variability of the loan
8 rate in the Loan Disclosure Documents presented to Plaintiff, Defendant further
9 fails to disclose the amount of the employee rate discount in its supplemental
10 addendum or any specific reference within PenFed's employee policies and
11 procedures that would purportedly apply to the mortgage loan rate discount.

12 35. Plaintiff is informed and believes, and thereupon alleges, that PenFed
13 was aware that this 11th hour disclosure of a variable rate condition in Plaintiff's
14 preferred fixed-rate mortgage was not properly disclosed to Plaintiff in PenFed's
15 Loan Disclosure Documents.

16 36. On or around August 2022, Plaintiff was informed her employment
17 with PenFed would be terminated.

18 37. On September 7, 2022, Plaintiff was informed the discount on her
19 mortgage rate would be eliminated resulting in an adjustment to her mortgage rate
20 from 2.875% to 3.15%. Exhibit D. The increase in the mortgage rate resulted in
21 Plaintiff paying a monthly mortgage amount of \$2,311 starting November 1, 2022,
22 instead of the \$2,240.42 she had been paying prior to her termination from PenFed.

23 38. From November 1, 2022, onward, Plaintiff has been subject to a
24 higher mortgage interest rate and has paid a higher monthly mortgage payment
25 because Defendant unlawfully rescinded Plaintiff's employee rate discount.

26 39. As a result of PenFed's violations of TILA and its implementing
27 Regulation Z as well as its unlawful business practices discussed herein, Plaintiff
28 and the Class suffered monetary damages from PenFed's unlawful conduct.

- 1 a. whether PenFed was required to follow the requirements of TILA
- 2 as a lender who issued residential mortgage financing to
- 3 borrowers;
- 4 b. whether PenFed instituted sufficient policies and procedures to
- 5 follow applicable disclosure regulations as promulgated by TILA;
- 6 c. whether PenFed was obligated under TILA whether a mortgage
- 7 loan was variable as to the type, interest rate, and conditions
- 8 underlying the variability in its Loan Disclosures;
- 9 d. whether PenFed's Loan Disclosures failed to properly disclose
- 10 whether a mortgage loan was variable as to the type, interest rate,
- 11 and conditions underlying the variability;
- 12 e. whether PenFed's alleged conduct is unlawful;
- 13 f. whether the PenFed's alleged conduct constitutes a violation of
- 14 TILA;
- 15 g. whether Plaintiff and the Class suffered actual damages as a result
- 16 of PenFed's alleged unlawful conduct; and
- 17 h. whether Plaintiff and Class members are entitled to appropriate
- 18 statutory remedies, including damages and restitution.

19 **Typicality**

20 46. Plaintiff's claims are typical of the claims of the members of the Class
21 because, inter alia, all Class members were injured through the uniform
22 misconduct described above and were subject to PenFed's failure to abide by
23 federal regulations governing the disclosure of mortgage loan type, interest, and
24 conditions triggering any variability as to the interest rate, amounts owed, and
25 timelines applicable to the repayment of the mortgage loan. Plaintiff is also
26 advancing the same claims and legal theories on behalf of herself and all members
27 of the Class.
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Adequacy of Representation

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2 47. Plaintiff will fairly and adequately protect the interests of the
3 members of the Class. Plaintiff has retained counsel experienced in complex
4 consumer class action litigation, and Plaintiff intends to prosecute this action
5 vigorously. Plaintiff has no adverse or antagonistic interests to those of the Class.

Superiority

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7 48. A class action is superior to all other available means for the fair and
8 efficient adjudication of this controversy. The damages or other financial
9 detriment suffered by individual Class members are relatively small compared to
10 the burden and expense that would be entailed by individual litigation of their
11 claims against PenFed. It would thus be virtually impossible for members of the
12 Class, on an individual basis, to obtain effective redress for the wrongs done to
13 them. Furthermore, even if Class members could afford such individualized
14 litigation, the court system could not. Individualized litigation would create the
15 danger of inconsistent or contradictory judgments arising from the same set of
16 facts. Individualized litigation would also increase the delay and expense to all
17 parties and the court system from the issues raised by this action. By contrast, the
18 class action device provides the benefits of adjudication of these issues in a single
19 proceeding, economies of scale, and comprehensive supervision by a single court.
20 It presents no unusual management difficulties under the circumstances here.

