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ENTER THE JUDICIARY

Michael Pfeifer, CMBA GENERAL COUNSEL, SMITH DOLLAR PC

"As a member of this Court I am not justified in writing my opinions into the Constitution, no matter how deeply I may cherish them. … It can never be emphasized too much that one's own opinion about the wisdom or evil of a law should be excluded altogether when one is doing one's duty on the bench." —Justice Felix Frankfurter, for the Dissent, West Virginia State Board of Education v. Barnette 319 U.S. 624 (1943).

In recent years, we have seen how the financial crisis of 2008 and subsequent economic travails resulting from a variety of causes—many of which have nothing to do with the banking and mortgage lending practices preceding the 2008 crisis—have spawned political demagogy on a scale unprecedented in modern times. In California, this culminated in the pretentiously-named "California Homeowner Bill of Rights," which became effective January 1, 2013. The manifold defects and unintended consequences of this legislation have been amply discussed in these pages, as has the avalanche of new, confusing, and economically suffocating rules promulgated by the federal "Dodd Frank Wall Street Reform and Consumer Protection Act" of 2010, and its spawn, the Consumer Financial Protection Bureau ("CFPB").

Now, as both state and federal legislative activity begins to wane, and the real-world impact of these new rules is felt, we are starting to hear from the judiciary. Whether the "third branch" of government will confine itself, however, to merely construing the new legislation or, undertake instead to write some of its own, remains to be seen. A trio of recent decisions does not augur well for judicial restraint.

In February of this year, the California Court of Appeal for the First District issued an opinion in the case of *Jolley v. Chase Home Finance, LLC.*, 213 Cal.App. 4th 872 (as modified on denial of rehearing on March 7, 2013), that clearly demonstrates how anxious some members of the judiciary are to write their views into the law governing mortgage lending and servicing. Reversing a summary judgment on a borrower's negligence claim, the court determined that

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The Voice of Real Estate Finance

California Court of Appeal Splits Over HAMP

Andrew W. Noble, SEVERSON & WERSON

In March the California Court of Appeal issued the latest in a series of opinions concerning a borrower's entitlement to a permanent modification pursuant to the Home Affordable Modification Program (HAMP). The troubling opinion in *West v. JP Morgan Chase Bank, N.A.* (2013) 214 Cal.App.4th 780 ("*West*") holds that "when a borrower complies with all the terms of the TPP [trial period plan], and the borrower's representations remain true and correct, the loan servicer must offer the borrower a permanent loan modification" even where the trial plan makes no such promise.

West ignores an earlier case in which the same court reached the opposite conclusion and found that a HAMP trial period plan did not entitle the borrower to a permanent modification. It also ignores federal court precedent holding that borrowers are not third party beneficiaries who are entitled to enforce HAMP servicer participation agreements between the federal government and servicers.

Pursuant to the Emergency Economic Stabilization Act of 2008, the U.S. Department of Treasury implemented HAMP as a program designed to provide affordable mortgage loan modifications and other alternatives to foreclosure for eligible borrowers. The Department negotiated a series of servicer participation agreements with servicers. Under HAMP's regulations, participating servicers must use a two-step process for HAMP modifications. Step one involves providing a trial plan outlining the terms of the trial period, and step two involves providing the borrower with an agreement that outlines the terms of the final modification.

In *West*, the servicer's trial period plan approval letter made no explicit promise of a permanent modification, providing instead: "If you comply with the terms of this Agreement, we'll **consider** you for a permanent workout solution for your loan once the Trial Plan has been completed."

The borrower alleged that she timely made all three plan payments and submitted the requisite documentation, but was denied a permanent modification. The court ruled that the borrower properly stated a claim for breach of the trial plan agreement, even though the servicer never promised a permanent modification. (*West*, *supra*, 214 Cal.App.4th at 798.)

