New Appellate Court Decision Holds That Lender Violates The FDCPA, The Rosenthal Act And California's Unfair Competition Law By Even *Attempting* To Collect On A Junior Lien After Foreclosure Of The Senior Mortgage

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In another blow to lenders in the Golden State, the California Court of Appeals, Second Appellate District, has ruled that a holder of a junior purchase money lien on a property that has been foreclosed upon violates the Fair Debt Collection Practices Act ("FDCPA"), the Rosenthal Act and California's Unfair Competition Law (California Business and Professions Code Section 17200, *et seq.*) by even ***attempting*** to collect on a junior lien after the senior mortgage holder has foreclosed, even if the foreclosure of the senior lien provided no payment to the junior lienholder. In other words, the Court of Appeal has held that a junior lienholder is completely without recourse in California after the senior lien has been foreclosed upon, even for foreclosures that took place prior to the 2013 amendments to California Civil Procedure Code Section 580b.

The case, *Alborzian v. J.P. Morgan Chase Bank, N.A.,* ____ Cal. App. 4th ____, 2015 DAR 2950 (2015), involved borrowers who took out two loans to purchase their home in 2005 - a first mortgage from Wells Fargo Bank, N.A. ("Wells Fargo"), and a second from J.P. Morgan Chase Bank, N.A. ("Chase"). *Id.* at 2. Wells Fargo foreclosed on the property when the borrowers defaulted. However, the proceeds of the foreclosure sale were not sufficient to pay off Chase's junior mortgage. *Id.* A year after the foreclosure sale, Chase sent a letter to the plaintiffs claiming that the plaintiffs still "owed" Chase the balance of the junior mortgage, and offered to accept a reduced payment in order to settle the balance. *Id.* Chase subsequently sent another letter to the plaintiffs in which it claimed that the balance of the mortgage was "currently due," and offered a settlement in order to "close this debt once and for all." *Id.* at 3.

The plaintiffs brought suit on behalf of themselves and a class of similarly situated borrowers against Chase, alleging that former Section 580b of the California Civil Procedure Code extinguished the plaintiffs' debt on the second mortgage after the foreclosure sale and that, therefore, the letters sent by Chase were misleading by implying that the debt was still owed. *Id.* Plaintiffs asserted claims under the Rosenthal Fair Debt Collection Practices Act, California's Unfair Competition Law and the Consumer Legal Remedies Act (the "CLRA"). They also sued the debt collector employed by Chase for violating the federal FDCPA.

Prior to 2013, California Civil Procedure Code Section 580b provided that "no deficiency judgment shall lie in any event after a sale of real property . . . under a deed of trust or mortgage given to the vendor to secure payment of the balance of the purchase price of that real property." In 2013, the statute was amended to prohibit any "collect[ion]" of a junior lien after foreclosure of the senior lien. The question in *Alborzian* was whether a lender could ***attempt*** to collect an uncollectable debt with respect to a foreclosure that happened prior to

the statutory amendments without running afoul of the debt collection statutes and the Unfair Competition Law.

The Court of Appeal answered "no." The trial court had sustained the defendants' demurrers to the claims asserted by the plaintiffs, but the Court of Appeal reversed. The appellate court held that the letters sent by Chase violated the FDCPA - and consequently the Rosenthal Act and the Unfair Competition Law, which both incorporate the FDCPA - because "[t]he unspoken but unmistakable premise of these letters is that plaintiffs' debt is still valid, due, and owing - in a word, enforceable." *Alborzian*, 2015 DAR 2950, at 7. The Court did, however, state that Chase could have avoided the FDCPA problem by "disclosing that its debt was no longer enforceable against the letter's recipient and that Chase was merely seeking voluntary repayment of its unenforceable debt." *Id.* at 8. But as the Court of Appeal recognized, "such a disclosure would have substantially undermined the likely effectiveness of Chase's collection efforts." *Id.* Accordingly, the Court of Appeal reversed the trial court's order sustaining the demurrers (the appellate court did, however, affirm the dismissal of the CLRA claim because a loan is not a "good or service" under the CLRA). *Id.* at 12.

This decision obviously has a negative impact on the holders of junior liens in California. The decision holds that a junior lienholder may not even ***attempt*** to collect on the junior mortgage after a pre-2013 foreclosure of the senior loan, unless the lender affirmatively discloses in the communications that the debt is not enforceable, and that it is merely seeking voluntary repayment of the loan (collection activity on junior liens for foreclosures that happen after the 2013 amendments to California Civil Code Section 580b is prohibited by the statute). Consumers who have lost their homes to foreclosure are, of course, unlikely to agree to such voluntary repayment. And the *Alborzian* court held that negative credit reporting after the foreclosure was sufficient harm to provide the borrower standing under the Unfair Competition Law to sue.

Accordingly, holders of junior liens would be well-advised to monitor the status of the senior lien and, if foreclosure activity is started on that senior mortgage, aggressively attempt to collect their debt ***before*** the foreclosure sale (assuming the borrowers have defaulted on the junior lien as well). Any attempt to collect the debt after the foreclosure of the senior mortgage has been completed are likely to result in liability (particularly after the 2013 amendments).

Alborzian (and the 2013 amendments to California Civil Procedure Code Section 580b) continue a trend in California of anti-lender legal developments. Holders of junior liens in the Golden State now have one less arrow in their quiver when attempting to collect the money they have lent.

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