CALIFORNIA LAND TITLE ASSOCIATION
FORMS AND PRACTICES COMMITTEE

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AGENDA

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November 7-8, 2013

Thursday: 1:00 PM - 5:00 PM
Friday: 9:00 AM - 1:00 PM

Hyatt Regency Sacramento
1209 L Street
Sacramento, California 95814
916-443-1234

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1. Administrative Section (Elliot Smith)

A. Approval of the Minutes of the September 5–6, 2013 meeting.
See Exhibit 1A

2. Bankruptcy Section (Wayne Condict)

A. In re Armstrong (Band of America v. Armstrong)
Bankruptcy Appellate Panel – 8th Circuit
Filed 9-19-13
See Exhibit 2A

B. In re Fluellen (Hope v. Acorn Financial)
11th Circuit
Filed 9-26-13
See Exhibit 2B

C. Carpenters Pension Trust Fund for No. Cal. v. Moxley
9th Circuit
Filed 8-20-13
See Exhibit 2C

D. <u>In re Utnehmer (Utnehmer v. Crull)</u>
Bankruptcy Appellate Panel – 9th Circuit

Filed 10-10-13

See Exhibit 2D

E. <u>In re ABC Learning Centres</u>
3rd Circuit

Filed 8-27-13

See Exhibit 2E

F. <u>In re Wilshire Courtyard (Wilshire v. CA Franchise Tax Board)</u>
9th Circuit

Filed 9-10-13

See Exhibit 2F

G. <u>In re Mendaros (Mendaros v. JP Morgan Chase)</u>
Bankruptcy Appellate Panel – 9th Circuit

Filed 10-2-13

See Exhibit 2G

H. <u>In re Underhill</u>
Bankruptcy Appellate Panel – 6th Circuit

Filed 9-16-13

See Exhibit 2H

I. <u>In re Flores (Danielson v. Flores)</u>
9th Circuit

Filed 8-29-13

See Exhibit 2I

J. <u>Weiss v. Wells Fargo Bank</u>
Bankruptcy Appellate Panel – 1st Circuit

Filed 10-1-13

See Exhibit 2J

3. <u>Court Decisions Section (Laura Lowe)</u>

A. <u>Stewart Title Guaranty Co. v. Sterling Savings Bank</u>
Washington Supreme Court

Filed 10-3-13

See Exhibit 3A

B. Swanson v. State Farm General Insurance Co.
Cal.App. 2nd Dist.
Filed 9-23-13
See Exhibit 3B

C. Rossberg v. Bank of America
Cal.App. 4th Dist.
Filed 8-27-13
See Exhibit 3C

D. Siliga v. Mortgage Electronic Registration Systems
Cal.App. 2nd Dist
Filed 8-27-13
See Exhibit 3D

E. Chavez v. Indymac Mortgage Services
Cal. App. 4th Dist.
Filed 9-19-13
See Exhibit 3E

F. United States v. Brandt
U.S. Court of Appeals – 10th Circuit
Filed 9-11-12
See Exhibit 3F

G. Glaski v. Bank of America
Cal.App. 5th Dist.
Filed 7-31-13
See Exhibit 3G

H. King v. Wu
Cal.App. 2nd Dist.
Filed 8-14-13
See Exhibit 3H

I. Self v. Sharafi
Cal.App. 4th Dist., Div. 1
Filed 9-20-13 (Pub. Order 10-11-13)
See Exhibit 3I

4. **<u>Closing Instructions Section (Bill Jourdan)</u>**

Assertion of escrow liability for missed deeds of trust.

Exhibit 4A: First lien letter-Requested by lender

Exhibit 4B: Proposed recording instruction

5. **<u>Governmental Regulations Section (Jeff Dondanville)</u>**

Nothing Scheduled.

6. **<u>Subdivision and Land Use Section (Douglas Borchert)</u>**

Nothing Scheduled.

7. **<u>Legislation Section (Tim Reardon)</u>**

A. Chapter 62, AB 116 – Subdivision Map Act
See Exhibit 7A

B. Chapter 65, SB 426 – Foreclosure
See Exhibit 7B

C. Chapter 78, AB 464 – Vital Records
See Exhibit 7C

D. Chapter 104, AB 727 – Public Trust
See Exhibit 7D

E. Chapter 137, AB 379 – Manufactured Housing
See Exhibit 7E

F. Chapter 159, AB 625 – Notaries Public
See Exhibit 7F

G. Chapter 176, SB 551 – Judgments
See Exhibit 7G

H. Chapter 219, SB 692 – Redevelopment Agencies
See Exhibit 7H

I. Chapter 251, SB 310 – Foreclosure
See Exhibit 7I

J. Chapter 380, AB 1169 – Escrow Agents
See Exhibit 7J

K. Chapter 396, SB 46 – Privacy
See Exhibit 7K

L. Chapter 406, AB 551 – Property Taxation
See Exhibit 7L

M. Chapter 431, SB 652 – Disclosures
See Exhibit 7M

N. Chapter 432, AB 253 – Subdivision Map Act
See Exhibit 7N

O. Chapter 544, SB 684 – Redevelopment Agencies
See Exhibit 7O

P. Chapter 605, SB 752 – Common Interest Developments
See Exhibit 7P **(Bill is 98 pages – only summary included with agenda.)**

Q. Chapter 659, SB 470 – Redevelopment Agencies
See Exhibit 7Q

R. Chapter 750, AB 1386 – Liens
See Exhibit 7R

S. Chapter 767, AB 325 – Land Use and Planning
See Exhibit 7S

T. Chapter 796, SB 341 – Redevelopment Agencies
See Exhibit 7T

8. <u>Taxes, Bonds and Assessments Section (Gytis Nefas)</u>

Nothing Scheduled.

9. <u>Title Documents Section (Ed Rusky)</u>

Nothing Scheduled.

10. Title Forms Section (Paul Flores)

A. **Action Item:** Condition of Title Guarantee (“CTG”)

1. **Discussion:** Form is modeled after Litigation Guarantee Form. Note that the proposed CTG doesn’t require an application. Also, review the language at the top of page two (2). Should the proposed language be retained or deleted from the draft CTG?

   See Exhibit 10.A.1

2. Conditions and Stipulations for draft CTG same as for other CLTA Guarantees

   See Exhibit 10.A.2

3. Table for further refinement or proceed to finalize form for Board Approval and CA DOI filing?

B. **Non-action item:** Report re: review of CLTA’s (1) Guarantee Face Page (Rev. 12-15-95), (2) Guarantee Conditions and Stipulations (Rev. 09-12-08) and (3) 21 Guarantee Forms (exclusive of Guarantee No. 22 (TSG):

1. Review Process: Commencing in 2014.
2. Review process of new guarantee form or forms (i.e. Transferable Development Rights Guarantee): Commencing in 2014.

C. **Non-Action Item:** New Definition of “Public Records”.

See Exhibit 10.C

D. **Conditional Action Items-Proposed ALTA Forms (12-03-13):** Motion to recommend to the Board that the CLTA adopt and direct the CLTA to file with the CA DOI with corresponding CLTA endorsement nos. on the condition that the forms are adopted by the ALTA “as is” with the revised or adoption date of 12-03-13 as follows:

1. Ex. 10.D.1: ALTA 11.2-06 Mortgage Mod. CLTA 110.11.2-06
2. Ex. 10.D.2: ALTA 41.0-06 Water-Buildings CLTA 143-06
3. Ex. 10.D.2.1: ALTA 41.1-06 Water-Improvements CLTA 143.1-06
4. Ex. 10.D.2.2: ALTA 41.2-06 Water-Described Improvements CLTA 143.2-06
5. Ex. 10.D.2.3: ALTA 41.3-06 Water-Land Under Development CLTA 143.3-06
6. Ex. 10.D.3: ALTA 42-06 Commercial Lender Group CLTA 144-06
7. Ex. 10.D.4: ALTA 43-06 Anti-Taint CLTA 145-06
8. Ex. 10.D.5: ALTA 44-06 Insured Mortgage Recording-Loan CLTA 146-06
9. Ex. 10.D.6: ALTA Expanded Coverage Residential Loan Policy Revised 12-03-13 – PROPOSED

10. Ex. 10.D.6.1: ALTA Expanded Coverage Residential Loan Policy Revised 12-03 – REDLINED
11. Ex. 10.D.7: ALTA/CLTA Homeowner's Policy – PROPOSED
12. Ex. 10.D.7.1: ALTA CLTA Homeowner's Policy – REDLINED

11. Special Sub-Committee - Electronic Recording and Signatures (Paul Flores)

Nothing Scheduled.

12. Special Sub-Committee – Copyright Protection of CLTA Forms and Manual

Nothing Scheduled.

13. CLTA Staff Report

Nothing Scheduled.

14. Court Decisions Section – Honorable Mention (Laura Lowe)

A. Centennial Development Corp. v. Lawyers Title Insurance Corp.
Arizona Court of Appeals – Div. 1

Filed 9-19-13

1. Under A.R.S. 20-1562, a title company is not liable for negligence in failing to reflect an encumbrance in a commitment or title policy because these products are not representations of the condition of title. Rather, a title policy is a contract under which the insurer agrees to indemnify the insured for losses caused by claims arising from encumbrances not identified in the insurer's commitment or policy.

2. A title policy generally only covers loss or damage incurred during the period of ownership (although it continues as to warranties of title made upon a sale of the property), but it does not require the insured to make such a claim before it sells the affected property. Therefore, plaintiff's sale of the property does not bar its claim for damages it alleges it incurred prior to the sale.

See Exhibit 14A

B. Chicago Title Insurance Co. v. Aurora Loan Services
Illinois Court of Appeals – 3rd Div.

Filed 8-30-13

Breach of warranties of title.

See Exhibit 14B

C. <u>Metropolitan National Bank v. Jemal (UNPUBLISHED)</u>
New Jersey Superior Court, Appellate Division

Filed 9-23-13

Knowledge of unrecorded mortgage based solely on credit report.

See Exhibit 14C

D. <u>Keshish v. Allstate Insurance Company</u>
U.S. District Court, Central District of California

Filed 4-22-13

Bad faith claims based on allegations that the value paid was too low. The court found no bad faith.

See Exhibit 14D

Bulletin 13/14 – 30
September 27, 2013

2013
Minutes of the Meeting
of the

CALIFORNIA LAND TITLE ASSOCIATION
FORMS AND PRACTICES COMMITTEE

Held at

Hilton Palm Springs
400 E. Tahquitz Canyon Way
Palm Springs, CA 92262
760-320-6868

September 5-6, 2013
Thursday: 1:00 PM - 5:00 PM
Friday: 9:00 AM - 1:00 PM

Members Present:	Therien, Roger - Chair	Miron, Avi
	Cavallaro, Robert - Vice-Chair	Herrington, Greg
	Hammann, Paul – Vice-Chair	Imperiale, Tom
	Bernath, Tom	Jourdan, Bill
	Bishop, Chuck	Kerns, Jeff
	Buchanan, Dan	Klarin, Ric
	Chandler, Tom	Nefas, Gytis
	Condict, Wayne	Reardon, Tim
	Dondanville, Jeff	Rusky, Ed
	Feryus, Jan	Saez, Karen
	Flores, Paul	Shepherd, Mark
	Heller, Marc	Smith, Steve
	Helmer, Dwight	Westcott, David
	Lee, Margery	Windle, David
Members Absent:	Borchert, Doug	Morgan, Tim
	Chalmers, Jerry	O'Connell, William
	Griffin, Larry	Smith, Elliot
	Guerino, Jerry	Thomas, Bill
	Lowe, Laura	Updegraff, John
	Morey, Shaun	
Also Present:	Page, Craig	
	Stonum, Neil	

a non-profit service organization of title companies since 1907
1215 K Street, #1816, Sacramento, CA 95814 * 916-444-2647 * Fax 916-444-2851
www.clta.org * mail@clta.org * Federal Tax ID# 95-0595810

1. Administrative Section (Elliot Smith)

It was moved and seconded, and the motion unanimously passed, that the Minutes of the June 6-7, 2013 meeting be approved as written.

2. Bankruptcy Section (Wayne Condict)

A. Palomar v. First American Bank
7th Circuit — Filed 7-11-13

One day before the Trustee filed his no asset report in the Debtors' Chapter 7 case, the Debtors filed an adversary proceeding to strip off a second mortgage on their "underwater property." The bankruptcy court denied the debtors' request to reopen and the Court of Appeals affirmed. Since there were no available assets the lender had not filed a proof of claim. But even if it had, the Court following *Dewsnup v. Timm* (502 U.S. 410) (1992) declined to construe an "allowed secured claim" under 506 (d) to be the same as an "allowed claim of a creditor secured by a lien on property" in 506 (a). There is no provision in the Code or public policy rationale that permits a debtor to strip a wholly-unsecured mortgage claim. Citing *Dewsnup* the Court held that Chapter 7 debtors cannot rely on Section 506 to import a strip off power into a Chapter 7 proceeding. This case addressed the question whether the *Dewsnup* rule (no stripping in a Ch. 7) would apply when the junior lien was completely "out of the money" and not just partially "unsecured".

There was no practice recommendation and the case was dropped.

B. In re Ryan (Ryan v. U.S.)
7th Circuit — Filed 7-8-13

The debtor sought to void or strip unpaid portions of federal tax liens through the filing of an adversary proceeding in advance of proposing a plan, arguing that Bankruptcy Code Section 506 (d) allowed that to be done in a Chapter 13 although not allowed in a Chapter 7. The United States Court of Appeals affirmed the bankruptcy court's refusal to order the lien strip. Relying on the US Supreme Court decision in *Dewsnup v. Timm* (1992), the Court of Appeal said section 506(d) should be given the same reading in both bankruptcy chapters. While Bankruptcy Code section 1322(b)(2) allows a plan to modify the rights of secured interest holders (other than primary residence lienholders the general provisions of the Code applicable to all Chapters (such as 506) do not.

The subject of lien stripping in Chapter 13s and so-called Chapter 20s (Chapter 7s followed by Chapter 13s) has been reported on by this committee, but no practice recommendations or manual revisions were suggested and the case was dropped.

C. Lien Stripping Articles

The articles were briefly discussed. *There was no practice recommendation and the matter was dropped.*

D. In re Lively
5th Circuit — Filed 5-29-13

This Fifth Circuit case affirmed the bankruptcy court's denial of confirmation of a Chapter 11 plan proposed by an individual debtor (Philip Lively) because it violated the absolute priority of Bankruptcy Code section 1129(b)(2)(B). Debtor's plan would have allowed him to retain all of his property - including the net value of a mortgage loan and rental income from

9 leased railroad tank cars. The absolute priority rule prohibits a lower class of creditors from receiving anything from a Chapter 11 plan until the superior class has been repaid in full. The rule's code provisions were amended in 2005 as part of the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) by exempting out property of an individual Chapter 11 debtor as that property is set forth in Code section 1115. Because section 1115 not only referred to property acquired after commencement of the case but also property described in section 541, Lively argued that the absolute priority rule did not apply as to any property of an individual debtor. The Fifth Circuit followed decisions in the 10th and 4th Circuits holding that the amendment to section 1115 by BAPCPA was intended to exempt only post-petition acquired property from the prohibition of the absolute priority rule.

There was no practice recommendation and the case was dropped.

E. <u>In re Castleton Plaza</u>

7th Circuit — Filed 2-14-13

This 7th Circuit case also addressed the absolute priority rule discussed in the case above. It did so in the context of what might constitute property that a debtor is prohibited from receiving as a result of a plan which does not pay superior class creditors in full. The introduction of new value by an insider complicates adherence to the absolute priority rule. To ensure that a junior class creditor (including an owner or shareholder of debtor) will receive nothing of value other than what is attributable to the new value being infused, the U.S. Supreme Court in RadLAX Gateway Hotel v. Amalgamated Bank, 132 S. Ct. 2065 (2012) required competitive bidding and permitted credit bidding by the estate's secured creditors. Here, debtor owned a shopping center. Debtor itself was owned entirely by George Broadbent. The only significant creditor held $10,000,000 in mortgage debt. The proposed plan would reduce that amount by $1,500,000, extend the repayment term with low principal payments for 10 years, reduce the interest rate and transfer ownership of the reorganized debtor to Broadbent's wife, Mary, in exchange for her payment of $375,000. Over mortgage lender's objections the bankruptcy court confirmed the plan. On appeal (certified directly to the 7th Circuit) to resolve the question of whether transfer of equity to an insider (here Broadbent's wife) requires that mortgage lender be allowed to credit bid, the 7th Circuit held that it does. The indirect benefit that George Broadbent would receive as a result of his wife's succession to ownership of the reorganized debtor was sufficient value to require the application of the RadLAX rule.

There was no practice recommendation and the case was dropped.

F. <u>In re Pringle (Hasse v. Rainsdon)</u>

Bankruptcy Appellate Panel – 9th Circuit — Filed 7-2-13

This Ninth Circuit BAP decision affirmed the bankruptcy court's 548 set-aside order and elaborated on Executive Benefits Ins. Agency v. Arkison (In re Bellingham Ins. Agency) reported in Minutes Feb. 8 &9, 2013. It confirmed the "authority" (which it assiduously declined to refer to as "jurisdiction") of the bankruptcy judge to enter an order against Jolene Hasse, a non-creditor defendant in a 548 adversary proceeding. Within 2 years preceding his Chapter 7 filing, Raymond Pringle conveyed his Idaho residence to his girlfriend Hasse by gift deed. Hasse contended that she gave reasonably equivalent consideration by way of her promise to pay the taxes, utilities and upkeep on the home, let Pringle continue to live there and to take care of him for the rest of his life. In granting the trustee's complaint to set her deed aside, the bankruptcy judge held that only consideration resulting in actual benefit to creditors can be taken into account when calculating equivalent value. Neither did the bankruptcy court accept Hasse's "no harm – no foul" argument that Pringle's Idaho homestead exemption would have insulated the house from his creditor's reach had he not transferred it to Hasse.

After finding sufficient support for the bankruptcy judge's 548 ruling the BAP turned to the Stern v. Marshall issue. The Panel acknowledged that the U.S. Supreme Court's grant of certiorari in the 9th Circuit's decision in Bellingham will resolve the split of authority between the 6th (Waldman v. Stone) and the 9th Circuits on whether challenges to a bankruptcy judge's authority can be consented to (or waived) either expressly or impliedly by the defendant. In Bellingham, the 9th Circuit found implied consent by "sand-bagging" i.e. withholding challenges to authority while seeking to take advantage of any positive result and only asserting lack of authority after an adverse ruling. In the present case the BAP found waiver by Hasse's counsel's failure to assert lack of authority until the BAP itself requested briefing on the issue. There was no evidence that Hasse was aware of the issue but the Panel held that her counsel should have been aware of it – and that duty and failure to assert to be sufficient. Bellingham will be heard in the 2013 Term of the Supreme Court and be reported to this Committee for consideration.

There was no practice recommendation and the case was dropped.

G. <u>In re Spokane Raceway Park (Moe v. Munding)</u>
Bankruptcy Appellate Panel – 9th Circuit Filed 8-2-13

This BAP opinion affirmed the order closing the debtor's Chapter 11 case. The case was filed in August of 2006 and during its more that 6 year pendency involved objections and appeals by the owner (Orville Moe) of the debtor from almost every order including the appointment of a trustee, the trustee's proposed settlement of a contractual dispute with the Kalispell Tribe, confirmation of the proposed liquidating plan for 100% payment to all creditors, and the trustee's final accounting. Each objection and appeal raised the argument against the settlement and transfer of land to the Tribe. The BAP declined to consider his arguments because the settlement was approved by the bankruptcy court and Moe's appeal was denied. The law of the case doctrine precludes attack on the transfer unless the approval order was clearly erroneous, would do a manifest injustice, would be affected by intervening controlling authority or was based on evidence substantially different from new evidence introduced.

While the case *is a cautionary tale on the persistence of some litigants in challenging title transfers, no practice recommendations or manual changes were suggested.*

H. <u>In re Lavasseur</u>
U.S. District Court – District of Massachusetts Filed 6-3-13

The U.S. District Court affirmed the bankruptcy court's determination that Levasseur's $160,000 debt to Old Republic Title Insurance Company (as Bank of America's assignee) under an unreleased HELOC was non-dischargeable – the loan funds having been obtained under false pretenses (BK Code Sec. 523(a)(2)(A)). Lavasseur, who was at one time a real estate agent, took out a HELOC with BofA's predecessor, Fleet Bank, secured by a deed of trust encumbering her Rowley, MA property. She sold the Rowley property in 2003 at which time Fleet was paid in full; however, Fleet failed to close the line of credit. Levasseur then began receiving statements from Fleet (and later B of A) reflecting both the credit limit and available credit on the account as $124,200. In 2005, Levasseur went to a B of A branch and in two separate withdrawals drew the account down to the limit.

The District Court confirmed the bankruptcy court's findings that the facts sufficiently established that Levasseur knew she was making withdrawals under a closed account and that her explanation that she thought she was drawing on a new line of credit was implausible. The District Court also found that the outcome was not affected by BofA's negligent record-keeping or its failure to search the public records for the Rowley property; it concluded that B of A justifiably relied on Levasseur's implied representation of her right and ability to draw on the account.

There was no practice recommendation and the case was dropped.

I. <u>In re Pazdzierz (Pazdzierz V. First American Title Ins. Co.)</u>
6th Circuit Filed 6-10-13

The Sixth Circuit Court of Appeals affirmed the district court's reversal of the bankruptcy court's order denying First American Title Insurance Company's request for an order of non-dischargeability. Pazdzierz had applied for and obtained loans in excess of $1,000,000 for properties that he did not own. After Pazdzierz defaulted on the loans, as part of a settlement, lender assigned a 75% interest in the promissory notes to First American. First American filed a non-dischargeability complaint in Pazdzierz's Chapter 7 arguing that the loans were made in reliance on Pazdzierz's false financial statements (BK Code Sec. 523(a)(2)(B)). The bankruptcy court disagreed holding that pursuant to Michigan state law claims of fraud are personal and not assignable rendering First American's interest invalid. On review the district court distinguished First American's claim, which was based upon a debt owed under a promissory note, from that of a "naked fraud" claim contemplated by the Michigan law. The Sixth Circuit agreed and remanded the matter to the bankruptcy court.

There was no practice recommendation and the case was dropped.

J. <u>In re Papazov (Goldenberg v. Deutsche Bank National Trust Co.)</u>
Bankruptcy Appellate Panel – 9th Circuit Filed 5-30-13

In 2006 Irina Lukashin secured her borrowing from Money Warehouse (later assigned to Deutsche Bank) with a $1.8 million deed of trust on property in Los Angeles.. In 2008 she quitclaimed the property to Goldenberg. In spite of that deed she later executed a $30,000 deed of trust to Papazov. Papazov then filed a chapter 7 listing the note as personal property in his Schedule B. Deutsch Bank thereafter obtained a lift-stay order (also applicable to successors to Papazov) and foreclosed. Papazov's case was dismissed in October, 2011 and closed in January, 2012.

Deutsch Bank filed an unlawful detainer action in state court. Goldenberg petitioned to reopen the Papazov bankruptcy and to stay the unlawful detainer action. Her motions were denied and she appealed to the BAP. Affirmed: Goldenberg did not have standing to open Papazov's BK case because she could not show an injury, nor causation nor redressability. She was neither a creditor nor a successor as to any of Papzov's bankruptcy estate. Moreover, a case that was not fully administered cannot be reopened. Since Papazov's case was dismissed not fully administered.

There was no practice recommendation and the case was dropped.

K. <u>In re Pekrul (Weimar Investments v. First Financial Bank)</u>
Bankruptcy Appellate Panel – 9th Circuit Filed 7-22-13

Weimar Investments, Inc. was in the foreclosure avoidance business. To help borrowers (unnamed in the case) threatened with foreclosure on a property located in Las Vegas, Weimar aided them in their deeding of a 1% interest in that property to John Hammer, a debtor under a pending chapter 13. Hammer amended his Schedule A to add his 1% interest. First Financial Bank, the lender, obtained relief from the automatic stay. Weimer then assisted in the deeding of another 1% interest from borrower to Brett Pekrul. Pekrul soon filed a chapter 13 and listed his 1% interest on Schedule A. First Financial, in addition to obtaining relief from the automatic stay, moved to examine the books and records of Weimar. Ultimately the bankruptcy court approved the contempt sanctioning of Weimar and the awarding of $25,000 in attorney's fees for failure to comply with document production and other orders. On appeal the BAP found no error in holding Weimar and its owner in contempt.

There was no practice recommendation and the case was dropped.

L. In re Wren Alexander Investments (Alexander Investments v. I.R.S.)
5th Circuit Filed 6-4-13

This case involved a dispute between the IRS and bankruptcy debtor Wren Alexander Investments, Inc. (Wren LLC). The IRS recorded a tax lien for $23,385,778.97 on April 14, 2008 against a large parcel of horse property in Texas. The lien was aimed at the unpaid payroll taxes of United Capital Investment Group, Inc. ("UCIG") a previous owner of the property. Prior to recordation of the IRS lien the horse property had been transferred from UCIG to Medina Heritage Ltd. and then from Medina Heritage to Wren LLC. Wren LLC disputed that the lien attached to the property. The District Court affirmed the bankruptcy courts' finding that the IRS lien attached. The Fifth Circuit agreed and affirmed. The IRS Lien attached because 1) Wren LLC never offered evidence that there was a legal deficiency in the IRS lien and 2) the transfers to Medina Heritage and to Wren LLC were not bona fide because the grantor and grantee in each case were connected, intermingled and not at arm's length. Moreover, the purchase price paid by Wren LLC was the amount of the existing mortgage indebtedness (not the fair market value) with a lease back to grantor for less than fair rental value.

There was no practice recommendation and the case was dropped.

M. In re Ceralde (Smith v. Bank of New York Mellon)
Bankruptcy Appellate Panel – 9th Circuit Filed 8-6-13

This involuntary individual Chapter 7 bankruptcy involves a dispute between a borrower (who apparently was known by many different names) and the secured lender (BNYM) who conducted a same-day (but post-petition) trustee's sale and then filed a motion to retroactively annul the automatic stay and validate the trustee's deed. An involuntary Chapter 7 was filed on September 16, 2011 by "alleged creditors" against Norma Ceralde aka Michael Henry aka Nolan A. Smith, names of the trustor. The name appearing on the title and on the deed of trust, that of Nolan Smith, Jr., was not placed on the involuntary petition. The BNYM foreclosure sale was also conducted on September 16th. Deposition testimony revealed that the foreclosure trustee received notice that there may be a bankruptcy affecting the property but because of the name disparity a decision was made to proceed with the sale. Nevertheless, on November 21, 2011 the lender rescinded the sale. On January 30, 2012 the lender conducted another foreclosure sale and followed it with an unlawful detainer action in state court. On May 8, 2012 the debtor filed a (voluntary) chapter 13 petition. Debtor also filed a lawsuit in Superior Court seeking Injunctive Relief, Declaratory Relief and Quiet Title based on lender's purported violation of the automatic stay. On June 20, 2012 the lender filed a motion in the Chapter 7 court to annul the stay. Motion granted. Debtor appealed.

The Bankruptcy Appellate Panel applied two main factors in determining whether annulment of the stay was proper: (1) Did the creditor have knowledge of the bankruptcy and (2) did the debtor engage in unreasonable conduct. The BAP found that even though the creditor knew about the bankruptcy the debtor engaged in unreasonable conduct. Specifically, it found that the involuntary chapter 7 was fraudulent. The creditors who filed the involuntary proceeding never appeared in the action. The court found that debtor was the only one to benefit from the chapter 7 because he lived in the house rent free for two years. Moreover the debtor never took any preventive steps in the chapter 7 proceeding until the UD action was filed against him.

There was no practice recommendation and the case was dropped.

N. <u>In re Perle (Perle v. Fiero)</u>
9th Circuit — Filed 8-2-13

Creditors claiming on certain non-dischargeable debts must nevertheless file an action objecting to discharge in order to preserve their claim post discharge. (Bankruptcy Code Section 523(c).) Under Federal Rules of Bankruptcy Procedure 4007(c) a creditor has 60 days from the date of the 541 meeting to file such a complaint. But if the debt was not properly listed and the creditor had no knowledge of the bankruptcy case the time for filing, a nondischargeabilty complaint can be extended.

Fiero Brothers filed motions to reopen the Perle BK case and to determine non-dischargeability of its $350,000 arbitration debt four years after Perle received his discharge and the case was closed. Perle objected for two reasons: first, that the debt was properly scheduled and second, that Fiero had imputed knowledge of the bankruptcy because Fiero's attorney in the arbitration (Russo) represented another of Perle's creditors (Corsair Capital) in a non-dischargeability complaint in Perle's bankruptcy. The bankruptcy court found that the debt was not properly listed because the petition did not use Fiero's name, misstated the year of award and claimed the amount of the debt was unknown (it was clearly $350,000) – even though Perle obviously knew how to schedule debts as he had listed his others creditors and debts correctly. As for imputed knowledge of the bankruptcy, the court noted that generally speaking the knowledge of the attorney is imputed to the client during the attorney-client relationship. However, the relationship is over when the services are performed. In this case Russo represented Fiero in the arbitration proceeding and through the domestication of the arbitration award in CA but not beyond that. Affirmed by the BAP.

No practice recommendations were made but it was suggested that the manual make reference to this case *where unlisted debts are identified as non-dischargeable. [CLTA Manual 07:14 F(c)].*

O. <u>In re Ly (Ly v. Che)</u>
Bankruptcy Appellate Panel – 9th Circuit — Filed 5-29-13

This case is an appeal by debtor Ly to the bankruptcy court's granting Che relief from stay to pursue an unlawful detainer proceeding in state court. Che leased her residential property to Ly's sister Vanessa in March, 2006. Ly moved in sometime in 2008. Neither Vanessa nor Ly has paid rent. Che claimed that Ly forged her signature on a deed of the property to himself in 2009. Che got a state court quiet title judgment against Ly by default and the judgment became final. Ly scheduled the residence as his property in Schedule A of his chapter 13 petition. He objected to Che's motion for relief from stay arguing that Che had no standing since she was not a creditor. The court rejected that argument holding that Che's declaration in support of her motion had indeed made a colorable claim of title to property of the estate. The BAP found Ly's appeal to be frivolous (simply a means of extending his rent free occupancy) and awarded sanctions.

There was no practice recommendation and the case was dropped.

P. <u>In re Eleiwa (Eleiwa v. Whitmore)</u>
Bankruptcy Appellate Panel – 9th Circuit Filed 6-5-13

Debtor filed a petition for chapter 7 relief stating under penalty of perjury that her residence was in the City of Colton, San Bernardino County, California. Concurrently she filed her Statement of Financial Affairs wherein she denied living at any other address within three years prior to filing. Subsequently, upon the filing of amended schedules, debtor claimed two properties of the estate as exempt residential homesteads under California exemption laws, each of these two properties being located in Orange County, California. Trustee objected, claiming, alternatively, (i) these properties were not property of the estate and (ii) that debtor did not reside in either of these two properties. The bankruptcy court held for the trustee. Debtor appealed to Ninth Circuit BAP, which affirmed, noting that California exemption law applies to only one qualifying residence not two.

There was no practice recommendation and the case was dropped.

Q. <u>In re Heldt (Goddard v. Heldt)</u>
10th Circuit Filed 5-14-13

Within 2 years of her 2009 Chapter 7 filing Heldt transferred her title to an Oklahoma residence to her sister for no consideration. The bankruptcy trustee sought to set the transfer aside under the strong arm powers of 544. The bankruptcy judge found against the trustee holding that the debtor had only bare legal title and finding that she was trustee of a resulting trust in favor of her mother who had conveyed the title to her several years earlier while she was a minor. Since the mother was still in possession any hypothetical purchaser or judgment lien creditor would have been on constructive notice (applying Oklahoma law) of the mother's interest. Although nothing of value was received by debtor in exchange for her deed, nothing of value was given away. So even if the transfer occurred while the debtor was insolvent, it was not a constructive fraudulent transfer. On appeal by the bankruptcy trustee to the 10th Circuit, affirmed. Deed was not overturned.

There was no practice recommendation and the case was dropped.

R. <u>In re Fadel (Fadel v. DCB United)</u>
Bankruptcy Appellate Panel – 9th Circuit Filed 5-31-13

The Bankruptcy Appellate Panel for the Ninth Circuit affirmed the bankruptcy court's granting of relief from stay to the third party purchaser of foreclosure-sold property in order to allow the purchaser to proceed with an unlawful detainer action. Debtor filed a chapter 13 petition two days before the scheduled foreclosure sale by lender Bank of America. Debtor was the wife of the record owner/obligor under the note and deed of trust. Debtor had deeded her interest to her husband as his sole and separate property when he first acquired the home more than ten years earlier. In spite of having been notified of the bankruptcy filing of borrower's spouse, B of A proceeded to sale whereupon Appellee DCB United LLC purchased at the auction. DCB contended that debtor lacked any legal or equitable interest in the property. Debtor claimed a community property interest.

The existence and scope of an "interest" under § 541(a)(1) of the Bankruptcy Code is a question of state law. The general community property presumption (Cal. Fam. Code § 760) for property acquired during marriage is contradicted by the affirmative act of taking title in the name of one spouse during marriage with the consent of the other spouse. The court rejected debtor's claim that she was the subjected to "undue influence" when she deeded to her husband noting that 1) the deed would only be voidable and not void and 2) it could not be set aside as against a purchaser for value without notice of such alleged duress. The court also rejected debtor's claim that the payment of community funds to reduce principal of the debt secured by the deed of trust created a pro tanto community property interest under the

"*Moore / Marsden rule*". Because of CA Evid. Code §662 (the owner of legal title is presumed to hold all beneficial title) tracing OF funds used to purchase the property was not sufficient to prove by clear and convincing evidence that an agreement existed that the record title was anything other than what was intended. Use of community funds would only provide a basis for reimbursement to the non-owning spouse. CA Fam. Code § 920.

There was no practice recommendation and the case was dropped.

S. <u>JP Morgan Chase Bank v. Johnson</u>
8th Circuit Filed 7-9-13

The Eighth Circuit Court of Appeals affirms the U.S. District Court's reversal of the bankruptcy court's ruling that Arkansas' "Emergency Amendment" required federal lender JP Morgan Chase Bank to register to do business in Arkansas in order to conduct foreclosures under the Statutory Foreclosure Act of 1987. This appeal was from an action filed by JP Morgan in federal court and consolidated with a number of bankruptcy and other civil cases invoking the Emergency Amendment as a challenge JP Morgan's foreclosures. In the bankruptcy cases, JP Morgan appealed plan confirmation orders in which the debtors' chapter 13 plans failed to include certain foreclosure fees and costs. The Emergency Amendment required that a foreign entity conducting foreclosures be "authorized to do business" in the Arkansas. The Eighth Circuit agreed with the district court that being 'authorized to do business' might not mean the same thing as 'register to do business'. Since the law did not specifically require JP Morgan to register to do business in Arkansas it could conduct foreclosures there is it was authorized to do business there. It held that federal banks are authorized to do business in all states under the National Banking Act, 12 USC § 21 et seq. The court also noted that the US Supreme Court has held that federal control shields national banking from unduly burdensome and duplicative state regulation.

There was no practice recommendation and the case was dropped.

3. <u>Court Decisions Section (Laura Lowe)</u>

A. <u>Biancalana v. TD Service Company</u>
Cal. Supreme Court Filed 5-16-13

A trustee under a deed of trust may declare a trustee's sale to be void where the trustee made an error in communicating the lender's credit bid to the auctioneer, and the error was coupled with a grossly inadequate bid price. The court pointed out that its holding was premised on the trustee discovering its mistake before it issues the deed, and that after the deed is issued, a bona fide purchaser is entitled to a conclusive presumption that the sale was conducted regularly and properly. .

This case will be referenced in Section 58.15Q of the CLTA Manual. There was no other practice recommendation and the case was dropped.

B. <u>Zhang v. Superior Court</u>
Cal. Supreme Court Filed 8-1-13

Fraudulent conduct by an insurer does not give rise to a private right of action under the Unfair Insurance Practices Act (Insurance Code section 790.03 et seq.), but it can give rise to a private cause of action under the Unfair Competition Law ("UCL") (Business and Professions Code section 17200 et seq.). The court pointed out that the UCL permits only injunctive relief and restitution, not damages.

There was no practice recommendation and the case was dropped.

C. <u>Chicago Title Ins. Co. v. Washington State Office of the Insurance Commissioner</u>
Washington Supreme Court — Filed 8-1-13

The case holds that a title insurance company can be held liable for the acts of its agents as to spending in excess of state limits for entertainment.

There was no practice recommendation and the case was dropped.

D. <u>Hollingsworth v. Perry</u>
U.S. Supreme Court — Filed 6-26-13

Proposition 8 amended the California State Constitution to provide that "[o]nly marriage between a man and a woman is valid or recognized in California". The 9th Circuit upheld the District Court's decision holding that Proposition 8 is unconstitutional because it violates the Equal Protection Clause of the U.S. Constitution. The Supreme Court vacated the judgment of the 9th Circuit on the basis that petitioners, who were the official proponents of Proposition 8, do not have standing to appeal. This leaves in place the District Court's decision because the plaintiffs in that case were actual aggrieved parties.

This case will be referenced in an appropriate place in the CLTA Manual. There was no other practice recommendation and the case was dropped.

E. <u>Coker v. JP Morgan</u>
Cal. App. 4th Dist. — Filed 7-23-13

The Court of Appeal reverses San Diego Superior Court's sustaining of defendant's demurrer without leave to amend. Plaintiff is a borrower on a purchase money loan secured by her residence sold at a short sale. Defendant is a successor to the original lender. This is a case of first impression.

The question here is whether the lender can seek a deficiency from the borrower after approving a short sale where the lender conditioned the sale on borrower being responsible for the deficiency. Borrower brought this action for Declaratory Relief in response to collection efforts by the lender. Borrower alleged protection from deficiency under the language of CCP § 580b. The lower court ruled that the statute applied only after the property was sold by judicial or nonjudicial foreclosure.

In applying the plain language of the statute, the court held that § 580b applies to any loan used to purchase residential real property regardless of the mode of the sale. The statute plainly states that "No deficiency … shall lie in any event … after a sale of real property … for failure of the purchaser to complete his or her contract of sale … under a deed of trust …given to the lender to secure repayment of a loan which was in fact used to pay all or part of the purchase price of that dwelling …" [Emphasis supplied]

There is nothing in the statute that says foreclosure is a precondition to its application. The court also recognizes that as in all of the Depression era anti-deficiency legislation, that the courts have liberally construed the interpretation of statutes in favor of enforcing the nonrecourse goals of the legislation. The Legislature passed § 580b in order to stabilize purchase money secured land sales [prices] by [preventing] overvaluing property and to ensure that purchasers as a class are harmed less during economic decline when property values drop.

The court concludes that there cannot be a waiver of the anti-deficiency protection under §580b as it would be contrary to public policy.

Reference will be made CLTA Manual Section 58:13 noting that C.C.P. Section 580b also extends to short sale situations. There was no other practice recommendation and the case was dropped.

F. Enloe v. Kelso
Cal.App. 2nd Dist. Filed 7-3-13

The Court of Appeal affirms the granting of summary judgment in favor of defendant borrowers against plaintiff lenders' action for deficiency after a short sale of the secured property. Lenders consented to the short sale for a partial payment and reconveyed their third deed of trust. Plaintiffs filed action to recover the deficiency. The loan was deemed a purchase money loan, notwithstanding that the deed of trust recorded after the close of escrow.

Lenders were the individual sellers of the subject property taking a carry-back deed of trust. The primary lender, Washington Mutual, secured its loan with a first and second deed of trust. It objected to the carry-back by the sellers of a third deed of trust in escrow for $93,750.00. The purchase price was $1.9 million.

In order to circumvent Washington Mutual's objection to seller's loan, sellers recorded their deed of trust after the close of escrow, and refunded to the buyers the amount of the loan from the sale proceeds.

CCP § 580b provides that no deficiency judgment shall lie "… under a deed of trust … given to the vendor to secure payment of the balance of the purchase price of the real property …"

Sellers argued that the loan was not purchase money since the trust deed recorded after the close of escrow and that the buyers closed the transaction with sufficient funds. The court considered the fact that the parties had agreed previously to finance the purchase, but did not do so through the sale escrow due to Washington Mutual's objection. The fact that they carried out the agreement after close of escrow did not change the fact that it was for the purpose of financing the purchase.

Section 580b does not change the character of a purchase money loan because the loan is made after the close of escrow, as long as it is made to finance the purchase. Section 580b is liberally construed to effect its purpose to discourage vendors from overvaluing properties, and to prevent the aggravation of a downturn that may result from an economic depression.

There was no practice recommendation and the case was dropped.

G. Bank of America v. Roberts
Cal.App. 5th Dist. Filed 7-17-13

The July 2011 amendment to CCP Section 580e, which extends anti-deficiency protection to borrowers with respect to all deeds of trust secured by a 1-4 family residential property (as opposed to just a first-position deed of trust, which was the case prior to the amendment), cannot retroactively be applied as a legal prohibition to a second-position lender's pursuit of a deficiency judgment in an instance where defendant and plaintiff entered into a short-sale agreement, prior to the date the amendment took effect, in which defendant expressly acknowledged and agreed to her obligation to repay the unpaid balance of the loan. As well, any rights defendant may have had under CCP Section 726 (the one form of action rule) were waived based upon her request for and consent to the short sale arrangement.

There was no practice recommendation and the case was dropped.

H. Liberty National Enterprises v. Chicago Title Insurance Co.
Cal.App. 2nd Dist. Filed 5-22-13 (Pub. Order 6-13-13)

TITLE INSURANCE: The court followed *Safeco Title Ins. Co. v. Moskopoulos* (1981) 116 Cal.App.3d 658, holding that the insuring clause of a title insurance policy did not cover an action that did not allege defective title, but rather tortious conduct in the manner in which the insured acquired title. There was no potential for coverage and therefore no duty to defend. The court did not address whether any policy exclusions applied because an occurrence not within the insuring clause does not also have to be excluded by the policy's exclusions.

There was no practice recommendation and the case was dropped.

I. Jenkins v. JP Morgan Chase
Cal.App. 4th Dist. Filed 5-17-13

TRUSTEE'S SALES: The court upheld the trial court's sustaining of a demurrer without leave to amend, finding:

1. Production of the note is not required for a lender to process a trustee's sale.

2. Plaintiff's claim that defendant violated the terms of a securitized investment trust's pooling and servicing agreement fails because plaintiff was not a third party beneficiary of that agreement.

3. A borrower cannot bring a preemptive judicial action to challenge whether the person initiating the foreclosure is authorized to do so because California's trustee's sale statutes do not allow for an additional requirement that the foreclosing entity must demonstrate in court that it is authorized to initiate a foreclosure.

4. Civil Code Section 2932.5's requirement that an assignment be recorded before the power of sale can be exercised applies to mortgages, but not to deeds of trust.

5. Plaintiff lacked standing under Business and Professions Code Section 17200 et seq. (Unfair Competition Law) because one of the requirements is for a plaintiff to show economic injury resulting from the defendant's unlawful acts. Here, plaintiff's economic injury was a result of her default on her loan, which occurred prior to defendants' allegedly unlawful acts.

6. Plaintiff's claim of a breach of the implied covenant of good faith and fair dealing fails because the covenant must be related to a contract. Here, the only contracts were the note and deed of trust and defendants' alleged conduct was in connection with plaintiff's efforts to have the loan modified and in connection with the conduct of the trustee's sale, not to a violation of any provision of the note and deed of trust.

7. Plaintiff did not state a cause of action for violation of RESPA's Qualified Written Request rules because any harm plaintiff suffered occurred as a result of her own default on the loan.

There was no practice recommendation and the case was dropped.

4. Closing Instructions Section (Bill Jourdan)

Assertion of escrow liability for missed deeds of trust.

This item was reviewed and discussed, particularly the importance of each company stressing to employees the importance of reviewing lenders' instructions to make sure they do not create additional liability.

5. Governmental Regulations Section (Jeff Dondanville)

Board of Governors request for the Forms and Practices Committee to review the issue of cities using eminent domain to acquire mortgages and to make recommendations.

This matter was reviewed and discussed. No action was recommended at this time other than to continue to monitor the situation.

6. Subdivision and Land Use Section (Douglas Borchert)

A. Koontz v. St. Johns River Water Management District
U.S. Supreme Court Filed 6-25-13

In Koontz v St. Johns River Water management District, the Supreme Court ruled, in a five to four decision by Justice Alito, that when a government – any government – engages in land-use regulation, including by denying a permit or demanding payment as a condition for a permit, the government must show that there is a nexus and rough proportionality between its demand on the landowner and the effects of the proposed land use. The case broadens property owners' rights to bring constitutional challenges to land-use decisions, and is likely to result in increased litigation.

There was no practice recommendation and the case was dropped.

7. Legislation Section (Tim Reardon)

A. Redevelopment Agency update

This matter was reviewed and briefly discussed.

8. Taxes, Bonds and Assessments Section (Gytis Nefas)

A. Taxation – Indian leases

This matter was reviewed and briefly discussed.

9. Title Documents Section (Ed Rusky)

Nothing Scheduled.

10. Title Forms Section (Paul Flores)

A. **Non-Action Item:** CLTA Form Filing dated August 5, 2013, covering nine (9) ALTA Endorsements and the revised ALTA Short Form Residential Limited Coverage Junior Loan Policy (04-02-13). Anticipated DOI approval date on or about 9-5-13.

Each of the items provided as Exhibits for this item was reviewed and briefly discussed.

B. **Action Item:** Motion to recommend to the Board that the CLTA adopt and direct the CLTA staff to file with the CA DOI the revisions to CLTA endorsement form nos. 100.23-06, 100.24-06 and 100.29-06 which includes an option to exclude from coverage a specific exercise of rights as described in a particular interest excepted from Schedules A or B.

This item was reviewed and briefly discussed and it was then moved and seconded, and the motion unanimously passed, to request that CLTA file the referenced amended forms with the California DOI on behalf of all member companies.

C. **Action Item**: Covered risk no. 25 needs to be modified to limit damages due to fracking activity. Proposed modification to CLTA/ALTA Homeowner's Policy is the addition of exclusion language from paragraphs 5(d) and 5(e) of ALTA 9.7-06 (04-02-12). [Carried over from CLTA F&P Nov. 2012, agenda item no. 10.C and June 2013, agenda item no. 10E.2].

This item was reviewed and discussed and it was then moved and seconded, and the motion unanimously passed, to request that CLTA file the referenced modified form with the California DOI on behalf of all member companies with the following changes after they are approved by the American Land Title Association:

Add the following Exclusions:

8. Contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence.

9. Negligence by a person or an Entity exercising a right to extract or develop minerals, water, or any other substances.

Modify Paragraph 2.b(3) of the Conditions to read as follows:

(3) the trustee or successor trustee of Your Trust or any Estate Planning Entity created for You to whom or to which You transfer Your Title after the Policy Date;

D. **Action Item:** Title Forms subcommittee report and draft of a new product that provides title information with liability cap and without contemplation of issuance of a title insurance policy. [Carried over from CLTA F&P June 2013, agenda item no. 10.D re: *Abengoa Bioenergy v. Chicago Title Insurance Co.* (Missouri unpublished decision)].

After discussion, this was sent back to the Forms Section to draft a standard exception for General Index matters.

E. **Action Item:** Motion to recommend to the Board **1)** that the CLTA withdraw the ALTA Residential Title Insurance Policy (6-1-87) and archive the same as the ALTA has decertified it (08-01-2013) and **2)** to file the current ALTA Residential Limited Coverage Jr. Loan Policy (08-01-12) with a technical correction (08-01-13).

This item was reviewed and briefly discussed and it was then moved and seconded, and the motion unanimously passed, to request that CLTA file a withdrawal of the ALTA Residential Title Insurance Policy and file the referenced amended ALTA Residential Limited Coverage Jr. Loan Policy with the California DOI on behalf of all member companies.

11. Special Sub-Committee – Electronic Recording and Signatures (Paul Flores)

Proposed Amendments to ERDS Regulations Open for Public Comment

This matter was reviewed and briefly discussed.

12. Special Sub-Committee – Copyright Protection of CLTA Forms and Manual

Nothing Scheduled.

13. CLTA Staff Report

Nothing Scheduled.

14. Court Decisions Section – Honorable Mention (Laura Lowe)

A. Heritage Financial v. Monroy
Cal.App. 1st Dist. — Filed 3-29-13 (Pub. Order 4-25-13)

An assignment of a promissory note does not include an assignment of a tort cause of action for fraud, unless the fraud claim is specifically included in the assignment.

B. C 1031 Properties v. First American Title Insurance Co.
Washington State Court of Appeals — Filed 5-23-13

An exclusion in a title insurance policy requiring knowledge on the part of the insured requires *actual* knowledge. *Constructive* knowledge is not sufficient.

C. Fidelity National Title Co. v. First American Title Insurance Co.
Colorado Court of Appeals — Filed 5-23-13

A title agent was liable for the total loss paid by the underwriter where the agent had knowledge of a prior lien and failed to pay it off. The court did not address the provision of the underwriting agreement limiting the agent's liability to $500 because the agent did not preserve the argument for appeal.

D. Kondaur Capital Corp. v. Fidelity National Title Insurance Corp.
Arizona Court of Appeals (UNPUBLISHED) — Filed 5-7-13

1. A title company does not have an obligation to issue another title policy following the issuance a title policy or trustee's sale guarantee. 2. Refusal to issue a title policy does not constitute a cloud on title. 3. Where the legal description in a title policy is correct, the title company does not have a duty to verify that the assessor's parcel number is correct.

E. Insight Assets v. Farias
Utah Supreme Court — Filed 8-6-13

A vendor purchase money mortgage has priority over a third party purchase money mortgage, so a foreclosure by the third party mortgage does not wipe out the vendor's mortgage. Here, a subsequent purchaser of the property was not a BFP because the vendor/lender's mortgage was of record, but the purchaser nevertheless prevailed because the vendor/lender was guilty of laches.

F. Riverisland Cold Storage v. Fresno-Madera Production Credit Assn.
California Supreme Court — Filed 1-14-13

Evidence of oral promises or agreements at variance with the terms of a written contract may be considered to determine if the contract should be invalidated as having been procured by fraud, even where the contract contains an "integration clause". The court overruled its 1935 decision in *Bank of America v. Pendergrass*, which held that evidence offered to prove fraud "must tend to establish some independent fact or representation, some fraud in the procurement of the instrument or some breach of confidence concerning its use, and not a promise directly at variance with the promise of the writing." The court pointed out that a showing of justifiable reliance would still be necessary to establish the alleged fraud.

G. Logan v. U.S. Bank National Association
9th Circuit 7-16-13

This action was for injunctive relief alleging that defendant's failure to provide a 90-day notice prior to evicting plaintiff/tenant was a violation of the federal Protecting Tenants at Foreclosure Act of 2009. The court held:
1. Even though plaintiff was the defendant in a state court unlawful detainer action, the District Court should not have abstained from hearing this action because the state court action did not implicate "important state interests".
2. There is no private right of action under the Act because it does not evince a congressional intent to create a private right of action and, therefore, the court affirmed the District Court's dismissal of the complaint.

H. Deutsche Bank v. First American Title Insurance Co.
Massachusetts Supreme Judicial Court 7-11-13

There is no duty under a title insurance policy to defend a lawsuit alleging predatory lending because title insurance does not cover defects in the note secured by the insured mortgage.

United States Bankruptcy Appellate Panel

For the Eighth Circuit

No. 13-6013

In re: Robert N. Armstrong

Debtor

Bank of America, N.A

Plaintiff - Appellee

v.

Robert N. Armstrong

Defendant - Appellant

Appeal from United States Bankruptcy Court
for the Eastern District of Missouri - St. Louis

Submitted: July 17, 2013
Filed: September 19, 2013 (Corrected September 20, 2013)

Before FEDERMAN, Chief Judge, SHODEEN and NAIL, Bankruptcy Judges.

FEDERMAN, Chief Judge

Debtor Robert N. Armstrong appeals from the Order of the Bankruptcy Court[1] finding his debt to Bank of America nondischargeable under 11 U.S.C. § 523(a)(2) for fraud and § 523(a)(4) for embezzlement. For the reasons that follow, the Judgment finding the debt nondischargeable under § 523(a)(4) is AFFIRMED.

FACTUAL BACKGROUND

Debtor Robert N. Armstrong was the owner, sole member, and primary manager of RNA Properties, LLC. In August 2001, RNA Properties acquired a strip mall in Dallas, Texas though financing from Southwest Bank. The financing came from two loans, one in the amount of $1.6 million, and a second in the amount of $400,000. The first note was secured by a Deed of Trust on the mall. As relevant here, the Deed of Trust required RNA Properties to list Southwest Bank as the loss payee on its insurance policies. The mall was insured by Public Service Mutual Insurance Company ("PSM"), but the policy listed Southwest as the mortgage holder, rather than as a loss payee as was required under the loan documents.

On January 25, 2009, a fire destroyed one of the three structures at the mall. PSM issued nine checks under the policy, totaling $917,149.26, made payable to the Debtor d/b/a RNA Properties. The Debtor endorsed and deposited all of the checks.

At issue here are three of those insurance checks in the amounts of $80,000, $50,000, and $5,500 – totaling $135,500 – which were made jointly payable to

[1] The Honorable Kathy A. Surratt-States, Chief Judge, United States Bankruptcy Court for the Eastern District of Missouri.

"Robert Armstrong d/b/a RNA Properties LLC and Southwest Bank, An M&I Bank, ISAOA" (the "Three Checks"). The first two checks, for $80,000 and $50,000, respectively, were dated February 12, 2009, and were deposited into RNA Properties LLC's account at Bank of America on February 13, 2009. The third check, for $5,500, was dated May 26, 2009, and was deposited into RNA Properties' account on June 1, 2009. All three checks were deposited into RNA Properties' account without Southwest's endorsement, despite the fact that Southwest was a co-payee on each of the checks.

