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YEAR IN REVIEW 2014

Relevant California Decisions in 2014

Bankruptcy Review

G&T Case of the Year

No. 6 and Counting...

Greetings,

We are pleased to present the sixth annual installment of Garrett & Tully's Year in Review Newsletter.

For those reading an electronic copy of this newsletter, we have included hyperlinks for all court opinions, so that you may easily read and print an opinion that catches your attention.

For those reading a hardcopy of this newsletter, the relevant authorities are available on our website at www.Garrett-Tully.com - click the link "Industry Decisions" found on the home page.

As always, we welcome any suggestions for improving this newsletter. Please feel free to e-mail me at smahler@garrett-tully.com with any comments or suggestions, and/or if you would like to receive our regular e-mails concerning new appellate decisions throughout the year.

Warm regards,

Scott Mahler

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- About the Firm -

Garrett & Tully, P.C. is a law firm with offices in Pasadena and Westlake Village, California, serving clients throughout the state. Combined, our attorneys have more than 150 years of experience in the title and escrow fields. We represent title and escrow companies, and title insurers and their insureds, in a broad range of real estate and business disputes. Our attorneys have considerable experience handling claims such as escrow and title negligence, defalcation, mechanic's liens, title defects, easements, claims between escrows, subescrow liability, class actions, lien priority, and defending title insurers in coverage and bad faith suits. The firm also has a significant practice representing clients in major accounting and securities suits, and defends employers in employment disputes. The firm handles civil appeals in all areas of the law.

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Title Insurance

An Insurer Has No Duty of Care to An Insured When It Purportedly "Volunteered" to Have a Notice of Abatement Released; a Notice of Possible Future Enforcement is Not a "Defect, Encumbrance, or Lien" on Title

By Zi C. Lin

***Stockton v. Tope* (2014) 233 Cal.App.4th 437**

In *Stockton*, plaintiffs, who were investors in a failed real estate development project sued lender/developer Stockton Mortgage, its principal, and related entities for failing to obtain the release of a notice of abatement from San Joaquin County, which required that certain dilapidated physical conditions on the subject property be fixed. Stockton (who foreclosed and took title to the property) tendered a claim to First American Title Insurance Company, who denied the claim on the grounds that the notice abatement did not constitute a "defect, lien, or encumbrance" on title because it only gave notice of possible future action, and there was no evidence that the County took any steps to abate the property.

Stockton cross-complained against First American, alleging, among other things, breach of the title policy and breach of an oral contract, claiming that First American agreed to have the notice of abatement released. The only purported evidence of an oral agreement was the following statement in the preliminary report pertaining to the notice of abatement: "Prior to close of escrow Alliance Title Company will require that a FULL RELEASE be obtained".

The trial court granted First American's motion for summary judgment and the court of appeal affirmed. The court of appeal found that the preliminary report was not a contract or representation of title under Ins. Code § 12340.11, that there was no evidence of an oral agreement requiring First American to obtain a release of the notice of abatement, and that the notice of abatement was not a "defect, lien, or encumbrance" on title under *Elysian Investment Group v. Stewart Title Guaranty Co.* (2002) 105 Cal.App.4th 315 ("*Elysian*").

The court of appeal also rejected Stockton's new argument on appeal that First American owed it a duty of care because it "volunteered" to obtain a release of the notice of abatement, citing the "Good Samaritan rule," which provides that "[T]he volunteer who, having no initial duty to do so, undertakes to come to the aid of another -- the 'good Samaritan[,]' [h]e is under a duty to exercise due care in performance and is liable if (a) his failure to exercise such care increases the risk of such harm, or (b) the harm is suffered because of the other's reliance upon the undertaking." (*Stockton, supra*, 253 Cal. App.4th at p. 456.) The court of appeal held that the Good Samaritan rule does not apply where there is no physical harm, citing federal authority, *Love v. United States*, 915 F.2d 1242, 1248 (9th Cir. 1989). This appears to be the first time that this principle has been applied in the insurance context.

The opinion also extends the holding of *Elysian* to a different set of facts. Stockton argued that *Elysian* – which holds that a notice of future enforcement, such as the notice of abatement in this case, is not a defect, lien or encumbrance on title – is distinguishable because monetary assessments accrued against Stockton's property. The opinion, at pages 13-14, holds that the mere accrual of assessments – without the recording of a lien to enforce those assessments – does not transform the notice of abatement into a defect, lien, or encumbrance on title.

Finally, the court of appeal found that the parties suing First American were not "insureds" under the policy and that they could not use the doctrine of third party beneficiaries to contravene the express terms of the contract.

Ryan C. Squire and Zi C. Lin of Garrett & Tully represented First American in this case.

A Deed of Trust Executed Before the Borrower Took Title to Property is Valid as Long as the Borrower Later Acquires the Title

By Zi C. Lin

***RNT Holdings., LLC v. United General Title Ins. Co.* (2014) 230 Cal. App.4th 1289**

Lender RNT Holdings tendered a claim to its title insurer United General Title, claiming that its deed of trust was invalid because the deed of trust was executed by the borrower before his purchase of the encumbered property closed, and the borrower was not on title when its deed of trust was recorded. RNT later reconveyed the deed of trust in an attempt to confirm that its deed of trust was invalid. United General Title denied the claim, and RNT Holdings sued. The trial court granted summary judgment in favor of United General Title, and RNT Holdings appealed.

The court of appeal affirmed the grant of summary judgment, holding:

1. The deed of trust was valid even though the borrower did not have title to the property at the time he executed the deed of trust under the theory of after-acquired title. "Title to real property acquired after it is mortgaged is deemed to be covered by the lien on the theory that the mortgagor is estopped from denying title under such circumstances." (*RNT Holdings, LLC, supra*, 230 Cal.App.4th at p. 1296.)

2. The deed of trust was valid despite the fact that the borrower was not on title to the property when RNT Holding's deed of trust was recorded under the doctrine of bona fide purchaser for value, which provides that a purchaser takes title free of unrecorded liens if the purchaser "(1) purchase[d] the property in good faith for value, and (2) ha[d] no knowledge or notice—actual or constructive—of the asserted rights of another." (*Id.*) The court of appeal held that the deed of trust was valid because the owner of the property at the time RNT's deed of trust was recorded, Tregub, had actual notice of it.

3. RNT's claim was not covered under Condition 10(b) of the title policy which provides that "The voluntary satisfaction or release of the Insured Mortgage shall terminate all liability of [United] except as provided in Section 2 of these Conditions", because RNT reconveyed the deed of trust. (*RNT Holdings,* at p. 1298.)

See RNT Holdings, continued on p. 16

Title Insurance

Ninth Circuit Affirms that the Lack of a DRE "White Report" is Not a Matter Affecting Title; Title Insurance Does Not Cover Matters Solely Affecting the Saleability or Market Value of Property

By Zi C. Lin

***Security Service Federal Credit Union v. First American Title Co.*, 585 Fed.Appx. 591 (9th Cir. 2014), affirming *Security Service Federal Credit Union v. First American Title Co.*, CV 10-04824 SJO VBKX, 2012 WL 5954815 (C.D. Cal. Jan. 27, 2012)**

First American Title Insurance Company insured 12 lots in Riverside County under 12 loan policies. Lender Security Service foreclosed and took title to the 12 lots. Security Service tendered a claim to First American Title Insurance Company maintaining that it did not have clear title to each lot due to the lack of a California Department of Real Estate final public report ("FPR", also known as a "white report") under the Subdivided Lands Act, which prohibits the sale of five or more lots without a FPR. The claim was denied.

Security Service sued First American Title Insurance Company in U.S. District Court for breach of contract, bad faith, and fraud. Security Service maintained that the lack of a FPR made the 12 lots separately unmarketable. (Security Service conceded that it could sell the 12 lots as one property in a bulk sale.) Security Service also alleged that First American Title Insurance Company had a duty to obtain the FPR and to disclose the lack of a FRP because a related title company, First American Title Company, had assisted prior owners of the 12 lots with their DRE applications, and that the *act* of issuing the 12 loan policies was a representation that the 12 lots were marketable.

The district court granted First American Title Insurance Company's motion for summary judgment. The court found that Security Service's claim was not covered because the lack of a FPR was not a matter affecting title. The Court relied on the holding of *Dollinger DeAnza Associates v. Chicago Title Ins. Co.* (2011) 199 Cal.App.4th 1132, wherein the court of appeal held that a similar notice of merger under the Subdivision Map Act – which prevented the individual sale of seven parcels – was not a matter affecting title. *Dollinger* held that "The notice of merger may restrict a landowner's ability to sell a portion of the merged land without compliance with the applicable provisions of the [SMA], but the notice of merger does not affect the landowner's title to the land." (*Security Service,* 2012 WL 5954815 at p. *6, citing *Dollinger*, at p. 1152.) Following this reasoning, the Court held that Security Service had good title to the 12 lots: "Defendant owes no duty to indemnify Plaintiff against circumstances affecting the saleability or market value of the Lots unless those circumstances also affect the marketability of title. Plaintiff has title to the Lots as against the world and has not alleged that any other person or entity may claim an interest in the Lots. In addition, there is no question that Plaintiff is able to sell the Lots, with or without a FPR, and transfer title in fee simple, albeit not in Plaintiff's desired manner or for the desired price." (*Id*. at p. *8.)

See Security Service v. First American, continued on p. 17

Foreclosure

A Lender's Full Credit Bid at a Foreclosure Sale Extinguishes Any Right to Insurance Proceeds as Mortgagees Under the Deed of Trust

By Jennifer R. Slater

***Najah v. Scottsdale Ins. Co.* (2014) 230 Cal.App. 4th 125**

Appellants Najah and Akhavain sold a commercial property agreeing to take as partial payment a promissory note secured by a second trust deed. Upon the borrower's default, they purchased the note secured by the first trust deed and commenced foreclosure proceedings on the second trust deed. Appellants reacquired the property by making a bid equal to the unpaid debt securing the second trust deed, including costs and fees. Appellants then sued the borrowers' insurer Scottsdale Insurance Company ("Scottsdale") for breach of contract and bad faith seeking to recover under the mortgagee coverage provision for known pre-foreclosure damage deliberately caused by the borrowers.

Scottsdale moved for summary judgment contending that the appellants' full credit bid extinguished the debt and any claim to insurance proceeds and the damages were not covered under the policy. The trial court denied the motion but granted Scottsdale's subsequent motion for summary adjudication on the punitive damages issue. Prior to trial, the trial court granted Scottsdale's motion to bifurcate the insurance coverage issue from the bad faith claim. After hearing the evidence on the insurance coverage issue, the trial court issued a written statement of decision in favor of Scottsdale holding that: (1) an owner of real property could not vandalize or steal his own property; and (2) any claim appellants had to insurance proceeds as mortgagees under the second deed of trust was extinguished by their full credit bid at the foreclosure sale.

The appellate court reasoned that applying the full credit bid rule to the combined debt where the holder of multiple deeds of trust forecloses on the most junior lien protects the integrity of the foreclosure auction process. Accordingly, the appellate court affirmed the trial court's judgment and concluded that the appellants' full credit bid at the foreclosure sale under the second trust deed precluded appellants from making a claim on the insurance proceeds.

-Ms. Slater is a partner in the Pasadena Office and has extensive experience handling title litigation and claims, including defending insured lenders against attacks on their deeds of trust. She also has substantial federal court and appellate experience.

Foreclosure

Deed in Lieu Does Not Destroy the Deed of Trust if There are Junior Liens

By Alex Levy

***Decon Group, Inc. v. Prudential Mortgage Capital Co., LLC* (2014) 227 Cal.App.4th 665**

In *Decon Group, Inc. v. Prudential Mortgage Capital Co., LLC* (2014) 227 Cal.App.4th 665, the court nicely summarizes the case at the outset: "AZ Wellesley Plaza, LLC (Wellesley), owned real property in Los Angeles (the Property) subject to a first deed of trust and a junior mechanic's lien. Wellesley defaulted on the loan secured by the trust deed. Faced with foreclosure on that senior debt, Wellesley gave the trust deed beneficiary title to the Property by means of a grant deed in lieu of foreclosure. The grantee/beneficiary then foreclosed, thereby eliminating all junior liens. The grantee/beneficiary also bought the Property at the foreclosure sale and later sold it to a third party. The holder of the mechanic's lien filed suit to foreclose its lien, arguing that the lien was not eliminated by the foreclosure. The holder of the mechanic's lien contended that when the trust deed beneficiary accepted the deed in lieu of foreclosure, those two interests (as beneficiary under the trust deed and as grantee under the deed in lieu) merged—the merger destroyed the senior lien, so the purported foreclosure on that lien was a sham. The superior court agreed and ordered foreclosure on the mechanic's lien. The trust deed beneficiary, the third party buyer, and another related party timely appealed."

"We reverse. Under well-established California law, the senior beneficiary's lien and title ordinarily do not merge when a deed in lieu of foreclosure is given if there are junior lienholders of record. The foreclosure after acceptance of the deed [in lieu] was therefore valid and eliminated all junior liens, including plaintiff's mechanic's lien. The third party now owns the Property free of all such junior encumbrances."

The court notes that the application of this rule is fair because it does not prejudice the junior lienholder, who bargained for a junior lien when it took its security, and who, notwithstanding the deed in lieu, retains all the rights of a junior lien holder facing a foreclosure of a more senior lien.

The court rejected the junior's argument that acceptance of the deed in lieu caused the deed of trust to be merged out of existence.

Comment: Equitable lien subrogation being an equitable doctrine, each case must be evaluated in the context of the equities made out by the fact pattern. This case is helpful in that it cites a number of factors that will not defeat the application of the doctrine.

