TORT LAW

DON'T BUY THAT BRIDGE IN BROOKLYN – REAL ESTATE TORT LAW

by Jeremy Robinson, Column Editor

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Well it is officially fall in San Diego, and as I type this at my humble dwelling, I am wondering what happened to all those "sunshine dollars" I was promised upon moving here. Overcast 65 degree days (18 degrees Celcius, for my international readers) do not seem to be the stuff of local realtors' dreams. Still, I consider myself lucky to have a dwelling at all, given that many people in this economy have lost or are in the process of losing their homes. In consideration of this, and in light of all the unsavory real estate practices coming to light in the press recently, I thought it might be appropriate to take a small detour from the usual escapades of this column and look at a few recent real property tort cases.

I'll start first with the home buying process itself. We all probably remember from law school that a real estate broker who represents the seller of property owes a duty of disclosure to the buyer. In particular, if the broker knows of facts that materially affect the value or desirability of the property and also knows that such facts are not within the reach of the diligent observation of the buyer, the agent must disclose them to the buyer. *Lingsch v. Savage* (1963) 213 Cal.App.2d 729, 736. See also, Civil Code §2079.16.

But, of course, no case is ever that cut and dry. In the recent matter of *Holmes v. Summer,* 2010 WL 3896726, Division 3 of the Fourth District was tasked with analyzing a uniquely modern twist on this age old duty. In *Holmes*, the defendant agent for a home seller in Huntington Beach offered the seller's home to plaintiff buyers for $749,000. What the agent declined to mention was that the home in question was encumbered with $1,141,000 in liens in the form of deeds of trust, $392,000 **more** than the sale price. Plaintiff buyers agreed to the sale, not knowing about the deeds of trust, sold their own house to enable them to complete the purchase and entered into escrow. Not surprisingly, escrow never closed because the lenders were not willing to reduce their liens that substantially (if at all) and the seller was unwilling to cover the difference. The plaintiffs then sued the broker for failing to disclose the liens against the property and the fact that there was a substantial likelihood the seller would be unable to convey clear title.

The agent demurred, arguing that agents should not be charged with predicting when a seller may or may not back out of escrow and also suggesting that requiring such a disclosure would violate their oath of confidentiality to the seller. The appellate court didn't buy either argument. The court held that when the agent knows the property is subject to liens and encumberances that

exceed the sale price of the property, such that a short sale or substantial contribution from the seller would be required to obtain clear title, the agent must disclose that to the prospective buyers so that the buyers can factor that into their decisions. Id. at *7.

As for the breach of confidentiality, the court noted that the information was not necessarily confidential in the first place, and even if it could be construed as such, the agent's duty under Civil Code §2079.16 trumps that consideration. *Holmes v. Summer, supra*, at p. *9. According to the court, "[i]n the presently downtrodden economy, it behooves us all for... members of the public to have confidence in real estate agents and brokers." *Id*. at *1.

At the other end of the spectrum is home foreclosure. Foreclosures have been the subject of numerous articles in the press lately, and are an indicia of the troubled state of the economy as a whole. But what can borrowers do if they feel they are being or have been wrongly foreclosed upon? The court (again Division 3 of the Fourth District) in *Mabry v. Superior Court* (2010) 185 Cal.App.4th 208 examined one potential remedy.

But first, a bit of background on the foreclosure process. California is a "nonjudicial foreclosure" state, meaning, unsurprisingly, that the lienholder (I'll call him the "lender" for the sake of convenience even though the actual holder of the lien (trust deed) is typically far removed from the original loan servicer) is not required to use the court system in order to effect a foreclosure sale. The lender cedes the ability to collect a deficiency judgment against the borrower (*i.e*., the difference between what the borrower owes and what the property fetches at auction) in a nonjudicial foreclosure, but the process is much more streamlined and therefore generally preferred. And while this procedure is doubtless a boon to our overburdened courts, it does also tend to strip the borrower of some of the protections provided by the judicial foreclosure process.