The Debtor used less than $5,000 of the funds from the Three Checks to make repairs to a portion of the mall. Instead, the Debtor diverted the majority of the funds to his personal use. Shortly after depositing the funds into the RNA Properties account, the Debtor caused $100,000 of the money to be transferred to his and his wife's personal bank account. The Debtor's wife then wrote two checks dated February 17, 2009 from their personal account – one for $70,000 to pay down their home equity line of credit, and a second check for $30,000 which was deposited into their personal savings account. The Debtor admitted he used the insurance proceeds for personal or other business issues at his sole discretion. Indeed, despite being paid over $900,000 in total insurance proceeds, there was no work started at the mall, except for some cleanup and $4,863.39 in minor repairs to the adjoining building's roof.

Meanwhile, despite being required to do so under the loan documents, the Debtor never informed Southwest of the fire or of any of the insurance checks. Instead, he continued to make the regular payments on the loans to Southwest and pay property taxes. Southwest learned of the fire sometime around August to October 2009, from another source or from a routine inspection of the property. On December 9, 2009, Southwest declared the notes in default and made demand for payment of approximately $1.6 million under the two notes. The Debtor paid Southwest $400,000 from six different personal accounts in response to the demand, but Southwest foreclosed on the mall in February 2010. PSM sued the Debtor, RNA Properties, and Southwest Bank in the District Court of Dallas County, Texas. Bank of America was joined by Southwest as a third-party defendant in relation to the Three Checks. Bank of America filed a cross-claim against the Debtor and RNA Properties. On April 2, 2011, Bank of America and Southwest settled Southwest's claim for negotiating the unendorsed checks. As part of that settlement, Bank of America paid Southwest the $135,500 represented by the Three Checks. The Order of Dismissal of Bank of America expressly preserved any claims by Bank of America against the Debtor and RNA Properties.

The Debtor filed a Chapter 7 bankruptcy case on October 28, 2011, staying the state court litigation. Bank of America filed a proof of claim in the Debtor's bankruptcy case, based on the Three Checks. Bank of America also sought denial of the discharge of the debt pursuant to § 523(a)(2)(A), (a)(4), and (a)(6) of the Bankruptcy Code.

On cross motions for summary judgment, the Bankruptcy Court held in favor of Bank of America, finding that the debt was excepted from the Debtor's discharge under § 523(a)(2)(A) for fraud, as well as embezzlement under § 523(a)(4) of the Code. The Debtor appeals.

STANDARD OF REVIEW

We review the Bankruptcy Court's grant of summary judgment *de novo*.[2] Summary judgment is appropriate if the record shows that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law.[3] The Bankruptcy Court is not to weigh evidence and make credibility

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[2] *Williams v. Marlar* (*In re Marlar*), 252 B.R. 743, 750 (B.A.P. 8th Cir. 2000) (citations omitted).

[3] *Id.* (citations omitted); Fed. R. Civ. P. 56(c), made applicable here by Fed. R. Bankr. P. 7056.

determinations, or to attempt to determine the truth of the matter, but is, rather, solely to determine whether there is a genuine issue of fact for trial.[4] The Court is to view the facts in a light most favorable to the nonmoving party and to give that party the benefit of all reasonable inferences to be drawn from that evidence.[5] "Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial."[6]

Because we conclude that the Bankruptcy Court did not err in finding the debt to be nondischargeable under § 523(a)(4) for embezzlement, we limit our analysis to that basis for nondischargeability. As a result, we do not reach the § 523(a)(2)(A) fraud issue.

DISCUSSION

Section 523(a)(4) of the Bankruptcy Code provides that a discharge under § 727 "does not discharge an individual debtor from any debt . . . for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny."[7] "Embezzlement, for purposes of section 523(a)(4), is the fraudulent appropriation of property of another by a person to whom such property has been entrusted or

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4 *Id.* (citations omitted).

5 *Id.* (citations omitted).

6 *Id.* (quoting *Celotex Corp. v. Catrett*, 477 U.S. 317, 322, 106 S.Ct. 2548, 2552, 91 L.Ed.2d 265 (1986)).

7 11 U.S.C. § 523(a)(4).

into whose hands it has lawfully come."[8] "A plaintiff must establish that the debtor was not lawfully entitled to use the funds for the purposes for which they were in fact used."[9]

"To show embezzlement, the creditor has to prove that it entrusted its property to the debtor, the debtor appropriated the property for a use other than that for which it was entrusted, and the circumstances indicate fraud."[10] Courts often examine whether the terms by which a debtor came into possession of the funds create an obligation on the debtor.[11] "Obligations sufficient to support a claim of embezzlement are ones which make the debtor's discretionary use of the payment, prior to complying with the obligations, improper."[12]

First, the Debtor asserts that the Bankruptcy Court erred in finding that Bank of America proved standing to pursue a claim under § 523(a)(4) because Bank of America did not plead or prove that the Debtor embezzled funds from it, as opposed to Southwest Bank. Rather, the Debtor asserts, his debt to Bank of America is based on breach of the presentment warranty under § 3.417 of the Uniform Commercial Code and the Texas UCC (for depositing the checks without Southwest Bank's endorsement), not embezzlement. He further asserts that Bank

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8 *In re Phillips*, 882 F.2d 302, 304 (8th Cir. 1989) (quoting *In re Belfry*, 862 F.2d 661, 662 (8th Cir.1988)) (internal brackets and quotation marks omitted).

9 *In re Belfry*, 862 F.2d 661, 662 (8th Cir. 1988).

10 *Hamilton v. Green* (*In re Green*), 2012 WL 3028462 at *4 (Bankr. W.D. Mo. 2012) (slip copy) (citation omitted).

11 *In re Belfry*, 862 F.2d at 663.

12 *Id*. (citation omitted).

of America could not pursue this cause of action on behalf of Southwest Bank because there were no contractual subrogation rights between the two banks.

To the contrary, however, the Debtor expressly stipulated that Bank of America was subrogated to Southwest's claims against him.[13] Since Bank of America is subrogated to Southwest, and stands in the shoes of Southwest,[14] this cause of action for embezzlement is not based on a breach of the presentment warranty to Bank of America; rather, it is based on the Debtor's use of funds in which Southwest Bank claimed an interest. Bank of America does, therefore, have standing to pursue the embezzlement claim.

Next, pointing out that "[o]ne cannot embezzle one's own property,"[15] the Debtor asserts that the Court erred when it found he had no ownership interest in the insurance proceeds and that he had, therefore, fraudulently appropriated the funds of another. Further, the Debtor asserts, a borrower cannot embezzle funds which are proceeds of a creditor's collateral, because the borrower retains an ownership interest in the collateral subject to the creditor's security interest.[16] The Debtor asserts that he owned the mall property, and thus the insurance proceeds, which were merely pledged as collateral for the loan by Southwest Bank.

13

See, e.g., Stipulation of Certain Undisputed Facts Between Bank of America, N.A. and Robert N. Armstrong at ¶¶ 30 and 48, Adversary No. 12-4045 (Bankr. E.D. Mo. Jan. 10, 2013), ECF No. 41.

14

The term "subrogate" means "[t]o substitute (a person) for another regarding a legal right or claim." Black's Law Dictionary (9th ed. 2009).

15

In re Belfry, 862 F.2d at 662.

16

See In re Phillips, 882 F.2d at 304.

The Bankruptcy Court held that Southwest Bank was the owner of the insurance proceeds because (i) the Deed of Trust specifically stated that Southwest Bank was to be the loss payee of any insurance policy concerning the mall; (ii) RNA Properties, "by way of Debtor," was required to immediately inform Southwest Bank of any insurance claim; (iii) the Deed of Trust called for all insurance proceeds to be paid directly to Southwest Bank rather than to Southwest Bank and RNA Properties jointly; (iv) the Deed of Trust stated that Southwest Bank had the power to endorse any check that was jointly payable to Debtor and Southwest Bank; and, "most importantly," (v) the Deed of Trust stated that, "[Southwest] Bank shall have the right, as its sole option, to apply all such monies as shall be thus collected and received [from insurance proceeds]... toward the payment of the Secured Indebtedness of the cost of rebuilding or restoring the damaged property ... or to apply all or any part of such monies against any part of the Secured Indebtedness, without regard to the maturity thereof, and in any order as Bank shall elect."

Based on this language in the Deed of Trust, the Bankruptcy Court held that neither the Debtor nor RNA Properties had any ownership interest in the insurance proceeds, particularly the Three Checks. Rather, the Court held, Southwest Bank held more than a mere security interest in the proceeds – it owned them.

In so holding, the Bankruptcy Court acknowledged, but distinguished, the contrary conclusion reached by the Eighth Circuit in *In re Phillips*.[17] In that case, the debtors were officers and shareholders of Midwest Poultry Equipment, Inc. Midwest granted First National Bank of Fayetteville (FNB) a security interest in proceeds owed to the company under a lease. Although Midwest had instructed the funding bank to make the check for the lease payable jointly to Midwest and FNB, the bank made the check payable only to Midwest. Midwest deposited the check directly into its general funding account. After the debtors (who were Midwest's officers and directors), learned of the mistake, they did nothing to

[17] 882 F.2d 302 (8th Cir. 1989).

correct the problem and did not notify FNB of it. When the debtors filed bankruptcy, FNB alleged that the debtors had embezzled the funds. Notably, although some of the funds were used to pay corporate debts which the officers (debtors) had guaranteed, the debtors did not themselves walk off with the funds; instead, they kept the funds for their corporation without paying them over to the bank. The Eighth Circuit held that, despite certain "assignment" language in the loan documents, Midwest owned the funds subject only to FNB's security interest.

Crucially, what no one has fully appreciated in our case thus far is the distinction between the Debtor and RNA Properties LLC as separate entities. The Eighth Circuit did not acknowledge the distinction in *Phillips*, either, apparently because it had concluded that FNB, as the holder of a security interest, had no ownership interest in the money to the exclusion of the owner/borrower (Midwest), under the loan documents there.

Here, regardless of whether *RNA Properties* had an ownership interest in the insurance proceeds to the exclusion of Southwest (as was the case in *Phillips*), there is nothing in the record at all suggesting that *the Debtor* had any ownership interest in mall property or the insurance proceeds.[18] The Debtor's repeated unsupported statements in pleadings that he owned the property are perplexing.

We held in *In re Potts* that there could be "no doubt" that a contractual co-payee of a check has an interest in the funds represented by the check.[19] Similarly

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18

For instance, the Deed of Trust identifies the "Borrower" as "RNA Properties LLC A/K/A RNA Properties, L.L.C." and warrants that "Borrower is lawfully seized of indefeasible title and estate to the Mortgaged Property. . . ." The Debtor signed the Deed of Trust on behalf of RNA Properties, but he is not a party to it.

19

469 B.R. 310, 313 (B.A.P. 8th Cir. 2012). *See also Option One Mortgage Corp. v. Fitzgerald*, 687 F.Supp.2d 520, 525 (M.D. Pa. 2009) (holding that, where

here, there can be no doubt that, under the terms of the Deed of Trust and as co-payee of the Three Checks, Southwest had an interest in the funds represented by the Three Checks. Consequently, since the Debtor had no ownership interest in the insurance proceeds, he either took money which was owned outright by Southwest (as the Bankruptcy Court held), or he took money that was owned by RNA Properties, subject to a lien in favor of Southwest Bank. Either way, in contrast to *Phillips* – where the debtors themselves were not alleged to have taken the money – the Debtor here did misappropriate "property of another."

The gloss over the distinction between the Debtor and RNA Properties is also relevant on the question of whether the Debtor initially came into possession of the funds lawfully, one of the elements of embezzlement. As stated, the Three Checks were made payable to Robert Armstrong d/b/a RNA Properties and Southwest Bank.[20] This is likely because, for some reason, the insurance policy itself appears to have been issued to Robert Armstrong d/b/a RNA Properties LLC,[21] even though the Debtor had no ownership interest in the mall property. Because the Debtor had no ownership interest in the mall property, neither the insurance policy nor any of the checks from it should have been issued to the

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the plaintiff was a named co-payee on a check, and the mortgage agreement provided that the defendants were obligated to turn the check over to the plaintiff, the plaintiff's right in an insurance check vested at the time it was issued, and the defendants had no rights in the check without plaintiff's endorsement).

20

Similarly, all of the other insurance checks were made payable to Robert Armstrong d/b/a RNA Properties LLC.

21

See Affidavit of Jeffrey T. Bannon in Support of Public Service Mutual Insurance Company's Application for Temporary Restraining Order and Temporary Injunction at ¶ 2, attached as *Exhibit A* to *Affidavit of Rupert Baron*, Adversary No. 12-4045 (Bankr. E.D. Mo. Nov. 21, 2012), ECF No. 27-4; and *Exhibit B* to *Defendant's Reply to Bank of America's Response to Motion for Summary Judgment*, Adversary No. 12-4045 (Bankr. E.D. Mo. Nov. 27, 2012) ECF No. 31.

Debtor. Nevertheless, because the checks were issued to the Debtor, we conclude that he came into possession of the funds lawfully. But even if that were not the case, the only difference between a nondischargeable debt for embezzlement and a nondischargeable debt for larceny under § 523(a)(4) is whether the initial possession of the property was lawful.[22] While we conclude that the Debtor's initial possession of the Three Checks was lawful, if it was not, his taking of the money was larceny. Either way, the debt is nondischargeable under § 523(a)(4).

The Debtor next asserts that the Bankruptcy Court erred in finding fraudulent intent. While the Bankruptcy Court's findings on this element of § 523(a)(4) were scant, the undisputed facts amply support a finding of intent.

A debtor's fraudulent intent for purposes of § 523(a)(4) may be, and often must be, shown by circumstantial evidence.[23] Here, the undisputed and indisputable facts include the following circumstantial evidence of the Debtor's fraudulent intent: (i) the Debtor failed to disclose the fire to Southwest, despite the obvious requirement in the loan documents that he do so; (ii) the Debtor failed to disclose to Southwest that he had made an insurance claim or that he had received over $900,000 in insurance proceeds, despite the requirement in the loan documents that he do so, and despite the fact that the loan documents required payment of any insurance proceeds be made to Southwest Bank to be applied at its sole discretion; (iii) the Debtor deposited the checks without Southwest's

[22] *Treadwell v. Glenstone Lodge, Inc.* (*In re Treadwell*), 459 B.R. 394, 406 (Bankr. W.D. Mo. 2011) (quoting 4 Collier on Bankruptcy ¶ 523.10[2] (15th ed. Rev.) ("In short, section 523(a)(4) excepts from discharge debts resulting from the fraudulent appropriation of another's property, whether the appropriation was unlawful at the outset, and therefore a larceny, or whether the appropriation took place unlawfully after the property was entrusted to the debtor's care, and therefore was an embezzlement.").

[23] *See Kruse v. Murray* (*In re Murray*), 408 B.R. 268, 275 (Bankr. W.D. Mo. 2009).

endorsement or approval, despite the fact that the loan documents required Southwest's approval, Southwest's endorsement was clearly required on the checks as they were made jointly payable, and despite the fact that the deposit without the endorsement was in contravention of Texas law; (iv) the Debtor immediately diverted the money from RNA Properties' bank account and used the money for personal and other business purposes at his sole discretion, despite the fact that the loan documents authorized only Southwest Bank to apply the proceeds at its own discretion; and (v) RNA Properties, which was controlled by the Debtor, made almost no repairs to mall.

We recognize that fraudulent intent is ordinarily a question to be determined by the fact-finder and is difficult to demonstrate on a motion for summary judgment.[24] However, when the "unmistakable picture painted by . . . stipulation" establishes fraudulent intent, summary judgment is appropriate.[25]

Based on the foregoing undisputed circumstantial evidence, Bank of America met its initial burden of showing no genuine issue of material fact that the Debtor took the money with fraudulent intent. That being the case, the Debtor was required to "advance specific facts to create a genuine issue of material fact for trial."[26] While the Debtor generally asserted in responses to discovery and in

[24] *See Jackson v. Star Sprinkler Corp. of Florida*, 575 F.2d 1223, 1231 (8th Cir. 1978). *See also Thoms v. Vucurevich* (*In re Vucurevich*), 2013 WL 662688 (Bankr. D. S.D. Feb. 25, 2013) ("Where motive and intent are at issue, disposition of the matter by summary judgment may be more difficult.").

[25] *Id*. at 1234 (finding that the stipulated facts in that case left no material issue of fact remaining and that those facts established as a matter of law that the transfer at issue was made with intent to hinder, delay, and defraud creditors).

[26] *F.D.I.C. v. Bell*, 106 F.3d 258, 263 (8th Cir. 1997) ("Mere arguments or allegations are insufficient to defeat a properly supported motion for summary judgment; a 'nonmovant must present more than a scintilla of evidence and must

pleadings that he was not aware of any of loan documents' requirements to notify Southwest of anything, or of his obligation to obtain Southwest's endorsement on checks which were made payable to Southwest, and that he had done so in the past, he pointed to no "specific facts" to support those claims.[27] Moreover, that assertion in light of the facts defies common sense.

In sum, the in order to prevail under § 523(a)(4), "[a] plaintiff must establish that the debtor was not lawfully entitled to use the funds for the purposes for which they were in fact used."[28] Southwest Bank established that the Debtor was not lawfully entitled to use the insurance proceeds for the purposes for which he used them and the Debtor has produced nothing to the contrary.

ACCORDINGLY, the Order of the Bankruptcy Court finding the Debtor's debt to Bank of America, as subrogee to Southwest Bank, to be nondischargeable under 11 U.S.C. § 523(a)(4) is AFFIRMED.

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advance specific facts to create a genuine issue of material fact for trial.") (citation omitted).

27

The Debtor's attempt to offer evidence of specific instances of consistent conduct in the past for the first time on appeal is not appropriate. *McCleary v. ReliaStar Life Ins. Co.*, 682 F.3d 1116, 1120 (8th Cir. 2012) ("Our review of the evidence includes only the record that was before the [Bankruptcy Court] when it ruled on the summary judgment motion.").

28

In re Belfry, 862 F.2d at 662.

H
Only the Westlaw citation is currently available.

United States Court of Appeals,
Eleventh Circuit.
Camille **HOPE**, Trustee for Rickey Fluellen, Plaintiff–Appellant,
v.
ACORN FINANCIAL, INC., Defendant–Appellee.

No. 12–10709.
Sept. 26, 2013.

Background: Chapter 13 trustee brought adversary proceeding against creditor, seeking to avoid as preferential transfer perfection of creditor's security interest in debtor's vehicle. The Bankruptcy Court, No. 10–52284 JPS,James P. Smith, J., granted summary judgment in favor of creditor, 446 B.R. 612, and the United States District Court for the Middle District of Georgia, No. 5:11–CV–276 MTT,Marc T. Treadwell, J., affirmed, 2012 WL 74874. Trustee appealed.

Holdings: The Court of Appeals, Jordan, Circuit Judge, held that:
(1) trustee's post-confirmation adversary proceeding against creditor was precluded, and
(2) bankruptcy court's confirmation of plan in which creditor was given a secured position can bind trustee who was aware of defect, failed to object, and affirmatively recommended confirmation.

Affirmed.

West Headnotes

[1] Bankruptcy 51 3779

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3779 k. Scope of Review in General. Most Cited Cases

Bankruptcy 51 3782

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3782 k. Conclusions of Law; De Novo Review. Most Cited Cases

On an appeal of a bankruptcy court's judgment, Court of Appeals acts as the second court of review, and exercises plenary review of any determinations of law, whether made by the bankruptcy court or by the district court.

[2] Bankruptcy 51 2704

51 Bankruptcy
51V The Estate
51V(H) Avoidance Rights
51V(H)1 In General
51k2704 k. Trustee as Representative of Debtor or Creditors. Most Cited Cases

Bankruptcy 51 3009

51 Bankruptcy
51VIII Trustees
51k3008 Powers, Duties and Fiduciary Capacity
51k3009 k. Representation of Debtor, Estate, or Creditors. Most Cited Cases

Bankruptcy 51 3715(11)

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51 Bankruptcy
51XVIII Individual Debt Adjustment
51k3704 Plan
51k3715 Acceptance and Confirmation
51k3715(9) Effect
51k3715(11) k. Property of Estate. Most Cited Cases

The Chapter 13 trustee acts in a representative capacity when she seeks post-confirmation avoidance; the bankruptcy court's confirmation of the proposed plan generally vests the property of the estate in the debtor, and the primary purpose of the Chapter 13 trustee is to serve the interests of all creditors. 11 U.S.C.A. § 1327(b).

[3] Bankruptcy 51 3009

51 Bankruptcy
51VIII Trustees
51k3008 Powers, Duties and Fiduciary Capacity
51k3009 k. Representation of Debtor, Estate, or Creditors. Most Cited Cases

Bankruptcy 51 3715(6)

51 Bankruptcy
51XVIII Individual Debt Adjustment
51k3704 Plan
51k3715 Acceptance and Confirmation
51k3715(6) k. Objections; Sua Sponte Determinations. Most Cited Cases

Bankruptcy Code provisions pertaining to Chapter 13 trustee's duties to object to allowance of improper claims and to appear at confirmation hearing, taken together, generally require a Chapter 13 trustee to object to the confirmation of a plan if a claim is invalid or improperly characterized. 11 U.S.C.A. §§ 704(a)(5), 1302(b)(1), (b)(2)(B).

[4] Bankruptcy 51 2586.1

51 Bankruptcy
51V The Estate
51V(D) Liens and Transfers; Avoidability
51k2586 Knowledge of or Notice to Trustee, Debtor, or Creditor
51k2586.1 k. In General. Most Cited Cases

Bankruptcy 51 3715(10)

51 Bankruptcy
51XVIII Individual Debt Adjustment
51k3704 Plan
51k3715 Acceptance and Confirmation
51k3715(9) Effect
51k3715(10) k. Conclusiveness; Res Judicata; Collateral Estoppel. Most Cited Cases

Chapter 13 plan trustee's post-confirmation adversary proceeding to avoid, as preferential, postpetition perfection of creditor's security interest in debtor's vehicle, was precluded, where trustee knew about defect in perfection of security interest 30 days before confirmation hearing, and knew that plan treated creditor's claim as secured, but did not object to plan's classification of claim, and affirmatively recommended to the bankruptcy court that it confirm the proposed plan. 11 U.S.C.A. §§ 546(a)(1)(A), 547, 1327(a).

[5] Bankruptcy 51 2922

51 Bankruptcy
51VII Claims
51VII(E) Determination
51k2922 k. Summary Allowance; Necessity for Objection. Most Cited Cases

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Bankruptcy 51 2928

51 Bankruptcy
51VII Claims
51VII(E) Determination
51k2925 Evidence
51k2928 k. Effect of Proof of Claim. Most Cited Cases

A secured creditor under Chapter 13 who files a claim has a correct and lawful expectation that the validity and amount of its claim, absent objection, is proven and binding upon the debtor, the trustee, and other creditors. 11 U.S.C.A. § 1327(a).

[6] Bankruptcy 51 2586.1

51 Bankruptcy
51V The Estate
51V(D) Liens and Transfers; Avoidability
51k2586 Knowledge of or Notice to Trustee, Debtor, or Creditor
51k2586.1 k. In General. Most Cited Cases

Bankruptcy 51 3715(10)

51 Bankruptcy
51XVIII Individual Debt Adjustment
51k3704 Plan
51k3715 Acceptance and Confirmation
51k3715(9) Effect
51k3715(10) k. Conclusiveness; Res Judicata; Collateral Estoppel. Most Cited Cases

Where a Chapter 13 trustee is aware of defects in a creditor's security interest well before confirmation, chooses not to object to the creditor's claim, and affirmatively recommends to the bankruptcy court that it confirm a proposed plan in which the creditor is given a secured position, the bankruptcy court's confirmation of the plan binds the trustee and precludes a post-confirmation avoidance action against the creditor. 11 U.S.C.A. § 1327(a).

Camille Hope, Macon, GA, pro se.

Jenny Martin Stansfield, Martin & Snow, LLP, Macon, GA, for Defendant–Appellee.

Appeal from the United States District Court for the Middle District of Georgia. D.C. Docket No. 5:11–cv–00276–MTT, Bkcy No. 5:10–05108.

Before BARKETT and JORDAN, Circuit Judges, and SCHLESINGER,[FN*] District Judge.

JORDAN, Circuit Judge:

***1** A Chapter 13 bankruptcy proceeding involves a number of participants. The debtor sets events in motion by filing a petition for relief and submitting a proposed bankruptcy plan, which serves as a road map for the things to come; the creditors try to preserve as much of their interests as possible; and the trustee "oversees the administration of the debtor's assets." *Litton v. Wachovia Bank (In re Litton),* 330 F.3d 636, 640 (4th Cir.2003). "Upon satisfaction of the plan and completion of the plan's terms, the debtor is discharged of his or her debts and, in theory, faces a future of solvency." *Universal Mortgage Co. v. Bateman (In re Bateman),* 331 F.3d 821, 826 (11th Cir.2003).

Under 11 U.S.C. § 1327(a) ("Effect of Confirmation"), the "provisions of a confirmed [Chapter 13] plan bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted, or has rejected the plan." As the quoted text indicates, however, § 1327(a) makes no mention of the trustee. It is that word left unwritten which has led to the dispute in this case.

We are called upon to decide whether a confirmed Chapter 13 plan which gives a creditor a secured position is binding on a trustee who, aware of defects in that creditor's security interest, does not assert any objections to, and affirmatively recommends confirmation of, the plan. We hold that, notwithstanding her omission from the language of § 1327(a), under such circumstances a Chapter 13 trustee is bound by a confirmed plan and may not pursue a post-confirmation avoidance action against the creditor.

I

In June of 2010, Ricky Fluellen purchased a car from TCL Auto Sales. Mr. Fluellen financed the purchase through Acorn Financial, Inc., which obtained a security interest in the vehicle. Shortly thereafter, Mr. Fluellen found himself financially insolvent, and on July 21, 2010, he filed for bankruptcy relief under Chapter 13. Acorn did not perfect its security interest in the vehicle until July 27, 2010, when it delivered an application for a certificate of title to the Commissioner of the Georgia Department of Revenue.

As part of Mr. Fluellen's bankruptcy proceeding, Acorn filed a proof of claim on August 12, 2010. Someone in the office of the Chapter 13 trustee, Camille Hope, then contacted the office of the local county tax commissioner to find out whether Acorn had a perfected lien on Mr. Fluellen's vehicle. On August 24, 2010, the tax commissioner responded that, according to his office's records, Acorn's security interest was not perfected until July 27, 2010, six days after Mr. Fluellen filed his bankruptcy petition. The bankruptcy court therefore found that Ms. Hope "knew about the defects in Acorn's security interest 30 days prior to the confirmation hearing." *See* Bankruptcy Court's Memorandum Opinion [D.E. 55] at 12. Ms. Hope, despite this knowledge, did not take any further immediate action concerning Acorn's claim.

***2** In the meantime, Mr. Fluellen had submitted a proposed bankruptcy plan. The plan provided, in relevant part, for "payments to secured creditors, whose claims are duly proven and allowed[,]" and treated Acorn as a secured creditor entitled to monthly payments of $146. In her report to the bankruptcy court, Ms. Hope "recommend[ed] that [the] plan be confirmed" because it complied with the requirements of 11 U.S.C. § 1325. The bankruptcy court, noting Ms. Hope's recommendation, confirmed the proposed plan on September 30, 2010, thereby "vest[ing] all of the property of the estate in [Mr. Fluellen]." 11 U.S.C. § 1327(b).

On October 8, 2010, a week or so following confirmation of the plan, Ms. Hope filed an adversary proceeding against Acorn, seeking to avoid its lien as a preferential transfer, *see* 11 U.S.C. § 547, and designate its claim as unsecured debt. Acorn moved for summary judgment, arguing that Ms. Hope was bound by the terms of the confirmed Chapter 13 plan and that, as a result, her complaint was barred by *res judicata* (i.e., claim preclusion). The bankruptcy court granted summary judgment in favor of Acorn, and the district court affirmed. *See Hope v. Acorn Financial, Inc.*, 2012 WL 74874 (M.D.Ga. January 10, 2012). Ms. Hope now appeals. With the benefit of oral argument, we too affirm.

II

[1] On an appeal of a bankruptcy court's judgment, we act as "the second court of review." *Barrett Dodge Chrysler Plymouth, Inc. v. Cranshaw (In re Issac LeaseCo, Inc.*), 389 F.3d 1205, 1209 (11th Cir.2004). We exercise plenary review of any "determinations of law, whether made by the bankruptcy court or by the district court." *Williams v. EMC Mortgage Corp. (In re Williams*), 216 F.3d 1295, 1296 (11th Cir.2000).

A

Ms. Hope argues that, because § 1327(a) does not specifically say that trustees are also bound by a confirmed Chapter 13 plan, they are not so bound and can pursue post-confirmation avoidance actions within the two-year limitations period set forth in 11

U.S.C. § 546(a)(1)(A). She points out that several other provisions of Chapter 13 specifically mention trustees, [FN1] and reasons that the exclusion of trustees from § 1327(a) was not a mere legislative oversight. *See Russello v. United States,* 464 U.S. 16, 23, 104 S.Ct. 296, 78 L.Ed.2d 17 (1983) ("[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.") (internal quotation marks and citation omitted). She also notes our previous refusal, in the bankruptcy context, to add (or read in) missing statutory language. *See Myers v. Toojay's Management Corp.,* 640 F.3d 1278, 1284–86 (11th Cir.2011) (explaining, in part, that we are not "licensed to practice statutory remodeling").

This is a close case, and Ms. Hope's statutory argument is simple and straightforward. But, for a number of reasons, it does not carry the day.

B

***3** Choosing the most appropriate canon of construction in a given circumstance is usually a matter of contextual judgment, for statutory interpretation "is a holistic endeavor." *United Savings Ass'n of Texas v. Timbers of Inwood Forest Ass., Ltd.,* 484 U.S. 365, 371, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988). The *Russello* presumption on which Ms. Hope relies is only a presumption, and a rebuttable one at that. *See Springer v. Gov't of Philippine Islands,* 277 U.S. 189, 206, 48 S.Ct. 480, 72 L.Ed. 845 (1928) ("The general rule that the expression of one thing is the exclusion of others is subject to exceptions. Like other canons of statutory construction, it is only an aid in the ascertainment of the meaning of the law, and must yield whenever a contrary intention on the part of the lawmaker is apparent."). Indeed, the Supreme Court, in a case involving an interstate compact among several states, recently declined to apply the presumption because it "fail[ed] to account for other sections of the compact that cut against its reading" and "produce[d] ... anomalous results." *Tarrant Regional Water District v. Herrmann,* ––– U.S. ––––, 133 S.Ct. 2120, 2131–32, 186 L.Ed.2d 153 (2013) ("At the very least, the problems that arise from Tarrant's proposed reading [under *Russello*] suggest that § 5.05(b)(1)'s silence is ambiguous regarding cross-border rights under the compact."). *See also Pugliese v. Pukka Dev., Inc.,* 550 F.3d 1299, 1304 (11th Cir.2008) (finding *Russello* presumption inapplicable).

Here, as in *Herrmann,* the *Russello* presumption does not quite work. As a statutory matter, § 1327(a) cannot be read in isolation, and other provisions of Chapter 13 strongly suggest that a confirmed plan is binding for at least some purposes on the trustee. For example, § § 1326(a)(2) and (c) require the trustee to make certain distributions as required by the confirmed plan, and one would think that no duty to distribute can or would arise unless such a plan was binding on the trustee. In addition, § 1329(a) provides that, after confirmation, the plan may be modified in certain ways "upon request of the debtor, the trustee, or the holder of an allowed unsecured claim," while § 1330(a) permits any "party in interest" (which a Chapter 13 trustee certainly is) to request revocation of a plan for fraud within 180 days of confirmation. These provisions would be "unnecessary if the confirmed plan did not already bind the trustee as it does the debtor." *Bankowski v. Wells Fargo Bank, N.A. (In re Reid),* 480 B.R. 436, 445 (Bankr.D.Mass.2012).

[2] The trustee, moreover, acts in a representative capacity when she seeks post-confirmation avoidance. The bankruptcy court's confirmation of the proposed plan generally vests the property of the estate in the debtor, *see* § 1327(b), and the "primary purpose of the Chapter 13 trustee is ... to serve the interests of all creditors." *Overbaugh v. Household Bank, N.A. (In re Overbaugh),* 559 F.3d 125, 129–30 (2d Cir.2009). So, whether the trustee is (generally speaking) trying to benefit the debtor or certain credi-

tors through an avoidance action, she is not acting for her own account.

C

***4** Significantly, the bankruptcy terrain we traverse is not pristine. In *Wallis v. Justice Oaks II, Ltd. (In re Justice Oaks II, Ltd.),* 898 F.2d 1544, 1553 (11th Cir.1990), a Chapter 11 case, we held that certain creditors could not mount a post-confirmation challenge to the claim of another creditor because they had "waived their right to object by failing to object prior to confirmation of the plan." We found "compelling" the rationale of the Fifth Circuit in *Simmons v. Savell (In re Simmons),* 765 F.2d 547, 553 (5th Cir.1985), a Chapter 13 case, which we summarized as follows: "[W]hen the objection is based on an argument that the plan misclassified the objectionable claim, the objection must be made prior to confirmation of the plan[,]" and the right to object is lost "when the bankruptcy court confirm[s] the plan." *Justice Oaks II,* 898 F.2d at 1553.[FN2]

Justice Oaks II did not involve a post-confirmation challenge by the trustee, and neither did *Simmons.* Nevertheless, both cases hold that the ability to object to a claim generally evaporates upon the bankruptcy court's confirmation of the plan. And we have since applied the holding of *Justice Oaks II* in the Chapter 13 context, ruling that "a secured creditor cannot collaterally attack a confirmed Chapter 13 plan, even though the plan conflicted with the mandatory provisions of the [B]ankruptcy [C]ode, when the secured creditor failed to object to the plan's confirmation or appeal the confirmation order." *Bateman,* 331 F.3d at 822. *See also id.* at 827 ("Universal timely filed a proof of claim before the Plan's confirmation. Accordingly, unless Bateman [the debtor], or any other party in interest objected to the proof of claim, it is 'deemed allowed' and is 'prima facie evidence of the validity and amount' of [the debt]."). Relying on *Justice Oaks II* and *Simmons,* we explained in *Bateman* that a confirmed Chapter 13 plan has *res judicata* effect, even if the plan does not, by its terms, comply with the Bankruptcy Code: "Confirmation of a Chapter 13 plan by a bankruptcy court of competent jurisdiction, in accordance with the procedural requirements of notice and hearing of confirmation, 'is given the same effect as any district court's final judgment on the merits.' " *Id.* at 829–30 (quoting *Justice Oaks II,* 898 F.2d at 1550).

[3] *Justice Oaks II* and *Bateman,* we think, are relevant to the issue we confront today. Pursuant to 11 U.S.C. § 1302(b)(1), one of the duties of a Chapter 13 trustee is to "examine proofs of claims and object to the allowance of any claim that is improper." 11 U.S.C. § 704(a)(5). And the Bankruptcy Code provides that a Chapter 13 trustee "shall," among other things, "appear and be heard at a hearing that concerns ... confirmation of a plan." 11 U.S.C. § 1302(b)(2)(B). These provisions, taken together, generally require a Chapter 13 trustee to object to the confirmation of a plan if a claim is invalid or improperly characterized.

***5** [4][5] The principles articulated in *Justice Oaks II* and *Bateman* carry even more weight given what happened here. First, as the bankruptcy court found, and as Ms. Hope later conceded, her office had all the information she needed to challenge Acorn's claim as an avoidable lien well prior to confirmation. *See* Transcript of Hearing on Motion to Reconsider [D.E. 99] at 12–13. Second, Ms. Hope did not merely forego her opportunity to file a timely objection to Acorn's claim; she affirmatively recommended to the bankruptcy court that Mr. Fluellen's proposed plan—which listed Acorn as a secured creditor—be confirmed. We agree with the Second Circuit that, on these facts, the bankruptcy court correctly precluded Ms. Hope from filing a post-confirmation avoidance action against Acorn. *See Celli v. First Nat. Bank of Northern New York (In re Layo),* 460 F.3d 289, 295–96 (2d Cir.2006). If a trustee, like a debtor or creditor, is obliged to make a timely objection to the confirmation of a plan, and foregoes an objection she is aware of, it is difficult to

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see why the trustee, like a debtor or creditor, would not also be bound by confirmation. "A secured creditor [like Acorn] who files a claim has a correct and lawful expectation that the validity and amount of its ... claim, absent objection, is proven and binding upon the debtor, the trustee, and other creditors." *In re Hudson,* 260 B.R. 421, 431 (Bankr.W.D.Mich.2001).

D

We have tried, given our existing precedent, to make the best of bankruptcy provisions which do not mesh very well together, but we know that our ruling is not ideal. We recognize, as did the bankruptcy court, that in certain routine Chapter 13 cases the confirmation of proposed plans will take place before the bar dates for proofs of claims and avoidance actions. We also acknowledge that not all scheduled creditors file proofs of claims, thereby creating administrative nightmares for busy trustees. Our holding, therefore, is a narrow one, necessarily limited by the facts before us: a Chapter 13 trustee who is aware, prior to confirmation, about the defects in a creditor's security interest and who, despite that knowledge, does not object to the creditor's claim and affirmatively recommends confirmation of a proposed plan in which the creditor is given a secured position. We need not, and do not, address a scenario where the trustee is unaware of the defects in the creditor's security interest until after confirmation. *Cf. Hope v. First Family Fin. Serv. of Georgia, Inc. (In re Harrison),* 259 B.R. 794, 797–98 (Bankr.M.D.Ga.2000) (addressing a similar set of facts).

We pause to add that Ms. Hope's reading of § 1327(a) is also not perfect and, if adopted, would create problems of its own. As one bankruptcy court has persuasively explained:

> [T]he confirmation of a[C]hapter 13 plan is a collective and omnibus proceeding, one that attempts, as much as possible, to address the obligations of a debtor to all his or her creditors, and the priority among those creditors, at once. It would be unusual and unworkable for the order that confirms such a plan to bind the debtor and the creditors but not also the trustee. If the plan is not final as to all, it is not final as to any. Where the confirmation of a plan fixes a matrix of interdependent rights, it is often difficult to alter one part without affecting many others. In this kind of proceeding, finality is not finality unless it applies to all. Especially where the trustee's role after confirmation is to collect payments from the debtor and distribute those payments to creditors, it is difficult to imagine how the plan can be final if it is not binding on her.

***6** *Bankowski,* 480 B.R. at 445. *See also In re Smith,* 2004 WL 41401, at *2 (Bankr.W.D.Mo. January 6, 2004) ("A failure to timely object to a claimed exemption prevents a [Chapter 13] trustee from later challenging that exemption—even if the debtor does not have a good faith or reasonably disputable basis for claiming it.").

Finally, we note that virtually all of the federal courts to have passed on (or opined on) on this issue—bankruptcy, district, and circuit—have (albeit with somewhat different rationales) come to the same conclusion: that a confirmed Chapter 13 plan binds the trustee in circumstances like those here and does not allow her to mount post-confirmation challenges. *See, e.g., Celli,* 460 F.3d at 295–96; *Bankowski,* 480 B.R. at 444–46; *Evabank v. Baxter,* 278 B.R. 867, 887 (N.D.Ala.2002); *In re Euler,* 251 B.R. 740, 746 (Bankr.M.D.Fla.2000); *Ledford v. Brown (In re Brown),* 219 B.R. 191, 194 (6th Cir. BAP 1998). The leading treatises are also in accord. *See* 8 COLLIER ON BANKRUPTCY ¶ 1327.02[1] (16th ed.2013); 7 NORTON BANKR.L. & PRAC. 3d § 151:25 (2013). This weight of authority is not, of course, dispositive, but it does give us some comfort.[FN3]

III

[6] Where, as here, the Chapter 13 trustee is aware of defects in a creditor's security interest well

before confirmation, chooses not to object to the creditor's claim, and affirmatively recommends to the bankruptcy court that it confirm a proposed plan in which the creditor is given a secured position, the bankruptcy court's confirmation of the plan binds the trustee and precludes a post-confirmation avoidance action against the creditor. The decisions of the bankruptcy court and the district court are affirmed.

AFFIRMED.

FN* Honorable Harvey E. Schlesinger, United States District Judge for the Middle District of Florida, sitting by designation.

FN1. *See, e.g.,* 11 U.S.C. §§ 1329(a) (permitting plan modification "upon request of the debtor, the trustee, or the holder of an allowed unsecured claim"), and 1325(b)(1) (listing trustee as a party who can object to the confirmation of the plan). When originally enacted, §§ 1325(b)(1), 1327(a), and 1329(a) did not mention the trustee. *See* Pub.L. No. 95–598, §§ 1325, 1327, 1329, 92 Stat. 2649–51 (1978). Congress added the trustee to §§ 1329(a) and 1325(b)(1) when it amended those provisions in 1984, but never amended § 1327(a) in the same way. *See* Pub.L. No. 98–353, Title III, §§ 317, 319, 98 Stat. 356–57, 389 (1984).

FN2. Under the Bankruptcy Code, "[a] claim ... is deemed allowed, unless a party in interest ... objects." 11 U.S.C. § 502(a). Although Bankruptcy Rule 3007 sets forth the procedure for filing an objection to a claim, it is silent as to the time limits for the filing of such an objection. The Fifth Circuit in *Simmons,* however, found such a deadline implicit in the Code, holding that under § 502(a) "a proof of secured claim must be acted upon—that is, allowed or disallowed—before confirmation of the plan or the claim must be deemed allowed for purposes of the plan." *Simmons,* 765 F.2d at 553.

FN3. As an aside, the parallel provision to § 1327(a) in Chapter 12 of the Bankruptcy Code, 11 U.S.C. § 1227(a), also does not list the trustee as one of the persons or entities bound by confirmation of the plan. Nevertheless, courts have held that, under principles of *res judicata,* confirmation is binding on the Chapter 12 trustee. *See* *In re Ted Wiest & Sons, Inc.,* 446 B.R. 441, 445–46 (Bankr.D.Mont.2011); *In re Ogle,* 261 B.R. 22, 26 (Bankr.D.Idaho 2001); *In re Roesner,* 153 B.R. 328, 336 (Bankr.D.Kan.1993).

C.A.11 (Ga.),2013.
Hope v. Acorn Financial, Inc.
--- F.3d ----, 2013 WL 5366291 (C.A.11 (Ga.)), 24 Fla. L. Weekly Fed. C 680

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

CARPENTERS PENSION TRUST FUND FOR NORTHERN CALIFORNIA, *Appellant*, v. MICHAEL GORDON MOXLEY, AKA MGM's Cabinet Installation Services, *Appellee*.	No. 11-16133 D.C. No. 3:10-cv-00756-RS OPINION

Appeal from the United States District Court
for the Northern District of California
Richard Seeborg, District Judge, Presiding

Argued and Submitted
June 13, 2013—San Francisco, California

Filed August 20, 2013

Before: Mary M. Schroeder and Consuelo M. Callahan, Circuit Judges, and Sarah S. Vance, Chief District Judge.*

Opinion by Judge Schroeder

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* The Honorable Sarah S. Vance, Chief United States District Judge for the Eastern District of Louisiana, sitting by designation.

SUMMARY[**]

Bankruptcy

The panel affirmed the district court's order affirming the judgment of the bankruptcy court in an adversary proceeding regarding the dischargeability in bankruptcy of a construction industry contractor's "withdrawal liability" to a pension fund following the expiration of the collective bargaining agreement under which the fund was administered.

Distinguishing *Stern v. Marshall*, 131 S. Ct. 2594 (2011), the panel held that the bankruptcy court had jurisdiction to adjudicate the dischargeability of the pension fund's claim against the contractor because a dischargeability determination is central to federal bankruptcy proceedings and therefore constitutes a public rights dispute that a bankruptcy court may decide.

The contractor was subject to withdrawal liability under the Employee Retirement Income Security Act because he continued doing work covered by the collective bargaining agreement after it expired. The panel held that this debt was dischargeable because it did not qualify as a debt created via defalcation by a fiduciary under 11 U.S.C. § 523(a)(4). The panel concluded that the contractor was not a fiduciary of the fund pursuant to ERISA because he had nothing to do with the fund's administration or investment policy and did not exercise control respecting disposition of its assets. The panel held that the fund's assets did not include the unpaid

[**] This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

withdrawal liability. It reasoned that the withdrawal liability was a statutory obligation, and was different from unpaid contributions arising from contractual obligations under the collective bargaining agreement. The panel held that the contractor's failure to challenge the withdrawal liability amount in arbitration did not act as a waiver of his right to discharge the debt.

COUNSEL

Christian L. Raisner (argued), Emily P. Rich, Roberta D. Perkins, Weinberg, Roger & Rosenfeld, Alameda, California, for Appellant.

Wayne A. Silver (argued), Sunnyvale, California; R. Kenneth Bauer, Law Offices of R. Kenneth Bauer, Walnut Creek, California, for Appellee.

OPINION

SCHROEDER, Circuit Judge:

INTRODUCTION

When contractors in the construction industry stop working under the terms of a collective bargaining agreement, but continue in business, they cannot simply stop making payments to the pension fund administered under that agreement. Pursuant to the Employee Retirement Income Security Act ("ERISA"), they are liable to the fund in the amount determined necessary to ensure payment of benefits to employees whose rights have vested. 29 U.S.C. §§ 1381,

1391. The issue in this appeal is whether that "withdrawal liability" is dischargeable in bankruptcy. The answer requires some analysis of possible differences between withdrawal liability and liability for delinquent contributions, but we ultimately agree with the result reached by both the bankruptcy court and the district court that the debt is dischargeable. The pension fund cannot establish that the debtor is a fiduciary with respect to money it owes as withdrawal liability.

BACKGROUND

The debtor is Michael G. Moxley, who did business as MGM's Cabinet Installation Service. In 1999 he became a signatory to the multiemployer bargaining agreement entitled "The 46 Northern California Counties Carpenter's Master Agreement of Northern California," (the "Agreement"). He was required under the Agreement to make contributions to the Carpenters Pension Trust Fund for Northern California (the "Fund"). When the Agreement expired in June 2004, he was no longer a signatory to a collective bargaining agreement. He stopped making payments to the Fund, but continued doing carpentry work in the Bay Area.

In March of 2005 the Fund notified Moxley that because he was still doing work covered by the Agreement, he was subject to withdrawal liability pursuant to 29 U.S.C. § 1381. That amount had been determined to be $172,045 and for purposes of this appeal is not disputed. The Fund filed suit in United States District Court for the Northern District of California, but proceedings there were stayed when Moxley filed for bankruptcy.

In the bankruptcy court, Moxley sought a discharge of his debt to the Fund, and the Fund filed a complaint under 11 U.S.C. § 523(c) to prevent discharge. The Fund sought to establish that the debt qualified as one created via defalcation by a fiduciary under § 523(a)(4). It provides that a bankruptcy discharge "does not discharge an individual debtor from any debt . . . for fraud or defalcation while acting in a fiduciary capacity . . . ." *Id.*

The Fund's position was that because it is a trust fund, and those who administer, own, or control assets of a trust fund are fiduciaries, Moxley was a fiduciary for funds in his control representing the amount of withdrawal liability that he should pay to the Fund. In order to prevent the discharge, the Fund therefore had to establish both that Moxley was acting in a fiduciary capacity with respect to the money he had not paid to the Fund, and that the failure to pay constituted "defalcation" within the meaning of the Code. We need not reach the issue of defalcation, because we determine Moxley was not a fiduciary.

In trying to establish that Moxley was a fiduciary under the Bankruptcy Code, the Fund faces a number of hurdles, the first, of course, is having to show that Moxley was a fiduciary of the Fund pursuant to ERISA. Fiduciaries under ERISA are defined as entities who manage a plan, give investment advice to a plan, or control assets of a plan. ERISA provides in 29 U.S.C. § 1002(21)(A) that a fiduciary is one who:

> [1] exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets, [2] renders investment advice for

> a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or [3] has any discretionary authority or discretionary responsibility in the administration of such plan.

Since Moxley has had nothing to do with the administration or investment policy of the plan, the only conceivable part of the definition that might apply is one who "exercises . . . control respecting . . . disposition of [the Fund's] assets." *Id.* The Fund therefore argued in the bankruptcy court that its "assets" include money that is owed to the Fund, and that Moxley has exercised control over that money so as to become a fiduciary.

The problem with this simple proposition is that money that is owed to the Fund is not in the Fund, and is therefore not yet a Fund "asset." That is what this court held in *Cline v. Indus. Maint. Eng'g & Contracting Co.*, 200 F.3d 1223 (9th Cir. 2000). There, we dealt with a claim brought by employees against their employers, alleging that the employers' failure to contribute adequately to the employee benefit plan constituted a prohibited transaction under ERISA. While we rejected the contention that the employers had failed to contribute adequately to the plan, we also said that the claim failed for the independent reason that unpaid funds are not plan assets because they have not yet been paid. *Id.* at 1234. "Until the employer pays the employer contributions over to the plan, the contributions do not become plan assets over which fiduciaries of the plan have a fiduciary obligation." *Id.*

Thus, the bankruptcy court in this case, relying on *Cline* and our earlier opinion in *Collins v. Pension & Ins. Comm. of S. Cal. Rock Products & Ready Mixed Concrete Ass'ns*, 144 F.3d 1279 (9th Cir. 1998), held that Moxley was not a fiduciary with respect to the debt he owed the Fund. It said that the Fund's theory conflicted with *Cline*, *Collins*, and "numerous cases . . . holding that persons owing contributions are not automatically ERISA fiduciaries."

In its appeal to the district court, therefore, the Fund argued that money a contractor owed to the Fund as a result of the bargaining agreement could be considered an asset of the Fund if the agreement itself so provided. The Fund contended this agreement did, and pointed to the Article of the Agreement establishing the Fund and the employers' obligations to it. In relevant part, the Agreement defined the Fund as consisting of "all Contributions required by the Collective Bargaining Agreement . . . to be made for the establishment and maintenance of the Pension Plan . . . ."

The Fund contended that Moxley's debt to the Fund was in the nature of "contributions required . . . to be made," and, for that reason, was within the Agreement's definition of plan assets. This would make Moxley a fiduciary by virtue of his control over those assets. *See Trustees of S. Cal Pipe Trades Health & Welfare Trust Fund v. Temecula Mech., Inc.*, 438 F. Supp. 2d 1156, 1163 (C.D. Cal. 2006) (concluding that unpaid contributions, though generally not plan assets, could be made plan assets by contract between the employer and the union).

Moxley pointed out, however, that under the Fund's theory he became a fiduciary only because he did not make the payment. This court has held that where a statute creates a fiduciary relationship, as the Fund contends ERISA does here, that fiduciary relationship will not be recognized for the purposes of § 523(a)(4) if the claimed fiduciary relationship resulted from the wrongdoing that created the debt. *In re Hemmeter*, 242 F.3d 1186, 1190 (9th Cir. 2001). The fiduciary status has to be in existence before the debt was owed. *Id.* (the fiduciary obligations must exist "prior to the alleged wrongdoing."). The district court agreed that under the Fund's theory, Moxley's own wrongdoing, *i.e.*, his failure to pay, created the asserted fiduciary relationship. Relying on *Hemmeter*, the district court affirmed the bankruptcy court.

The district court also rejected the Fund's contention that Moxley had waived his right to discharge the debt in bankruptcy by failing to contest the debt in arbitration. ERISA requires that all disputes over withdrawal liability be resolved by arbitration. *Teamsters Pension Trust Fund-Bd. of Trustees of W. Conference v. Allyn Transp. Co.*, 832 F.2d 502, 504 (9th Cir. 1987). The district court ruled that this was not a dispute over the existence of the liability, but an issue of discharge governed by § 523(a)(4). The court rejected the Fund's contention that the ERISA arbitration provision can override the Bankruptcy Code.

In this appeal, the Fund contends that Moxley is a fiduciary of the Fund because he controlled money that he owed to the Fund for withdrawal liability, which his agreement with the union recognized as an asset of the Fund. The Fund also reasserts its argument that Moxley's failure to contest the withdrawal liability in arbitration resulted in a waiver of his right to seek a discharge in bankruptcy. Moxley raises a threshold jurisdictional argument that Article III of the Constitution prohibits the bankruptcy court from adjudicating the Fund's claim, so we turn to that first.

DISCUSSION

I. The Bankruptcy Court Had Jurisdiction to Adjudicate the Dischargeability of the Fund's Claim Against Moxley

After the district court's decision in this case, the Supreme Court decided *Stern v. Marshall*, 131 S. Ct. 2594, 2611 (2011), holding that a bankruptcy court could not adjudicate a counterclaim for tortious interference because a bankruptcy court is not an Article III court and the counterclaim did not involve "public rights." Bankruptcy judges, because they do not have the tenure and salary protections of Article III, may not exercise the judicial power of the United States, except in cases involving public rights. *Id.* at 2609–11. Public rights are identified as those rights closely related to a federal government function. *Id.* at 2613.

Moxley therefore asserts a threshold objection to the bankruptcy court's jurisdiction to decide dischargeability in this case because he claims it has no connection to any federal function. The contention is without substance, because the dischargeability determination is central to federal bankruptcy proceedings. *Cent. Va. Cmty. Coll. v. Katz*, 546 U.S. 356, 363–64 (2006). The dischargeability determination is necessarily resolved during the process of allowing or disallowing claims against the estate, and therefore constitutes a public rights dispute that the bankruptcy court may decide. *See In re Bellingham Ins. Agency, Inc.*, 702 F.3d 553, 564–65 (9th Cir. 2012) (concluding that public rights disputes in bankruptcy are those that "necessarily ha[ve] to be resolved in the course of the claims-allowance process"); *see also In re Global Technovations Inc.*, 694 F.3d 705, 721–22 (6th Cir. 2012) (bankruptcy court has jurisdiction over disputes that must be resolved before ruling on proof of claim).

II. Moxley Is Not a Fiduciary of the Fund Because the Unpaid Withdrawal Liability Is Not an Asset of the Fund

The district court held that Moxley was not a fiduciary under § 523(a)(4) with respect to money he owes as withdrawal liability, because the Bankruptcy Code requires a fiduciary relationship to exist before the bad act of nonpayment, rather than as a result of it. *See Hemmeter*, 242 F.3d at 1190. In this court, the Fund makes a more creative argument. It contends Moxley did not become a fiduciary as a result of his failure to pay this debt, but instead has been a fiduciary with respect to all the contributions he was ever required to pay in to the Fund, including withdrawal liability.

