November, 2014

How Should the Law Treat Roommate Relationships? A Tale of Two Cases

Tim Iglesias

How Should the Law Treat Roommate Relationships? A Tale of Two Cases

Tim Iglesias

Introduction

How should courts construe the legal status of roommates vis-a-vis other occupants and third parties? Two courts came to diametrically opposed views. In *Fair Hous. Council v Roommate.com, LLC* (9th Cir 2012) 666 F3d 1216, reported at 35 CEB RPLR 54 (Mar. 2012), the Ninth Circuit presumed that roommates are intimate, opining: "Aside from immediate family or a romantic partner, it's hard to imagine a relationship more intimate than that between roommates." 666 F3d at 1221. More recently, in *Mercury Cas. Co. v Chu* (2014) 229 CA4th 1432, California's Fourth District Court of Appeal assumed that roommates are legal strangers unless evidence demonstrates otherwise. "We find no significance in the mere status of cohabitation." 229 CA4th at 1454.

Roommate.com employed a bright-line rule; *Mercury* appears to require a fact-based analysis to determine the nature of a roommate relationship from which legal rights and duties can be determined. Although *Roommate.com* was a fair housing case and *Mercury* is an auto insurance case, these different approaches to the legal status of roommates may impact a surprisingly wide range of real estate practice areas, including insurance, landlord-tenant law, condominium law, and zoning.

Mercury Cas. Co. v Chu

Hung Chu and Tu Pham were roommates. In October 2008, Pham was injured in an accident while he was riding in Chu's car, which Chu was driving. Pham obtained a $333,300 personal injury judgment against Chu. Chu was insured by Mercury Casualty Company. Mercury defended Chu but reserved its rights, asserting that Pham's injuries were not covered by the policy. Mercury sought a declaratory judgment that it did not have a duty to indemnify Chu for Pham's judgment because Pham was an "insured" under Chu's policy, but the policy's "resident exclusion" clause excluded Pham from policy benefits coverage because he lived with Chu. Chu filed a cross-complaint for bad faith, breach of contract, and negligence, in which Pham joined.

The trial court granted Mercury's motion for summary adjudication and judgment on the pleadings. On appeal, the Fourth District Court of Appeal reversed, holding as a matter of first impression that the roommate Pham could not be included as "an insured" under Chu's policy and therefore could not be excluded from coverage under the policy by the "resident exclusion" clause in Pham's lawsuit against Chu. The court's decision explained that the "resident exclusion" clause in Mercury's policy was an overbroad expansion of a statutorily permitted exclusion and was also contrary to public policy.

California Ins C §11580.1(c)(5) specifically authorizes coverage exclusion for "Liability for bodily injury to an insured or liability for bodily injury to an insured whenever the ultimate benefits of that indemnification accrue directly or indirectly to an insured." In other words, the policy may exclude paying benefits from otherwise covered incidents to people who will or might pass that money on to the (named) insured. This is the legal basis for the "resident relative" exclusion, which would exclude, for example, a wife, brother, or child of the named insured from benefit coverage under the policy. The prototypical example is that a wife cannot collect benefits under the insurance policy if she sues her husband for injuries she suffered when he was negligently driving the family car. The rationale for this permitted exclusion is the high degree of risk that husband and wife (or other relatives) could collude to fraudulently claim injury and then share the benefits paid from the policy. Cumulatively, the effect of such claims could substantially impact the pool of money available to pay legitimate claims. Therefore, the statute allows this exclusion. The court found the "resident relative" exclusion well established and consistent with the public policy protecting insurers from collusion by insureds. However, Mercury's policy included a "resident exclusion" provision that expanded this exclusion to nonrelative residents, *i.e.,* mere cohabitants of insured persons. The court found this exclusion was not intended by the legislature and was contrary to public policy.

In brief, the court examined whether the relevant provisions of California's extensive mandatory insurance statutory scheme (Ins C §§280, 11580.1, and 11580.06), read as a whole, limited how an insurer may define "an insured" for purposes of excluding that insured from coverage benefits under the policy. Generally, liability insurance must be supported by an insurable interest in the covered risk. In other words, to be "an insured," a person must be capable of being held liable for harm caused by the named insured of the vehicle. So, the court inquired: Does a roommate like Pham have an insurable interest in his roommate's auto liability policy? The court reasoned that someone who is only a roommate or cohabitant—neither a relative, nor a permissive user of the vehicle, nor a business partner—does not have an insurable interest. Pham's status as merely Chu's roommate would not provide any cognizable legal basis for anyone to sue Pham for damage caused by Chu's car or by Chu's actions as a driver. "Stated another way,

Mercury would not be exposed to any risk of liability with respect to Chu's vehicle simply by the fact he has roommates." 229 CA4th at 1453. The court held that the policy justification for the "resident relative" exclusion—avoiding potential collusion among insureds against the insurer—does not apply to mere cohabitants or roommates. The court suggested that "Mercury named Pham 'an insured' for the sole purpose of excluding him from coverage for bodily injury caused by use of the insured vehicle by the named insured." 229 CA4th at 1454.

Mercury argued that the risk of collusion by roommates was similar to that by relatives. The court rejected this argument because "the possibility of collusion exists to a certain extent in any case" (229 CA4th at 1455) and because Mercury had not explained why cohabitants are a greater risk than friends, neighbors, or coworkers. From a public policy perspective, Mercury's resident exclusion provision drew the circle too widely. California's financial responsibility laws intend to provide monetary protection to the public.

> If an insurer can define "an insured" as including a large population of the public (such as all persons inhabiting a large apartment complex on the basis of cohabitation) without regard to insurable interest, it would defeat the public policy behind requiring mandatory automobile insurance liability and undermine financial responsibility laws.

229 CA4th at 1455. The court explained that the normal adversarial process was sufficient to uncover fraudulent lawsuits; a prompt and effective investigation by insurers could quickly establish the essential facts of any suspected collusion.

Insurers may be less optimistic than the court about insurers' capacity to "quickly establish the essential facts" and, perhaps, the ability of courts and juries to recognize fraudulent lawsuits. Nonetheless, based on the *Mercury* opinion, insurers must redraft their clause defining "an insured," their exclusion clause, or both.

Mercury: Roommates Are Legal Strangers Without Proof of More

The *Mercury* opinion takes the view that, at least for insurance coverage purposes, courts should not make any presumptions about roommate relationships or, if they do, they should presume roommates are legal strangers without specific other evidence. "We find no significance in the mere status of cohabitation." 229 CA4th at 1454.

Although the case was decided on statutory interpretation, the trial court heard, and the court of appeal considered, numerous facts discovered for trial about the relationship between Chu and Pham. Chu and Pham were roommates at a home owned by one of Chu's relatives for about two years. They "shared a bedroom ... to minimize their expenses" and each paid rent separately to Chu's aunt. They mutually described each other as "friends" (229 CA4th at 1438), but the court opined that they did not have a "close friendship." 229 CA4th at 1453. Chu described Pham as a "family friend" he met in Vietnam. 229 CA4th at 1439. Chu ate meals with his relatives every day, while Pham ate with the family about half of the time. After the accident, Chu and Pham continued to live together at subsequent residences until Pham returned to Vietnam in June 2012 after earning his college degree. While they lived together, they "drove to school together" but "did not attend social functions together." Rather, Chu "spent time with his own friends." 229 CA4th at 1440.

None of these facts moved the court to think that the roommate relationship between Chu and Pham was relevantly similar to a resident relative relationship.

Roommate.com: Roommates Are Inherently Intimate

When a fair housing group sued an Internet roommate-matching website called Roommate.com, a long and complex litigation ensued. Other Internet roommate-matching websites (*e.g.,* Craig's list) had successfully claimed immunity from fair housing liability under the federal Communications Decency Act (CDA) because they merely served as electronic bulletin boards. However, the design of the Roommate.com website required users to disclose their roommate preferences regarding sex (male or female), sexual orientation, and familial status (the presence of minor children in the household)—precluding it from enjoying CDA immunity. Roommate.com's operations used this information to sort, steer, and match users with each other, raising a distinct discrimination issue under the federal Fair Housing Act (FHA) and the California Fair Employment and Housing Act (FEHA).

Late in the litigation, Roommate.com claimed that application of fair housing laws to a homeowner or renter selecting a roommate would violate the user's federal constitutional right of freedom of intimate association. Applying the analysis from *Board of Directors of Rotary Int'l v Rotary Club* (1987) 481 US 537, 107 S Ct 1940, the court agreed that the case presented this constitutional problem because the right to intimate association also implies a right to *not* associate.

The court found that Roommate.com had standing to raise the issue on behalf of its users. The court then invoked the canon of constitutional avoidance, which allows courts to construe statutes to avoid constitutional problems if the construction is not plainly contrary to legislative intent. *Frisby v Schultz* (1988) 487 US 474, 108 S Ct 2495. Despite numerous FHA cases applying the statute to shared living situations, the court found the FHA's definition of "dwelling" and FEHA's definition of "housing accommodation" to be similarly ambiguous

regarding whether they applied to shared living units. It construed these terms to mean independent housing units. On the court's interpretation, shared living units (such as when people take on roommates) are not subject to the FHA or FEHA because the selection of roommates is outside the scope of the FHA and FEHA. Therefore, Roommate.com had no liability under either statute.

The court recognized that the right of freedom of intimate association protects only "highly personal relationships," citing *Roberts v U.S. Jaycees* (1984) 468 US 609, 618, 104 S Ct 3244. The court applied the traditional test, articulated in *Rotary Int'l*, which considers the "size, purpose, selectivity, and whether others are excluded from critical aspects of the relationship." 481 US at 546. Yet, while no evidence was taken about any roommate relationship of Rooommate.com's users, or of any actual roommate relationship, the court found that all roommate relationships meet this standard, opining: "Aside from immediate family or a romantic partner, it's hard to imagine a relationship more intimate than that between roommates, who share living rooms, dining rooms, kitchens, bathrooms, even bedrooms." 666 F3d at 1221. The court applied what might be called structural determinism to find that all roommate relationships presumptively qualify for constitutional protection under the test. There was no attention to the intentions of roommates or to any capacity for (formal or informal) bargaining or contractual arrangement of their relationship.

What Difference Does *Mercury* Make?

Mercury raises numerous issues in the insurance context. To the degree that "resident exclusion" clauses are common in homeowner's insurance policies and renter's insurance policies, *Mercury* may invalidate them. One might wonder whether the court's rationale could even undermine the currently accepted "relative resident" exclusion. After all, the risk of collusion among relatives might vary depending on their closeness; *e.g.,* contrast a husband and wife or father and child with uncle and his niece or two cousins who live together. This issue is especially salient as the nature of families is changing, with the proliferation of intergenerational families, boomerang children, and blended families.

There is a slew of unresolved roommate conundrums in the residential leasing context. Although *Mercury* is not a residential landlord-tenant case, and Pham was clearly a rent-paying tenant vis-a-vis the landlord, it may shed some light on these issues because of the approach it suggests.

Most leases define a "tenant," a "guest," and a "sublessee," but there are no clear generally accepted definitions for a "roommate." Colloquially, a roommate may be a tenant on the lease, but often a roommate is an occupant who is neither a tenant, a guest, nor a sublessee, and is someone who may or may not contribute to paying rent. Another possible legal status for a roommate is as a "licensee" of the tenant, under which the roommate has the tenant's explicit and revocable permission to be on the premises, usually for a defined purpose and limited scope, and who may or may not pay a fee to the tenant for this privilege. This undefined status of roommates raises issues both in legal disputes between roommates and other occupants (especially tenants) and between roommates and third parties, especially landlords. The issue can be framed as:

- What is the scope of rights that a leasehold interest acquires?
- To what degree can the landlord limit these rights if they are not already defined by statute or ordinance?

As noted in a prior comment, a lease can explicitly limit occupancy to the persons named in the lease; some residential lease forms do so. *Parkmerced Co. v San Francisco Rent Stabilization & Arbitration Bd.* (1989) 215 CA3d 490, reported at 13 CEB RPLR 58 (Feb. 1990). If so, then a landlord would presumably have a right to refuse the roommate occupant. See California Landlord-Tenant Practice §§5.28–5.29 (2d ed Cal CEB). But this approach is in tension with California's rules allowing residential tenants some right to sublet. As the prior commenter noted, "[I]t is conceivable, however, that occupancy limitation clauses will be subjected to a reasonableness standard because they restrain the tenant's ability to sublet." *Parkmerced, supra*. But it is not always clear that taking on a roommate amounts to subletting, especially when the named tenant continues to occupy.

Moreover, it is not even clear when an occupant is a "resident." The *Mercury* court quotes *Kibbee v Blue Ridge Ins. Co.* (1999) 69 CA4th 53, 61, reported at 22 CEB RPLR 82 (Apr. 1999), for the proposition that residence "connotes any factual place of abode of some permanency, more than a mere temporary sojourn." Unfortunately, this definition can be hard to apply, especially when documenting a roommate's stay can be costly and potentially intrusive to a tenant's privacy (eliciting complaints of harassment) and when roommates can resort to a wide range of tactics to avoid detection. Nor is the required legal process for getting the roommate to leave (unlawful detainer?) clear. Even if a landlord cannot evict a roommate merely for being an unauthorized occupant, can she do so if the roommate breaches some specific covenant in the lease? In this case, can the landlord just force a roommate to leave without evicting the named tenant? If there is domestic violence between the tenant and a roommate and the tenant is ordered to leave, does the roommate have right to continue occupancy?

Similar issues are likely to arise in the common interest community context (*e.g.,* condominiums) when owners become landlords by renting their units. These developments' conditions, covenants, and restrictions (CC&Rs) and homeowner association rules often attempt to regulate such leasing. Do they also anticipate and resolve these potential roommate issues?

In an era of Airbnb, what is the legal status of the temporary occupant who pays to stay in the unit? Tenants who use Airbnb often take in such occupants. Clearly, the occupant is not a tenant or sublessee. She is also not a guest, since guests typically do not pay for lodging. Is she a roommate for the time of the occupancy? Making a direct link to the insurance issue from the *Mercury* case, how likely is it that an Airbnb guest could conspire with the Airbnb host to make a claim against Airbnb's $1,000,000 insurance policy for loss and damage to the premises?