The Ninth Circuit Rules that Certain Claims Under Arizona and Nevada Law may be Maintained Against MERS

By Zi C. Lin

***Robinson v. Am. Home Mortg. Servicing, Inc. (In re Mortg. Electronic Registration Systems, Inc.)*, 754 F. 3d 772 (9th Cir. 2014)**

State recording statutes require assignments of the beneficial interests in deeds of trusts to be recorded in the recorder's offices of the counties where the properties encumbered by those deeds of trusts are located. Recordation of the assignments gives notice of who owns the deeds of trust to borrowers and the public.

Mortgage Electronic Registration Systems, Inc. ("MERS") operates a private electronic mortgage index called "the MERS System" that circumvents the State recording requirements. Various banks and financial institutions are members of the MERS System. Under the MERS System, MERS is designated as the beneficiary of the deed of trust instead of the actual lender or lender's assignee who owns the beneficial interest.

"Use of the MERS System typically begins when a borrower from a MERS member signs a promissory note and a deed of trust. The MERS member takes possession of the note, and MERS is recorded as the beneficiary under the deed of trust. The note is almost always assigned to others, often several times over. If the note is assigned to a MERS member, MERS remains the beneficiary under the deed of trust. MERS contends that there is no need to record the assignment of the note so long as the assignee is a MERS member. However, when an assignment is made to a nonmember of MERS, the identity of the assignee is recorded. About half of the residential mortgages in the United States are now recorded with MERS named as the beneficiary under the deed of trust." (*Robinson v. Am. Home Mortg. Servicing, Inc. (In re Mortg. Electronic Registration Systems, Inc.*), 754 F.3d 772, 776-777 (9th Cir. 2014) ("*Robinson*").)

The advantage of the MERS System is that it allows lenders to avoid the expense of recording every change of ownership of deeds of trust. MERS has been sharply criticized because it is impossible for a borrower to determine who owns the deed of trust from an inspection of the County records. The MERS System, where the information regarding the actual holder of the deed of trust is held, is not accessible to the public. This makes it difficult for borrowers who are in default to determine if the lender complied with state foreclosure statutes.

Although many states have passed statutes to increase the transparency of the foreclosure process, – for example, California enacted the Homeowner's Bill of Rights (Civ. Code § 2920.5, et seq.), requiring lenders to communicate with home-owners to discuss alternatives to foreclose – many lawsuits have been filed challenging the validity of the MERS System.

See Robinson v. Am. Home Mortg., continued on p. 17

Foreclosure

A Debtor May Not Bring a Preforeclosure, Preemptive Action to Challenge the Foreclosing Entity's Authority to Foreclose

By Candie Y. Chang

Kan v. Guild Mortgage Co. (2014) 230 Cal.App. 4th 736

In July 2007, Lindsay Kan signed two notes secured by two deeds of trust on real property in Stevenson Ranch in favor of Guild Mortgage Company as the lender, Guild Administration Corp. as the trustee, and Mortgage Electronic Registration Systems, Inc. (MERS) as the beneficiary acting as nominee for the lender, its successors, and assigns.

In October 2010, MERS substituted Recontrust Company as the trustee under the first deed of trust and assigned all beneficial interest under the first deed of trust to The Bank of New York Mellon, as trustee for CWALT, Inc., a mortgage-backed investment trust. Recontrust recorded a notice of default on December 8, 2010, and served a notice of trustee's sale in March 2012, but did not conduct a foreclosure sale.

In July 2012, MERS assigned the second deed of trust to Bank of America, N.A.

In October 2012, Kan filed a quiet title complaint against Guild Mortgage Company and "all persons or entities unknown, claiming any legal or equitable right, title, estate, lien or interest in the property." The complaint alleged, among other things, that the loan under the first deed of trust was securitized, the securitization process was deficient, and therefore the underlying debts had been extinguished as a result of the deficiency. Kan's allegations are based on the fact that the transfer of the promissory notes to a securitized trust did not comply with the terms of the servicing and pooling agreement governing the securitized trust.

The Second District Court of Appeal acknowledged that Kan's argument was not a novel one, and the argument that a defendant lacks standing to foreclose because of an improper securitization process has recently become particularly popular. The argument was addressed in *Jenkins v. JPMorgan Chase Bank, N.A.* (2013) 216 Cal.App.4th 497, 511, and *Gomes v. Countrywide Home Loans, Inc.* (2011) 192 Cal.App.4th 1149, 1154.

The trial court sustained the lender's demurrer without leave to amend. The court of appeal affirmed, holding that a borrower lacks standing to assert a preemptive challenge to the authority of the entity initiating the foreclosure process in a non judicial foreclosure before the foreclosure sale occurs. The Second District held that even if the securitization process was deficient, the parties injured under such a deficiency would be the parties to the servicing and pooling agreement and the third party acquirers of the notes, not the borrower, who was an unrelated third party to the securitization.

- Ms. Chang is a partner in the Pasadena office. Her practice focuses primarily on title insurance issues, real estate litigation, and business litigation. She also has extensive experience defending lenders and servicers against mortgage origination and wrongful foreclosure claims by the borrowers.

A Party Seeking to Defeat the Statute of Frauds Based on Promissory Estoppel Must Allege an Actual Change in Position

By Candie Y. Chang

Jones v. Wachovia Bank (2014) 230 Cal.Ap.4th 935

In *Jones*, the borrowers defaulted on their loan with Wachovia Bank and so the bank initiated foreclosure by recording a notice of default. Although the borrowers and Wachovia subsequently entered into a forbearance agreement, the borrowers failed to bring the loan current. As a result, Wachovia recorded a notice of trustee's sale.

The foreclosure trustee must provide the borrower with written notice of default followed by written notice of sale. (Civ. Code §§2924, 2924.3, 2924b.) The trustee is required to postpone a sale under certain circumstances, including mutual agreement of the trustor and the beneficiary, whether oral or in writing. (Civ. Code §2924g(c)(1)(C).) When the trustee postpones a sale date, it provides notice by public declaration at the time and place last appointed for sale. (Civ. Code §2924g(d).) The public declaration sets forth the new sale date; no other notice of postponement is required.

Here, the trustee's sale was postponed three times. Although the borrowers confirmed the first two postponements with the trustee in a written certificate, the borrowers did not confirm the third postponement date in writing. The borrowers alleged that a Wachovia representative gave them a sale date of June 18, 2009 during a phone call, but the property was actually sold on June 8, 2009.

The borrowers sued Wachovia to set aside the trustee's sale, to cancel the trustee's deed, and for promissory estoppel. Although the borrowers did not have sufficient funds to cure their default, they nonetheless alleged that they detrimentally relied on Wachovia's alleged oral sale date of June 18 because they lost the opportunity to cure their default.

The trial court sustained demurrers to the borrowers' claims to set aside the trustee's sale and to cancel the trustee's deed upon sale, and granted summary judgment in favor of Wachovia on the borrowers' promissory estoppel claims. The borrowers appealed the trial court's ruling on their promissory estoppel claim. The Sixth District of the Court of Appeal affirmed the summary judgment ruling in favor of Wachovia.

The court held that the borrowers failed to establish a triable issue of material fact regarding detrimental reliance or injury under the doctrine of promissory estoppel because the borrowers did not relinquish any legal right in exchange to stay the bank's foreclosure. Therefore, the borrowers could not establish that they substantially changed their position as a result of Wachovia's alleged misrepresentation that the foreclosure was scheduled for June 18, 2009.

The court also rejected the borrowers' claim that they were harmed by Wachovia's verbal representation because they had "arranged with their friend" to pay the entire amount of their loan. Not only was this theory not pleaded in the operative complaint, even if it was, the court held that "An informal agreement to borrow money from a friend is not a change in position, much less a substantial change of position needed to establish an estoppel."

Easements

A Reference to Public Road Purposes In an Easement Does Not Necessarily Create a Public Right-of-Way Over a Reserved Easement

By Scott B. Mahler

***Schmidt v. Bank of America, N.A.* (2014) 223 Cal.App.4th 1489**

The Schmidts owned a parcel of land. On an adjacent parcel to the east, a developer constructed a condominium project that would consist of three condominium buildings abutting the plaintiffs' parcel. The developer financed the project through a revolving credit agreement with Bank of America.

The two parcels were once under common ownership of Rose Miller Parks. In 1941, Parks conveyed a portion of her property, which would later become the Schmidt parcel, to Edith Ford. However, Parks reserved an easement over the portion of the conveyed property adjacent to the property she retained, via a grant deed that stated "RESERVING to the grantor, her successors, assigns and/or heirs, the right of ingress and egress for public road purposes over, along and across the Easterly 40 feet thereof." Four years later, Parks sold her retained parcel, which would become the developer's parcel, to Smith. Parks's grant to Smith stated "ALSO an easement for public road purposes, and incidental purposes, over the Easterly 40 feet of the following described land . . ."

Years later, the developer began construction of the project and completed two condominium buildings. As part of the project, the developer graded and paved the easement area for a private roadway, Troy Lane, that facilitated access from El Cajon Boulevard to a parking garage for the project. At the end of the roadway, the developer installed a locked gate on the Schmidt parcel to prevent traffic from using Troy Lane as a thoroughway between El Cajon Boulevard and Troy Terrace.

After the first phase of the construction, the developer deeded the parcel to the homeowner's association. However, the easement reserved by Parks was not recited in the deed. The developer did not complete the third and final phase of the project because it defaulted on its credit agreement with Bank of America. The bank foreclosed and acquired some of the parcels in foreclosure.

The Schmidts later sued, claiming trespass, nuisance, and injunctive and declaratory relief. They alleged that the construction of the project violated the easement rights and restrictions. Bank of America and the homeowners' association filed a motion for summary judgment, which the court granted.

The appellate court held that the reference to public road purposes in the easement grant did not create a public right-of-way over the reserved easement because the phrase "for public road purposes" reflected the impetus for the reservation and the reason for the right of ingress and egress. It was a qualification of, and limitation on, the right of ingress and egress reserved in the grant. It did not expand the right to include activities other than ingress and egress. Accordingly, the appellate court disagreed with the contention of Bank of America and the homeowners association that the phrase "for public road purposes" created a public right of way over the reserved easement and the trial court erred in its finding on summary judgment. Incidental purposes, which were included unless excepted under Civil Code section 1084, did not qualitatively expand the grant. The appellate court held that whether the improvements unreasonably interfered with a private easement is a question of fact and thus summary judgment was inappropriate.

Railroad Right of Way Under 1875 Act is an Easement Not Fee Title

By Alex Levy

***Brandt Trust v. United States* (2014) 134 S Ct 1257; L.Ed. 2d 272; 2014 U.S. LEXIS 1788**

The question decided by the U.S. Supreme Court in *Brandt Trust v. United States* (2014) was: ". . . what happens to a railroad's right of way granted under a particulate statute - the General Railroad Right-of-Way Act of 1875 - when the railroad abandons it: does it go to the Government, or to the private party who acquired the land underlying the right of way?" The court held that a right of way granted under the 1875 Act is an easement and not a fee, so that upon abandonment the easement no longer burdens the land owner's title. The Court reviewed early railroad grant legislation. In the early 1860's, Congress enacted legislation granting tracts of land in a "checker board" pattern to the railroad companies in order to induce private capital to build the railroads (in this case, in Wyoming). By 1872, public opinion, and therefore legislative intent, had changed. The public and legislature came to resent the give away of rights to the railroad companies and wanted to preserve public lands for settlors. The General Railroad Right-of-Way Act was enacted in 1875.

In 1987, the then owner of the subject right of way notified the Surface Transportation Board of its intent to abandon it. With the Board's approval the ties and tracks were torn up and the abandonment completed in 2004. In 2006, the United States sued the landowners to quiet title to fee title in the abandoned right of way. All of the landowners defaulted or settled, except for the appellant Mr. Brandt, who counterclaimed. The case turned on whether the 1875 Act granted railway companies fee or easement rights only. The Supreme Court held that the United States was bound by the position it had taken in 1942 with regard to the same issue. In *Great Northern Railway Co. v. United States* (1942) 315 U.S. 262, 62 S. Ct. 529, 86 L. Ed. 836, the Government sought to prevent a railroad company from drilling for oil in a right of way. The railroad company claimed it had right to drill, based on a right of way created under the 1875 Act. The Government countered that rights it granted to the railroad companies before 1871 were fee, but that "those granted under the 1875 Act were mere easements." The Supreme Court observed that it had adopted the Government's interpretation of the 1875 Act in *Great Northern* and that it was not about to allow the Government to argue otherwise now. The court then held that the right of way easement having been abandoned in this case, "basic common law principles" dictated that the easement had been extinguished.

The court noted that the Government patent conveying the subject property to the land owner had not reserved any rights created under the 1875 Act. The court rejected the Government's other arguments, *i.e.*, that other statutes and reported decisions support the contention that 1875 Act right of ways are fee not easements.

See Brandt Trust v. United States, continued on p. 18

Appraisal

A Borrower May Not Reasonably Rely On An Appraisal That Its Lender Obtained For Loan Underwriting Purposes

By Scott B. Mahler

***Willemsen v. Mitrosilis* (2014) 230 Cal.App.4th 622**

Plaintiff entered into a contract to purchase 4.83 acres of vacant land. As part of the transaction, plaintiff's lender hired a real estate appraiser to appraise the property as part of its loan underwriting process. The appraisal report stated that the intended users of the report was the lender and the lender's representatives. The report also stated that the intended use of the report was to assist the lender in analyzing a loan for the property. It also stated that the report could not be used for any purpose by any person other than the lender without the written consent of the appraiser.