This holding runs counter to the Court of Appeal's opinion in *Nungaray v. Litton Loan Servicing, LP* (2011) 200 Cal.App.4th 1499 ("*Nungaray*"). In *Nungaray*, like *West*, the borrowers alleged that they entered into and fully performed a HAMP trial period plan and were entitled to a permanent modification. But *Nungaray* concludes that "[a]s a matter of law, there was no contract here." (*Id.* at 1504.)

Quoting portions of the trial plan, the court in *Nungarary* found that the trial plan "is not a modification of the Loan Documents" and the loan would not be permanently modified unless the borrowers "meet all of the conditions required for modification" including the borrowers' receipt of a "fully executed copy of a Modification Agreement." (200 Cal.App.4th at 1504.) The borrowers were not entitled to a modification absent receipt of a final, fully executed modification agreement.

West does not even mention *Nungaray*, and all but concedes that the trial plan itself does not entitle the borrower to a permanent modification. (*West*, *supra*, 214 Cal.App.4th 797–798.) The court also pointedly declined to consider whether the trial plan may be unenforceable for lack of consideration, offer and acceptance, certain terms, or any element necessary to create an enforceable contract because the servicer apparently did not raise those issues. Instead, the court relied on the servicer's HAMP agreement with the federal government.

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"When Chase Bank received public tax dollars under the Troubled Asset Relief Program, it agreed to offer TPP's and loan modifications under HAMP according to guidelines, procedures, instructions, and directives issued by the Department of the Treasury." (*West, supra*, 214 Cal.App.4th at 797.).) Specifically, the court cited U.S. Department of the Treasury HAMP Supplemental Directive 09–01: "If the borrower complies with the terms and conditions of the [TPP], the loan modification will become effective on the first day of the month following the trial period…." So the servicer "must offer" a permanent modification even though the trial plan provided only that "we'll consider you" for one, the court ruled.

By reaching beyond the trial period plan the court in *West* impliedly found that the servicer participation agreement was enforceable by borrowers. In so doing, the court ignored the general rule that parties benefitting from a government contract are generally assumed to be incidental beneficiaries, and may not enforce the contract absent a clear intent to the contrary. Government contracts often benefit the public, but individual members of the public are treated as incidental beneficiaries unless a different intention is manifested. (*Klamath Water Users Protective Ass'n v. Patterson* (9th Cir. 2000) 204 F.3d 1206, 1210–1211.)

Nothing about HAMP demonstrated a clear intent to grant the borrowers enforceable rights. There is no reference to individual borrowers regarding remedies under the HAMP agreements, only the federal government. (*Newell v. Wells Fargo Bank, N.A.* (N.D.Cal. Jan. 5, 2012) 2012 WL 27783, *6–*7.)

A number of courts in the Ninth Circuit have addressed whether borrowers are third party beneficiaries of a HAMP servicer participation agreement. The overwhelming majority of those courts have held that borrowers are not third party beneficiaries of that government contract. (*See, e .g., Albert v. Wells Fargo Bank, N.A.* (N.D.Cal. Apr. 11, 2012) 2012 WL 1213718, *3; *Gutierrez v. PNC Mortgage* (S.D.Cal. Mar. 26, 2012) 2012 WL 1033063, *12; *Dodd v. Federal Home Loan Mortgage Corp.* (E.D.Cal. Dec. 19, 2011) 2011 WL 6370032, at *12; *Hunter v. CitiMortgage, Inc.* (D.Ariz. Oct. 5, 2011) 2011 WL 4625973, at *2; *Ottolini v. Bank of Am.* (N.D.Cal. Aug.19, 2011) 2011 WL 3652501, at *10; *Kim v. Bank of Am.* (W.D.Wash. Aug.11, 2011) 2011 WL 3563325, at *3–4; *Warner v. Wells Fargo Bank, N.A.* (C.D.Cal. June 21, 2011) 2011 WL 2470923, at *3.)

But the Court of Appeal in *West* ignored this federal caselaw holding that HAMP is not privately enforceable, and the court's own precedent in *Nungaray* holding that a trial period plan does not create a right to a permanent modification absent a signed modification agreement.

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