This contention is grounded in the language of the Agreement defining the plan assets to include "all contributions required . . . to be made" to the Fund. There is some district court and bankruptcy court authority supporting the proposition that an employer is a fiduciary under the Bankruptcy Code with respect to unpaid contributions, where the collective bargaining agreement includes unpaid contributions as plan assets. *See Bos v. Bd. of Trustees of Carpenters Health & Welfare Trust Fund for California*, No. 2:12-CV-02026-MCE, 2013 WL 943520, at *3 n.6 (E.D. Cal. Mar. 11, 2013) (citing *Hemmeter*, 242 F.3d at 1190); *In re O'Quinn*, 374 B.R. 171, 181–82 (Bankr. M.D.N.C. 2007). According to these cases, it is ERISA and the provision of the particular collective bargaining agreement, and not the contractor's nonpayment of the debt, that are responsible for a fiduciary relationship. If the agreement creates the obligation to pay contributions and defines plan assets to include the unpaid contributions, then ERISA makes the person who controls those plan assets a fiduciary. Section 523(a)(4) prevents discharge from a "debt . . . while acting in a fiduciary capacity." As the court in *O'Quinn* stated, "It is the *obligations* of the fiduciary, however, as opposed to the debt, that must preexist the alleged wrongdoing. In the Section 523(a)(4) context, a context in which one party's claim is grounded in the other's wrongdoing, the *debt* will always arise at the time of the wrongdoing." *O'Quinn*, 374 B.R. at 182 (emphasis in original).

Relying on these cases involving the obligation to make contributions, the Fund makes a persuasive case that, given the provisions of this agreement, unpaid contributions required by the Agreement can be considered plan assets. Here, however, we do not have to decide the question of whether unpaid contributions are plan assets. This is because we do not deal with unpaid contributions arising from contractual obligations.

This case involves withdrawal liability under ERISA that is imposed because the employer no longer has a contractual obligation to contribute. This obligation is statutory. ERISA recognizes that contributions, on the other hand, are contractual obligations that ERISA enforces, but does not create. *See Sw. Adm'rs, Inc. v. Rozay's Transfer*, 791 F.2d 769, 773 (9th Cir. 1986) ("For an employer to be obligated to make employee benefit contributions to a trust fund, there must exist a binding collective bargaining agreement.").

For an employer, like Moxley, in the building and construction industry, withdrawal liability does not arise until the "employer ceases to have an obligation to contribute under the plan," and the employer "continues to perform work in the jurisdiction of the collective bargaining agreement of the type for which contributions were previously required." 29 U.S.C. § 1383(b). Because withdrawal liability does not arise until the employer ceases to have an obligation to contribute to the plan, it cannot be considered an unpaid contribution under the collective bargaining agreement.

Withdrawal liability is based on the recognition that, even though the employer no longer has a contractual obligation to pay, there may be employees whose rights have vested and whom the plan must pay. "When an employer withdraws from [] a plan, the plan remains liable to the employees who have vested pension rights, though it no longer can look to the employer to contribute additional funds to cover these obligations." *Chi. Truck Drivers, Helpers & Warehouse Workers Union (Indep.) Pension Fund v. CPC Logistics, Inc.*, 698 F.3d 346, 347–49 (7th Cir. 2012) (describing withdrawal liability and how it is calculated). Withdrawal liability acts as an "exit price equal to [the employer's] pro rata share of the pension plan's funding shortfall." *Id.* at 347.

As a result, an employer who has made all of the required contributions before leaving the agreement may still have a withdrawal liability. "Even when, upon an employer's withdrawal, that employer and every other participating employer has made every contribution that ERISA required of them, the plan may nonetheless be underfunded, resulting in withdrawal liability for the departing employer." *In re CD Realty Partners*, 205 B.R. 651, 658 n.8 (Bankr. D. Mass. 1997). In sum, withdrawal liability is imposed by ERISA to account for the pension fund's needs going forward, and therefore is distinct from the contributions required to be made by the plan agreements.

The Fund points to § 1451(b) of ERISA that establishes the same procedural framework for recovering delinquent contributions and unpaid withdrawal liability. The Fund contends that unpaid contributions and withdrawal liability are thus to be treated as substantively the same. This contention is incorrect.

The provision at issue reads:

> In any action under this section to compel an employer to pay withdrawal liability, any failure of the employer to make any withdrawal liability payment within the time prescribed shall be treated in the same manner as a delinquent contribution (within the meaning of section 1145 of this title).

29 U.S.C. § 1451(b). This provision means only that the venue, statute of limitations, and right to receive costs and expenses in actions to enforce withdrawal liability are the same as those applicable to actions to collect delinquent plan contributions. *See Trs. of Amalgagmated Ins. Fund v. Geltman Indus., Inc.*, 784 F.2d 926, 931–32 (9th Cir. 1986) (explaining that the attorney's fees provision applies to actions to recover contributions under 29 U.S.C. § 1145 and therefore also applies to "actions to collect unpaid employer withdrawal liabilities"). It does not mean that they are otherwise similar obligations. One obligation is created by statute, the other by contract.

Accordingly, even if we assume that unpaid contributions can be considered assets of the Fund under the particular provisions of this agreement, and non-dischargeable, the withdrawal liability is not an unpaid contribution. We therefore agree with the conclusion of both the bankruptcy and district court that this withdrawal liability is dischargeable.

III. Moxley's Failure to Challenge the Withdrawal Liability Amount in Arbitration Did Not Act as a Waiver of His Right to Discharge the Debt

The Fund continues to assert its position, rejected by the district court, that Moxley waived his right to a discharge of his withdrawal liability because he failed to challenge the amount or existence of the liability in arbitration. The Multiemployer Pension Plan Amendments Acts, 29 U.S.C. § 1401(a)(1), states that all disputes over withdrawal liability must be arbitrated, *Allyn Transp. Co.*, 832 F.2d at 504, and the Fund claims that an employer cannot seek a discharge of a debt for withdrawal liability, if the employer failed to dispute the withdrawal liability in arbitration.

The arbitration provision of ERISA expressly applies where an employer contests the existence or the amount of an alleged liability. 29 U.S.C. § 1401. Moxley does not here dispute the amount or existence of the withdrawal liability. He has invoked the provisions of the Bankruptcy Code to discharge existing obligations and receive a "fresh start." *Cent. Va. Cmty. Coll.*, 546 U.S. at 364. The district court correctly held that this case is governed by the dischargeability provisions of the Bankruptcy Code. 11 U.S.C. § 523.

CONCLUSION

The district court's order affirming the judgment of the bankruptcy court is **AFFIRMED**.

FILED

OCT 10 2013

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OF THE NINTH CIRCUIT

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UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re: WILLIAM ROGER UTNEHMER and MARIE CLAIRE UTNEHMER, Debtors.	BAP No. NC-12-1362-PaDJu Bk. No. 11-12159 Adv. No. 11-01239
WILLIAM ROGER UTNEHMER; MARIE CLAIRE UTNEHMER, Appellants, vs. PATRICK CRULL; MARY CRULL, Appellees.	**O P I N I O N**

Argued and Submitted on September 20, 2013
at San Francisco, California

Filed - October 10, 2013

Appeal from the United States Bankruptcy Court
for the Northern District of California

Hon. Alan Jaroslovsky, Chief Bankruptcy Judge, Presiding

Appearances: William Roger Utnehmer argued pro se. Steven Marc Olson argued for appellees Patrick and Mary Crull.

Before: PAPPAS, DUNN and JURY, Bankruptcy Judges.

PAPPAS, Bankruptcy Judge:

Chapter 7[1] debtors William Roger Utnehmer ("William")[2] and Marie Claire Utnehmer ("Marie" and together, "Debtors") appeal pro se[3] the judgment of the bankruptcy court awarding creditors Patrick ("Patrick") and Mary Crull (together, "Crulls") $100,000 plus interest, and determining that the judgment debt is excepted from discharge under § 523(a)(4). We REVERSE.

FACTS

John Kwan ("John") and William did business as CW Development Partners ("CWDP"), a general partnership involved in real estate development in California. In February 2005, CWDP purchased a property in Venice, California (the "Property") for $1,250,000, which the partners intended to develop as a "spec house" by tearing down the existing structure and building a new luxury residence for resale. Title to the Property was taken in Debtors' individual names because John's credit was not as good as theirs. However, both William and John always considered the

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[1] Unless otherwise indicated, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and "Rule" references are to the Federal Rules of Bankruptcy Procedure. Civil Rule references are to the Federal Rules of Civil Procedure.

[2] We refer to several of the parties by their first names for clarity; no disrespect is intended.

[3] While appearing pro se in this appeal, Debtors were represented in the bankruptcy court by counsel. The record indicates that William has in the past been a member of the California bar.

Property to be owned by CWDP.

Crulls were long-term acquaintances of John. Sometime in 2005, John offered Crulls “an opportunity to get in on this particular project.” Trial Tr. 69:16-17, June 12, 2012. In June 2005, there was a telephone conversation between William and Patrick. The record is unclear as to who initiated the call and the specifics of the conversation. After the conversation, William sent Crulls a packet of documents, including the following:

1. A transmission letter addressed to Mary[4] Crull, indicating that a “cover letter, loan agreement/note and the private offering was attached.”

2. A cover letter from William to Crulls. The letter contained the following statement: “Until the formal operating agreement is drafted and executed pursuant to the terms of the Private Offering, John and I will be executing promissory notes with you for the amount of your equity contribution.”

3. A “Loan Agreement” proposing a $100,000 loan from Crulls to CWDP, including the following material terms:

   (A) The loan was to be for a term of not more than twelve months. The interest rate was twelve percent per annum, payable monthly. The entire balance of principal and interest was due upon sale of the property, or at the end of the twelfth month, whichever was sooner. The loan could be paid off at any time without any penalty for prepayment.

   (B) The loan was to be secured by a trust deed on the Property.

   (C) The loan proceeds were to be used by CWDP at

[4] In their dealings with one another, and in submissions to the courts, the parties occasionally refer to Marie as Mary.

their sole discretion.

(D) CWDP would procure liability, property and worker's compensation insurance as required, and name Lender [Crulls] as loss payee for an amount equal to the loan.

(E) The Parties agreed that $50,000 of the initial $100,000 loan was intended to be super[s]eded by execution of a formal operating agreement which would recharacterize this $50,000 of the lenders' interest as an investors' equity interest in a limited liability company to be formed, with a 10% annual preferred return, and 35% participation in profits on a prorated basis. The documents for formation of the limited liability company, and the operating agreement, were supposedly being drafted.

3. A promissory note ("Note") to be executed by William and John consistent with the Loan Agreement. However, the Note makes no reference to the Loan Agreement's provision for recharacterizing $50,000 of the money to be loaned as an equity interest at some later time.

4. A twelve-page "Private Offering," describing the Property and the investment opportunity.

On or about June 15, 2005, Crulls wire-transferred $100,000 to the CWDP Partnership Account at Bank of America. On June 15, 2005, William signed the Note evidencing the loan from Crulls.

William and John expected, and had informed Crulls of their intention, to complete the Property project within ten months. However, significant delays were experienced resulting from design changes. Over the next two years, Debtors obtained several additional loans to finance the construction project, which loans were secured, at least in part, by the Property.[5]

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[5] For example, in November 2005, Debtors borrowed $1.025 million from Bay Area Financial Corporation. In June 2006, Debtors borrowed another $200,000 from Bay Area Financial Corporation, secured in part by the Property. In the fall of (continued...)

Patrick testified at trial that Crulls were never informed about these refinancings of the Property. Trial Tr. 71:13 ("We had no idea there was refinancings at all."). This is not disputed by Debtors.

The check ledger for the Property project reflects that $25,175.00 in interest payments were paid to Crulls from mid-2006 to mid-2008. Although the Loan Agreement with Crulls by its terms ended on June 15, 2007, the principal balance was not repaid.

By early 2008, the Property project had been completed. Crulls retained counsel to attempt to enforce their rights. On April 7, 2008, their attorney sent a letter to Debtors, confirming the parties' intention "to modify the [Loan] agreement." Those revisions provided that Debtors would pay Crulls $50,000 by April 28, 2008, plus $2,000 per month until the remaining balance due on the Note of $50,000 had been repaid. Notably, the modified terms of the parties' agreement included the following:

> When the Property sells, the remaining $50,000 principal sum of the Note shall be re-characterized as an investor's equity interest in the Property and the Crulls shall be paid first, their initial $50,000 equity, second 10% preferred return thereon, third their pro rata 35% share of the net sales proceeds.

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[5](...continued) 2006, Debtors obtained a $2,083,000 construction loan from Anchor Loans for development of the Property. The loan cleared existing encumbrances against the Property, including a first and second deed of trust of Countrywide Mortgage held on the Property, and made a partial payment of the loans held by Bay Area Financial Corporation. In Summer 2007, Debtors borrowed another $110,000 from a Mr. Propp, using the Property in part as collateral. In Autumn 2007, Debtors refinanced the construction loan from Anchor Loans with a $2,550,000 loan from Loan Oak Fund.

William signed the modification, consenting to the revision of the Loan Agreement on April 8, 2008. Debtors made only one $4,000 payment on the obligations created in the revisions to the Loan Agreement.

In June 2008, the Property was sold for $3,725,000. All creditors on the Property project were paid in full from the proceeds, but no payment was made to Crulls. Crulls asserted that William informed them that he was unable to pay the debt from the proceeds of sale.

On September 30, 2009, Crulls filed a complaint against William in Los Angeles Superior Court, to collect the balance due on the Note. Crull v. Utnehmer, Case no. SC105077. When William did not respond, a default judgment was entered in favor of Crulls against him on June 28, 2010, in the amount of $213,645.17.

Debtors filed a chapter 7 bankruptcy petition on June 6, 2011. On their Schedule F and Statement of Financial Affairs, they listed a contingent, unliquidated, disputed debt owed to Crulls for $220,259.43 for the default judgment.

Crulls filed an adversary complaint against Debtors on September 12, 2011. In it, they requested that their claim against Debtors be excepted from discharge under § 523(a)(2) and (a)(6), alleging that William made numerous false statements on which they relied in connection with the Loan Agreement and to persuade them to refrain from objecting to the closure of escrow for the sale of the Property. Debtors answered the complaint on October 1, 2011, generally denying the allegations in the complaint.

A trial in the adversary proceeding was held on June 12, 2012. Early in the trial, the bankruptcy court indicated that it had read the parties' proposed findings of fact and conclusions of law that had been submitted earlier, and that it was not convinced that Crulls could establish any fraud or malice sufficient for exception to discharge under § 523(a)(2) or (a)(6). However, the court "saw that there may be liability under [§] 523(a)(4) . . . if a partnership arrangement is shown." Trial Tr. 10:12-14.[6]

John, William and Patrick testified at the trial. At the close of testimony, the bankruptcy court repeated its conclusion that Crulls had not established that any fraud or malicious actions occurred to support an exception to discharge under § 523(a)(2) or (a)(6). Addressing Crulls' counsel, the court stated that "Your case, if at all, is based on your client's status as a partner . . . . If your client was a fiduciary in relation to the venture and cannot account for the proceeds, I think that that's enough to establish defalcation." Trial Tr. 78:3-5, 82:18-20.

The bankruptcy court took the issues under submission and, on June 18, 2012, entered a Memorandum after Trial. In it, the court dismissed Crulls' § 523(a)(2) and (a)(6) claims because

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[6] Though Crulls at no time asked to amend their complaint, significantly, the parties offered no formal objection to the bankruptcy court proceeding with a trial on a claim for an exception to discharge under § 523(a)(4), even though a right to relief under this Code provision had not been pled in Crulls' complaint. They also do not cite the bankruptcy court's decision to adjudicate the issues based on this new theory as error on appeal. Accordingly, we, also, will examine the merits of the parties' arguments concerning that claim under § 523(a)(4).

there was no evidence to show fraud in the inducement, or willful and malicious conversion, by Debtors. Crulls have not appealed this aspect of the court's decision.

The bankruptcy court, however, made other factual findings regarding the original Loan Agreement:

> The parties memorialized their transaction in a "loan agreement." Under the terms of this agreement, the $100,000 was to be paid in full when the property was sold, or after 12 months, whichever came first. However, they also agreed that "$50,000 of this initial $100,000 is intended to be super[s]eded by execution of [a] formal operating agreement which will re-characterize $50,000 of the lender's interest to an investor's equity interest with a 10% annual preferred return and 35% participation in profits on the equity contribution on a prorated basis."

Based on these findings, the bankruptcy court concluded that Crulls were entitled to an exception to discharge under § 523(a)(4) because the Loan Agreement was:

> sufficient to make Utnehmer a partner of Crulls in the project. A partner has the responsibilities of a fiduciary within the meaning of § 523(a)(4) as to partnership property. Ragsdale v. Haller, 780 F.2d 794, 796-97 (9th Cir. 1986). Since Utnehmer took title to the project in his own name and refinanced several times without involving the Crulls, he has the burden of accounting for all of the proceeds as well as the costs and expenditures relating to the venture; failure to do so is defalcation, notwithstanding lack of demonstrated intent to harm or cheat his partners. In re Lewis, 97 F.3d 1182, 1186-87 (9th Cir. 1996). Utnehmer has not met his fiduciary duties. His accounting is not professional[ly] prepared and admittedly contains expenses not attributable to the partnership. He has not met his burden of showing that nothing is due to the Crulls.

On June 25, 2012, the bankruptcy court entered judgment for Crulls against William, and the community property interest of Marie,[7] for the $100,000 in principal owed under the Note, plus

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[7] The bankruptcy court at trial had indicated its willingness to grant Debtors' request to dismiss Crulls' claims (continued...)

interest from April 1, 2008. The judgment declared this debt excepted from discharge under § 523(a)(4).

Debtors filed a timely appeal on July 7, 2012.

JURISDICTION

The bankruptcy court had jurisdiction over this proceeding under 28 U.S.C. §§ 1334 and 157(b)(2)(I). We have jurisdiction under 28 U.S.C. § 158.

ISSUES

1. Whether the bankruptcy court erred in determining that a partnership relationship existed between William and Crulls.
2. Whether the bankruptcy court erred in determining that the debt owed by Debtors to Crulls was excepted from discharge pursuant to § 523(a)(4).

STANDARDS OF REVIEW

"In bankruptcy discharge appeals, the Panel reviews the bankruptcy court's findings of fact for clear error and conclusions of law de novo, and applies de novo review to 'mixed questions' of law and fact that require consideration of legal concepts and the exercise of judgment about the values that animate the legal principles." Oney v. Weinberg (In re Weinberg), 410 B.R. 19, 28 (9th Cir. BAP 2009), aff'd 407 Fed. Appx. 176 (9th Cir. 2010), citing Wolkowitz v. Beverly (In re Beverly), 374 B.R. 221, 230 (9th Cir. BAP 2007), aff'd in part & dismissed in part, 551 Fed. Appx. 1092 (9th Cir. 2008), citing

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[7](...continued) against Marie personally, but her interest in the community property could be liable for exception to discharge. Trial Tr. 6:21-24.

Murray v. Bammer (In re Bammer), 131 F.3d 788, 791-92 (9th Cir. 1997).

The bankruptcy court's determination that a partnership existed between the parties under California law was based on its interpretation of the Loan Agreement. A trial court's interpretation of the terms of a contract is reviewed de novo. Ameron Int'l Corp. v. Ins. Co. of State of Pa., 242 P.3d 1020, 1024 (Cal. 2010).

DISCUSSION

Applying California law to the facts of this case, we conclude that the bankruptcy court erred when it decided that a partnership existed between William and Crulls based upon the Loan Agreement. Since there was no partnership, William owed no fiduciary obligations to Crulls and, as a result, the bankruptcy court also erred in determining that William's debt to Crulls should be excepted from discharge as a defalcation by a fiduciary pursuant to § 523(a)(4). We therefore REVERSE.

The exception to discharge relied upon by the bankruptcy court, § 523(a)(4), provides that:

> (a) A discharge under section 727 [discharge in a chapter 7 case such as this one] . . . does not discharge any debtor from any debt — . . . (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny[.]"

Case law makes clear that the broad, general definition of fiduciary - a relationship involving confidence, trust and good faith - is inapplicable in the context of exception to a bankruptcy discharge. Ragsdale v. Haller, 780 F.2d 794, 796 (9th Cir. 1986). Whether the debtor was acting in a fiduciary capacity within the meaning of § 523(a)(4) is a question of federal law. <u>Lewis v. Scott (In re Lewis)</u>, 97 F.3d 1182, 1185 (9th Cir. 1996). A debt is nondischargeable under § 523(a)(4) only "where (1) an express trust existed, (2) the debt was caused by fraud or defalcation, and (3) the debtor acted as a fiduciary to the creditor at the time the debt was created." <u>Otto v. Niles (In re Niles)</u>, 106 F.3d 1456, 1459 (9th Cir. 1997). Thus, § 523(a)(4)'s exception to discharge results only where, among other things, the fiduciary relationship between the debtor and the creditor arises in relation to an express or technical trust that pre-dates the alleged defalcation. <u>In re Lewis</u>, 97 F.3d at 1185.

State law determines whether the requisite trust relationship exists. <u>Id.</u> Under California law, "all partners [are] trustees over the assets of the partnership." <u>Ragsdale</u>, 780 F.2d at 796; <u>see</u> CAL. CORP. CODE § 16404(b)(1) (partner has a duty to hold as trustee any "property, profit, or benefit derived" from partnership business or use of partnership property). Accordingly, "California partners are fiduciaries within the meaning of § 523(a)(4)." <u>Ragsdale</u> 780 F.2d at 796-97. Thus, the determination by a bankruptcy court that a partnership existed between William and the Crulls under California law would establish one important component of the proof required for an exception to discharge under § 523(a)(4).

However, even if a fiduciary relationship existed, the bankruptcy court must also find that William committed a "defalcation." As that term was understood in the Ninth Circuit at the time the bankruptcy court entered its judgment, a defalcation was a "misappropriation of trust funds or money held in any fiduciary capacity; [the] failure to properly account for such funds." In re Lewis, 97 F.3d at 1186 (quoting BLACK'S LAW DICTIONARY 417 (6th ed. 1990)).

The court also ruled in Lewis that, for purposes of § 523(a)(4), a defalcation "includes the innocent default of a fiduciary who fails to account fully for money received. . . . In the context of section 523(a)(4), the term 'defalcation' includes innocent, as well as intentional or negligent defaults so as to reach the conduct of all fiduciaries who were short in their accounts." Id. at 1186 (internal citations ommitted). But in this respect, In re Lewis is no longer good law.

In May 2013, after the bankruptcy court entered its judgment, the United States Supreme Court decided Bullock v. BankChampaign, N.A., 133 S. Ct. 1754 (2013). Bullock effectively abrogated that part of In re Lewis holding that a debtor who failed to account to another need not possess any particular state of mind to except a debt from discharge based on fiduciary defalcation under § 523(a)(4). To the contrary, in Bullock, the Supreme Court interpreted § 523(a)(4) to require that, in order to except a debt for a defalcation by a fiduciary, the debtor must possess "a culpable state of mind . . . akin to that which accompanies application of the other terms in the same statutory phrase. We describe that state of mind as one involving knowledge of, or gross recklessness in respect to, the improper nature of the relevant fiduciary behavior." Id. at 1757.

Based upon the Supreme Court's holding in Bullock, the bankruptcy court erred when it concluded that William committed a defalcation "notwithstanding [his] lack of demonstrated intent to harm or cheat his partners. In re Lewis, 97 F.3d [at 1186-87]." Memorandum after Trial at 3, June 16, 2012. As the Crulls acknowledged at oral argument, at a minimum, then, the bankruptcy court's judgment must be vacated and the matter remanded to the bankruptcy court to address the intent requirement for a defalcation under Bullock.

But there is a more consequential error in the bankruptcy court's decision which requires reversal, not merely remand. As discussed above, a bankruptcy court's determination that a California partnership was formed by the parties would ordinarily allow us to conclude that the requisite fiduciary relationship was established for § 523(a)(4) purposes. In this case, though, the bankruptcy court simply ruled, without explanation, that

> The court somewhat reluctantly agrees with the Crulls that there is liability under § 523(a)(4). The 'Loan Agreement' is sufficient to make Utnehmer a partner of the Crulls in the project. A partner has the responsibilities of a fiduciary within the meaning of § 523(a)(4) as to partnership property. Ragsdale v. Haller, 780 F.2d 794, 796-97 (9th Cir. 1986)).

Memorandum after Trial at 2.

We disagree that, without more, the Loan Agreement's terms were sufficient under California law to create a partnership agreement at the time the Loan Agreement was executed. We therefore must reverse the bankruptcy court's conclusions that a partnership existed based on the Loan Agreement and was effective at the time the Loan Agreement was signed.

In this appeal, Crulls argue strenuously that the bankruptcy court's decision that a partnership existed was a finding of fact which may only be reversed for clear error, a highly deferential standard.[8] While, as noted above, the bankruptcy court's decision construing the parties' contract is reviewed de novo, even if the clear error standard applied, it would not protect a finding based on "an erroneous view of the law." Power v. Union P.R. Co., 655 F.2d 1380, 1382-83 (9th Cir. 1981) ("We may regard a finding of fact as clearly erroneous . . . if it was induced by an erroneous view of the law. . . . The question, then, is whether the [trial] court's findings and conclusions are based on a proper view of [] state law[.]"). Indeed, the Supreme Court has cautioned that the clear error rule is not a shield for a fact finding that is inconsistent with underlying law:

> But Rule 52(a) [applicable in bankruptcy adversary proceedings via Rule 7052] does not inhibit an appellate court's power to correct errors of law, including . . . a finding of fact that is predicated on a misunderstanding of the governing rule of law.

Bose Corp. v. Consumers Union of United States, Inc., 466 U.S. 485, 501 (1984); see also, Inwood Labs., Inc. v. Ives Labs., Inc., 456 U.S. 844, 855 n.15 (1982); United States v. Singer Mfg. Co., 374 U.S. 174, 194 n.9 (1963).

As we discuss below, the bankruptcy court's finding that there was a partnership established by the Loan Agreement was inconsistent with the governing law applicable in this case, the California law of partnerships. Moreover, since at bottom we

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[8] At oral argument, William also seemed to agree that, based on the testimony at trial, the parties considered themselves partners at all times. However, as reflected in its decision, the bankruptcy court's finding that a partnership existed was based solely on documentary evidence, and in particular the Loan Agreement, and not on testimony at trial.

are determining whether William’s debt to Crulls should be discharged, we review the bankruptcy court’s determination of that question as a mixed question of law and fact de novo and not as a simple fact determination for clear error. In re Weinberg, 410 B.R. at 28.

To determine whether the Loan Agreement established a partnership, its legal effect, we look first to the terms of the Loan Agreement as directed by the California courts. Kersch v. Taber, 67 Cal. App. 2d 499, 501 (Cal. Ct. App. 1945) (“The question of the existence of a partnership should be determined primarily by ascertaining the intention of the parties, and where they have entered into a written agreement such intention should be determined chiefly from the terms of the writing.”). In examining the written agreement, we are obliged to follow a plain meaning analysis:

> The fundamental rules of contract interpretation are based on the premise that the interpretation of a contract must give effect to the mutual intention of the parties. Under statutory rules of contract interpretation, the mutual intention of the parties at the time the contract is formed governs interpretation. Such intent is to be inferred, if possible, solely from the written provisions of the contract. The clear and explicit meaning of these provisions, interpreted in their ordinary and popular sense, unless used by the parties in a technical sense or a special meaning is given to them by usage, controls judicial interpretation. . . . An agreement is not ambiguous merely because the parties (or judges) disagree about its meaning. Taken in context, words still matter.

In re Installment Fee Cases, 211 Cal. App. 4th 1395, 1409 (Cal. Ct. App. 2013).

As noted above, the Loan Agreement is composed of five paragraphs. The first four paragraphs clearly reflect the terms of what appears to be a loan of money from Crulls to CWDP; they make no reference to the creation or existence of a partnership between the parties. The only paragraph in the Loan Agreement that could arguably serve as the foundation of a partnership is paragraph 5, which provides:

> The Parties agree that $50,000 of this initial $100,000 loan is intended to be super[s]eded by execution of a formal operating agreement which will recharacterize $50,000 of the lender's interest to an investor's equity interest with a 10% annual preferred return and 35% participation in profits on the equity contribution on a prorated basis. Said operating agreement and formation of a Limited Liability Company is being drafted.

There can be no dispute about the plain meaning of this paragraph: it contemplates that, <u>at some future point in time</u> (i.e., upon the "execution of a formal operating agreement" for a yet-to-be formed limited liability company), a portion of the Crulls' loan would be "recharacterized" as an equity interest in the Property project entitling them, thereafter, to participate in the profits of the venture. There is nothing in the Loan Agreement to indicate any intent to form a partnership or LLC at the time of signing the Loan Agreement, nor at any point before the execution of the operating agreement or LLC formation. As we discuss below, this would be an essential element for defalcation under § 523(a)(4), because if the partnership was not in existence before any alleged wrongful behavior, there was no fiduciary duty and therefore there cannot be defalcation under § 523(a)(4).

Although the bankruptcy court's reasoning was perhaps not fully presented in its decision, we assume that the court relied upon the Loan Agreement's provisions for sharing profits by the parties as an indication that the parties intended to form a partnership. But if this was the court's conclusion, it is inconsistent with the requirements of California law regarding formation of partnerships. Simply stated, "where the parties purport to establish a partnership to engage in business at a future time or upon the happening of a contingency, the partnership does not come into being until the time specified or until the contingency is removed." Solomont v. Polk Development Co., 245 Cal. App. 2d 488, 496 (Cal. Ct. App. 1966) [2d Dist.]; Kersch v. Taber, 67 Cal. App. 2d at 504 [3d Dist.]; Taylor v. Nelson, 26 Cal. App. 681, 682 (Cal. Ct. App. 1915) [1st Dist.]; accord Hollis v. Rock Creek Pack Station, 594 F. Supp. 156, 160 (D. Ariz. 1984) (applying California law: "where parties purport to establish a partnership to engage in business upon the happening of a contingency, the partnership does not come into being until the contingency has occurred."). We have located no California case law varying the rule that an agreement to form a partnership in the future, upon fulfillment of a contingency, does not, at the time of entry of the agreement, create a partnership.

In this case, if no partnership between William and Crulls was formed at the time they executed the Loan Agreement then, under California law, no fiduciary duty by William to Crulls arose at that time. If there was no partnership, no trust relationship existed between the parties, and no fiduciary duty was imposed upon William at the time of execution of the Loan Agreement. And any subsequent behavior, whether or not accompanied by bad intent, would not be a fiduciary breach triggering exception to discharge under § 523(a)(4). In re Lewis, 97 F.3d at 1185 (holding that an express trust [i.e., a partnership] must exist before any defalcation).

Other concerns arise from the bankruptcy court's reasoning that a partnership arose from the Loan Agreement. As discussed above, the court apparently considered a future agreement to share profits as an indication of partnership. It is true that an agreement to share profits may be evidence of a partnership agreement. Holmes v. Lerner, 74 Cal. App. 4th 442, 453-54 (Cal. Ct. App. 1999); Bank of Cal. v. Connolly, 36 Cal. App. 3d 350, 364 (Cal. Ct. App. 1973). However, the presence of profit sharing does not support a presumption of the existence of the partnership unless there was also an actual sharing of the profits. CAL. CORP. CODE § 16202 (2013)("A person who receives a share of the profits of a business is presumed to be a partner in the business.")(emphasis added). Here, the facts are undisputed that no limited liability company was ever formed, no operating agreement was ever executed, and there was no actual sharing of profits between William and Crulls.

Moreover, profit-sharing is not considered the most important indicia of a partnership under California law. The existence of a partnership is ordinarily evidenced by some degree of participation by alleged partners in the management and control of the business. Sperske v. Rosenberg, 2013 WL 3817067, at *2 (C.D. Cal. 2013); Fredianelli v. Jenkins, 2013 WL 1087653 (N.D. Cal. 2013); Dickinson v. Samples, 104 Cal. App.2d 311, 315 (Cal. Ct. App. 1951) ("To participate to some extent in the management of a business is a primary element in partnership organization, and it is virtually essential to a determination that such a relationship existed.”). Here, the Loan Agreement grants Crulls no rights to participate in the management of the Property project, and in particular in paragraph 4, reserves the right to decide how the loan proceeds will be used solely to CWDP. Consistent with these terms, at trial, Patrick acknowledged that he was not consulted concerning management decisions, nor about the multimillion dollar financing arrangements made concerning the Property: “we had no idea there was refinancings at all.” Trial Tr. 71:13.

Perhaps in recognition of the deficiencies in the bankruptcy court’s conclusion concerning the existence of a partnership, on appeal, Crulls raise the alternative argument that because the Crulls detrimentally relied on William’s promise to form a limited liability company, he should be estopped from denying the existence of such a promise. They urge that, under California law, since a manager of an LLC owes a fiduciary duty to members, we should hold that William was a fiduciary to Crulls when he “helped himself to millions of dollars from refinancing the partnership’s Abbot Kinney property.”

Our review of the record satisfies us that Crulls did not properly raise this argument in the bankruptcy court. An appellate court in this circuit will not consider arguments that “were not properly raised in the trial court.” O’Rourke v. Seabord Sur. Co. (In re E.R. Fegert, Inc.), 887 F.2d 955, 957 (9th Cir. 1989); see also In re Cybernetic Servs., Inc., 252 F.3d 1039, 1045 n.3 (9th Cir. 2001) (stating that the appellate court will not explore ramifications of an argument because it was not raised in the bankruptcy court and therefore waived).

Not only was the promissory estoppel argument not made in the bankruptcy court, Crulls have not properly raised it in this appeal. Crulls cite no authority for their argument that the manager of an LLC has the fiduciary duties as contemplated by § 523(a)(4) to other members of the LLC.[9] And in their brief, Crulls do not explain how a fiduciary duty that may arise in an LLC that does not come into existence until sometime in the future does not suffer from the same infirmity as a future partnership (i.e., defalcation under § 523(a)(4) requires the fiduciary duty to arise before any alleged wrongdoing takes place).

For these reasons, we conclude that the bankruptcy court erred in its determination that a partnership was formed by the Loan Agreement. At best, the parties agreed to form an LLC based upon events to occur in the future, events that never came to pass. Since no partnership existed between the parties during their dealings, we conclude that, as a matter of law, William was not a fiduciary as to Crulls for purposes of § 523(a)(4), and that the bankruptcy court erred in excepting the debt from discharge under that provision of the Bankruptcy Code.

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[9] Even if this were so, since no LLC was ever formed and no operating agreement ever drafted, there is no evidence that William would be the managing member with a fiduciary duty to other members. Additionally, we observe that the Ragsdale rule that a California partnership implies the fiduciary duty for defalcation purposes under § 523(a)(4) only applies to a partnership. We have found no case law that applies the Ragsdale rule to a California LLC.

CONCLUSION

The bankruptcy court erred in ruling that it need not find that William acted with bad intent toward Crulls to conclude that the debt was excepted from discharge under § 523(a)(4). The Supreme Court's recent decision in <u>Bullock</u> overrules prior Ninth Circuit authority allowing such a conclusion. Therefore, at best, a remand to the bankruptcy court would be required to examine William's intent under the <u>Bullock</u> standard.

However, in this case, no remand is necessary because we conclude that the bankruptcy court erred when it decided that a partnership existed between Crulls and CWDP based on the Loan Agreement. Since no partnership was created, and no fiduciary duty existed, we REVERSE the decision of the bankruptcy court excepting William's debt to Crulls from discharge under § 523(a)(4).

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United States Court of Appeals,
Third Circuit.
In re **ABC LEARNING** CENTRES LIMITED, n/k/a ZYX Learning Centres Limited; A.B.C. USA Holdings Pty Ltd, Debtors in Foreign Proceedings
RCS Capital Development, LLC, Appellant.

No. 12–2808.
Argued: March 5, 2013.
Filed: Aug. 27, 2013.

Background: Foreign liquidators petitioned for recognition, as foreign main or foreign non-main proceeding, a voluntary winding-up of corporate entities under the Corporations Act of Australia. The Bankruptcy Court, Kevin Gross, J., 445 B.R. 318, granted petition and entered order staying actions against debtor and its property in United States but granted limited relief to unsecured creditor. Creditor appealed. The United States District Court for the District of Delaware, Richard G. Andrews, J., affirmed. Creditor appealed.

Holdings: The Court of Appeals, Scirica, Circuit Judge, held that:
(1) voluntary winding-up of corporate entities under Corporations Act of Australia was in nature of collective proceeding;
(2) Australian law that allowed secured creditors to realize full value of their debts, and tender excess to company, did not manifestly contravene public policy of United States; and
(3) foreign corporation retained equitable interests in its fully leveraged property that was located in United States, and thus it had to be considered "property of the debtor."

Affirmed.

West Headnotes

[1] Bankruptcy 51 3782

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3782 k. Conclusions of Law; De Novo Review. Most Cited Cases

Bankruptcy 51 3836

51 Bankruptcy
51XIX Review
51XIX(D) Review of District Court
51k3836 k. Review. Most Cited Cases

The Court of Appeals reviews the legal standards applied by the district court and the bankruptcy court de novo.

[2] Bankruptcy 51 2341

51 Bankruptcy
51III The Case
51III(H) Cases Ancillary to Foreign Proceedings
51k2341 k. In General. Most Cited Cases

Voluntary winding-up of corporate entities under Corporations Act of Australia was in nature of collective proceeding, which was necessary prerequisite for recognition thereof as "foreign main proceeding" under Chapter 15 of Bankruptcy Code, since liquidator had to distribute assets on pro-rata basis to creditors of same priority; although debtor's assets were entirely leveraged which left nothing to distribute to unsecured creditors, there was no exception to recognition based on debt to value ratio at time of insolvency. 11 U.S.C.A. § 1517(a).

[3] Bankruptcy 51 🔑2341

51 Bankruptcy
51III The Case
51III(H) Cases Ancillary to Foreign Proceedings
51k2341 k. In General. Most Cited Cases

Australian law that allowed secured creditors to realize full value of their debts, and tender excess to debtor, did not manifestly contravene public policy of United States, and thus public policy exception did not apply to recognition of liquidation proceeding which was pending against foreign corporation in Australia as foreign main proceeding that would trigger automatic stay; although secured creditors in United States generally had to turn over assets and seek distribution from bankruptcy estate, Australian law established different way to achieve similar goals. 11 U.S.C.A. §§ 362(a), 1506.

[4] Bankruptcy 51 🔑2341

51 Bankruptcy
51III The Case
51III(H) Cases Ancillary to Foreign Proceedings
51k2341 k. In General. Most Cited Cases

Foreign corporation in Australia retained equitable interests in its fully leveraged property that was located in United States, and thus it had to be considered “property of the debtor” and subject to automatic stay under Chapter 15 of Bankruptcy Code, since receiver had to repay any amount of realized assets in excess of value of the charges to that corporation, corporation retained right to redeem encumbered property, and liquidator could challenge charges receiver claimed on company assets, and if charges were found invalid, corporation would retain encumbered property. 11 U.S.C.A. §§ 362(a), 1520(a).

[5] Bankruptcy 51 🔑2341

51 Bankruptcy
51III The Case
51III(H) Cases Ancillary to Foreign Proceedings
51k2341 k. In General. Most Cited Cases

A court does not create a separate bankruptcy estate under the portion of the Bankruptcy Code that requires United States bankruptcy courts to recognize a foreign insolvency proceeding; the law provides for an ancillary proceeding so the foreign representative does not need to file a new bankruptcy action in the United States. 11 U.S.C.A. § 1501 et seq.

[6] Bankruptcy 51 🔑2532

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)1 In General
51k2532 k. Interest of Debtor in General. Most Cited Cases

Bankruptcy 51 🔑2543

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2543 k. Property Held by Debtor as Trustee, Agent, or Bailee. Most Cited Cases

Property rights the debtor does not have do not become part of the bankruptcy estate, such as secondary mortgages and assets the debtor holds in trust for a non-debtor. 11 U.S.C.A. § 541(d).

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Before: SCIRICA, JORDAN, and ROTH, Circuit Judges.

OPINION OF THE COURT

SCIRICA, Circuit Judge.

***1** RCS Capital Development LLC appeals from an order of recognition of an Australian insolvency proceeding under Chapter 15 of the Bankruptcy Code, and an order staying actions against the debtor, ABC Learning Centres, and its property in the United States. We must determine whether the Australian insolvency proceeding should be recognized as a foreign main proceeding under Chapter 15 of the Bankruptcy Code, and whether the debtor's fully-encumbered property in the United States is subject to the automatic stay under 11 U.S.C. § 1520.

I.

ABC Learning Centres Ltd. is a publicly-traded Australian company that provided child care and educational services in Australia, the United States and other countries through its 38 subsidiaries. It conducted business in the United States principally through its subsidiaries, ABC Developmental Learning Centres (USA) Inc. (ABC Delaware) and the Learning Care Group. In June 2008, RCS Capital Development LLC contracted with ABC Delaware to develop child care facilities in the United States, and ABC guaranteed ABC Delaware's loan obligations. RCS won a $47 million verdict on a breach of contract claim against ABC Delaware in Arizona state court on May 14, 2010. RCS is a defendant to a Nevada lawsuit brought by ABC Learning and ABC Delaware, seeking $30 million.

In November 2008 ABC's directors entered into Voluntary Administration in Australia, and appointed administrators to determine whether ABC could be restructured to address its insolvency, or whether it had to be liquidated. [FN1] Entering into Voluntary Administration breached ABC's loan agreements with its secured creditors. This breach triggered the secured creditors' rights to realize their assets through the receivership process prescribed by Australia's Corporations Act. Corporations Act 2001 § 554E(3) (Austl.) (hereinafter "Corporations Act"). The secured creditors exercised that right and appointed a receiver. ABC was entirely leveraged, so the value of all its assets was encumbered by its secured creditors' charges.[FN2]

ABC's directors voted to enter liquidation proceedings on June 2, 2010, and appointed two of the administrators as the liquidators to wind up the company. The receivership continued through the commencement of liquidation proceedings, and operated in tandem with the winding up. ABC's liquidators granted the receiver permission to manage and operate ABC. A liquidator realizes assets for the benefit of all the creditors, investigates charges claimed by the secured creditors, takes an accounting and payment of the value of assets the receiver realized beyond the amount of the debenture, and distributes assets on a pro rata basis among creditors of the same priority.

On May 26, 2010, the administrators-turned-liquidators petitioned the Bankruptcy Court of Delaware as ABC's foreign representatives for recognition of the Australian insolvency proceedings under Chapter 15 of the Bankruptcy Code. The petition was filed before the Arizona verdict was rendered into judgment, and the immediate focus of the stay was ABC's suit against RCS in Nevada state court. The Bankruptcy Court found the liquidation was a foreign main proceeding that met the recognition requirements and did not manifestly contravene U.S. public policy. The Bankruptcy Court ordered recognition and an automatic stay of actions against ABC and ABC's property within the United States' jurisdiction. The Bankruptcy Court granted RCS's motion to lift the stay for the purpose of rendering its Arizona verdict to judgment, and applying the judgment against the Nevada action. The District Court of Delaware upheld the Bankruptcy Court's orders, noting that RCS was granted all the relief it initially sought. RCS appeals from the District Court's order.

II. [FN3]

***2** [1] Congress created Chapter 15 of the Bankruptcy Code in Title VIII of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. 11 U.S.C. § 1501 *et seq.* Under Chapter 15, U.S. bankruptcy courts must recognize a foreign insolvency proceeding when it is "a collective judicial or administrative proceeding in a foreign country ... under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation." 11 U.S.C. § 101(23); *id.* § 1517(a).[FN4] The statute requires recognition when the foreign proceeding meets the requirements of section 1502. *Id.* § 1517(a). "Upon recognition of a foreign [main] proceeding ... sections 361 and 362 apply with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States." *Id.* § 1520(a)(1). Section 362 stays "the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title." *Id.* § 362(a)(2).

Congress enacted Chapter 15 to provide effective mechanisms for dealing with cases of cross-border insolvency with the following objectives:

(1) cooperation between ... courts of the United States, ... and the courts and other competent authorities of foreign countries involved in cross-border insolvency cases;

(2) greater legal certainty for trade and investment;

(3) fair and efficient administration of cross-border insolvencies that protects the interests of all creditors, and other interested entities, including the debtor;

(4) protection and maximization of the value of the debtor's assets; and

(5) facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment.

11 U.S.C. § 1501; *see also* UNCITRAL Model Law on Cross–Border Insolvency preamble (stating nearly identical purposes). "Title VIII is intended to provide greater legal certainty for trade and investment as well as to provide for the fair and efficient administration of cross-border insolvencies, which protects the interests of creditors and other interested parties, including the debtor. In addition, it serves to protect and maximize the value of the debtor's assets." H.R.Rep. No. 109–31(1), at 105 *reprinted in* 2005 U.S.C.C.A.N. 88, 169 (2005). The statute adopts, nearly in its entirety, the Model Law on Cross–Border Insolvency promulgated in 1997 by the United Nations Commission on International Trade Law (UNCITRAL). *Id.*

UNCITRAL developed the Model Law on Transnational Insolvency in response to the challenges of multinational bankruptcies where multiple insolvency regimes lacked effective mechanisms for coordination. Multiple systems limited the ability of

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any one bankruptcy regime to protect assets against dissipation, and allowed creditors to skip ahead of their priority by seizing assets in foreign jurisdictions. The UNCITRAL Legislative Guide explains the Model Law was designed to address

> ***3** inadequate and inharmonious legal approaches, which hamper the rescue of financially troubled businesses, are not conducive to a fair and efficient administration of cross-border insolvencies, impede the protection of the assets of the insolvent debtor against dissipation and hinder maximization of the value of those assets. Moreover, the absence of predictability in the handling of cross-border insolvency cases impedes capital flow and is a disincentive to cross-border investment.... Fraud by insolvent debtors, in particular by concealing assets or transferring them to foreign jurisdictions, is an increasing problem, in terms of both its frequency and its magnitude.

U.N. Comm'n on Int'l Trade Law, UNCITRAL Legislative Guide on Insolvency Law, at 310, U.N. Sales No. E.05.V.10 (2005). Both the United States and Australia have adopted the Model Law.

The American Law Institute's Global Principles for Cooperation in International Insolvency Cases elaborates "the overriding objective [is to] enable[ ] courts and insolvency administrators to operate effectively and efficiently in international insolvency cases with the goals of maximizing the value of the debtor's global assets, preserving where appropriate the debtors' business, and furthering the just administration of the proceeding." American Law Institute, Global Principles for Cooperation in Int'l Insolvency Cases 1.1 (2012).[FN5] "[T]he emphasis must be on ensuring that the insolvency administrator, appointed in that proceeding, is accorded every possible assistance to take control of all assets of the debtor that are located in other jurisdictions." *Id.* at cmt. to Global Principle 24. Chapter 15 creates an ancillary proceeding in the United States to provide support to the foreign insolvency administrator. Jay Lawrence Westbrook, *Chapter 15 at Last*, 79 Am. Bankr.L.J. 713, 726 (2005). The goal is to direct creditors and assets to the foreign main proceeding for orderly and fair distribution of assets, avoiding the seizure of assets by creditors operating outside the jurisdiction of the foreign main proceeding.

The Model Law reflects a universalism approach to transnational insolvency. It treats the multinational bankruptcy as a single process in the foreign main proceeding, with other courts assisting in that single proceeding. Westbrook, *supra*, at 715. In contrast, under a territorialism approach a debtor must initiate insolvency actions in each country where its property is found. *Id.* This approach is the so-called "grab rule" where each country seizes assets and distributes them according to each country's insolvency proceedings. *Id.; see also* Andrew T. Guzman, *International Bankruptcy: In Defense of Universalism*, 98 Mich. L.Rev. 2177, 2179 (2000).

Chapter 15 embraces the universalism approach. The ancillary nature of Chapter 15 proceedings "emphasizes the United States policy in favor of a general rule" that our courts "act ... in aid of the main proceedings, in preference to a system of full bankruptcies ... in each state where assets are found." H.R.Rep. No. 109–31(1), at 109 (2005) *reprinted in* 2005 U.S.C.C.A.N. 88, 171. Congress rejected the territorialism approach, the "system of full bankruptcies," in favor of aiding one main proceeding. *Id.* "The purpose is to maximize assistance to the foreign court conducting the main proceeding." *In re Fairfield Sentry Ltd. Litig.*, 458 B.R. 665, 678–79 (S.D.N.Y.2011) (citing *In re Condor Ins. Ltd.*, 601 F.3d 319, 329 (5th Cir.2010)). "Thus, a Chapter 15 court in the United States acts as an adjunct or arm of a foreign bankruptcy court where the main proceedings are conducted." *Id.*

***4** Chapter 15 supplanted Section 304 of the Bankruptcy Code, which authorized courts to stay

U.S. actions against companies or property subject to a foreign insolvency proceeding. 11 U.S.C. § 304 (2000) (*repealed by* Pub.L. 109–8. Title VIII, § 802(d)(3) (2005)). Section 304 relief was largely discretionary. *See In re Treco,* 240 F.3d 148, 155 (2d Cir.2001) (explaining that Section 304 "by its terms requires an exercise of judicial discretion"). Chapter 15 improved predictability by mandating recognition when a foreign proceeding meets Section 1517 recognition requirements. Leif M. Clark, *Ancillary and Other Cross–Border Insolvency Cases Under Chapter 15 of the Bankruptcy Code* 10–11 (2008). Before the Model Law, many countries did not assist U.S. insolvency proceedings, even though the United States opened its courts to foreign representatives. *In re Condor Ins., Ltd.,* 601 F.3d 319, 321–22 (5th Cir.2010). One of the reasons Congress changed so little of the wording in the Model Law was to endorse it wholesale, and encourage wide adoption by other nations. Westbrook, *supra,* at 719. Mandatory recognition when an insolvency proceeding meets the criteria fosters comity and predictability, and benefits bankruptcy proceedings in the United States that seek to administer property located in foreign countries that have adopted the Model Law.

Chapter 15 also encourages communication and cooperation with foreign courts, and authorizes our courts to communicate directly with foreign courts. 11 U.S.C. § 1525. Foreign representatives can access U.S. courts to request enforcement of orders of the foreign proceeding and to stay actions against foreign debtors' property in the United States. *Id.* §§ 1509, 1520, 1521. Chapter 15 ancillary proceedings bring people and property beyond the foreign main proceeding's jurisdiction into the foreign main proceeding through the exercise of the United States' jurisdiction.

A.

In Australia a company's directors may determine the company is insolvent and initiate liquidation proceedings. Corporations Act § 436A. Here, ABC went into Voluntary Administration, where the appointed administrators determined whether the company was salvageable. *Id.* § 438A. In this case, the administrators decided ABC should be liquidated, and two of the administrators became the liquidators, responsible for collecting and distributing the company's assets to the company's creditors. *Id.* ss 478, 556; Australian Sec. & Invest. Comm'n., *Liquidation: A Guide for Creditors* 2 (2012) *available at* www.asic.gov.au. Only unsecured creditors are barred from initiating or continuing legal proceedings against the company. Corporations Act § 471B–C. Secured creditors have their own proceeding where they may appoint a receiver to realize the secured assets, and distribute the proceeds to satisfy the debts that the property secured. *Id.* § 420.

Receivership can function in tandem with liquidation. *Id.* § 420C(1). Secured creditors may elect to surrender the secured assets to the liquidator, and receive distribution through the liquidation proceeding, or appoint a receiver to realize the assets. *Id.* § 554E(3). The receiver represents the interest of secured creditors, whereas the liquidator represents the interests of all the creditors. *Id.* § 420. The receiver's only duty to unsecured creditors is to sell the assets for a fair price. *Id.* § 420A. But the receiver does not operate entirely independently from the liquidator. The liquidator has authority to review the appointment of the receiver, and monitor the progress of the receivership. Australian Sec. & Invest. Comm'n., *Receivership: A Guide for Creditors* 4 (2008) *available at* www.asic.gov.au [hereinafter *Receivership*]. The receiver must pay to the company any amount realized above the amount of debt owed to the secured creditors.[FN6] *Id.* at 2; Corporations Act § 441EA. The liquidator investigates the charges claimed by secured creditors, and may challenge asserted charges. *Receivership, supra,* at 4. The liquidator may also grant permission to the receiver to operate and manage the company while the liquidator proceeds with winding up the company. Corporations Act § 420C(1)(a).

B.

***5** [2] Under Chapter 15 "an order recognizing a foreign proceeding shall be entered if ... such foreign proceeding for which recognition is sought is a foreign main proceeding" and the petition meets the administrative requirements of Section 1515. 11 U.S.C. § 1517(a). " '[F]oreign main proceeding' means a foreign proceeding pending in the country where the debtor has the center of its main interests." *Id.* § 1502(4).

> The term "foreign proceeding" means a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.

Id. § 101(23). This definition can be broken down into seven elements: (i) a proceeding; (ii) that is either judicial or administrative; (iii) that is collective in nature; (iv) that is in a foreign country; (v) that is authorized or conducted under a law related to insolvency or the adjustment of debts; (vi) in which the debtor's assets and affairs are subject to the control or supervision of a foreign court; and (vii) which proceeding is for the purpose of reorganization or liquidation.

The Bankruptcy Court in this case thoroughly evaluated these elements and found they were met. RCS does not challenge that ABC has met the Section 1515 administrative requirements, nor that the liquidation is an administrative proceeding in a foreign country for the purpose of liquidation, authorized under a law which relates to insolvency, and is subject to the supervision or control of Australian courts. The only other U.S. court that has considered Australian liquidation found it was a foreign main proceeding. *In re Betcorp Ltd.*, 400 B.R. 266, 285 (Bankr.D.Nev.2009).