The answers to some questions are clear in rent control jurisdictions in which tenants have more defined rights. In these jurisdictions, the landlord has less scope to define a "roommate" in the lease. For example, Berkeley's rent control ordinance includes an expansive definition of "tenant" that includes "any other person entitled to the use or occupancy of such rental unit." *DeZerega v Meggs* (2000) 83 CA4th 28, reported at 23 CEB RPLR 285 (Oct. 2000). This definition can include a roommate, at least one who contributes to paying rent.

Does a roommate become a tenant if the landlord accepts rent from her? The answer is "Yes," at least in the rent control jurisdiction of the City of West Hollywood. *Getz v City of W. Hollywood* (1991) 233 CA3d 625, reported at 14 CEB RPLR 309 (Nov. 1991). Similarly, in San Francisco (another rent control jurisdiction), if a landlord acquiesces to a roommate's occupancy, including by accepting rent money from her, the roommate will gain the legal status and rights of a tenant. *Parkmerced Co. v San Francisco Rent Stabilization & Arbitration Bd., supra*.

It is unclear whether the answers for rent control jurisdictions would apply in other localities.

The *Mercury* Court Presents the Better View

At this point, the *Mercury* case only applies to insurance contracts and the *Roommate.com* case only applies to fair housing law. But courts could look to either case for guidance on other roommate issues as they arise in other legal contexts.

In the author's view, the *Mercury* court's fact-based approach seems preferable. Cohabitation alone does not necessarily imply any relationship, both because of the wide variety of types of cohabitation relationships (including mere economic convenience, companionship, and intimacy) and because while they cohabit, occupants make many decisions to control the relationship (if any) that develops. For this reason, discerning the nature of a roommate relationship requires attention to the mutual intentions of the parties. Cohabitation is neither a necessary nor a sufficient condition for intimacy. A couple who share a dwelling and even a bed every night may lack any real intimacy. In contrast, individuals who share only an Internet connection and never meet in person may develop intensely intimate relationships.

Roommate.com was poorly reasoned and not well supported by authority. Arguably, the court's presumption about roommates *constructed* the very constitutional problem that in its view necessitated the application of the principle of avoidance. (For an extended comment on the *Roommate.com* case, see Iglesias, *Does Fair Housing Law Apply to "Shared Living Situations"? Or, the Trouble with Roommates*, Cal Real Prop J, Vol 31,-No. 4 (Fall 2013).

The *Mercury* decision's approach is consistent with how roommate issues have been treated in other areas of law in California. For example, under California's community property law, mere cohabitation and even sexual intimacy do not trigger any special property relationships between the cohabitants that courts will recognize at the termination of the relationship. *Marvin v Marvin* (1976) 18 C3d 660. Rather, mere cohabitants are in a "meretricious" relationship in which the law treats them as legal strangers and applies only traditional common law (property, contract law, and tort) that would otherwise regulate their transactions. However, if a party can demonstrate that she had a valid contract (express, oral, or implied-in-fact) that intended to regulate their property relationship as a couple, then they are in a "*Marvin* relationship." The court will enforce the terms of that contract, including applying the whole range of equitable remedies.

The issue of how to legally characterize roommates also arises in the zoning context, most saliently in the definition of "family" that local jurisdictions employ to limit the use of residential dwellings in "single family" zones. Parallel to the "resident relative" and "other resident" distinction drawn in the *Mercury* opinion, in the zoning context, courts regularly treat blood relatives differently than unrelated persons living together. In *Moore v City of E. Cleveland* (1977) 431 US 494, 97 S Ct 1932, the Court found a zoning ordinance preventing a grandmother from living with her grandson unconstitutional. In contrast, in *Village of Belle Terre v Boraas* (1974) 416 US 1, 94 S Ct 1536, the Court upheld the village's single family zoning ordinance excluding cohabitating students because they did not qualify as a "family" under the ordinance. See Iglesias, *Defining "Family" for Zoning: Contemporary Policy Challenges,*

Legal Limits and Options, Zoning & Planning L Rep, Vol. 37, No. 5 (May 2014).

But in *City of Santa Barbara v Adamson* (1980) 27 C3d 123, reported at 3 CEB RPLR 99 (July 1980), California's Supreme Court found that the California Constitution's right to privacy voided a local zoning code that prohibited more than five unrelated people from living together in a single family zone. Following *Adamson*, many cities allow unrelated people to live in single family zones if they constitute "a single-housekeeping-unit," which means operating as a functional family, *e.g.,* cooking and eating together regularly. These cities require something more of roommates than merely cohabitating in the same building to claim legal status as "family." This issue is particularly relevant, given changing societal definitions of "family."

The varied legal issues raised by roommates can be reduced to these two:

- How to characterize mere cohabitation; and
- What legal rights and duties, if any, to infer from cohabitation vis-a-vis other cohabitants or third parties.

There are two kinds of cases that arise, each with a different key issue:

- The nature of the relationship among the occupants, as in the *Roommate.com* case; or
- The relationship between the roommate and some third party, such as a landlord, a city, or an insurance company, as in the *Mercury* case.

From a landlord's perspective, if statutes and ordinances allow it, the lease should contain a provision defining a roommate. This could be combined with a notice requirement to the landlord for taking on a roommate and allowing exceptions with the landlord's explicit permission (*e.g.,* for a tenant's mother to stay for a month to help care for a new baby). To be useful, of course, this definition would need to be enforceable. This partial solution still leaves information costs and unresolved enforcement issues.

The *Mercury* opinion does not provide specific and complete guidance on all of the issues raised in this article. However, it does imply an approach: If the lease does not define "roommate," then there is a rebuttable presumption that a mere cohabitant is a legal stranger to other cohabitants (*i.e.,* tenants) and to third parties unless additional facts provide otherwise. This presumption is better that inferring that a roommate is a "tenant," a "guest," or a "sublessee" because each of these legal statuses has distinct and substantial legal significance.

A rebuttable presumption that a mere cohabitant is a legal stranger combined with some specific types of facts that would rebut the presumption relevant for a particular legal context may be the most efficient and effective kind of legal rule, as opposed to a bright-line rule or a factor test. For example, sometimes cohabitants have other legally significant dimensions to their relationship that take them out of the mere cohabitant category (*e.g.,* by contract). In the landlord-tenant context, payment of rent (or rent equivalent) could have decisive significance.

The Law of Roommates Is Important and Requires More Development

Whenever there are financial hard times, people tend to reduce their housing costs by doubling up and taking (or becoming) roommates. These issues are not going away on their own. Eventually, the legislature or courts will need to fashion additional legal rules regarding roommates in a wide variety of contexts. They will need to define "roommate" and to articulate what the legal rights and duties of roommates are to each other and to third parties (such as landlords and insurers). This jurisprudence will also need to define the scope of freedom of contract regarding the status, rights, and duties of roommates, as the *Mercury* court began to do in the auto insurance context. Distinct tests will probably be needed for different contexts, to take into account the variety of relationships among occupants and diverse interests of parties in those contexts. Based on these rules, landlords and others can then develop best practices for drafting lease or contract terms and for responding to the actions of tenants and roommates.

The author is grateful to Roger Bernhardt and Christine Tour-Sarkissian for their help in developing this article.

When Is an Elder's Property "Taken"?—*Bounds v Superior Court*

Christine Tour-Sarkissian

Introduction

Real estate lawyers often find themselves in deals where at least one of the parties is elderly. Because of Welf & I C §15630 (part of the Elder Abuse-and Dependent Adult Civil Protection Act (EADACPA)), transactional attorneys need to know what precautions they should take to make a real estate deal hold. Litigators need to know what would it take to draft or defend against an elderly plaintiff's complaint.

Bounds v Superior Court

Bounds v Superior Court (2014) 229 CA4th 468, reported at 36 CEB Est Plan Rep 61 (Oct. 2014), recently held that to allege a "taking" under EADACPA, it was

sufficient to plead that an elder had entered into a real estate agreement that significantly impaired the value of her property. It did not matter that the agreement had not been performed and title had not transferred.

Until *Bounds* came down, no case had given us a binding authority on what the legislature had meant by the word "takes" in Welf & I C §15610.30(a)(1): "Financial abuse" of an elder occurs when a person "[t]akes, secretes, appropriates, obtains, or retains real or personal property of an elder."

In *Bounds*, an 88-year-old widow suffering from Alzheimer's alleged that her property was "taken" since defendants had engaged in abusive conduct toward her, resulting in her signing documents authorizing the sale of her real property so that she could not enter into another contract with third parties or get a loan secured by the property, thus impairing her property rights. However, because escrow was cancelled and the agreement was not *consummated* (and thus plaintiff retained title and remained in possession of the property), the trial court sustained defendants' demurrer without leave to amend. The court of appeal disagreed, adopting plaintiff's arguments and concluding that because "property rights" included, among other things, the right to use and sell property, and plaintiff's rights had been negatively affected, she had properly pleaded a "taking" under the statute.

Elder abuse allegations carry a broad spectrum of damages, *i.e.,* equitable remedies such as rescission, compensatory damages (including noneconomic damages such as pain and suffering), treble damages or punitive damages, and, most importantly, attorney fees. Thus, plaintiffs will strive to make a prima facie case and defendants will want to defeat it at the stage of the initial pleadings.

What Should the Financial Elder Abuse Complaint Include?

It is well settled that plaintiffs must plead a minimum number of allegations to overcome a demurrer or motion to strike. Most of these allegations track the language of the statute (Welf & I C §15610.30) as follows:

- The victim was "elderly" (age 65 or older).
- The defendant took, secreted, appropriated, obtained, or retained real or personal property of an elder
  - For a wrongful use or with the intent to defraud or both; or
  - By undue influence, as broadly defined in Welf & I C §§15610 and 15610.70.
- Defendant knew or should have known that this conduct was likely to be harmful to the elder.
- Defendant caused the elder to be deprived of a property right.

Some of the Ways to Defend Against Financial Elder Abuse Claims

Based on the available case law, defense counsel should look for:

- The claim was not brought within four years after the plaintiff discovered or through reasonable diligence should have discovered the facts constituting the financial abuse (Welf & I C §15657.7).
- The complaint did not properly track the language of the statute.
- Plaintiff is not elderly or vulnerable within the meaning of the statute.
- Plaintiff does not have standing to bring the action, *i.e.,* when a spouse is the perpetrator of the financial abuse, he/she would be statutorily barred from standing to sue.
- Plaintiff is not an interested person. Counsel should look into the interplay between the cause of action and its effect on the family members as beneficiaries.
- The complaint does not state specific facts to support each alleged violation of elder abuse, as general allegations of wrongdoing will be insufficient to state a claim.
- Plaintiff consented to the deal and there is evidence from a health care professional that she was competent to transact.
- Defendant did not act wrongfully and with the requisite knowledge (actual or constructive) that his conduct was harmful to plaintiff.
- Defendant did not exert undue influence on the elderly person (need to track the language of the new undue influence statute under Welf & I C §15610.70).
- Defendant has an immunity or privilege under California law, *i.e.,* the beneficiary of a deed of trust is entitled to the protection of a qualified privilege from liability under EADACPA in connection with its nonmalicious attempt to take real property from a protected individual through a nonjudicial foreclosure process (*Consumer Solutions REO, LLC v Hillery* (ND Cal 2009) 658 F Supp 2d 1002).
- The claim is subject to arbitration per the parties' agreement (so as to avoid a jury trial).
- Even if the court were to find a "taking," plaintiff suffered no damages.
- A federal statute preempts the cause of action for elder abuse, *i.e.,* a borrower's elder abuse and negligence claims against a lender were preempted by the federal Home Owner Lender Act, which addresses consumer-credit cost disclosures. 15 USC §1641.
- Plaintiff has failed to meet its burden of proof by a preponderance of the evidence at trial as required by Welf & I C §15657.5(a) to recover such damages.
- Plaintiff did not meet its burden of proof (at trial) by clear and convincing evidence to recover remedies as punitive damages or treble damages.

What Are the Consequences of Bounds on Elders' Rights to Freely Contract?

After *Bounds*, if an elderly person wants to enter into a real estate contract, several questions arise:

- Will she have to do more convincing that she is not vulnerable or does not need any protection?
- What kind of document would she need to give to anyone entering into a real estate deal with her to dispel the fear that the deal can be construed as elder abuse?
- Will bringing a doctor's certificate attesting to her mental state be enough in light of *Bounds*?
- How often should the doctor's clean bill of health be sought, since the mental health condition of an elderly person is likely to change rapidly?

How Does Bounds Affect Real Estate Lawyers?

- Attorneys are not immune, since they too can be potentially accused of elder abuse. This may mean that fewer attorneys will be willing to represent elderly people for fear of being sued.
- An attorney handling financial elder abuse matters should do a thorough investigation before taking on a case. Deficient investigation of an elder abuse claim often leads to deficient evidence. Making matters worse, elderly victims can make poor witnesses who are susceptible to impeachment.
- The attorney taking on an elderly client should determine the client's mental state. As such, the ABA Model Rules of Professional Conduct enumerate five factors for a practitioner to consider in evaluating the capacity of a client:
  - The client's ability to articulate reasoning leading to a decision;
  - Variability of state of mind;
  - The ability to appreciate consequences of a decision;
  - The substantive fairness of the decision; and
  - The consistency of a decision with the known long-term commitments and values of the client. ABA Model Rules of Prof. Cond 1.14, Comment 6 (2012).
- Once the attorney decides to take on the case, he or she should insist on having the elderly client involved in deals or litigation provide, on a periodic basis, a medical report from a physician attesting to the client's mental health. This should be done even at the inception of the representation.
- The attorney representing an elderly client should memorialize everything in writing, lest he or she be later accused of elder abuse.
- The attorney should have the elderly client communicate with the attorney in writing (e-mail is preferable whenever possible), so as to preserve the evidence for future use.
- The attorney planning ahead needs to collect witnesses attesting to the elderly client's mental state at every step of the transaction or the litigation.
- The attorney should consider whether taking an elderly client's deposition is needed, to guard against the possibility that the elderly victim might die or become disabled before trial and would thus be unavailable to testify and provide critical evidence. California deposition procedure authorizes the taking of video depositions. Deposition testimony is admissible at trial in lieu of live testimony if the witness is "[d]ead or unable to attend or testify because of existing physical or mental illness or infirmity." CCP §2035.010(a).
- The attorney must include in the contingency fee calculation the amount of expert witness expenses that are likely to be incurred during trial preparation and the trial itself. Frequently, financial scams are uncovered only with the assistance of forensic accountants, who must sift through detailed financial records at considerable expense.
- Every attorney should consider collectability of the judgment in financial abuse cases. In recognition of the problems facing the elderly in collecting elder abuse judgments, California has legislation under which elder abuse judgments have priority against all competing judgments for the same wage garnishment, excepting only judgments for child support and for taxes.