21 49. Plaintiff seeks statutory relief on behalf of the Class, on grounds
22 generally applicable to the entire Class and Subclasses requiring PenFed to provide
23 full statutory relief to Plaintiff and Class members.

24 50. Unless a Class is certified, PenFed will inequitably retain monies
25 received as a result of its conduct that were taken from Plaintiff and Class
26 members.

Rule 23(b)(3)

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2 51. The Class may be certified under Rule 23(b)(3) when questions of law
3 or fact that are common to class members predominate over questions concerning
4 individual members. Certification under Rule 23(b)(3) is appropriate when
5 necessary to attain time, effort, and resource efficiencies as well as uniformity of
6 decision applicable to similarly situated persons without sacrificing procedural
7 fairness. Predominance is found on sufficient cohesiveness among class members
8 with a focus on whether common questions can be resolved in a single
9 adjudication.

10 52. Very few members of the Class will have the means to seek individual
11 redress for the unlawful conduct committed against them by Defendant. Once
12 PenFed's liability has been established as to its failure to abide by the disclosure
13 requirements promulgated by TILA and Regulation Z to the same PenFed
14 preferred rate loans held by all members of the Class, the Court can readily oversee
15 the efficient administration of the Class claims.

16 53. Individualized litigation presents a potential for inconsistent or
17 contradictory judgments. In contrast, a class action presents far fewer management
18 difficulties; allows the hearing of claims that might otherwise go unaddressed; and
19 provides the benefits of single adjudication, economies of scale, and
20 comprehensive supervision by the Court.

COUNT I

**Violation of Truth In Lending Act
15 U.S.C. § 1639; 21 CFR §1026.19(b)
(On Behalf of Plaintiff and the Class)**

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25 54. Plaintiff repeats and re-alleges the allegations in the paragraphs above
26 as if fully set forth herein.

27 55. Plaintiff brings this claim individually and on behalf of the Class.
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1 56. As alleged herein, Plaintiff applied for and received a preferred rate
2 mortgage loan from PenFed.

3 57. The preferred rate mortgage loan was presented as a fixed rate
4 mortgage transaction as presented in the PenFed Loan Disclosures.

5 58. The preferred rate mortgage loans were amended to be variable-rate
6 mortgage transactions without the requisite disclosures and applicable timing as
7 promulgated under TILA and Regulation Z.

8 59. TILA and Regulation Z require creditors to disclose material terms of
9 a variable mortgage transaction under 12 CFR §1026.19(b).

10 60. The Official Staff Commentary to Regulation Z, 12 CFR
11 §1026.19(b)(2)(vii), provides pointed examples of circumstances that would
12 trigger a rate increase in a preferred rate mortgage loan, such as the termination of
13 employment of the borrower with a creditor.

14 61. PenFed violated TILA and Regulation Z by failing to disclose in its
15 Loan Disclosure Documents that the preferred mortgage rate transactions with
16 Plaintiff and the Class are variable-rate mortgage transactions.

17 62. PenFed further violated TILA and Regulation Z by failing to disclose
18 all information required under a variable rate mortgage transaction.

19 63. PenFed's violations of TILA and Regulation Z harmed and continue
20 to harm Plaintiff and the Class, including the loss of an interest rate discount within
21 the preferred rate loan which increases the monthly mortgage payments and total
22 cost of the mortgage to Plaintiff and the Class.

23 64. As a result of PenFed's violations and actions and/or failures as
24 alleged above, Plaintiff and the Class seek all available actual and statutory
25 damages as well as attorney fees and costs of the action under 15 U.S.C. §
26 1640(a)(3).