The Bankruptcy Court recognized the liquidation proceeding as the foreign main proceeding. RCS acknowledges that the liquidation is a collective proceeding, because the liquidator must consider the rights of all the creditors in distributing assets, and must distribute assets according to priorities on a pro rata basis. In this case, the practical effect of the receivership leaves little for the liquidator to administer, aside from investigating the charges claimed by the secured creditors.

RCS contends that only the receivership benefits from Chapter 15 recognition, so that only the receivership was effectively granted Chapter 15 recognition. The receivership is not a collective proceeding, because the receiver only represents the interests of the secured creditors. At oral argument, RCS conceded that an Australian liquidation proceeding operating parallel to a receivership could be granted Chapter 15 recognition "in a case where the secured creditors only have a portion of the assets." Oral Argument at 29:24, Mar. 5, 2013. Nevertheless, RCS asserts the receivership dominates the liquidation proceeding in this case because ABC's assets are entirely leveraged, leaving nothing for the liquidator to distribute to the unsecured creditors. But that does not affect the collective nature of the Australian liquidation proceeding. Instead, it turns on the particular facts of ABC's debts.

***6** Chapter 15 makes no exceptions when a debtor's assets are fully leveraged. Subject to the public policy exception, Chapter 15 recognition must be ordered when a court finds the requisite criteria are met,[FN7] replacing the Section 304 list of guiding principles.[FN8] We do not find any exception to recognition based on the debtor's debt to value ratio at the time of insolvency. Moreover, we find such an exception could contravene the stated purposes of Chapter 15 and the mandatory language of Chapter

15 recognition.

C.

[3] "Nothing in [Chapter 15] prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States." 11 U.S.C. § 1506. RCS contends we should not recognize the liquidation proceeding or uphold the stay, because the receivership would gain all the benefits of the ordered relief, and because it is a non-collective proceeding which contravenes our public policy in favor of collective insolvency proceedings.

The public policy exception has been narrowly construed, because the "word 'manifestly' in international usage restricts the public policy exception to the most fundamental policies of the United States." H.R.Rep. No. 109–31(1), at 109 (2005) *reprinted in* U.S.C.C.A.N. 88, 172; *see also In re Ephedra Prods. Liab. Litig.*, 349 B.R. 333, 336 (S.D.N.Y.2006) (explaining why the exception is a narrow one). "The purpose of the expression 'manifestly', ... is to emphasize that public policy exceptions should be interpreted restrictively and that [the exception] is only intended to be invoked under exceptional circumstances concerning matters of fundamental importance for the enacting State." U.N. Comm'n on Int'l Trade Law, *Guide to Enactment of the UNCITRAL Model Law on Cross–Border Insolvency,* ¶ 89, U.N. Doc A/CN.9/442 (1997).

The public policy exception applies "where the procedural fairness of the foreign proceeding is in doubt or cannot be cured by the adoption of additional protections" or where recognition "would impinge severely a U.S. constitutional or statutory right." *In re Qimonda AG Bankr. Litig.*, 433 B.R. 547, 570 (E.D.Va.2010). An Israeli insolvency proceeding was found to be manifestly contrary to public policy in *In re Gold & Honey, Ltd.*, because the receivership initiated in Israel after Chapter 11 proceeding began in the U.S. seized the debtor's assets, violating the bankruptcy court's stay order. 410 B.R. 357, 371–72 (Bankr.E.D.N.Y.2009). This conduct hindered two fundamental policy objectives of the automatic stay: "preventing one creditor from obtaining an advantage over other creditors, and providing for the efficient and orderly distribution of a debtor's assets to all creditors in accordance with their relative priorities." *Id.* at 372 (discussing "serious ramifications" if future creditors followed suit and seized assets under a United States court's jurisdiction in violation of its orders). In *In re Ephedra Prods.* a Canadian insolvency proceeding was challenged under the public policy exception because it did not afford a right to a jury trial. 349 B.R. at 335. Despite our constitutional right to a jury, Canada's lack of a right to a jury trial did not contravene a fundamental policy because the Canada proceedings afforded substantive and procedural due process protections, and "nothing more is required by § 1506 or any other law." *Id.* at 337.

***7** The collective proceeding requirement reflects U.S. policy " 'to provide an orderly liquidation procedure under which all creditors are treated equally.' " *In re Schimmelpenninck*, 183 F.3d 347, 351 (5th Cir.1999) (quoting H.R.Rep. No. 95–595, 1st Sess., at 340 (1977)) ("Ultimately, the interests of all creditors, foreign and domestic, are to be put on a level playing field, with like-situated claimants being treated equally."). It is undisputed that the Australian liquidation proceeding is a collective proceeding. The liquidator must distribute assets on a pro-rata basis to creditors of the same priority. Secured creditors are entitled to recover the full value of their debts by realizing the value of the assets securing those debts and submitting an accounting to the liquidator.

Rather than contravene public policy, recognition advances the policies that animate the collective proceeding requirement. RCS seeks to attach assets before the secured creditors can realize them. Without Chapter 15 recognition, RCS could skip ahead of the priorities of the secured creditors. At oral argument, RCS contended this was fair to the other unse-

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cured creditors, because they too could bring suits in the United States to attach ABC's assets. Oral Argument at 29:54, Mar. 5, 2013. RCS's approach would eviscerate the orderly liquidation proceeding, and ignores all priority of debts. Efficient, orderly and fair distribution are not only the policies behind the collective proceeding requirement, but are some of the "chief purpose[s] of the bankruptcy laws." H.R. Rep. 95–595 1st Sess., at 345 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6006 n.380; *Katchen v. Landy*, 382 U.S. 323, 328, 86 S.Ct. 467, 15 L.Ed.2d 391 (1966). Without bankruptcy proceedings, creditors would race to the courthouse to collect from a troubled entity, depleting assets and enabling some creditors to collect fully on the debts and others not at all, and with no regard for priority. Accordingly, it would contravene our policy "to provide an orderly liquidation procedure under which all creditors are treated equally" if RCS could evade collecting its debt through the Australian liquidation proceeding.

Moreover, we are unconvinced the Australian insolvency proceeding conflicts with our own rules. The United States Bankruptcy Code prioritizes secured creditors, as does Australia's Corporations Act. 4 *Collier on Bankruptcy* ¶ 506.02 (16th ed.2013). Several courts have refused to turn over assets under Section 304 to foreign insolvency proceedings that did not prioritize secured creditors. *In re Treco*, 240 F.3d 148, 159–60 (2d Cir.2001) (refusing to turn over assets to a Bahamian liquidation proceeding because it prioritized administrative expenses over secured creditors, and summarizing other cases denying turnover because the foreign proceeding failed to sufficiently protect prioritized secured interests). The sole difference here is that Australian law allows secured creditors to realize the full value of their debts, and tender the excess to the company, whereas secured creditors in the United States must generally turn over assets and seek distribution from the bankruptcy estate.

***8** The Dutch bankruptcy system also exempts secured creditors from surrendering their interests to the liquidation process. *In re Schimmelpenninck*, 183 F.3d at 352. The Court of Appeals for the Fifth Circuit reviewed the Dutch proceedings under the precursor to Chapter 15, Section 304. *Id.* at 351. To enjoin actions against a foreign debtor's property, Section 304 required the estate to be distributed in manner substantially similar to Chapter 11 preferences. *Id.* at 365. The Fifth Circuit found the Dutch proceeding distributed assets in a manner "substantially in accordance with Title 11" even though it allowed a secured creditor who "holds either a mortgage or a pledge encumbering that asset [to] exercise his rights irrespective of the authority of the Curator." *Id.* ("Dutch bankruptcy law clearly is not repugnant to Title 11...."). The court further found if the unsecured creditor was permitted to bring suit he would "unjustly gain a first-come/first-served preference, [and] the remaining creditors ... would suffer a concomitant disadvantage" which "would oppugn the very equitable foundation on which bankruptcy is built." *Id.* at 351–52.

Australia's Corporations Act prioritizes secured creditors with a mechanism similar to the Dutch bankruptcy regime, both allowing independent enforcement of secured interests outside the insolvency proceeding. Despite the different method chosen to create the priority, the Fifth Circuit found the Dutch proceeding was not "repugnant to [U.S.] laws and policies." *Id.* at 365 (finding "sufficient congruity between Dutch and American bankruptcy laws to eschew such repugnance"). The Australian legislators selected a different method to prioritize secured creditors. Rather than manifestly contravene our policy, Australian law established a different way to achieve similar goals. Recognition of the Australian liquidation proceeding does not manifestly contravene public policy. On the contrary, allowing RCS to use U.S. courts to circumvent the Australian liquidation proceedings would undermine the core bankruptcy policies of ordered proceedings and equal treatment.

D.

[4] Upon recognition of the foreign main proceeding, the automatic stay under Section 362 applies to multinational bankruptcies "with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States." 11 U.S.C. § 1520(a). Section 362 provides for an automatic stay of actions "against the debtor or against property of the estate." 11 U.S.C. § 362(a).[FN9] RCS seeks to enforce its state court verdict against ABC property located in the United States. RCS contends the secured creditors, not ABC, effectively own the property because the property is entirely leveraged, and the receiver has the right to use and dispose of those assets at its discretion. But the secured creditors' equitable interest in the property does not resolve the question of ABC's equitable interests.

***9** RCS contends ABC's assets in the United States are not "property of the debtor" because ABC only holds bare legal title to those assets. This argument is based on the premise that ABC does not hold any equitable interest in its encumbered property because it is entirely leveraged.

We find ABC does retain equitable interest in its encumbered property. First, the receiver must repay any amount of the realized assets in excess of the value of the charges to ABC. Corporations Act § 554H. Second, ABC retains the right to redeem the encumbered property. *Id.* § 554F. Third, the liquidator may challenge the charges the receiver claims on company assets, and if the charges were found invalid, ABC would retain the encumbered property. *Receivership, supra* at 4. Since ABC retains equitable interests in its property, it is "property of the debtor" and is subject to the automatic stay under Section 1520(a).

1.

[5] "The Bankruptcy Code does not define 'property of the debtor.' " *Begier v. I.R.S.,* 496 U.S. 53, 58, 110 S.Ct. 2258, 110 L.Ed.2d 46 (1990). Outside of the Chapter 15 context, the Supreme Court has looked to Section 541 defining "property of the estate" to interpret "property of the debtor." *Id.* ("[T]he term 'property of the debtor' ... is best understood as that property that would have been part of the estate had it not been transferred before the commencement of bankruptcy proceedings."). But under Chapter 15 a court does not create a separate bankruptcy estate. *In re Condor Ins. Ltd.,* 601 F.3d 319, 327 (5th Cir.2010). Chapter 15 provides for an ancillary proceeding so the foreign representative does not need to file a new bankruptcy action in the United States. *Id.* at 320–21 (citing Clark, *supra,* at 35). Accordingly, courts interpreting Chapter 15 have not found Section 541 relevant to defining "property of the debtor." *In re Qimonda AG,* 482 B.R. 879, 887 (Bankr.E.D.Va.2012) ("Upon recognition of a foreign main proceeding, an estate is not created, as Section 541 of the Bankruptcy Code is not among the enumerated Sections of the Bankruptcy Code that become operative upon recognition under Section 1520."); *In re Lee,* 472 B.R. 156, 178 (Bankr.D.Mass.2012) ("[N]either section 541(a) nor 541(c)(1) are applicable to a determination of property of the Hong Kong bankruptcy estates, and the determination of property of the estates must be made under Hong Kong law."); *In re Atlas Shipping A/S,* 404 B.R. 726, 739 (Bankr.S.D.N.Y.2009) ("The statute refers to 'property of the debtor' to distinguish it from the 'property of the estate' that is created under § 541(a)."). On these facts, we need not decide whether Section 541 defines "property of the debtor." Here, ABC's property rights under Australia's Corporations Act would inform an application of Section 541(d). Under Australian law ABC holds several equitable interests in the property. Accordingly, even if we applied Section 541 to define "property of the debtor," Section 541(d) would not exclude ABC's property in the United States from a bankruptcy estate.

2.

***10** RCS contends ABC's assets in the United

States are not property of the debtor because Section 541 defining "property of the estate" excludes assets in which the debtor holds empty title alone and no equity. RCS asserts ABC holds bare legal title alone because the full value of the assets are leveraged, and the receiver may use or dispose of the assets at will for the benefit of the secured creditors.FN10

[6] Section 541 defines "property of the estate" as "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541. Section 541(d) excludes property in which the debtor only holds legal title from the debtor's estate. 11 U.S.C. § 541(d). Section 541(d) provides:

> Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

11 U.S.C. § 541(d). This provision stands for the unremarkable proposition that property rights the debtor does not have do not become part of the bankruptcy estate. *See Matter of Cont'l Airlines, Inc.,* 134 B.R. 536, 541 (Bankr.D.Del.1991); 124 Cong.Rec. H11096 (daily ed. Sept. 28, 1978) (statement of Congressman Edwards) ("To the extent that such an interest is limited in the hands of the debtor, it is equally limited in the hands of the estate...."). It pertains to property such as secondary mortgages and assets the debtor holds in trust for a non-debtor. 5 *Collier on Bankruptcy* ¶ 541.29; *City of Farrell v. Sharon Steel Corp.,* 41 F.3d 92, 96 (3d Cir.1994) (finding the debtor held employee income tax withholdings in a trust, and it was not property of the estate); *Cont'l Airlines, Inc.,* 134 B.R. at 541–42 ("Section 541(d) was enacted to protect the secondary mortgage market but has been read expansively to include express and constructive trusts as well." (citation omitted)). Section 541(d) "reiterates the general principle that where the debtor holds bare legal title without any equitable interest, ... the estate acquires bare legal title without any equitable interest in the property." 124 Cong. Rec. 33999 (1978) (remarks of Sen. DeConcini).

RCS further contends that under Australia's Corporation's Act ABC does not hold any equitable interest in its fully-leveraged property. The only authority RCS cites for this proposition is a treatise on Australian insolvency law, stating "[t]he major practical effect of [debt] crystallization is that the debenture holder is given equitable interest in the property secured, which revokes the company's power to deal with such assets in the ordinary course of business." Michael Murray, *Australian Insolvency Management Pract.* ¶ 65–500(CCH). A floating charge crystallizes and becomes a fixed charge upon default or appointment of a receiver.FN11 In this case there is no question the receiver has the power to operate and manage ABC, and to use and dispose of its encumbered assets. The question is whether the receiver's control over the assets divests ABC of all equitable interests in them.

***11** Although the full value of ABC's assets are leveraged, ABC nevertheless holds several important equitable interests in its property. First, it has the right to surplus proceeds from the sale of the encumbered assets. In *United States v. Whiting Pools* the Supreme Court held assets the IRS seized to enforce its lien were part of the debtor's estate. 462 U.S. 198, 210, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983). The IRS was authorized to seize and sell property belonging to the debtor to satisfy the lien imposed on that property, and took physical possession of the assets before the debtor filed for bankruptcy. *Id.* at 211, 103 S.Ct.

2309. The Court held the property was property of the estate, in part, because the IRS was obligated to return to the debtor any proceeds from the sale that exceeded the value of the lien. *Id.* In *Whiting* it was unlikely there would be any surplus because the debt owed to the IRS was $92,000, but the liquidation value of the property seized was only $35,000. *Id.* at 200, 103 S.Ct. 2309. Even though the IRS held an equitable interest in and a right to possess the property, "[o]wnership of the property is transferred only when the property is sold to a bona fide purchaser at a tax sale." *Id.* at 211, 103 S.Ct. 2309.

The same obligation to pay any surplus from the sale of assets exists under Australia's Corporations Act. The receiver must pay to the company any proceeds from the sale of assets that exceed the value of the charge. *Receivership, supra,* at 2; Corporations Act § 441EA. Although both parties agree there will be no surplus from the sale of the assets, that same circumstance did not change the Supreme Court's analysis in *Whiting Pools*. Since the IRS's lien and control over the debtor's assets were insufficient to deprive the debtor of all equitable interests in *Whiting Pools*, the same would appear to be true of the charges and control over ABC's assets before they are sold. Since the receiver did not sell ABC's assets in the United States, under U.S. bankruptcy law, the assets would be property of the estate and subject to the automatic stay under Section 362.[FN12]

Second, ABC retains the right of redemption under Australia's Corporations Act. Corporations Act § 554F(2) ("The liquidator may, at any time, redeem the security interest on payment to the creditor of the amount of the creditor's estimate of its value."). U.S. bankruptcy courts consistently recognize the right of redemption as an equitable interest in property, which must be turned over to the debtor's estate. *In re Moffett,* 356 F.3d 518, 521–22 (4th Cir.2004); *Charles R. Hall Motors, Inc. v. Lewis,* 137 F.3d 1280, 1284–85 (11th Cir.1998); 5 *Collier on Bankruptcy* ¶ 541.05. We also find ABC's right of redemption is an equitable interest. Accordingly, Section 541(d) does not exclude ABC's property in the United States from "property of the debtor" because ABC holds more than bare legal title to the property. Since ABC's assets in the United States are "property of the debtor" they are subject to the automatic stay under 11 U.S.C. § 1520.

III.

***12** RCS could not enforce its judgment against ABC under either the U.S. or Australian insolvency regimes. RCS is an unsecured creditor. Under Australia's Corporation's Act, an unsecured creditor must recover its judgment against ABC through the liquidation proceeding. Under the U.S. Bankruptcy Code an unsecured creditor must seek to recover a judgment through the bankruptcy estate. Allowing an unsecured creditor to recover a judgment under these circumstances would require a hodgepodge of United States and Australian bankruptcy law. This is one of the outcomes Chapter 15 was designed to prevent by recognizing foreign main proceedings in United States courts.

For the foregoing reasons we will affirm the District Court's order affirming the Bankruptcy Court's order recognizing the Australian liquidation proceeding as a foreign main proceeding, and accompanying orders.

FN1. Insolvency proceedings under Australia's Corporations Act of 2001 may commence by appointing an administrator to determine the company's solvency.

FN2. Under Australian law, a charge is a security interest in property similar to a lien in the United States.

FN3. The Bankruptcy Court had jurisdiction under 11 U.S.C. § 105. The District Court had jurisdiction over the appeal from the

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Bankruptcy Court's final order under 28 U.S.C. § 158(a). We have jurisdiction over this appeal from the final order of the district court under 28 U.S.C. § 158(d). We review the legal standards applied by the district court and the bankruptcy court de novo. *In re DeSeno*, 17 F.3d 642, 643 (3d Cir.1994).

FN4. A foreign representative must petition for recognition, which shall be granted where the proceeding is pending in the country where the debtor has the center of its main interests (main) or where it has an establishment (nonmain), the foreign representative is a person or body, and where the petition meets § 1515 filing requirements. 11 U.S.C. § 1517(a).

FN5. The ALI principles "provide authority for resolution of a number of issues not fully addressed by Chapter 15 or addressed only in part." Jay Lawrence Westbrook, *Chapter 15 at Last*, 79 Am. Bankr.L.J. 713, 714 (2005).

FN6. The receiver may also prove to the liquidator it could not realize the value of all the secured creditors' charges through the secured assets, and seek the remainder from the liquidation process. Corporations Act § 554E(4).

FN7. Subject to section 1506, after notice and a hearing, an order recognizing a foreign proceeding shall be entered if—

(1) such foreign proceeding for which recognition is sought is a foreign main proceeding or foreign nonmain proceeding within the meaning of section 1502;

(2) the foreign representative applying for recognition is a person or body; and

(3) the petition meets the requirements of section 1515.

11 U.S.C. § 1517(a).

FN8. In determining whether to grant relief under subsection (b) of this section, the court shall be guided by what will best assure an economical and expeditious administration of such estate, consistent with—

(1) just treatment of all holders of claims against or interests in such estate;

(2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;

(3) prevention of preferential or fraudulent dispositions of property of such estate;

(4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

11 U.S.C. § 304 (2000) *repealed by* Pub.L. 109–8, Title VIII, § 802(d)(3) (2005).

FN9. Although the stay is generally automatic, a court may modify, terminate or condition the stay on request of a party. 11

U.S.C. § 362(d). In this case, the Bankruptcy Court modified the stay to allow RCS to bring its verdict to judgment.

FN10. The Bankruptcy Court's Stay Order appears to apply to the receiver as well. In order to realize ABC assets in the United States, the receiver must go through the liquidator as the foreign representative.

FN11. A floating charge is a debt secured by interchangeable property, such as stocks that may be purchased or sold frequently. A fixed charge encumbers a specific item of property. In this case the secured creditors already held fixed charges in addition to the floating charges that crystallized when ABC went into Voluntary Administration.

FN12. We note that this comparison is somewhat strained because secured creditors must surrender the assets securing their debts under U.S. bankruptcy law, but not under Australia's Corporations Act. This illustrates one of the challenges of using Section 541 to define “property of the debtor” in the Chapter 15 context.

C.A.3 (Del.),2013.
In re ABC Learning Centres Ltd.
--- F.3d ----, 2013 WL 4516820 (C.A.3 (Del.)), 58 Bankr.Ct.Dec. 91

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

IN RE: WILSHIRE COURTYARD,
Debtor,

WILSHIRE COURTYARD; JEROME H. SNYDER GROUP I, LTD.; LEWIS P. GEYSER REVOCABLE TRUST; GEYSER CHILDREN'S TRUST, FBO JENNIFER GEYSER, LEWIS P. GEYSER, TRUSTEE; WENDY K. SNYDER; JEROME H. SNYDER; GEYSER CHILDREN'S TRUST, FBO DANIEL GEYSER, LEWIS P. GEYSER, TRUSTEE; RUSSELL & RUTH KUBOVEC, DECEASED, KUBOVEC FAMILY TRUST, RITA FARMER, TRUSTEE; WILLIAM N. SNYDER; JOAN SNYDER; GEYSER CHILDREN'S TRUST, FBO DOUGLAS GEYSER, LEWIS P. GEYSER, TRUSTEE; LON J. SNYDER; SNYDER CHILDREN'S TRUST, FBO WILLIAM N. SNYDER, LEWIS P. GEYSER, TRUSTEE,
Appellants,

v.

CALIFORNIA FRANCHISE TAX BOARD,
Appellee.

No. 11-60065

BAP No. 10-1275

OPINION

Appeal from the Ninth Circuit
Bankruptcy Appellate Panel
Kirscher, Pappas, and Sargis, Bankruptcy Judges, Presiding

Argued and Submitted
March 6, 2013—Pasadena, California

Filed September 10, 2013

Before: Dorothy W. Nelson and Richard A. Paez Circuit Judges, and Suzanne B. Conlon, District Judge.*

Opinion by Judge Paez

SUMMARY**

Bankruptcy

Reversing the judgment of the Bankruptcy Appellate Panel, the panel held that the bankruptcy court had jurisdiction to reopen a bankruptcy proceeding to consider the tax consequences of the reorganization, pursuant to a chapter 11 plan, of the debtor, a general partnership that owned two commercial buildings in Los Angeles, into a limited liability company with a 1% ownership interest in the property.

* The Honorable Suzanne B. Conlon, District Judge for the U.S. District Court for the Northern District of Illinois, sitting by designation.

** This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

As part of the bankruptcy, over $200 million of partnership debt was forgiven, and the individual partners reported cancellation of debt income on their tax returns. The California Franchise Tax Board sought to assess $13 million in unpaid income taxes on the partners, characterizing the transaction as a disguised sale and the reported cancellation of debt income as capital gains. The reorganized LLC asked the bankruptcy court to reopen the case.

The panel agreed with the BAP that the bankruptcy court had neither "arising under" nor "arising in" subject matter jurisdiction over the dispute. But it disagreed with the BAP's holding that the bankruptcy court lacked post-confirmation "related to" jurisdiction. The panel reaffirmed that a "close nexus" exists between a post-confirmation matter and a closed bankruptcy proceeding sufficient to support jurisdiction when that matter affects the "interpretation, implementation, consummation, execution, or administration of the confirmed plan." The panel concluded that the ultimate merits question of the sale/non-sale attributes of the transaction depended in part on interpretation of the confirmed plan and confirmation order. In addition, the parties disputed the distinctly federal question of whether 11 U.S.C. § 346 (preempting state tax law) applies to non-debtor general partners of a debtor partnership that was dissolved as part of the reorganization. The panel also concluded that post-confirmation jurisdiction was consistent with the equitable objectives of the Bankruptcy Code.

Holding that the character of the core transaction of the debtor's bankruptcy was an issue that the bankruptcy court had jurisdiction to decide, the panel remanded the case to the BAP to determine in the first instance whether the bankruptcy court's answer to this question gave due consideration to the "economic realities" of the transaction as structured under the plan and confirmation order.

COUNSEL

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Howard E. Abrams, Atlanta, Georgia, for Amicus Curiae.

OPINION

PAEZ, Circuit Judge:

Spanning an entire city block on the "Miracle Mile" portion of Wilshire Boulevard in central Los Angeles are two commercial buildings at the center of a fifteen-year-old bankruptcy proceeding, eleven-year-old state tax dispute, and the present case about the scope of a bankruptcy court's post-confirmation subject matter jurisdiction. The buildings were owned by a California general partnership, Wilshire Courtyard, which filed for chapter 11 bankruptcy after defaulting on secured debt. As part of the bankruptcy, the partnership was reorganized into a limited liability company ("LLC") with a 1% ownership interest in the property, over $200 million of partnership debt was forgiven, and the individual partners reported cancellation of debt income on their tax returns. The California Franchise Tax Board ("CFTB") now wishes to assess $13 million in unpaid income taxes on the individual partners, characterizing the transaction as a disguised sale and the reported cancellation of debt income as capital gains.

In 2009, the reorganized LLC asked the bankruptcy court to reopen the case to protect the confirmed reorganization plan from CFTB's "collateral attack." The only question we must decide is whether the bankruptcy court had jurisdiction to reopen the bankruptcy proceeding. We hold that the bankruptcy court had jurisdiction, reverse the Bankruptcy Appellate Panel ("BAP"), and remand for further proceedings.

I. Background

As we do not address the merits of the underlying issue, we present an abridged version of the facts as recounted by the BAP. *See CFTB v. Wilshire Courtyard (In re Wilshire Courtyard)*, 459 B.R. 416, 419–23 (B.A.P. 9th Cir. 2011).

A. Events before reopening of the bankruptcy case

Wilshire Courtyard was a California general partnership ("Debtor" or "Wilshire Partnership") that developed and owned two commercial complexes on Wilshire Boulevard ("the Property"). After defaulting on its financing arrangements concerning the Property, amounting to almost

$350 million in secured debt, Debtor filed a chapter 11 bankruptcy petition in July 1997. *Id.* at 419. CFTB was listed in the creditor's matrix and received initial notice of the commencement of the bankruptcy proceeding. *Id.* The secured creditors, Debtor, and the individual non-debtor Wilshire partners ("Wilshire Partners") negotiated a Joint Plan of Reorganization ("Plan"). *Id.* As relevant here, Debtor was restructured from a California general partnership into a Delaware limited liability company ("Reorganized Wilshire") that continued to own and operate the Property. *Id.*[1] The senior secured creditors took a 99% ownership interest in Reorganized Wilshire, with the Wilshire Partners retaining the remaining 1%. *Id.* The senior secured creditors contributed $23 million to Reorganized Wilshire and released the secured indebtedness in exchange for the receipt of $100 million in new loan proceeds. *Id.* Debtor's disclosure statement, approved by the bankruptcy court in February 1998, did not address the state tax consequences for the Wilshire Partners and recommended that partners consult their own tax advisors. *Id.* The bankruptcy court confirmed the Plan on April 14, 1998 (the "Confirmation Order"), and closed the chapter 11 case in October 1998. *Id.* at 420.

After the Plan was confirmed, the various Wilshire Partners reported approximately $208 million in aggregate cancellation of debt income on their individual 1998 state tax returns. *Id.* In November 2002, CFTB audited the Wilshire Partnership and challenged the characterization of the tax consequences of the transactions in the Plan as cancellation of debt income. *Id.* CFTB took the position that the Wilshire

[1] According to the order confirming the Plan, "Wilshire Courtyard LLC and Reorganized Wilshire Courtyard are successors of the debtor for purposes of Bankruptcy Code sections 1123, 1129, and 1145."

Partnership and ultimately the individual partners should have reported $231 million in capital gain income because the Plan had effected a disguised sale of the Property. *Id.* In June 2004, CFTB issued notices of proposed assessments to individual partners totaling $13 million in unpaid state income taxes. *Id.* Although Wilshire Partners and CFTB engaged in several rounds of administrative hearings over the next five years, the administrative proceedings were suspended when Reorganized Wilshire sought relief in the bankruptcy court.

B. Bankruptcy court proceedings

In May 2009, Reorganized Wilshire filed a motion to reopen the bankruptcy case, arguing that CFTB was attempting to collaterally attack the confirmed Plan. *Id.* The bankruptcy court granted the motion, and ordered CFTB to show cause why it should not be held in contempt. *Id.* at 420–21. The bankruptcy court also ordered that the Wilshire Partners be joined as parties. *Id.* at 421. Reorganized Wilshire and the Wilshire Partners filed a joint motion for summary judgment asserting that the tax assessment was precluded by the Plan and Confirmation Order. *Id.* In response, CFTB argued that the bankruptcy court lacked subject matter jurisdiction to rule on the motion. *Id.*

Following hearings on the order to show cause and summary judgment motion, the bankruptcy court granted summary judgment to Reorganized Wilshire and the Wilshire Partners, and held that the terms of the confirmed plan also applied to the Wilshire Partners. *In re Wilshire Courtyard,* 437 B.R. 380 (Bankr. C.D. Cal. 2010). At the hearing, the bankruptcy court explained that a finding in the 1998

Confirmation Order ("Finding V")[2] meant that the transaction in the plan was not a sale for any purpose, and thus there was no gain to be taxed to the partnership. *See* 459 B.R. at 422. In its written opinion the bankruptcy court held that the "interests of the partners are wholly derivative from the status of the property in the partnership. In consequence, [CFTB] cannot recharacterize the plan transactions at the partner level without recharacterizing them at the partnership level as well." 437 B.R. at 383.

The bankruptcy court also ruled that it had subject matter jurisdiction for three reasons. *Id.* at 384. First, the bankruptcy court retained subject matter jurisdiction even post-confirmation because the case involved the interpretation of the confirmed Plan. *Id.* The bankruptcy court explained that the determination of income at the partnership level "requires interpretation of the plan and confirmation order." *Id.* Second, a bankruptcy court retains jurisdiction to interpret and enforce its own orders. *Id.* Third, CFTB's argument that the court did not have jurisdiction with respect to the non-debtor Wilshire Partners was unavailing because "this case involves income tax attributes at the individual partner level that derive directly from the plan confirmation order." *Id.* (citing *United*

[2] Finding V in the Confirmation Order reads: "The Joint Plan and the agreements, settlements, transactions and transfers contemplated thereby do not provide for, and when consummated will not constitute, the liquidation of all or substantially all of the property of the Debtor's Estate under Bankruptcy Code section 1141(d)(3)(A)." 459 B.R. at 422.

States v. Basye, 410 U.S. 441, 448 (1973)).[3] CFTB appealed to the BAP.

C. Bankruptcy Appellate Panel proceedings

The BAP reversed the bankruptcy court's jurisdictional ruling. *Id.* at 424–34. The BAP analyzed each prong of the statute prescribing the bankruptcy's court's jurisdiction, 28 U.S.C. § 1334(b): "the district courts [and by reference pursuant to 28 U.S.C. § 157, the bankruptcy courts] shall have original but not exclusive jurisdiction of all civil proceedings *arising under* title 11, or *arising in* or *related to* cases under title 11." *Id.* at 424 (emphasis added) (alteration in original).

The BAP reasoned that this case did not meet "arising under" or "arising in" jurisdiction because the right to relief sought in this case is not created by title 11: "No provision of the bankruptcy code dealing with the state tax consequences is at issue, nor were other chapter 11 provisions used by Wilshire in an attempt to restructure the tax consequences of plan confirmation. . . . [T]his contest is at bottom a tax dispute between the Wilshire Partners and CFTB arising under California state tax law, not the bankruptcy code." *Id.* at 425. The BAP also rejected the bankruptcy court's interpretation of Finding V—that no sale had occurred—as a basis for jurisdiction because the disclosure statement and Plan made "no mention of the 'sale/no-sale' attributes of the

[3] The bankruptcy court cited *Basye* for the proposition that "partnerships are individual taxable entities and conduits through which taxpaying obligations pass to individual partners," and thus that income character must be determined at the partnership level. 437 B.R. at 384 (citing 410 U.S. at 448).

property transfers, or of the state tax consequences to the Wilshire Partners." *Id.* at 424 n.11. The BAP interpreted § 1334(b)'s "arising in" provision as referring to causes of action which are not expressly rooted in the bankruptcy code but are "unique" to the bankruptcy process, have no "independent existence" outside of bankruptcy, and which cannot not be brought in another forum. *Id.* at 425 (citing *Battle Ground Plaza, LLC v. Ray (In re Ray)*, 624 F.3d 1124, 1131 (9th Cir. 2010)).

Turning to "related to" jurisdiction, the BAP held that the bankruptcy court had misapplied the "close nexus" test when it concluded that interpretation of the Plan and Confirmation Order established a sufficiently close nexus for "related to" jurisdiction. *Id.* at 427. Rather, the BAP held that a nexus is sufficiently close to give rise to post-confirmation jurisdiction only when "the outcome of the issues before the bankruptcy court . . . potentially impact[s] the debtor, the estate, or the implementation of the plan of reorganization," and the tax consequences for the Wilshire Partners would affect none of these. *Id.* at 427, 430.

Finally, the BAP concluded that without any statutory basis for jurisdiction, the bankruptcy court could not exercise supplemental jurisdiction under 28 U.S.C. § 1367(a). *Id.* at 430–31. It also rejected the bankruptcy court's reliance on ancillary jurisdiction to "enable [the bankruptcy court] to vindicate its authority and effectuate its decrees." *Id.* at 431. Once again, the BAP reasoned that the claim here would have no effect on the reorganized debtor (Reorganized Wilshire) or the administration of the bankruptcy estate, because the bankruptcy court's orders interpreting the Plan "did not act to preserve a benefit negotiated in the plan or, indeed, have any effect on the plan of reorganization." *Id.* at 431, 434.

Reorganized Wilshire and the Wilshire Partners timely appealed.

II. Standard of Review

We review de novo questions of subject matter jurisdiction. *Montana v. Goldin (In re Pegasus Gold Corp.)*, 394 F.3d 1189, 1193 (9th Cir. 2005). The burden of establishing subject matter jurisdiction rests on the party asserting that the court has jurisdiction. *McNutt v. GM Acceptance Corp.*, 298 U.S. 178, 182–83 (1936).

III. Discussion

The resolution of this case turns on a careful parsing of questions relevant to the jurisdictional issue as distinct from questions relevant to the merits. To some extent, the two are intertwined; the dispute ultimately involves difficult questions about overlapping state tax and federal bankruptcy laws. *See In re Wilshire Courtyard*, 459 B.R. at 418.[4] Nonetheless, the jurisdictional nexus in this case rests on the need to interpret the Plan and Confirmation Order to resolve the merits questions.

[4] As we analyze the statutory bases for post-confirmation bankruptcy court jurisdiction, we bear in mind the "general rule" that "when the question of jurisdiction and the merits of the action are intertwined, dismissal for lack of subject matter jurisdiction is improper." *Williston Basin Interstate Pipeline Co. v. An Exclusive Gas Storage Leasehold & Easement in the Cloverly Subterranean, Geological Formation*, 524 F.3d 1090, 1094 (9th Cir. 2008) (internal alterations and quotation marks omitted).

A. Statutory jurisdiction

We begin with the statutory scheme. Like all federal courts, the jurisdiction of the bankruptcy courts is created and limited by statute. *Celotex Corp. v. Edwards*, 514 U.S. 300, 307 (1995); *In re Ray*, 624 F.3d at 1130. Bankruptcy courts have subject matter jurisdiction over proceedings "arising under title 11, or arising in or related to cases under title 11." 28 U.S.C. § 1334(b); *see also id.* 28 U.S.C. § 157(b)(1).[5] We examine each potential basis below.

1. "Arising under" and "arising in" jurisdiction

We begin where we agree with the BAP: the bankruptcy court had neither "arising under" nor "arising in" subject matter jurisdiction over the present dispute.

"Arising under" and "arising in" are terms of art. *Harris v. Wittman (In re Harris)*, 590 F.3d 730, 737 (9th Cir. 2000). Proceedings "arising under" title 11 involve causes of action created or determined by a statutory provision of that title. *Id.* Similarly, proceedings "arising in" title 11 are not those created or determined by the bankruptcy code, but which would have no existence outside of a bankruptcy case. *Maitland v. Mitchell (In re Harris Pine Mills)*, 44 F.3d 1431, 1435–37 (9th Cir. 1995).

The Wilshire Partners argue that the bankruptcy court had "arising under" subject matter jurisdiction to reopen the case because the tax dispute is "determined" by 11 U.S.C. § 346.

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[5] Because we hold that the bankruptcy court had "related to" jurisdiction, we do not address the parties' arguments regarding supplemental or ancillary jurisdiction.

Section 346 preempts state tax law in favor of specific provisions detailed in several subsections. 11 U.S.C. § 346(a). The Wilshire Partners argue that § 346(j)(1) determines the result in the present dispute. The relevant version of that statute provides:

> Except as otherwise provided in this subsection, income is not realized by the estate, the debtor, or a successor to the debtor by reason of forgiveness or discharge of indebtedness in a case under this title.

Id. § 346(j)(1) (1997).[6]

The Wilshire Partners' argument fails because it presumes the answer to the merits question presented to the bankruptcy court: whether the disputed transaction was a cancellation of indebtedness or a disguised sale. For that question, § 346(j) does not provide the substantive rule of decision. Nor does that question require "resolution of a substantial question of bankruptcy law." *See Haw. Airlines, Inc. v. Mesa Air Grp., Inc.*, 355 B.R. 214, 217 (D. Haw. 2006). The merits question—whether the Plan resulted in a disguised sale or forgiveness of debt—is one that appears to involve a close look at the economics of the disputed transaction, which will warrant analysis of the Plan and Confirmation Order as well

[6] The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005 amended 11 U.S.C. § 346(j)(1) to read: "For purposes of any State or local law imposing a tax on or measured by income, income is not realized by the estate, the debtor, or a successor to the debtor by reason of discharge of indebtedness in a case under this title, except to the extent, if any, that such income is subject to tax under the Internal Revenue Code of 1986." We consider only the pre-2005 version here.

as reference to state and federal tax and partnership law.[7] *See, e.g.*, *Comm'r v. Tufts*, 461 U.S. 300, 309–10 (1983) (upholding the Commissioner's consideration of the economic realities of disputed transactions, including consideration of the assumptions behind those transactions); *Frank Lyon Co. v. U.S.*, 435 U.S. 561, 573 (1978) ("In applying this doctrine of substance over form, the Court has looked to the objective economic realities of a transaction rather than to the particular form the parties employed."); *Basye*, 410 U.S. at 448; *2925 Briarpark, Ltd. v. Comm'r*, 163 F.3d 313, 317–19 (5th Cir. 1999) (looking to treasury regulations, federal income tax law, and the "particular facts" of the transaction record to characterize whether a partnership realized "a gain from dealings in property" or cancellation of indebtedness income). The merits question does not rest on a substantive provision of the Bankruptcy Code. We decide here only whether the bankruptcy court has jurisdiction to resolve the complex merits question.

Wilshire Partners dispute the BAP's conclusion that "no provision of the bankruptcy code is at issue" by arguing that § 346 was explicitly "at issue" because it "undergirded" Reorganized Wilshire's motion to reopen under 11 U.S.C.

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[7] We do not address whether or not the bankruptcy court's reliance on Finding V in the Confirmation Order is sufficient to characterize the transactions at issue as something other than a sale. Similarly, we decline to address the Wilshire Partners' argument that Finding V settles the matter as to the application of § 346. Resolution of these merits questions will require interpreting the Plan in conjunction with the Confirmation Order. Indeed, the Confirmation Order itself states that "to the extent there is any conflict between the Joint Plan and this Order, this Order shall control." On remand, the BAP may consider these issues in the first instance.

§ 1146(d) (1997).[8] Section 1146(d) permits bankruptcy courts to

> authorize the proponent of a plan to request a determination, limited to questions of law, by a State or local governmental unit charged with responsibility for collection or determination of a tax on or measured by income, of the tax effects, under section 346 of this title and under the law imposing such tax, of the plan. In the event of an actual controversy, the court may declare such effects after the earlier of (1) the date on which such governmental unit responds to the request under this subsection; or (2) 270 days after such request.

Bankruptcy courts have restricted the post-confirmation availability of § 1146(d), and we have not addressed the issue.[9] We need not decide the issue here. The § 1146(d) procedural mechanism for obtaining a determination from a

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[8] Section 1146(d) was recodified in 2005 as § 1146(b).

[9] *See, e.g.*, *Kmart Corp. v. Ill. Dep't of Revenue (In re Kmart Corp.)*, No. 02 B 02474, 2012 WL 1744708 (Bankr. N.D. Ill. May 15, 2012); *Allis-Chalmers Corp. v. Goldberg (In re Hartman Material Handling Sys., Inc.)*, 141 B.R. 802, 813 n.16 (Bankr. S.D.N.Y. 1992); S. Rep. No. 989, 95th Cong., at 133 (2d Sess. 1978) ("Subsection (d) permits the court to authorize the proponent of a reorganization plan to request from the Internal Revenue Service (or State or local tax authority) an advance ruling on the tax effects of the proposed plan. If a ruling is not obtained within 270 days after the request was made, or if a ruling is obtained but the proponent of the plan disagrees with the ruling, the bankruptcy court may resolve the dispute and determine the tax effects of the proposed plan.")

state taxing authority or the IRS of the tax consequences of a proposed reorganization plan—authorizing the bankruptcy court to do so only if the taxing authority fails to respond within 270 days—does not transform § 346(j)(1) into a substantive right to relief where the relief sought depends on the characterization of a plan transaction. Section 346(j) addresses the tax consequence of a transaction once the definitive character of "forgiveness or discharge of indebtedness" has been determined. It does not, by itself, create a right to relief sufficient to establish "arising under" subject matter jurisdiction when the character of the transaction is disputed.

The Wilshire Partners do not argue that this case "arises in" the jurisdiction of the bankruptcy court, and we agree with the BAP that this case does not present an issue unique to bankruptcy proceedings "that has no independent existence outside of bankruptcy and could not be brought in another forum." *In re Ray*, 624 F.3d at 1131. "[T]he fact that a matter would not have arisen had there not been a bankruptcy case does not *ipso facto* mean that the proceeding qualifies as an 'arising in' proceeding." 1-3 *Collier on Bankruptcy* ¶ 3.01[3][e][iv] (Myron M. Sheinfeld, Fred T. Witt & Milton B. Hyman, 16th ed. Dec. 2011). Had Wilshire negotiated a similar deal with its creditors outside of bankruptcy, the same dispute with CFTB over whether to categorize the income as cancellation of debt income or capital gains may have arisen.

2. "Related to" jurisdiction

We disagree with the BAP's holding that the bankruptcy court did not have "related to" jurisdiction over the present dispute. "A bankruptcy court's 'related to' jurisdiction is very broad, including nearly every matter directly or indirectly related to the bankruptcy." *Sasson v. Sokoloff (In re Sasson)*, 424 F.3d 864, 868 (9th Cir. 2005) (internal quotation marks omitted).

The test for post-confirmation "related to" jurisdiction was modified from the seminal pre-confirmation *Pacor* test for "related to" jurisdiction, which had been previously adopted by the Ninth Circuit in *Fietz v. Great W. Savings (In re Fietz)*, 852 F.2d 455, 457 (9th Cir. 1988) (citing *Pacor, Inc. v. Higgins*, 743 F.2d 984, 994 (3d Cir. 1984)). Surveying the courts that had applied a limited version of the *Pacor* test in the post-confirmation context, we recognized that the *Pacor* test of whether "'the outcome of the proceeding could conceivably have any effect on the estate being administered in bankruptcy. . . . [I]f the outcome could alter the debtor's rights, liabilities, options, or freedom of action . . . and which in any way impacts upon the handling and administration of the bankrupt estate'" was "somewhat overbroad in the post-confirmation context." *Pegasus Gold Corp.*, 394 F.3d at 1193, 1194 (quoting *In re Fietz*, 852 F.3d at 457).[10]

The "close nexus" test determines the scope of bankruptcy court's post-confirmation "related to" jurisdiction. *Pegasus Gold Corp.*, 394 F.3d at 1194. As adopted from the Third Circuit, the test encompasses matters "affecting the 'interpretation, implementation, consummation, execution, or administration of the confirmed plan.'" *Id.* (quoting *Binder v. Price Waterhouse & Co. (In re Resorts Int'l, Inc.)*, 372 F.3d 154, 166–67 (3d Cir. 2004)). The close

[10] We note that all of the cases surveyed finding post-confirmation subject matter jurisdiction under some modified version of the *Pacor* test dealt with bankruptcy proceedings that had been confirmed but not completely consummated. *See id.* at 1193–94.

nexus test "recognizes the limited nature of post-confirmation jurisdiction but retains a certain flexibility." *Id.*

Applying the close nexus test in *Pegasus Gold*, we held that "related to" jurisdiction existed because some claims concerning post-confirmation conduct—specifically, alleged breach of the liquidation/reorganization plan and related settlement agreement as well as alleged fraud in the inducement at the time of the plan and agreement—would "likely require interpretation of the [settlement agreement and plan]." *Id.* The claims and remedies could also "affect the implementation and execution" of the as-yet-unconsummated plan itself. *Id.*

In contrast, the close nexus test was not satisfied in *Sea Hawk Seafoods, Inc. v. Alaska (In re Valdez Fisheries Development Association, Inc.)*, 439 F.3d 545, 548 (9th Cir. 2006). The bankruptcy court there had reopened a dismissed chapter 11 case—in which no plan had ever been confirmed—to determine whether a settlement agreement between a creditor (a seafood processing plant) and former debtor (a fisheries development association) also protected the State of Alaska from the creditor processing plant's fraudulent conveyance claim, where the State was also a creditor but not a party to the settlement agreement. *Id.* at 546–47. The district court affirmed the bankruptcy court's reopening of the case. We reversed because "there was no confirmed plan and there is no claim that the dispute between two creditors, [the processing plant and the State], would have any effect on the now-closed bankruptcy estate." *Id.* at 548. The creditors' dispute was outside the scope of bankruptcy court post-confirmation jurisdiction because the dispute "implicate[d] the term of a settlement agreement approved by the court as a precondition of the dismissal of [debtor's] bankruptcy. But that agreement has been fully implemented with respect to [the debtor]." *Id.*

Contrary to the BAP's characterization, *Valdez Fisheries* did not restrict or refine the meaning of the close nexus test. Rather, we simply concluded that the claims in the case were outside those matters "affecting the interpretation, implementation, consummation, execution, or administration of the confirmed plan." *Pegasus Gold Corp.*, 394 F.3d at 1194. Because there was no confirmed plan in *Valdez Fisheries*, we reached the same conclusion separately under both the pre-confirmation *Fietz/Pacor* test and the post-confirmation *Pegasus Gold* "close nexus" test.

In interpreting *Valdez Fisheries,* the BAP improperly conflated the two tests. The BAP reasoned that "to show a close nexus, the outcome of a dispute must 'alter the debtor's rights, liabilities, options, or freedom of action or in any way impact upon the handling and administration of the bankrupt estate.'" *In re Wilshire Courtyard*, 459 B.R. at 429 (quoting *In re Fietz*, 852 F.2d at 457). The BAP's reasoning makes the pre-confirmation *Fietz/Pacor* test of whether a separate civil proceeding could "alter the debtor's rights, liabilities, options or freedom of action . . . [or] in any way impact[] upon the handling and administration of the bankruptcy estate," part and parcel of the post-confirmation *Pegasus Gold* post-confirmation "close nexus" test. The two are distinct. The BAP recognized why when it stated,"[t]he *Pacor* test, however, proved less than useful in determining related to jurisdiction after confirmation of a plan because the *bankruptcy estate no longer exists*." *Id.* at 427 (emphasis added).

Similarly, we do not read *Ray*, 624 F.3d at 1134, to have "refined" the *Pegaus Gold* "close nexus" test to incorporate the *Fietz/Pacor* test. *In re Wilshire Courtyard*, 459 B.R. at 430. The lack of jurisdiction in *Ray* was premised on the fact that the dispute there was a matter of pure state law that "did not necessarily depend upon resolution of a substantial question of bankruptcy law" and which could have existed "entirely apart from the bankruptcy proceeding." 624 F.3d at 1135. The breach of contract claim that the state court in *Ray* referred to the bankruptcy court had a relationship to the bankruptcy proceeding only because the bankruptcy court had approved a settlement agreement that sold property free and clear of the right of first refusal. The dispute in *Ray*, unlike that in *Pegasus Gold*, did not involve "implementation and execution of [the bankruptcy plan]." *Id.* at 1134 (quoting *In re Valdez Fisheries,* 439 F.3d at 548).

The BAP "distill[ed]" too narrow a version of the "close nexus" test from *Valdez Fisheries* and *Ray*: "[T]o support jurisdiction, there must be a close nexus connecting a proposed post-confirmation proceeding in the bankruptcy court *with some demonstrable effect on the debtor or the plan of reorganization*." *In re Wilshire Courtyard*, 459 B.R. at 430 (emphasis added). *Valdez Fisheries* and *Ray* simply applied the *Pegasus Gold* "close nexus" test to the unique—and distinguishable—facts of those cases. We reaffirm that a close nexus exists between a post-confirmation matter and a closed bankruptcy proceeding sufficient to support jurisdiction when the matter "affect[s] the interpretation, implementation, consummation, execution, or administration of the confirmed plan." *Pegasus Gold Corp.*, 394 F.3d at 1194 (internal citation and quotation marks omitted).

The *Pegasus Gold* "close nexus" test requires particularized consideration of the facts and posture of each case, as the test contemplates a broad set of sufficient conditions and "retains a certain flexibility." *Id.* Such a test can only be properly applied by looking at the whole picture.

First, the ultimate merits question depends in part on the interpretation of the confirmed Plan. *Id.* While it is true that the Plan itself is ambiguous as to the sale/non-sale issue and makes no mention of state tax consequences,[11] determination of the sale/non-sale attributes of the transaction requires a close look at the economics of the transaction as detailed in the Plan and Confirmation Order. *See, e.g.*, *Tufts*, 461 U.S. at 309–310, *2925 Briarpark, Ltd.*, 163 F.3d at 317–19. The disputed transaction, described in detail in the Plan and Confirmation Order, was presumably consummated as described, making interpretation of both essential to classifying the character of the transaction.

Understanding "interpretation" to include the Confirmation Order as well as the Plan finds further support in the logic of ancillary jurisdiction—a close cousin to "related to" jurisdiction—because it is well recognized that a bankruptcy court has the power to interpret and enforce its own orders. In the recent decision *Travelers Indemnity Company v. Bailey*, 557 U.S. 137, 151 (2009), the Supreme Court upheld the bankruptcy court's jurisdiction to enter a

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[11] As CFTB noted in its opposition to the motion for summary judgment in the bankruptcy court, the Plan itself says nothing about a sale of the Properties and does not reference the Bankruptcy Code provisions that provide for a sale of the Property. The Confirmation Order does not comment on whether the debtor retained property of the estate, the tax consequences of the plan, or whether the plan could be treated as a sale for tax purposes.

"Clarifying Order" interpreting the scope of an injunction contained in a prior order confirming a chapter 11 plan entered in 1986 because the bankruptcy court "plainly had jurisdiction to interpret and enforce its own orders." Travelers was the insurer of an asbestos supplier who filed for chapter 11 bankruptcy protection when faced with the prospect of overwhelming liability. *Id.* at 140. To address the needs of future injured claimants, the bankruptcy court and parties confirmed a plan of reorganization in 1986 that created a settlement trust. *Id.* at 141. Travelers and other insurers contributed to the trust on the condition that they were protected by an injunction against future direct claims from injured persons. *Id.* at 141–42. The settlement order was incorporated by reference in the bankruptcy court's order confirming the chapter 11 plan. *Id.* at 142. Over a decade later, direct actions against Travelers commenced, and Travelers sought the bankruptcy court's protection. *Id.* at 142–43. The bankruptcy court issued a Clarifying Order in 2004, providing that the 1986 orders barred the direct actions. *Id.* at 145. The Second Circuit ultimately reversed on jurisdictional grounds, holding that the direct actions were based on a different theory of liability than was covered by the scope of the original injunction and that the claims did not seek remedy from the *res* of the bankruptcy estate. *Id.* at 147.

The Supreme Court reversed on the "easy" jurisdictional issue of whether the bankruptcy court could enter the Clarifying Order. *Id.* at 151 (citing *Local Loan Co. v. Hunt*, 292 U.S. 234, 239 (1934)). The citation to *Hunt* signals the Supreme Court's interpretation that ancillary jurisdiction exists where necessary to preserve a benefit the parties initially bargained for. "That a federal court of equity has jurisdiction of a bill ancillary to an original case or proceeding in the same court, whether at law or in equity, to secure or preserve the fruits and advantages of a judgment or decree rendered therein, is well settled." *Hunt*, 292 U.S. at 239.

The bankruptcy court in *Travelers* had ancillary jurisdiction to enter the Clarifying Order interpreting the original plan and incorporated injunction precisely because the injunction was critical to the plan's approval. The BAP identified in its analysis that which we find exactly relevant to the present appeal: "the record clearly indicates that the essential parties (the debtor and the insurance companies) would not have agreed to plan confirmation without the settlement agreement and injunction . . . . The Clarifying Order related to an injunction that had been negotiated and considered an *essential part* of the plan of reorganization." *In re Wilshire Courtyard*, 459 B.R. at 433 (emphasis added). We agree with the BAP's characterization of the *Travelers* opinion, but not its application of that opinion to the present case. Here, Reorganized Wilshire and the Wilshire Partners forcefully argue that the "feasibility of any reorganization in this case—which is the entire point of chapter 11 proceedings—was contingent on the cancellation of debt." The Plan itself referenced a number of Bankruptcy Code sections that included the authority to discharge debt. Indeed, the discharge of debt seems central to the conceptual framework of the reorganization plan. Interpretation of the Plan and Confirmation Order is the only way for a court to determine the essential character of the negotiated Plan transactions in a way that reflects the deal the parties struck in chapter 11 proceedings. Under *Travelers* and *Hunt*, this is reason enough for the bankruptcy court to exercise jurisdiction in this case.