Conclusion

We will see more financial elder abuse cases in the future in real estate deals—not only because the elderly population is growing and living longer, but because we have created, by awarding attorney fees, great incentive for lawyers to take on these matters. The broader definition of undue influence in the elder abuse statute will also bring more health care professionals to the forefront of this battle. No one has a practical roadmap to follow; no one is protected—the insurance industry woke up some time ago, as it has amended its policies to limit and sometimes exclude elder abuse claims. Attorneys are, for the most part, on their own; thus, they need to read these cases carefully, learn from them, avoid the pitfalls, and tread gently and carefully when dealing with the elderly.

Traditional California Water Rights Take a Significant Hit

Howard N. Ellman

Introduction

The California Court of Appeal for the First Appellate District filed its opinion in *Light v State Water Resources Control Bd.* on June-26, 2014. The opinion, published at 226 CA4th 1463 and reported at 37 CEB RPLR 95 (July 2014), profoundly unsettles accepted perceptions of fundamental water rights. A simple fact setting provided the catalyst for that decision.

Analysis

To protect their vines and orchards in the Russian River Valley, owners of vineyards and fruit trees divert water from the Russian River and its tributaries to spray their plantings during periods of frost. The ice that then coats the branches insulates them from the worst and most damaging of the cold.

As frost incidents generally occur in large areas of the valley at the same time, often without much warning as to their severity, the diversions for protection against frost tend to be sudden, unpredictable, and substantial. If the flows in the river are low at the same time, the diversion can reduce water levels precipitously, stranding juvenile Endangered Species Act protected salmon smolts in shallow water at the margins of the river current. High levels of mortality often result.

The first paragraph of the opinion in *Light* summarizes just such an incident and the regulatory reaction to it. That reaction consists of a program to formulate regulations that will restrict frost protection diversions in the future, if the diversions will threaten fish life (226 CA4th at 1472):

> The [Board's] regulation declares that any water use inconsistent with the programs, once they have been formulated and approved by the Board, is unreasonable and therefore prohibited.

That sentence contains the punch line: Any use inconsistent with the programs that will be developed and approved by the Board will constitute an unreasonable use and thus violate art-X, §2, of the California Constitution.

In almost every case, the property owners who will be the targets of the regulation are holders of valid, legally effective water rights, some as riparians (*i.e.,* owners of land contiguous with the river itself or its tributaries) and some as holders of appropriative permits that the Board itself issued. Some of those permits date back to the period before 1914, at a time when the Board's jurisdiction was purely ministerial, with no regulatory authority other than to determine that the permittee had performed the perfunctory steps necessary to be entitled. It has been established law for decades that the Board has no regulatory jurisdiction over riparians at all, whether pre-1914 or not.

Light proclaims with brutal clarity the legal principle that, although the Board has *no permit jurisdiction* over riparian and pre-1914 appropriative rights, it retains regulatory control over those water users, including the power to find and punish unreasonable uses of water, whether within the terms of a permit or riparian right. The court readily disposed of the argument that while the Board has no permit jurisdiction over riparian and pre-1914 appropriative rights, it has the power to enforce art-X, §2, of the California Constitution requiring that all water be used for beneficial purposes and to prevent wasteful or unreasonable use. That section states:

> It is hereby declared that because of the conditions prevailing in this State the general welfare requires that the water resources of the State be put to beneficial use to the fullest extent of which they are capable, and that the waste or unreasonable use or unreasonable method of use of water be prevented, and that the conservation of such waters is to be exercised with a view to the reasonable and beneficial use thereof in the interest of the people and for the public welfare.... Riparian rights in a stream or water course attach to, but to no more than so much of the flow thereof as may be required or used consistently with this section.

As the opinion makes clear, the determination of "beneficial use" depends on the context and the countervailing factors at the time.

Few would doubt that preserving perennial plantings (orchards and vineyards) is a beneficial use, but a use that apparently pales in comparison with possible injury to fisheries resources that continued diversion during frost periods would risk. The introduction of the fisheries factor invokes the *public trust*, a doctrine clarified and enunciated with profound effect in *National Audubon Soc'y v Superior Court* (1983) 33 C3d 419, reported at 6 CEB RPLR 60 (Apr. 1983). Provided with two rationales, the *Light* court relied on both: the idea that diverting water for frost protection was not (or in certain contexts would not be) a beneficial use that complies with art-X, §2, and would also contribute to injuring public trust resources, *i.e.,* endangered salmon.

At a stroke, the opinion subordinates water rights, otherwise constitutionally protected, to two amorphous concepts that cannot be defined except in the context of each particular fact setting. Presumably, this applies to the water rights held by public agencies as well as those of private parties.

Let your mind run with that for awhile. What reliance can safely be placed on such things as a "will serve" letter or water supply assessment from a local water supplier

that is relying in turn on a water right or permit that appears valid on its face but has not run the gauntlet of a beneficial use or public trust challenge? Defense against one such challenge does not foreclose the issue as against a later one based on different facts.

It is hard to contemplate the legal landscape after *Light* without concluding that the very concept of "water rights" in California has been shaken to its foundation.

For further discussion of water rights and public trust issues in California, see California Easements and Boundaries: Law and Litigation §§3.8–3.16, 3.20–3.24A (Cal CEB).

California Retroactively Extends Mortgage Debt Tax Relief, But Only for 2013

Bonnie C. Maly

Recent Legislation

At the end of July, the California State Legislature enacted an extension of its modified conformity to federal mortgage debt forgiveness tax relief for only 1 year, through 2013. See Stats 2014, ch 152. The law allows exclusion of income realized as a result of debt reduction on a taxpayer's principal residence resulting from a loan modification, workout, short sale, foreclosure, or deed in lieu of foreclosure. It was retroactively extended to apply to discharges occurring on or after January 1, 2013, and before January 1, 2014. Qualified principal residence indebtedness is limited to $800,000 ($400,000 for married/RDP filing separate); taxpayers may exclude from gross income up to $500,000 ($250,000 for married/RDP filing separate) of mortgage debt forgiven. See Rev & T C §17144.5.

In addition to the retroactive legislation that conformed California law to the 2013 extension of federal tax relief law, the California Franchise Tax Board issued guidance on short sale state tax relief that is still effective for taxable year 2013 and beyond, and posted instructions for amending returns for taxpayers claiming debt tax relief on a previously filed 2013 tax return, available at https://www.ftb.ca.gov/aboutFTB/newsroom/Mortgage_Debt_Relief_Law.shtml.

On the federal level, the only extension bill showing any life in 2014 is S 2260, §103, 113th Cong, 2d Sess (2014), which would extend the relief into 2014 and 2015 (previous bills had extended it through 2013). Senator Boxer's bill, which was introduced in June 2013, would extend federal mortgage debt tax relief through the end of 2015, but so far it's gone nowhere. See S 1187, §2, 113th Cong, 1st Sess (2013). Several other bills with various extension dates (up to 2 years to the end of 2015) have been introduced in the House since mid-2013 and are still pending with no recent activity. Among them are HR 2994, §2, 113th Cong, 1st Sess (2013) and HR 2788, §2, 113th Cong, 1st Sess (2013).

For further discussion of debt relief tax laws, as well as foreclosures, short sales, and loan modifications, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chaps 2–3, 7, 10 (4th ed Cal CEB). Previous CEB law alerts on tax relief laws can be viewed online at http://ceb.com/lawalerts/lawalerts.asp.

What Do Those Who Disagree With a Development Agreement Do?

Roger Bernhardt

San Francisco Tomorrow v City & County of San Francisco

Law firms with clients hoping to get their proposed development projects approved (over expected neighborhood opposition), or who represent the neighborhood groups desiring to stop or cut back the proposed nearby project, should keep the decision in *San Francisco Tomorrow v City & County of San Francisco (Parkmerced Investors Props., LLC)* (2014) 229 CA4th 498 ready for frequent reference—its unpublished as well as its published parts—because it serves well as a source book for guidance on many issues. The case involved the city's Parkmerced complex—a 152-acre, 3221-unit middle-class residential development, built by Met Life in the 1940s and now starting to fade. The current owners sought to replace many of the lower buildings with highrises and increase its overall capacity to some 9000 units.

There are more details in the case write-up on p 152, but briefly, this was a project that needed

- An EIR;
- An amendment to the San Francisco General Plan;
- Planning Code amendments (to create a special Parkmerced Use District);
- A zoning map amendment;
- A coastal zone permit; and
- A development agreement between the developer and the city, as well as review by the city's Historic Preservation Commission and its Board of Supervisors (and who knows how many other unmentioned local agencies).

Add to that the need to deal with judicial challenges (by traditional mandamus and administrative mandate) to San

Francisco's urban design (land use), housing, and circulation elements of its general plan and their internal consistency with the project, as well as with due process challenges to the hearing process by rent-stabilized tenants fearing displacement. All give this opinion the flavor of a near-complete minicourse on land use.

The Other Parts of the Case

Personally, I wish that the unpublished parts of this lengthy (14,000 words) opinion, which dealt with plan consistency and CEQA issues, had also been published, although at the same time I could have lived without the published discussion and rejection of the project opponents' contentions that San Francisco's general plan failed to comply with the requirement of the state's zoning enabling act that the project be consistent with the population density standards of its general plan—because the general plan did not have adequate standards on the feature. It wasn't as if the question were why a community needs a general plan at all (*why not just pass zoning ordinances and then grant permit approvals or make development agreements on an ad hoc basis after an applicant has made a proposal?*), or why a general plan must include a land use element in the first place (*if everyone is already satisfied with the way things are?*), or why all the pieces have to be consistent with one another (*if different groups or different neighborhoods prefer different life styles?*); rather, it was the narrower and duller question of whether the general plan actually did include satisfactory population density standards—an issue not hard for the city to knock over in light of the many tables and numerical provisions in its plans. About the most that the rest of us can learn from this part of the decision is that a general plan does not need to say precisely just how many people the town wants per acre in this neighborhood, as long as some number can be inferred from its height and bulk limits and FAR ratios. (Similarly for building density: Height maps, bulk maps, and floor intensity ratios tell the public as much as its needs to know about the way neighborhood congestion should be regulated, making the plan valid enough to justify ordinances that are consistent with it. Since, as far as both population and building density are concerned, it is generally the developers rather than the planning staff who make the initial development decisions, expecting more precision from master plans does not sound too realistic or promising anyway.)

Due Process for the Objectors

The most interesting issue dealt with in the opinion was whether the tenants in rent-stabilized units that would be demolished under the new plans could claim that they had been denied procedural due process because they had not been given notice or an opportunity to be heard on the development agreement and the project approvals—features that were likely to lead to their displacement and thereby adversely affect their property rights.

Some of the tenants' arguments were more interesting than persuasive:

- That they had vested rights because the development agreement gave the developers (contrary) vested rights to go ahead with their project (which I don't think is what the decision in *Pennsylvania Coal Co. v Mahon* (1922) 260 US 393, 43 S Ct 158, meant by its phrase "an average reciprocity of advantage"); or
- That a development agreement is an "entitlement" rather than a law, thus triggering due process protections (for those disentitled by it?).

But the premise behind these arguments does have some populist appeal.

Legislative or Adjudicative?

Constitutional rights are enforced by the United States Supreme Court and include due process notice and hearing protection, but enforcement differs depending on whether the challenged state action is legislative or adjudicative (often referred to as administrative or quasi-judicial). A landowner may have a mandatory right to be heard if its rights are being affected by an administrative action, but not if what is involved is a general legislative activity instead. The Supreme Court has left it to the state courts to decide on which side of that line the local process falls. For example, in *City of Eastlake v Forest City Enters.* (1976) 426 US 668, 95 S Ct 2358, the Court let the Ohio Supreme Court determine that rezoning of a parcel from industrial to dense residential was legislative rather than adjudicative, even though it affected only eight acres of land (owned by one entity).

Form Versus Substance

In California, our courts employ a formalistic rather than a substantive test for answering this question; they look at the process that generated the decision rather than the nature of the decision itself. Thus, an initiative blocking a multifamily development and, instead, rezoning the affected 68 parcels to single-family residential was held in *Arnel Dev. Co. v City of Costa Mesa* (1980) 28 C3d 511, 514, reported at 4 CEB RPLR 25 (Mar. 1981), to be legislative activity, despite those particularizing features:

> [Z]oning ordinances, whatever the size of parcel affected, are legislative acts.... A decision that some zoning ordinances, depending on the size and number of parcels affected and perhaps on other factors, are adjudicative acts would unsettle well established rules which govern the enactment of land use restrictions, creating confusion which would require years of litigation to resolve. Since such a decision is unnecessary to protect either the rights of the landowners or the public interest in orderly community planning and development, we adhere to

established precedent and conclude, accordingly, that the ordinance rezoning plaintiffs' property was a legislative act.

That classification meant that, under *Horn v County of Ventura* (1979) 24 C3d 605, reported at 2 CEB RPLR 114 (Aug. 1979), it was insulated from procedural due process constraints of notice and hearing for the adversely affected owners. Going one step farther, our legislature has said that development agreements are legislative, getting their approvals from the local legislative body (Govt C §65867.5(a)), even though such an agreement, when negotiated with a single developer over an integrated piece of property, might look much more like a quasi-judicial decision rather than a general policy enactment, and subject accordingly to narrower judicial review.