COUNT II
VIOLATION OF THE CALIFORNIA UNFAIR COMPETITION LAW
Cal. Civ. Code § 17200 *et seq.*
(on Behalf of Plaintiff Individually)

65. Plaintiff repeats and re-alleges every allegation above as if set forth herein in full.

66. The UCL prohibits any “unlawful”, “fraudulent”, or “unfair” business act or practice.

67. The acts and practices of PenFed as alleged above have caused Plaintiff to lose money or property as a result of PenFed’s violations of the TILA as discussed herein. PenFed’s acts and practices are actionable under the “unlawful” and “unfair” prongs of the UCL, as alleged with more specificity below.

68. Plaintiff may properly seek injunctive relief under the UCL as she has no adequate remedy for declaratory or injunctive relief available at law to cease or otherwise halt Defendant’s ongoing and future unlawful behavior under TILA or its implementing Regulation Z.

Unlawful Prong

69. Liability under the UCL is established through a predicate violation of a relevant statute applicable to the underlying unfair and deceptive conduct.

70. A violation of a relevant statute is an independently actionable violation of the UCL.

71. As discussed more fully above, PenFed is alleged to have violated material provisions of TILA that govern mortgage loan disclosures.

72. PenFed violated TILA by, among other things, failing to disclose in its Loan Disclosure Documents, the loan type, interest rate, and conditions that would trigger a change in the interest rate applicable to Plaintiff’s mortgage.

1 73. PenFed’s conduct is unlawful within the context of the unlawful prong
2 of the UCL.

3 74. As a result of PenFed’s unlawful conduct in violation of the TILA,
4 Plaintiff was economically harmed by PenFed’s violation of the unlawful prong of
5 the UCL by virtue of Plaintiff paying a higher monthly mortgage under an
6 unlawfully established variable interest rate.

7 **Unfair Prong**

8 75. PenFed engaged in “unfair” business acts or practices by, among other
9 things, failing to abide by TILA statutory regulations requiring PenFed to timely
10 disclose the true costs and variability of its preferred mortgage rate product to
11 Plaintiff.

12 76. In the course of conducting business, PenFed committed “unfair”
13 business acts or practices, by which it has been unjustly enriched. Because the
14 gravity of harm to Plaintiff and the competitive market outweighs the utility of
15 PenFed’s conduct (zero), PenFed’s conduct is “unfair” having offended an
16 established public policy in the form of TILA which sets forth requirements,
17 regulations, and remedies for the protection of the preferred rate mortgage
18 borrower.

19 77. PenFed engaged in immoral, unethical, oppressive, and unscrupulous
20 activities that are reasonably avoidable and substantially injurious to the public at
21 large. There were reasonably available alternatives to further PenFed’s legitimate
22 business interests other than the conduct described herein.

23 78. Plaintiff was economically harmed by PenFed’s alleged violations of
24 the “unfair” prong of the UCL.

25 79. On behalf of herself, Plaintiff seeks injunctive relief to have the
26 Employee Addendum/Rider that PenFed inserted and applied to Plaintiff’s
27 mortgage struck as unlawful and unfair under the UCL.
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PRAYER FOR RELIEF

Wherefore, Plaintiff prays for a judgment:

- A. Certification of this case as a class action on behalf of the Class and certification of Plaintiff as an adequate Class Representative and her counsel as Class Counsel for the Class;
- B. Issuance of a Court order finding PenFed in violation of the TILA as to Plaintiff and the Class;
- C. Issuance of a Court order finding PenFed in violation of the UCL as to Plaintiff;
- D. Issuance of a Court order awarding financial and statutory damages to Plaintiff and the other members of the Class, including any applicable interest as permitted under law;
- E. Issuance of a Court order awarding appropriate equitable relief to Plaintiff, including declaratory and injunctive relief compelling PenFed to reinstate her unlawfully adjusted preferred rate mortgage product to the rate prior to the unlawful adjustment;
- F. An award of costs and reasonable attorneys' fees; and
- G. Such other and further relief as this Court finds necessary and proper.