Second, the BAP erred in holding that *only* state law claims are at issue in the present dispute. *In re Wilshire Courtyard*, 459 B.R. at 432. Even if the primary question of whether the transaction resulted in capital gains or forgiven debt were a question of pure state tax law, the parties also dispute the distinctly federal question of whether 11 U.S.C. § 346 applies to non-debtor general partners of a debtor partnership that was dissolved as part of the reorganization. The "non-debtor" parties in this case are partners of the former Debtor Partnership that filed a voluntary chapter 11 petition.[12] CFTB argues that it seeks to assess tax liability only against the non-debtor partners, not the non-taxable partnership, and that the latter does not have standing to assert bankruptcy court jurisdiction. CFTB further argues that by its terms, 11 U.S.C. § 346(j)(1) excludes the non-debtor partners of a debtor partnership, referring only to "the estate, the debtor, or a successor to the debtor," and because of this

[12] It is not clear from the record whether the general partnership was dissolved as a consequence of the reorganization after the voluntary bankruptcy petition was filed. Nevertheless, even if the partnership was dissolved, under California's Uniform Partnership Act, "a partnership continues after dissolution only for the purpose of winding up its business. The partnership is terminated when the winding up of its business is completed." Cal. Corp. Code § 16802 (1994). Moreover, we disagree with CFTB's characterization that this dispute is one of pure state law between the non-debtor Wilshire Partners and CFTB. In particular, we note that 11 U.S.C. § 346(c)—which also preempts state law, as provided by § 346(a)—may bear on the unsettled bankruptcy law question of whether § 346(j)(1) applies to non-debtor partners. "The commencement of a case under this title concerning a corporation or a partnership does not effect a change in the status of such corporation or partnership for the purposes of any State or local law imposing a tax on or measured by income." 11 U.S.C. § 346(c)(1). We do not address the complicated intersection of bankruptcy and partnership law, but note that it may be relevant to the bankruptcy court's ultimate determination of the merits.

the bankruptcy court lacks jurisdiction to determine the tax liabilities of the non-debtor partners. That legal question is an unsettled one, but ultimately a merits determination and not itself dispositive as to the bankruptcy court's post-confirmation subject matter jurisdiction.

CFTB argues that the identical phrasing in 11 U.S.C. § 505(c) and 11 U.S.C. § 346(j)(1) limiting the application of those statutes to "the estate, the debtor, or a successor to the debtor" requires us to conclude that the bankruptcy court lacked jurisdiction here. CFTB relies on *American Principals Leasing Corporation v. United States*, 904 F.2d 477 (9th Cir. 1990). There, we held that the bankruptcy court lacked jurisdiction to determine the "tax liabilities of non-debtor partners" under § 505(c). *Id.* at 481–82. Our holding in *American Principals* does not aid our interpretation of § 346 because, as explained *supra*, § 346 is not a basis for bankruptcy court jurisdiction, and has never been interpreted to be a "jurisdictional" statute. In contrast, we have consistently interpreted § 505 as jurisdictional because it explicitly confers upon or deprives the bankruptcy court of certain authority. *See Cent. Valley AG Enters. v. United States*, 531 F.3d 750, 755 (9th Cir. 2008).

Moreover, the facts of *American Principals* are inapposite to the present case. There, the tax dispute concerned pre-bankruptcy petition activities reported by non-debtor partners on their pre-bankruptcy tax returns—not transactions that were consummated by the partnership as part of a bankruptcy reorganization plan or proceeding. *Id.* at 479. We held that § 505, which permits a bankruptcy court to "determine the amount or legality of any tax," did not permit the bankruptcy court to determine the tax liabilities of non-debtor partners. *Id.* at 481. Here, the jurisdictional question does not rest on a determination of tax *liabilities*, although that may be the ultimate consequence of the bankruptcy court's decision. The jurisdictional question here centers on whether the Plan transactions were a sale or a cancellation of debt income and whether that determination bears a sufficiently "close nexus" to the original bankruptcy proceeding. Secondary to that jurisdictional inquiry is whether § 346(j) applies to non-debtor partners of a debtor partnership.[13]

Finally, post-confirmation jurisdiction in this case is consistent with the equitable objectives of the Bankruptcy Code. Here, the bankruptcy court has "related to" subject matter jurisdiction under the *Pegasus Gold* test despite the fact that the Plan transactions have been long since consummated—unlike those in *Pegasus Gold*. To restrict post-confirmation jurisdiction *only* to cases where successful consummation depends on bankruptcy court monitoring would have the practical effect of excluding state tax determinations from bankruptcy court oversight, rendering

[13] Moreover, we note that in 2002 CFTB audited the original debtor "Wilshire Courtyard Partnership" as the taxpayer for the year 1998. After the bankruptcy case was reopened on Reorganized Wilshire's motion and while the Order to Show Cause was pending, the bankruptcy court ordered the joinder of the non-debtor partners. Although the tax bill would ultimately be paid by the non-debtor partners, taxable income is "ascertained and reported" at the level of the partnership. *Basye*, 410 U.S. at 448. Only after ascertaining income is the partnership's existence "disregarded since each partner must pay tax on a portion of the total income as if the partnership were merely an agent or conduit through which the income passed." *Id.*; *see also Thompson v. Comm'r*, 631 F.2d 642, 649 (9th Cir. 1980) ("Partnership income or loss is determined at the partnership level and not at the level of the individual partners. The distributive share of income or loss of the individual partners can be determined only by reference to the income or loss of the partnership itself.")

11 U.S.C. § 346 a nullity.[14] Moreover, such a stringent interpretation ignores the fact that tax consequences of reorganization are fundamental to virtually every corporate bankruptcy. Parties to bankruptcy proceedings negotiate against the backdrop of the tax-policy legislative choices codified in the Bankruptcy Code. Here, Reorganized Wilshire and the Wilshire Partners argue that the feasibility of any reorganization was contingent on the cancellation of debt. Had the Wilshire Partners known that CFTB would reclassify the core transaction of the reorganization as a sale and attempt to treat the discharged debt as capital gains, they may never have consented to the reorganization plan, perhaps opting to liquidate the property to the highest bidder, potentially resulting in less or no taxable income for CFTB to assess. Reorganization is often contingent upon the debtor's or plan proponents' assumption of a cancellation of debt that chapter 11 proceedings typically facilitate.[15] Restricting post-confirmation jurisdiction on the grounds that the transactions were long ago consummated and thus taxation would have no

[14] A leading treatise identifies the temporal problem presented by tax disputes in bankruptcy proceedings: "[T]axable income and associated tax attributes of the confirmation transactions are always be determined and reported on tax returns filed post confirmation, so by definition, any subsequent audit dispute as to the tax treatment of confirmation transactions will occur post confirmation." 11 *Collier on Bankruptcy* ¶ TX12.02[2][b][ii] (Myron M. Sheinfeld, Fred T. Witt & Milton B. Hyman, 16th ed. Dec. 2011) (alteration in original). We see no practical distinction between post *confirmation* and post *consummation* of a bankruptcy plan and related transactions.

[15] We do not mean that this assumption automatically decides whether cancellation of debt is cancellation of debt *income* or capital gains income. As discussed *supra*, that is a merits question that a bankruptcy court must resolve in the event it is disputed. *See Tufts*, 461 U.S. at 308–09, 310; *2925 Briarpark Ltd.*, 163 F.3d at 317.

effect on the debtor or estate effectively refashions the terms of the deal the parties to the bankruptcy struck in chapter 11 proceedings.

Thus, under the "close nexus" test, post-confirmation jurisdiction in this case extends to matters such as tax consequences that likely *would* have affected the implementation and execution of the plan if the matter had arisen contemporaneously. This application of the *Pegasus Gold* test does not prejudice either taxing entities or bankruptcy parties, nor requires the tax consequences to be assessed before transactions are consummated and taxes are due. It merely allows the bankruptcy court to retain jurisdiction over post-confirmation, post-consummation disputes related to the interpretation and execution of the confirmed Plan as if they had arisen prior to consummation. Thus, we reject CFTB's argument that jurisdiction was lacking because the bankruptcy case had been long since closed by the time the tax dispute began, and that neither the Plan nor Reorganized Wilshire could be affected.

B. Bankruptcy court jurisdiction does not violate the Tax Injunction Act

CFTB argues that bankruptcy is not an exception to the Tax Injunction Act, and that here the non-debtor partners are attempting to use a debtor's bankruptcy to shield themselves from the state's tax collection efforts. The Tax Injunction Act provides that "the district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341.[16] We have also held, however, that the bankruptcy court may exercise jurisdiction over proceedings that would otherwise violate the Act where the relief sought was necessary to the enforcement of specific Bankruptcy Code provisions. The Act "did not abridge the power specifically granted to the bankruptcy court to make such judgments as may be necessary for the enforcement of the provisions of the Bankruptcy Act. The process of dealing with state tax assessments is one essential to the administration of a bankruptcy estate and does not amount to a suit against the state." *Goldberg v. Ellett (In re Ellett)*, 254 F.3d 1135, 1149 (9th Cir. 2001) (citing *Cal. State Bd. of Equalization v. Goggin*, 191 F.2d 726, 728 (9th Cir. 1951)); *accord In re Hechinger Inv. Co. of Delaware, Inc.*, 335 F.3d 243, 247 n.1 (3d Cir. 2003) ("It is well established, however, that the Tax Injunction Act does not prevent a Bankruptcy Court from enforcing the provisions of the Bankruptcy Code that affect the collection of state taxes.").

Here, the merits question that the bankruptcy court has jurisdiction to decide is a necessary predicate to the enforcement of 11 U.S.C. § 346(j), should the court determine that the transactions were a cancellation of debt income and not a disguised sale under California state law. Indeed, as we recognized in *Ellett*, "it is quite apparent that the Act is incompatible with the Bankruptcy Code's detailed scheme governing the dischargeability of tax debts." 254 F.3d at 1149. CFTB's argument, like Wilshire's argument about § 346 "determining" the outcome of this dispute, presupposes

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[16] CFTB supports its argument with cases that deal with a different statute, the Anti-Injunction Act, 26 U.S.C. § 7421(a), though that statute is not the basis of CFTB's argument. We do not address the applicability of 26 U.S.C. § 7421(a) here.

the answer to the merits question: that tax is due *because* the core transaction was a disguised sale resulting in capital gains. We only address here whether the bankruptcy court had jurisdiction to decide that question.[17]

Conclusion

The character of the core transaction of the Debtor's bankruptcy is an issue that the bankruptcy court has jurisdiction to decide. We remand this case to the BAP to determine in the first instance whether the bankruptcy court's answer to this question gave due consideration to the "economic realities" of the transaction as structured under the Plan and Confirmation Order. The real relief sought in this case involves complexities of tax, partnership, and bankruptcy law, which we do not here decide. What we do determine is that the bankruptcy court had subject matter jurisdiction to make the determination, as it is sufficiently closely related to the bankruptcy proceeding. We therefore reverse the BAP's judgment and remand to the BAP for further proceedings consistent with this opinion.

REVERSED AND REMANDED.

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[17] Similarly, we need not address whether the bankruptcy court may enjoin the collection of state taxes against non-debtor partners, *see In re Ellett*, 254 F.3d at 1149 n.7, because we leave for the BAP to consider in the first instance the bankruptcy law question of whether 11 U.S.C. § 346(j) applies to non-debtor partners.

FILED

OCT 2 2013

NOT FOR PUBLICATION

SUSAN M. SPRAUL, CLERK
U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP No. NC-12-1322-JuPaD
MARITESS TAMONDONG MENDAROS,	Bk. No. NC-11-73139-RLE
Debtor.	
MARITESS TAMONDONG MENDAROS,	
Appellant,	
v.	M E M O R A N D U M*
JPMORGAN CHASE BANK, N.A.,	
Appellee.	

Argued and Submitted on September 20, 2013
at San Francisco, California

Filed - October 2, 2013

Appeal from the United States Bankruptcy Court
for the Northern District of California

Honorable Roger L. Efremsky, Bankruptcy Judge, Presiding

Appearances: Appellant Maritess Mendaros argued pro se; Kerry Ann Moynihan, Esq., of Bryan Cave LLP, argued for appellee JPMorgan Chase Bank, N.A.

Before: JURY, PAPPAS, and DUNN, Bankruptcy Judges.

* This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

Chapter 7[1] debtor, Maritess Tamondong Mendaros, appeals from the bankruptcy court's order granting the motion of JPMorgan Chase Bank, N.A. (Chase), which sought annulment of the automatic stay nunc pro tunc to validate a postpetition foreclosure sale of debtor's property (Motion). We AFFIRM.

I. FACTS

On December 2, 2005, debtor and Edwin Mendaros[2] (collectively, Borrowers), executed and delivered a promissory note made payable to Washington Mutual Bank, FA (WaMu) in the original principal amount of $1,860,000 (the Note). The Note was secured by an interest in Borrower's real property located on Deer Hollow Drive, Danville, California (the Property) evidenced by a Deed of Trust dated December 2, 2005, and recorded on December 13, 2005, in the official records of Contra Costa County as Document Number 2005-0476726 (the Deed of Trust).

On September 25, 2008, the Office of Thrift Supervision closed WaMu and the Federal Deposit Insurance Corporation (FDIC) was appointed as receiver. On the same date, Chase entered into a Purchase and Assumption Agreement with the FDIC to purchase certain assets, including all loans and loan commitments, of WaMu.

By March 2009, Borrowers were in default under the terms of

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[1] Unless otherwise indicated, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and "Rule" references are to the Federal Rules of Bankruptcy Procedure.

[2] Edwin Mendaros is either debtor's husband or her son. It makes no difference for purposes of this appeal.

the Note in the approximate amount of $91,621.35. On March 9, 2009, Chase recorded a notice of default as Document No. 09-48725.

On April 27, 2010, Edwin filed a chapter 7 petition, Case No. 10-44753, listing the Property as his residence.

On May 19, 2010, the bankruptcy court dismissed the case because Edwin failed to file required documents, including schedules.

Seven days later, on May 26, 2010, Edwin filed a second chapter 7 petition, Case No. 10-46045. Edwin listed the prior bankruptcy case, listed the Property as his residence and listed a joint tenancy interest in the Property.

On August 4, 2010, Chase obtained relief from stay to file a notice of sale and proceed with its foreclosure of the Property.[3]

On September 1, 2010, Chase recorded a notice of trustee sale as Document No. 10-184801 setting the foreclosure sale for September 22, 2010.

On September 21, 2010, one day prior to the scheduled foreclosure sale, debtor filed a chapter 13 petition, Case No. 10-70804.

On October 7, 2010, the bankruptcy court dismissed her case because she failed to file the required documents.

On December 19, 2011, debtor filed her chapter 13 petition

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[3] On January 21, 2011, the case was initially closed without a discharge because Edwin failed to file the financial management course certificate. The case was reopened on March 17, 2011, and Edwin obtained a discharge on April 13, 2011.

at 9:21 a.m.

On the same date, the foreclosure sale took place at 10:28 a.m. At the time of the foreclosure sale, Borrowers were forty-two months in default and owed over $2 million on the Loan.

The chapter 13 trustee moved to have debtor's case converted to one under chapter 7, which the bankruptcy court granted by order entered on January 11, 2012.

On February 22, 2012, Chase filed its Motion to validate the foreclosure sale, relying on the factors set forth in Fjeldsted v. Lien (In re Fjeldsted), 293 B.R. 12, 24 (9th Cir. BAP 2003) for annulment of the stay, and § 362(d)(4), alleging debtor's bankruptcy was filed in bad faith. In light of the multiple bankruptcy filings affecting the Property, Chase's Motion requested that the order granting relief be binding in any other bankruptcy case purporting to affect the Property and as to debtor for a period of 180 days.

On March 6, 2012, debtor filed her opposition to the Motion. Debtor requested that Chase's Motion be heard together with her motion for an order requiring Chase to show cause for its violation of the stay. Debtor also stated that, in the meantime, she would attempt to negotiate a settlement with Chase by entering into a loan modification that would allow her to retain her home.

On March 14, 2012, debtor appeared at the preliminary stay relief hearing and asserted that she had evidence that notice of the automatic stay had been given to the foreclosure trustee, Quality Loan Service (QLS), prior to the foreclosure sale.

Debtor also alleged that she had documents from Chase or its agent indicating that the sale would be reversed. As a result, the bankruptcy court continued the hearing so that the parties could file supplemental declarations with supporting documentation.

On March 16, 2012, debtor filed her declaration stating that she authorized her daughter, Kathryn Mendaros, to contact QLS about her bankruptcy filing. Debtor also alleged that she was never contacted through telephone or in person by the lender and/or its agents prior to thirty days before recording of the notice of default or to assess her financial situation as required by Cal. Civ. Code § 2923.5.[4]

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[4] Cal. Civ. Code § 2923.5 provides in relevant part:

> (a)(1) A mortgage servicer, mortgagee, trustee, beneficiary, or authorized agent may not record a notice of default pursuant to Section 2924 until both of the following:
>
> > (A) Either 30 days after initial contact is made as required by paragraph (2) or 30 days after satisfying the due diligence requirements as described in subdivision (e).
> >
> > (B) The mortgage servicer complies with paragraph (1) of subdivision (a) of Section 2924.18, if the borrower has provided a complete application as defined in subdivision (d) of Section 2924.18.
>
> (2) A mortgage servicer shall contact the borrower in person or by telephone in order to assess the borrower’s financial situation and explore options for the borrower to avoid foreclosure. During the initial contact, the mortgage servicer shall advise the borrower that he or she has the right to request a

(continued...)

On the same date, debtor filed Kathryn’s declaration. Kathryn declared that she called QLS at 10:32 a.m. on December 19, 2011, and faxed it a copy of the bankruptcy filing. Kathryn also stated that she made follow-up calls to QLS and that she was assured that the foreclosure sale would be reversed due to the bankruptcy filing.

Chase submitted the supplemental declaration of Bounlet Louvan, the Foreclosure Legal Liaison for QLS, who confirmed that the foreclosure sale occurred at 10:28 a.m. Louvan also declared that a telephone call was received from debtor at 10:58 a.m. on December 19, 2011, after the foreclosure sale had taken place. Chase also filed a Relief from Stay Cover Sheet which reflected that the pre-foreclosure principal balance exceeded $2 million and that the Loan was due for the July 1, 2008 payment, with a total delinquency of approximately $281,958.

At the final hearing on March 28, 2012, debtor and Chase appeared through counsel. After balancing the equities and considering the factors in Nat’l Envtl. Waste Corp. v. City of Riverside (In re Nat’l Envtl. Waste Corp.), 129 F.3d 1052, 1055

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[4](...continued)
subsequent meeting and, if requested, the mortgage servicer shall schedule the meeting to occur within 14 days. The assessment of the borrower's financial situation and discussion of options may occur during the first contact, or at the subsequent meeting scheduled for that purpose. In either case, the borrower shall be provided the toll-free telephone number made available by the United States Department of Housing and Urban Development (HUD) to find a HUD-certified housing counseling agency. Any meeting may occur telephonically.

(9th Cir. 1997), and Fjeldsted, the bankruptcy court ruled in favor of Chase and annulled the automatic stay retroactively to the petition date.[5]

On May 29, 2012, the bankruptcy court entered the order granting Chase's Motion. Debtor timely appealed.

On November 28, 2012, the Clerk issued a Notice of Possible Mootness. After considering the responses of both parties, the Panel issued an order finding the Clerk's Order re Mootness satisfied.

II. JURISDICTION

The bankruptcy court had jurisdiction over this proceeding under 28 U.S.C. §§ 1334 and 157(b)(2)(G). We have jurisdiction under 28 U.S.C. § 158.

III. ISSUE

Whether the bankruptcy court abused its discretion in annulling the automatic stay.

IV. STANDARD OF REVIEW

A bankruptcy court's decision to grant retroactive relief from the automatic stay is reviewed for an abuse of discretion. In re Nat'l Envtl. Waste Corp., 129 F.3d at 1054. A bankruptcy court abuses its discretion if it applied the wrong legal standard or its findings were illogical, implausible or without

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[5] At the hearing, the bankruptcy court referenced proceedings and documents with respect to Edwin's bankruptcy filings which have not been included in the Designation of Record or Excerpts of Record. On October 24, 2012, Chase filed a motion requesting the Panel to take judicial notice of the relevant documents in Edwin's bankruptcies, Case Nos. 10-44753 and 10-46045. Pursuant to Fed. R. Evid. 201, we take judicial notice of the documents and grant the motion.

support in the record. TrafficSchool.com, Inc. v. Edriver Inc., 653 F.3d 820, 832 (9th Cir. 2011).

V. DISCUSSION

When debtor filed her bankruptcy petition the automatic stay under § 362(a) went into effect. Here, the postpetition foreclosure violated the stay. See § 362(a)(3). Actions taken in violation of the automatic stay are void. Schwartz v. United States (In re Schwartz), 954 F.2d 569, 571–72 (9th Cir. 1992). However, an action taken in violation of the automatic stay may be declared valid if cause exists for retroactive annulment of the stay. Id. at 573.

Section 362(d), which empowers the bankruptcy court to annul the stay, provides in relevant part:

> On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—
>
> (1) for cause, including the lack of adequate protection of an interest in property of such party in interest.

§ 362(d); In re Schwartz, 954 F.2d at 572 ("[S]ection 362(d) gives the bankruptcy court wide latitude in crafting relief from the automatic stay, including the power to grant retroactive relief from the stay.").

In analyzing whether "cause" exists to annul the stay under § 362(d)(1), the bankruptcy court is required to balance the equities of the creditor's position in comparison to that of the debtor. In re Nat'l Envtl. Waste Corp., 129 F.3d at 1055. Under this approach, the bankruptcy court considers (1) whether the creditor was aware of the bankruptcy petition and automatic stay, and (2) whether the debtor engaged in unreasonable or inequitable conduct. Id.

Additional factors for consideration include the number of bankruptcy filings by the debtor; the extent of any prejudice, including to a bona fide purchaser; the debtor's overall good faith; the debtor's compliance with the Code; the relative ease of restoring parties to the status quo ante; the costs of annulment to debtors and creditors; how quickly the creditor moved for annulment; whether annulment will cause irreparable injury to the debtor; and whether stay relief will promote judicial economy or other efficiencies. In re Fjeldsted, 293 B.R. at 25. "In any given case, one factor may so outweigh the others as to be dispositive." Id.

On appeal, debtor does not take issue with the bankruptcy court's identification of the relevant factors for annulment of the stay, or for that matter, the application of those factors to the facts of this case. Based upon our review of the record, and construing debtor's pro se briefs liberally, we conclude the bankruptcy court did not abuse its discretion in annulling the automatic stay to validate the postpetition foreclosure sale.

In applying the first factor under In re Nat'l Envtl. Waste Corp. to the evidence presented, the bankruptcy court found that Chase was not aware of debtor's bankruptcy case before the foreclosure. This finding was supported by debtor's failure to produce any documentary evidence suggesting that Chase or QLS had been notified of her bankruptcy filing prior to the foreclosure. Instead, the record shows that debtor's daughter, Kathryn, notified QLS at 10:32 a.m. about the filing, which was after the foreclosure sale took place. Louvan's declaration confirmed that QLS did not receive a telephone call from debtor or her daughter prior to the foreclosure sale. There is no evidence in the record regarding any other forms of communication such as a fax that were sent to QLS or Chase prior to the sale.

In addition, the bankruptcy court found that debtor engaged in unreasonable or inequitable conduct that showed she was utilizing the bankruptcy process to delay or hinder Chase. The record amply supports these findings: (1) the bankruptcy filings by co-debtor Edwin; (2) debtor's two bankruptcy filings (including the instant case); (3) debtor's failure to comply with chapter 13 requirements, which resulted in the conversion of this case; and (4) debtor's loan being forty-two months in default. These findings overlap with some of the Fjeldsted factors: the number of bankruptcy filings by debtor, debtor's overall good faith and debtor's compliance with the Code. The bankruptcy court properly concluded that these factors and debtor's one-sided use of the bankruptcy process weighed in favor of annulment.

Moreover, regarding the costs of annulment to debtor and Chase, the bankruptcy court gave consideration to debtor's right to bring an action in the state court for any alleged wrongful acts in violation of Cal. Civ. Code § 2923.5. Chase's counsel acknowledged that debtor's right was preserved, and the bankruptcy court repeatedly stated on the record that the annulment of the stay did not mean that the foreclosure was valid under California law.

The bankruptcy court further found that Chase had not delayed in bringing its motion to annul the stay nunc pro tunc. There is nothing in the record that suggests otherwise, and the motion to annul the stay was filed a little more than two months after the sale took place.

Finally, the court observed that debtor had ample opportunity to present her case, but did not meet her burden of showing that she faxed or telephoned Chase or QLS regarding her bankruptcy filing prior to the foreclosure sale.

In the end, the court concluded that the Nat'l Envtl. Waste Corp. and Fjeldsted factors weighed in Chase's favor. This balancing was within the wide latitude accorded to the bankruptcy court and was not an abuse of discretion. In re Schwartz, 954 F.2d at 572; In re Fjeldsted, 293 B.R. at 21.

VI. CONCLUSION

For all these reasons, we AFFIRM.

C
Only the Westlaw citation is currently available.

United States Bankruptcy Appellate Panel
of the Sixth Circuit.
In re Robert D. **UNDERHILL** and Beth **Underhill**,
Debtors.

No. 12–8045.
Submitted: Aug. 20, 2013.
Decided and Filed: Sept. 16, 2013.

Background: Order was entered by the United States Bankruptcy Court for the Southern District of Ohio, reopening Chapter 7 case to allow trustee to administer allegedly undisclosed estate asset, and appeal was taken.

Holdings: The Bankruptcy Appellate Panel, Marci B. McIvor, Chief Judge, held that:
(1) bankruptcy court did not abuse its discretion in reopening Chapter 7 case based on evidence of debtor's receipt of $44,985 from settlement of undisclosed cause of action belonging to limited liability company (LLC) of which debtor was the sole member, and
(2) cause of action was sufficiently rooted in prebankruptcy past, notwithstanding that it was not settled until after bankruptcy case was closed.

Affirmed and remanded.

West Headnotes

[1] Bankruptcy 51 3767

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3766 Decisions Reviewable
51k3767 k. Finality. Most Cited Cases

Order granting motion to reopen bankruptcy case to administer asset is “final” order, appealable as of right. 28 U.S.C.A. § 158(a)(1).

[2] Bankruptcy 51 3767

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3766 Decisions Reviewable
51k3767 k. Finality. Most Cited Cases

Order is “final,” for purposes of appeal, if it ends litigation on merits and leaves nothing for court to do but execute judgment. 28 U.S.C.A. § 158(a)(1).

[3] Bankruptcy 51 3444.20

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.20 k. Discretion. Most Cited Cases

Bankruptcy 51 3784

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3784 k. Discretion. Most Cited Cases

Decision on motion to reopen bankruptcy case is within sound discretion of bankruptcy court, and reviewing court should not set aside bankruptcy court's decision absent an abuse of discretion. 11 U.S.C.A. § 350(b).

[4] Bankruptcy 51 ⚷3784

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3784 k. Discretion. Most Cited Cases

"Abuse of discretion" occurs when bankruptcy court applies incorrect legal standard, misapplies correct legal standard, or relies upon clearly erroneous findings of fact; if reasonable persons could differ as to the issue, then there is no abuse of discretion.

[5] Bankruptcy 51 ⚷3782

51 Bankruptcy
51XIX Review
51XIX(B) Review of Bankruptcy Court
51k3782 k. Conclusions of Law; De Novo Review. Most Cited Cases

Determinations as to whether property forms part of the bankruptcy estate are conclusions of law, that are reviewed de novo. 11 U.S.C.A. § 541(a).

[6] Bankruptcy 51 ⚷3444.10

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.10 k. In General. Most Cited Cases

Bankruptcy 51 ⚷3444.30(1)

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.30 Grounds and Objections
51k3444.30(1) k. In General. Most Cited Cases

Motions to reopen bankruptcy case are decided on case-by-case basis, after bankruptcy court has weighed equities of case. 11 U.S.C.A. § 350(b).

[7] Bankruptcy 51 ⚷3444.20

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.20 k. Discretion. Most Cited Cases

Bankruptcy 51 ⚷3444.30(2)

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.30 Grounds and Objections
51k3444.30(2) k. Unadministered Assets. Most Cited Cases

While motion to reopen bankruptcy case is addressed to sound discretion of bankruptcy court, court has the duty to reopen whenever there is prima facie proof that estate has not been fully administered. 11 U.S.C.A. § 350(b).

[8] Bankruptcy 51 ⚷3444.30(2)

51 Bankruptcy
51XI Liquidation, Distribution, and Closing
51k3444 Reopening
51k3444.30 Grounds and Objections
51k3444.30(2) k. Unadministered Assets. Most Cited Cases

Bankruptcy court did not abuse its discretion in reopening Chapter 7 case based on evidence of debtor's receipt of $44,985 from settlement of undisclosed

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cause of action belonging to limited liability company (LLC) of which debtor was the sole member, and which LLC had been listed as having no value on debtors' bankruptcy papers. 11 U.S.C.A. § 350(b).

[9] Bankruptcy 51 ⚷2531

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)1 In General
51k2531 k. In General. Most Cited Cases

"Property of the estate" is broadly defined to bring anything of value that debtors have into bankruptcy estate. 11 U.S.C.A. § 541(a).

[10] Bankruptcy 51 ⚷2553

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2552 Rights of Action; Contract Rights Generally
51k2553 k. In General. Most Cited Cases

"Property of the estate" include debtor's causes of action. 11 U.S.C.A. § 541(a).

[11] Bankruptcy 51 ⚷2553

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2552 Rights of Action; Contract Rights Generally
51k2553 k. In General. Most Cited Cases

"Property of the estate" is not restricted by state law concepts such as when cause of action ripens or statute of limitations begins to run; estate property may include claims that were inchoate on petition date. 11 U.S.C.A. § 541(a).

[12] Bankruptcy 51 ⚷2556

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2552 Rights of Action; Contract Rights Generally
51k2556 k. Tort Claims. Most Cited Cases

Bankruptcy 51 ⚷2558

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2558 k. After-Acquired Property; Proceeds; Wages and Earnings. Most Cited Cases

While tortious interference claims belonging to Chapter 7 debtor's wholly-owned limited liability company (LLC) were not settled until after bankruptcy case was closed, whereupon debtor received $44,985 of settlement proceeds based on her membership interest in LLC, cause of action was sufficiently rooted in prebankruptcy past, when this interference allegedly occurred, such that debtor's share of settlement proceeds was estate property, administrable by trustee. 11 U.S.C.A. § 541(a)(1).

[13] Bankruptcy 51 ⚷2557

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2557 k. Property Omitted from Schedules. Most Cited Cases

Bankruptcy 51 ⚷3133

51 Bankruptcy
51IX Administration
51IX(D) Abandonment
51k3133 k. Concealed or Undiscovered Assets. Most Cited Cases

Asset or property of the estate that has been concealed or not scheduled by debtor will not be deemed to have been abandoned upon closure of case, and belongs to bankruptcy estate. 11 U.S.C.A. § 554(d).

[14] Bankruptcy 51 ⚷3133

51 Bankruptcy
51IX Administration
51IX(D) Abandonment
51k3133 k. Concealed or Undiscovered Assets. Most Cited Cases

Chapter 7 debtor's placement of value of $0.00 on her interest in wholly-owned limited liability company, with knowledge that LLC had potentially valuable cause of action for tortious interference based upon conduct predating petition date, was a failure to disclose estate asset, which prevented asset from being abandoned to debtor upon entry of order closing case. 11 U.S.C.A. § 554(d).

[15] Bankruptcy 51 ⚷2535(1)

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2535 In General
51k2535(1) k. In General. Most Cited Cases

Bankruptcy 51 ⚷2556

51 Bankruptcy
51V The Estate
51V(C) Property of Estate in General
51V(C)2 Particular Items and Interests
51k2552 Rights of Action; Contract Rights Generally
51k2556 k. Tort Claims. Most Cited Cases

While Chapter 7 debtor's placement of value of $0.00 on her interest in wholly-owned limited liability company (LLC), with knowledge that LLC had potentially valuable cause of action for tortious interference based upon conduct predating petition date, was a failure to disclose estate asset, asset was not tortious interference claim itself, but debtor's membership interest in LLC, which had value to extent that LLC's assets, including cause of action, had value in excess of claims of creditors of LLC. 11 U.S.C.A. § 541(a).

[16] Corporations and Business Organizations 101 ⚷3628

101 Corporations and Business Organizations
101XV Unincorporated Business Organizations
101XV(E) Limited Liability Companies
101k3627 Capital and Stock; Contributions
101k3628 k. In General. Most Cited Cases

Under Ohio law, membership interests in limited liability company (LLC) have value only to the extent the LLC's assets exceed its liabilities.

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Appeal from the United States Bankruptcy Court for the Southern District of Ohio, Case No. 10–10061.David S. Blessing, The Blessing Law Firm, Cincinnati, OH, for Appellants.

Jody Michelle Oster, The Huntington National Bank, Columbus, OH, for Appellee.

Before: EMERSON, LLOYD, and McIVOR, Bankruptcy Appellate Panel Judges.

OPINION

MARCI B. McIVOR, Chief Bankruptcy Appellate Panel Judge.

***1** Robert and Beth Underhill ("Debtors") appeal the bankruptcy court's order granting Huntington National Bank's motion to reopen Debtors' bankruptcy case. After Debtors received their discharge, Golf Chic Boutique, LLC, ("Golf Chic, LLC") an LLC in which Debtor Beth Underhill was the sole member, filed a claim for tortious interference against several entities. The lawsuit was settled and $80,000 was awarded to the plaintiff LLC. However, the settlement check was made payable to Debtor Beth Underhill and her attorney, rather than to the LLC. Huntington National Bank discovered that Debtor Beth Underhill had received the settlement proceeds and moved to reopen the Debtors' case so that the proceeds of the settlement could be administered as an asset of the bankruptcy estate. For the reasons that follow, the Panel affirms the bankruptcy court's order granting Huntington National Bank's motion to reopen the Debtors' bankruptcy case. The Panel also remands this matter to the bankruptcy court for a determination as to the value of Debtor Beth Underhill's membership interest in Golf Chic, LLC, based on Golf Chic LLC's recovery on its lawsuit.

STATEMENT OF ISSUES

There are two issues on appeal. The first issue is whether the bankruptcy court abused its discretion in granting Huntington National Bank's motion to reopen. The second issue is whether the bankruptcy court erred in ruling that all of the settlement proceeds received by Debtor Beth Underhill, as the sole member of Golf Chic, LLC were property of the Debtors' bankruptcy estate.

JURISDICTION AND STANDARD OF REVIEW

[1][2] The Bankruptcy Appellate Panel of the Sixth Circuit has jurisdiction to decide this appeal. The United States District Court for the Southern District of Ohio has authorized appeals to the Bankruptcy Appellate Panel, and none of the parties has timely elected to have this appeal heard by the district court. 28 U.S.C. §§ 158(b)(6), (c)(1). A bankruptcy court's final order may be appealed as of right pursuant to 28 U.S.C. § 158(a)(1). For purposes of appeal, an order is final if it "ends the litigation on the merits and leaves nothing for the court to do but execute the judgment." *Midland Asphalt Corp. v. United States*, 489 U.S. 794, 798, 109 S.Ct. 1494, 1497, 103 L.Ed.2d 879 (1989) (citation and quotation marks omitted). An order granting a motion to reopen the bankruptcy case to administer an asset is a final and appealable order, because the determination that the trustee may administer the asset as property of the estate is conclusive on the merits. *See, e.g., Bonner v. Sicherman (In re Bonner)*, 330 B.R. 880 (B.A.P. 6th Cir.2005) (table).

[3][4] A decision on a motion to reopen is within the sound discretion of the bankruptcy court. The reviewing court should not set aside the bankruptcy court's decision, absent an abuse of discretion. *Smyth v. Edamerica, Inc. (In re Smyth)*, 470 B.R. 459, 461 (B.A.P. 6th Cir.2012). An abuse of discretion occurs when the bankruptcy court "applies the incorrect legal standard, misapplies the correct legal standard, or relies upon clearly erroneous findings of fact." *Id.* (citing *Schenck v. City of Hudson*, 114 F.3d 590, 593 (6th Cir.1997)). "The question is not how the reviewing court would have ruled, but rather whether a reasonable person could agree with the bankruptcy

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court's decision; if reasonable persons could differ as to the issue, then there is no abuse of discretion." *Barlow v. M.J. Waterman & Assocs., Inc. (In re M.J. Waterman & Assocs., Inc.),* 227 F.3d 604, 608 (6th Cir.2000).

***2** [5] Determinations as to whether property forms a part of the bankruptcy estate are conclusions of law that are reviewed *de novo.* *Mueller v. Hall (In re Parker),* No. 06–8053, 2007 WL 1376081, at *2 (B.A.P. 6th Cir. May 10, 2007) (table). "Under a *de novo* standard of review, the reviewing court decides an issue independently of, and without deference to, the trial court's determination." *Menninger v. Accredited Home Lenders (In re Morgeson),* 371 B.R. 798, 800 (B.A.P. 6th Cir.2007) (citation omitted). Essentially, the reviewing court decides the issue "as if it had not been heard before." *Mktg. & Creative Solutions, Inc. v. Scripps Howard Broad. Co. (In re Mktg. & Creative Solutions, Inc.),* 338 B.R. 300, 302 (B.A.P. 6th Cir.2006). "No deference is given to the trial court's conclusions of law." *Id.*

FACTS

On January 6, 2010, David R. Underhill and Beth Underhill filed a voluntary petition under Chapter 7 of the Bankruptcy Code. Harold Jarnicki was appointed Chapter 7 Trustee.

On January 26, 2010, the Debtors filed their bankruptcy schedules. On Schedule B, the Debtors listed their 100% interest in a number of businesses including Golf Chic Boutique, LLC.[FN1] Golf Chic, LLC is not a debtor in bankruptcy. Schedule B states that the Debtors have a 100% ownership and membership interest in Golf Chic, LLC and that Golf Chic, LLC has no value. The Debtors also listed all secured and unsecured claims of Golf Chic, LLC. The Debtors further represented that they held no contingent or unliquidated claims on the petition date. In other words, the Debtors represented that neither they, nor Golf Chic, LLC, owned any causes of action.

Schedule D lists Huntington National Bank ("Creditor Bank") as a creditor holding a claim totaling $25,000, secured by a lien on all of Golf Chic, LLC's property. Debtor Beth Underhill personally guaranteed repayment of the obligations of Golf Chic, LLC to Creditor Bank pursuant to a Commercial Guaranty.

In addition to Creditor Bank's secured claim, it also holds a non-priority unsecured claim in the amount of $105,000, by virtue of a loan and lease made to Underhill Landscaping, Inc.

On April 29, 2010, the Chapter 7 Trustee filed a report of no distribution.

On May 19, 2010, an order was entered discharging the Debtors.

On June 15, 2010, the Debtors' bankruptcy case was closed.

On October 25, 2010, Golf Chic, LLC filed a complaint in the Hamilton County, Ohio Court of Common Pleas against The Ladies Pro Shop, Inc., Golf Gear, Inc., and Andrea Walch ("Hamilton County Defendants") (Case No. A1009767) ("Hamilton County Action"). The Debtors were not named as plaintiffs in the Hamilton County Action. Golf Chic, LLC claimed that in 2009 the Hamilton County Defendants "embarked on an unlawful plan and conduct to disrupt price competition from Golf–Chic by trying to drive Golf–Chic out of business." Docket No. 75, Complaint, Exh. D, p. 2, ¶ 7. In the Hamilton County Action, Golf Chic, LLC described how the Hamilton County Defendants attempted to disrupt Golf Chic, LLC's business by contacting suppliers and vendors by e-mail and phone asking those suppliers and vendors to cease selling products to Golf Chic, LLC, resulting in lost income and business. As a result of the Hamilton County Defendant's actions, Golf Chic, LLC requested an award of damages exceeding $25,000. In connection with the Hamilton County Action, Debtor Beth Underhill and Hamilton County Defendant, Andrea Walch, testified under oath in a deposition.

***3** On February 17, 2012, the Hamilton County Defendants issued a settlement check in the Hamilton County Action for the sum of $80,000, made payable to "The Blessing Law Firm Trust Account." *Id.* at Exh. E. Copies of the settlement check obtained during discovery reflect that the proceeds were distributed on February 28, 2012. Debtor Beth Underhill individually received $44,985, and William H. Blessing Office Account received the sum of $35,015.

On February 23, 2012, the Debtors and Golf Chic, LLC executed a "Full and Final Release," releasing the Hamilton County Defendants and Old Dominion Insurance Company from claims resulting from any and all facts set forth in the Hamilton County Action. The Full and Final Release was signed by the Debtors.

On February 28, 2012, Creditor Bank learned of the settlement entered into between Golf Chic, LLC and the Hamilton County Defendants. Creditor Bank filed an action in Franklin County Court of Common Pleas against the Debtors, The Blessing Law Firm and William H. Blessing, and others, requesting a turnover of the settlement proceeds.

On July 25, 2012, Creditor Bank filed a motion to reopen the Debtors' bankruptcy case for cause in order to administer undisclosed assets. On August 30, 2012, the Debtors filed an objection to the Creditor Bank's motion to reopen.

On October 1, 2012, the bankruptcy court held a hearing on Creditor Bank's motion to reopen. At the conclusion of the hearing, the bankruptcy court granted Creditor Bank's motion to reopen.

On October 10, 2012, the bankruptcy court entered an order in accordance with its ruling. Relying on evidence submitted by the parties from the Hamilton County Action, including affidavits and deposition testimony, the bankruptcy court held that Creditor Bank

> met its burden of demonstrating that the Claim was sufficiently rooted in the Debtors' pre-bankruptcy past so as to constitute property of the estate and that the $80,000 settlement funds paid by or on behalf of the [Hamilton County] Defendants to settle the Claim and the Hamilton County Action also constitute property of the estate. 11 U.S.C. § 541. *Mueller v. Hall (In re Parker)*, 2007 Bankr.LEXIS 1523, 2007 WL 1376081 (B.A.P. 6th Cir.2007).... [T]he testimony of Debtor Beth Underhill in addition to her Affidavit as well as the testimony of the Defendants in the Hamilton County Action make clear that events relating or giving rise to the Claim occurred as early as April of 2009, continued later into 2009 and in 2010 subsequent to the filing of the petition herein.

(Docket No. 87, p. 4).

On October 24, 2012, the Debtors filed a timely appeal of the bankruptcy court's order granting Creditor Bank's motion to reopen the Debtors' bankruptcy estate to administer the settlement proceeds.

DISCUSSION

There are two issues on appeal. The first issue is whether the bankruptcy court abused its discretion in granting Creditor Bank's motion to reopen. The second issue is whether the bankruptcy court erred in ruling that all of the settlement proceeds received by Beth Underhill in her capacity as the sole member of Golf Chic, LLC are property of the Debtors' bankruptcy estate.

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I. *The bankruptcy court did not abuse its discretion in granting Creditor Bank's motion to reopen.*

***4** [6][7] Section 350(b) of the Bankruptcy Code provides that "[a] case may be reopened in the court in which such case was closed to administer assets, to accord relief to the debtor, or for other cause." 11 U.S.C. § 350(b); Fed. R. Bankr.P. 5010. Section 350 "confers upon the bankruptcy court broad discretion in determining whether to reopen a case and its decision to grant or deny a motion to reopen is binding absent a clear abuse of discretion." *Mead v. Helm,* No. 88–105, 1989 WL 292, at *3 (6th Cir. Jan. 4, 1989) (table) (citing *Rosinski v. Boyd (In re Rosinski),* 759 F.2d 539, 540–41 (6th Cir.1985)). Motions to reopen are decided on a case-by-case basis after the bankruptcy court weighs the equities of the case. *In re Jenkins,* 330 B.R. 625, 628 (Bankr.E.D.Tenn.2005). "[A]lthough a motion to reopen is addressed to the sound discretion of the bankruptcy court, 'the court has the duty to reopen an estate whenever prima facie proof is made that it has not been fully administered.' " *Lopez v. Specialty Rests. Corp. (In re Lopez),* 283 B.R. 22, 27 (B.A.P. 9th Cir.2002) (citing *Kozman v. Herzig (In re Herzig),* 96 B.R. 264, 266 (B.A.P. 9th Cir.1989)). A bankruptcy court abuses its discretion if it bases its ruling on an erroneous rule of law or where the Panel finds that the trial court has committed a clear error of judgment in the conclusion it reached. *Lopez,* 283 B.R. at 26. A court also abuses its discretion if it denies a motion to reopen where "assets of such probability, administrability and substance ... appear to exist as to make it unreasonable under all the circumstances for the court not to deal with them." *Herzig,* 96 B.R. at 266.

[8] In this appeal, Creditor Bank filed a motion to reopen the Debtors' bankruptcy case in order to administer undisclosed assets consisting of settlement proceeds it claims are part of the Debtors' bankruptcy estate. The bankruptcy court did not abuse its discretion in reopening the bankruptcy case because Creditor Bank established a prima facie claim that Debtor Beth Underhill received $44,985 from the $80,000 settlement of a lawsuit filed by an LLC in which she was the sole member. The existence of settlement proceeds from a claim held by the LLC, an entity the Debtors owned entirely, is sufficient evidence of an asset to grant a motion to reopen.

The Debtors do not seriously challenge the bankruptcy court's broad authority to reopen the case. Instead the Debtors argue that the court wrongly concluded that the check received by Debtor Beth Underhill was property of the bankruptcy estate. The Debtors raise two arguments as to why the settlement proceeds are not property of their bankruptcy estate. The Debtors' first argument is that because the settlement proceeds were received after the Debtors received a discharge, the proceeds are not property of the estate. The Debtors' second argument is that even if a cause of action against the Hamilton County Defendants existed at the time the Debtors filed for bankruptcy, that cause of action was abandoned by the Trustee when the Debtors' bankruptcy case was closed. The Panel will address each of these arguments below.

A. *The check received by Debtor Beth Underhill post-petition was evidence of an asset to be administered by the bankruptcy estate* .

***5** The Debtors first argue that the portion of the settlement paid to Debtor Beth Underhill is not property of the estate because it was paid to Debtor Beth Underhill long after the Debtors' bankruptcy case was closed.

[9][10][11] Section 541 of the Bankruptcy Code defines property of the estate as "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). The purpose of this broad definition is to " 'bring anything of value that the debtors have into the [bankruptcy] estate.' " *In re Webb,* BAP No. 11–8016, 2012 WL 2329051, at *11 (B.A.P. 6th Cir. Apr. 9, 2012) (table) (citing *Lyon v. Eiseman (In re Forbes),*

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372 B.R. 321, 330 (B.A.P. 6th Cir.2007)). It is well settled that "interests of the debtor in property" include causes of action. *See* *U.S. v. Whiting Pools, Inc.*, 462 U.S. 198, 205 n. 9, 103 S.Ct. 2309, 2314, 76 L.Ed.2d 515 (1983). Moreover, § 541(a) "is not restricted by state law concepts such as when a cause of action ripens or a statute of limitations begins to run, and 'property of the estate' may include claims that were inchoate on the petition date." *Winick & Rich, P.C. v. Strada Design Assocs., Inc. (In re Strada Design Assocs., Inc.),* 326 B.R. 229, 236 (Bankr.S.D.N.Y.2005).

The seminal case discussing the scope of "property of the estate" is the Supreme Court's decision in *Segal v. Rochelle,* 382 U.S. 375, 86 S.Ct. 511, 15 L.Ed.2d 428 (1966). In *Segal,* the Supreme Court determined that a loss-carryback refund claim is property of the estate because even though the refund could not be claimed from the Government until a future time, it was "sufficiently rooted in the pre-bankruptcy past" that it should be regarded as property of the bankruptcy estate.[FN2] *Segal,* 382 U.S. at 379, 86 S.Ct. at 515. Since *Segal* was decided, courts have consistently held that causes of action that are sufficiently rooted in the debtor's pre-bankruptcy conduct are property of the estate under § 541. *See* *Mueller v. Hall (In re Parker),* No. 06–8053, 2007 WL 1376081, at *7 (B.A.P. 6th Cir. May 10, 2007) (table) (holding that a malpractice claim, that the debtor listed in the schedules and caused debtor to file for bankruptcy is property of the estate); *In re Richards,* 249 B.R. 859, 861 (Bankr.E.D.Mich.2000) (debtor's asbestos injury claim is property of the estate where all allegedly wrongful conduct that gave rise to the claim occurred prepetition).

[12] Applying the *Segal* test to the evidence in the record, the Panel finds that the Debtors' interest in Golf Chic, LLC included a contingent, unliquidated value for the LLC's claim for tortious interference. The claim had its roots in prebankruptcy and pre-abandonment conduct such that the Debtors' interest in the LLC included some or all of the settlement proceeds. This property constitutes property of the Debtors' estate, but the value must be determined after payment of all claims senior in priority to the Debtors' membership interest. The evidence submitted by the parties consisting of the deposition testimony of Debtor Beth Underhill, the deposition testimony of the Hamilton County Defendant Andrea Walch, affidavits, email correspondence, and pleadings from the Hamilton County Action all support the conclusion reached by the bankruptcy court that the events giving rise to Golf Chic, LLC's claim for tortious interference began in 2009 and culminated in 2010 when the Hamilton County Defendants terminated their business relationship with Golf Chic, LLC. Since Debtor Beth Underhill was the sole member of Golf Chic, LLC, her membership interest potentially had value on the date she filed for bankruptcy and certainly before abandonment because Golf Chic, LLC had a cause of action against the Hamilton County Defendants that was undisclosed. Although the settlement of Golf Chic, LLC's cause of action did not occur until after Debtors' case was closed, the settlement related to a prepetition cause of action held by the LLC, and Debtor Beth Underhill received payment because of her prepetition interest in Golf Chic, LLC. The bankruptcy court's conclusion that the settlement proceeds were rooted in prepetition activities is correct as a matter of law.

***6** The Panel affirms the bankruptcy court's conclusion that the settlement proceeds received by Debtor Beth Underhill post-discharge were sufficiently rooted in the Debtors' pre-bankruptcy past to require administration of the net settlement proceeds by the bankruptcy estate.

B. *Debtor failed to disclose that Golf Chic, LLC had a cause of action against the Hamilton County Defendants. Therefore, the cause of action was not abandoned when the bankruptcy estate was closed.*

[13][14] The Debtors' second argument is that even if the settlement proceeds from the Hamilton

County Action would have been property of the bankruptcy estate, the cause of action is not an asset because it was abandoned when the case was closed. Reopening a bankruptcy case to administer an asset may only occur when there are assets that are not known to the trustee at the time the case was closed. *Collier on Bankruptcy,* ¶ 350.03[1] (16th ed rev.2012). Section 554 addresses this point and states in relevant part that:

> (c) ... *[A]ny property scheduled* under section 521(a)(1) of this title not otherwise administered at the time of the closing of a case is abandoned to the debtor and administered for purposes of section 350 of this title.
>
> (d) ... [P]roperty of the estate that is not abandoned under this section and that is not administered in the case *remains property of the estate.*

11 U.S.C. § 554 (emphasis added). Therefore, an asset or property of the estate that has been concealed or not scheduled by the debtor will not be deemed to have been abandoned by the trustee and belongs to the bankruptcy estate. The bankruptcy court record shows that the Debtors only disclosed their 100% membership interest in Golf Chic, LLC and represented in their schedules that they possessed no contingent or unliquidated claims. Under § 554 an unscheduled asset is not automatically abandoned. The tort claim held by Golf Chic, LLC was not abandoned when the Debtors' trustee abandoned the membership interest to the Debtors because the tort claim was known to Debtor Beth Underhill and affected the value of her membership interest. Placing a value of zero on the LLC membership interest with knowledge of the tort claim and the failure to list such claim constituted a failure to disclose the asset and warrants reopening and a determination by the bankruptcy court of the value of the Debtors' interest in the LLC.

II. *Valuation of Debtor Beth Underhill's membership interest in Golf Chic, LLC.*

[15] While the bankruptcy court correctly concluded that Creditor Bank's motion to reopen should be granted, it is unclear from the record what portion of the settlement proceeds from Golf Chic, LLC's lawsuit belongs to creditors of Golf Chic, LLC, and what portion belongs to creditors of Beth and Robert Underhill. Some of the proceeds of the settlement are an asset of the bankruptcy estate only because Debtor Beth Underhill is the sole member of Golf Chic, LLC. On the date the Debtors filed for bankruptcy, Golf Chic, LLC had a cause of action against the Hamilton County Defendants. Debtor Beth Underhill stated that her membership interest in Golf Chic, LLC had a value of zero, but that statement was inaccurate because her membership interest potentially had value if Golf Chic, LLC recovered on its cause of action. Once Golf Chic, LLC recovered on its cause of action, the unresolved issue is the value of Debtor Beth Underhill's membership interest in Golf Chic, LLC after Golf Chic, LLC received the settlement.

***7** [16] Debtor Beth Underhill's interest in the settlement proceeds obtained by Golf Chic, LLC is defined by state law. Pursuant to Ohio law, a person owning an interest in a limited liability company is a member of that limited liability company. Ohio Rev.Code § 1705 .01(G). This membership interest confers upon the member a right to a “share of the profits and losses of [the] limited liability company and the right to receive distributions from that company.” Ohio Rev.Code § 1705.01(H). A person's membership interest in a limited liability company is personal property. Ohio Rev.Code § 1705.17. “A ‘membership interest’ in a limited liability company, however, does not confer upon the ‘member’ any specific interest in company property, whether personal property or real property. Such property is, instead, held and owed [sic] solely by the company.” *In re Liber*, No. 08–37046, 2012 WL 1835164, at *4 (Bankr.N.D.Ohio May 18, 2012). Therefore, if the company is dissolved the assets of Golf Chic, LLC are retained for the benefit of creditors of the company, not for the benefit of its members. Ohio Rev.Code § 1705.46. "Under this principle, membership interests in the company only have value to the extent assets exceed the liabilities." *In re Saunier*, No. 11–60997, 2012 WL 5898601, at * 1 (Bankr.N.D.Ohio Nov.20, 2012); *see also, In re Hopkins*, No. DG 10–13592, 2012 WL 423916 (Bankr.W.D.Mich. Feb.2, 2012).

