Borrower Claims Sounding in Contract and Tort

Based on HAMP are Trending Towards More Traditional Legal Analysis

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Since passage of the Emergency Economic Stabilization Act of 2008, borrowers have inundated California courts with lawsuits seeking to enforce trial period plans under the Home Affordable Modification Program ("HAMP") as loan modification agreements. Courts initially rejected this approach on the ground that HAMP trial period plans do not constitute enforceable contracts. (*See*, *e.g.*, *Nungaray v. Litton Loan Servicing, LP* (2011) 200 Cal.App.4th 1499, 1504.) Subsequent case law suggested that HAMP trial period plans were not only enforceable contracts in their own right, but also required the lender to permanently modify a loan if the borrower made all payments under the plan and submitted the required documentation—irrespective of the actual terms in the HAMP trial period plan. (*See*, *e.g.*, *West v. JPMorgan Chase Bank, N.A.* (2013) 214 Cal.App.4th 780, 798 ("*West*").)

In 2013, the Court of Appeal issued a series of opinions refining its approach to claims based on HAMP trial period plans. With the troubling opinion in *West v. JPMorgan Chase Bank, N.A.* (2013) 214 Cal.App.4th 780 ("*West*"), the Court of Appeal initially seemed to impose obligations beyond the express terms of the HAMP trial period plan by referring to the Troubled Asset Relief Program. (*West*, *supra*, 214 Cal.App.4th at 797-98.) The HAMP trial period plan at issue in *West* did not require a permanent modification, providing instead: "[i] f all payments are made as scheduled, we will reevaluate your application for assistance and determine if we are able to offer you a permanent workout solution to bring your loan current." (*West* at 796.) Taking a result-oriented approach, the Court of Appeal infused the HAMP trial period plan with a new obligation—to permanently modify the loan as long as the borrower made all payments and submitted all documents required under the plan. (*West* at 798.)

Subsequent appellate opinions suggest courts now understand *West* is too broad and reliance on extrinsic matters unwarranted for the purpose of interpreting HAMP trial period plans. Beginning with *Corvello v. Wells Fargo Bank, N.A.* (9th Cir. 2013) 728 F.3d 878 ("*Corvello*"), the Ninth Circuit Court of Appeals confined its interpretation of the HAMP trial period plan to the express terms of the written document. In *Corvello*, the HAMP trial period plan provided: "I understand that after I sign and return two copies of this Plan to the Lender, the Lender will send me a signed copy of this Plan if I qualify for the Offer or will send me written notice that I do not qualify for the Offer." (*Corvello*, *supra*, 728 F.3d 878, 881.) Noting that the lender neither modified the loan nor gave notice that the borrower did not qualify, the Ninth Circuit reversed the trial court's granting of a motion to dismiss and remanded. (*Id.* at 882.)

In *Chavez v. Indymac Mortgage Services* (2013) 219 Cal.App.4th 1052 ("*Chavez*"), the Court of Appeal followed the Ninth Circuit's lead in *Corvello* by confining its analysis to the language in the HAMP trial period plan, noting the plan permitted the lender to either modify the loan or notify the borrower that she did not qualify: "Defendants were required to either send Chavez a signed copy of the Trial Period Plan if she qualified for the offer, or send her a notice that she did not qualify for the offer." (*Chavez*, *supra*, 219 Cal.App.4th 1052, 1059.) The Court of Appeal reversed the trial court's judgment in favor of the lender, explaining: "Defendants did neither…" (*Ibid.*, citing *Corvello*, 728 F.3d 878, 883.)

Like the *West* court's reliance on the extrinsic matter of the Troubled Asset Relief Program, the Court of

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including loan level audit checks, into the origination process and prior to the loan closing may have to be passed on in the form of higher interest rates or fees to consumers.