Plaintiff later sued the appraiser for negligent misrepresentation, contending that the appraiser failed to account for either an earthquake fault line running across the property or the loss of land that would be suffered when a local government entity ran a planned road over the property, and that his reliance on the appraisal was a substantial factor in causing him monetary harm. The trial court granted the appraiser's motion for summary judgment, finding: (1) plaintiff was not the intended beneficiary of the appraisal; (2) plaintiff could not establish that he justifiably relied on the appraisal; and (3) neither the appraiser nor the lender intended the appraisal to influence plaintiff's decision to buy the property.

The appellate court affirmed the trial court's order granting summary judgment. It found that a borrower should be expected to know that the appraisal is intended for the lender's benefit to assist it in determining whether to make the loan, and not for the purpose of ensuring that the borrower has made a good bargain, i.e., not to insure the success of the investment. The appellate court also stated that one who seeks financing to purchase real property has many means available to assess the property's value and condition, including comparable sales, advice from a realtor, independent appraisal, contractors' inspections, and personal observations and opinion. Further, the court held that whether the lender conducts the appraisal in house or hires an outside appraiser, the considerations are the same. The appraisal is ordered by the lender for its own protections and the borrower has his or her own means of ascertaining the desirability of the property.

The appellate court held that while the appraiser may have known that the plaintiff was the borrower, it did not mean that it knew that plaintiff would rely on the appraisal. It also held that the appraiser did not manifest an intent to supply information for the plaintiff's use in determining whether the property was suitable for his purposes. Rather, the appraisal report specifically limited its intended use to the use of the bank.

The appellate court also distinguished *Soderberg v. McKinney* (1996) 44 Cal.App.4th 1760. In *Soderberg*, a mortgage broker obtained an appraisal of certain real property in order to shop a loan to certain deed of trust investors. The court in *Soderberg* found that although the appraiser did not know the identity of any particular investor, the appraiser knew that this group of persons would rely on his report when investing in a deed of trust. The appellate court in *Willemsen*, however, held that there was no indication that the appraiser issued its appraisal report with the knowledge or intent that the plaintiff would rely on it in deciding to purchase the property. Rather, the appraiser knew and intended that the lender would use the appraisal report in determining whether the property had sufficient value to serve as its collateral.

Scott Mahler represented the appraiser parties in this case.

Mortgage Borrowers Are Legally Precluded From Asserting Claims Against Lenders or Appraisers Based on Appraised Values of Homes

By Brian W. Ludeke

***Graham v. Bank of America* (May 23, 2014) 226 Cal.App.4th 594**

In 2004, plaintiff borrowed $391,000 to purchase a home. In the course of underwriting the loan, the lender's appraiser appraised the subject property at $525,000. Plaintiff alleged that the defendants falsely told plaintiff that the amount represented the home's fair market value, that its value was increasing and would continue to do so, and that the home and the loan were good for plaintiff. By 2011, plaintiff was in default on the subject loan, and defendants began foreclosure proceedings by sending plaintiff a notice of trustee's sale.

Consequently, plaintiff sued the defendants, who were all involved in the loan process in some respect, alleging that they engaged in practices that artificially inflated home prices, they knew the appraisal of the subject property was speculative, and they falsely represented the value of the home would appreciate. After defendants demurred, plaintiff filed a similar First Amended Complaint ("FAC"), attaching a copy of a consent judgment entered against lenders, including Bank of America, to settle governmental actions related to their lending, foreclosure, and loan modification practices.

After the trial court sustained the defendants' demurrer to the FAC, plaintiff filed his Second Amended Complaint ("SAC"), which contained causes of action for fraudulent misrepresentation and concealment, Unfair Competition Law ("UCL") violations, legal and equitable relief based on fraud and public policy, and declaratory relief. The trial court sustained defendants' demurrer to the SAC without leave to amend. Plaintiff appealed, and the Court of Appeal affirmed the trial court's ruling, finding plaintiff's allegations were insufficient to establish any of plaintiff's causes of action.

With respect to plaintiff's fraud-based causes of action, plaintiff failed to establish the essential elements of an actionable, factual misrepresentation; his justifiable reliance on the defendants' appraisal; or, causation. First, the court found that all the misrepresentations alleged in the SAC were statements of opinion, not actionable fact. "Statements regarding the appraised value of the property are not actionable fraudulent misrepresentations. Representation of opinion, particularly involving matters of value, are ordinarily not actionable misrepresentations of fact." (Citing *Neu-Visions Sports, Inc. v. Soren/McAdams/Bartells* (2000) 86 Cal.App.4th 303, 308.)

See Graham v. Bank of America, continued on p. 18

Electronic Signatures

Heightened Showing Needed Under Cal. Code of Civ. Proc. § 664.6 for Electronic Signatures on Settlement Agreements

By Brian W. Ludeke

***J.B.B. Investment Partners, Ltd. v. R. Thomas Fair* (Dec. 5, 2014) 2014 Cal.App. LEXIS 1190**

Defendants appealed from a judgment rendered pursuant to the trial court granting a motion under Cal. Code of Civ. Proc. § 664.6 to enforce a settlement between the plaintiffs and defendants. The Court of Appeal reversed, finding the printed name of a defendant at the end of an email purporting to accept a settlement was not a signature under California's Uniform Electronic Transactions Act (UETA).

Defendant Fair owned various entities that were named as defendants and held title to Arizona apartment properties. Plaintiffs invested in those entities and later alleged that Fair had made various misrepresentations. Before plaintiffs filed their complaint, the parties discussed settlement, which led to plaintiffs' counsel sending Fair a July 4, 2013 email that set forth terms of a proposed settlement and demanded that Fair state "I accept" but did not include a signature block or plaintiffs' signatures.

On July 5, 2013, Fair sent an email stating that the facts did not support the plaintiffs' theories, but he stated "I agree." Plaintiffs' counsel demanded that he provide an unambiguous response. After plaintiffs apparently had not received a response from Fair, they filed their complaint and served it upon Fair, who responded the same day with numerous communications questioning why plaintiffs filed their lawsuit after Fair agreed to their terms. Plaintiffs' counsel stated he believed the messages constituted an agreement and that he would begin working on paperwork to confirm the agreement.

On July 11, 2013, plaintiffs' counsel sent a proposed written agreement to Fair, noting it could be signed electronically. Fair later stated he would review the agreement and provide comments and later suggested that he and plaintiffs' counsel meet to discuss plaintiffs' claims. Plaintiffs responded that the case would not be stayed until the written agreement was signed; it never was.

On August 6, 2013, plaintiffs moved, pursuant to Cal. Code of Civ. Proc. § 664.6, to enforce the settlement agreement they contended was created by the July 4 and 5, 2013 communications. In support, plaintiffs submitted those communications and Fair's deposition testimony, in which he admitted that he deliberately typed his name at the end of the July 5, 2013 email. Fair argued, in opposition, that the July 5, 2013 agreement was not a signed settlement agreement and was intended only to indicate that he would work toward a settlement in good faith.

Although the trial court questioned how plaintiffs could contend the communications were a settlement agreement when they subsequently sent a written agreement and asked for Fair's signature, the court granted plaintiffs' motion based on Fair's deliberate typing of his name at the end of the email and his other messages, which the trial court found indicated a meeting of the minds. The plaintiffs and trial court relied heavily on Cal. Civ. Code § 1633.7, which states, in essence, that a contract cannot be found invalid because it was signed electronically.

On appeal, Fair argued that his printed name at the end of the email did not constitute a signature, because the parties had agreed that no settlement existed until a final agreement had been drafted, "signed and delivered by facsimile." He cited the communications that referenced the need for subsequent signatures and noted that, at the time he printed his name at the end of the email, none of the parties had authorized electronic signatures.

The Court of Appeal determined that Civil Code § 1633.7 was not determinative, and the trial court's decision that Fair's printed name constituted his signature was "manifestly erroneous." Although an electronic signature may satisfy requirements for written agreements under UETA, it was necessary to determine whether Fair's printed name was a signature pursuant to Civil Code § 1633.2, which states that an electronic signature can consist of any sound, symbol, or process adopted with the intent to sign an electronic record. Whether the parties agreed to conduct a transaction by electronic means is determined from the context and surrounding circumstances, including the parties' conduct.

The trial court's analysis focus on Fair's admission that he typed his name at the end of the email was too simplistic. Although, in some circumstances, typed names may be electronic signatures, plaintiffs also needed to provide evidence of the parties' conduct and other circumstances showing Fair's intent to sign the electronic record. The court found a lack of evidence of such intent, specifically noting the absence of an explicit agreement to conduct an electronic transaction. Although plaintiffs asked Fair, in the July 4, 2013 email, to indicate "I accept," and Fair typed his name, the court found the parties' other communications indicated only an intent to negotiate a settlement by email, not to finalize and sign such a settlement electronically. The July 4, 2013 email also did not include a request for a signature, a signature block, or plaintiffs' signatures, and plaintiffs' other communications advised Fair that finalizing paperwork was being prepared.

The court further found that subsequent communications between the parties indicated only an agreement with the terms proposed by plaintiffs, as evidenced by plaintiffs' transmission of a draft of a written agreement to Fair on July 11, 2013 and their statements that there would be no stay of the action without a signed deal in place. Unlike the July 4 and 5, 2013 emails, the July 11 agreement had signature lines and invited electronic signatures.

Finally, the court addressed the trial court's finding that the July 5, 2014 email was an enforceable settlement agreement under common law pertaining to contracts that held that typed names on telegraphs were sufficient to satisfy the statute of frauds. The trial court found such signatures analogous to printed names on emails. The Court of Appeal, however, noted there was no authority holding that such "signatures" satisfied the strict requirements of Code of Civ. Proc. § 664.6. Furthermore, even if such authority existed, plaintiffs would still have to prove, and did not do so, that Fair printed his name at the end of the email in question with the intent to authenticate the writing.

Based on the foregoing, the Court of Appeal reversed the trial court's order and the judgment against the defendants.

Mechanic's Liens

Mechanic's Lien Prejudgment Interest Against Successor Owner Is Seven Percent

By Alex Levy

***Palomar Grading & Paving, Inc. v. Wells Fargo Bank, N.A.* (2014) 230 Cal.App.4th 686**

In *Palomar Grading & Paving, Inc. v. Wells Fargo Bank, N.A.* (2014) 230 Cal.App.4th 686, a case of first impression in California, the Fourth District Court of Appeal held that a successful mechanic's lien claimant is entitled to 7%, not 10%, prejudgment interest as against innocent successive owners of the property; that is, owners who take title after the date on which a previous owner entered into the construction contract that gave rise to mechanic's lien claim.

In *Palomar*, plaintiffs were two subcontractors suing, among others, successor property owners, who were not parties to the construction contract. The trial court had awarded 10% prejudgment interest against the successor owners. In reversing the trial court's prejudgment interest award, the Appellate Court reasoned: (1) that the question is whether the 7% default rate under Article XV, Section 1, of the California Constitution for "things in action" applied, or whether the 10% default rate for breaches of contract under Civil Code section 3289(b) applied; (2) that the Constitutional provision applies in both contract and non-contract *e.g.*, tort, actions, unlike section 3289, which applies only in contract; (3) that the "salient fact" in deciding that the Constitutional rate applied was that the successor owners were not parties to the construction contract and were innocent (*e.g.*, they were not colluding with the contracting party); (4) that the imposition of a mechanic's lien arises from statute not contract; (5) that burdening the successor's interest in the land with a mechanic's lien and awarding prejudgment interest is justified because the successor owner has the benefit of the work or materials provided by the mechanic's lien claimant; and (6) that the 7% rate is the rate applied to prejudgment awards in non-contract cases.

The court rejected the plaintiffs' arguments that: (1) a successor owner should not pay less interest than the owner who contracted for the work (but the court stated that, unlike the contracting prior owner, the successor's liability is not voluntarily assumed, and instead is imposed by statute); and (2) for the same reasons, a successor is not bound by the interest rate set forth in the construction contract

Comment: This will be a benefit in the defense of successor owners, reducing any prejudgment award against them from 10% to 7%. Where large damage awards are involved, as in many mechanic's lien actions, the savings to the successor owners would be substantial.

Investment Fraud

Investment Fraud - Lack of Reliance and What Is a Fraudulent Transfer of an Asset.

By Ndubisi A. Ezeolu

***Hasso v. Hapke* (2014) 227 Cal.App.4th 107**

In *Hasso v. Hapke* (2014) 227 Cal.App.4th 107, the California Court of Appeal, Fourth Appellate District, held that hedge fund-related defendants were not liable for a successor trustee's fraud-related claims because even if they had made any material misrepresentations or omissions, and even if the initial trustee had relied thereon, any such reliance would have been unreasonable, considering the initial trustee's financial and business knowledge.

In *Hasso v. Hapke*, a successor trustee brought an investment fraud action and related claims against a hedge fund (Rockwater or RAM Fund), its manager (RMA), the manager's chief executive officer (Bryan Williams), and the fund's chief financial officer (John Hapke) when the trust's fund was devastated by the stock market crash in 2008. A jury awarded the trust a $4,640,380 judgment against Rockwater, RMA, Williams, and Hapke. Rockwater/RAM Fund, RMA, Williams and Hapke appealed, claiming the RAM Fund was simply the victim of the market crash. The trustee also appealed, seeking to hold liable the defendants who "got away" - CFI and Charles Fish, the chairman and chief executive officer of CFI.

In a lengthy opinion, the appellate court affirmed the judgment as to breach of fiduciary duty against those defendants who were investment advisors, but reversed on the actual and constructive fraudulent transfer causes of action as well as for breach of fiduciary duty and professional negligence against some of the defendants "because there is no substantial evidence to show that they were investment advisors within the meaning of Corporations Code section 25009."