Although California legislators and judges approach the issue that way, not everyone else does. About a dozen state courts have chosen to follow the position articulated by the Oregon Supreme Court in *Fasano v Board of County Comm'rs* (1972) 264 Ore 574 that

> [W]e would be ignoring reality to rigidly view all zoning decisions by local governing bodies as legislative acts to be accorded a full presumption of validity and shielded from less than constitutional scrutiny by the theory of separation of powers. Local and small decision groups are simply not the equivalent in all respects of state and national legislatures.... "It is not a part of the legislative function to grant permits, make special exceptions, or decide particular cases. Such activities are not legislative but administrative, quasi-judicial, or judicial in character. To place them in the hands of legislative bodies, whose acts as such are not judicially reviewable, is to open the door completely to arbitrary government." [Citation omitted.]

Consequences of whether the activity is called legislative or administrative include not only deciding whether validity is tested by a deferential irrational and arbitrary test or by a more stringent substantial evidence one, but how those who want to oppose get to make themselves heard—the point on which the disagreers were shot down on the Parkmerced Development Agreement.

It is hard for me to say that the negotiating of a local development concerning a parcel of land in western San Francisco—even one comprising over 150 acres—is comparable to the creation process route taken for an act of Congress in Washington and thereby entitled to the same judicial deference and restriction on constitutional due process challenges. The *Parkmerced* court opined here that development agreements are "conduct that does not fit well within the framework of adjudicatory decisions." 229 CA4th at 528. But when they are as site-specific as this one was, do they fit the framework of general legislation any better? Does the legislature's calling a development agreement "legislative" mean the courts have to agree if they think it isn't?

Condemnation

Valuation

The income approach and testimony that a mining operation was the highest and best use provided legally sufficient evidence of the fair market value of condemned property containing undeveloped minerals.

San Diego Gas & Elec. Co. v Schmidt (2014) 228 CA4th 1280

Plaintiff San Diego Gas & Electric Co. (SDG&E) filed an eminent domain proceeding to condemn an easement for electric transmission lines across property owned by defendant Owners after the parties could not agree on an appropriate valuation. The jury agreed with Owners' experts that open-pit mining operations were the highest and best use for the land and valued the property at around $8 million. The trial court entered judgment on the jury verdict, denied SDG&E's motion for judgment notwithstanding the verdict, and denied Owners' motion for an award of litigation expenses. SDG&E appealed, arguing that insufficient evidence supported the verdict and that the trial court abused its discretion in limiting the cross-examination of an appraisal expert and improperly allowing the appraiser to testify. Owners cross-appealed, asserting that the trial court erred in denying their request for litigation expenses.

The court of appeal affirmed as to SDG&E's appeal and reversed as to Owners' cross-appeal for litigation expenses. The court held that the income approach and testimony that a mining operation was the highest and best use provided legally sufficient evidence of the fair market value of condemned property containing undeveloped minerals. Ample authority supports the income approach when the property at issue contains undeveloped natural resources. The court rejected the argument that Owners' experts could not testify that mining operations were the highest and best use with no current mining operations on the property. Rather, condemnees may present evidence that a property is suitable for a particular purpose even if the property has not yet been developed to that particular highest and best use.

As to the motion for litigation expenses, SDG&E's final offers were about $7.1 million less than the verdict, amounting to about 11 percent of the verdict. These offers were seemingly unreasonable. As to the good faith, care, and accuracy in the manner of determining the final offer, Owners argued that SDG&E's appraiser never investigated mining as a highest and best use or seriously analyzed the mining use issue. Instead, SDG&E stuck to its legal theory that the highest and best use of the

property was as a residential development. The court of appeal could not uphold the trial court's determination that SDG&E's offer was reasonable, as the undisputed facts show only one conclusion was possible. Owners were entitled to recover their litigation expenses because the final offer of compensation was unreasonable in light of the uncontroverted evidence of high-quality mineral deposits and the compensation awarded.

CROSS-REFERENCE: For discussion of highest and best use valuation in eminent domain cases, see Condemnation Practice in California §4.2 (3d ed Cal CEB).

Construction

Prevailing Wage Law

Prevailing wage law did not apply to subcontractor's employees who fabricated materials for public works project at permanent, offsite facility that was not exclusively dedicated to project.

Sheet Metal Workers' Int'l Ass'n v Duncan (2014) 229 CA4th 192

A community college awarded Subcontractor a job to do heating, ventilation, and air conditioning work on a public project modernizing an administration building. The contract required that Subcontractor pay a prevailing wage under California law. Subcontractor's employee (Employee), who had fashioned customized sheet metal items for the project at a permanent, offsite manufacturing facility, filed a complaint with the Department of Industrial Relations, Division of Labor Standards Enforcement (DLSE), alleging he should have been paid a prevailing wage on work done for the project. DLSE found in favor of Employee. The Department of Industrial Relations (Department) determined that Subcontractor was not entitled to the material supplier exemption from the prevailing wage law.

In an administrative appeal, the Department reversed its decision. Employee and the relevant local union filed a petition for a writ of mandate in the superior court challenging the decision that the prevailing wage law did not apply. Because the Department had used federal law principles, the superior court remanded the case for reconsideration on the basis of California state law principles. Subcontractor appealed the decision on reconsideration. The court of appeal affirmed.

The material supplier exemption from the California prevailing wage law has three requirements:

- Sales to the public;
- Establishment of the fabrication or manufacturing facility for multiple jobs over time and not just for the particular public works contract; and
- The location of the fabrication or manufacturing facility must not be at the public work project site.

Subcontractor could establish the second and third elements, but it did not sell products to the general public. Indeed, many of the items crafted for the project were based on nonstandard dimensions and were considered custom for that project.

Although the prevailing wage law covers all those employed in the execution of a public works contract under Lab C §§1772, 1774, using that phrase as an interpretive analysis "would lead to a potentially overbroad application of the prevailing wage law without some limiting guidelines." 229 CA4th at 202. There is a geographical component to the prevailing wage law, as seen in the Lab C §1773.2 requirement to post the per diem wage at the jobsite, which means at the public works project. Labor Code §1777.5(e), (f), (m)(1) contains references to the site of the work. Nevertheless, the law is ambiguous about its geographical scope. Case law is not dispositive of this fabrication issue, but since 1984, the Department has determined that offsite fabrication work done at a permanent facility is not subject to the prevailing wage law. The agency's legal interpretation is not binding, but it is persuasive. Such an interpretation rests easily with the purpose of the law because permanent manufacturing facilities could exist anywhere, so local labor markets are not necessarily affected (the focus of the law). If coverage were expanded to potentially far-flung locations, both administrative and enforcement actions could be burdened.

This case, however, may be distinguished from earlier cases because it involved a manufacturing facility not selling to the general public and creating custom work. California's prevailing wage law is similar to the federal Davis-Bacon Act. California and federal courts have focused on whether an operation is truly independent of the project contract construction activities. Operations at a permanent offsite facility are independent of the project. The court rejected any focus on custom work because "the worker's role is no more integral to the process of construction when fabricating items with customized specifications than it is when fabricating items with specifications that are considered standard." 229 CA4th at 213. Furthermore, the issue of sales to the public does not bear on the independence or integral nature of the fabrication work. If the prevailing wage law is to be expanded, it is the legislature that must do so.

CROSS-REFERENCE: For detailed discussion of the prevailing wage law in public works projects, see California Construction Contracts, Defects, and Litigation §6.9 (Cal CEB) and The California Municipal Law Handbook §§7.51, 7.174 (Cal CEB).

Damages

Nuisance

Triable issues of material fact as to whether tree was part of work of public improvement precluded summary adjudication of insurer's inverse condemnation cause of action.

City of Pasadena v Superior Court (2014) 228 CA4th 1228

A tree owned by defendant City fell on a private residence, causing significant damage. Mercury Casualty Company (Insurer) compensated the owner under a homeowners insurance policy and then sued City for inverse condemnation and nuisance based on the damage caused by the tree. City moved for summary adjudication on all claims. The trial court denied the motion, concluding that as to inverse condemnation, the evidence showed that the subject tree was part of a work of public improvement that may properly be the subject of an inverse condemnation action. As to nuisance, the trial court held that negligence was not required to establish nuisance, and City did not submit evidence excluding the probability that the public improvement was a substantial factor in causing the damage. City challenged by writ of mandate the denial of summary adjudication. City argued that summary adjudication should have been granted because

- The subject tree was not a work of public improvement such that City may be held liable for inverse condemnation.
- Insurer failed to submit any evidence that City negligently maintained the tree such that it may be held liable for nuisance.

The court of appeal denied the writ, finding triable issues of material fact as to whether the tree was part of a work of public improvement. The sole issue was whether City's public tree, as part of City's forestry program, constituted a public improvement such that it could provide the basis for an inverse condemnation claim. A public improvement involves a deliberate action by the state taken in furtherance of public purposes. There is no "deliberate governmental action" when the purported public improvement is neither an instrumentality of the state nor controlled by the state, or when a governmental entity merely owns undeveloped land and has refused to stabilize part of that land. As to whether the deliberate governmental action was taken in furtherance of a public purpose, the California Supreme Court has found that the planting of trees to beautify public streets benefits the public and serves the public purpose of improving public roads. Thus, if the instrumentality that allegedly caused plaintiff's damages (such as a tree) is part of the construction of a public improvement (such as a highway beautification plan), the public improvement element of an inverse condemnation claim is satisfied. Here, City's evidence failed to show that no triable issue of fact existed as to whether the subject tree was a part of a public improvement. The evidence showed that the subject tree was a street tree that was part of a City program to enhance residents' quality of life through maintaining City trees and that City took deliberate actions to manage the program by cataloging its trees and regularly maintaining them. However, the subject tree was part of a government program to maintain trees along roads, and thus served the public purpose of improving public roads. This evidence was sufficient to demonstrate a triable issue of fact as to whether the tree, as part of the forestry program, constituted a public improvement. Because evidence showed that City's forestry program, of which the subject tree was a part, resulted from a deliberate governmental action serving a public purpose, summary adjudication of the inverse condemnation cause of action was properly denied.

In addition, City did not meet its burden of establishing that the insurer could not show nuisance. The complaint alleged a cause of action for nuisance based on City's alleged failure to "prevent and/or stop the collapse" of the tree. Thus, City's liability for nuisance was predicated on its failure to abate the nuisance and negligence was involved. As the moving party, City had the initial burden to present evidence showing that Insurer could not establish an element of its nuisance cause of action. City argued that Insurer could not establish a nuisance claim based on negligence because City had pruned the tree twice in the seven years before a windstorm. However, City did not present evidence as to the type of maintenance required to prevent the tree from damaging this property. For City to meet its burden of showing it had not been negligent, it had to present some evidence that it had not breached its duty of care. Although City's evidence that it twice pruned the tree may potentially show that it fulfilled its duty of care, to reach this conclusion, City must first present some evidence establishing the nature and extent of its duty of care. Absent this context, the burden never shifted to Insurer to raise a triable issue of fact as to whether City negligently maintained the tree.

CROSS-REFERENCE: For detailed discussion of what constitutes a public improvement and proximate cause for purposes of inverse condemnation claims, see Condemnation Practice in California §§13.3B, 13.7A (3d ed Cal CEB) and Neighbor Disputes: Law and Litigation §3.44 (Cal CEB).

Development

CEQA

Tentative subdivision map constituted CEQA project despite lack of specific plan for development.

Rominger v County of Colusa (Adams Group Inc.) (2014) 229 CA4th 690

In a mandamus action under CEQA, opponents of a proposed subdivision challenged a mitigated negative declaration approved by County as to that subdivision. The trial court denied the petition, concluding that, notwithstanding County's approval of a mitigated negative declaration, County's action in approving the subdivision map was not a project for CEQA purposes, and thus no review beyond the preliminary review stage was required.

The court of appeal affirmed in part and reversed in part. It held that the trial court erred in concluding that the proposed subdivision was not a CEQA project even though the proposal did not include any specific plans for development. Whether an activity constitutes a project subject to CEQA is a categorical question regarding whether the activity is of a general kind with which CEQA is concerned, without regard to whether the activity will actually have environmental impact. Thus, for CEQA purposes, "project" means an activity that may cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment, and that is undertaken by any public agency or by a person deriving support from a public agency or that involves the issuance of a lease, permit, or other entitlement by a public agency.

The subdivision here qualified as a CEQA project because the legislature has determined that the approval of a tentative subdivision map is the sort of activity that might cause physical changes to the environment. Specifically, the court of appeal held that plaintiffs adequately showed there was substantial evidence in the record that the subdivision may have a significant unmitigated impact on traffic at a particular intersection adjacent to the project site. Thus, the mitigated negative declaration was inappropriate. On that basis alone, the court reversed and remanded for the preparation of an EIR.

The court held that the common sense exemption did not apply, as it remained an eminently reasonable possibility that the creation of smaller parcels that were easier to finance would lead to development that might not otherwise occur, and to attendant significant environmental effects. The common sense exemption applies only when it is certain that the activity in question will not have any significant effect on the environment. The court rejected the argument that a map approval merely establishing new parcel lines could not have any possible effect on the environment.

COMMENT: *Because this case involves land use, development, and CEQA issues, I asked Howard Ellman, a widely recognized expert who has spoken and taught extensively on various real estate and land use law topics at Boalt Hall, Stanford, and Golden Gate University, to comment on this decision. Thanks, Howard.—RB*

All in all, I found this case unremarkable, adding nothing to existing law. The court clearly disagreed, as it went to substantial lengths to deal with prosaic arguments and then certified the opinion for publication. The biggest question for me is why the court published the opinion.—*Howard N. Ellman*

CROSS-REFERENCE: For further discussion of what types of public agency actions constitute a "project" for purposes of CEQA, or are specifically excluded from CEQA review, see Practice Under the California Environmental Quality Act §§4.12, 4.23 (2d ed Cal CEB).

Easements and Licenses

Prescriptive Easement

Servient tenement owners' fraud challenge to landscape easement and prescriptive easement rights of ingress and egress failed because no relationship existed between parties and no justifiable reliance could be shown.

Hoffman v 162 N. Wolfe LLC (2014) 228 CA4th 1178

On property adjacent to a law firm (LLC), a licensed real estate broker and businessman (Broker) set up a manufacturing business for medical exercise devices intended to provide relief for back and neck pain. Broker decided to purchase the property, but before the close of escrow, two issues arose:

- LLC employees were parking in front of his building.
- Various service vehicles (Federal Express, DHL, a shredding company, and others) were driving over and using his property.