A foreclosure dispute can implicate a vast array of statutory schemes, including the Truth in Lending Act ("TILA"), 15 U.S.C. §§1601 *et seq*., the Real Estate Settlement Procedures Act ("RESPA"), 12 U.S.C. §§2605 *et seq*., and many others that are outside the scope of this column. Here, I wanted to focus mostly on one act in particular, the Perata Mortgage Relief Act, California Civil Code §§2923.5, 2923.6, 2924.8 and 2929.3.

The Perata Mortgage Relief Act is a recent addition to a detailed series of statutes spanning Civil Code §§2920 to 2967 that govern mortgages in California. The Act was urgency legislation drafted in response to the collapse of the housing market in California and the staggering number of properties being foreclosed upon. Among other things, the Act requires lenders to: (1) contact the borrower by phone or in person to "assess the borrower's financial situation and explore options for the borrower to avoid foreclosure" (Civ. Code §2923.5); (2) wait 30 days after this initial contact or after the lender has completed its due diligence in trying to contact the borrower before filing a notice of default; (Civ. Code §2923.5) and (3) provide the borrower with a 60-day eviction notice after instituting foreclosure proceedings (Civ. Code §2924.8).

Unfortunately, the drafters of the Act neglected to include any provisions describing how it may be enforced, who may enforce it or the remedies available for violations of the Act. This made construing it something of a challenge for the court in *Mabry v. Superior Court, supra*, 185 Cal.App.4th 208.

Mabry involved the all-too-common scenario of a borrower taking out a sizable home loan and then ending up unable to make the payments. The borrowers ended up filing for Chapter 11 bankruptcy protection and, after that case was dismissed, the lender began foreclosure proceedings. Shortly before the foreclosure sale was scheduled to take place, the borrowers filed a complaint against the lender alleging that the lender failed to comply with the notice and contact requirements of Civil Code §2923.5. The lender disputed these claims, and its notice of default included boilerplate language to the effect that it had tried to contact the borrowers, but to no avail. The borrowers filed an amended complaint adding class action allegations and sought multiple restraining orders to prevent the foreclosure sale from occurring, but the trial court ultimately vacated the TROs. The borrowers then petitioned the court of appeal for a writ of mandate and the court stayed all proceedings.

During the writ proceedings, the lender argued that: (1) the action is preempted by federal law; (2) there is no private right of action under Civil Code §2923.5; and (3) the Mabrys were required to at least tender all arrearages to enjoin any foreclosure proceedings. *Mabry v. Superior Court, supra*, 185 Cal.App.4th at 217. The court disagreed with each contention, but in so doing construed the remedies available under Civil Code §2923.5 extremely narrowly. The *Mabry* court first decided that there must be a private right of enforcement of the provisions of Civil Code §2923.5 because to hold otherwise would mean that the Legislature enacted a statute that was entirely illusory since there would be no penalty for failing to comply with it. Also persuasive to the court was the fact that Civil Code §2923.5 sets forth specific and detailed requirements that lenders **must** follow, whereas a similar statute, Civil Code §2923.6 (dealing with home loan modifications), only expresses the **desire** that lenders offer such services.

On the issue of preemption, the court held Civil Code §2923.5 was not preempted by federal law, but only because the **only** remedy provided is a postponement of sale before it happens **Id**. at 218 (emphasis added). Failure to comply does not cause any cloud on the property's title, meaning once the foreclosure sale has been completed, the borrower has no claim under Civil Code §2923.5. *Id.* See also, *Mehta v. Wells Fargo Bank, N.A.* (S.D. Cal. 2010) 2010 WL 3385020 [following *Mabry*]. Accordingly, while the court avoided the preemption issue, in the process it essentially gutted Civil Code §2923.5 of any real substance.

Both of these cases are, I suspect, just the proverbial tip of the iceberg. As I mentioned earlier, this is a complex area and it will be interesting to see how things play out both in the courts and legislatures. I hope this little digression has been of interest and I didn't step on the Real Property column editor's toes. I'm just hoping for some sunshine.