The trustee's causes of action for actual and constructive fraudulent transfer were based on the unwinding of a contribution agreement between CFI, Fish, RMA, and Rockwater CFI, LLC, a wholly owned subsidiary of RMA. He claimed that the management of investor assets was collusively transferred "back to CFI" upon a premature unwinding of the contribution agreement, and that the creditors of RMA were thereby denied an income stream upon which to levy. The jury found that RMA and Williams were liable on both the actual and constructive fraudulent conveyance causes of action, but that CFI and Fish were not liable on either cause of action. The appellate court held that the finding of liability as to RMA and Williams was unsupported by the evidence.

The assets transferred to CFI upon unwinding were the same assets it had transferred to RMA: the CFI investor account portfolios. What was transferred, the appellate court found, was the right to manage those accounts and to enjoy the management fees generated from those accounts. At issue, the appellate court found, was whether such property constituted an asset within the meaning of the Uniform Fraudulent Transfer Act (UFTA).

See Hasso v. Hapke, continued on p. 16

Deficiency Judgments

A Lender May Not Intervene in a Borrower's Tort Action to Seek Additional Recovery After a Non-Judicial Foreclosure Unless The Deed of Trust Specifically Provides for Such Recovery

By Jennifer R. Slater

***Thoryk v. San Diego Gas & Elec. Co.* (2014) 225 Cal. App. 4th 386**

Thoryk owed farmland with avocado orchards subject to a first deed of trust held by PFI and a second deed of trust held by Highland.

In 2007, the property suffered major damage from a wildfire allegedly caused by several third parties including defendant San Diego Gas & Electric.

In 2008, Highland foreclosed on the property acquiring title by a partial credit bid. One year later, Thoryk sued the third parties for negligence and inverse condemnation. In 2010, PFI foreclosed on the property and acquired title by a full credit bid. PFI and Highland sought to intervene into Thoryk's tort action seeking imposition of a lien on any judgment he may obtain against the third parties. The trial court refused to allow PFI to intervene holding that its full credit bid eliminated any claim it could make for additional recovery. However, the trial court permitted Highland to intervene and Thoryk appealed.

The appellate court reversed the trial court's decision holding that the general granting language in the deed of trust stating "all other rights, royalties and profits relating to the real property" was not sufficient to create a security interest in the after-acquired tort claims where there was no express language in the deed of trust pertaining to these claims. The appellate court held that Highland had no basis for seeking proportional equitable conversion damages because as a result of its non-judicial foreclosure, the subject land was no longer at issue. Moreover, the appellate court held that because tort claims do not constitute additional security or substitute security, a lien on such tort claims is tantamount to an impermissible deficiency judgment.

Lender's Failure to Obtain All Borrowers' Consent To Release Encumbered Property Constitutes a Waiver of Lender's Right to a Deficiency Judgment Under CCP 726(a)

By Jennifer R. Slater

***First California Bank v. McDonald* (2014)**

In March 2009, husband and wife John and Sally DeVincenzo signed a five-year promissory note for a $1,509,000 loan issued by First California Bank ("Bank"), secured by a deed of trust for property in Wasco, California. Under the terms of the note, monthly installment payments were to be made with a final balloon payment due in April 2014. Upon their default, the Bank could accelerate the note and declare all monies immediately due and payable. As additional security for the loan, Sally signed a deed of trust encumbering her own separate property located in Shafter, CA. Sally later sold the Shafter property and requested the Bank agree to the sale, which it did with the understanding that it would receive the net proceeds and Sally and John would not be released from liability.

John died in September 2009 and his children were appointed personal representatives of the estate. The note went into default in December 2009 and the Bank declared all sums due and payable immediately, including interest and late charges.

In November 2010, the Bank sued for judicial foreclosure on the Wasco property and for a deficiency judgment against Sally and the personal representatives of John's estate. In March 2013, the trial court granted the Bank's motion for summary adjudication as to the third cause of action for judicial foreclosure.

In June 2013, the trial court signed and filed a formal order, decree for judicial foreclosure and order for writ of sale. The decree stated the appellants were liable for the debt and a deficiency judgment could be entered against them in an amount to be determined after the sale of the Wasco property.

The appellants appealed and relied upon the court's holding in *Pacific Valley Bank v. Schwenke* (1987) 189 Cal.App.3d 134 to support their argument that the security first principle in section 726(a) bars any liability for a deficiency because the Bank, without their consent, released part of the security for the note when it allowed Sally to sell the Shafter property in a private sale. The appellate court agreed with appellants and reversed the trial court's grant of summary adjudication and issuance of the related decree and writ holding that based on the language of section 726, the Bank was required to include both the Wasco and Shafter properties in its judicial foreclosure action unless it could show that all of the debtors consented to the release of the Shafter property as security for the loan. The appellate court held that Bank's release of the Shafter property without appellant's consent would operate as a waiver of the Bank's right to a deficiency judgment under section 726(b) unless the judgment for any deficiency as waived by the judgment creditor. The appellate court further held that appellant's consent to release the Shafter property is a material fact for purposes of summary adjudication. Accordingly, the appellate court remanded the case to the superior court with directions to enter a new order denying the motion for summary adjudication.

California Supreme Court Declines to Review or Depublish Appellate Decision Granting a Broad Exception to the Legislature's Regulation of CC&R Transfer Fees

By Ryan C. Squire

The CLTA recently asked the California Supreme Court to review and depublish a decision issued by the California Court of Appeal in December 2014: *Marina Pacifica Homeowners Assn. v. Southern California Financial Corp.*(2014) 232 Cal. App. 4th 494.

This is an important case for title insurers, title companies, and escrow companies, as well as buyers and lenders. The net effect of the holding appears to be as follows: A "transfer fee" may be enforced against title even if relevant information concerning the fee (such as its existence and amount) is not identified in a recorded document, so long as a recorded document refers to an unrecorded document that identifies the fee.

Marina Pacifica concerned "transfer fees" governed by Civil Code section 1098, et seq. "Transfer fees" are fees that are imposed by a developer or builder during the initial sale-outs, which then must be paid during subsequent transfers of title. Such fees can generate income for builders/developers long after they no longer hold any interest in the subject property.

Marina Pacifica involved a 570-unit waterfront condominium complex in Long Beach built in the 1970s. Title to each unit was held via a leasehold. Unit "owners" acquired their interests by way of assignments of the leaseholds. The leases required the unit owners to pay an "assignment fee" imposed by the developer in the 1970s. This fee was nominal ($13-$35 per month) until 2006, when it increased substantially (in 2006, the fee began to be based on a percentage of the value of each unit—4% per annum).

Some states have banned such fees. California has not. Instead, in 2008, the California Legislature enacted legislation regulating these fees. The CLTA was active in advocating this legislation, which defined a "transfer fee" as "any fee payment requirement imposed within a covenant, restriction, or condition contained in any deed, contract, security instrument, or other document affecting the transfer or sale of, or any interest in, real property that requires a fee be paid upon transfer of the real property." (Civ. Code §1098.)

The Legislature recognized that such fees were often buried in lengthy and arcane CC&Rs, and realized that many buyers, lenders, title companies, and other interested parties do not discover these fees until it is too late. The Legislature sought to avoid these problems through a two-pronged approach:

(1) by requiring the recipient of the fee to record a stand-alone document concerning specific information about the fee — which the public, lenders, escrow companies, title companies, title insurers, and other interested parties could find (Civ. Code, §1098.5), and

(2) by requiring the seller of property to give the buyer a *separate* disclosure statement — ensuring notice to the buyer (Civ. Code, §1102.6e).

The *Marina Pacifica* court agreed that the assignment fee at issue fell within the general rubric of a "transfer fee," but relied on what it termed the "substantial compliance exception" to hold that the statutory scheme did not apply. That exception states, "A transfer fee does *not* include any of the following: ... (i) Any fee reflected in a document recorded against the property, that is separate from any covenants, conditions, and restrictions, and that substantially complies with subdivision (a) of Section 1098.5 by providing a prospective transferee notice of the following: (1) Payment of a transfer fee is required. (2) The amount or method of calculation of the fee. (3) The date or circumstances under which the transfer fee payment requirement expires, if any. (4) The entity to which the fee will be paid. (5) The general purposes for which the fee will be used." (Section 1098, subd. (i), italics added.)

Because a fee that falls within this exception is by definition not a "transfer fee," it is *not* subject to the recording and disclosure requirements of sections 1098.5 and 1102.6e, respectively.

No single recorded document identified the condominium "assignment fee" or the items required under Section 1098, subdivision (i). Nevertheless, the court held that a "fee reflected in a document recorded against the property" as used in the exception includes a fee detailed in an *unrecorded* document that is *mentioned* in a recorded document. Thus, because some recorded documents "incorporated the unit lease[s] by reference," and because the unrecorded leases identified all required criteria, the fee recipient was not required to record a "separate document" under section 1098.5. The court cited law holding that persons are on inquiry notice of matters referred-to in recorded documents. The court also based its holding on the fact that buyers had received an unrecorded "information sheet," which, in the court's view, identified the criteria required by subdivision (i).

The CLTA asked the Supreme Court to review and depublish *Marina Pacifica*, believing the decision was erroneous on several grounds, including: (1) the Legislature mandated that the required criteria be set-forth in a single, stand-alone recorded document so that buyers, lenders, title companies, and other interested parties would not need to hunt through recorded and unrecorded documents to locate information concerning transfer fees; (2) the fact that buyers received an unrecorded "information sheet" did not excuse the requirement of a stand-alone *recorded* document, because the Legislature mandated that buyers be given a transfer disclosure statement concerning a transfer fee *in addition* to requiring recordation of a separate stand-alone document; and (3) as a general proposition, persons are on inquiry notice of matters mentioned in recorded documents, but that rule does not apply where, as here, the Legislature mandates a separate recorded notice.

On March 11, 2015, the California Supreme Court denied review and declined to depublish, leaving the decision in *Marina Pacifica* intact.

Ryan Squire, Esq. of Garrett & Tully, P.C. in Pasadena, California, represented the CLTA in the California Supreme Court.

- Mr. Squire's practice includes real estate litigation, title insurance claims, title insurance bad faith lawsuits, business disputes, general and professional liability litigation, and intellectual property litigation. Mr. Squire also heads the firm's civil appellate practice and he is a certified specialist in appellate law through the State Bar of California Board of Legal Specialization.

Breach of Guaranty

Summary Adjudication of Lender's Breach of Guaranty Claim is Appropriate Where Borrowers Fail to Provide Admissible Evidence of Sham Guaranty Defense

By Jennifer R. Slater

***California Bank & Trust v. Lawlor* (2013) 222 Cal.App. 4th 625**

Defendants/appellants Smith and Lawlor were real estate investors and developers who created several entities along with Smith's wife for their development projects. Alliance made a $2 million loan to one of their entities, Cartwright Properties ("Cartwright") in December 2004 and a second loan of $1.4 million in October 2006. Cartwright signed a business loan agreement, commercial security loan agreement and promissory note for each loan. As security for the loans, Cartwright executed trust deeds for its office building. Smith, his wife, and Lawlor were required to execute separate commercial guarantees for each loan and their entity, Covenant Management, had to execute a commercial guaranty for the second loan.

In June 2008, Alliance loaned $10.5 million to Heritage Orcas Partners ("Heritage"), another one of Smith and Lawlor's entities. In connection with this loan, Heritage was required to execute a business loan agreement, a promissory note and a trust deed on two parcels of real property.

After California Bank & Trust ("CA B&T") acquired Alliance's assets from the FDIC in February 2009, Cartwright and Heritage defaulted on their loans and Smith, his wife and Lawlor refused to pay their guarantees. CA B&T filed a lawsuit against Cartwright, Smith, his wife, Lawlor and Covenant Management to recover on the loans to Cartwright, judicially foreclose on the secured property and to enforce the commercial guarantees. CA B&T filed a second lawsuit against Heritage seeking the same relief.

In the first half of 2011, CA B&T non-judicially foreclosed on the trust deeds securing both the Cartwright and Heritage loans. CA B&T purchased the Cartwright and Heritage properties for credit bids that left outstanding balances of nearly $2 million and more than $13 million, respectively.

CA B&T moved for summary adjudication in July 2012 on the guaranty claims seeking to recover deficiency judgments for the balance of all loans. Defendants Smith, Smith's wife and Lawlor did not dispute that they signed the guarantees or the balances due, but rather claimed they were sham guaranties and their relationships with Cartwright and Heritage made them primary obligors on the loan, not true guarantors. Accordingly, they claimed to be protected by California's anti-deficiency statutes precluding CA B&T from obtaining a judgment for the difference between the loan balance and the value of the security. Defendants' opposing evidence consisted of declarations to show: (1) the principal purpose of each entity was to hold title to property; (2) the entities had no other business activities; (3) the defendants were the only members, managers and owners; (4) Alliance required extensive financial information from defendants prior to issuance of the loans; and (5) Alliance relied on this information to issue the loans. The trial court sustained CA B&T's evidentiary objections to the declarations finding they were irrelevant, conclusory, lacked foundation and were barred by the secondary evidence rule. The trial court then granted CA B&T's motions finding defendants could not create a triable issue of material fact because they failed to allege the sham guaranty defense as an affirmative defense in their answers.

The appellate court affirmed the trial court's grant of summary adjudication noting first that defendants did not challenge any of the trial court's evidentiary rulings, resulting in the appellate court's exclusion of the defendants' evidence. In affirming the trial court's decision, the appellate court found that defendants had failed to present sufficient evidence to create a triable issue of material fact with respect to their sham guaranty defense. Specifically, the appellate court found that the defendants had presented insufficient evidence to show: (1) there was no legal separation between them and the primary obligors on the loan; and (2) their entities were not properly formed. Furthermore, the appellate court opined that it was not unusual for banks to require financial information from a person or entity guaranteeing a loan.