Under Ohio law, the settlement proceeds of the Hamilton County Action should have been paid to Golf Chic, LLC. Debtor Beth Underhill, in her capacity as a member of Golf Chic, LLC was required to pay creditors of Golf Chic, LLC before she made a distribution to herself on account of her membership interest. Instead, the settlement proceeds were distributed directly to the attorney who represented Golf Chic, LLC, in the amount of $35,015, and to Debtor Beth Underhill, in the amount of $44,985, leaving Creditor Bank with no remedy but to reopen the Debtors' bankruptcy case to seek payment on their claim against Golf Chic, LLC.

If Debtor Beth Underhill had listed Golf Chic, LLC's cause of action against the Hamilton County Defendants on her bankruptcy schedules, the cause of action would have been litigated for the benefit of the bankruptcy estate. Once the litigation was settled, Beth Underhill's membership interest would have been $80,000, less amounts owed to creditors of Golf Chic, LLC. The creditors of Golf Chic, LLC (including the Blessing Law Firm) would have been paid, and the balance of the settlement proceeds would belong to the Debtors' bankruptcy estate for distribution to Debtors' creditors.

Now that this case is reopened, the bankruptcy court must determine what portion of the settlement proceeds belongs to creditors of Golf Chic, LLC pursuant to Ohio law. Those proceeds are recoverable by creditors of Golf Chic, LLC. Under Ohio law, Debtor Beth Underhill's membership interest has value to *her* bankruptcy estate, but only to the extent that the proceeds of the settlement exceed creditor claims against Golf Chic, LLC. Therefore, the Panel is remanding this matter back to the bankruptcy court so that the bankruptcy court can determine how the settlement proceeds of the Hamilton County Action should have been distributed under Ohio state law.

CONCLUSION

***8** For the foregoing reasons, the Panel AFFIRMS the bankruptcy court's order granting Creditor Bank's motion to reopen the Debtors' bankruptcy case. The Panel also REMANDS this matter to the bankruptcy court for further findings as to what portion of the settlement proceeds should have been paid to creditors of Golf Chic, LLC and what portion of the proceeds should be paid into Debtor Beth Underhill's bankruptcy estate on account of her membership interest in Golf Chic, LLC.

FN1. The other interests include: (1) 100% stock in Underhill Landscaping, Inc.; (2) 100% stock in Cincinnati Landscape Design Build Group; and (3) 100% ownership interest in Bud Properties, LLC. All are listed as having zero value.

FN2. Although *Segal* was decided under § 70a(5) of the Bankruptcy Act rather than the Bankruptcy Code, courts follow the reasoning and adhere to the test enunciated in *Segal* when determining whether a claim is property of the estate. *See Parker*, 2007 WL 1376081, at *7.

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--- B.R. ----, 2013 WL 5042056 (6th Cir.BAP (Ohio))

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FOR PUBLICATION

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

In the Matter of: CESAR IVAN FLORES; ANA MARIA FLORES, *Debtors*.	No. 11-55452
	D.C. No 6:10-29956-MJ
ROD DANIELSON, *Trustee-Appellant*, v. CESAR IVAN FLORES; ANA MARIA FLORES, *Debtors-Appellees*.	OPINION

Appeal from the United States Bankruptcy Court
for the Central District of California
Meredith A. Jury, Bankruptcy Judge, Presiding

Argued and Submitted En Banc
March 19, 2013—San Francisco, California

Filed August 29, 2013

Before: Alex Kozinski, Chief Judge, and Harry Pregerson, Diarmuid F. O'Scannlain, Sidney R. Thomas, Barry G. Silverman, Susan P. Graber, Kim McLane Wardlaw, Richard A. Paez, Mary H. Murguia, Morgan Christen, and Jacqueline H. Nguyen, Circuit Judges.

Opinion by Judge Graber;
Dissent by Judge Pregerson

SUMMARY*

Bankruptcy

Affirming the judgment of the bankruptcy court, the en banc court held that when a Chapter 13 debtor has no "projected disposable income," 11 U.S.C. § 1325(b)(1)(B) permits plan confirmation only if the length of the proposed plan is at least equal to the applicable commitment period under § 1325(b)(4).

The en banc court overruled the holding of *Maney v. Kagenveama (In re Kagenveama)*, 541 F.3d 868 (9th Cir. 2008), that § 1325(b)(1)(B) does not impose a minimum duration for a Chapter 13 plan if the debtor has no projected income. Joining the Sixth, Eighth, and Eleventh Circuits, and reaffirming another aspect of *Kagenveama*, the en banc court held that under § 1325(b)(1)(B), the applicable commitment period acts as a temporal, as distinct from a monetary, requirement that defines a plan's minimum duration. Agreeing with the Sixth and Eleventh Circuits, the en banc court held that this temporal requirement applies regardless of the debtor's protected disposable income.

Dissenting, Judge Pregerson, joined by Chief Judge Kozinski, wrote that the majority's interpretation of

* This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

§ 1325(b)(1)(B) promoted goals that were at odds with Congress's purpose when it enacted Chapter 13 to provide debtors with a fresh start. In addition, the majority read language into Chapter 13 bankruptcy law that was not present in the plain text of § 1325(b)(1)(B). Judge Pregerson interpreted § 1325 to mean that the applicable commitment period in which debtors are required to distribute projected disposable income to unsecured creditors applies only to debtor with projected disposable income.

COUNSEL

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Tara Twomey, National Consumer Bankruptcy Rights Center, San Jose, California, for Amicus Curiae National Association of Consumer Bankruptcy Attorneys.

OPINION

GRABER, Circuit Judge:

In *Maney v. Kagenveama (In re Kagenveama)*, 541 F.3d 868, 875 (9th Cir. 2008), we held that 11 U.S.C. § 1325(b)(1)(B) does not impose a minimum duration for a Chapter 13 bankruptcy plan if the debtor has no "projected disposable income," as defined in the statute. Today, sitting en banc, we overrule that aspect of *Kagenveama* and hold that the statute permits confirmation only if the length of the proposed plan is at least equal to the applicable commitment period under § 1325(b)(4). Accordingly, we affirm the judgment of the bankruptcy court.

I. Background

Debtors Cesar and Ana Flores filed a petition for relief under Chapter 13 of the Bankruptcy Code. They have unsecured debts. They proposed a plan of reorganization under which they would pay $122 per month (1%) of allowed, unsecured, nonpriority claims for three years. Chapter 13 Trustee Rod Danielson objected to the plan, arguing, as now relevant, that § 1325(b) requires a minimum duration of five years for persons in Debtors' circumstances.[1]

The bankruptcy court sustained the Trustee's objection, holding that Debtors were not entitled to a shorter plan duration because the Supreme Court's decision in *Hamilton v. Lanning*, 130 S. Ct. 2464 (2010), is clearly irreconcilable

[1] The Trustee has never questioned Debtors' good faith in proposing the plan. *See* 11 U.S.C. § 1325(a)(3) (setting forth requirement of the debtors' good faith).

with *Kagenveama*.[2] The bankruptcy court confirmed a plan of five years' duration, which provided for monthly payments of $148 to unsecured creditors.[3]

Debtors timely appealed to the Bankruptcy Appellate Panel. The bankruptcy court then certified the plan-duration issue for direct appeal to this court pursuant to 28 U.S.C. § 158(d)(2). A divided panel of this court reversed, reasoning that *Lanning* is not clearly irreconcilable with *Kagenveama* and that, under *Kagenveama*, § 1325(b) allows a shorter plan duration for Debtors. *Danielson v. Flores (In re Flores)*, 692 F.3d 1021, 1038 (9th Cir. 2012). We then voted to rehear the case en banc. *Danielson v. Flores (In re Flores)*, 704 F.3d 1067 (9th Cir. 2012).[4]

II. Analysis

Chapter 13 is a mechanism available to "individual[s] with regular income" whose debts are within statutory limits. 11 U.S.C. §§ 101(30), 109(e). Unlike Chapter 7, which requires debtors to liquidate nonexempt assets to pay creditors, Chapter 13 permits debtors to keep those assets if

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[2] *See Miller v. Gammie*, 335 F.3d 889, 900 (9th Cir. 2003) (en banc) (holding that a three-judge panel is not bound by prior circuit precedent if an intervening decision of a higher authority "undercut[s] the theory or reasoning underlying the prior circuit precedent in such a way that the cases are clearly irreconcilable").

[3] Debtors do not dispute the increase from $122 to $148 per month.

[4] We review de novo issues of statutory construction, including a bankruptcy court's interpretation of the Bankruptcy Code. *Samson v. W. Capital Partners, LLC (In re Blixseth)*, 684 F.3d 865, 869 (9th Cir. 2012) (per curiam).

they "agree to a court-approved plan under which they pay creditors out of their future income." *Lanning*, 130 S. Ct. at 2468–69 (citing 11 U.S.C. §§ 1306(b), 1321, 1322(a)(1), 1328(a)). A bankruptcy trustee oversees the filing and execution of the plan. 11 U.S.C. § 1322(a)(1); *see also* 28 U.S.C. § 586(a)(3).

Section 1325 of the Bankruptcy Code sets forth the circumstances in which the bankruptcy court "shall" confirm a debtor's proposed repayment plan and those in which it "may not" do so. Under subsection 1325(b)(1), if the trustee or an unsecured creditor objects to a debtor's proposed plan, the court may not approve the plan unless at least one of two conditions is met. As relevant here, the second of those conditions is that "the plan provides that all of the debtor's projected disposable income to be received in *the applicable commitment period* beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan." 11 U.S.C. § 1325(b)(1)(B) (emphasis added). The statute further provides that the "applicable commitment period" of a plan "shall be" either

> (A) subject to subparagraph (B), . . .
>
> > (i) 3 years; or
> >
> > (ii) not less than 5 years, if the [debtor's] current monthly income . . . , when multiplied by 12, is not less than [the median annual family income in the applicable state]; and

> (B) may be less than 3 or 5 years, whichever is applicable under subparagraph (A), but only if the plan provides for payment in full of all allowed unsecured claims over a shorter period.

Id. § 1325(b)(4). The debtor's "current monthly income" and "disposable income" are calculated according to statutorily defined formulae. *See id.* § 101(10A) (defining "current monthly income"); *id.* § 1325(b)(2) (defining "disposable income"); *see also Lanning*, 130 S. Ct. at 2469, 2471–74, 2478 (holding that courts must calculate "*projected* disposable income," which is not statutorily defined, using a "forward-looking" approach (emphasis added)).

It is undisputed that Debtors' current monthly income is above-median and that subsection 1325(b)(4)(B)'s exception to the five-year applicable commitment period set forth in § 1325(b)(4)(A)(ii) does not apply. Debtors nonetheless contend that their proposed three-year plan was permissible because § 1325(b)(1)(B) does not set forth a minimum plan duration for debtors who, like them, have no projected disposable income.

Courts have interpreted § 1325(b)(1)(B)'s condition for plan confirmation in three distinct ways. *See Baud v. Carroll*, 634 F.3d 327, 336–38 (6th Cir. 2011) (describing split of decisions and collecting cases), *cert. denied*, 132 S. Ct. 997 (2012). First, a minority of bankruptcy courts view the "applicable commitment period" solely as a monetary "multiplier"; under that "monetary" approach, the number of months in the applicable commitment period is multiplied by the debtor's projected disposable monthly income to determine the total payments that a debtor must make, but the period has no temporal significance. *Id.* at 336–38 & n.7. Second, other bankruptcy courts, as well as this court in *Kagenveama*, have held that, although the statute does set forth a temporal requirement, that temporal requirement does not apply to debtors whose projected disposable income is less than or equal to $0. *Baud*, 634 F.3d at 337. Third and finally, a majority of courts have held that a plan cannot be confirmed unless its length is at least as long as the applicable commitment period, without regard to "whether the debtor has positive, zero[,] or negative projected disposable income." *Id.* at 336–37. We therefore must consider two issues: (1) whether, under § 1325(b)(1)(B), the applicable commitment period acts as a *temporal* requirement that defines a plan's minimum duration; and (2) if it does, whether that requirement applies to debtors who have no projected disposable income.

With respect to the first issue, we hold that the statute defines a *temporal*, as distinct from a *monetary*, requirement for confirmation under § 1325(b)(1)(B). Most importantly, the statute defines the applicable commitment period as having a duration: "3 years," "not less than 5 years," or "less than 3 or 5 years," depending on the debtor's current monthly income and the plan's provisions for payments to unsecured creditors. 11 U.S.C. § 1325(b)(4). Furthermore, the requirement of § 1325(b)(1)(B) that the plan provide for payment of the debtor's disposable income "to be received in the applicable commitment period" suggests an ongoing series of payments for the future duration of that period. A plan cannot provide for the payment of income to be received during a defined period unless it remains in effect during that period.[5]

Three of our sister courts—the Sixth, Eighth, and Eleventh Circuits—are among the courts that have rejected the view that the applicable commitment period is merely a monetary multiplier for determining the amount that the debtor must pay to unsecured creditors. *Baud*, 634 F.3d at 344; *Whaley v. Tennyson (In re Tennyson)*, 611 F.3d 873, 880 (11th Cir. 2010); *Coop v. Frederickson (In re Frederickson)*, 545 F.3d 652, 660 (8th Cir. 2008). We join those courts and hold that the applicable commitment period determines the minimum duration that a plan must have to be confirmable under § 1325(b)(1)(B). In doing so, we reaffirm one aspect of the decision in *Kagenveama*, in which the panel reasoned that, in general, the applicable commitment period imposes a temporal requirement because the "plain meaning of the word 'period' indicates a period of time." 541 F.3d at 876.

With respect to the second issue, we must decide whether a court may confirm a plan that is shorter than the applicable commitment period defined by § 1325(b)(4) if the debtor has

[5] Our interpretation of § 1325(b)(1)(B) does not render that provision redundant with § 1322(d), which sets forth the *maximum* periods of time for a Chapter 13 bankruptcy, because § 1325(b)(1)(B) concerns the plan's *minimum* duration. Although both the maximum and the minimum will be five years for many debtors whose income, like that of the debtors in this case, is above-median, 11 U.S.C. §§ 1322(d)(1), 1325(b)(4)(A)(ii), a range of permissible plan durations remain possible if a proposed plan to repay all allowed unsecured creditors' claims in full warrants a shorter applicable commitment period under § 1325(b)(4)(B). Furthermore, § 1325(b) is triggered only if the trustee or a creditor objects, whereas § 1322(d) applies in all cases, a distinction that suggests that Congress intended the two sections to serve different functions.

no projected disposable income. In light of the statute's text, purpose, and legislative history, we now hold that the temporal requirement of § 1325(b) applies regardless of the debtor's projected disposable income.

In *Kagenveama*, we held that the § 1325(b)(1)(B) temporal requirement contains an implicit exception because the "'applicable commitment period' is exclusively linked to § 1325(b)(1)(B) and the 'projected disposable income' calculation." 541 F.3d at 876. Noting that "[n]othing in the Bankruptcy Code states that the 'applicable commitment period' applies to all Chapter 13 plans," the panel concluded that "[w]hen there is no 'projected disposable income,' there is no 'applicable commitment period.'" *Id.* at 876, 877. The Sixth and Eleventh Circuits have disagreed and have held that § 1325(b) contains no such exception for debtors with no projected disposable income. *See Baud*, 634 F.3d at 351 ("[T]he temporal requirement of the applicable commitment period applies to debtors facing a confirmation objection even if they have zero or negative projected disposable income."); *Tennyson*, 611 F.3d at 880 ("[T]he 'applicable commitment period' is a temporal term that prescribes the minimum [plan] duration . . . . The only exception to this minimum period, if unsecured claims are fully repaid, is provided in § 1325(b)(4)(B).").[6] We now agree with the other circuits' interpretation.

Our analysis begins with the statute's text. *Miranda v. Anchondo*, 684 F.3d 844, 849 (9th Cir.), *cert. denied*,

[6] In *Frederickson*, the Eighth Circuit expressly declined to decide whether such an exception to § 1325(b)'s temporal requirement exists when a debtor's projected disposable income is either zero or negative. 545 F.3d at 660 n.6.

133 S. Ct. 256 (2012). Although § 1325(b) is somewhat ambiguous, *see Baud*, 634 F.3d at 351 (noting that "the plain-language arguments" for and against an exception to § 1325(b)'s temporal requirement "are nearly in equipoise"), that subsection is best read to impose its temporal requirement regardless of the debtor's projected disposable income. Most significantly, the statute makes neither § 1325(b)(4)'s calculation of the applicable commitment period nor § 1325(b)(1)(B)'s requirement that a plan provide for payments over that period explicitly contingent on a particular level of projected disposable income. Thus, even though a debtor's payments to unsecured creditors will, at least initially, amount to $0 if the debtor has no projected disposable income, the statute requires the debtor to commit to the plan for the duration of the applicable commitment period.

Furthermore, "the words of a statute must be read in their context and with a view to their place in the overall statutory scheme." *Gale v. First Franklin Loan Servs.*, 701 F.3d 1240, 1244 (9th Cir. 2012) (internal quotation marks omitted). The structure of Chapter 13 confirms that § 1325(b)(1)(B) establishes a minimum plan duration even if the debtor has no projected disposable income. A debtor's applicable commitment period is not, as the panel reasoned in *Kagenveama*, "exclusively linked to § 1325(b)(1)(B) and the 'projected disposable income' calculation." 541 F.3d at 876. Rather, the applicable commitment period is expressly incorporated as a temporal limit for purposes of plan modification under § 1329.

Under § 1329(a), a bankruptcy court may modify a plan at any time after plan confirmation, so long as the modification occurs before the completion of payments under the plan. But a modified plan "may not provide for payments over a period that expires after *the applicable commitment period* under section 1325(b)(1)(B) after the time that the first payment under the original confirmed plan was due." 11 U.S.C. § 1329(c) (emphasis added). Thus, the statute defines the temporal window within which modified payments under § 1329 may be made by reference to the applicable commitment period. Indeed, the quoted text would make no sense unless the applicable commitment period describes a length of time that can expire or be altered. With respect to plan modification, then, the applicable commitment period serves as a measure of plan duration that is wholly unrelated to the amount of the debtor's disposable income.

A minimum duration for Chapter 13 plans is crucial to an important purpose of § 1329's modification process: to ensure that unsecured creditors have a mechanism for seeking increased (that is, non-zero) payments if a debtor's financial circumstances improve unexpectedly. *See Fridley v. Forsythe (In re Fridley)*, 380 B.R. 538, 543 (B.A.P. 9th Cir. 2007) ("Subsequent increases in [a debtor's] actual income can be captured for creditors by way of a § 1329 plan modification . . . ."). The bankruptcy court may modify a plan to "increase . . . the amount of payments on claims of a particular class." 11 U.S.C. § 1329(a)(1). In other words, even if a debtor has no projected disposable income at the time of plan confirmation, and his or her statutorily required payments under § 1325(b)(1)(B) are therefore $0, unsecured creditors may request a later modification of the plan to increase the debtor's payments if the debtor acquires disposable income during the pendency of the applicable commitment period. Creditors' opportunity to seek increased payments that correspond to changed circumstances would be undermined by an interpretation of § 1325(b)(1)(B) that relieves debtors from a minimum plan duration merely because they have no projected disposable income at the time of plan confirmation.[7]

Interpreting § 1325(b)(1)(B) to impose a minimum plan duration is also consistent with the prevailing interpretation in our circuit of §§ 1328(a) and 1329(a). Much as § 1329(a) permits modification until "completion of payments under [the] plan," § 1328(a) entitles the debtor to discharge "after completion by the debtor of all payments under the plan." In *Fridley*, the Ninth Circuit Bankruptcy Appellate Panel ("BAP") considered when a plan is "completed" for purposes of § 1329(a) and § 1328(a). The debtors in that case had not paid all allowed unsecured claims in full, but sought discharge after prepaying the payments that they were required to make under their confirmed plan. *Fridley*, 380 B.R. at 540. The BAP ruled that the debtors were not entitled to discharge because "prepayment does not 'complete' [a] plan for purposes of §§ 1328(a) or 1329." *Id.* at 545. Rather, it held, "[t]he 'applicable commitment period' in § 1325(b) is a temporal requirement . . . [and] the statutory concept of 'completion' of payments includes the completion of the requisite period of time." *Id.* at 546. The BAP reached that conclusion even though that case, like this one, involved debtors who had no projected disposable income and for

[7] This conclusion is bolstered by the sections of the Code that allow creditors to monitor a debtor's financial situation during the bankruptcy. For instance, Chapter 13 debtors, upon request, must provide post-petition reports of the amount and sources of their income, *see* 11 U.S.C. § 521(f)–(g), and the "obvious purpose of this self-reporting obligation is to provide information needed by a [creditor] to decide whether to propose hostile § 1329 plan modifications," *Fridley*, 380 B.R. at 544. The purpose of these monitoring provisions would be undermined if each plan did not have a minimum duration.

whom § 1325(b)(1)(B) accordingly would permit monthly payments of $0 to unsecured creditors. *Id.* at 540.

Because the text of § 1325(b) is ambiguous, we also look to legislative history in construing its temporal requirement. *See Wilson v. Comm'r*, 705 F.3d 980, 987–88 (9th Cir. 2013) (holding that we may consult legislative history as an aid to the interpretation of ambiguous text). Congress amended § 1325(b), adding the statutory text concerning the "applicable commitment period" that is at issue here, in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), Pub. L. No. 109-8, § 318, 119 Stat. 23. The legislative history of BAPCPA supports our interpretation of § 1325(b)(1)(B) as requiring a minimum plan duration:

> **Chapter 13 Plans To Have a 5–Year Duration in Certain Cases.** Paragraph (1) of section 318 of the Act amends Bankruptcy Code sections 1322(d) and 1325(b) to specify that a chapter 13 plan may not provide for payments over a period that is not less than five years if the current monthly income of the debtor and the debtor's spouse combined exceeds certain monetary thresholds. If the current monthly income of the debtor and the debtor's spouse fall below these thresholds, then the duration of the plan may not be longer than three years, unless the court, for cause, approves a longer period up to five years. The applicable commitment period may be less if the plan provides for payment in full of all allowed unsecured claims over a shorter period. Section 318(2), (3), and (4)

> make conforming amendments to sections 1325(b) and 1329(c) of the Bankruptcy Code.

H.R. Rep. No. 109–31(I), § 318, at 79 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 146 (boldface type added). Although the quoted section of the House Report is confusingly worded, its title suggests that above-median debtors are to be held to a five-year minimum plan duration without regard to their expenses or disposable income, unless they pay unsecured claims in full over a shorter period.

Finally, our interpretation of § 1325(b)(1)(B) is consistent with the policies that underlie the Bankruptcy Code and the BAPCPA amendments. "The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'" *Marrama v. Citizens Bank*, 549 U.S. 365, 367 (2007) (quoting *Grogan v. Garner*, 498 U.S. 279, 286, 287 (1991)). But that generality is not the end of the story. We have recognized that bankruptcy also serves the "often conflicting" policy of promoting creditors' interest in repayment. *Dumont v. Ford Motor Credit Co. (In re Dumont)*, 581 F.3d 1104, 1111 (9th Cir. 2009); *see also Ransom v. FIA Card Servs., N.A.*, 131 S. Ct. 716, 729 (2011) (describing "BAPCPA's core purpose [as] ensuring that debtors devote their full disposable income to repaying creditors"). The imposition of a minimum duration is consistent with both of those policies: By ensuring the availability of plan modification over the applicable commitment period, even when the debtor cannot make any payments at the outset, our reading permits Chapter 13 to operate as a mechanism for repayment *over time* by wage earners, in accordance with their actual ability to pay. *See generally* 8 *Collier on Bankruptcy* ¶ 1300.02 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2012).

In *Lanning*, the Supreme Court relied in part on similar considerations in rejecting an interpretation of § 1325(b) that would require courts to calculate projected disposable income using a "mechanical approach" that depends only on a debtor's current monthly income during the six-month period preceding the bankruptcy filing date. 130 S. Ct. at 2469–70. The Court favored a "forward-looking" approach that takes into account known or nearly certain information about changes in a debtor's earning power during the plan period. *Id.* at 2475. The policy justification for looking to future earnings is that a failure to do so "would deny creditors payments that the debtor could easily make." *Id.* at 2476. In other words, the statute is meant to allow creditors to receive increased payments from debtors whose earnings happen to increase. *Lanning* involved *pre*-confirmation adjustments to plan payments, "to account for known or virtually certain changes" in a debtor's income. *Id.* at 2475. But the same logic persuades us that Congress intended § 1325(b)(1)(B) to ensure a plan duration that gives meaning to § 1329's modification procedure as a mechanism for *post*-confirmation adjustments for unforeseen increases in a debtor's income. That mechanism will achieve its purpose most effectively if the Chapter 13 plan has a minimum duration within which modification is possible. Accordingly, the policy that underlies *Lanning* also supports our reading of § 1325(b)(1)(B).

III. Conclusion

In summary, we hold that a bankruptcy court may confirm a Chapter 13 plan under 11 U.S.C. § 1325(b)(1)(B) only if the plan's duration is at least as long as the applicable commitment period provided by § 1325(b)(4). Accordingly, we overrule *Kagenveama*'s holding regarding the meaning of "applicable commitment period" and affirm the bankruptcy court's ruling.

The mandate shall issue forthwith.

AFFIRMED.

PREGERSON, Circuit Judge, dissenting, with whom KOZINSKI, Chief Judge, joins:

The majority overrules our holding in *Maney v. Kagenveama* that the Chapter 13 "applicable commitment period" does not mandate a five-year plan length for above median debtors with no projected disposable income. 541 F.3d 868, 876 (9th Cir. 2008). The majority's interpretation of 11 U.S.C. § 1325(b)(1)(B) promotes goals that are at odds with Congress's purpose when it enacted Chapter 13 to "provide the debtor with a fresh start." H.R. REP. NO. 95-595, at 117 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6079. The majority also reads language into Chapter 13 bankruptcy law that is not present in the plain text of § 1325(b)(1)(B).

I. Bankruptcy's Purpose is to Provide Debtors with a Fresh Start

Congress enacted the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 to make "bankruptcy a more effective remedy for the unfortunate consumer debtor." H.R. REP. NO. 95-595, at 4 (1977). At the time, Congress lamented that "[e]xtensions on plans, new cases, and newly incurred debts put some debtors under court supervised repayment plans for seven to ten years." *Id.* at 117. Congress went on to say that such lengthy repayment plans were "the closest thing there is to indentured servitude." *Id.* Congress stated that "bankruptcy relief should be effective, and should *provide the debtor with a fresh start*." *Id.* (emphasis added). Chapter 13 bankruptcy was intended to be helpful to debtors and creditors. Debtors are able to preserve existing assets if they complete a repayment plan under the supervision of a Chapter 13 trustee. SCOTT ET AL., 8 COLLIER ON BANKRUPTCY 1300-12 (Lawrence P. King et al. eds., 15th ed. rev. 2007). Creditor interests are promoted through recoveries from future income that are not available in Chapter 7 liquidation. *Id.*

Congress updated the bankruptcy laws for the first time since 1978 with the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (2005). At the law's signing, President George W. Bush reiterated many of the purposes expressed by Congress in 1978:

> Our bankruptcy laws are an important part of the safety net of America. *They give those who cannot pay their debts a fresh start*. . . . Under the new law, Americans who have the ability to pay will be required to pay back at least a portion of their debts. Those who fall behind their state's median income will not be required to pay back their debts. . . . The act of Congress I sign today will protect those who legitimately need help, stop those who try to commit fraud, and bring greater stability and fairness to our financial system.

Press Release, White House Press Office, President Signs Bankruptcy Abuse Prevention, Consumer Protection Act (Apr. 20, 2005), *reprinted in* 2005 U.S.C.C.A.N. S7, 2005 (emphasis added).

II. The Applicable Commitment Period does not Mandate a Five-Year Chapter 13 Plan for Debtors with no Projected Disposable Income

Unlike the majority, I interpret § 1325 to mean that the applicable commitment period in which debtors are required to distribute projected disposable income to unsecured creditors applies only to debtors with projected disposable income.

Chapter 13 bankruptcy, as enacted in the Bankruptcy Reform Act of 1978, allows a debtor to use future income to pay off debt, while allowing her to keep her assets. *See* H.R. REP. NO. 95-595 at 118 (1977); *see also* 8 SCOTT ET AL., supra, at 1300–12. A Chapter 13 debtor is designated "above median" when her annualized "current monthly income," 11 U.S.C. § 101(10A), is greater than the yearly "median family income" in her state. 11 U.S.C. § 1325(b)(2)–(3); 11 U.S.C. 101(10A). The Floreses are above median debtors. When an above median Chapter 13 debtor's monthly expenses are greater than her monthly income as calculated under 11 U.S.C. § 707(b)(2)(A)–(B), she is deemed to have no projected disposable income. *See* 11 U.S.C. § 1325(b)(3). Here, it is undisputed that the Floreses' expenses are greater than their income and that they have no projected disposable income.

A Chapter 13 debtor is solely responsible for filing a proposed payment plan. 11 U.S.C. § 1321. Among the requirements for Chapter 13 plans are: that the plan is proposed and the petition is filed in good faith; that the holders of secured claims approve of the plan; that the debtor will be able to make all payments under and comply with the plan; and that the total payments to be made under the plan are not less than the amount that would be paid if the estate of the debtor were liquidated under Chapter 7. 11 U.S.C. § 1325(a)(3)–(7). Above median debtors are instructed that "the [Chapter 13] plan [they propose] may not provide for payments over a period that is longer than five years." 11 U.S.C. § 1322(d)(1).

The Floreses proposed a three-year plan during which they would make monthly payments of $122. The trustee objected to the Floreses' proposed plan on the ground that the plan should have required payments for five years, rather than three years. The bankruptcy judge increased the monthly payments to $148 and the length of the plan to five years; the monetary increase is not contested on appeal. It is undisputed that the Floreses' three-year Chapter 13 plan was proposed in good faith, that the Floreses are able to comply with the plan, and that the Floreses are paying more than they would be if they liquidated their assets under Chapter 7. It is also undisputed that the Floreses' three-year Chapter 13 bankruptcy plan was less than five years pursuant to § 1322(d)(1).

If a trustee or unsecured creditor objects to a debtor's Chapter 13 plan, the bankruptcy court may not approve the plan unless "the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period . . . will be applied to make payments to unsecured creditors under the plan." 11 U.S.C. § 1325(b)(1)(B). The applicable commitment period is three years for debtors with below median income and five years for debtors with above median income. 11 U.S.C. § 1325(b)(4)(A). Because the Floreses are above median debtors, their corresponding applicable commitment period is five years. The Floreses, however, have no projected disposable income. Thus, the Floreses will contribute no projected disposable income to unsecured creditors over their five year applicable commitment period.

Courts have approached the applicable commitment period in several different ways. Some courts, such as the majority here, endorse what is called the temporal approach, where the applicable commitment period is treated as a time requirement for Chapter 13 plan length. This approach has been endorsed by the Sixth, Eighth, and Eleventh Circuits, and district courts in the Fifth, Seventh, and Tenth Circuits. *See Baud v. Carroll*, 634 F.3d 327 (6th Cir. 2011); *In re Tennyson*, 611 F.3d 873 (11th Cir. 2010); *In re Frederickson*, 545 F.3d 652 (8th Cir. 2008); *In re Martin*, 464 B.R. 798 (C.D.Ill. 2012)*; In re Wing*, 45 B.R. 705 (D. Co. 2010)*; In re Meadows*, 410 B.R. 242 (N.D. Tx. 2009). Other courts have endorsed the monetary approach, where debtors contribute a set amount of money in a time period that may be shorter than the applicable commitment period. This approach has been endorsed by district courts in the Second and Third Circuits. *See In re Green*, 378 B.R. 30 (N.D.N.Y. 2007); *In re Vidal*, 418 B.R. 135 (M.D. Pa. 2009). I continue to endorse the hybrid approach we endorsed in *Kagenveama* and in the original *Flores* opinion. Under that approach, "the 'applicable commitment period' sets the minimum temporal duration of a plan, but it is inapplicable to a plan submitted . . . by a debtor with no 'projected disposable income.'" *Danielson v. Flores*, 692 F.3d 1021, 1027 (9th Cir. 2012).

The Chapter 13 "applicable commitment period" does not explicitly apply to debtors who qualify for Chapter 13 bankruptcy but have no projected disposable income. The majority concludes, however, that the "applicable commitment period" should determine the requisite length of a Chapter 13 plan for all debtors, whether or not they have projected disposable income. The majority disregards the portion of § 1325(b)(1)(B) that ties the "applicable commitment period" to the period of time when projected disposable income is supposed to be distributed to unsecured creditors. Under § 1325(b)(1)(B), the bankruptcy court may not approve the plan unless "the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period . . . will be applied to make payments to unsecured creditors under the plan." By doing so, the majority interprets § 1325(b)(1)(B) to say that when a trustee objects to a Chapter 13 plan, the bankruptcy court may not approve the plan unless "the plan provides that all of the debtor's [Chapter 13 *payments*] to be received in the applicable commitment period . . . will be applied to make payments to unsecured creditors under the plan." § 1325(b)(1)(B).

The majority's reading of § 1325(b)(1)(B) is at odds with the provision's plain language. A debtor's payments under a Chapter 13 bankruptcy plan are different than the disposable income a debtor is projected to earn over a period of years. After the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), a debtor does not need to have projected disposable income to qualify for, and make payments under, a Chapter 13 bankruptcy plan. *See* Henry E. Hildebrand II, *Impact of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 of Chapter 13 Trustees*, 79 AM. BANKR. L.J. 373, 389 (2005) ("The formula utilized in the means test [to determine projected disposable income] has no relation to the proposed plan and bears no relationship to the amount of money that actually may be available from a debtor for payments to unsecured creditors if a plan is confirmed.").

Nor is there any indication from Congress that the statutory difference between projected disposable income and Chapter 13 plan payments was an unintended consequence or oversight. *See* Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485, 567–68 (2005) (explaining that, like the Bankruptcy Reform Act of 1978, the BAPCPA of 2005 was adopted in the absence of economic depression and panic, and is the culmination of nearly ten years of work, involving hundreds of participants) (citation omitted).

The majority concludes that the exception permitting a shorter applicable commitment period under § 1325(b)(4)(B) does not apply to the Floreses. The majority's conclusion is correct, but the majority's reasoning is flawed. The majority understands shortening the applicable commitment period to be the same thing as shortening the length of the plan. The exception reads:

> [The applicable commitment period] may be less than 3 or 5 years . . . only if the plan provides for payment in full of all allowed unsecured claims over a shorter period.

Id. The majority reasons that the Floreses may not propose a plan with an applicable commitment period that is shorter than five years because the Floreses have not proposed a plan in which their unsecured claims will be paid in full. Under a reading of the plain text of the statute, however, the exception is inapplicable to the Floreses. Because the Floreses have no projected disposable income to distribute to unsecured creditors during the applicable commitment period, there is no applicable commitment period that applies to them. Thus, the § 1325(b)(4)(B) exception has no bearing on the length of the plan the Floreses may propose.

The majority's concern that only a mandatory minimum plan duration will "allow creditors to receive increased payments from debtors whose earnings happen to increase" is unfounded. Maj. 16. As above median debtors with no projected disposable income, the Floreses are bound by several statutory requirements that are helpful to creditors: that their plan be proposed in good faith; that they are able to comply with the plan and make all payments; and that they pay more in Chapter 13 bankruptcy than they would in Chapter 7 bankruptcy. Moreover, the Floreses' plan may be modified after the plan is confirmed, but before payments are completed, by the debtor, trustee, or the holder of an allowed unsecured claim. 11 U.S.C. § 1329(a). The plan may be modified to:

> (1) increase or reduce the amount of payments on claims of a particular class provided for by the plan;
>
> (2) extend or reduce the time for such payments;
>
> (3) alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of

> any payment of such claim other than under the plan; or
>
> (4) reduce amounts to be paid under the plan by the actual amount expended by the debtor to purchase health insurance.

Id. Section 1329(c) reiterates that even though a plan may be extended after it is confirmed, a "court may not approve a [Chapter 13 plan] period that expires after five years."

There is no statutory language to support the majority's finding that when Trustee Danielson objected to the Floreses' proposed plan length of three years, the bankruptcy court was statutorily prohibited from approving a plan shorter than five years in length.

CONCLUSION

Under the majority's reading of § 1325(b)(1)(B), above median debtors with no projected disposable income will be forced to propose five year plans in contravention of Congress's purpose when it implemented Chapter 13 to make "bankruptcy a more effective remedy for the unfortunate consumer debtor." H.R. REP. NO. 95-595, at 5966 (1977). The majority misreads § 1325(b)(1)(B) to require that the bankruptcy court approve a Chapter 13 plan only if all of a debtor's Chapter 13 payments—rather than projected disposable income—will be received during the applicable commitment period.

After Trustee Danielson objected to the Floreses' proposed plan, the bankruptcy court was not statutorily precluded from approving the Floreses' three-year Chapter 13 repayment plan. Therefore, I respectfully dissent.

FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL FOR THE FIRST CIRCUIT

BAP NO. MS 13-012

Bankruptcy Case No. 12-30538-HJB
Adversary Proceeding No. 12-03013-HJB

SHAWN G. KELLEY and
ANNEMARIE KELLEY,
Debtors.

STEVEN WEISS, Chapter 7 Trustee,
Plaintiff-Appellant,

v.

WELLS FARGO BANK, N.A.,
Defendant-Appellee.

Appeal from the United States Bankruptcy Court
for the District of Massachusetts
(Hon. Henry J. Boroff, U.S. Bankruptcy Judge)

Before
Haines, Deasy, and Godoy,
United States Bankruptcy Appellate Panel Judges.

Steven Weiss, Esq., and L. Alexandra Hogan, Esq., on brief for Plaintiff-Appellant.

Peter J. Haley, Esq., and David E. Fialkow, Esq., on brief for Defendant-Appellee.

October 1, 2013

Godoy, U.S. Bankruptcy Appellate Panel Judge.

Steven Weiss, the chapter 7 trustee (the "Trustee"), appeals from: (1) a bankruptcy court order denying his motion for summary judgment against Wells Fargo Bank, N.A. ("Wells Fargo") on his complaint seeking to avoid a certain mortgage granted by the debtors to Wells Fargo, because of an allegedly defective acknowledgment; and (2) granting Wells Fargo's cross-motion for summary judgment. For the reasons set forth below, we **REVERSE** the orders of the bankruptcy court and **REMAND** to the bankruptcy court for the entry of orders consistent with this opinion.

BACKGROUND

Shawn G. Kelley and Annemarie Kelley (the "Debtors") own real property located in Chicopee, Massachusetts (the "Property"). On June 11, 2007, the Debtors executed a Limited Power of Attorney, whereby they designated Shannon Obringer ("Obringer"), among others, as their "Agent" or "Attorney in Fact" to effectuate a refinancing of the Property with Wachovia Mortgage Corporation (now Wells Fargo, by virtue of a merger). The Debtors executed the Limited Power of Attorney in Holyoke, Massachusetts. On the same date, in Allegheny County, Pennsylvania, Obringer executed on their behalf a $280,000.00 mortgage (the "Mortgage") on the Property in favor of Wachovia Mortgage Corporation.[1]

Obringer signed the Mortgage for Shawn as follows: "Shawn G. Kelley by Shannon Obringer as attorney in fact." She executed the Mortgage on behalf of Annemarie similarly: "Annemarie Kelley by Shannon Obringer as attorney in fact."

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[1] The parties used a "Fannie Mae/Freddie Mac Massachusetts" preprinted form.

The acknowledgment, which was affixed to the Mortgage immediately following and on the same page as the Debtors' proxy signatures, recites:

COMMONWEALTH OF ~~MASSACHUSETTS~~, Pennsylvania, Allegheny County ss:

> On this 11 day of June 2007, before me, the undersigned notary public, personally appeared Shawn G. Kelley and Annemarie Kelley by Shannon Obringer as Attorney in Fact
>
> proved to me through satisfactory evidence of identification which was/were [left blank]
>
> to be the person(s) whose name(s) is/are signed on the preceding document, and acknowledged to me that he/she/they signed it voluntarily for its stated purpose.
>
> My Commission Expires: 10.4.09
>
> /s/ Magda Esposito
> Notary Public

(Seal)

The Debtors filed a voluntary petition for chapter 7 relief in the United States Bankruptcy Court for the District of Massachusetts in April 2012. Thereafter, the Trustee filed a two-count adversary complaint against Wells Fargo, alleging that the acknowledgment affixed to the Mortgage was defective because: (1) it stated that the Debtors appeared before the notary public when, in fact, they did not; and (2) it failed to state that Obringer personally appeared before the notary public and signed the Mortgage on behalf of the Debtors as their free act and deed.[2] Accordingly, in Count I, he asked the court to "determine the validity, priority and extent of the

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[2] The Trustee also alleged that because Obringer was not in receipt of the actual power of attorney on the date that she executed the Mortgage, her execution was unauthorized. Because the Trustee did not pursue this claim in the proceedings below or on appeal, we need not address it herein. See Evans Cabinet Corp. v. Kitchen Int'l, Inc., 593 F.3d 135, 148 n.20 (1st Cir. 2010) (stating argument not raised in opening brief is waived).

Mortgage as a lien on the Property and issue an order avoiding the Mortgage," pursuant to §§ 506(d) and 544 and Bankruptcy Rule 7001(2).[3] In Count II, he asked the court to "preserve the Mortgage for the benefit of the estate."[4]

Wells Fargo filed an answer, and the Trustee then moved for summary judgment as to both counts of the complaint. In his accompanying memorandum of law, the Trustee argued that Massachusetts law imposes a stringent requirement that a grantor or mortgagor express that the execution of the instrument was his or her free act and deed. Accordingly, he maintained that the acknowledgment in this case was materially defective because it "create[d] confusion and uncertainty as to whether the document was signed voluntarily by Ms. Obringer or by the Debtors." Asserting the status of a bona fide purchaser under § 544(a)(3), the Trustee contended that he was entitled to judgment as a matter of law. In support, he relied on a line of cases highlighted by Agin v. Mortg. Elec. Registration Sys., Inc. (In re Giroux), Adv. No. 08-1261, 2009 WL 1458173 (Bankr. D. Mass. May 21, 2009), aff'd, No. 09-CV-10988-PBS, 2009 WL 3834002 (D. Mass. Nov. 17, 2009); Agin v. Mortg. Elec. Registration Sys., Inc. (In re Bower), Adv. No. 10-1092, 2010 WL 4023396 (Bankr. D. Mass. Oct. 13, 2010); and DeGiacomo v. CitiMortgage, Inc. (In re Nistad), Adv. No. 11-1179, 2012 WL 272750 (Bankr. D. Mass. Jan. 30, 2012).

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[3] Unless otherwise indicated, the terms "Bankruptcy Code," "section" and "§" refer to Title 11 of the United States Code, 11 U.S.C. §§ 101, et seq., as amended. All references to "Bankruptcy Rule" are to the Federal Rules of Bankruptcy Procedure, and all references to "Rule" are to the Federal Rules of Civil Procedure.

[4] The Trustee subsequently amended the complaint to accurately reflect the name of the defendant, among other things.

Wells Fargo opposed the summary judgment motion and countered with a cross-motion for summary judgment. Wells Fargo challenged the Trustee's assertion of bona fide purchaser status, arguing that he "had actual and/or constructive knowledge of the Mortgage . . . ." Additionally, Wells Fargo disputed that Massachusetts law requires strict compliance with formalities in the execution of mortgage acknowledgments.

The bankruptcy court conducted a hearing on the Trustee's motion for summary judgment and Wells Fargo's cross-motion and opposition in February 2013. During the course of the hearing, the Trustee reiterated that the acknowledgment was defective because it failed to unequivocally and unambiguously identify who appeared in front of the notary, in what capacity, and whether the execution of the Mortgage was the free act and deed of the mortgagors.

Wells Fargo countered that the use of the term "by" in the context of the subject acknowledgment meant that the Debtors "were acting by or through or by the agency of their power of attorney Shannon Obringer." It stressed that "[a]ny objective bona fide purchaser . . . would not be confused that it was Shannon Obringer [who] was appearing before the notary," but neglected to address whether or how the acknowledgment expressed the voluntary nature of the grantors' execution of the Mortgage. Although Wells Fargo rejected the notion that Massachusetts is a "strict compliance state," it contended that the acknowledgment in this case satisfied either a substantial or strict compliance standard.

The court denied the Trustee's motion for summary judgment and granted Wells Fargo's cross-motion, ruling from the bench as follows:

> I just don't find this notarization to be ambiguous. . . . I read the language to mean that these two debtors appeared through a power of attorney and that the holder of that power of attorney personally stood before the notary.

> Now, granted it would have been nice if the he/she/it/their references further down were properly attended to, but until you get to that point, it's clear to me that it's the holder of the power of attorney that is standing before the notary. And I don't think that the failure to eliminate the extraneous words he/she/their/its creates sufficient ambiguity or any ambiguity really, other than shaking one's head and thinking, well, I should have crossed out some of these words, but I had no doubt on reading it who was standing there in front of the notary.
>
> Giroux is different. In Giroux no one was listed as standing in front of the notary and in Bower there was clearly the same ambiguity. And in Nistad it was actually somebody else's name. That's not what we have here.
>
> So I don't think I need to reach the question of whether there needs to be substantial or strict compliance, although I think this -- some room for arguing that in Massachusetts the standard ought to be substantially strict, but it doesn't really make any difference on my reading. I don't read the notarization to be defective and accordingly I am compelled to grant summary judgment to the defendant.

Thereafter, the court entered an order denying the Trustee's motion for summary judgment and a separate order, granting Wells Fargo's cross-motion for summary judgment. This appeal ensued.

On appeal, the Trustee maintains that the bankruptcy court erred when it denied his motion for summary judgment and granted Wells Fargo's cross-motion. Continuing to rely on Giroux, Bower, and Nistad, *supra*, he argues that the Mortgage is materially defective, due to "[t]hree fatal flaws": (1) the use of the phrase "personally appeared," when in fact it is undisputed the Debtors did not appear; (2) the failure to specify in the appropriate blank space the method by which the notary identified the signer (or signers) of the Mortgage; and (3) the failure to indicate whose free act and deed the notary was verifying. He continues to insist that in Massachusetts, every acknowledgment must unequivocally express whether the instrument was signed freely by the grantor. As in the proceedings below, Wells Fargo urges that "[t]he word 'by' unquestionably indicates through which individual the mortgagors appeared." There is also no question, Wells Fargo argues, that the execution was the free act and deed of Obringer, on behalf of the Debtors. Wells Fargo warns that voiding this Mortgage "may have grave consequences."

JURISDICTION

A bankruptcy appellate panel is "duty-bound" to determine its jurisdiction before proceeding to the merits even if not raised by the litigants. See Boylan v. George E. Bumpus, Jr. Constr. Co. (In re George E. Bumpus, Jr. Constr. Co.), 226 B.R. 724, 725-26 (B.A.P. 1st Cir. 1998). A panel may hear appeals from "final judgments, orders and decrees [pursuant to 28 U.S.C. § 158(a)(1)] or with leave of the court, from interlocutory orders and decrees [pursuant to 28 U.S.C. § 158(a)(3)]." Fleet Data Processing Corp. v. Branch (In re Bank of New England Corp.), 218 B.R. 643, 645 (B.A.P. 1st Cir. 1998) (internal quotation marks omitted). "An order granting summary judgment, where no counts remain, is a final order." Frykberg v. JPMorgan Chase Bank (In re Frykberg), 490 B.R. 652, 656 (B.A.P. 1st Cir. 2013) (citation omitted). Thus, we have jurisdiction.

STANDARD OF REVIEW

We review an order granting summary judgment *de novo*. DCC Operating, Inc. v. Rivera Siaca (In re Olympic Mills Corp.), 477 F.3d 1, 14 (1st Cir. 2007) (citing Razzaboni v. Schifano (In re Schifano), 378 F.3d 60, 66 (1st Cir. 2004)).

DISCUSSION

I. The Standards

A. The Summary Judgment Standard

"In bankruptcy, summary judgment is governed in the first instance by Bankruptcy Rule 7056." Desmond v. Varrasso (In re Varrasso), 37 F.3d 760, 762 (1st Cir. 1994). "By its express terms, the rule incorporates into bankruptcy practice the standards of Rule 56 of the Federal Rules of Civil Procedure." Id.; see also Fed. R. Bankr. P. 7056; Fed. R. Civ. P. 56.[5] "It is apodictic that summary judgment should be bestowed only when no genuine issue of material fact exists and the movant has successfully demonstrated an entitlement to judgment as a matter of law." In re Varrasso, 37 F.3d at 763 (citing Fed. R. Civ. P. 56(c)). The "mere existence of *some* alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; the requirement is that there be no *genuine* issue of *material* fact." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 247-48 (1986).

B. Section 544(a) and The Trustee's Avoidance Powers

Referred to as the "strong arm" clause, § 544(a) "gives a trustee various rights and powers, one of which is the power to avoid a transfer by the debtor of an unperfected security interest in real property to the same extent a bona fide purchaser could avoid the transfer, regardless of any actual knowledge of the trustee." In re Nistad, 2012 WL 272750, at *3 (citing

[5] Fed. R. Civ. P. 56(a) provides, in pertinent part, that "[t]he court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law. The court should state on the record the reasons for granting or denying the motion." Fed. R. Civ. P. 56(a).

11 U.S.C. § 544(a)(3);[6] Me. Nat'l Bank v. Morse (In re Morse), 30 B.R. 52, 54 (B.A.P. 1st Cir. 1983)). "While a trustee's avoidance power is not subject to any actual knowledge he or she may possess, it is subject to constructive knowledge." In re Nistad, 2012 WL 272750 at *5. "The extent of the [t]rustee's avoidance powers are determined by state law." Carrion v. USDA Rural Hous. Serv. (In re Roldan), Adv. No. 11-00094, 2012 WL 2221410, at *7 (Bankr. D.P.R. June 13, 2012) (citations omitted).

C. Acknowledgments: Their Purpose and Requirements in Massachusetts[7]

"An acknowledgment is the formal statement of the grantor to the official authorized to take the acknowledgment that the execution of the instrument was his free act and deed." McOuatt v. McOuatt, 69 N.E.2d 806, 810 (Mass. 1946). Mass. Gen. Laws ch. 183, § 29 provides:

> No deed shall be recorded unless a certificate of its acknowledgment or of the proof of its due execution, made as hereinafter provided, is endorsed upon or annexed to it, and such certificate shall be recorded at length with the deed to which it relates . . . .

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[6] Section 544(a) provides:

> The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by–
> . . . .
>> (3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

11 U.S.C. § 544(a)(3).

[7] The parties did not raise a choice-of-law issue. Moreover, the Mortgage provides that it "shall be governed by federal law and the law of the jurisdiction in which the Property is located."

Mass. Gen. Laws ch. 183, § 29. Thus, "if it is desired to record the deed in order to charge the world with notice of the conveyance, then it is necessary that the deed be acknowledged and that a certificate reciting this fact be attached to the deed." McOuatt, 69 N.E.2d at 809. "Doubtless, that is the principal function of a certificate of acknowledgment." Id. (citations omitted). "When 'an instrument of defeasance, not being acknowledged' is 'improvidently admitted to registration' then 'the record does not operate as constructive notice' of the conveyance." Allen v. Allen, No. 10 MISC 420492 GHP, 2013 WL 139318, at *10 (Mass. Land Ct. Jan. 10, 2013) (quoting Graves v. Graves, 72 Mass. 391, 392-93 (1856)).

Mass. Gen. Laws ch. 183, § 30 requires certain formalities in the execution of an acknowledgment. That statute provides, in pertinent part:

> The acknowledgment of a deed or other written instrument required to be acknowledged shall be by one or more of the grantors or by the attorney executing it. The officer before whom the acknowledgment is made shall endorse upon or annex to the instrument a certificate thereof. Such acknowledgment may be made–
>
> . . .
>
> (b) If without the commonwealth, in any state, territory, district or dependency of the United States, before a justice of the peace, notary public, magistrate or commissioner appointed therefor by the governor of this commonwealth, or, if a certificate of authority in the form prescribed by section thirty-three is attached thereto, before any other officer therein authorized to take acknowledgments of deeds.

Mass. Gen. Laws ch. 183, § 30(b). "It is well established law in Massachusetts that a defectively acknowledged mortgage cannot be legally recorded, and if recorded the mortgage does not, as a matter of law, provide constructive notice to future purchasers." In re Bower, 2010 WL 4023396, at *5.

In McOuatt, the seminal case regarding the validity of acknowledgments in Massachusetts, the Supreme Judicial Court instructed that in an acknowledgment "[n]o particular words are necessary as long as they amount to an admission that [the grantor] has voluntarily and freely executed the instrument." McOuatt, 69 N.E.2d at 810 (citations omitted). In that case, the court was called upon to construe a deed from the grantor to his wife, which was taken while the grantor was near death. According to the court:

> McOuatt told the physician that he knew what he was about to do, that he was to sign papers to protect his wife, and that he had been intending to do this for some time. The defendant obtained a deed which the attorney had prepared and brought it to the hospital. She told her husband what it was, and in her presence a hospital clerk, who was a notary public, asked him if he knew what he was about to sign. He said that he did and that he was turning over his property to his wife. He executed the deed by making an X . . . . At some time thereafter he requested the defendant to have the deed recorded, which she did. He died some eight hours after he executed the deed.

Id. at 808. Following a review of a master's report, the court was "unable to discover anything . . . that would justify a conclusion that McOuatt acknowledged the instrument of conveyance to be his free act and deed." Id. at 810. The court ruled that the "only conclusion that [could] be reached from the report [was] that the deed was not duly acknowledged as required by the statute." Id. (citation omitted). Thus, "[n]o effect [could] be given to it." Id.