Broker allegedly protested these uses of the property more than once. At one point, before close of escrow, one

member of LLC said he "would take care of it." Nevertheless, the use of the property became a "common occurrence." Escrow closed and LLC sued to quiet title to a landscape easement and a prescriptive easement for rights of ingress and egress. Broker and alleged servient tenement owner cross-complained for fraud, alleging concealment/suppression of facts and intentional misrepresentation about the easements' existence. The trial court granted LLC's summary judgment motion and entered a judgment after the parties settled the remaining causes of action. On appeal by the Broker, the court of appeal affirmed.

Broker argued that LLC owners should have disclosed their prescriptive easement claim. That argument failed because there was no relationship between LLC and Broker. Further, Broker could not show that he justifiably relied on the LLC member's statement that he "would take care of it." A defendant must have a legal duty to disclose. Here, there was no relationship between the parties that would trigger such a duty—not even a transactional relationship, because Broker was not in contract to buy the property from LLC. None of the members of LLC was a party to the sale of the property. No member had volunteered to speak about the easements, but had they, they would have been obligated to speak the "whole truth" without concealing any material qualifications. Here, Broker never directly asked any LLC member about the potential existence of an easement, which also would have triggered a disclosure obligation.

The fraudulent concealment and intentional misrepresentation claims failed as well because Broker could not credibly show that he reasonably relied on a one-time promise to "take care of it." Yet, Broker even admitted that it became a "common occurrence" to have vehicles park on or cross his property. Given Broker's experience and sophistication and his failure to make any further inquiry or complaint after seeing vehicle trespasses for 8 months, his reliance on one vague assurance, stretched to become an understanding that LLC had no adverse claims over the property, was not justifiable.

CROSS-REFERENCE: On litigating fraud, prescriptive easements, and adjacent owner property rights, including settlement agreement and complaint forms, see California Easements and Boundaries: Law and Litigation §§1.32, 8.23, 8.59, 10.45A, 10.47, 10.57 (Cal CEB).

Environment

CEQA

Environmental group's election to prepare record under CEQA's alternative record preparation provision did not preclude award to public agency of supplemental record preparation costs incurred to ensure statutorily complete record.

Coalition for Adequate Review v City & County of San Francisco (2014) 229 CA4th 1043

In an underlying writ action, Environmental Group's challenge under the California Environmental Quality Act (CEQA) to a public project failed. Environmental Group had elected to prepare the project record through the alternative process set out in Pub Res C §21167.6, which gives a project challenger the opportunity to select and prepare a project record for public agency certification and thus reduce record preparation costs. During the underlying action, City partially certified Environmental Group's record, but City moved to supplement the record with 12 additional volumes of material. The court granted City's motion to supplement, finding most of the documents were statutorily required under Pub Res C §21167.6(e), and then cited a few of those supplemental documents in its lengthy decision. City, which had prevailed, filed a memorandum of costs totaling $64,144, generally reflecting costs incurred in preparing a supplemental record of the proceedings. Environmental Group filed a motion to tax, which the trial court granted, denying all costs claimed by City. On City's timely appeal, the court of appeal reversed in part and remanded for additional proceedings.

The trial court's reasoning behind the denial of all costs was faulty in these two respects:

- The trial court erred in concluding that costs cannot be ordered under Pub Res C §21167.6, particularly when it was City that sought to supplement the record.
- The court feared that granting costs would chill environmental challenges to important public projects, but City was entitled to a statutorily complete record.

Further, CEQA expressly allows a prevailing party, including a public agency, to recover record preparation costs under Pub Res C §21168. The alternative record production statute under Pub Res C §21167.6 seeks to give the challenging party an opportunity to control and reduce public agency preparation costs, which also gives the challenger the advantage of avoiding an order to pay record preparation costs to the public agency even before the merits of the case are heard. Nevertheless, case law

instructs that an election to prepare an alternate record "does not ipso facto bar the recovery of record preparation costs by a public agency." 229 CA4th at 1055. Public Resources Code §21167.6(e) outlines what documents must be included in the record. City did not need to put itself at risk of having a statutorily incomplete record, which one might reasonably presume would prejudice the project proponents because the record had been prepared by the project challenger. Here, City did not unilaterally prepare a supplemental record, but obtained a court order to do so. The purpose of making parties pay for the record production protects the public fisc. When the project challenger loses on the merits, protection of the public fisc is even more compelling. Thus, City was entitled to recovery of reasonable costs (but not all claimed costs).

CROSS-REFERENCE: For detailed discussion of record preparation in CEQA litigation, see Practice Under the California Environmental Quality Act §23.69 (2d ed Cal CEB).

CERCLA

Under ability to pay settlement analysis, court was not required to conduct comparative fault analysis in determining whether CERCLA consent decree was procedurally and substantively fair.

U.S. v Coeur D'Alenes Co. (9th Cir 2014) 767 F3d 873

The United States filed lawsuits under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) against various potentially responsible parties (PRPs) to recover costs of pollution clean-up at an Idaho mine site. The government crafted a consent decree for one PRP based on the PRP's ability to pay, with a focus on maintaining the PRP's viability even after the agreed settlement was paid. The government moved for entry of the consent decree, but another mine site PRP opposed the consent decree and intervened in the proceeding. The district court declined to conduct a comparative fault analysis and upheld the consent decree. On the timely appeal of the intervenor, the appellate court affirmed the consent decree as being substantively and procedurally fair under CERCLA.

CERCLA statutorily favors an entity that settles early with the government, thus reducing litigation on pollution clean-ups. Recalcitrant nonsettlors bear the risk of being assigned a disproportionate share of liability for the pollution because CERCLA liability is joint and several. Here, the government properly considered the settling PRP's ability to pay in fashioning the settlement and consent decree. It is only when a PRP's liability is *not* based on its limited ability to pay that a substantive fairness analysis requires an agreement be "based upon, and roughly correlated with, some acceptable measure of comparative fault, apportioning liability among the settling parties according to rational (if necessarily imprecise) estimates of how much harm each [potentially responsible party] has done" (quoting *U.S. v Charter Int'l Oil Co.* (1st Cir 1996) 83 F3d 510, 521). Under an ability to pay analysis, the district court need not quantify exactly how deeply the intervening PRP might bear disproportionate liability.

CROSS-REFERENCE: For general discussion of CERCLA, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §12.99 (Cal CEB 4th ed) and The Municipal Law Handbook §11.240 (Cal CEB Annual).

Financing

Appraisers and Appraisals

Purchaser of vacant land failed to raise triable issue of material fact to show that his lender's appraisers intended to influence his decision whether to buy property.

Willemsen v Mitrosilis (2014) 230 CA4th 622

Purchaser of vacant land intended to build a recycling facility. The purchase agreement had multiple contingencies including financing, physical and soils inspections, survey, title review, and reviews of certain government approvals and other documents. There was no appraisal contingency that would allow Purchaser to decline to purchase the property if his own appraisal found the value of the land too low.

The last contingency satisfied was the financing one, after Bank hired Appraisal Company to value the land to assist it in underwriting the loan. The appraisal report valued the land at $1,780,000. After close of escrow, Purchaser challenged the appraised value as being too high and complained that the appraisal report had failed to take into account an earthquake fault line running through the property and a nearby city's plans to build a road over the property. Purchaser brought a claim for negligent misrepresentation against Appraisal Company claiming he had relied on the appraisal report in determining whether to buy the land. Appraisal Company successfully sought summary judgment and the court of appeal affirmed.

Purchaser had ample contingencies in the purchase agreement that protected his interest, but not the critical appraisal contingency that might have allowed him to reject the purchase agreement based on a low appraised value. Nevertheless, Purchaser was not barred from obtaining an appraisal for his own benefit, seeking comparable sales data, or receiving advice from an independent realtor. But "instead of doing investigations that would help [Purchaser] determine whether the property suited his needs, he chose to rely on the bank's willingness to make him a loan as a sufficient indicator of the suitability of the property." The appraisal report did

mention Purchaser's name, but clearly stated that the client and intended user of the appraisal was Bank.

Purchaser's claim failed because he could not show any justifiable reliance on the appraisal report. Appraisal Company did not intend to influence Purchaser in deciding whether the land was suitable and whether he should purchase it. The actual purpose of the appraisal report was to influence Bank in its decision whether to lend money.

CROSS-REFERENCE: For discussion of appraisals and due diligence contingencies in real estate purchases, see California Real Property Sales Transactions §§1.60, 4.47 (4th ed Cal CEB).

Bankruptcy

Foreclosures

Bankruptcy court properly granted foreclosure sale buyer's motion for relief from stay.

Cruz v Strauss (In re Cruz) (BAP 9th Cir 2014) 516 BR 594

Homeowner defaulted on her home loan and a Notice of Sale for the property was recorded 3 years after the Notice of Default. A trustee's sale was scheduled on October 24, 2012. Homeowner filed multiple "skeletal" bankruptcy filings from November 2009 to February 2013. All filings were dismissed for failure to file proper documents and/or for failure to meet with creditors under 11 USC §341(a). After Homeowner had transferred a 5 percent interest in the property to two other apparent family members (totaling a 10 percent interest), the bankruptcy court granted her lender stay relief on May 31, 2011, finding that the filing of the petition was part of a scheme to delay, hinder, or defraud creditors under 11 USC §362(d)(4).

On July 15, 2013, the property was sold at a foreclosure sale. Just hours before the sale, Homeowner had transferred another 5 percent interest in the property to Cruz. Two days before the sale and transfer, Cruz, acting in pro per, had filed a "skeletal" Chapter 7 bankruptcy case. Cruz did not list his fractionalized interest in the property on Schedule A and also failed to file all necessary documents, ultimately resulting in the dismissal of his case. Once the foreclosure sale buyer and new bank discovered the Cruz deed and bankruptcy, it filed a stay relief motion seeking to annul the automatic stay to validate the trustee's sale or, alternatively, to confirm that no stay was in effect at the time of the sale. The court granted the motion and again found a bad faith attempt to delay, hinder, or defraud creditors. The bankruptcy appellate panel affirmed.

As a preliminary matter, the bankruptcy appellate panel held that it had jurisdiction to review the court's stay relief order because Cruz had timely filed a motion for reconsideration; thus, the bankruptcy appellate panel had jurisdiction to review both the underlying order and the order denying reconsideration. Although the trustee's deed had not yet been recorded, the new bank showed a colorable claim to the property because it had shown an ownership interest in the property by filing a "Trustee's Sale Results" document.

The bankruptcy appellate panel held that Cruz's fractionalized interest was not part of the bankruptcy estate, because Cruz's interest in the property was acquired after the Chapter 7 case was filed. Thus, no stay was in effect at the time of the sale. But, arguably, the 5 percent interest did qualify as property of the debtor, so the bankruptcy court properly annulled the stay. To decide whether a stay should be annulled, a court balances the equities between the parties. Twelve factors guide the analysis, although a strong showing of one factor may be dispositive. Here, Cruz had acted unreasonably and in bad faith. The court found that 5 of the 12 factors had been met, as follows:

- The debtor generally lacked good faith under a totality of the circumstances test.
- The creditors did not know about the stay.
- The debtor did not comply with the Bankruptcy Code and Rules—particularly because he did not file required documents.
- Creditors moved quickly for an annulment of the stay.
- After learning of the bankruptcy case, creditors moved expeditiously to gain relief.

CROSS-REFERENCE: For discussion of borrower bad faith and lender's right to relief from the automatic stay in foreclosures, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§7.90, 11.20 (4th ed Cal CEB).

Residential borrower's preforeclosure quiet title action, claiming that beneficiary lacked standing to foreclose, failed.

Kan v Guild Mortgage Co. (2014) 230 CA4th 736

In a quiet title action brought by a residential borrower (Borrower) seeking to avoid foreclosure, the court of appeal rejected Borrower's claims that the deed of trust was improperly securitized, so the beneficiary lacked standing to foreclose. This argument was already made and rejected in *Jenkins v JPMorgan Chase Bank, N.A.* (2013) 216 CA4th 497, 511. The court agreed with *Jenkins* that, given the exhaustive nature of California's nonjudicial foreclosure scheme, courts should not create an additional requirement that the foreclosing entity must demonstrate *in court* that it is authorized to initiate a foreclosure before the foreclosure can actually happen. This simply was not contemplated by the nonjudicial foreclosure statutes. The court of appeal also found persuasive the *Jenkins* court's further conclusion that Borrower lacked standing to challenge the purported violations to the securitization. Borrower was not a party

to any agreement concerning the pooling process. Thus, even if the transfers were invalid, Borrower would not have been injured.

The court found misplaced Borrower's reliance on *Glaski v Bank of America* (2013) 218 CA4th 1079, reported at 36 CEB RPLR 111 (Sept. 2013). Although the *Glaski* court concluded that a borrower had standing to contest a defective assignment to a real estate investment trust, *Glaski* was a wrongful foreclosure case. Here, Borrower sought to assert a preforeclosure cause of action for quiet title. *Glaski* did not apply. The court went on to express that, while it was not necessary to its decision, the vast majority of courts analyzing *Glaski* have found it unpersuasive. In fact, the one published California appellate decision that analyzed *Glaski* in the context of a preforeclosure lawsuit explicitly disagreed with the decision. See *Keshtgar v US Bank N.A.* (2014) 226 CA4th 1201, reported at 37 CEB RPLR 98 (July 2014). Thus, the court of appeal found that the trial court properly sustained the demurrer without leave to amend.

CROSS-REFERENCE: For comprehensive discussion of borrower strategies concerning foreclosure of securitized loans, including enjoining nonjudicial foreclosure sales, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§7.15, 7.23, 7.38, 12.27 (4th ed Cal CEB).

Borrower's wrongful foreclosure claims based on an alleged failed attempt to securitize the loan, as well as impermissible robo-signing, failed.

Mendoza v JPMorgan Chase Bank, N.A. (2014) 228 CA4th 1020

In a wrongful foreclosure action, the court of appeal addressed Borrower's claim that she was a victim of so-called "robo-signing" and was prejudiced by alleged improprieties in the securitization of her loan. Borrower did not dispute that she was in default. Rather, she asserted (among other things) that the defendants were attempting to take advantage of the complex securitization process and defraud yet another homeowner. She argued that "the Court should not allow the bank defendants to trample over 200 years of well-settled property laws just because Plaintiffs at one time 'owed somebody the money'."