Shades of the Initial Transferee: Bankruptcy Fraudulent Transfers and the Pure Dominion Rule

By Tomás A. Ortiz

***In re The Mortgage Store, Inc.*, 2014 Westlaw 6844630 (9th Cir. 2014)**

In an appeal of a fraudulent transfer adverse proceeding filed in connection with a Chapter 7 bankruptcy, the Ninth Circuit Court of Appeals has held that an "initial transferee" of a fraudulent transfer made by an insolvent corporation was strictly liable under the "pure dominion" rule, even though the debtor corporation's insider was the party who exercised control over the funds and even though the recipient of the money was unaware of its sources.

The owner of a shopping center entered into a $3 million sales agreement with an individual buyer, under which the buyer would provide the owner with $300,000 in "earnest money" and would execute a promissory note for the balance, secured by a mortgage in favor of the seller. The "earnest money" was to be funneled through an attorney, acting on behalf of both the seller and buyer.

What the seller did not know was that the buyer himself did not provide the "earnest money." Instead, the money came from a separate corporation controlled by the buyer. At the time, the corporation was experiencing financial trouble.

Less then two years later, the corporation filed a Chapter 7 petition. The trustee sued the seller for recovery of the earnest money as a fraudulent transfer under § 548(a) (the bankruptcy "fraudulent transfer" code section). The trustee alleged that the corporate debtor received no value in exchange for the payment and that the seller was the "initial transferee" of the earnest money payment. Under 11 U.S.C. § 550(a)(1), the "initial transferee" is strictly liable for the receipt of a fraudulent transfer and cannot interpose a "good faith" defense under § 550(b). The trustee moved for summary judgment. The bankruptcy court ruled in favor of the trustee, as did the District Court.

The Ninth Circuit affirmed. The seller argued that the buyer himself was the actual "initial transferee." In support, the seller cited *In re Presidential Corp.,* 180 B.R. 233 (9th Cir. BAP 1995) which stood for the proposition that a party should be deemed the initial transferee when another party receives and distributes funds on the first party's behalf. The court disagreed with the holding in *Presidential* because it relied on the "flexible 'dominion and control'" test; instead, the court held the "pure dominion" test articulated in *In re Incomnet,* 463 F.3d 1064 (9th Cir. 2006) the better test – "[T]he touchstones in this circuit for initial transferee status are legal title and the ability of the transferee to freely appropriate the transferred funds."

Accordingly, the court held that the individual buyer never had legal title to the funds in question. Moreover, the use of the attorney as escrow agent played a part – according to the court "because the conditions precedent for the contract's consummation had been satisfied by the time [the insolvent corporation] transferred the funds to the [the attorney], [the buyer] had no right to control their distribution."

The seller also argued that imposing strict liability on a completely innocent party was an inequitable and harsh result. The court seemed to recognize this fact, but still was not swayed by the argument.

Instead, the court reasoned that "[i]n virtually every case involving the bankrupt entity, a third party will be injured because the debtor's obligations to creditors, by definition, outstrip its assets . . . injury must fall on either the transferee of the conveyance or the debtor's creditors . . . the aim of §550 . . . must be to allocate risk such that the parties tending to have the lowest monitoring costs must bear the costs of a debtor's failings." The court went further, "initial transferees tend to have relationships and influence with the debtor . . . by placing the risk on initial transferees rather than creditors, Congress ensured that creditors "need not monitor debtors so closely . . . making businesses more productive."

The court explained that the seller was not helpless to protect itself against the risk of fraudulent transfer liability:

"Although [the seller] asserts it did not have direct contact with the debtor until well after the transfer, [the seller] was represented by counsel in the transaction and entered a contract that allowed [the buyer] to satisfy his obligations under the contract through a third party. In doing so, [the seller] assumed the risk that [the buyer's] obligation would be satisfied through an avoidable conveyance."

The court also suggested the somewhat unworkable solution that "conveyance recipients could hold cash reserves or obtain liability insurance to hedge against the possibility of a fraudulent conveyance."

It is a truly remarkable result underscoring the not always fair or equitable side of bankruptcy.

- Mr. Ortiz is a partner in the Pasadena office. His practice focuses primarily in the areas of bankruptcy and complex real estate litigation. He is managing partner of Garrett & Tully's bankruptcy practice group, which represents and consults real estate clients in connection with bankruptcy issues and proceedings.

Supreme Court Round Up – Third Time Is a Charm For Stern and Article III Limitations on Bankruptcy Courts

By Tomás A. Ortiz

For the third time in four years, the Supreme Court recently heard argument on the issue of Article III limitations on bankruptcy courts. It all started with *Stern v. Marshall* and continued with the Court's decision last spring in *Executive Benefits Insurance Agency v. Arkison.*

In *Stern v. Marshall*, the Supreme Court introduced the concept of an "unconstitutional core proceeding." A proceeding that may be "core" by Bankruptcy Code standards, but one that the bankruptcy court does not have authority to rule on constitutionally. The case involved a state law counter claim filed by the debtor in an adversary proceeding filed against the debtor. The Court ruled that although the counter claim was "core" by statute, the bankruptcy court did not have the authority constitutionally to enter a final judgment on the counter claim.

The *Stern* decision was widely viewed as limiting bankruptcy court authority and the debate in the years that followed has been how broadly the decision should be read or construed.

The Court's decision in *Executive Benefits Insurance Agency v. Arkison* did little to shed light on the debated issue. Instead, the Court's decision focused more on the process by which district courts supervise the adjudicative proceedings of the bankruptcy court. To some, it was a punt on fourth and one.

Less than a year later, the Court faces another "fourth and one" in *Wellness International Network v. Sharif.*

The dispute is a perfect illustration of the difficulty of the Court's existing doctrine. Wellness, a creditor in the bankruptcy of Sharif, filed a motion arguing that Sharif should be denied his discharge. Wellness pointed to several million dollars of assets, previously listed on loan applications by Sharif, but remarkably missing from the estate and Sharif's schedules. Wellness wanted the bankruptcy court to rule that the assets belonged to Sharif, which would both justify denial of a discharge and make the assets available to pay the debt owed to Wellness.

The question before the Court is whether Wellness' claim can constitutionally be heard and adjudicated by the bankruptcy court. On the one hand, Wellness argues that the ownership of property and the determination of whether an asset is part of the bankruptcy estate is at the core of the bankruptcy power. On the other hand, Sharif argues it is a purely state-law claim. He argues the assets are held by a trust, which makes Wellness' claim really a claim to extinguish the interest of a third party in those assets.

Also at issue is whether Sharif's protracted litigating can be treated as an implied consent to the bankruptcy court's jurisdiction.

Only time will tell how significant this case will be, but the expectation is that the Court's decision could be the game changer *Executive Benefits* was not.

See Supreme Court Round Up, continued on p. 16

The Code "Giveth and Taketh" Away - a Bankruptcy Trustee's Powers Are Not Limitless

By Tomás A. Ortiz

***In re Kenny G Enterprises, LLC*, 512 B.R. 628 (C.D. Cal. 2014)**

A buyer and his family purchased a residential property in California from a LLC. At the time of the purchase, the LLC was a Chapter 11 debtor with a confirmed plan. Per the confirmed plan, the property vested back to the debtor. The buyer purchased the property for $3.2 million – the listed and appraised price.

Unbeknownst to the buyer, the selling LLC had represented to the bankruptcy court before confirmation that the value of the property was only $1.2 million. The plan was confirmed based in part on that value as creditors agreed (or were forced to agree) to accept pennies on the dollar over the life of the plan. Under the plan, the LLC would rent the property, using the income to pay the estate's creditors. The plan did not authorize the sale of the property, but it also did not bar it, and it clearly vested the property back to the LLC upon confirmation.

Four months after confirmation, the sale to the buyer closed. $1.3 million of the sale proceeds went to pay off the only then existing secured creditor, with the remainder going to the LLC. The LLC, however, rather than pay off the creditors per the terms of the plan, purportedly absconded with the remainder of the sale proceeds – transferring the funds to several other "insider" entities. Certain creditors balked, the court converted the proceeding to a Chapter 7 and a trustee was appointed.

The trustee sued the buyer for recovery of the residential property. The central allegation was that the sale was a fraudulent transfer. The trustee sought to avoid the sale under Section 544(b) and California Civil Code section 3439.04.

Section 544(b) gives the trustee the authority to pursue fraudulent transfer claims otherwise available to existing creditors under state law. ***[T]he trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim.***

The buyer moved to dismiss the adversary proceeding on several grounds, including that Section 544(b) was only available to avoid pre-petition transfers. Although there was a split of authority, the majority of cases (and several treatises) agreed with that position. Unfortunately, the 9th Circuit had not ruled on the subject.

The bankruptcy court denied the motion on the section 544(b) issue. Although it acknowledged the long line of authorities and treatises, the court reasoned that none of the cases were very detailed in their analysis and that the few that did go through some explanation also involved the applicability of Section 549, which specifically addresses post-petition transfers. Section 549 could not be applied in this case because the code section is specific to "property of the estate." The home was not property of the estate having vested back to the debtor before the sale. The bankruptcy court concluded that the trustee had no other recourse – Section 544(b) should therefore apply.

The buyer appealed to the district court. **The district court reversed the bankruptcy court ruling.**

See The Code "Giveth and Taketh," continued on p. 16

The Code "Giveth and Taketh," continued from p. 15

The court agreed that the language of Section 544(b) was ambiguous as to the temporal context of the statute, but recognized that its "sister" subsection, Section 544(a), clearly applied to pre-petition transfers with language such as "transfer of property of the debtor" and "as of the commencement of the case." It would be "strange drafting" to have these two subsections have different temporal limitations. Otherwise, one would expect Section 544(b) would have been set out on its own, like Section 549.

"[S]ince the strong-arm powers exist at the commencement of the case, and since § 544(a) is limited to 'any transfer of property of the debtor,' these powers could only ever apply to prepetition transfers . . . Congress necessarily understood the transfer to be the debtor's own property, *i.e.*, not property of the estate."

The court recognized that the case presented a "Frank-Abagnale-esque transfer that escapes the trustee's reach," but reasoned that the trustee's avoidance powers were specifically vested and conscribed by Congress. A trustee's powers under the Code are broad, but they are not unlimited. A single creditor might be able to sue to avoid certain transactions under state law, that does not necessarily mean the trustee can do the same.

"Congress may well recognize the window it has left open in a case like this one and enact a statute to close it." Limiting Section 544(b) may "take one arrow out of the trustee's quiver, but it does not leave a trustee powerless to deal with misbehavior."

Mr. Ortiz represented the buyer in the trustee's adversary proceeding and on the subsequent appeal.

Supreme Court Round Up, continued from p. 15

The Other Supremes – Lien Stripping in Chapter 7

In late 2014, the Supreme Court granted petitions for certiorari on two cases – *Bank of America v. Calukett* and *Bank of America v. Toledo-Cardona* – involving mortgage lien stripping in bankruptcy. In both cases, now consolidated by the Court, the inquiry will be whether a "strip off" of a mortgage is to be barred in the same way that a "strip down" already is under the Court's ruling in *Dewsnup v. Timm*.

In Calukett and Toledo-Cardona, Florida home-owners filed for bankruptcy under Chapter 7. Each had a first and second mortgage on their homes. The second in both cases was held by Bank of America. Both debtors ask to have their respective seconds avoided noting that their homes had lost so much value that even the first mortgages involved debts beyond the value of the property. Bank of America took both cases to the Supreme Court arguing that the "strip off" of lower ranking liens is no more allowed than a "strip down."

RNT Holdings, continued from p. 3

4. RNT's claim was also excluded under Exclusion 3(a) of the title policy which precludes from coverage "[d]efects, liens, encumbrances, adverse claims, or other matters [¶] (a) created, suffered, assumed, or agreed to by [RNT]" because, even assuming that there was a title defect, RNT, through its agent Tregub, created the circumstances which lead to the defect. The court of appeal held that Exclusion 3(a) applies where the conduct was "intentional and deliberate" even if there was no intent to create a defect, or knowledge that a defect may occur. (*RNT Holdings*, at p. 1300.)

Hasso v. Hapke, continued from p. 10

CFI and Fish argued that CFI's option to unwind the contribution agreement and receive a return of its assets was tantamount to a lien against those assets. As a result, the property returned to CFI at the time of unwinding did not constitute an "asset" within the meaning of the UFTA because it was subject to a lien. The court agreed. When CFI entered into the transaction with RMA, it contributed its assets in exchange for an ownership interest in RMA coupled with a right to a return of assets if the value of its ownership interest in RMA was compromised. It clearly had a documented right, supported by consideration, to seize those assets, a right that predated both the financial calamity that gave rise to this lawsuit and the lawsuit itself. CFI's right to the return of its assets constituted a lien. Because property subject to a valid lien does not constitute an "asset" within the meaning of Civil Code section 3439.01(a)(1), and a "transfer" within the meaning of section 3439.01(i) means the transfer of an asset, there was no transfer, and thus no fraudulent transfer, for purposes of the UFTA.

The appellate court also reversed to the extent the judgment was against any of the defendants for fraud by intentional misrepresentation, concealment or negligent misrepresentation, stating that even if the defendants "had made any material misrepresentation or omissions, and even if the initial trustee of the trusts had relied thereon, any such reliance would have been unreasonable." The record failed to show any misrepresentations either to the trustee who made the investments or to the trust family member who was present when Hapke and Williams met with the trustee to tell him about the RAM Fund. The closest thing the court found to a misrepresentation was Williams's and Hapke's expression of opinion that the investment was low risk and suitable for the trusts, and the puffery that the most money that could be lost was 10 percent "if the world fell apart." Given the trustee's assertion that he was a "very, very successful" businessman who was familiar with financial and business analysis, as well as his stated acknowledgement that he knew there was a possibility the entire investment could be lost, the suggestion that he could have reasonably relied on Williams's and Hapke's "10 percent" puffery was untenable.

