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Mixed Messages on Mortgage Foreclosures

Roger Bernhardt
Golden Gate University School of Law, rbernhardt@ggu.edu

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Midcourse Corrections.

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Aceves v U.S. Bank

The Second District's decision in *Aceves v U.S. Bank N.A.* (2011) 192 CA4th 218, 120 CR3d 507 leaves me unsure of who won this latest battle on wrongful foreclosure litigation in California: the proponents or the opponents. On the one hand, the borrower won by getting her complaint against the lender moved beyond the demurrer stage. But, on the other hand, her victory may have been more than offset by her inability to have the trustee sale set aside and her other contentions about sale irregularity accepted.

The Estoppel Claim

The most pronounced feature of the opinion was the holding that the lender was guilty of promissory estoppel for telling its borrower that it would not negotiate with her until after she abandoned her bankruptcy defenses and then—after she had complied—foreclosing rather than negotiating. But I cannot consider the outcome a great victory, since the allegations of the complaint made this an even easier case for promissory estoppel than what had happened in *Garcia v World Savings* (2010) 183 CA4th 1031, 107 CR3d 683, on which I commented last year (see 33 CEB RPLR 73 (May 2010)): The promise was clearer, the detrimental reliance more serious, and the borrower had no dirty hands to clutter the issues. What these two decisions on the same issue should do is truly convince lenders that they will get into trouble by making promises to delay trustee sales and then not honoring them.

But the "trouble" that a lender may have to face is damages, rather than sale invalidation, even when—as here—it appears that there was no bona fide third-party purchaser able to rely on the recitals of validity in the trustee's deed. A trustor's damages may amount to little more than her lost equity, which might not be very large if the property was already over-encumbered, as is so often the case. Attorney fees may also be involved, but because class actions are unlikely in these particularized situations, those will not be significant either.

In addition, the burden imposed on a lender in these promissory estoppel circumstances is not a duty to actually modify the loan or to successfully conclude a forbearance, but merely an obligation to engage in negotiations and to delay foreclosing while the negotiations are going on. Because there are numerous federal and state laws already requiring such activity, what this decision really adds is a remedy that the new statutes failed to include. See my Editor's Takes on *Mabry v Superior Court* (2010) 185 CA4th 208, 110 CR3d 201 (33 CEB RPLR 112 (July 2010)), and *Vuki v Superior Court* (2010) 189 CA4th 791, 117 CR3d 86 (34 CEB RPLR 31 (Jan. 2011)).

But, conversely, the fact that this lender who was allegedly guilty of promissory estoppel was still allowed to hold onto the property it had acquired at its foreclosure sale could mean that a borrower who was misled might nevertheless be subject to a successful unlawful detainer action and would need to find another place to live while her lawsuit was going on. Protracted litigation is not as advantageous for a defaulting borrower as it is when she can stay in the property without having to pay her mortgage when her lender is under an injunction against foreclosure. See my Midcourse Corrections column, *The Cost of Defaulting* (33 CEB RPLR 10 (Jan. 2010)), also available at www.rogerbernhardt.com.

The Other Nonirregularities

This trustor had some other interesting challenges to the conduct of the foreclosure proceedings, but the appellate court's rather peremptory dismissal of them constitutes bad news for the foreclosure defense bar if other courts follow the same reasonings.

The trustor claimed that the substitution of trustee was improper because it had been signed only by the bank's attorney-in-fact, to which the court replied that there was no authority for saying that was improper when the Civil Code (and the deed of trust) permits an attorney-in-fact to sign the substitution. Allowing a junior officer of the beneficiary to execute the substitution of trustee form seems, in and of itself, appropriate, since obviously some human being employed at the bank has to sign such documents.

The opinion says that the original lender (Option One) assigned the deed of trust to US Bank on March 25 and, on the same day, US Bank substituted in Quality Loan as the new trustee (the old trustee's name is not given). The briefs make it appear that the substitution was signed by an officer of Quality—who may not, at that date, have been an employee either of the bank or of the old trustee. Perhaps Quality's assistant vice president could have still qualified as an attorney-in-fact for US Bank, but the circumstances start to look dangerously like the robosigning controversy that has bedeviled the industry so much lately. In the midst of our recent fussiness about proper signing of notices of default, the court's rejection of this trustor's contentions as to improper substituting of trustees seems oddly cavalier.

More distressing to foreclosure defense attorneys should be the court's rejection of the trustor's second objection that the notice of default "mistakenly identified Option One as the beneficiary under the deed of trust when US Bank was actually the beneficiary." That was a clear irregularity being alleged, and the opinion does not dispute that contention. However, the court responds that "it is of no legal consequence. Aceves did not suffer any prejudice as a result of the error" (because the Notice of Default she received advised her to contact the trustee, not the lender, to discuss matters).