The court of appeal recognized Borrower's flair for the dramatic and her long dissertation on the evils of Wall Street's greed and the securitization of predatory loans. It concluded, however, that the allegations of flaws in the securitization of her specific loan were rather sparse and affirmed the order sustaining the lender's demurrer.

The court addressed the causes of action for wrongful foreclosure, quiet title, and declaratory relief. The wrongful foreclosure claim was based on the premise that the foreclosure sale was void because a botched attempt to securitize Borrower's loan "poisoned" the subsequent foreclosure. Borrower alleged that:

- Her note and deed of trust were improperly transferred into trusts before applicable closing dates set forth in pooling and servicing agreement (PSA).
- Those trusts therefore had no interest in the note or deed of trust.
- The lender's beneficial interest in the loan vanished once it signed the PSA.
- A later assignment of the deed of trust and note in anticipation of the foreclosure were fraudulently executed by a "robo-signer" (*i.e.,* the "officer" executing various documents was in fact an employee of the trustee, so lacked authority).

The court rejected the wrongful foreclosure claim, explaining that securitization of a loan does not alter or affect the legal beneficiary's standing to enforce the deed of trust. Rather, it merely creates a separate contract, distinct from the borrower's debt and obligations. In support of its conclusion, the court noted California's comprehensive statutory framework regulating nonjudicial foreclosure sales and joined other courts in refusing to read any additional requirements into the statutes. See, *e.g., Gomes v Countrywide Home Loans, Inc.* (2011) 192 CA4th 1149, reported at 34 CEB RPLR 66 (Mar. 2011). The court acknowledged that if someone without the power to convey property executes a deed under the statutory scheme, the deed is void, not merely voidable. There is a critical distinction between a glitch in an attempted securitization and an attempt to pass title by an entity without an interest to convey. See *Dimock v Emerald Props.* (2000) 81 CA4th 868, reported at 23 CEB RPLR 250 (Aug. 2000).

The court cited numerous cases holding that plaintiffs lack standing to challenge noncompliance with a PSA in securitization unless they are parties to the PSA or a third party beneficiary. Simply put, Borrower lacked standing because she was not a party to the PSA. The court noted cases like *Gomes* that have unsuccessfully attacked the authority of Mortgage Electronic Registration Systems (MERS) to initiate a foreclosure. Borrower's attempt to distinguish *Gomes* ignored the central holding of the case—the comprehensive statutory nonjudicial scheme did not provide for judicial action to determine whether the person initiating the foreclosure process is indeed authorized to do so (and the court refused to imply one). More fundamentally, whether there was flaw in the securitization process was immaterial to whether the proper parties foreclosed. The court acknowledged a lone case that appeared to support Borrower's securitization argument (*Glaski v Bank of America* (2013) 218 CA4th 1079, reported at 36 CEB RPLR 111 (Sept. 2013)), but found no state or federal support for the *Glaski* analysis

and followed the federal lead in rejecting this minority holding.

The court also noted that even if it were to accept *Glaski*'s standing analysis, Borrower still could not show that she was prejudiced. See *Fontenot v Wells Fargo Bank, N.A.* (2011) 198 CA4th 256, reported at 34 CEB RPLR 168 (Sept. 2011). Borrower could not show that an allegedly improper assignment interfered with her ability to pay or that the lender would not have foreclosed under the circumstances. The court further held that prejudice would not be presumed. Moreover, Borrower had to allege specific facts. Here, she offered no evidence that improprieties in the securitization negatively affected her ability to pay or prevented her from curing the defaults.

The court also rejected Borrower's robo-signing allegations, which she claimed resulted in void assignments. Borrower failed to cite any cases holding that a court can set aside a trustee's sale on the basis of a robo-signed document. In fact, a 2013 case rejected a similar claim. *Maynard v Wells Fargo Bank, N.A.* (SD Cal, Sept. 11, 2013, No. 12cv1435 AJB (JMA)) 2013 US Dist Lexis 130800. In *Maynard*, the plaintiffs' robo-signing allegations failed because they lacked standing to challenge the alleged fraudulent transfers because they were not parties to the assignment and were not intended recipients of the assignment.

The court rejected the declaratory relief and quiet title causes of action. Because the property was sold, there were no claims appropriate for declaratory relief. Because Borrower did not argue the merits of her quiet title cause of action, that cause of action failed as a matter of law.

The court also rejected the defendants' argument that the claims were barred because Borrower failed to tender payment of her debt. Citing *Lona v Citibank, N.A.* (2011) 202 CA4th 89, reported at 35 CEB RPLR 51 (Mar. 2012), the court explained that tender need not be alleged when a trustee sale is void. Here, the gravamen of Borrower's claim was that the foreclosure sale was void, so tender could not be a threshold issue.

COMMENT: A petition for review of this decision was filed in late September 2014.—*Eds.*

THE EDITOR'S TAKE: This opinion was initially unpublished, but the court of appeal apparently had second thoughts and later certified it for publication. I too had initial doubts about a comment or its public significance, but I also have since come around to thinking that it is worth paying attention to—for three reasons.

1. It cites almost everything. In many respects, *Mendoza* looks like just another, almost humdrum decision rejecting a homeowner's postforeclosure attack on the trustee sale that was conducted after she stopped paying her mortgage and rejecting her contention that the foreclosure was bad because her loan had been improperly securitized—a claim frequently made by the foreclosure defense bar and almost as frequently vetoed by the judiciary. But on that point, the opinion is worth saving because of its citation-laden summary of the many decisions that have pronounced a foreclosure sale not wrongful simply because the underlying loan might not have been properly securitized.

Glitches in the trustee sale process (*e.g.,* relating to substitution of trustee, notice of default, notice of sale, and conduct of the sale) can matter and, when they occur, may give a borrower—even one in default—a plausible defense or basis for vacating the sale. On the other hand, glitches in a loan's earlier securitization (*e.g.,* regarding compliance with applicable pooling and servicing agreements, or federal REMIC rules, or the state's trust laws) are not likely to eliminate her obligation to pay her mortgage, notwithstanding the possibility that someone other than her foreclosing lender or servicer might be better entitled to collect that debt.

This opinion's defense of a lender against this sort of "securitization attack" can save similarly situated ones a good deal of library time by serving as their research engine—and at the same time provide borrowers with a ready list of the hurdles they will have to overcome to even get close to a jury. On the other hand, I expect that both crowds have those lists already (including similar pre-*Glaski* rulings, such as in *Wise v WFB* (CD Cal 2012) 850 F Supp 2d 1047, and last-minute refusing-to-take-a-stand holdings, as in *Kan v Guild Mortgage Co.*, ordered published on October 15 of this year and reported in this issue on p 147).

2. Foreclosure audits. Many of the securitization attacks have suffered from being overspeculative, unpersuasively arguing that *perhaps* something had been done wrong when the individual loan was being transferred into the pool, but not demonstrating that it had actually occurred. Mendoza's attack, however, did attempt to overcome that difficulty. She argued that "unlike Gomes, whose allegations were based on sheer speculation, she has identified the true beneficiary and has provided the factual basis lacking in *Gomes*—an audit report."

These "foreclosure audits" or "forensic loan audits" have become increasingly popular for borrowers in default looking for better weapons to stop or undo foreclosures that threaten to wipe them out. The complicated federal and state securitization rules, and the thousands of pages in the transactional documents designed to bring their securitized pools into compliance with those rules, include enough fussy and complicated requirements and deadlines as to make them often easier to be missed than to be met. Especially during the boom years, when the activity was so frantic, undoubtedly many loans—perhaps entire pools—were not in perfect compliance with all those mandates.

But although speculating that *perhaps* a loan's securitization was wrongly done might not suffice as a

defense, a borrower who could actually show that her particular loan was truly mishandled may have a stronger case. A loan that had not been deposited into the trust pool within the window of time set by its PSA has arguably never gotten into the hands of the pool trustee if applicable state trust law says so; thus, it may be held by someone else, which could mean that the wrong party might be trying to enforce it—*if all of that could actually be proven*.

Those hopes and prospects have brought foreclosure auditors into the picture, with their promises of documenting for borrowers just how their loans were—in the auditor's opinion—defectively securitized (as well as also, according to them, probably defectively made). These audits might constitute a useful service, if they were well done, but the data seems to indicate that this is not quite the case. The Federal Trade Commission has said "there is no evidence that forensic loan audits will help you get a loan modification or any other foreclosure relief, even if they're conducted by a licensed, legitimate and trained auditor, mortgage professional or lawyer." (FTC, Consumer Information, Forensic Loan Audits.) Too many foreclosure audits are just phony rescue scams. (The latest one I read about cost the borrowers $3600 and got their attorney in trouble. *Matter of Smithwick*, State Bar Court Case No. 11-O-11334, Review Department, May 16, 2014, available at http://www.statebarcourt.ca.gov/Portals/2/documents/opinions/Smithwick.pdf.)

Audit reports often sound as speculative as information and belief pleadings on this issue sound. A truly thorough audit of a loan's securitization would review all of the requirements in the prospectuses, the loan purchase agreements, and the pooling and servicing agreements (and in all of the amendments, supplements, and schedules to those documents). It would then compare those requirements with the terms of the borrower's note (and its endorsements and allonges and delivery mechanisms), and the terms of her deed of trust (and its assignments and recordations), to see whether all requirements and deadlines in those documents were met. We'll never know what the audit in *Mendoza* actually reviewed or concluded because it was not included in the appellate record. But since Mendoza claimed that she had "identified the true beneficiary" of her loan, I suspect that her auditor had concluded that her loan had not been properly transferred into the trust and was therefore still held by the original beneficiary and trustee, which made them, according to the auditor, the only ones entitled to enforce it.

Counsel for a borrower contemplating paying for such an audit should admonish her client that for even a competent one to do any good, the audit will have to be admitted into evidence and its authoring auditor permitted to testify on it—which will entail his being deposed and then subject to cross-examination by the offended lender regarding the basis for his adverse conclusions. Even if all of those obstacles can be overcome, the judge could decide that the audit report is immaterial because it does not impact the borrower's obligation to pay her loan notwithstanding those defects. That is the issue that may well be decided next.

3. Yvanova*,* Keshtgar*, and* Glaski*.* The *Mendoza* court is not the first one to grapple with this issue, nor the first to rule that a bad securitization does not entitle a borrower to stop paying her mortgage or challenge her foreclosure sale. In fact, its lengthy review of federal and state opinions shows that only one state appellate court—the Fifth District, in *Glaski v Bank of America* (2013) 218 CA4th 1079—had publicly declared its belief that a borrower can get much profit from a bad securitization, while every other court after *Glaski* appears to have rejected that conclusion. (Westlaw told me that it knew of 64 opinions declining to follow that decision.)

But 64–1 may not count for much if the minority has the support of the California Supreme Court. Right now, our high court has that issue squarely before it. Earlier this year, the Second District in *Yvanova v New Century Mortgage Corp.* (2014) 226 CA4th 495, like the Third District in *Mendoza* and earlier in *Keshtgar v US Bank* (2014) 226 CA4th 1201, rejected the *Glaski* position. The Reporter reported on those earlier decisions, but all that was before our supreme court granted review in *Yvanova* (on Aug. 27, 2014, S218973) and *Keshtgar* (on Oct. 1, 2014, S220012). *Keshtgar* involves a preforeclosure challenge and *Yvanova* a postforeclosure one, but both hold that improper securitization does not make a foreclosure wrongful. Whether or not *Mendoza* also goes up, the high court can give us a much more definitive understanding of where California stands on this contentious issue. 64–1 sounds compelling, and a better tally might include non-California forums, although some notable tribunals have surprised lenders by demanding they adhere to the rules requiring the proper transfer of notes, even when others would argue that it does not matter. See, *e.g., Ibanez v US Bank Nat'l Ass'n* (2012) 856 F Supp 2d 273 (Massachusetts).

If the California Supreme Court sides with the "majority" view and rejects bad securitization as a defense, then defaulting borrowers will have to find defects outside that process if they hope to stop or avoid their foreclosures. Improper securitization may be relevant to other parties in the secondary market, and the lending industry may have a lot of cleaning up to do for, *e.g.,* pool investors, but not for prepool borrowers who received their loan funds before any securitization of their documents even started.

On the other hand, if the court endorses the *Glaski* position (which its proponents predict may happen because of the court's earlier refusal to review *Glaski* itself or to depublish it) and holds that securitization mistakes may invalidate foreclosures, there is going to be a lot of follow-up litigation. Do all securitization mistakes have the same effect, or do some hurt borrowers more than others? Must an individual borrower show how she was actually hurt or prejudiced

by what went on? Does the blunder justify her in demanding more proof of entitlement to collect from her adversary? Even if no one else is also demanding payment? Or does the mistake—as some claim—completely excuse her from having to pay anybody or having her property remain encumbered by the original mortgage? A pro-*Glaski* result will keep us all quite busy for a long time.—*Roger Bernhardt*

CROSS-REFERENCE: For comprehensive discussion of borrower strategies concerning foreclosure of securitized loans, including enjoining nonjudicial foreclosure sales, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§1.24, 2.16, 2.25, 2.49, 7.15, 7.23, 7.67B, 12.47, 12.92 (4th ed Cal CEB).

Mortgage Fraud

Lenders owed duty to exercise reasonable care in reviewing borrowers' loan modification applications once they agreed to consider them.

Alvarez v BAC Home Loans Servicing, L.P. (2014) 228 CA4th 941

Plaintiff home loan borrowers alleged, among other things, fraud and unfair business practices in the origination of their residential mortgage loans and negligence in the subsequent servicing of the loans (failing to process applications for modification in a timely manner; "dual tracking," *e.g.,* pursuing foreclosure while evaluating the applications; and losing documents). The trial court concluded that the complaint failed to allege fraud for which defendants were responsible and that defendants owed no duty of care to plaintiffs when reviewing their loan modification applications.

The court of appeal reversed. Although poorly drafted, the court found that potentially meritorious claims could be distilled from the allegations of the complaint. Plaintiffs' failure to tender the outstanding balances on the loans did not deprive them of standing to assert negligence because tender is not necessarily required to set aside a sale in actions based on allegedly fraudulent and unlawful business practices in the marketing of the subject loan. Once defendants agreed to consider the loan modification applications, they owed plaintiffs a duty to exercise reasonable care in their review.