Rundgren v. Washington Mutual Bank, continued from p. 23

The Ninth Circuit affirmed, holding that the district court lacked jurisdiction to hear the Rundgrens' fraud claims. The appellate court concluded that the claims in the Rundgrens' complaint were "claims" for purposes of section 1821(d)(3)(D) and that their claims "relate to any act or omission" of WaMu. Further, the appellate court continued, it is established that the FIRREA bars judicial review of any non-exhausted claim, monetary or nonmonetary, which is susceptible to resolution through the FIRREA claims procedure. The Rundgrens provided no reason for the court to believe that FIRREA exhaustion would have been futile or that their claims were otherwise not susceptible of resolution through the FIRREA's administrative procedure.

Security Service v. First American, continued from p. 4

The district court also held that First American Title Insurance Company did not have a duty to obtain the FPR or to disclose the lack of a FRP because a title policy is not a representation of title, title policies are contracts of indemnity, not of guarantee, and "A title insurer contracting at arm's length is free to disclose absolutely nothing about even the most defective title ... " (*Id.* at p. *8.)

Finally, the district court held that Security Services's fraud claims were barred by the three year statute of limitations under Civil Code § 338(d). Because the title policies were issued over three years before Security Service filed its lawsuit, it was required to produce "facts to show that [the plaintiff] is not at fault for having failed to discover the fraud sooner." (*Id*. at p. *14, citing *Shapiro v. Equitable Life Assurance Soc. of U.S.* (1946) 76 Cal.App.2d 75, 88.) Security Service failed to present any evidence of when its predecessor-in-interest (the party alleged to have been defrauded by the non-disclosure of the lack of a FRP) discovered the purported fraud. (*Id.*)

Security Service appealed to the Ninth Circuit Court of Appeals. The Ninth Circuit affirmed the district court, finding that "Security Service concedes that it holds unchallenged title to the lots, but maintains that title to each of the lots is not "saleable" without an FPR, and therefore is unmarketable. The lack of a FPR and the need to comply with the SLA before selling the lots individually are matters affecting the marketability of the property, not the marketability of the title. (*Security Service, supra*, 585 Fed.Appx. at p. 591.)

Ryan C. Squire, and Zi C. Lin of Garrett & Tully represented First American in this case. Mr. Squire and Mr. Lin also represented the California Land Title Association as amicus curiae in the Dollinger appeal.

Robinson v. Am. Home Mortg. continued from pg 5

In *Robinson*, several federal lawsuits challenging MERS were consolidated and transferred to a Multidistrict Litigation Court ("MDL Court") in the District of Arizona. The plaintiffs, who reside in Arizona, California, Nevada, Oregon, and South Carolina, filed a "consolidated amended complaint" against financial institutions who are involved with MERS. The complaint was dismissed with prejudice by the MDL court, and the plaintiffs appealed.

The Ninth Circuit Court of Appeals ruled as follows:

1. Count I for damages and declaratory relief under Arizona's false document statute, Ariz. Rev. Stat. § 33-420. The complaint alleges that defendants filed foreclosure documents, such as notices of trustees sale, which were not properly notarized and "robosigned" with forged signatures. The Ninth Circuit reversed the MDL Court, holding that the false document statute applied to foreclosure documents, and that plaintiffs could go forward with this claim.

2. Count II for wrongful foreclosure in violation of Arizona, California, and Nevada law. Plaintiffs claim that the MERS System impermissibly "splits" ownership of the promissory note from the deed of trust. The Ninth Circuit affirmed the dismissal of this count, holding that the plaintiffs failed to show a lack of default, did not tender the amount of outstanding indebtedness, or an excuse from the tender requirement.

3. Count III for violation of Nev. Rev. Stat. § 107.080, which specifies procedures for nonjudicial foreclosures, and that a trustee's sale may be set aside for lack of compliance. Plaintiff alleged that once MERS is designated as a beneficiary, the promissory note and the deed of trust is "irreparably split" and MERS cannot initiate foreclosure proceedings. The Ninth Circuit affirmed the dismissal of this count, as MERS has authority under Nevada laws to make assignments to "reunify" the deed of trust and the promissory note.

Although *Robinson* gives some guidance as to what claims may be maintained against MERS, this issue is far from settled.

Graham v. Bank of America, continued from p. 8

Similarly, the court found that the other alleged representations by defendants regarding the increasing value and suitability of the property and/or loan for plaintiff were not actionable misrepresentations, but rather "opinions or predictions about future events."

Next, the court addressed plaintiff's lack of justifiable reliance, finding that "[a]n appraisal is performed in the usual course and scope of the loan process to protect the lender's interest to determine if the property provides adequate security for the loan. Since the appraisal is a value opinion performed for the benefit of the lender, there is no representation of fact upon which a buyer may reasonably rely." The court further stated, "[w]hile it is foreseeable the appraisal might be considered by plaintiff in completing the loan transaction, . . . the borrower should be expected to know that the appraisal is intended for the lender's benefit to assist it in determining whether to make the loan, and not for the purpose of ensuring that the borrower has made a good bargain . . ." (Citing *Nymark v. Heart Fed. Savings & Loan Assn.* (1991) 231 Cal.App.3d 1089, 1099.) A borrower like plaintiff has access to information to allow him to rely on his own judgment or risk assessment.

Furthermore, the court found that plaintiff could not demonstrate causation, as there was an insufficient nexus between defendants' alleged misrepresentations and the alleged harm therefrom. Regardless of the source of loans during the relevant time period, the decline in the overall market meant that borrowers would suffer losses in the value of their homes. Moreover, plaintiff did not allege he could have obtained a better loan from another lender absent the alleged misrepresentations, and the risk of foreclosure was due to plaintiff's default, not any acts or omissions by defendants.

Next, the court found plaintiff's UCL cause of action failed because he had not established any unlawful or unfair practices by defendants and could not show any misrepresentations, his reliance thereon, or causation of his alleged damages. The court noted there were three types of UCL claims—unlawful, unfair, or fraudulent business practices—and found plaintiff could not establish any of them.

First, a predicate to an action based on unlawful business practices claims is a showing that a defendant's practices violate rules, laws, or regulations. Plaintiff failed to allege such a violation. He alleged defendant's appraisal was calculated to render the highest fair market value in their appraisal, not the most probable one, which plaintiff alleged violated Federal law, but that allegation, in fact, constituted an admission that the appraisal was within the range of the fair market value of the home.

Second, unfair business practices claims require a showing that a defendant's conduct is tethered to an underlying constitutional, statutory, or regulatory provision or that it violates anti-trust law. Plaintiff's allegations that the defendants contributed to the artificial inflation of real estate values through speculative appraisal methods to support unreasonable loans that were harmful to consumers and provided defendants with an unfair windfall failed to fulfill the foregoing requirements.

Third, a fraud-based UCL claim is stated where members of the public are likely to be deceived by defendants' conduct, and plaintiff establishes defendant's duty to disclose, as well as actual reliance on the defendants' conduct or statements. Here, the defendants did not undertake any duty to disclose related to appraisals performed on behalf of lenders, nor did they guarantee the success of investments by borrowers like plaintiff.

The court further found that, even if plaintiff had been able to establish a UCL violation, he lacked standing to bring such claims, because he could not establish a causal link between defendants' alleged conduct and his alleged harm. The value of his home declined with the rest of the housing market; he would have incurred the same fees and costs with any other lender; and, the foreclosure of his home was the result of his default, not defendants' conduct.

Finally, plaintiff's declaratory relief cause of action failed, because he could not establish the existence of a justiciable controversy. Plaintiff sought declarations that defendants failed to comply with the consent judgment/settlement and should, therefore, refinance his loan on more favorable terms and that the defendants' note and deed of trust were not enforceable because the loan agreement was unconscionable. With respect to plaintiff's first argument, the court found that individual borrowers like plaintiff were only incidental beneficiaries of the settlement and consent judgment, which did not permit third-party suits to enforce it.

Next, the court found that the loan agreement was not unconscionable. Plaintiff could have simply chosen not to sign the agreement or could have chosen another lender. Furthermore the terms of the agreement did not "shock the conscience." Although plaintiff alleged that the interest-only and adjustable rate features of the loan were unfair, the court noted that such terms are commonly offered and thus not improper or predatory.

Because plaintiff failed to establish any of his causes of action, and because, after three tries to do so, there was no indication that he would be able to remedy the deficiencies in the SAC, the Court affirmed the trial court's order sustaining defendants' demurrer without leave to amend.

Brandt Trust v. United States, continued from p. 7

The court concluded its discussion with the observation that it was ironic that the Government was relying on Sections 43 USC 912 (Disposition of abandoned or forfeited railroad grants), and 43 USC 940 (Forfeiture of rights where railroad not constructed in five years after location): (1) because those statutes evidence Congressional intent to divest the Government of any interests in railroad right of ways and to free property owners from those claims; and (2) because Congress' attempt in 1988 to reserve rights in railroad right of ways in the Government was enacted 12 years after the land patent was issued to the land owner in this case. Justice Sotomayor dissented, arguing that the court had not really grappled with the applicable case law, and had ignored the fact that railroad rights have long been treated as sui generis; not decided by common law. The 1875 Act was repealed in 1976.

Comment: The decision is important because it clears the titles of all properties that were once burdened by rights of way under the 1875 Act.

Local Actions

"Locals only" is Still the Rule in California Courts. The Local Action Doctrine Limits the Subject Matter Jurisdiction of California Courts with Respect to Actions Involving Injury to Real Property

By Brian W. Ludeke

***Eldee-K Rental Props., LLC v. DIRECTV, Inc.* (9th Cir 2013) 748 F.3d 943**

In this case, the Ninth Circuit Court of Appeals affirmed the Northern District of California's dismissal of an action brought by a rental property owner against DIRECTV based on its allegedly unfair business practices related to the illegal installation of equipment in common areas of apartment buildings. The plaintiff owned an apartment building in Connecticut and sued DIRECTV in the District Court based on California's Unfair Competition Law (UCL), alleging that DIRECTV's unauthorized installations amounted to trespasses and were thus violative of the UCL. DIRECTV moved to dismiss the action on the ground that the District Court lacked subject matter jurisdiction based on the local action doctrine, which requires certain types of actions involving real property be brought in the state in which the property is located. Because the plaintiff's claims related to alleged trespasses on real property located in Connecticut, the case had to be heard in Connecticut.

The Ninth Circuit examined the history of the local action doctrine, which originated in early English common law, when courts did not allow witness testimony and jurors needed to use personal, local knowledge to decide cases. Later, after courts began hearing witness testimony, courts relaxed the requirement with certain types of actions but maintained it with respect to actions pertaining to real property, which were still required to be brought in the county where the land was located.

By the 19th century, the distinction between local and transitory actions was criticized, but courts still applied the doctrine, as shown by Chief Justice Marshall's holding, in *Livingston v. Jefferson* (1811) 15 Fed. Cas. 660, that former President Thomas Jefferson could not maintain an action in Virginia related to real property in Louisiana. Nearly 100 years later, the Supreme Court similarly found a federal court in Ohio lacked jurisdiction over an action involving real property in West Virginia. (*Ellenwood v. Marietta Chair Co.* (1895) 158 U.S. 107-108.) The court dismissed that matter sua sponte, finding the lower court had no subject matter jurisdiction where the action was purely local. (*Id.* at 107-108.)

The doctrine is narrowly interpreted such that, where the gravamen of an action is damage to personal property, rather than to land, such an action is "transitory" and may be brought outside the state in which the land is located. (See, *e.g.*, *Stone v. U.S.* (1897) 167 U.S. 178, 182 [where complaint addressed value of property taken off land, rather harm to the land, action was not local].)

The plaintiff in this case argued that, because Congress had amended the Federal venue statute, 28 U.S.C. § 1391 (a)(2), to exclude the local vs. transitory distinction from courts' decisions related to venue, the doctrine should not affect courts' decisions with respect to jurisdiction. The court disagreed, finding that venue and subject matter jurisdiction are two separate concepts and that *Ellenwood* and its progeny have not been overruled.

The court then addressed California's law, which governs whether an action before a California court is local or transitory. Under California law, there are three broad categories of local actions. They are: 1) actions to recover or determine rights or interests in real property; 2) actions to remedy injuries to real property; and, 3) actions to foreclose on liens and mortgages on real property. To determine if a complaint falls under one of those categories, California courts look at the allegations therein and the judgment that could be rendered thereunder. Where the substance of the complaint is injury to real property, the action is deemed local (See, *e.g.*, *Strosnider v. Pomin* (1939) 32 Cal.App.2d 103, 104-105.)

Plaintiff argued that the court should not consider California decisions arising from Cal. Code of Civ. Proc. § 393, which addresses venue and discusses the local action doctrine. The court disagreed, finding that such authority sets forth California's local action doctrine and is consistent with the common law on which it is based. Relatedly, plaintiff argued that, if the court were bound by California's determination of local vs. transitory actions, because California treats the issue as one of venue allowing courts to transfer cases, as opposed to dismissing them, Federal courts in California should do the same. The court rejected that argument, finding that, although state law could determine which actions are local, that determination does not affect Federal courts' subject matter jurisdiction.