As one Massachusetts bankruptcy court stated, McOuatt signaled the Supreme Judicial Court's "adherence to a stringent requirement, namely that a *grantor or mortgagor* expressly state to the notary that the execution of the instrument was *his or her* free act or deed." Giroux, 2009 WL 1458173, at *8 (emphasis added). Thus, "Massachusetts requires, in addition to the other formalities associated with acknowledgments, an affirmative declaration by the grantor or mortgagor." Id. Relying heavily on McOuatt, the bankruptcy courts in both Giroux and Bower held that the omission of the grantor's name on the acknowledgment form was a material defect that, despite the recording of the instrument, rendered the instrument incapable of providing constructive notice of the conveyance to a subsequent purchaser for value. See Giroux, 2009 WL 1458173, at *7; Bower, 2010 WL 4023396, at *3. Similarly, in Nistad, where an incorrect name was inserted in the identification clause of the acknowledgment, the bankruptcy court concluded that the mortgage was materially defective. Nistad, 2012 WL 272750, at *3-4.

Although the Massachusetts statutory scheme does not require specific language in an acknowledgment, it provides forms in an appendix which "may be used." Mass. Gen. Laws ch. 183, § 42. These include a form for the acknowledgment of an individual acting by an attorney. See Mass. Gen. Laws ch. 183 App., Form (14).[8] The language of the statutory form reflects that when a person is acting through an attorney, the attorney should acknowledge that he executed the instrument as the free act and deed of the grantor.[9] See supra note 8; see also Byers Bros. &

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[8] Form (14) provides:

> (Caption specifying the state and place where the acknowledgment is taken.)
>
> On this ______ day of _______ 19__, before me personally appeared A B, to me known to be the person who executed the foregoing instrument in behalf of C D, and acknowledged that he executed the same as the free act and deed of said C D.
>
> (Signature and title of officer taking acknowledgment. Seal, if required.)

Mass. Gen. Laws ch. 183 App., Form (14).

[9] We note that the acknowledgment form provided by Revised Executive Order No. 455 (04-04), promulgated by the Governor of the Commonwealth of Massachusetts and cited by the parties in their respective briefs, is at odds with Form (14). Revised Executive Order No. 455 provides, in pertinent part:

> (d) A notary shall take the **acknowledgment** of the signature or mark of persons acknowledging for themselves or in any representative capacity by using substantially the following form:

Co. Live Stock Comm. Corp. v. McKenzie, 239 P. 525, 525 (N.M. 1925) (discussing statutory form for New Mexico and explicitly stating that when a natural person is acting by an attorney, the attorney must acknowledge that he executed the instrument as the free act and deed of his principal).

II. The Standards Applied

Here, the parties did not use Form (14), the Massachusetts statutory form for the acknowledgment of an individual acting in a representative capacity. Instead, they adapted a pre-printed form for taking the acknowledgment of an individual acting on his or her own behalf. We are therefore confronted with questions concerning the acknowledgment's sufficiency under Massachusetts law.

Our examination logically begins with the first paragraph of the acknowledgment, which recites, in pertinent part: "[p]ersonally appeared Shawn G. Kelley and Annemarie Kelley *by*

> On this ____ day of ______, 20__, before me, the undersigned notary public, personally appeared ________ (name of document signer), proved to me through satisfactory evidence of identification, which were ________, to be the person whose name is signed on the proceeding or attached document, and acknowledged to me that (he) (she) signed it voluntarily for its stated purpose.
>
> (as partner for ______, a partnership)
> (as _______ for ______, a corporation)
> (as attorney in fact for ______, the principal)
> (as ______ for ______, (a) (the) ______)

___________________ (official signature and seal of notary)

Revised Executive Order No. 455 (04-04) § 5(d). Unlike Form (14), the Executive Order form does not clearly express that the voluntariness of the execution relates to the principal when the execution is performed by an individual acting in a representative capacity. This failure reflects the danger of attempting to craft a one-size-fits-all acknowledgment form. In any event, Form (14) supercedes the Executive Order form. See Revised Executive Order No. 455 § 1(c) (stating "[n]othing in this Executive Order supercedes the provisions of any court rule, including court forms, Massachusetts General Law, including but not limited to, chapter 183, section 42 or the forms set forth in the appendix thereto").

Shannon Obringer as Attorney in Fact." (emphasis added). Mindful that "by" means "through the agency or instrumentality of," see http://www.merriam-webster.com/dictionary/by, we are unpersuaded by the Trustee's first argument, that this language is so confusing that "one is forced to guess who appeared before the notary public." Although inartful, the challenged language sufficiently signals that Obringer was present in a representative capacity.

Our analysis next proceeds to the remaining paragraphs of the acknowledgment, which provide:

> [p]roved to me through satisfactory evidence of identification which was/were [left blank]
>
> to be the person(s) whose name(s) is/are signed on the preceding document, and acknowledged to me that he/she/they signed it voluntarily for its stated purpose.

We are similarly unconvinced by the Trustee's second argument, that the notary's failure to fill in the blank provided for specifying the evidence of identification, which was presented to the notary, standing alone, is a "fatal flaw." Courts already reject this argument, on the ground that the requirement for "satisfactory evidence of identity" is imposed only by Revised Executive Order No. 455 (04-04), and not by statute. In re Dessources, 430 B.R. 330, 335 (Bankr. D. Mass. 2010). Because the Executive Order does not supersede anything in Mass. Gen. Laws ch. 183, § 42, or the forms set forth in the appendix thereto, the argument that the blank identifiers affect the validity of the acknowledgment is easily dispatched.

We agree with the Trustee's third argument, however, namely that the foregoing language fails to unequivocally express that the execution of the Mortgage was the free act and deed of the principals, i.e., the Debtors, and that this flaw is, indeed, fatal. Here, the preprinted form utilized by the notary combined with her failure to attend to the blank space and the inapplicable verbiage creates ambiguity concerning whether the execution of the Mortgage was the voluntary act of the Debtors. Although the acknowledgment contains a recitation that the Mortgage was signed "voluntarily for its stated purpose," we are left to speculate whether the voluntariness relates to the principals (the Debtors) or to the attorney-in-fact (Obringer). Wells Fargo's assertion that the acknowledgment was clearly Obringer's free act and deed is not only unsupported by the language of this acknowledgment, but, more importantly, misapprehends the essential requirement for a valid acknowledgment of an individual acting in a representative capacity: namely, that the attorney must acknowledge that he executed the instrument as the free act and deed of the grantor. Moreover, a review of the language of this acknowledgment does not justify a conclusion that Obringer ever said anything to the one who made out the certificate of acknowledgment to indicate that the Mortgage was the voluntary act of the Debtors.

We therefore conclude that the acknowledgment is materially and patently defective under Massachusetts law, such that it is incapable of providing constructive notice to a subsequent purchaser for value. To conclude otherwise would undermine the acknowledgment's very purpose. Thus, the bankruptcy court erred in denying the Trustee's motion for summary judgment on his complaint to avoid the Mortgage pursuant to his § 544 strong arm powers and in granting Wells Fargo's cross-motion for summary judgment.

CONCLUSION

For the foregoing reasons, we **REVERSE** the order granting Wells Fargo's cross-motion for summary judgment, and **REVERSE** the order denying the Trustee's motion for summary judgment. We **REMAND** to the bankruptcy court for the entry of orders consistent with this opinion.

FILE
IN CLERKS OFFICE
SUPREME COURT, STATE OF WASHINGTON
DATE OCT 03 2013
Madsen, C.J.
CHIEF JUSTICE

This opinion was filed for record
at 8:00 am on Oct 3, 2013
Ronald R. Carpenter
Supreme Court Clerk

IN THE SUPREME COURT OF THE STATE OF WASHINGTON

STEWART TITLE GUARANTY COMPANY, a Texas corporation, Appellant, v. STERLING SAVINGS BANK, a Washington corporation; STERLING FINANCIAL CORPORATION, a Washington corporation, Defendants, WITHERSPOON, KELLEY, DAVENPORT & TOOLE, PS, a Washington corporation; DUANE M. SWINTON and JANE DOE SWINTON, and the marital community composed thereof, Respondents.	NO. 87087-0 EN BANC Filed OCT 03 2013

GORDON McCLOUD, J.—A title insurer, Stewart Title Guaranty Company, hired the law firm Witherspoon, Kelley, Davenport & Toole PS (collectively Witherspoon) to defend its insured, Sterling Savings Bank, from a claim of lien priority on real property by a construction company (Mountain West). The claim was resolved in favor of Mountain West, and Stewart Title then sued Witherspoon for malpractice. Stewart Title claimed the law firm had improperly failed to raise the viable defense of equitable subrogation. Witherspoon defended by arguing that there was no duty and no breach, specifically, (1) that Witherspoon's client was Sterling, not Stewart Title, and hence Witherspoon owed no duty to Stewart Title that would support that nonclient third party payor's claim of malpractice; and (2) that equitable subrogation would not have been a viable argument anyway.

Witherspoon moved for summary judgment on both grounds: (1) that it owed a duty only to the client, Sterling, rather than to the payor, Stewart Title; and (2) that an equitable subrogation argument would have failed. The trial court ruled against Witherspoon on the first, no-duty, ground but agreed with it on the second, no-breach, ground. The court therefore granted summary judgment in favor of Witherspoon. We accepted review of both the duty issue and the equitable subrogation issue. We affirm the trial court's grant of summary judgment dismissing Stewart Title's malpractice case against Witherspoon on the basis that Witherspoon owed no duty to Stewart Title. We do not reach the equitable subrogation issue.

FACTS

Because we resolve this case on the basis that Witherspoon owed no duty to Stewart Title that would permit Stewart Title to maintain a malpractice action against Witherspoon, we do not reach the parties' equitable subrogation arguments. Consequently, we recite the facts relevant to the issue of Witherspoon's duty to Stewart Title.

A lender—Sterling—agreed to lend money to a borrower to purchase property to develop. As a condition of the loan, Sterling required a first priority security interest in the property. The lender's title insurance company—Stewart Title—negligently failed to inspect the property before the loan went through; as a result, Stewart Title failed to discover that the builder—Mountain West—had already started construction on the property. By statute, Mountain West gained an interest in the form of a mechanics' lien as of the date construction began.

After a payment dispute arose, Mountain West discovered that its mechanics' lien held first position. The lender, Sterling, asked its title insurance company, Stewart Title, to defend it in the ensuing foreclosure action, because the insurer's policy covered mechanics' liens. Stewart Title admitted its duty to defend Sterling and hired Sterling's long time law firm—Witherspoon—to do so.

In that underlying lawsuit, Witherspoon stipulated that Mountain West had first priority and sought a swift settlement with the construction company. At some point after the stipulation, Stewart Title fired Witherspoon over disagreements related to whether equitable subrogation was a viable defense for Sterling. Stewart Title hired new counsel, who tried to argue that Sterling was equitably subrogated to the prior interests it paid off and therefore had priority after all. The trial court held the parties were bound by the earlier stipulation and disallowed the equitable subrogation defense.

Stewart Title then sued the law firm, Witherspoon, for malpractice based on Witherspoon's failure to raise the equitable subrogation defense for the lender, Sterling, before stipulating the construction company had priority. As discussed above, Witherspoon argued that (1) its client was the insured lender, not the title insurer, and it therefore owed no duty to the title insurer that would permit the insurer to sue the firm for malpractice; and, alternatively, that (2) an equitable subrogation argument would have failed under the facts of the case. As also discussed above, the trial court rejected Witherspoon's argument that it had no duty and denied Witherspoon's motion for summary judgment based on lack of a duty to Stewart Title. But the trial court agreed with Witherspoon that equitable subrogation would not have been a viable argument at the time of the underlying trial and granted summary judgment to Witherspoon on that basis. We accepted review and now affirm the grant of summary judgment in favor of Witherspoon, albeit on a different basis than that adopted by the trial court.

ANALYSIS

I. STANDARD OF REVIEW

We review a trial court's order granting summary judgment de novo. *Mohr v. Grantham*, 172 Wn.2d 844, 859, 262 P.3d 490 (2011) (citing *Rivas v. Overlake Hosp. Med. Ctr.*, 164 Wn.2d 261, 266, 189 P.3d 753 (2008)). We view all the evidence in the light most favorable to the nonmoving party. *Id.* Summary judgment is appropriate if "there is no genuine issue as to any material fact and . . . the moving party is entitled to a judgment as a matter of law." CR 56(c).

II. ATTORNEYS' DUTIES TO NONCLIENTS

Witherspoon's only client was Sterling. Stewart Title was a nonclient third party payor. In *Trask v. Butler*, 123 Wn.2d 835, 872 P.2d 1080 (1994), this court expressly adopted a multifactor test to determine whether an attorney may be liable for malpractice to such a nonclient third party. The relevant factors are:

> 1. The extent to which the transaction was intended to benefit the plaintiff [that is, the third party suing the attorney];
>
> 2. The foreseeability of harm to the plaintiff;

3. The degree of certainty that the plaintiff suffered injury;

4. The closeness of the connection between the defendant's [that is, the attorney's] conduct and the injury;

5. The policy of preventing future harm; and

6. The extent to which the profession would be unduly burdened by a finding of liability.

Trask, 123 Wn.2d at 843. We explained that the first factor is the "primary inquiry" in determining an attorney's liability to third parties. *Id.* at 842. We further explained that "under the modified multi-factor balancing test, the threshold question is whether the plaintiff is an intended beneficiary of the transaction to which the advice pertained" and that "no further inquiry need be made unless such an intent exists." *Id.* at 843.

We have addressed the *Trask* factors only once, holding under very different facts that an insurance claim adjuster had a duty to the unrepresented claimants she had helped. *Jones v. Allstate Ins. Co.*, 146 Wn.2d 291, 307-08, 45 P.3d 1068 (2002). The issue presented here, in contrast, is whether an attorney hired by a title insurer to represent its insured owed a duty to the nonclient insurer and, hence, whether that insurer can sue the lawyer for negligently representing the insured during the defense. This is an issue of first impression in Washington.

Here, the trial court found that Witherspoon owed a duty to Stewart Title under *Trask*. It held that under the first *Trask* factor,[1] Stewart Title was an intended beneficiary of Witherspoon's representation of Stewart Title's insured. We disagree.

The trial court based its determination that Stewart Title was an intended beneficiary under *Trask* on two legal conclusions. First, it found that the interests of Stewart Title and Witherspoon were aligned during the representation. Second, it found a contractual basis for a duty running from Witherspoon to Stewart Title. We disagree with both conclusions.

i. Alignment of Interests Is Insufficient To Establish that Witherspoon Owed a Duty to Stewart Title

The alignment of interests is insufficient to find a duty running from Witherspoon to Stewart Title for purposes of a malpractice claim. Stewart Title argues, in support of the trial court's decision, that as long as there is no actual conflict of interest between an insurer and its insured, a nonclient insurer is *presumed* to be an intended beneficiary and "can bring a claim for malpractice" against its insured's attorney. Suppl. Br. of Appellant at 3; *see also id.* at 20. Under Stewart Title's analysis, unless there is an actual and demonstrable conflict

[1] The first and most important factor is "the extent to which the transaction was intended to benefit [the nonclient suing the attorney]." *Trask*, 123 Wn.2d at 843.

of interest, an insurer may always sue its insured's attorney for malpractice under *Trask*.

We reject that analysis. The *Trask* standard requires a showing that the "transaction was *intended* to benefit" a third party to some extent before we will permit that third party to sue for malpractice. *Trask*, 123 Wn.2d at 843 (emphasis added). The fact that an insurer's and insured's interests happen to align in some respects—though perhaps not in all respects, as shown by contrasting Witherspoon's strategy of seeking a speedy, yet just, settlement with Stewart Title's different strategy—does not by itself show that the attorney or client *intended* the insurer to benefit from the attorney's representation of the insured.[2]

Indeed, a contrary conclusion would conflict with *Trask*. It could also make any third party payor an intended beneficiary of a legal services contract to whom

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[2] We recognize that other jurisdictions have come to a different conclusion. *See Paradigm Ins. Co. v. Langerman Law Offices, P.A.*, 200 Ariz. 146, 155, 24 P.3d 593 (Ariz. 2001) (holding that a "lawyer's services are ordinarily intended to benefit both insurer and insured when their interests coincide"); *Atlanta Int'l Ins. Co. v. Bell*, 438 Mich. 512, 523, 475 N.W.2d 294 (1991) (permitting insurer to bring malpractice action where "the interests of the insurer and the insured generally merge"); *Unigard Ins. Group v. O'Flaherty & Belgum*, 38 Cal. App. 4th 1229, 1236-37, 45 Cal. Rptr. 2d 565 (1995) (permitting malpractice action "where there is otherwise no actual or apparent conflict of interest between the insurer and the insured" (emphasis omitted)); *see also* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 51 cmt. g (2000) (stating, regarding a test with an intended beneficiary factor similar to Washington's, that "a lawyer designated by an insurer to defend an insured owes a duty of care to the insurer with respect to matters as to which the interests of the insurer and insured are not in conflict").

a duty of care runs, in violation of RPC 5.4(c).[3] We cannot endorse an analysis that would violate both of these settled rules of law.

ii. Witherspoon's Duty To Inform Stewart Title Is Insufficient To Establish that Witherspoon Also Owes a Duty of Care to Stewart Title that Supports a Malpractice Claim by Stewart Title

The trial court also held that Stewart Title was an intended beneficiary of Witherspoon's representation of Sterling because of Stewart Title's retention letter. It found that the retention letter created a contractual duty on the part of Witherspoon to keep Stewart Title informed about the progress of the lien priority litigation. We conclude that Witherspoon's duty to inform Stewart Title is insufficient to establish a further duty of care permitting Stewart Title to bring a malpractice claim based on an alleged breach of a different duty to a different entity—that is, Witherspoon's duty of care to its client, Sterling.

Based on the agreement of the parties and the terms of the retention letter sent to Witherspoon by Stewart Title, the trial court found a duty on the part of Witherspoon to inform Stewart Title. Moreover, it found that the "duty that Witherspoon could have to Stewart Title, a nonclient, comes from the duty to inform." Clerk's Papers (CP) at 523-24.

[3] RPC 5.4(c) states, "A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services."

The trial court erred in finding in this case that a duty to inform could lead to a duty of care to an entity other than the client for malpractice purposes. An attorney hired to represent a client by a third party payor may generally, as part of the terms of the retention, have a duty to keep the payor informed (within the bounds of the attorney-client privilege and the duty of confidentiality). But such a limited duty to inform the nonclient third party payor does not give rise to a broad duty of care that would support a malpractice claim by the third party payor. It does not create that separate duty of care for the same reasons that the client's and nonclient payor's alignment of interests does not create such a separate duty: first, because acceptance of a duty to inform a nonclient third party payor does not show that the attorney's representation was *intended* to benefit the third party payor, as *Trask* requires; and second, because an attorney cannot contract away his or her professional duty to "not permit a person who . . . pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services." RPC 5.4(c).

The trial court concluded that Stewart Title was an intended beneficiary of Witherspoon's representation of Sterling and thus that Witherspoon owed a duty of careful representation to Stewart Title, based in part on finding a contractual duty on the part of Witherspoon to inform Stewart Title and in part on the alignment of interests between Witherspoon and Stewart Title. We hold that an alignment of interests is insufficient to support a duty of care to a nonclient. We further hold that a contractual duty to inform is insufficient to support a duty of care to a nonclient. Putting both of them together does not cure the insufficiency. Therefore, the trial court erred in finding that the first *Trask* factor was satisfied and should have granted Witherspoon's motion for summary judgment based on lack of a duty to Stewart Title.

The trial court did, however, grant summary judgment to Witherspoon on the basis that equitable subrogation could not have succeeded as a defense in the lien priority lawsuit upon which Stewart Title's malpractice action was based. We therefore affirm the trial court's grant of summary judgment to Witherspoon, albeit on different grounds.[4]

CONCLUSION

[4] We take no position on whether the trial court's analysis of the parties' equitable subrogation claims was correct. We note, however, that the equitable subrogation issue in this case is very limited and fact-specific. The malpractice claim is based on professional decisions made in 2008, not today, and the viability of the malpractice claim therefore depended on not just whether the lawyers' decisions were incorrect but whether those decisions demonstrated a failure, at the time they were made, to "exercise the degree of care, skill, diligence, and knowledge commonly possessed and exercised by a reasonable, careful, and prudent lawyer in the practice of law in this jurisdiction." *Hizey v. Carpenter*, 119 Wn.2d 251, 261, 830 P.2d 646 (1992) (citing *Hansen v. Wightman*, 14 Wn. App. 78, 90, 538 P.2d 1238 (1975)).

The trial court erred when it found a duty running from Witherspoon to Stewart Title for purposes of a malpractice claim by Stewart Title. Our case law establishes that a nonclient may not pursue a claim of malpractice against another's attorney unless the nonclient shows, as a threshold matter, that the attorney's representation was to some extent intended to benefit the nonclient. Stewart Title has not shown that it was an intended beneficiary of Witherspoon's services to Sterling. Thus Stewart Title cannot pursue a malpractice claim against Witherspoon based on Witherspoon's services to Sterling. The trial court granted summary judgment in favor of Witherspoon on a different basis. We therefore affirm that order, but on different grounds.

Gordon McCloud, J.

WE CONCUR:

Madsen, C.J.	J.M. Johnson, J.
C. Johnson, J.	Stephens, J.
Owens, J.	Wiggins, J. - result only
Fairhurst, J.	González, J.

Filed 9/23/13

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION SEVEN

TERRY ANN SWANSON, Plaintiff and Appellant, v. STATE FARM GENERAL INSURANCE COMPANY, Defendant and Respondent.	B240016 (Los Angeles County Super. Ct. No. EC055177)

APPEAL from a judgment of the Superior Court of Los Angeles County, Laura A. Matz, Judge. Affirmed.

Blasco & Hawekotte General Counsel Services and Richard E. Blasco for Plaintiff and Appellant.

Robie & Matthai and Kyle Kveton for Defendant and Respondent.

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INTRODUCTION

An insurer agrees to provide a defense with a reservation of rights and approves independent counsel selected by the insured to represent the insured in an underlying tort action, pursuant to Civil Code section 2860 and *San Diego Federal Credit Union v. Cumis Ins. Society, Inc.* (1984) 162 Cal.App.3d 358 (*Cumis*). The insurer subsequently withdraws all reservations of rights and coverage defenses that give rise to the insured's right to *Cumis* counsel.[1] Must the insurer continue to pay the insured's *Cumis* counsel after the insurer's withdrawal of the *Cumis*-triggering reservations eliminated the conflict that created the need for *Cumis* counsel? We answer this question in the negative.

Plaintiff Terry Ann Swanson appeals from a judgment entered after the trial court had granted a motion for summary judgment in favor of defendant State Farm General Insurance Company (State Farm). The trial court determined that State Farm did not breach its insurance contract with Swanson by refusing to pay any attorneys' fees incurred by her *Cumis* counsel after State Farm withdrew its reservation of rights. We affirm.

FACTUAL BACKGROUND

State Farm issued Swanson Homeowners Insurance Policy No. 71-71-9553-0 (the Policy) that provided personal and general liability coverage for her real property in La Crescenta, for the period of May 12, 2004 to May 12, 2006. The Policy provided that if a third party brought a suit against an insured for damages for covered "bodily injury" or "property damage" caused by an "occurrence," State Farm would "provide a defense at our expense by counsel of our choice." (Bold omitted.)

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[1] Courts often refer to the independent counsel hired by the insured as "*Cumis* counsel," a term we will use in this opinion. (See *The Housing Group v. PMA Capital Ins. Co.* (2011) 193 Cal.App.4th 1150, 1152, fn. 1.)

On October 21, 2005 Swanson's personal attorney, Richard E. Blasco, requested that State Farm defend and indemnify Swanson in an action on a cross-complaint by her neighbors, Mark and Patricia Bitetti (the Bitetti Action), which alleged claims for premises liability and negligence in connection with an incident that occurred on January 10, 2005. Blasco was already representing Swanson in the underlying lawsuit on her claims against the Bitettis for damage to her property and for personal injury caused by failure of the Bitettis' retaining wall after the La Crescenta area experienced substantial rainfall in December 2004.

On November 4, 2005 State Farm wrote to Swanson and stated that it was accepting "the defense of the lawsuit subject to our reservation of rights." State Farm tentatively accepted Swanson's choice of Blasco as her *Cumis* counsel, subject to his compliance with the requirements of Civil Code section 2860.[2] State Farm asserted that there was "a question whether we have a duty, under the terms of the policy, to defend or indemnify" Swanson for the loss alleged in the Bitetti Action. The rights reserved by State Farm involved questions regarding whether some of the claimed damages "would qualify as bodily injury or property damage as defined by the policy," whether they "arose out of an occurrence as defined by the policy," and whether they were excluded from coverage by policy provisions excluding certain bodily injury or property damage. (Bold omitted.) State Farm also advised Swanson that it was "reserving the right to supplement or amend this reservation of rights to add or remove any policy defenses," as well as "the right to withdraw this defense if we determine there is no duty to defend or indemnify you." State Farm also reserved the right "to submit any disagreement over [defense attorney] fees to arbitration as outlined in C[ivil] C[ode section] 2860."

On December 5, 2005 Blasco responded that the terms of State Farm's November 4, 2005 letter were generally acceptable, except for State Farm's proposed

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[2] Civil Code section 2860 sets forth qualifications and hourly rate limits for independent counsel paid by an insurer along with related provisions governing some aspects of the relationship between independent counsel chosen by the insured (i.e., *Cumis* counsel) and counsel chosen by the insurer. (See fn. 9, *post*.)

hourly rate of $150. Blasco requested an hourly rate of $200, the same rate Swanson had been paying him. Blasco also provided information about himself and his firm to demonstrate his qualifications to serve as defense counsel under Civil Code section 2860.

On December 20, 2005 State Farm notified Blasco that he had met the requisite statutory qualifications for *Cumis* counsel but advised him that the compensated hourly rate would remain $150. The parties resolved the issue by Blasco agreeing to accept payment from State Farm at the hourly rate of $150 and Swanson agreeing to pay Blasco the $50 hourly rate difference.

On April 11, 2006 State Farm amended its original reservation of rights and withdrew certain policy defenses it had previously asserted in its reservation of rights. It is undisputed that State Farm's withdrawal of these reservations "eliminated the *Cumis*-triggering conflict" between the insurer and its insured.[3] State Farm informed Swanson that it had chosen and retained an attorney from the firm of Procter, McCarthy and Slaughter (Procter) to "take over the defense of" the Bitetti Action. State Farm also advised Swanson that "elimination of the *Cumis*-triggering conflict" relieved it of its obligation "to pay for independent counsel." State Farm explained that "in the absence of any obligation to provide independent counsel of the insured's choosing, State Farm had the right to 'provide a defense at our expense by counsel of our choice.'"

Prior to the April 11, 2006 letter, State Farm had not asked for Swanson's consent to turn control of the Bitetti Action over to Proctor or to have Proctor serve as defense cocounsel with Blasco. Swanson subsequently agreed to add Proctor as cocounsel without removing Blasco as her defense counsel. Proctor and Blasco then worked together as cocounsel in the defense of the Bitetti Action. Blasco continued billing State Farm and Swanson as he had been doing before State Farm withdrew the reservations of

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3 In response to State Farm's undisputed material fact number 7, Swanson stated: "Undisputed legal conclusion that: 'The effect of the withdrawal of certain reservations in the April 11, 2006 [letter] eliminated the *Cumis*-triggering conflict.'"

rights that had triggered Swanson's right to *Cumis* counsel. State Farm, however, did not make any further payments to Blasco.[4]

The Bitetti Action went to trial in November 2006. Both Blasco and Proctor defended Swanson. The jury found in favor of Swanson and did not award the Bitettis any monetary damages.[5] The trial court in the Bitetti Action entered judgment on January 14, 2008.

PROCEDURAL BACKGROUND

Swanson filed this action in April 2009.[6] Her first cause of action asked the court to submit the dispute over Blasco's fees to arbitration pursuant to the terms of the Policy and Civil Code section 2860. Her second cause of action for breach of insurance contract sought damages in the amount of $60,384.76 for post-April 11, 2006 attorneys' fees billed by Blasco for the defense of the Bitetti Action. Her third cause of action for breach of the covenant of good faith and fair dealing sought damages for mental suffering and emotional distress, as well as punitive damages.

In July 2009 Swanson filed a motion to compel arbitration of the Blasco fee dispute.[7] On August 28, 2009 the trial court denied the motion.

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4 State Farm did pay Swanson in February 2009 all $10,116.54 in costs she incurred in the Bitetti Action.

5 Swanson had settled her claims against the Bitettis for $300,000.

6 Swanson instituted this action by filing a petition asserting three causes of action: (1) to compel arbitration pursuant to Civil Code section 2860, (2) breach of insurance contract, and (3) tortious breach of insurance contract. On January 14, 2011 the trial court converted the case from a petition to an unlimited civil action, and changed the Los Angeles Superior Court case number from ES012997 to EC055177.

7 From the case summary for *Swanson v. State Farm General Insurance Company*, Los Angeles County Superior Court Case No. ES012997, we take judicial notice on our own motion of July 27, 2009 as the date Swanson filed the motion to compel arbitration. (See Evid. Code, §§ 452, subd. (d), 459.)

In October 2010 Swanson filed a motion for summary adjudication on all three causes of action. In January 2011 the trial court denied the motion, noting that the court had previously decided the arbitration issue in August 2009.

In September 2011 State Farm filed a motion for summary judgment or in the alternative for summary adjudication. State Farm argued that when it withdrew all *Cumis*-triggering reservations of rights regarding Swanson's defense on April 11, 2006, Swanson was no longer entitled to independent *Cumis* counsel paid by State Farm. State Farm argued that at that point it was entitled to appoint counsel of its choosing and had no further obligation to pay for Swanson's personal attorney. Swanson filed an opposition to State Farm's motion for summary judgment and a cross-motion for summary adjudication on the issues in Swanson's previously-denied motion for summary adjudication. State Farm argued on reply that the court could not consider Swanson's cross-motion because she had filed it on only 14 days' notice in violation of Code of Civil Procedure section 437c.

On January 17, 2012 the trial court granted State Farm's motion for summary judgment and denied Swanson's cross-motion. The trial court stated: "The parties agree that there is no disputed issue of material fact and that this motion presents purely an issue of law of first impression. That issue is whether, after *Cumis*-triggering reservations are withdrawn by an insurer, an insurer remains obligated to pay the insured's personal counsel if the insured does not wish to be represented by panel counsel on a going-forward basis." The trial court concluded that "when State Farm ultimately withdrew its *Cumis*-triggering reservations, plaintiff insured was no longer entitled to independent *Cumis* counsel. Under the terms of the Policy, where there was no *Cumis*-trigger, State Farm had the right to 'provide a defense at our expense by counsel of our choice.'" The court rejected Swanson's claim that State Farm, Swanson, and Blasco had created a modified insurance agreement when State Farm and Blasco agreed in 2005 to a rate of reimbursement for his fees. The trial court stated: "Agreeing on the hourly rate was the satisfaction of an obligation imposed by statute. Civil Code section 2860 does not expand or broaden an insurer's duty to defend." On February 2, 2012 the trial court entered judgment in favor of State Farm. Swanson filed a timely notice of appeal.

DISCUSSION

The primary issue on appeal is whether State Farm had the right to take control of the litigation with an attorney of its choosing and to cease paying Blasco, *Cumis* counsel chosen by Swanson, after State Farm withdrew its *Cumis*-triggering reservation of rights. We agree with the trial court that State Farm had such a right. As we explain below, an insurer has a duty to provide *Cumis* counsel to its insured only while the insurer maintains a *Cumis*-triggering reservation of rights. Thus, when State Farm withdrew its *Cumis*-triggering reservation of rights, it no longer had an obligation to allow Swanson to control the litigation or an obligation to pay the attorneys' fees of Swanson's *Cumis* counsel.

A. *Standard of Review*

We review a trial court's order granting a defendant's motion for summary judgment motion de novo. (*Biancalana v. T.D. Service Co.* (2013) 56 Cal.4th 807, 813; *Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826, 860; *GreenLake Capital, LLC v. Bingo Investments, LLC* (2010) 185 Cal.App.4th 731, 735.) Code of Civil Procedure section 437c, subdivision (c), provides that a "motion for summary judgment shall be granted if all the papers submitted show that there is no triable issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." A moving defendant "'bears the burden of persuasion that there is no triable issue of material fact and that he is entitled to judgment as a matter of law.'" (*Morgan v. United Retail Inc.* (2010) 186 Cal.App.4th 1136, 1141, quoting *Aguilar*, *supra*, at p. 850; see Code Civ. Proc., § 437c, subds. (*o*), (p)(2).) If the moving defendant meets that burden, "the burden shifts to the plaintiff . . . to show that a triable issue of one or more material facts exists . . . ." (Code Civ. Proc., § 437c, subd. (p)(2); *Aguilar*, *supra*, at p. 849.) "We must affirm where it is shown that no triable issue of material fact exists and the moving party is entitled to judgment as a matter of law." (*Morgan, supra,* at p. 1142.)

B. *State Farm's Duty To Defend and To Provide Cumis Counsel*

The provisions of the standard general liability insurance policy impose on "the insurer a duty to indemnify the insured, generally stating that the insurer 'will pay all sums that the insured becomes legally obligated to pay as damages' for harm proved within coverage. [¶] [A secondary provision of] the standard policy imposes on the insurer a duty to defend the insured, generally stating that the insurer has a 'duty to defend' the insured 'in any suit seeking damages' for harm alleged within coverage." (*Certain Underwriters at Lloyd's of London v. Superior Court* (2001) 24 Cal.4th 945, 957.)[8] An "insurer's duty to defend is broader than its duty to indemnify." (*Buss v. Superior Court* (1997) 16 Cal.4th 35, 46.) "The insurer's duty to indemnify runs to claims that are actually covered, in light of the facts proved. . . . [¶] By contrast, the insurer's duty to defend runs to claims that are merely potentially covered, in light of facts alleged or otherwise disclosed." (*Ibid.*)

At the time an insurer accepts an insured's tender of defense, the insurer has an incentive to reserve a broad spectrum of coverage defenses in order to preserve its right to limit its obligation to indemnify to covered claims. (*Blue Ridge Ins. Co. v. Jacobsen* (2001) 25 Cal.4th 489, 497-498.) By giving notice to its insured, "[a]n insurer may agree to defend a suit subject to a reservation of rights. [Citation.] In this manner, an 'insurer meets its obligation to furnish a defense without waiving its right to assert coverage

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[8] The Policy provided: "If a claim is made or a suit is brought against an insured for damages because of bodily injury or property damage to which this coverage applies, caused by an occurrence, we will: [¶] 1. pay up to our limit of liability for the damages for which the insured is legally liable; and [¶] 2. provide a defense at our expense by counsel of our choice. We may make any investigation and settle any claim or suit that we decided is appropriate. Our obligation to defend any claim or suit ends when the amount we pay for damages, to effect settlement or satisfy a judgment resulting from the occurrence, equals our limit of liability." (Bold omitted.)

defenses against the insured at a later time.' [Citation.]" (*Id.* at p. 498.) "'[I]f the insurer adequately reserves its right to assert the noncoverage defense later, it will not be bound by [any] judgment [against its insured]. If the injured party prevails, that party or the insured will assert his claim against the insurer. . . . At this time the insurer can raise the noncoverage defense previously reserved.'" (*J. C. Penney Casualty Ins. Co. v. M. K.* (1991) 52 Cal.3d 1009, 1017, fn. omitted, quoting *Gray v. Zurich Insurance Co.* (1966) 65 Cal.2d 263, 279; see *State Farm General Ins. Co. v. Mintarsih* (2009) 175 Cal.App.4th 274, 283 ["an insurer may provide the required defense under a reservation of its rights to later assert its objections to coverage as to one or more of the claims alleged against its insured"].)

When an insurer undertakes defense of its insured, an attorney selected by the insurer provides dual representation to the insured and the insurer. An insurer that owes "a duty to defend an insured, arising because there exists a potential for liability under the policy, 'has the right to control defense and settlement of the third party action against its insured, and is . . . a direct participant in the litigation.' [Citations.] The insurer typically hires defense counsel who represents the interests of both the insurer and the insured. [Citations.] In this 'usual tripartite relationship existing between insurer, insured and counsel, there is a single, common interest shared among them. Dual representation by counsel is beneficial since the shared goal of minimizing or eliminating liability to a third party is the same.' [Citation.]" (*Long v. Century Indemnity Co.* (2008) 163 Cal.App.4th 1460, 1468.)

The benefits of dual representation give way to the need for independent *Cumis* counsel for the insured, however, if an insurer reserves its rights to deny indemnification on specific coverage issues, and the reservation creates a conflict of interest between the insurer and its insured that precludes dual representation because of the attorney's ethical obligations to refrain from representing conflicting interests. (Civ. Code, § 2860, subd. (b); *Long v. Century Indemnity Co., supra*, 163 Cal.App.4th at pp. 1470-1471.) As the court explained in *Cumis*, "the Canons of Ethics impose upon lawyers hired by the insurer an obligation to explain to the insured and the insurer the full implications of joint representation in situations where the insurer has reserved its rights to deny coverage. If the insured does not give an informed consent to continued representation, counsel must cease to represent both. Moreover, in the absence of such consent, where there are divergent interests of the insured and the insurer brought about by the insurer's reservation of rights based on possible noncoverage under the insurance policy, the insurer must pay the reasonable cost for hiring independent counsel by the insured. The insurer may not compel the insured to surrender control of the litigation [citations]. Disregarding the common interests of both insured and insurer in finding total nonliability in the third party action, the remaining interests of the two diverge to such an extent as to create an actual, ethical conflict of interest warranting payment for the insured['s] independent counsel." (*Cumis*, *supra*, 162 Cal.App.3d at p. 375; accord, *James 3 Corp. v. Truck Ins. Exchange* (2001) 91 Cal.App.4th 1093, 1099, fn. 1.)

In 1987 the Legislature codified the *Cumis* rule in Civil Code section 2860 (Stats. 1987, ch. 1498, § 4, p. 5779). (*Compulink Management Center, Inc. v. St. Paul Fire & Marine Ins. Co.* (2008) 169 Cal.App.4th 289, 294.) Pursuant to Civil Code section 2860 if the insurance contract requires the insurer to provide a defense and a disqualifying conflict of interest arises that creates a duty to provide the insured with *Cumis* counsel, the insurer must provide *Cumis* counsel unless the insured waives the right to *Cumis* counsel in writing. (*Id.*, subds. (a), (e).) A disqualifying conflict of interest may arise when the insurer reserves its rights with respect to a specific coverage issue "and the outcome of that coverage issue can be controlled by counsel first retained by the insurer for the defense of the claim" or claims involving the questioned coverage. (*Id.*, subd. (b).)[9] "'It is only when the basis for the reservation of rights is such as to cause

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9 Civil Code section 2860 provides in pertinent part: "(a) If the provisions of a policy of insurance impose a duty to defend upon an insurer and a conflict of interest arises which creates a duty on the part of the insurer to provide independent counsel to the insured, the insurer shall provide independent counsel to represent the insured unless, at the time the insured is informed that a possible conflict may arise or does exist, the insured expressly waives, in writing, the right to independent counsel. An insurance assertion of factual or legal theories which undermine or are contrary to the positions to be asserted in the liability case that a conflict of interest sufficient to require independent counsel, to be chosen by the insured, will arise.'" (*Gafcon, Inc. v. Ponsor & Associates* (2002) 98 Cal.App.4th 1388, 1421-1422.) To be disqualifying, the conflict of interest must be "'significant, not merely theoretical, actual, not merely potential.'" (*Gulf Ins. Co. v. Berger, Kahn, Shafton, Moss, Figler, Simon & Gladstone* (2000) 79 Cal.App.4th 114, 130; *Dynamic Concepts, Inc. v. Truck Ins. Exchange* (1998) 61 Cal.App.4th 999, 1007.)

Consistent with these principles, State Farm reserved coverage rights that the parties agree created a disqualifying conflict of interest triggering State Farm's duty to pay for *Cumis* counsel for Swanson. Swanson does not dispute that an insurer like State Farm that reserves *Cumis*-triggering defenses can later waive some or all of those defenses and that State Farm expressly reserved its right to make such a waiver in its November 4, 2005 reservation of rights letter. Then, on April 11, 2006, after having further considered coverage issues, State Farm gave Swanson notice that it was withdrawing its broadest coverage reservations.

Swanson and State Farm agree that once State Farm waived its *Cumis*-triggering defenses on April 11, 2006, the disqualifying conflict of interest no longer existed.

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contract may contain a provision which sets forth the method of selecting that counsel consistent with this section.

"(b) For purposes of this section, a conflict of interest does not exist as to allegations or facts in the litigation for which the insurer denies coverage; however, when an insurer reserves its rights on a given issue and the outcome of that coverage issue can be controlled by counsel first retained by the insurer for the defense of the claim, a conflict of interest may exist. No conflict of interest shall be deemed to exist as to allegations of punitive damages or be deemed to exist solely because an insured is sued for an amount in excess of the insurance policy limits."

Civil Code section 2860 also provides that, if the insured selects *Cumis* counsel, the insurer may continue to participate in the litigation and be represented by its chosen attorney. (*Id.*, subd. (f).) *Cumis* counsel and the insured must cooperate with the insurer's counsel in the exchange of non-privileged information and other matters relevant to the litigation and consult with the insurer "on all matters relating to the action." (*Id.*, subds. (d), (f).)

Swanson and State Farm also agree that under Swanson's Policy, "in the absence of any obligation to provide independent counsel of the insured's choosing, State Farm had the right to 'provide a defense at our expense by counsel of our choice.'" Swanson and State Farm further agree that, pursuant to the Policy provisions regarding the duty to defend, State Farm at any time could appoint counsel of its choice to represent Swanson and State Farm.

As explained above, the duty to provide and pay for *Cumis* counsel arises only where a disqualifying conflict of interest exists. (Civ. Code, § 2860; *Long v. Century Indemnity Co.*, *supra*, 163 Cal.App.4th at pp. 1468-1471; *Cumis*, *supra*, 162 Cal.App.3d at p. 375; see *Musser v. Provencher* (2002) 28 Cal.4th 274, 282-283.) Otherwise, "'[t]he insurer owes no duty to provide independent counsel . . . because the *Cumis* rule is not based on insurance law but on the ethical duty of an attorney to avoid representing conflicting interests.'" (*James 3 Corp. v. Truck Ins. Exchange*, *supra*, at p. 1101, quoting *Golden Eagle Ins. Co. v. Foremost Ins. Co.* (1993) 20 Cal.App.4th 1372, 1394.) Thus, when the ethical bar to dual representation does not exist, the insurer has no duty to provide and pay for *Cumis* counsel. We are not aware of any authority, and Swanson cites none, holding that once an insurer provides and pays for *Cumis* counsel, the insurer cannot take over control of the litigation and cease paying *Cumis* counsel if the disqualifying conflict ceases to exist later in the litigation. Here, it is undisputed that the disqualifying conflict of interest between State Farm and Swanson ceased to exist on April 11, 2006. After that date, State Farm did not have a duty to continue to provide and pay for *Cumis* counsel.[10]

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10 Of course, an insurer's decisions to withdraw the reservation of rights that gives rise to the need for *Cumis* counsel, to take control of the litigation, and to cease paying *Cumis* counsel, as well as the timing of those decisions, are, like all of the insurer's decisions, subject to the insurer's duty of good faith and fair dealing to its insured.

C. *There Was No Relinquishment of a Right To Cease Paying Cumis Counsel*

Swanson contends that even if State Farm had a unilateral right under the Policy to stop paying for *Cumis* counsel, State Farm relinquished that right by modifying the Policy in the exchange of letters among State Farm, Swanson, and Blasco in November and December 2005. Swanson argues State Farm also waived its right to take control of the defense and stop paying *Cumis* counsel by failing to reserve such a right. We reject both of these arguments.[11]

1. There Was No Modification of the Insurance Contract

Swanson argues that the exchange of correspondence with State Farm in November and December 2005 constituted a modification of the Policy. We find no such modification. The November and December 2005 letters were the means by which State Farm preserved its rights and fulfilled its duties under the Policy and applicable law. The November 4, 2005 letter to Swanson satisfied State Farm's contractual duty to provide a defense based on State Farm's initial position that at least some of the claims in the Bitettis' cross-complaint were potentially covered. (See *Horace Mann Ins. Co. v. Barbara B.* (1993) 4 Cal.4th 1076, 1081.) The letter also protected State Farm's interest in not waiving, but rather preserving, its coverage defenses. (See *Blue Ridge Ins. Co. v. Jacobsen*, *supra*, 25 Cal.4th at pp. 497-498; *Long v. Century Indemnity Co.*, *supra*, 163 Cal.App.4th at p. 1470, fn. 9.) Similarly, State Farm's November 4, 2005 letter to Blasco and the December 2005 letters exchanged between Blasco and State Farm implemented the provisions of Civil Code section 2860 that authorized State Farm to require Blasco to meet certain professional qualifications for *Cumis* counsel and to limit the amount State

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11 Swanson also raises several evidentiary issues. Because we are able to resolve this appeal without reaching the merits of these issues, we decline to address them. (See *Kaiser Foundation Health Plan, Inc. v. Superior Court* (2012) 203 Cal.App.4th 696, 715-716 [appellate court may "decline to review an issue that will have no effect on the parties"]; *Shaw v. County of Santa Cruz* (2008) 170 Cal.App.4th 229, 259 ["we do not see these matters as necessary to our appellate decision and we accordingly decline to resolve them"].)

Farm had to pay Blasco to the rates State Farm usually paid counsel it retained.[12] Swanson concedes that there is no signed modification of the Policy and that she did not give additional consideration for any such modification. (See *Buss v. Superior Court, supra,* 16 Cal.4th at p. 50 [“a separate contract supported by separate consideration” would “supersede the [original] policy”].)

Swanson’s reliance on *Behnke v. State Farm General Ins. Co.* (2011) 196 Cal.App.4th 1443, which she claims supports her modification argument and involved “an almost identical set of facts as occurred in this case,” is misplaced. Behnke tendered defense of an action against him to State Farm. State Farm agreed to defend, reserved disqualifying coverage defenses, approved Behnke’s selection of *Cumis* counsel subject to Civil Code section 2860, and agreed to pay counsel at an hourly rate lower than counsel’s indicated rate. (*Behnke, supra*, at pp. 1448-1449.) State Farm then sent a second reservation of rights letter withdrawing the *Cumis*-triggering reservation of coverage defenses and instructing Behnke that another attorney, one selected by State Farm, would be taking over the defense of the litigation. (*Id.* at p. 1449.) Behnke objected to the change in attorneys and wanted to continue with the firm that had been representing him as *Cumis* counsel. (*Ibid*.) So far, the facts in *Behnke* are similar to those in this case.

In *Behnke*, however, State Farm then terminated the services of the attorney it had selected and agreed to allow *Cumis* counsel to continue defending Behnke. (*Behnke v. State Farm General Ins. Co.*, *supra*, 196 Cal.App.4th at p. 1450.) A dispute arose

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12 Civil Code section 2860, subdivision (c), provides in part: “When the insured has selected independent counsel to represent him or her, the insurer may exercise its right to require that the counsel selected by the insured possess certain minimum qualifications which may include that the selected counsel have (1) at least five years of civil litigation practice which includes substantial defense experience in the subject at issue in the litigation, and (2) errors and omissions coverage. The insurer’s obligation to pay fees to the independent counsel selected by the insured is limited to the rates which are actually paid by the insurer to attorneys retained by it in the ordinary course of business in the defense of similar actions in the community where the claim arose or is being defended.”

between State Farm and *Cumis* counsel over the necessity and reasonableness of the firm's fees. The *Behnke* court stated that, given the fee limitation and arbitration requirement in Civil Code section 2860, subdivision (c), and State Farm's express reservation of the right to arbitrate fee disputes, "State Farm's consent to Behnke's decision to retain [the firm] as his independent defense counsel in the . . . action . . . must be deemed an agreement or promise by State Farm to pay any *Cumis* counsel fees billed by [the firm] . . . that were both *reasonably necessary* and *reasonable in amount* as determined by an arbitrator in the event a fee dispute arose . . . ." (*Behnke, supra*, at p. 1460.) The *Behnke* court concluded that "the factual allegations show that State Farm agreed to pay only for those *Cumis* counsel fees that were both reasonably necessary and reasonable in amount as determined by an arbitrator in the event of a dispute." (*Id.* at p. 1461.) *Behnke* says nothing about an insurer's duty to continue paying *Cumis* counsel after waiving *Cumis*-triggering reservations of rights or about modification of an insurance policy. Here, State Farm made the opposite choice of that made by the insurer in *Behnke*. State Farm did not retain Blasco and refused to continue paying him after waiving the disqualifying coverage defenses.

2. There Was No Waiver of the Right To Retake Control of the Defense

Swanson also argues that State Farm waived its right to retake control of the defense by counsel of its choosing because State Farm did not expressly reserve this right in its November 4, 2005 letter. As noted above, however, an insurer's obligations under *Cumis* and Civil Code section 2860 are "'not based on insurance law but on the ethical duty of an attorney to avoid representing conflicting interests.'" (*James 3 Corp. v. Truck Ins. Exchange*, *supra*, 91 Cal.App.4th at p. 1101, quoting *Golden Eagle Ins. Co. v. Foremost Ins. Co.*, *supra*, 20 Cal.App.4th at p. 1394.) Swanson has not cited any authority, and we are not aware of any, holding that an insurer may waive its rights under *Cumis* and Civil Code section 2860 by failing to reserve them.

None of the cases Swanson cites supports her contention that State Farm waived its right to retake control of the defense by failing to reserve its right to do so in its November 4, 2005 reservation of rights letter. For example, Swanson argues that the Supreme Court in *Buss v. Superior Court*, *supra*, 16 Cal.4th 35 held that if the insurer wants to reserve the right to terminate *Cumis* counsel and take over control of the litigation, the insurer must expressly say so in the same manner that the insurer reserves the right to pursue coverage defenses in a reservation of rights letter. *Buss* does not say this. The issue in *Buss* was whether an insurer could reserve the right to reimbursement for costs of defense where some of the claims were potentially covered and some of the claims were not. (*Id.* at pp. 49-50.) The Supreme Court held that an insurer cannot reserve the right to reimbursement for the defense costs of potentially covered claims because the insurer had no such right to reserve, but the insurer can seek reimbursement for the defense costs of claims that were not even potentially covered. (*Id.* at pp. 49-53.) There is no issue in this case about State Farm's right to reimbursement for defense costs, nor any contention that the Bitetti Action involved only claims that were not potentially covered by the Policy.

Swanson's reliance on *Hamilton v. Maryland Casualty Co.* (2002) 27 Cal.4th 718 is also misplaced. The court in *Hamilton* held that when an insured tenders a suit, the insurer has but one "chance to be heard" with regard to issues material to liability and "cannot reach back for due process to void" a settlement that the insured has entered into "to eliminate personal liability." (*Id.* at p. 728.) According to Swanson, *Hamilton* stands for the proposition that State Farm in April 2006 could not "reach back" and revisit its decision in November 2005 authorizing retention of and payment to *Cumis* counsel selected by the insured. The *Hamilton* court's use of the phrase one "chance to be heard," however, referred to the opportunity an insurer has to reserve its rights with respect to indemnification issues at the time the insurer first responds to an insured's tender and request for a defense. (*Ibid.*) The court was explaining that when an insurer denies that it has a duty to indemnify and defend a claim against the insured, the insured may enter into a reasonable, noncollusive settlement without the insurer's consent and then seek reimbursement from the insurer.[13] (*Id.* at pp. 728-729.) The insurer in *Hamilton* provided the insured with a defense, and there was no issue regarding a breach of the duty to defend or anything relating to *Cumis* counsel.

D. *Summary Judgment Was Appropriate*

Because State Farm had no duty to continue to allow Swanson's *Cumis* counsel to control the Bitetti litigation or to continue to pay *Cumis* counsel after State Farm waived the *Cumis*-triggering reservations of rights, there was no triable issue of material fact regarding whether State Farm breached its duty to defend Swanson by refusing to pay post-April 11, 2006 *Cumis* fees or by taking control of the litigation with counsel of its choice. Moreover, because State Farm did not breach the insurance contract, it cannot be liable for breach of the implied covenant of good faith and fair dealing. (See *Brown v. Mid-Century Ins. Co.* (2013) 215 Cal.App.4th 841, 858; *Minich v. Allstate Ins. Co.* (2011) 193 Cal.App.4th 477, 493.) Therefore State Farm was entitled to judgment as a matter of law. (Code Civ. Proc., § 437c, subd. (c); *Biancalana v. T.D. Service Co.*, *supra*, 56 Cal.4th at p. 813.) The trial court properly granted State Farm's motion for summary judgment.

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13 The issue in *Hamilton* was whether the amount of a stipulated settlement against the insured was the proper measure of the insured's damages caused by the insurer's breach of its duty to accept a reasonable settlement demand. (*Hamilton v. Maryland Casualty Co.*, *supra*, 27 Cal.4th at pp. 721-722.)

DISPOSITION

The judgment is affirmed. State Farm is to recover its costs on appeal.

SEGAL, J.*

We concur:

PERLUSS, P. J.

WOODS, J.

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* Judge of the Los Angeles Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

Filed 8/27/13; pub. & mod. order 9/26/13 (see end of opn.)

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

ALAN SHAUN ROSSBERG et al.,	
Plaintiffs and Appellants,	G047028 (cons. with G047355)
v.	(Super. Ct. No. 30-2011-00462732)
BANK OF AMERICA, N.A., et al.,	O P I N I O N
Defendants and Respondents.	

Appeal from a judgment of the Superior Court of Orange County, Gregory Munoz, Judge. Affirmed. Petition for writ of mandate dismissed as moot.

Robinson-Legal and Raymond G. Robinson for Plaintiffs and Appellants.

Bryan Cave, Sean D. Muntz and Thomas E. Nanney for Defendants and Respondents.