This was utterly harmless error, but it was error. There is great uncertainty in the foreclosure field about when and how we decide that an error is to be treated as harmless or consequential. In *Knapp v Doherty* (2004) 123 CA4th 76, 20 CR3d 1, cited in the opinion, a prematurely sent notice of sale was forgiven because it still gave the trustor more than the statutory wait time before the actual sale. But on the other hand, in *Dimock v Emerald Props. LLC* (2000) 81 CA4th 868, 97 CR2d 255 (not cited in the opinion), a foreclosure notice sent by the wrong trustee was not excused, even though it looked as harmless as the mistake in *Knapp*. See my Editor's Takes on *Knapp* (28 CEB RPLR 21 (Jan. 2005)) and *Dimock* (23 CEB RPLR 250 (Aug. 2000)).

It is probably as safe to predict that lenders make lots of mistakes while foreclosing as it is also to predict that most of those mistakes don't cause any particular harm. If harm from a mistake must also be shown, then most attacks on foreclosure sales will probably fail because attacking trustors are often in arrears anyway and usually lack sufficient funds to cure their defaults. Inclusion of a prejudice requirement would probably resolve most of the robosigning and "show me the note" challenges in favor of the lending industry. On the other hand, if any mistake makes a foreclosure sale ipso facto invalid, then many defaulting trustors may be able to stay in their properties, mortgage-free, for a long time.

Even with this uncertainty, the lessons for lenders are clear: Don't make mistakes (or promises you can't keep), and—if you do—try to correct them immediately; you never know how much your blunders can harm you. The lessons for trustors (and their attorneys) are cloudier: Check closely for mistakes made at any stage of the process, but don't be overconfident in estimating how much they will help.

Homeowner stated valid claims for promissory estoppel and fraud against lender who had promised to work with her to reinstate and modify her loan in exchange for her forbearance in converting her Chapter 7 bankruptcy to a Chapter 13 bankruptcy, but instead, on removal of bankruptcy stay, foreclosed on home.

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In April 2006, Homeowner obtained a loan secured by a deed of trust against her home, with initial monthly payments of $4857.09. In January 2008, Homeowner could no longer afford her monthly payments. Trustee recorded a "Notice of Default and Election to Sell Under Deed of Trust" in March 2008; shortly thereafter, Homeowner filed for Chapter 7 bankruptcy protection. Homeowner intended to seek her husband's financial assistance and then to convert her Chapter 7 bankruptcy to a more favorable Chapter 13 bankruptcy, so that she would be able to retain her home. On a promise from Lender that it would work with her to reinstate and modify her loan if she would forbear from converting her bankruptcy to Chapter 13, Homeowner did not oppose Lender's motion to remove the bankruptcy stay. On December 4, 2008, the court lifted the stay. Four days later, Lender scheduled Homeowner's home to be sold at public auction on January 9, 2009.

On December 10, 2008, Homeowner sent documents to Lender to achieve a loan reinstatement and modification. On December 23, 2008, Lender promised Homeowner that a negotiator would contact her on or before January 13, 2009 (which was 4 days after the proposed sale). A representative called Homeowner three times in December and January, culminating in a call on January 8, 2009 (the day before the auction), to verbally offer Homeowner reinstatement of the loan, with monthly payments of more than $7200 and the immediate payment of a $6500 deposit. Representative refused to put this offer in writing and Homeowner refused the offer. The home was sold on January 9, 2009. Homeowner filed suit for quiet title, slander of title, fraud, promissory estoppel, and declaratory relief, and also sought to set aside the trustee's sale and to void the trustee's deed on the sale of the home. The trial court sustained Lender's demurrer. The court of appeal reversed on causes of action for fraud and promissory estoppel.

Notably, the trial court found that Lender "never intended to work with [Homeowner] to reinstate and modify the loan." The court explained at length the advantages of a Chapter 13 bankruptcy proceeding over a Chapter 7 proceeding, with the primary advantage being that Homeowner could have retained her home. Nevertheless, a loan reinstatement and modification were even more appealing because then Lender could have "*modified* the terms of the loan, for example, by reducing the amount of the regular monthly payments or extending the life of the loan" (192 CA4th at 227; emphasis in original), which a bankruptcy court cannot do. Further, the time frame for repayment under a bankruptcy order is abbreviated to 5 years. The court of appeal held that Lender made a clear and unambiguous promise to work with Homeowner; Homeowner reasonably relied on that promise; that reliance was justifiable and foreseeable; and Homeowner was injured, most particularly by the loss of her home. The satisfaction of these four factors states a valid claim for promissory estoppel. No consideration for Lender's oral promise was required because "the doctrine of promissory estoppel is used to provide a substitute for the consideration which ordinarily is required to create an enforceable promise." 192 CA4th at 230, quoting *Raedeke v Gibraltar Sav. & Loan Ass'n* (1974) 10 C3d 665, 672, 111 CR 693. Although promissory estoppel will not support voiding the deed of sale or invalidating the foreclosure, it does provide a basis for damages.

The action for fraud was supported by the same facts, adding the existence of a false promise and promisor's knowledge of that falsity at the time—both of which were adequately pleaded by Homeowner. The court dismissed Homeowner's remaining complaints as lacking in legal merit. A substitution of trustee signed by an attorney-in-fact was not improper. An erroneous notice of default "is of no legal consequence" because Homeowner was not prejudiced by the error. Homeowner was awarded attorney fees and given the right to pursue her promissory estoppel and fraud claims in the trial court.