In light of the foregoing the 9th Circuit found that plaintiff's attempt to enjoin allegedly unfair business practices hinged upon an allegation of injury to money or property. Plaintiff's complaint alleged DIRECTV violated the UCL by adopting practices "with the purpose and effect of enabling the illegal installation" of DIRECTV's equipment and that the injury suffered was the "unauthorized use of common or restricted areas of [its] property," which constituted trespasses. As such, the gravamen of the plaintiff's claims addressed a trespass to land, so the action was properly deemed local. Because the subject real property was located in Connecticut, the Ninth Circuit affirmed the Northern District of California's dismissal based on the local action doctrine.

- Mr. Ludeke is an associate in the Westlake Village office. His practice focuses on business litigation issues. He has considerable experience in law and motion practice, litigation and discovery, and appellate matters.

Legislation

New Statute Protects Buyers and Lenders from Zombie HELOCs

By Zi. C. Lin

Civil Code section 2943.1

A home equity line of credit ("HELOC") is a type of loan where a home-owner can open a line of credit using his/her real property as collateral. It is similar to a credit card, with a pre-determined limit amount. HELOCs are secured by deeds of trust on property.

In a typical sale of property, senior liens are paid-off in escrow so the buyer is not burdened by deeds of trust given by the seller. The paid-off lender is required under Civil Code section 2941 to release or reconvey the deed of trust. Note that a deed of trust is deemed terminated as a matter of law when it is paid off, even without a reconveyance. "When the obligation secured by a trust deed is satisfied, the deed is terminated and title to the property automatically revests in the trustor or his successor without a reconveyance." (*Snider v. Basinger* (1976) 61 Cal.App.3d 819, 823.)

However, unlike traditional loans, borrowers may still draw funds from HELOCs while the property is in escrow for sale to a new buyer, or even after the sale has closed if the HELOC is not closed out. This is because the HELOC acts like a credit card. The borrower can pay down the debt on the HELOC to zero, then draw from it again as long as the HELOC is open. This means that a buyer could be saddled with the prior owner/seller's HELOC deed of trust, and any deed of trust given by the buyer to a lender could be subject to the unpaid HELOC and its lien priority reduced.

For example: Seller has a $100,000 HELOC from Nega Bank secured by a deed of trust on his property. Seller enters into escrow to sell his property to Buyer. The $100,000 HELOC is paid down to zero through escrow, but not closed. Buyer and his lender Potato Bank relies on the fact that the HELOC is paid off, and Potato Bank gives Buyer a $200,000 loan secured by a deed of trust. Potato Bank thinks that its $200,000 deed of trust is in *first* position because all senior liens, including the HELOC, have been paid off, and presumably closed/reconveyed. However, unbeknownst to Buyer, Seller did not close the HELOC and has run it up again to $50,000 after escrow closed. Seller does not pay the monthly payments on the HELOC, Nega Bank forecloses on what is now *Buyer's* property, and Potato Bank's deed of trust is now in *second* position, behind the $50,000 HELOC.

The recently passed California Senate Assembly Bill 1770, codified as Civil Code section 2943.1, effectively as of July 1, 2015, seeks to protect buyers and lenders from HELOCs that are not closed after a real estate transaction is consummated. Section 2943.1 provides a procedure by which a borrower, lender, or escrow, or title company can request the suspension and closure of a HELOC. Section 2943.1(b) requires that the payment demand issued by the beneficiary (usually the lender or its assignee) of a HELOC include an email address, fax number, or mailing address for the delivery of a "Borrower's Instruction to Suspend and Close Equity Line of Credit". The statute requires that the beneficiary of the HELOC suspend the HELOC for a minimum of 30 days once it receives a "Borrower's Instruction" signed by the HELOC borrower. The statute requires that the "Borrower's Instruction" be substantially as follows:

> Borrower's Instruction to Suspend and Close Equity Line of Credit
>
> Lender: [Name of Lender]
>
> Borrower(s): [Name of Borrower(s)]
>
> Account Number of the Equity Line of Credit: [Account Number]
>
> Encumbered Property Address: [Property Address]
>
> Escrow or Settlement Agent: [Name of Agent]:
>
> In connection with a sale or refinance of the above-referenced property, my Escrow or Settlement Agent has requested a payoff demand statement for the above-described equity line of credit. I understand my ability to use this equity line of credit has been suspended for at least 30 days to accommodate this pending transaction. I understand that I cannot use any credit cards, debit cards, or checks associated with this equity line of credit while it is suspended and all amounts will be due and payable upon close of escrow. I also understand that when payment is made in accordance with the payoff demand statement, my equity line of credit will be closed. If any amounts remain due after the payment is made, I understand I will remain personally liable for those amounts even if the equity line of credit has been closed and the property released.
>
> This is my written authorization and instruction that you are to close my equity line of credit and cause the secured lien against this property to be released when you are in receipt of both this instruction and payment in accordance with your payoff demand statement.

~

Once the beneficiary of the HELOC receives the "Borrower's Statement" and payment in accordance with its payoff demand, it must close the HELOC and release or reconvey the HELOC deed of trust.

This newly enacted statute will give buyers and their lenders greater assurance when purchasing property encumbered by HELOCs. It also affects title insurers, who are often asked by their insureds to clean up the priority and foreclosure problems caused by HELOCs that are run-up again after the close of escrow. Section 2943.1 should reduce title insurance claims concerning HELOCs.

Equitable Lien Subrogation

Equitable Lien Subrogation Proper, Notwithstanding a Number of Issues

By Alex Levy

***Branscomb v. JPMorgan Chase Bank, N.A.* (2014) 223 Cal. App. 4th 801**

In *Branscomb v. JPMorgan Chase Bank, N.A.* (2014) 223 Cal. App.4th 801, property owner (Navjot) had encumbered the property with three deeds of trust: (1) a first securing a loan of $5.1 million in favor of Washington Mutual recorded in 2005; (2) a second securing a $1.1 million loan in favor of MMB, a group of lenders recorded in 2006; and (3) a third that was to secure a loan of $500,000.00 in favor of plaintiff Branscomb, recorded in August 2007. Plaintiff's loan was brokered by defendant Menon, who caused the wrong amount to be shown in the deed of trust ($100,000 instead of $500,000) and who caused the recording of the deed of trust to be delayed for three months (it should have recorded in May 2007).

After the plaintiff's deed of trust recorded, the first and second deeds of trust were refinanced by the borrower, with the same lenders. The new loans were in the same amounts as the refinanced loans. The plaintiff's "$100,000" deed of trust appeared on the preliminary report in the refinance escrows. The escrow holder asked Menon for a demand to pay off plaintiff's loan. Menon gave escrow a zero demand. Escrow closed without paying off plaintiff's loan. Therefore, at the close of the refinance escrows, the Washington Mutual and MMB Deeds of Trust appeared in the public records to be second and third liens after plaintiff's first deed of trust.

In 2009, when Washington Mutual (Chase) commenced non-judicial foreclosure proceedings, plaintiff sued Chase and MMB. Plaintiff sought to reform his deed of trust to reflect the correct loan amount, and also sought to confirm that his deed of trust was in first position. The lenders argued: (1) that they were subrogated to the priority of the deeds of trust paid off in escrow; and (2) that they were bona fide encumbrancers who cut off the right of plaintiff to increase the amount secured by his deed of trust. After a three day bench trial, the trial court reformed the plaintiff's deed of trust, ordered it judicially foreclosed, awarded plaintiff attorney fees against the borrower, and awarded costs against the lenders. The trial court found the lenders were not entitled to subrogation and that they were not bona fide encumbrancers, because they had actual and constructive notice of the plaintiff's deed of trust. Plaintiff also sued the escrow holder, which was dismissed following a successful demurrer. The trial court later found escrow had been negligent.

In reversing the trial court's subrogation ruling, the First District Court of Appeal held that the following factors did *not* defeat the refinance lender's equitable subrogation claims: (1) that the lenders had actual knowledge of the plaintiff's deed of trust; (2) that the lenders were responsible for the escrow holder's negligence; (3) that the lenders had a cause of action against escrow; (4) that the plaintiff was unaware of the refinance transactions (where the refinance lenders did nothing to conceal the refinance transaction from plaintiff); and (5) that plaintiff was the victim of his agent's fraud (where plaintiff had continued to use the agent in the past after learning he had signed documents for him without authorization).

As courts have held before, if a lender knows of a lien, but reasonably expects it will be reconveyed or subordinated by the close of escrow, the lender is still entitled to subrogation, because the lender under those circumstances is not "culpable and inexcusable neglect." The court therefore distinguished *Lawyers Title Insurance Corporation v. Feldsher* (1996) 42 Cal. App. 4th 41. Nor, said the court, did the existence of a cause of action against escrow defeat subrogation, citing *JP Morgan etc. v. Banc of America etc*. (2012) 209 Cal.App.4th 862 (cause of action against title insurer does not defeat insured lender's subrogation rights) and *Katisvalis*. Nor, said the court, did escrow's failure to note the incorrect amount on plaintiff's deed of trust or the forged signature on plaintiff's pay off demand give rise to negligence that could be imputed to the refinance lenders, citing *Summit Financial*. The court concluded its discussion pointing out that in deciding whether to grant equitable subrogation, equity looks to carrying out the intentions of the parties. When plaintiff made his loan, he expected his deed of trust to be in third position.

Because the court had determined that plaintiff's deed of trust was junior to the subrogated liens of the defendants, the court said it had no need to address: (1) whether the refinance lenders were bona fide encumbrancers with respect to plaintiff's attempt to reform his deed of trust to increase the balance of the debt it secured; and (2) whether plaintiff had the right to include his attorney fees in the amount secured by his deed of trust.

Comment: The court does not discuss the fact that the refinance lenders' subrogated liens would have to be judicially foreclosed, based on the terms and priority of the original deeds of trust. Had the refinance balances been greater than the balances secured by the equitable liens, then the refinance lenders could have relied on a line of cases which hold that under the proper circumstances (as where the same lender takes a new note and deed of trust as a substitute for a prior one), subrogation will permit the entire balance secured *by a new deed of trust* to take its priority from an earlier deed of trust. See, for example, *Copp v. Miller* (1938) 11 Cal.2d 122, 126-127.

Lending

"Alter Ego" Additional Debtor Under California Code of Civil Procedure Section 187 - Res Judicata and Collateral Estoppel Do Not Apply to Enforcing a Judgment

By Ndubisi A. Ezeolu

***Wells Fargo Bank, N.A. v. Weinberg* (2014) 227 Cal.app.4th 1**

In *Wells Fargo Bank, N.A. v. Weinberg* (2014) 227 Cal.App.4th 1, Wells Fargo Bank sued an attorney, Steven Weinberg, as an individual guarantor, and his firm, Steven J. Weinberg, a Professional Law Corporation, for repayment of a business line of credit. The trial court sustained Weinberg's individual demurrer without leave to amend. The court later entered judgment in favor of Wells Fargo and against the law firm in the amount of $57,075.51. After obtaining alter ego evidence in a judgment debtor's examination, Wells Fargo then moved to have the judgment amended to add Weinberg as a judgment debtor.

Wells Fargo's motion to amend the judgment to add Weinberg was granted by the trial court. The Court of Appeal, Fourth Appellate District, affirmed, rejecting Weinberg's contention that the amendment was improper:

"Weinberg's primary argument is that res judicata bars Wells Fargo's amendment of the judgment because the trial court's ruling sustaining Weinberg's demurrer without leave to amend determined as a matter of law that Weinberg was not liable for the law corporation's debts on any theory-including alter ego-that could have been raised in the complaint. We disagree that res judicata applies."

The appellate court further explained, "[r]es judicata also does not operate because Weinberg's alter ego conduct was a separate and distinct harm from the law corporation's breach of contract. The motion to add Weinberg to the judgment sought a remedy, not for breach of contract, but for Weinberg's exercise of control over the law corporation that deprived Wells Fargo of the ability to collect the judgment against the law corporation for breach of contract. These are separate and distinct wrongs. …"

In reaching its holding, the appellate court recognized that res judicata and collateral estoppel do not preclude a bank from conducting a judgment debtor examination of lawyer affiliated with a law firm or from seeking to add the lawyer as a judgment debtor under Code of Civil Procedure section 187 on an alter ego theory:

"A claim against a defendant, based on the alter ego theory, is not itself a claim for substantive relief … , but rather, procedural, *i.e.*, to disregard the corporate entity as a distinct defendant and to hold the alter ego individuals liable on the obligations of the corporation where the corporate form is being used by the individuals to escape personal liability, sanction a fraud, or promote injustice.' [Citation.] Amending judgments under Code of Civil Procedure section 187 is an equitable procedure. [Citation.]"

Accordingly, because Wells Fargo was not seeking new relief but to enforce its judgment, res judicata did not apply.

Borrowers Need Not Plead Tender in Claims for Rescission Under TILA; Statute of Limitations of Violations of RESPA May Be Equitably Tolled

By Zi C. Lin

***Merritt v. Countrywide Financial Corp.*, 759 F. 3d 1023 (9th Cir.)**

The Truth in Lending Act (TILA) is a federal law requiring disclosures about the terms and costs of loans. TILA provides two remedies for violations: (1) rescission of the loan, and (2) damages. The Merritts obtained a home equity line of credit ("HELOC") loan from Countrywide, and were not given proper disclosures in violation of TILA. They sued Countrywide in district court for rescission under TILA, and for "marking" up charges associated with the loan under Section 8 of the Real Estate Settlement Procedures Act ("RESPA"). RESPA prohibits kickbacks and unearned fees by lenders.

The district court dismissed the case, holding that the Merritts failed to tender the value of their HELOC before filing suit, and were not entitled to rescission under TILA, and that the lawsuit as barred by the one year statute of limitations under Section 8 of RESPA, as the lawsuit was filed three years after the loan closed. The Merritts appealed.