Rockwell/Cannon: It remains to be seen how the market reacts to the ATR rules. Preliminary estimates indicate that about eighty percent of recently originated mortgage loans would qualify as QMs. Thus, for four out of every five transactions, the rules should not have a significantly negative impact. But which lender would gladly cut its business by twenty percent? Also, it is not clear how the mortgage brokerage community will weather the shift to originating qualified mortgages, especially with the stresses the three-percent cap on fees and charges may place on brokered transactions.

Thus, the challenge will be to see what appetite arises in the marketplace for ATR loans, for higher-priced QMs (which do not have safe-harbor protections), and for other types of transactions that satisfy the lender's obligation to verify the borrower's ability to repay but which do not receive the safe harbor protections. Further, assuming that lenders are willing to originate these non-safe harbor loans (and investors are willing to acquire them), it is not yet clear whether and to what extent these loans will be priced differently from loans receiving the safe harbor protections.

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Appeal in *Bushell v. JPMorgan Chase Bank, N.A.* (October 22, 2013)—Cal.Rptr.3d—, 2013 WL 5723074 ("*Bushell*"), resorted to an extrinsic matter when interpreting the HAMP trial period plan—a cover letter sent with the plan that stated: "If you make all [3] trial period payments on time [under the trial modification plan] and comply with all of the applicable [HAMP] program guidelines, you will have qualified for a final [permanent] modification." (*Id.* at *3.) The *Bushell* court offers no more convincing a rationale for its reliance on extrinsic matters than the court in *West*. The court merely cites to the *West* court's discussion on the guidelines, procedures, instructions, and directives issued by the Department of the Treasury. (*Bushell*, *supra*, at *7.) The court appears to have strained its legal analysis to reach what it deemed a just result—it was undisputed that the borrower's application was denied after he had made at least twenty six payments and his application was admittedly "dropped through the cracks" by the lender during a corporate merger. (*Id.* at *6.)

At first glance, the opinions issued in 2013 appear disparate, and far too often, result-oriented. However, the HAMP trial period plan at issue in *West* was, apparently, contractually uncertain—thus calling for reliance on extrinsic matters. (*See Bushell*, *supra*, 2013 WL 5723074, at *7.) Moreover, the borrowers in *West* and *Bushell* made trial plan payments well past the required three or four-month period. In *West*, the borrower made at least ten trial plan

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payments while waiting for a decision on her application. (*West*, *supra*, 214 Cal.App.4th at 790.) In *Bushell*, the borrower made twenty six payments before he was told the modification had been denied. (*Bushell*, *supra*, at *6.)

The trend toward more traditional analysis for claims sounding in contract—as the opinions in *Corvello* and *Chavez* suggest—appears to be emerging for claims sounding in tort as well. For example, in *Aspiras v. Wells Fargo Bank, N.A.* (2013) 219 Cal. App.4th 948 ("*Aspiras*"), the Court of Appeal ruled that a borrower cannot state a cause of action for fraud based on allegations that an unnamed representative made statements regarding the status of a foreclosure and review for modification. (*Aspiras*, *supra*, 219 Cal.App.4th 948, 955.) The borrower in *Aspiras* alleged that she spoke with someone at the bank by telephone and was told the foreclosure was postponed pending review of her request for a modification. (*Id.* at 958-59.) However, she could not identify the individual with whom she spoke and argued that she should not have to plead such facts because the bank had superior knowledge of the person's identity. (*Id.* at 958.) Distinguishing cases such as *West* where the borrower produced a written document containing the purported misrepresentation, the Court of Appeal rejected Aspiras' argument and held her to the heightened pleading standard applicable to claims of fraud. (*Id.* at 960.) The court also declined to impose a duty of care on the lender in handling the borrower's loan modification, citing well-settled precedent that no special duty of care arises in an arms' length transaction between a financial institution and its borrower. (*Aspiras*, *supra*, 219 Cal. App.4th at 963, distinguishing *Jolley v. Chase Home Finance, LLC* (2013) 213 Cal.App.4th 872.)

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