All the factors enunciated in *Biakanja v Irving* (1958) 49 C2d 647 clearly weigh in favor of this duty. The transaction was intended to affect plaintiffs and it was entirely foreseeable that failing to timely and carefully process the loan modification applications could result in significant harm to the applicants. Plaintiffs alleged that the mishandling of their applications caused them to lose title to their home, precluded seeking other remedies, damaged their credit, increased income tax liability, and caused them to incur costs to fight foreclosure. Although no modifications were guaranteed had the loan been properly processed, the mishandling of the documents deprived plaintiffs of the possibility of obtaining the requested relief. With respect to whether defendants' conduct was blameworthy—the fifth *Biakanja* factor—it was highly relevant that plaintiffs' ability to protect their own interests in the loan modification process was practically nil. A borrower's lack of bargaining power, coupled with conflicts of interest inherent in the modern loan servicing industry, provides a moral imperative that those with the controlling hand be required to exercise reasonable care in their dealings with borrowers seeking loan modifications. Moreover, the allegation of dual tracking increased the blame that could properly be assigned. The sixth *Biakanja* factor—preventing future harm—also strongly favored imposing a duty of care.

The court noted that while the California Homeowner Bill of Rights (HBR) was not effective on the relevant dates, the legislation sets forth policy considerations that should affect the assessment of the existence of a duty of care. Much of the challenged conduct is now regulated by the HBR. Although this explicit articulation of lender duties was not available when plaintiffs applied for their loan modification, these obligations fell well within the duty to use reasonable care in the processing of a loan modification.

CROSS-REFERENCE: For detailed discussion of mortgage loan modification fraud and lender liability, as well as necessity of tendering amount owed, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§7.24A, 7.67B, 12.5, 12.11D, 12.80 (4th ed Cal CEB).

Homeowners' complaint for breach of loan modification agreement adequately stated cause of action for breach of the covenant of good faith and fair dealing, breach of contract, fraud, and promissory estoppel.

Fleet v Bank of America (2014) 229 CA4th 1403

The Fleets applied to Bank of America (BofA) to modify a loan in 2009 under the Making Homes Affordable Act. Months of telephone conversations with and letters to various BofA-related personnel brought assurances that everything was proceeding smoothly or denials of any knowledge of any loan modification application. In November 2011, BofA informed the Fleets they had been approved for a trial period plan under a Fannie Mae modification program. The Fleets had to make three monthly payments starting on December 1, 2011. If they made the payments, then their financial hardship would be verified. If they passed that test, their loan would be permanently modified.

After the Fleets paid the first two payments for December 2011 and January 2012, a BofA representative told them that BofA had suspended foreclosure proceedings. Near the end of January 2012, the house was sold at a trustee's sale. When the buyer's representative served a notice to quit, the Fleets explained that the house had significant structural problems and the buyer evinced an intent to rescind the sale. The Fleets continued trying

to communicate with BofA and a bank representative left voicemail messages to the effect that BofA wanted to resolve the dispute. In light of the ensuing silence, interpreted to mean the buyer was trying to rescind the sale, the Fleets spent $15,000 to repair a broken sewer main. They were evicted in August 2012. The Fleets sued BofA, the trustee under their deed of trust, BofA officers and employees who handled their loan modification, and the buyer and its representative. The trial court sustained BofA's demurrer.

The court of appeal reversed and remanded. The court found this appeal to be yet another example of a now well-established and predictable pattern: Distressed homeowner is promised a mortgage modification under a program designed to avoid foreclosure; owner contacts lender to ensure everything is proceeding correctly and either receives assurances that it is or is passed along to people who claim no knowledge of the loan in question or its modification; the foreclosure notice is posted on the door; and the house is sold.

On appeal from a judgment of dismissal after sustaining a demurrer without leave to amend, a court reviews the complaint to determine whether it alleges facts to state a cause of action under any legal theory, regardless of the labels attached to the causes of action in the complaint itself. Here, although not a model of clarity, as the Fleets represented themselves, allegations of viable causes of action could be sufficiently discerned from the complaint to defeat a demurrer. The Fleets were accepted into a program that would have led to a permanent modification of their mortgage. They performed their duties until BofA foreclosed and sold the house. These actions injured the Fleets' right to receive the benefits of the agreement. These allegations suffice to state a cause of action for breach of the covenant of good faith and fair dealing. The Fleets were on the road to a loan modification when BofA foreclosed. The allegation that they performed the terms of the agreement until excused by BofA's conduct sufficed to state a cause of action for breach of contract against BofA.

The alleged facts might also support a cause of action for promissory estoppel if the Fleets could not establish a cause of action for breach of contract. The complaint also sufficiently alleged the requisite elements of promissory fraud by asserting that BofA never intended to modify the loan, that the Fleets relied on the false promise, and that they were damaged by the loss of payments and their home. The allegations of the complaint also supported a fraud cause of action against three employees who handled the loan modification as agents of BofA and participated in the fraud. The Fleets alleged that the agents never intended to honor the agreement and wrongfully stated that the foreclosure proceedings were suspended.

CROSS-REFERENCE: For detailed discussion of mortgage loan modification fraud and lender liability, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§7.67B, 12.5, 12.8, 12.11, 12.22, 12.80 (4th ed Cal CEB).

Land Use

Coastal Act

Homeowners' acceptance of benefits of permit issued by Coastal Commission barred them from challenging various conditions of that permit.

Lynch v California Coastal Comm'n (2014) 229 CA4th 658

Adjacent bluff top homeowners (Owners) sought a permit to replace a wooden erosion control structure and midbluff wall and to remove and replace the lower section of their private access beach stairway. The Coastal Commission approved the permit, except as to the stairway, subject to numerous conditions, including recording deed restrictions as approved by the Commission. The deed restrictions stated the Commission approved the permit subject to the special conditions, and but for those special conditions the project would not be consistent with the Coastal Act and the Commission would not have approved the permit. They also stated that Owners elected to comply with the special conditions to start the authorized work and, in consideration for its issuance, they irrevocably covenanted that the special conditions constituted covenants, conditions, and restrictions running with the land for the duration of the 20-year permit.

Owners challenged via mandamus the conditions barring them from rebuilding the stairway and limiting the permit to 20 years. Meanwhile, they signed and recorded the required deed restrictions, satisfied the other prior-to-issuance permit conditions, obtained the permit, and constructed their project. The trial court granted mandamus relief to Owners and directed the Commission to remove the challenged conditions.

The court of appeal reversed, holding that Owners waived the right to challenge the permit conditions when they signed and recorded deed restrictions agreeing to the permit conditions and then accepted the permit's benefit by constructing their project. In general, property owners may challenge an allegedly unreasonable permit condition only by refusing to comply and bringing a mandate action to have the condition declared invalid. If a property owner complies with the condition, the owner waives the right to legally challenge it. Neither exception to the general waiver rule applied. The first applies only to conditions imposed by local agencies that "divest the developer of money or a possessory interest in property" and does not

apply to conditions imposed by state agencies or to conditions that restrict the manner of use. The second applies only when an agency imposes new conditions on a permit for a later phase of a project already underway. Because starting a project involves contracts and costs, typically irrevocable decisions, the owner has no realistic option but to accept the new permit and conditions. However, this case did not involve any new conditions being imposed on a project already underway. Alternatively, even if Owners had not waived their right to challenge the permit conditions, the Commission lawfully limited the permit's duration and barred rebuilding the stairway. Substantial evidence supported these conditions.

CROSS-REFERENCE: For discussion of development permits in the coastal zone, see California Land Use Practice §14.63 (Cal CEB). On the Coastal Act generally, see The California Municipal Law Handbook §6.188 (Cal CEB).

Development Agreements

Equal Protection/Due Process

Tenants of rent-controlled units fearing displacement by long-term redevelopment project have no procedural due process rights to notice or opportunity to be heard.

San Francisco Tomorrow v City & County of San Francisco (Parkmerced Investors Props., LLC) (2014) 229 CA4th 498

Interest groups, including tenants of rent-controlled units fearing displacement, appealed the superior court's denial of their petition for writ of mandate seeking to overturn City's approval of the 152-acre Parkmerced Development Project. The project involves the long-term redevelopment of privately owned property by real party in interest Parkmerced Investors Properties, LLC.

The court of appeal affirmed. The adoption or amendment of a general plan is a legislative rather than adjudicative act that is presumed valid. Judicial review of a legislative act is limited to determining whether the public agency's action was arbitrary, capricious, entirely without evidentiary support, or procedurally unfair. Here, a reasonable person could conclude, as did City, that elements of the plan adequately included population density and building intensity standards. The court explained that the approval of the development agreement is also a legislative act. Because the approval process requires consideration of broad-based policy issues and the exercise of legislative discretion, it is conduct that does not fit well within the framework of adjudicatory decisions. Whether or not the approval is conduct applying to more than a few people, state law deems the approval a legislative act. Therefore, the tenants did not have any procedural due process rights to notice and a hearing as to the development agreement approval.

As to the contention that the trial court erred in including in the administrative record transcripts of a set of hearings before the City Board of Supervisors' Land Use and Economic Development Committee (LUEDC), the court of appeal affirmed. The LUEDC hearings undisputedly occurred before the Board's decision. This evidence was available to decision-makers before their decision. The Board's motion that it had "heard testimony and received public comment regarding the adequacy of the FEIR" was reasonably found to include public testimony before Board committees. Further, even if this evidence were not part of the administrative record, the order of inclusion would not constitute reversible error absent a showing of prejudice.

COMMENT: The opinion as modified was certified for publication with the exception of Part III on CEQA.

See Professor Roger Bernhardt's "Midcourse Corrections" column, on p 140 of this issue, for his commentary on *San Francisco Tomorrow v City & County of San Francisco.—Eds.*

CROSS-REFERENCE: For discussion of procedural due process rights in land use and development decisions, see California Land Use Practice §19.16 (Cal CEB).

Housing

Seniors-only mobilehome park owner had standing to file suit against city because it alleged concrete and particularized, actual injury from delay and added expenses resulting from city's alleged interference with subdivision application.

El Dorado Estates v City of Fillmore (9th Cir 2014) 765 F3d 1118

El Dorado owns and operates a seniors-only mobilehome rental park in defendant City. In 2008, City considered adopting a mobilehome rent control ordinance at the park residents' request. After publicly discussing opening the park to families, an action that requires no approvals, El Dorado decided to end the rental business by subdividing the park into single lots for sale to the residents. Litigation arose out of the subdivision application: Many residents opposed the subdivision and City twice deemed the application incomplete.

El Dorado sued in state court, alleging that City interfered with the application by causing unreasonable delays and imposing extralegal conditions for fear that El Dorado would open the park to families. El Dorado obtained a court order eliminating most of City's requirements. City then approved the application, subject to compliance with local flood mitigation regulations and CEQA. The latter condition was imposed contrary to City staff's finding that CEQA did not apply. City officials' statements suggested that City used the CEQA condition to prevent any conversion to a family park. City offered to waive the CEQA condition if El Dorado would commit to

maintaining the park as a senior park. El Dorado returned to state court to challenge these conditions. Although the court upheld the imposition of the CEQA environmental review, it barred City from imposing local regulations. El Dorado then filed this suit in federal court, alleging that City's actions violated the Fair Housing Act (FHA). Finding that El Dorado's inability to "potentially make housing available for families" was not a cognizable injury, the district court dismissed for lack of Article III standing.

The Ninth Circuit reversed and remanded, holding that El Dorado had Article III standing. Standing consists of three elements:

- Injury in fact;
- Causation; and
- Redressability.

The injury-in-fact element was at the crux of this case. An injury in fact is an invasion of a legally protected interest that is concrete and particularized and actual or imminent. In the context of the FHA and housing discrimination, a plaintiff need not be among the class discriminated against to have standing. The court first clarified that the alleged injury was the expenses incurred through unreasonable delays and extralegal conditions. El Dorado clearly suffered a concrete and particularized injury in the form of added costs caused by City's interference with its application. This injury is legally protected only because the FHA bars discrimination against families and creates a new legal right. The allegation that City discriminated against families by its interference was sufficient because the right not to have to endure housing discrimination, even if one is not among the class of persons discriminated against, is a constitutionally cognizable legal interest supporting standing. El Dorado established causation by showing that the delays and additional expenses it incurred were a direct result of City's alleged interference.

The district court could redress El Dorado's alleged injuries by compensatory damages and injunctive relief.

CROSS-REFERENCE: For further discussion of mobilehome park conversions, see California Land Use Practice §6.20 (Cal CEB), California Landlord-Tenant Practice §6.56 (2d ed Cal CEB), and Practice Under the California Environmental Quality Act §5.38 (2d ed Cal CEB).

Mechanics Liens

Construction and Construction Contracts

Case of first impression: When collecting from noncontracting innocent owners, mechanics lien claimants are entitled to receive prejudgment interest at constitutional default rate of 7 percent, not 10 percent as provided for in Mechanics Lien Law.

Palomar Grading & Paving, Inc. v Wells Fargo Bank, N.A. (2014) 230 CA4th 686

Expressing that it was writing on a "clean slate" because no published case had considered the issue, the court of appeal held that the amount of prejudgment interest that mechanics lien claimants are entitled to receive from noncontracting innocent property owners is the constitutional default rate of 7 percent, *not* the 10 percent provided for in the Mechanics Lien Law. The two current owners of the property, the construction lender, and a department store chain (Kohl's) appealed from judgments already obtained by Subcontractors. Subcontractors had brought actions to foreclose their mechanics liens because the general contractors failed to pay them for infrastructure work, which was done as part of a project to develop a Kohl's store and surrounding property.

As relevant to the appeal here, Subcontractors had direct contracts with the general contractor, *not* the now current owners of the property. At trial, the lien claimants had successfully argued for the applicability of a provision of the Mechanics Lien Law that provided for a 10 percent prejudgment interest rate, as distinct from the constitutional default rate of 7 percent (Cal Const art XV, §1). Civil Code §3289 provides in relevant part that "if a contract entered into ... does not stipulate a legal rate of interest, the obligation shall bear interest at a rate of 10 percent per annum after a breach."