The Ninth Circuit Court of Appeals reversed the district court, holding that a plaintiff need not allege tender. Only at the summary judgment stage could the court require tender before rescission, and then only on a case by case basis once the creditor/lender has established a potentially viable defense. The Ninth Circuit held that plaintiffs are not required to specifically plead tender under Federal Rules of Civil Procedure 8(a), which only requires "simplified" pleading.

The Ninth Circuit also held that the statute of limitations under RESPA could be equitably tolled, and remanded the issue to the district court for reconsideration, holding that the district court "may consider such evidence as it deems appropriate to determine on what date the Merritts discovered or had reasonable opportunity to discover the alleged Section 8 violations and whether they filed their complaint within a year of that date." (*Merritt v. Countrywide Financial Corp., supra*, 759 F.3d at p. 1040.)

- Mr. Lin is a partner in the Pasadena office. His practice focuses primarily on real proerty and title insurance issues, trials, and appeals. He has considerable experience in federal and bankruptcy matters and is admitted to all districts of the federal district court and bankruptcy court in California.

Lending

A Bank Can Be Held Liable For Conduct and Representations Occurring During the Loan Modification Process Under HAMP

By Candie Y. Chang

***Rufini v. CitiMortgage, Inc.* (2014) 227 Cal.App.4th 299**

The First District Court of Appeal held that a defaulting borrower can assert claims for breach of contract and wrongful foreclosure under the Home Affordable Modification Program (HAMP) if he could amend the complaint to clearly specify the nature and terms of the agreement allegedly breached and that the modification was pursuant to a written trial period plan. Lenders do not have a free pass to misrepresent important facts with impunity when they negotiate loan modification.

In reversing the trial court's decision sustaining CitiMortgage's demurrer, the court found that the borrower was entitled to allege a contract action founded on promissory estoppel based on the fact that CitiMortgage falsely and fraudulently informed the borrower that he would be approved for a permanent loan modification without any intention of actually providing the loan modification, that the borrower relied on those representations, and suffered damages. This is supported by recent opinions addressing the obligations of lenders and borrowers who engage in attempts to modify home mortgages under HAMP (*Bushell v. JPMorgan Chase Bank*, N.A. (2013) 220 Cal.App.4th 915, 922-923; *Chavez v. Indymac Mortgage Services* (2013) 219 Cal.App.4th 1052, 1057, *West v. JPMorgan Chase Bank*, N.A. (2013) 214 Cal.App.4th 780, *Barroso v. Ocwen Loan Servicing*, LLC (2012) 208 Cal.App.4th 1001.).

The court found that:

(1) The borrower made sufficient allegations of a writing and forbearance, and that satisfied the statute of frauds;

(2) The borrower need not show that he was ready and able to satisfy his entire outstanding obligation on the loan because the borrower's contract allegations here arose out of later oral representations based on an agreement to modify the loan, not the original loan agreement. Because the borrower did not default under the terms of the modified agreement, he was not required to tender his indebtedness to avoid foreclosure; and

(3) The borrower's claims may be sufficient to support a cause of action for negligent misrepresentation and bad faith.

Do Not Forget to Exhaust Administrative Remedies Provided by Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA)

By Ndubisi A. Ezeolu

***Rundgren v. Washington Mutual Bank, FA* (2014)760 F.3d 1060**

In *Rundgren v. Washington Mutual Bank, FA* (2014) 760 F.3d 1060, the United States Court of Appeals for the Ninth Circuit was faced with the following issue - whether the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) stripped a district court of jurisdiction over trustee's claims arising out of allegedly fraudulent acts by a bank. The Ninth Circuit held that the because Washington Mutual was placed into the receivership of the FDIC, the district court lacked jurisdiction to hear the fraud claims of the borrowers who did not exhaust their administrative remedies.

In 2005, Todd and Michelle Rundgren obtained a loan secured by a deed of trust in favor of Countrywide Home Loans, Inc., on their property. In 2008, the Rundgrens refinanced the loan with Washington Mutual. The Rundgrens later alleged that the loan refinancing was tainted by Washington Mutual's numerous fraudulent acts. According to the complaint, during the refinancing, Washington Mutual agents entered false information on the Rundgrens' loan application, highly exaggerating their supposed monthly income and supposed assets without their knowledge, and securing a false appraisal of the value of the subject property. Subsequently, Washington Mutual was seized by the Office of Thrift Supervision and placed into the receivership of the FDIC. The FDIC transferred specified Washington Mutual assets that included Rundgren's mortgage, to JPMorgan Chase Bank, N.A. under a purchase and assumption agreement.

After purchasing the loan from Washington Mutual, Chase determined that the Rundgrens were in default on their loan. Chase accelerated the payments secured by the Rundgrens' deed of trust and notified them that a nonjudicial foreclosure sale would occur on August 26, 2009. In response, the Rundgrens notified Chase that they were exercising their right to cancel their loan transaction, mortgage, and promissory note based on allegations that Chase and Washington Mutual violated state and federal law.

The Rundgrens sued Chase and Washington Mutual in state court. The Rundgrens alleged that Washington Mutual defrauded them and breached its fiduciary duty during the refinancing negotiation. Among other things, the Rundgrens sought declaratory and injunctive relief, rescission of the loan, and statutory damages under state and federal consumer protection statutes.

Chase removed the action to federal court. The district court dismissed the case against Chase for lack of jurisdiction, finding that the Rundgrens failed to exhaust their claims with the FDIC prior to bringing suit. The district court specifically found that such exhaustion was required under section 1821(d)(13)(D) of the FIRREA. The Rundgrens appealed.

See Rundgren v. Washington Mutual Bank, continued on p. 16

Foreseeability Remains An Essential Ingredient Of Any Award of Contract or Tort Damages

By Ryan C. Squire

***Ash v. North American Title Company, et al.* (2014) 223 Cal.App.4th 1258**

In *Ash v. North American Title Company*, the plaintiff, David Ash, sued North American Title, which served as escrow-holder in connection with Ash's purchase of commercial rental property.

Ash purchased the property as part of a 1031 exchange. He deposited several million dollars into a segregated account held by LandAmerica Exchange Services, the exchange accommodator. Escrow was originally intended to close on a Friday. For various reasons, escrow did not close on that Friday. North American, the seller, and Ash expected escrow would close on the following Monday (or possibly Tuesday). Not wanting to hold Ash's money over the weekend, North American's escrow officer decided not to request Ash's purchase money from LandAmerica.

On the following Monday, LandAmerica collapsed and closed its doors. Two days later, it filed for bankruptcy. Ash's funds were frozen: Neither Ash nor the escrow officer could obtain Ash's funds from LandAmerica.

Ash claimed he could not close escrow without the funds being held by LandAmerica. Ash asked the bankruptcy court to release his segregated funds, as did several others. In all, when it folded, LandAmerica was holding *hundreds of millions of dollars* in exchange funds --- a pot of money that was all too attractive to LandAmerica's creditors. After the creditors objected, the court refused to release Ash's money, concluding that the funds were property of the bankruptcy estate because the exchange agreement was not a true "trust" agreement, even though LandAmerica was required to hold the funds in a segregated account.

Eventually, 18 months after escrow was originally set to close, the bankruptcy court released all of Ash's funds, and escrow closed. Ash sued North American under contract and tort theories, claiming damages for the attorney's fees he incurred in the bankruptcy court, the rents he alleged he would have earned had escrow closed before LandAmerica's collapse, and interest on his purchase loan (which funded before LandAmerica's collapse).

Following a jury trial, the court entered judgment against North American, including $1 million in compensatory damages --- $250,000 of which were awarded as contract damages and $750,000 of which were awarded as tort damages.

North American appealed, and the court of appeal, in a published decision, reversed the damage awards. North American argued that Ash's contract damages were limited to the lost rents and loan interest that he incurred on the Saturday and Sunday between the date escrow was supposed to have closed (a Friday) and the date LandAmerica collapsed (a Monday). The court of appeal agreed that under the well-known case of *Hadley v. Baxendale* (1854) 156 Eng. Rep. 145, which the court discussed at length, Ash was not entitled to any contract damages incurred after LandAmerica collapsed --- including the hundreds of thousands of dollars in attorney's fees he spent in the bankruptcy court. The court of appeal explained that any damages incurred after LandAmerica collapsed were not reasonably foreseeable under a contract theory. Ash did not communicate to North American (or the seller) any apprehension about the possibility of LandAmerica collapsing, nor was there any evidence that the seller and North American knew of or should have known of the risk of LandAmerica collapsing. The court declined to set the amount of contract damages, instead remanding to the trial court to determine the proper amount of contract damages.

The court also reversed the award of tort damages. At trial, North American had asked the trial court to instruct the jury that LandAmerica's collapse --- and the bankruptcy court's refusal to allow Ash to access his segregated funds --- were intervening and superseding causes, thereby cutting-off any damages Ash claimed to have incurred after LandAmerica folded. The trial court refused the instruction, believing that the usual causation instructions --- which direct the jury to determine whether a defendant's conduct was a "substantial factor" in causing harm to the plaintiff --- were sufficient. The court of appeal reversed, finding that the usual causation instructions were not sufficient because the concept of "substantial factor" is distinct from the defense of "intervening and superseding cause." The court of appeal remanded the case for a new trial, and directed the trial court to instruct the jury on intervening and superseding cause.

The new trial occurred in December 2014. Following a two-week trial, the jury returned defense verdicts.

Ash is an important case in several respects. The *Hadley v. Baxendale* rule --- and the intervening and superseding cause rule --- both focus on the concepts of foreseeability. The court's holdings on contract and tort damages demonstrate the essential feature of foreseeability in our legal system. Even the venerable case of *Palsgraf v. Long Island Railroad* (N.Y. 1928) 162 N.E. 99 made a cameo appearance in the Ash case (at oral argument) --- demonstrating further that although the law has come a long way in the last two centuries, there are certain touchstones on which our system of jurisprudence is founded. Ash reminds us not to stray from our first principles.

Ryan C. Squire and Zi C. Lin, of Garrett & Tully, P.C. and Richard D. Marks, of Richard D. Marks Professional Corporation, represented North American in this appeal, and Robert Garrett, Esq., Mr. Squire, and Mr. Lin represented North American at the re-trial.

A Court May Appoint Its Clerk As An Elisor To Sign Escrow Documents to Enforce Its Judgments

By Scott B. Mahler

***Blueberry Properties, LLC v. Chow* (2014) 230 Cal.App.4th 1017**

Chow entered into an agreement to sell her apartment complex to Blueberry Properties, LLC. However, Chow refused to complete the sale and returned the money Blueberry had placed in escrow for the property. Blueberry brought an action for specific performance to enforce the purchase agreement. The parties later entered into a settlement where Chow agreed to sell the property to Blueberry in accordance with the terms of the original purchase agreement. However, Chow failed to comply with the settlement agreement by withholding her signature from the documents necessary to reopen and complete the sale of the property.

The trial court entered a judgment in favor of Blueberry and against Chow, setting forth the terms of their settlement agreement. It stated that Chow was ordered to do all things necessary and to execute all documents necessary to consummate the sale to Blueberry. The judgment also stated that Chow shall do all things necessary and execute all documents necessary to perform the terms of the purchase agreement, to perform the terms of all escrow documents previously executed by both parties, and to perform the terms of the settlement agreement.

Chow subsequently refused to execute the escrow documents to complete the sale of the property. Blueberry applied for an order appointing the clerk of the court as an elisor to execute the escrow documents on behalf of Chow, which the trial court granted. An elisor is a person appointed by the court to perform functions like the execution of a deed or document. Chow appealed the post judgment order.

The appellate court reviewed the issue of the court's authority and reasonableness in issuing the order appointing the elisor. A court typically appoints an elisor to sign documents on behalf of a recalcitrant party in order to effectuate its judgments or orders, where the party refuses to execute such documents. The appellate court affirmed the trial court's appointment of the elisor. It held that courts use elisors in matters like this one to enforce their orders. By appointing the clerk as an elisor to execute the documents on Chow's behalf, the trial court properly exercised its power under Code of Civil Procedure section 128(a)(4), which provides courts with the power to compel obedience to its judgments, order, and process.

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Conditions Precedent in California Real Property Purchase Agreement Deposit May Still Be Refundable Despite a Non-refundable Deposit Provision

By Ndubisi A. Ezeolu

***Rutherford Holdings, LLC v. Plaza Del Rey* (2014) 223 Cal.App.4th 221**

In *Rutherford Holdings, LLC v. Plaza Del Rey* (2014) 223 Cal. App.4th 221, Rutherford Holdings, LLC contracted for the purchase and sale of a mobile home park from Plaza Del Rey. Rutherford made a substantial deposit, but the sale was never completed and Rutherford sued to recover its deposit. The purchase agreement provided that the deposit was nonrefundable unless Plaza Del Rey materially breached the agreement or failed or refused to close.

On appeal, the California Court of Appeal, Sixth Appellate District, held Rutherford could state a cause of action "for money had and received" based on the total failure of consideration and it was not necessary to bring a formal action for rescission. The appellate court stated, "Where the failure of the consideration is total, 'the law implies a promise on the part of the other to repay what has been received by him under the contract . . . .' [Citation.] Such a promise is implied because the 'defendant cannot in equity and good conscience retain the benefits of the agreement and repudiate its burdens....' [Citation.]."

Accordingly, the appellate court reversed the judgment of dismissal and remanded with directions, holding that Rutherford sufficiently alleged that the nonrefundable-deposit provision of the purchase agreement was unlawful, and finding that at the pleading stage, it was sufficient that the purchase agreement was reasonably susceptible of the meaning that Rutherford ascribed to it.

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