In concluding that the 7 percent rate applied, the court of appeal pointed out that the owners of the property had *no contract with Subcontractors.* Rather, the liens were the result of the Mechanics Lien Law. The court rejected the lien claimants' two theories to support their position. One Subcontractor asserted that it wasn't "fair" to charge 10 percent against the improver of land (the general contractor) while letting an owner "get away" with only 7 percent. According to the court, it was perfectly "fair" that the defaulting contractor who breached the contract should pay a higher rate than an innocent owner.

The court found equally without merit the "entitlement" argument. One Subcontractor asserted that it was entitled to recover the amount due under its contract. That argument ignored the language of former

CC §3123 (providing that the liens shall be for, *e.g.,* the reasonable value of the labor or equipment *"or* for the price agreed upon by the claimant and the person with whom he or she contracted, *whichever is less*" [emphasis added]).

The court cautioned that its decision did not address the question of prejudgment interest in the case of culpable, contract-breaching owners (owners who breach their contracts with contractors or material suppliers and for that reason have a mechanics lien slapped on their property) or the possibility of a sham change of ownership to try to gain a better interest rate.

CROSS-REFERENCE: For further discussion of entitlement to prejudgment interest in mechanics lien claims, see California Mechanics Liens and Related Construction Remedies §§2.53, 3.112, 3.121 (4th ed Cal CEB).

Miscellaneous Remedies

Americans with Disabilities Act

Title II of the ADA requires cities to provide accessible on-street parking absent regulatory design specifications for on-street parking facilities.

Fortyune v City of Lomita (9th Cir 2014) 766 F3d 1098

Fortyune filed suit in state court alleging that City failed to provide accessible on-street diagonal stall parking in violation of the Americans with Disabilities Act (ADA) and the Disabled Persons Act (DPA). Fortyune is a paraplegic who uses a wheelchair for mobility. He alleged that he experiences "great difficulty, discomfort and, even[] fear for his safety" when frequenting City facilities, as none of the public on-street parking is accessible to people with disabilities. City removed the case to federal court and moved to dismiss, arguing that, absent the adoption of ADA implementing regulations specifically targeting on-street parking, it was not required to provide accessible on-street parking. The district court denied the motion to dismiss, concluding that "the broad language of the ADA requires public entities to ensure that all services, including on-street parking, are reasonably accessible to and usable by individuals with disabilities." The district court certified its order for interlocutory appeal.

The Ninth Circuit affirmed. At issue was whether Title II of the ADA required cities to provide accessible on-street parking absent regulatory design specifications for on-street parking facilities. The panel stated that the text of the ADA, the relevant implementing regulations, and the Department of Justice's interpretation of its own regulations all led it to conclude that public entities must ensure that all normal governmental functions are reasonably accessible to disabled persons, irrespective of whether the DOJ has adopted technical specifications for the particular types of facilities involved. City was so required because this was its normal function. The lack of a specific regulation did not exempt it because the ADA's text applied and could not eliminate a statutory duty. Regulations required cities to make each program accessible by disabled persons and required facilities built or altered after June 26, 1992, to be usable by disabled persons. City had such a duty because the DOJ's controlling regulatory interpretation required cities to provide accessible on-street parking.

City was not denied due process because the DOJ gave it notice of the duty to make services accessible without technical specifications. Therefore, the panel held that the plaintiff had stated claims under the ADA and the DPA based on City's alleged failure to provide accessible on-street diagonal stall parking.

CROSS-REFERENCE: For discussion of ADA claims, see The California Municipal Law Handbook §4.20 (Cal CEB), California Government Tort Liability Practice §9.76A (4th ed Cal CEB), and California Land Use Practice §14.44 (Cal CEB).

Insurance (Property)

Foreclosures

Full credit bid rule precluded lender from recovering insurance benefits for preforeclosure damage to the property caused by the former property owner.

Najah v Scottsdale Ins. Co. (2014) 230 CA4th 125

In an insurance action brought by Lenders following a foreclosure sale, the court of appeal held that the full credit bid rule precluded Lenders from recovering insurance benefits for preforeclosure damage to the property caused by the former property owner. Under this rule, when the lienholder obtains property at a foreclosure sale by making a full credit bid (*i.e.,* bidding an amount equal to the unpaid debt, including interest, costs, fees, and other expenses of foreclosure), it is precluded from later claiming that the property was actually worth less than the bid. To allow Lenders (now owners) to collect insurance proceeds for prepurchase damages would result in a double recovery. *Alliance Mortgage Co. v Rothwell* (1995) 10 C4th 1226, 1238, reported at 18 CEB RPLR 335 (Nov. 1995). Because of the court's conclusion concerning the full credit bid rule, it did not need to address other issues, including whether the insurance at issue covered damages intentionally caused by the property owner as "vandalism."

Lenders had sold the property to Borrower while taking back a promissory note and second deed of trust for $2.55 million. As required by the promissory note, Borrower obtained a general liability policy from Insurer, listing Lenders as mortgage holders under the policy. After

paying the balance due to the holder of the first note, Lenders foreclosed under the second trust deed and acquired the damaged property (requiring over $500,000 in repairs) by making a full credit bid. Insurer denied Lenders' claim for damages. In the subsequent action brought by Lenders, the trial court ruled for Insurer, concluding that Lenders' claim to insurance proceeds as mortgagee under the second deed of trust was extinguished by their full credit bid at the foreclosure sale.

The court of appeal affirmed. While not wholly agreeing with the trial court's reasoning, the court of appeal agreed that the full credit bid rule precluded Lenders from recovering insurance benefits under the policy. The court explained that, to appreciate why the rule has an effect on insurance proceeds, one had to understand basic principles governing mortgagee insurance. For one thing, as a trade-off for the broad coverage afforded under a standard mortgagee clause, the amount payable under the policy is limited to the amount necessary to satisfy the debt. According to the court, "[b]ecause a mortgage debt is extinguished by a full credit bid, it is well established that a mortgagee who purchases an encumbered property at a foreclosure sale by making a full credit bid is not entitled to insurance proceeds payable for preforeclosure damage to the property." 230 CA4th at 136. See, *e.g.*, *Caruso v Great W. Sav.* (1991) 229 CA3d 667, 672, reported at 14 CEB RPLR 201 (July 1991) (rule still applies if lender was junior creditor).

The court found without merit Lenders' assertion that the outcome of the case was different because Lenders held two deeds of trust securing two separate debts. Lenders unsuccessfully argued that they were entitled to pursue remedies available to a third party beneficiary. Lenders proposed a rule that all liens held by the mortgagee be aggregated to determine whether a full credit bid was made. Lenders' position was already rejected in *Romo v Stewart Title* (1995) 35 CA4th 1609, reported at 18 CEB RPLR 254 (Aug. 1995). The court expressed that applying the rule in these situations protects the integrity of the foreclosure action process, stating (230 CA4th at 140):

> [T]he effect of [Lenders'] bidding the full amount of their second lien, notwithstanding their belief that the property was worth less than the combined amount of the first and second liens, was to block other interested parties from "participat[ing] in setting the price for the property," and preventing the property from going to the party placing the highest actual value on it. [Citation omitted.] Having thus deprived [Insurer] of the benefit of a bona-fide mortgage foreclosure auction, they cannot now reasonably contend that they are entitled to insurance proceeds in the amount between what they freely paid to secure the property for themselves and the amount they now claim the property to be worth.

The court found distinguishable cases cited by Lenders to support their position. The court further reasoned that to adopt the aggregation rule proposed by Lenders would likely lead to the end of the full credit bid rule. A lender could divide a single loan between two promissory notes secured by two deeds of trust and foreclose with a full credit bid on the junior loan. This elevation of form over substance was rejected in a similar context. See *Simon v Superior Court* (1992) 4 CA4th 63, reported at 15 CEB RPLR 196 (May 1992) (lender could not circumvent antideficiency protections of CCP §580d by splitting debt into multiple deeds of trust and notes).

The court of appeal held that the trial court did not abuse its discretion in finding that Insurer's offer in compromise under CCP §998 was reasonable.

THE EDITOR'S TAKE: These lenders killed themselves by bidding the full amount of their second deed of trust when they knew that the property had been vandalized and was worth less than that. Their knowledge only made them look like bad guys, plotting to discourage rival bidders in order to get both the property and the insurance on it.

It is also a stupid strategy in California, with our full credit bid rule looming over the foreclosure process. Bidding one dollar at the sale won't stop the debtor or the insurer from contending that the property's fair market value (or fair value) was greater than that, but a full credit bid of $2 million will estop the lender from claiming that it was worth any less than that. We are not likely to change that rule or the doubtful logic behind it, but that is no reason why lenders cannot be a little more intelligent in their bidding under it.—*Roger Bernhardt*

CROSS-REFERENCE: For comprehensive discussion of the effect of a lender's full credit bid and a lender's right to property and casualty insurance proceeds, see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§2.86, 2.129, 8.61, 9.30 (4th ed Cal CEB).

Shared Use and Ownership

Common Interest Developments

Homeowners association could not continue foreclosure after owner tendered partial payment that reduced delinquent assessment amount below $1800. It was statutorily required to accept partial payment of amounts owed.

Huntington Continental Townhouse Ass'n v Miner (2014) 230 CA4th 590

Under a relatively new provision of the Davis-Stirling Common Interest Development Act, which took effect in 2006 (see Stats 2005, ch 452 (SB 137)), a homeowners association is prohibited from collecting delinquent

assessments through judicial or nonjudicial foreclosure (former CC §1367.4, now CC §5720(b)) unless

- They exceed $1799; or
- The assessments secured by a lien are more than 12 months delinquent.

The issue in this case concerned whether a unit-owner who had exceeded the statutory threshold could stave off the foreclosure of his unit by making a partial payment of the amounts owed. At the time the tendered payment of $3500 was made, Association had already spent over $2000 in attorney fees and the unit-owner had agreed to and then breached a payment plan agreement. Examining the clear words of the statute (see CC §5655(a)), the court of appeal agreed with the superior court appellate division that the Davis-Stirling Act not only permitted but *compelled* Association to accept the partial payment of the total amount owed on the account. Further, because the assessment amount was less than $1800 after the tender (the remaining assessment balance was $760), Association could no longer foreclose.

Section 5655 provides in relevant part that "[a]ny payments made ... shall first be applied to the assessments owed, and, only after the assessments owed are paid in full shall the payments be applied to the fees and costs of collection, attorney's fees, late charges, or interest." According to the court, this section unambiguously created an order of allocation, which the court concluded as recognizing that a payment might not cover the full amount of delinquency and other charges. Examining the clear words of the statute, the court rejected Association's claim that payments were permitted only when made pursuant to a payment plan under CC §5650. The court also found misplaced Association's reliance on CC §5658 to claim that if the owner disputed the charge, the remedy was to pay *all* the amounts in full under protest and file a small claims suit. The court explained that this section applies only when the owner disputes the validity or amount of a charge, which was not at issue here. Although the court did not need to resort to examining legislative history, it noted that the bill sought to protect owners from losing their home equity over small amounts of delinquent assessments. According to the court, the legislature engaged in a balancing process and chose to accept the risk of a clever owner seeking to dodge foreclosure of a lien. The court found without merit Association's (and amici curiae's) additional contentions to the contrary.

The court rejected Association's claim that the Davis-Stirling Act's requirement that any nonjudicial foreclosure be conducted in accordance with CC §§2924, 2924b, and 2924c compelled a different result. At issue was §2924c, which requires full payment of the entire amount due to stop a foreclosure proceeding that has already begun. According to the court (230 CA4th at 606):

> [T]he Legislature intended for section 5655(a), requiring an association to accept partial payments, and section 5720(b), limiting foreclosure, to apply to both judicial and nonjudicial foreclosure and to prevail to the extent of any conflict with Civil Code section 2924c, subdivision (a)(1).

CROSS-REFERENCE: For discussion of homeowners associations' remedies for collection of delinquent assessments, see Advising California Common Interest Communities §5.47 (2d ed Cal CEB).

Taxation

Change of Ownership

Recorder could impose documentary transfer tax on transfer of more than 50 percent of interest in partnership that was sole member of LLC that held title to realty.

926 N. Ardmore Ave., LLC v County of Los Angeles (2014) 229 CA4th 1335

Husband and Wife set up a trust that owned an apartment building (among other holdings). Husband predeceased Wife and the trust principal was distributed into four subtrusts, with Wife as beneficiary of all subtrusts. Wife designated their two sons as successor trustees of the limited liability limited partnership (LLLP) that owned the (federally disregarded) limited liability company (LLC), a single-member entity established to hold and manage the apartment building. The subtrusts then sold an approximately 45 percent interest to each of the two sons' trusts (for a total of approximately 90 percent interest in the LLLP transferred). These transfers were reported.

The City and County of Los Angeles passed ordinances under the Document Transfer Tax Act (Rev & T C §§11901–11935) to tax "realty sold" and claimed a tax was due for the transfer or "change of ownership" of the apartment building. The LLC paid the tax but applied for a tax refund, which was denied. On appeal by the LLC, the court of appeal affirmed.

A dispute arose about the interpretation of the undefined term "realty sold" in Rev & T C §11911. The LLC argued that the term did not include sales or transfers of legal entities that either hold property title or own separate legal entities that hold property title. The court of appeal found this argument unpersuasive. Discussing California case law and legislative history, the court determined that courts may look to the definitions of "change in ownership" set forth in the property tax provisions, chiefly Rev & T C §64, to determine the meaning of "realty sold" referenced in the Document

Transfer Tax Act. Here, Rev & T C §64(d) applied, which states:

> Whenever shares or other ownership interests representing cumulatively more than 50 percent of the total interests in the entity are transferred by any of the original co-owners in one or more transactions, a change in ownership of that real property owned by the legal entity shall have occurred.

When the subtrusts transferred approximately 90 percent of their interest in the LLLP, that triggered a change in ownership and consequently amounted to "realty sold."

> ***CROSS-REFERENCE:*** For discussion of documentary transfer taxes, see California Real Property Sales Transactions §§6.98, 10.11 (4th ed Cal CEB), The California Municipal Law Handbook §5.68 (Cal CEB), and Ground Lease Practice §2.48 (2d ed Cal CEB).