* * *

Plaintiffs and appellants Alan Shaun Rossberg (Shaun) and Brenda Rossberg (Brenda; collectively Rossbergs)[1] appeal from a judgment dismissing their complaint after the trial court sustained a demurrer by defendants and respondents Bank of America, N.A. (BofA) and U.S. Bank, National Association, as trustee for the certificate holders of Banc of America Funding Corporation Mortgage Pass-Through Certificates, Series 2007-C (U.S. Bank; collectively Defendants). The Rossbergs sued Defendants to prevent them from selling the Rossbergs' home at a nonjudicial foreclosure sale after the Rossbergs defaulted on two loans secured by deeds of trust. The Rossbergs alleged several causes of action against Defendants based on BofA's unperformed promises to modify the Rossbergs' loans and Defendants failure to comply with the statutory requirements for conducting a nonjudicial foreclosure.

We affirm the trial court's order sustaining Defendants' demurrer to the first amended complaint because the Rossbergs failed to adequately allege the existence of an enforceable agreement to modify their loans or that Defendants failed to comply with the statutory requirements for conducting a nonjudicial foreclosure. We also affirm the trial court's order denying leave to amend because the Rossbergs failed to specifically show how they could amend their pleading to state a cause of action. Finally, because we affirm the trial court's judgment dismissing the Rossbergs' action, we dismiss as moot the Rossbergs' petition for writ of mandate to prevent Defendants from evicting them from their home during this appeal.

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[1] We refer to Shaun and Brenda individually by their first names to avoid any confusion. No disrespect is intended. (*Martin v. PacifiCare of California* (2011) 198 Cal.App.4th 1390, 1393, fn. 1.)

I

FACTS AND PROCEDURAL HISTORY[2]

In February 2007, the Rossbergs borrowed more than $600,000 from BofA. They signed a promissory note (First Note) and gave BofA a deed of trust (First Deed of Trust) on their home in Irvine, California, to secure the loan. The First Deed of Trust named BofA as the beneficiary and PRLAP, Inc. as the trustee.

Two months later, BofA entered into a "Pooling and Servicing Agreement" with Banc of America Funding Corporation as depositor, Well Fargo Bank, N.A., as master servicer and securities administrator, and U.S. Bank as trustee. The Pooling and Servicing Agreement grouped together numerous mortgages to create mortgage backed securities, which were sold to investors who purchased certificates giving them an ownership interest. The Rossbergs alleged the First Note and First Deed of Trust "were part of the Pooling and Servicing Agreement . . . [and] were transferred to Defendant U.S. Bank as trustee."

The Rossbergs borrowed an additional $58,000 from BofA in August 2007. Again, they signed a promissory note (Second Note) and gave BofA a deed of trust on their home (Second Deed of Trust) as security for the loan. The Second Deed of Trust named BofA as the beneficiary and PRLAP, Inc. as the trustee. The Rossbergs do not allege whether the Second Note and Second Deed of Trust were part of the Pooling and Servicing Agreement.

In 2007, Shaun lost his job and then suffered a debilitating illness that prevented him from looking for new work for several months. After exhausting much of their savings and available credit, the Rossbergs fell behind in their loan payments. In

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[2] We summarize the underlying facts as alleged in the operative first amended complaint because this appeal follows the sustaining of a demurrer. (*Rosen v. St. Joseph Hospital of Orange County* (2011) 193 Cal.App.4th 453, 456.)

early 2009, they began discussions with BofA to modify their loans. These discussions dragged on for more than two and one-half years as the Rossbergs engaged in countless oral and written communications with BofA. They repeatedly sent BofA numerous tax and other financial documents to support their loan modification requests.

The Rossbergs alleged BofA employees told them on several occasions that they had been granted a loan modification. In July 2009, Esmerna, an employee in the loan modification processing department, told Brenda the Rossbergs had been granted a loan modification that would reduce their interest rate from 7.65 percent to 6.54 percent and would add $58,000 to the loan balance. In December 2010, Yazmin, another BofA loan modification employee, told Brenda the Rossbergs had been granted a loan modification that would (1) fix their variable interest rate at 7.65 percent for the term of the loan; (2) establish an impound account; and (3) require a $130,000 balloon payment at the end of the loan. Several other employees confirmed the Rossbergs had been granted these loan modifications.[3] All of these employees promised the Rossbergs would

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[3] The Rossbergs contend they attached three letters to their pleading in which BofA approved loan modifications, but the attached letters do not support the Rossbergs' contention. Two of the letters do not contain the language the Rossbergs quote in their pleading and the third letter merely states BofA has "approved your request for assistance." The third letter does not refer to modifying the Rossbergs' loans, let alone the specific terms of any modification; it merely asks the Rossbergs to contact BofA to discuss available options for resolving their loan delinquency.

The Rossbergs also contend BofA admitted the Rossbergs received loan modifications in two letters it sent after the trial court entered judgment. Because the operative pleading contains no allegations regarding these letters and they postdate the trial court's ruling, we may not consider them in evaluating the adequacy of the Rossbergs' allegations. (*Hensler v. City of Glendale* (1994) 8 Cal.4th 1, 8-9, fn. 3 (*Hensler*) [in ruling on a demurrer, courts are limited to allegations appearing on the face of the pleadings and facts properly subject to judicial notice]; *Vons Companies, Inc. v. Seabest Foods, Inc.* (1996) 14 Cal.4th 434, 444, fn. 3 ["normally 'when reviewing the correctness of a trial court's judgment, an appellate court will consider only matters which were part of the record at the time the judgment was entered'"].) To the extent we may consider these letters in deciding whether we should grant the Rossbergs leave to amend, the letters merely state BofA twice offered the Rossbergs a loan modification and receive documents to confirm and implement these loan modifications, but the Rossbergs never received those documents and BofA never implemented either loan modification. The Rossbergs did not allege what, if any payments, they made during their loan modification negotiations with BofA.

On September 22, 2009, as the Rossbergs continued their efforts to negotiate a loan modification, BofA executed a Substitution of Trustee designating Cal-Western Reconveyance Corporation (Cal-Western) as the new trustee on the First Deed of Trust. BofA did not have a notary public acknowledge the Substitution of Trustee until November 11, 2009, and it did not record the document until November 18, 2009.

Three days after BofA executed the Substitution of Trustee, and nearly two months *before* BofA recorded that document, Cal-Western executed a Notice of Default as "either the original trustee, the duly appointed substituted trustee, or acting as agent for the trustee or beneficiary" under the First Deed of Trust. The Notice of Default informed the Rossbergs they were nine months behind on their loan and the beneficiary had elected to start the nonjudicial foreclosure process on their property. Cal-Western recorded the Notice of Default on September 28, 2009, three days after executing it.

In June 2010, Cal-Western recorded a Notice of Trustee's Sale (Notice of Sale) under the First Deed of Trust. The Notice of Sale originally set July 14, 2010, as the sale date, but the date for the sale was rescheduled several times. Attached to the Notice of Sale was a declaration executed by BAC Home Loans Servicing, LP (BAC) that stated BAC obtained an exemption from certain statutory time limits for giving notice of the sale, but the declaration does not explain BAC's relationship to the First Deed of Trust or the Rossbergs' loan.

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the Rossbergs rejected those offers. Accordingly, the letters fail to show an agreement was ever reached on a specific loan modification.

In January 2011, Cal-Western, as Bank of America's attorney in fact, executed and recorded an "Assignment of Deed of Trust" that transferred all beneficial interest in the First Deed of Trust and First Note to "U.S. Bank, National Association, as Trustee for the Certificateholders of Banc of America Funding Corporation, Mortgage Pass-Through Certificates, Series 2007-C."

The Rossbergs filed this action in April 2011 to block the foreclosure sale. After the trial court sustained a demurrer to the original complaint, the Rossbergs filed a first amended complaint. The first amended complaint named BofA, U.S. Bank, and Cal-Western as defendants and alleged the following causes of action: (1) violation of Civil Code section 2923.5;[4] (2) violation of section 2924 et seq.; (3) fraud; (4) violation of Business and Professions Code section 17200; (5) breach of contract; (6) declaratory relief; and (7) quiet title.[5] The numerous exhibits the Rossbergs attached to the first amended complaint included the First Deed of Trust, portions of the Pooling and Servicing Agreement, the Substitution of Trustee, the Notice of Default, the Notice of Sale, and the Assignment of Deed of Trust.

The Rossbergs alleged the nonjudicial foreclosure sale could not proceed because (1) BofA failed to satisfy its statutory duty to contact the Rossbergs to assess their financial situation and explore options for avoiding foreclosure before it recorded the Notice of Default; (2) the Notice of Default is void because Cal-Western recorded the Notice before it was designated as trustee under the First Deed of Trust; (3) Cal-Western lacked authority to take any action as trustee under the First Deed of Trust because the Substitution of Trustee designating Cal-Western as trustee is a forgery; and (4) it is unclear who held the First Note and First Deed of Trust when the Notice of Default and Notice of Sale were recorded because the Servicing and Pool Agreement transferred the

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4 All statutory references are to the Civil Code unless otherwise stated.

5 Cal-Western is not a party to this appeal.

First Note and First Deed of Trust to U.S. Bank in April 2007, but the Assignment of Deed of Trust purported to make that same transfer in January 2011. The Rossbergs also alleged BofA committed fraud when it promised to grant them a loan modification but failed to implement the promised loan modification.[6]

BofA and U.S. Bank demurred to the first amended complaint on the ground each cause of action failed to allege sufficient facts to state a claim against either defendant. The trial court sustained the demurrer on every cause of action without leave to amend and entered a judgment of dismissal. The Rossbergs timely appealed.

Shortly after the trial court dismissed the Rossbergs' action, Cal-Western proceeded with the nonjudicial foreclosure and conducted the public sale because the Rossbergs failed to seek a stay of enforcement regarding the trial court's judgment. U.S. Bank purchased the property at the sale for a credit bid and then filed an unlawful detainer action to obtain possession.

In September 2012, the Rossbergs filed a petition for writ of mandate to prevent "BofA" from selling the property to a third party or proceeding with the unlawful detainer action during this appeal. We issued an order (1) treating the Rossbergs' petition as a petition for writ of supersedeas; (2) consolidating the Rossbergs' appeal from the judgment and their writ petition; and (3) inviting an informal response from BofA. BofA did not file a response and no further action was taken on the petition.

In July 2013, U.S. Bank obtained a judgment of possession against the Rossbergs in the unlawful detainer action after the Rossbergs failed to appear for trial.

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[6] The first amended complaint and the Rossbergs' opening brief include allegations and contentions suggesting BofA had a duty to grant the Rossbergs a loan modification, but their reply clarifies that the Rossbergs do not contend BofA had a duty to grant them a modification. We therefore do not address that issue.

II

DISCUSSION

A. *Standard of Review and the Rossbergs' Burden on Appeal*

When the trial court sustains a demurrer, we review the complaint de novo to determine whether it alleges facts stating a cause of action on any possible legal theory. (*Koszdin v. State Comp. Ins. Fund* (2010) 186 Cal.App.4th 480, 487 (*Koszdin*).) """We treat the demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law."' [Citations.]" (*Hoffman v. Smithwoods RV Park, LLC* (2009) 179 Cal.App.4th 390, 400.) "Further, 'we give the complaint a reasonable interpretation, reading it as a whole and its parts in their context.' [Citations.]" (*Melton v. Boustred* (2010) 183 Cal.App.4th 521, 528.) We also "consider matters that must or may be judicially noticed."[7] (*Hoffman*, at p. 400.)

Nonetheless, "[t]he plaintiff has the burden of showing that the facts pleaded are sufficient to establish every element of the cause of action and overcoming all of the legal grounds on which the trial court sustained the demurrer, and if the defendant negates any essential element, we will affirm the order sustaining the demurrer as to the cause of action. [Citation.] We will affirm if there is any ground on which the demurrer can properly be sustained, whether or not the trial court relied on proper grounds or the defendant asserted a proper ground in the trial court proceedings. [Citation.]" (*Martin v. Bridgeport Community Assn., Inc.* (2009) 173 Cal.App.4th 1024, 1031 (*Martin*); *Sui v. Price* (2011) 196 Cal.App.4th 933, 938 (*Sui*).)

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[7] The Rossbergs argue the trial court erred by failing to consider their opposition to Defendants' demurrer, considering evidence Defendants' counsel offered at the hearing on the demurrer, and requiring the Rossbergs to present evidence to overcome the demurrer. The record does not support any of these contentions. Nonetheless, they are irrelevant because we conduct a de novo review when determining the adequacy of the Rossbergs' pleading against the demurrer.

"When a demurrer is sustained without leave to amend, we also must decide whether there is a reasonable possibility that the defect can be cured by amendment." (*Koszdin, supra,* 186 Cal.App.4th at p. 487.) "The plaintiff bears the burden of proving there is a reasonable possibility of amendment. [Citation.] . . . [¶] To satisfy that burden on appeal, a plaintiff 'must show in what manner he can amend his complaint and how that amendment will change the legal effect of his pleading.' [Citation.] The assertion of an abstract right to amend does not satisfy this burden. [Citation.] The plaintiff must clearly and specifically set forth the 'applicable substantive law' [citation] and the legal basis for amendment, i.e., the elements of the cause of action and authority for it. Further, the plaintiff must set forth factual allegations that sufficiently state all required elements of that cause of action. [Citations.] Allegations must be factual and specific, not vague or conclusionary. [Citation.]" (*Rakestraw v. California Physicians' Service* (2000) 81 Cal.App.4th 39, 43-44 (*Rakestraw*).)

B. *Legal Background Regarding Deeds of Trust and Nonjudicial Foreclosures*

"The financing or refinancing of real property in California is generally accomplished by the use of a deed of trust." (*Jenkins v. JPMorgan Chase Bank, N.A.* (2013) 216 Cal.App.4th 497, 507 (*Jenkins*).) "A deed of trust . . . conveys title to real property from the trustor-debtor to a third party trustee to secure the payment of a debt owed to the beneficiary-creditor under a promissory note. [Citations.] The customary provisions of a valid deed of trust include a power of sale clause, which empowers the beneficiary-creditor to [foreclose] on the real property security if the trustor-debtor fails to pay back the debt owed under the promissory note. [Citations.]" (*Id*. at p. 508.)

"[A]lthough the deed of trust technically conveys title to the real property from the trustor-debtor to the trustee, the extent of the trustee's interest in the property is limited to what is necessary to enforce the operative provisions of the deed of trust." (*Jenkins, supra,* 216 Cal.App.4th at p. 508.) Generally, a deed of trust requires the trustee only to perform one of two "mutually exclusive duties: (1) should the trustor-debtor default on the debt, the trustee must initiate foreclosure on the property for the benefit of the beneficiary-creditor; or (2) should the trustor-debtor satisfy the secured debt, the trustee must reconvey title to the real property back to the trustor-debtor, extinguishing the security device." (*Ibid*.) Despite the security interest the deed of trust creates, "the trustor-debtor retains all incidents of ownership with regard to the real property, including the rights of possession and sale." (*Ibid*.)

When a trustor-debtor defaults "on a debt secured by a deed of trust, the beneficiary-creditor may elect to judicially or nonjudicially foreclose on the real property security. Sections 2924 through 2924k set forth a 'comprehensive framework for the regulation of a *nonjudicial* foreclosure sale pursuant to a power of sale contained in a deed of trust.' [Citation.]" (*Jenkins, supra*, 216 Cal.App.4th at p. 508, original italics.) "To initiate the nonjudicial foreclosure process, the 'trustee, mortgagee, or beneficiary, or any of their authorized agents,' must record a notice of default and election to sell. [Citation.]" (*Id*. at p. 509.) The "mortgagee, trustee, or other person authorized to take the sale" must then wait three months before proceeding with the sale. (§ 2924, subd. (a)(3); *Jenkins*, at p. 509.) "After the three-month period has elapsed, a notice of sale must be published, posted, recorded and mailed 20 days before the foreclosure sale." (*Jenkins*, at p. 509.) The property must be sold at a public auction to the highest bidder, but before the sale occurs the statutory scheme provides the trustor-debtor with several opportunities to cure the default and avoid losing the property. (*Ibid*.)

The statutory scheme authorizing nonjudicial foreclosures "'" cover[s] every aspect of [the] exercise of [a] power of sale contained in a deed of trust." [Citation.] . . .' [Citation.]" (*Jenkins, supra*, 216 Cal.App.4th at p. 509.) "'Because of the exhaustive nature of this scheme, California appellate courts have refused to read any additional requirements into the non-judicial foreclosure statute.' [Citations.]"

(*Debrunner v. Deutsche Bank National Trust Co.* (2012) 204 Cal.App.4th 433, 441 (*Debrunner*).)

"""The purposes of this comprehensive scheme are threefold: (1) to provide the [beneficiary-creditor] with a quick, inexpensive and efficient remedy against a defaulting [trustor-debtor]; (2) to protect the [trustor-debtor] from wrongful loss of the property; and (3) to ensure that a properly conducted sale is final between the parties and conclusive as to a bona fide purchaser." [Citation.]' [Citation.] 'Significantly, "[n]onjudicial foreclosure is less expensive and more quickly concluded than judicial foreclosure, since there is no oversight by a court, '[n]either appraisal nor judicial determination of fair value is required,' and the debtor has no postsale right of redemption." [Citation.]' [Citation.]" (*Jenkins*, *supra*, 216 Cal.App.4th at pp. 509-510.)

A nonjudicial foreclosure is "presumed to have been conducted regularly, and the burden of proof rests with the party attempting to rebut this presumption." (*Fontenot v. Wells Fargo Bank, N.A.* (2011) 198 Cal.App.4th 256, 270 (*Fontenot*) [applying presumption in action for wrongful foreclosure brought after sale conducted]; *Debrunner*, *supra*, 204 Cal.App.4th at p. 443 [applying presumption in action to prevent nonjudicial foreclosure sale from occurring].) A trustor-debtor seeking to prevent a nonjudicial foreclosure based on the foreclosing entity's purported lack of authority therefore must "affirmatively" plead facts demonstrating a lack of authority. (*Fontenot*, at p. 270; *Jenkins*, *supra*, 216 Cal.App.4th at p. 512 [to state a cause of action challenging a foreclosing entity's authority to initiate and conduct a nonjudicial foreclosure, the trustor-debtor must allege a "*specific factual basis*" establishing a lack of authority (original italics)]; *Gomes v. Countrywide Home Loans, Inc.* (2011) 192 Cal.App.4th 1149, 1155-1156.) A trustor-debtor may not bring a preemptive lawsuit seeking to force the foreclosing entity to prove its authority before it conducts a nonjudicial foreclosure. (*Jenkins*, at pp. 511-513.) Allowing a judicial action to prevent a nonjudicial foreclosure without specific factual allegations showing a lack of authority "would unnecessarily 'interject the courts into [the] comprehensive nonjudicial scheme' created by the Legislature, and 'would be inconsistent with the policy behind nonjudicial foreclosure of providing a quick, inexpensive and efficient remedy. [Citation.]' [Citation.]" (*Id*. at p. 512; see also *Gomes*, at pp. 1154-1156.)

C. *The Rossbergs Failed to Allege a Cause of Action on Any Theory*

1. First Cause of Action for Violation of Section 2923.5

"In 2008, the Legislature enacted . . . section 2923.5 in response to the foreclosure crisis." (*Stebley v. Litton Loan Servicing, LLP* (2011) 202 Cal.App.4th 522, 525.) When Cal-Western recorded the Notice of Default in 2009, section 2923.5 prohibited a "mortgagee, trustee, beneficiary, or authorized agent" from recording a notice of default until 30 days after (1) "contact[ing] the borrower in person or by telephone in order to assess the borrower's financial situation and explore options for the borrower to avoid foreclosure"; or (2) making diligent efforts to contact the borrower, including "sending a first-class letter that includes the toll-free telephone number made available by HUD to find a HUD-certified counseling agency," "attempt[ing] to contact the borrower by telephone at least three times at different hours and on different days," and "send[ing] a certified letter, with return receipt requested." (Former § 2923.5, subds. (a) & (g).) Former section 2923.5 further required the notice of default include a declaration stating "the mortgagee, beneficiary, or authorized agent . . . has contacted the borrower [or] tried with due diligence to contact the borrower as required by this section . . . ."[8] (Former §2923.5, subd. (b).)

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8 The Legislature amended section 2923.5 in 2009 and again in 2012 to modify some of its requirements. (Stats. 2009, ch. 43, § 1; Stats. 2012, ch. 86, § 4.) The basic requirements nonetheless remain that a mortgage servicer, mortgagee, trustee, beneficiary, or authorized agent may not record a notice of default until more than 30 days after they contact the borrower to assess the borrower's financial situation and explore options to avoid foreclosure, or make diligent efforts to contact the borrower for those purposes. The current version continues to require a notice of default include a

The Rossbergs concede the declaration section 2923.5 requires as part of a notice of default may simply track the statutory language regarding the mortgagee, beneficiary, or authorized agent's efforts to contact the borrower and the declaration need not be under penalty of perjury. (See *Mabry v. Superior Court* (2010) 185 Cal.App.4th 208, 232-235.) The Rossbergs further concede Cal-Western's declaration in its recorded Notice of Default satisfied the statute's requirements. Nonetheless, the Rossbergs argue they stated a cause of action under section 2923.5 because the declaration in the Notice of Default is false. According to the Rossbergs, neither BofA nor any of its agents contacted them to assess their financial situation and explore options for avoiding foreclosure before Cal-Western recorded the Notice of Default.

A borrower may state a cause of action under section 2923.5 by alleging the lender did not actually contact the borrower or otherwise make the required efforts to contact the borrower despite a contrary declaration in the recorded notice of default. (*Skov v. U.S. Bank National Assn.* (2012) 207 Cal.App.4th 690, 696.) The Rossbergs, however, failed to state a cause of action on this theory because they did not adequately allege BofA and its agents failed to contact them to assess their financial situation and explore options for avoiding foreclosure at least 30 days before Cal-Western recorded the Notice of Default.

The first amended complaint alleged, "*In the 30-days leading up* to [the date on which Cal-Western recorded the Notice of Default], no in person meeting took place and no telephonic conversation took place." (Italics added.) This does not allege a section 2923.5 violation because the statute requires the contact to occur *more* than 30 days before the notice of default is recorded, not during "the 30 days leading up to" the recording. Moreover, the first amended complaint alleged the Rossbergs had multiple

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declaration stating the mortgage servicer contacted the borrower or made diligent efforts to do so. (§2923.5, subds. (a), (b), (e).)

telephone conversations with BofA regarding a possible loan modification during July 2009, which was more than 30 days before Cal-Western recorded the Notice of Default in late September 2009. The Rossbergs also attached to the first amended complaint several letters they received from BofA more than 30 days before Cal-Western recorded the Notice of Default. These letters referred to programs designed to help borrowers avoid foreclosure and requested the Rossbergs contact BofA to discuss those programs. Accordingly, the trial court properly sustained the demurrer to the Rossbergs' first cause of action.[9]

2. Second Cause of Action for Violation of Section 2924 et seq.

This cause of action sought to enjoin Defendants from foreclosing on the Rossbergs' home because Defendants failed to record a proper notice of default. The Rossbergs alleged the Notice of Default was invalid because Cal-Western lacked authority to record it, and therefore the entire nonjudicial foreclosure process was void. Although the Rossbergs alleged several reasons for Cal-Western's purported lack of authority, they misconstrue the requirements for conducting a nonjudicial foreclosure and failed to allege any defect in the process that prevented Cal-Western from validly recording the Notice of Default. We therefore affirm the trial court's decision sustaining the demurrer to this cause of action.

The Rossbergs first contend Cal-Western lacked authority because it was not yet designated as trustee when it recorded the Notice of Default. According to the Rossbergs, Cal-Western did not become trustee until nearly two months *after* it recorded the Notice of Default when a notary acknowledged the Substitution of Trustee and

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[9] Defendants argue all of the Rossbergs' causes of action fail as a matter of law because the Rossbergs did not tender the full amount due and owing on the loans before bringing this action. Because we affirm the trial court's ruling on other grounds, we do not address whether a full tender was required before the Rossbergs could properly bring this action.

Cal-Western recorded the Substitution. Section 2934a, however, expressly authorized Cal-Western to record the Notice of Default because the Substitution of Trustee was executed *before* Cal-Western recorded the Notice of Default even though the Substitution of Trustee was not notarized or recorded until nearly two months later.

Specifically, section 2934a states, "[a] trustee named in a recorded substitution of trustee shall be deemed to be authorized to act as the trustee under the . . . deed of trust for all purposes *from the date the substitution is executed* . . . ." (§ 2934a, subd. (d), italics added.) That statute also provides a substituted trustee may record a notice of default *before* the substitution empowering the trustee to act is recorded. (§ 2934a, subd. (b); *Debrunner*, *supra*, 204 Cal.App.4th at pp. 443-444.) Here, the Substitution of Trustee attached to the first amended complaint shows BofA executed it on September 22, 2009, and recorded it on November 18, 2009. Accordingly, Cal-Western was authorized to act as trustee starting on September 22, 2009, and validly recorded the Notice of Default six days later.

In a related argument, the Rossbergs contend the Substitution of Trustee must be a forgery because a notary did not acknowledge the signature on that document until nearly two months after BofA signed it. This argument assumes a notary must acknowledge a document at the time it is executed and any delay between the execution and acknowledgment renders the document invalid. That is not the law and the Rossbergs do not cite any authority to support that proposition. Nothing requires a notary to acknowledge a document at the same time it is executed, and even a lengthy delay between the execution of the document and its acknowledgment does not invalidate the document. (*Wilson v. Pacific Coast Title Ins. Co.* (1951) 106 Cal.App.2d 599, 602 [assignment of beneficial interest in deed of trust validly transferred title despite notary acknowledging assignment nearly two years after it was executed]; *Pedersen v. Greenpoint Mortgage Funding, Inc.* (E.D.Cal 2012) 900 F.Supp.2d 1071, 1083 [same].)

The Rossbergs allege no other basis for their contention the Substitution of Trustee is a forgery.

The Rossbergs next contend Cal-Western lacked authority to record the Notice of Default because BofA was not the beneficiary under the First Deed of Trust when it executed the Substitution of Trustee designating Cal-Western as trustee. According to the Rossbergs, BofA transferred the First Note and First Deed of Trust to U.S. Bank in April 2007, when it entered into the Pooling and Servicing Agreement, and therefore only U.S. Bank could have validly executed the Substitution of Trustee in September 2009.[10] The allegation BofA could not properly designate Cal-Western as trustee, however, does not state a claim to invalidate the Notice of Default.

Section 2924 authorizes a notice of default to be recorded by the "trustee, mortgagee, or beneficiary, *or any of their authorized agents*." (§ 2924, subd. (a)(1), italics added.) The Notice of Default did not state Cal-Western was acting as a substituted trustee designated by BofA. Rather, the Notice of Default stated Cal-Western "is either the original trustee, the duly appointed substituted trustee, *or acting as agent for the trustee or beneficiary* under [the First Deed of Trust]." (Italics added.) Accordingly, to state a claim based on Cal-Western's purported lack of authority to record the Notice of Default, the Rossbergs had to allege not only that Cal-Western was not the trustee under the First Deed of Trust, but also that Cal-Western was not the agent of the trustee

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[10] In their brief, the Rossbergs mistakenly refer to U.S. Bank as the trustee under the First Deed of Trust. The Rossbergs, however, fail to recognize the proper legal effect of the Pooling and Servicing Agreement. That Agreement pooled together large numbers of mortgages to create investment instruments potential investors could purchase. Under the Pooling and Servicing Agreement, the beneficial interests in the mortgages (more specifically, the underlying promissory notes and deeds of trusts) were transferred to U.S. Bank, who acted as trustee and held the beneficial interests in the promissory notes and deeds of trusts for the investors. The Pooling and Servicing Agreement did not make U.S. Bank the trustee under the First Deed of Trust or any other deed of trust.

or beneficiary. (*Jenkins*, *supra*, 216 Cal.App.4th at pp. 515-516 [when notice of default states entity recorded it "'as agent for beneficiary,'" the debtor must allege facts showing the entity was not the beneficiary's agent to state a claim]; *Fontenot*, *supra*, 198 Cal.App.4th at p. 270 [to state cause of action based on foreclosing entity's lack of authority borrower must "affirmatively" plead facts establishing lack of authority].) The Rossbergs made no such allegations. Indeed, although they alleged BofA transferred the First Deed of Trust to U.S. Bank more than two years before Cal-Western recorded the Notice of Default, the Rossbergs fail to allege U.S. Bank, as the beneficiary under the First Deed of Trust, did not authorize Cal-Western to record the Notice of Default as its agent. Accordingly, assuming Cal-Western lacked authority to act as trustee when it recorded the Notice of Default, the Rossbergs nonetheless failed to allege sufficient facts establishing Cal-Western lacked authority to record the Notice as agent for the trustee or beneficiary.

Finally, the Rossbergs contend section 2932.5 rendered the Notice of Default invalid because Cal-Western recorded the Notice *before* U.S. Bank recorded its beneficial interest in the First Deed of Trust. According to the Rossbergs, BofA transferred the First Deed of Trust to U.S. Bank in April 2007, and section 2932.5 required U.S. Bank to record its beneficial interest in the First Deed of Trust before anyone could initiate nonjudicial foreclosure proceedings on its behalf. Because U.S. Bank did not record the Assignment of Deed of Trust until more than a year *after* Cal-Western recorded the Notice of Default, the Rossbergs contend the Notice is void. The Rossbergs are mistaken because section 2932.5 does not apply to deeds of trust.

Section 2932.5 states, "Where a power to sell real property is given to a mortgagee, or other encumbrancer, in an instrument intended to secure the payment of money, the power is part of the security and vests in any person who by assignment becomes entitled to payment of the money secured by the instrument. The power of sale may be exercised by the assignee *if the assignment is duly acknowledged and recorded*."

(Italics added.) "It has been established since 1908 that this statutory requirement that an assignment of the beneficial interest in a debt secured by real property must be recorded in order for the assignee to exercise the power of sale applies only to a mortgage and not to a deed of trust." (*Calvo v. HSBC Bank USA, N.A.* (2011) 199 Cal.App.4th 118, 122.)

The Rossbergs cite a United States Bankruptcy Court case that reached the opposite conclusion and held section 2932.5 can be applied to deeds of trust. (See *In re Cruz* (Bankr. S.D.Cal 2011) 457 B.R. 806, 814-817.) At least one California appellate court, however, has refused to follow *Cruz* because it misunderstood how a deed of trust operates. (*Haynes v. EMC Mortgage Corp.* (2012) 205 Cal.App.4th 329, 335-336.) The *Haynes* court explained, "Section 2932.5 requires the recorded assignment of a mortgage so that a prospective purchaser knows that the mortgagee has the authority to exercise the power of sale. This is not necessary when a deed of trust is involved, as the trustee conducts the sale and transfers title. [Citation.] It is the trustee's holding and transferring of title that underlies the application of different recording requirements than those required of mortgagees under section 2932.5." (*Haynes*, at p. 336.) Based on *Haynes*, we recently held "section 2932.5 [is] inapplicable to trust deeds." (*Jenkins*, *supra*, 216 Cal.App.4th at p. 518.) Accordingly, nothing in section 2932.5 rendered the Notice of Default invalid.[11]

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[11] The Rossbergs also question the validity of the nonjudicial foreclosure on their home because BAC attached a declaration to the Notice of Sale and the Rossbergs claim it was unclear what role BAC had regarding the nonjudicial foreclosure process or their loans. The declaration, however, solely relates to the servicing of the Rossbergs' loan and the timing of the Notice of Sale. BAC did not sign the Notice of Sale nor did it claim to have any role in the nonjudicial foreclosure process. The Rossbergs provide no explanation or authority to show that BAC's declaration attached to the Notice of Sale had any impact on the validity of the nonjudicial foreclosure process. Accordingly the Rossbergs forfeited any claim based on BAC signing the declaration. (See, e.g., *Salas v. Department of Transportation* (2011) 198 Cal.App.4th 1058, 1074 [appellant forfeited challenge by failing to present reasoned argument and explanation].)

3. Third Cause of Action for Fraud

This cause of action seeks to state a fraud claim based on Defendants' promises to modify the Rossbergs' loans. Promissory fraud or false promise "'is a subspecies of the action for fraud and deceit. A promise to do something necessarily implies the intention to perform; hence, where a promise is made without such intention, there is an implied misrepresentation of fact that may be actionable fraud.' [Citation.]" (*Engalla v. Permanente Medical Group, Inc.* (1997) 15 Cal.4th 951, 973-974; § 1572, subd. (4) ["Actual fraud . . . consists in any of the following acts: [¶] . . . [¶] A promise made without any intention of performing it"].)

"The elements of promissory fraud . . . are: (1) a promise made regarding a material fact without any intention of performing it; (2) the existence of the intent not to perform at the time the promise was made; (3) intent to deceive or induce the promisee to enter into a transaction; (4) reasonable reliance by the promisee; (5) nonperformance by the party making the promise; and (6) resulting damage to the promise[e]." (*Behnke v. State Farm General Ins. Co.* (2011) 196 Cal.App.4th 1443, 1453.) As with any other form of fraud, each element of a promissory fraud claim must be alleged with particularity. (*Beckwith v. Dahl* (2012) 205 Cal.App.4th 1039, 1059-1060 (*Beckwith*).)

Here, the Rossbergs alleged specific BofA employees promised on multiple occasions that the Rossbergs had been granted specific modifications to their loans, but neither BofA nor U.S. Bank ever intended to modify the Rossbergs' loans. The Rossbergs allege they relied on these promises by "execut[ing] continual loan modification papers and disclos[ing] their confidential, private and personal information." Finally, the Rossbergs allege their reliance on the promised loan modifications caused them "hundreds of thousands of dollars" in damages. These allegations fail to state a promissory fraud claim because they fail to specifically allege the harm the Rossbergs suffered and how the Rossbergs' reliance on the promised loan modifications caused them harm.

"'A plaintiff asserting fraud by misrepresentation is obliged to . . . "'establish a complete causal relationship' between the alleged misrepresentations and the harm claimed to have resulted therefrom."' [Citation.]" (*Beckwith*, *supra*, 205 Cal.App.4th at p. 1062.) This requires a plaintiff to allege specific facts not only showing he or she actually and justifiably relied on the defendant's misrepresentations, but also how the actions he or she took in reliance on the defendant's misrepresentations caused the alleged damages. (*Ibid*.)

""'"Misrepresentation, even maliciously committed, does not support a cause of action unless the plaintiff suffered consequential damages.'"' [Citation.]" (*Beckwith*, *supra*, 205 Cal.App.4th at p. 1064.) Indeed, "'"[a]ssuming . . . a claimant's reliance on the actionable misrepresentation, no liability attaches if the damages sustained were otherwise inevitable or due to *unrelated causes*." [Citation.]' [Citation.] If the defrauded plaintiff would have suffered the alleged damage even in the absence of the fraudulent inducement, causation *cannot* be alleged and a fraud cause of action cannot be sustained." (*Ibid*., original italics.)

The Rossbergs did not satisfy these standards. They did not allege any specific damages they suffered as a result of their reliance on the promised loan modifications nor did they allege how their execution of loan modification papers and disclosure of confidential information caused those unspecified damages. For example, the Rossbergs did not allege BofA or U.S. Bank used the confidential information the Rossbergs disclosed for an improper purpose or in any way that injured the Rossbergs. Indeed, there are no allegations at all regarding how BofA or U.S. Bank used the confidential information the Rossbergs disclosed. The logical inference is that BofA used the information to evaluate the Rossbergs' requests for a loan modification, but there is nothing improper about that. Significantly, the Rossbergs do not allege their reliance on the promised loan modifications caused them to default on their loans or prevented them from curing their existing defaults. In short, the Rossbergs failed to allege any connection between their reliance on the promised loan modifications and any specific damages that reliance caused.

In their brief, the Rossbergs argue BofA's promised loan modifications induced them to continue making loan payments to BofA instead of obtaining a replacement loan. The Rossbergs, however, did not allege this theory of reliance in their first amended complaint and therefore we may not consider this argument in evaluating whether they have shown a viable fraud cause of action. (*Hensler*, *supra*, 8 Cal.4th at pp. 8-9, fn. 3.) Moreover, the Rossbergs fail to explain how continuing to pay on their loans caused them damages when BofA credited those payments toward the amount they undisputedly owed and allowed them to remain in their home. The Rossbergs also failed to provide facts showing they had sufficient equity in their home and sufficient income to qualify for a replacement loan. The conclusory allegation they would have obtained a replacement loan does not state a cause of action.

The Rossbergs also argue the promised loan modifications induced them not to sell their home "early on" and payoff BofA before their home lost a significant amount of its value. Again, we cannot consider this theory because it was not alleged in the first amended complaint. (*Hensler*, *supra*, 8 Cal.4th at pp. 8-9, fn. 3.) Moreover, the Rossbergs failed to provide sufficient facts to support this theory. For example, they do not allege the value of their home "early on," the value of their home when BofA first promised a loan modification, the amount they owed BofA when it first promised a loan modification, or whether they could have sold their home for more than they owed. The conclusory allegation the Rossbergs could have sold their home and paid off their loans does not state a cause of action.[12]

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[12] In their brief, the Rossbergs also contend their fraud cause of action was based on the fraudulent nonjudicial foreclosure documents and their false notarizations. The Rossbergs, however, do not allege they did anything or refrained from doing anything based on the various nonjudicial foreclosure documents such as the Notice of Default or the Notice of Sale. Moreover, as explained above, the Rossbergs failed to

Next, the Rossbergs contend an exception to the particularity requirement exists when the defendant necessarily possesses full information concerning the facts supporting the alleged cause of action. Although the Rossbergs are correct that "[l]ess specificity is required when 'it appears from the nature of the allegations that the defendant must necessarily possess full information concerning the facts of the controversy' [citation]" (*Committee on Children's Television, Inc. v. General Foods Corp.* (1983) 35 Cal.3d 197, 217), that exception does not apply to the Rossbergs' failure to specifically allege their damages and how their reliance on BofA's promises caused those damages. This exception is usually applied to the elements regarding a defendant's representations and intent, not the elements regarding the plaintiff's own damages and reliance. Here, Defendants would not necessarily possess full information regarding the Rossbergs' damages or how the Rossbergs' reliance caused those damages without the Rossbergs providing that information.

Finally, the Rossbergs contend *Auerbach v. Great Western Bank* (1999) 74 Cal.App.4th 1172, supports their fraud cause of action because it upheld part of a damages award based on a lender's false promises it would grant a loan modification if the borrower continued to make payments on the underlying loan. The Rossbergs are mistaken. *Auerbach* did not address whether the borrower adequately alleged a promissory fraud claim. The issues in *Auerbach* concerned the type of out-of-pocket damages recoverable on a promissory fraud claim. (*Id*. at p. 1175.) The *Auerbach* court expressly stated it was not deciding "whether a lender's false promises made to induce nonrecourse borrowers to continue to make loan payments can ever support a claim of fraud." (*Id*. at p. 1187.)

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adequately allege the nonjudicial foreclosure documents were forged or otherwise false in any material way.

4. Fourth Cause of Action for Violation of Business and Professions Code Section 17200 et seq.

Business and Professions Code section 17200 et seq. is commonly referred to as the Unfair Competition Law (UCL). "'[T]o protect both consumers and competitors by promoting fair competition in commercial markets for goods and services' [citation], the 'UCL prohibits, and provides civil remedies for, unfair competition.' [Citation.]" (*Jenkins*, *supra*, 216 Cal.App.4th at p. 520.) "[T]he UCL's 'coverage is "sweeping, embracing '"anything that can properly be called a business practice and that at the same time is forbidden by law."'" [Citation.]' [Citation.] Furthermore, the UCL creates '"three varieties of unfair competition—acts or practices which are *unlawful*, or *unfair*, or *fraudulent*."' [Citation.]" (*Ibid*., original italics.)

The Rossbergs argue their UCL claim is "well pled" because they "allege fraud, and breach of statutes. Further, in terms of unfairness, it has been held that refusal to communicate with a borrower, and false communications as to loan status (e.g. the granting of the loan modification)[] are unfair. The complaint alleges over 100 ignored phone calls, and false communications. Furthermore, failing to abide by a valid court order, such as in the Stipulated Judgment with the California Attorney General is per se against California public policy and is unfair."

The foregoing paragraph is the Rossbergs' entire argument and explanation as to why they adequately alleged a UCL claim. They cite no authority showing what is required to allege a fraud claim under the UCL and make no attempt to explain how the first amended complaint's allegations adequately state such a claim. Similarly, although they contend they stated a UCL claim by alleging "breach of statutes," the Rossbergs fail to identify which statutes Defendants breached or how they violated those statutes. As explained above, the Rossbergs did not allege a breach of section 2923.5 or section 2924 et seq. The Stipulated Judgment to which the Rossbergs refer was entered into regarding Countrywide Financial Corporation's business practices before BofA acquired

Countrywide, does not require BofA to grant the Rossbergs or anyone else a loan modification, and may not be enforced by the Rossbergs because they are not parties to it. Moreover, the Rossbergs fail to identify any provision in the Stipulated Judgment that BofA or U.S. Bank allegedly breached. Finally, the Rossbergs fail to cite any authority to explain what constitutes an unfair business practice or act under the UCL or to support their statement "it has been held that refusal to communicate with a borrower, and false communications as to loan status . . . are unfair [under the UCL]."

As the plaintiffs and appellants, the Rossbergs bore the burden to show how the alleged facts are sufficient to establish every element of this cause of action. (*Martin*, *supra*, 173 Cal.App.4th at p. 1031; see also *Sui*, *supra*, 196 Cal.App.4th at p. 938.) But the Rossbergs failed to provide any reasoned explanation or cite any authority to support the statements in their brief. We therefore treat their challenge to the trial court's ruling sustaining the demurrer to the UCL claim as waived. (*Nelson v. Avondale Homeowners Assn.* (2009) 172 Cal.App.4th 857, 862 (*Nelson*) ["'When an appellant fails to raise a point, or asserts it but fails to support it with reasoned argument and citations to authority, we treat the point as waived'"]; *Paulus v. Bob Lynch Ford, Inc.* (2006) 139 Cal.App.4th 659, 685 (*Paulus*) ["'"Issues do not have a life of their own: if they are not raised or supported by argument or citation to authority, we consider the issues waived"'"].) "We are not bound to develop [the Rossbergs'] arguments for them." (*In re Marriage of Falcone & Fyke* (2008) 164 Cal.App.4th 814, 830; see also *Benach v. County of Los Angeles* (2007) 149 Cal.App.4th 836, 852.)

5. Fifth Cause of Action for Breach of Contract

This cause of action alleged the Rossbergs and Defendants entered into a "partially written, partially verbal, and verbal agreement" to modify the Rossbergs' loans based on BofA's oral representations that it had granted the Rossbergs' loan modification request and the statements on BofA's Web site describing its loan modification programs.

This cause of action fails as a matter of law because the Rossbergs failed to allege they entered into a signed, written agreement with BofA to modify their loans.

The statute of frauds requires any contract subject to its provisions to be memorialized in a writing subscribed by the party to be charged or by the party's agent. (§ 1624; *Secrest v. Security National Mortgage Loan Trust 2002-2* (2008) 167 Cal.App.4th 544, 552.) An agreement for the sale of real property or an interest in real property comes within the statute of frauds. That includes a promissory note and a deed of trust securing performance under the note. (*Secrest*, at p. 552.) "An agreement to modify a contract that is subject to the statute of frauds is also subject to the statute of frauds." (*Id*. at p. 553.) In *Secrest*, we therefore held a forbearance agreement, in which a lender agreed not to foreclose on the borrowers' home if the borrowers satisfied certain conditions, was subject to the statute of frauds because it modified the original promissory note and deed of trust the borrowers executed. (*Ibid*.)

Here, the Rossbergs alleged the loan modification agreement they entered into with BofA modified the terms of their promissory note and deed of trust by changing the interest rate and principal balance, among other things. The statute of frauds therefore required the loan modification agreement to be in a writing signed by BofA. The Rossbergs, however, concede there is no written loan modification agreement signed by BofA. They therefore failed to allege a cause of action for breach of the purported loan modification agreement.

The Rossbergs contend their loan modification agreement with BofA was not subject to the statute of frauds because the "object of the [loan modification] agreement was to arrange a refinancing loan," not to convey an interest in real property. This argument fails because it contradicts controlling precedent, as we explained in *Secrest*.

The Rossbergs also contend we should reject BofA's argument that the statute of frauds bars this cause of action because BofA never signs written agreements granting homeowner loan modifications. The Rossbergs, however, base their argument on facts not alleged on the face of their pleading. Because the Rossbergs sought to allege a contract subject to the statute of frauds, they must allege a written contract signed by BofA and their failure to do so is a legal issue properly decided on demurrer. (Weil & Brown, Cal. Practice Guide: Civil Procedure Before Trial (The Rutter Group 2013) ¶ 7:58, p. 7(I)-33 (rev. # 1 2013) citing *Parker v. Solomon* (1959) 171 Cal.App.2d 125, 136.) Whether BofA routinely signs a written agreement when it modifies a borrower's loan is irrelevant. The statute of frauds requires a signed writing and therefore the Rossbergs must allege facts establishing the existence of a signed writing to state this cause of action.

6. Sixth Cause of Action for Declaratory Relief and Seventh Cause of Action for Quiet Title

The sixth cause of action seeks a judicial declaration that the Substitution of Trustee, the Notice of Default, and the Notice of Sale are void based on the defects discussed above concerning the first and second causes of action, and also a judicial declaration modifying the First Note, First Deed of Trust, Second Note, and Second Deed of Trust to conform to the loan modifications BofA promised the Rossbergs. The seventh cause of action seeks to quiet title against Defendants and Cal-Western "for the reasons set forth hereinabove." The Rossbergs, however, fail to explain how the trial court erred in sustaining the demurrer to these causes of action or why they alleged sufficient facts to state these claims.

The Rossbergs' brief addresses these two causes of action in a single paragraph, citing *Curry v. Moody* (1995) 40 Cal.App.4th 1547, and *Exxess Electronixx v. Heger Realty Corp.* (1998) 64 Cal.App.4th 698. Both of these cases address whether a party may recover contractual attorney fees under section 1717 as the prevailing party in an action on a contract. (*Curry*, at pp. 1556-1557; *Exxess*, at p. 708.) They do not address what is required to state a declaratory relief or quiet title claim, and the Rossbergs provide no explanation regarding how these cases show the trial court erroneously sustained Defendants' demurrer to these causes of action. The Rossbergs therefore failed to meet their burden to show they alleged sufficient facts to state these causes of action. (*Martin*, *supra*, 173 Cal.App.4th at p. 1031; see also *Sui*, *supra*, 196 Cal.App.4th at p. 938.) We also treat the Rossbergs' challenge to the ruling sustaining the demurrer to these causes of action as waived because the Rossbergs did not provide any reasoned argument to support their challenge. (*Nelson*, *supra*, 172 Cal.App.4th at p. 862; *Paulus*, *supra*, 139 Cal.App.4th at p. 685.)

D. *The Rossbergs Are Not Entitled to Leave to Amend*

In their reply, the Rossbergs invoke California's liberal policy in favor of permitting amended pleadings and argue we should grant them leave to amend on any claim where they failed to adequately allege a cause of action. As explained above, however, it is not sufficient for the Rossbergs to assert "an abstract right to amend." (*Rakestraw*, *supra*, 81 Cal.App.4th at p. 43.) Instead, they must "clearly and specifically" set forth the legal authority for the claims they contend they can allege, the elements of each of those claims, and the specific factual allegations that would establish each of those elements. (*Ibid*.) The Rossbergs made no attempt to meet this burden.

III

DISPOSITION

The judgment is affirmed. Because we affirm the trial court's judgment dismissing the Rossbergs' action, we also dismiss the petition for writ of mandate as moot. Defendants shall recover their costs on appeal.

ARONSON, J.

WE CONCUR:

RYLAARSDAM, ACTING P. J.

IKOLA, J.

Filed 9/26/13

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

ALAN SHAUN ROSSBERG et al.,

Plaintiffs and Appellants,

v.

BANK OF AMERICA, N.A., et al.,

Defendants and Respondents.

G047028 (cons. with G047355)

(Super. Ct. No. 30-2011-00462732)

ORDER (1) DENYING PETITION FOR REHEARING; (2) MODIFYING OPINION; AND (3) GRANTING REQUEST FOR PUBLICATION; NO CHANGE IN JUDGMENT

Plaintiffs and appellants Alan Shaun Rossberg and Brenda Rossberg's petition for rehearing is DENIED.

It is ordered that the opinion filed in the above-entitled matter on August 27, 2013, is hereby MODIFIED as follows:

1. On page 2, the last sentence at the bottom of the page, beginning with "Finally, because we affirm the trial court's judgment," the words "evicting them from their home" are deleted and replaced with the words "initiating eviction proceedings" so the sentence reads:

> Finally, because we affirm the trial court's judgment dismissing the Rossbergs' action, we dismiss as moot the Rossbergs' petition for writ of mandate to prevent Defendants from initiating eviction proceedings during this appeal.

2. On page 6, the fourth item in the numbered list in the last paragraph on the bottom of the page, beginning with "(4) it is unclear who held the First Note," delete the words "Servicing and Pool Agreement" and replace them with the words "Pooling and Servicing Agreement" so the fourth item in the list reads:

> (4) it is unclear who held the First Note and First Deed of Trust when the Notice of Default and Notice of Sale were recorded because the Pooling and Servicing Agreement transferred the First Note and First Deed of Trust to U.S. Bank in April 2007, but the Assignment of Deed of Trust purported to make that same transfer in January 2011.

3. On page 14, the first sentence of the last paragraph at the bottom of the page, beginning with "The Rossbergs first contend," the word "was" is deleted and replaced with the word "had" and the word "yet" is deleted and replaced with the word "been" so the sentence reads:

> The Rossbergs first contend Cal-Western lacked authority because it had not been designated as trustee when it recorded the Notice of Default.

4. On page 16, the second sentence of the second full paragraph, beginning with "The Notice of Default did not state," insert the words "BofA designated" between the words "state" and "Cal-Western," delete the words "was acting" and replace them with the words "to act," and delete the words "designated by BofA" at the end of the sentence so the sentence reads:

> The Notice of Default did not state BofA designated Cal-Western to act as a substituted trustee.

5. On page 17, the bracketed statement following the citation to the *Jenkins* case at the top of the page, insert the words “to state a claim” between the words “debtor” and “must” and delete the words “to state a claim” at the end of the bracketed statement so the bracketed statement reads:

> [when notice of default states entity recorded it “‘as agent for beneficiary,’” the debtor to state a claim must allege facts showing the entity was not the beneficiary’s agent]

6. On page 18, the last sentence in footnote 11, beginning with “Accordingly, the Rossbergs forfeited,” delete the word “Accordingly” at the beginning of the sentence and replace it with the word “Consequently,” so the sentence reads:

> Consequently, the Rossbergs forfeited any claim based on BAC signing the declaration.

7. On page 19, the first sentence at the top of the page, beginning with “This cause of action,” delete the words “seeks to state” and replace them with the word “alleges” so the sentence reads:

> This cause of action alleges a fraud claim based on Defendants’ promises to modify the Rossbergs’ loans.

8. On page 21, following the third sentence of the first full paragraph at the top of the page, beginning with “Moreover, the Rossbergs fail to explain,” insert the citation “(See *West v. JPMorgan Chase Bank, N.A.* (2013) 214 Cal.App.4th 780, 795.)”

9. On page 21, the first sentence in footnote 12, beginning with “In their brief,” insert the words “they based” between the words “contend” and “their” and delete the words “was based” so the sentence reads:

> In their brief, the Rossbergs also contend they based their fraud cause of action on the fraudulent nonjudicial foreclosure documents and their false notarizations.

10. On page 21, the last sentence in footnote 12 beginning at the bottom of the page and continuing on the bottom of page 22, beginning with "Moreover, as explained above," delete the words "in any material way" at the end of the sentence so the sentence reads:

> Moreover, as explained above, the Rossbergs failed to adequately allege the nonjudicial foreclosure documents were forged or otherwise false.

Pursuant to California Rules of Court, rule 8.1105(c), and for good cause shown, Defendant and respondent Bank of America, N.A.'s request to publish the opinion is GRANTED. The opinion is ordered published in the Official Reports. (Cal. Rules of Court, rule 8.1105(b).)

These modifications do not change the judgment.

ARONSON, J.

WE CONCUR:

RYLAARSDAM, ACTING P. J.

IKOLA, J.

Filed 8/27/13

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION THREE

JOHNNY SILIGA et al., Plaintiffs and Appellants, v. MORTGAGE ELECTRONIC REGISTRATION SYSTEMS, INC., et al., Defendants and Respondents.	B240531 (Los Angeles County Super. Ct. No. BC454905)

APPEAL from a judgment of the Superior Court of Los Angeles County, Gregory W. Alarcon, Judge. Affirmed.

Law Offices of Nick A. Alden and Nick A. Alden for Plaintiffs and Appellants.

Locke Lord, Conrad V. Sison and Daniel A. Solitro for Defendants and Respondents.

Johnny Siliga and Fa'alagilagi Siliga appeal a judgment dismissing their complaint against Mortgage Electronic Registration Systems, Inc. (MERS), Quality Loan Services Company (QLS) and Deutsche Bank National Trust Company (Deutsche Bank) after the sustaining of a demurrer without leave to amend. The Siligas allege four counts arising from a nonjudicial foreclosure. They challenge MERS's authority to assign the deed of trust and the note to Deutsche Bank and QLS's authority to record a notice of default. They also contend they are entitled to leave to amend their complaint to correct particular defects. We conclude that they have shown no error and will affirm the judgment.

FACTUAL AND PROCEDURAL BACKGROUND

1. *Factual Background*

The Siligas executed a deed of trust in June 2004 against real property, their primary residence, located in Carson, California. The deed of trust secured a $280,000 promissory note in favor Accredited Home Lenders, Inc (Accredited). The deed of trust identified the Siligas as "Borrower" and Accredited as "Lender."

The deed of trust stated, "MERS is a separate corporation that is acting solely as a nominee for Lender and Lender's successors and assigns. **MERS is the beneficiary under this Security Instrument.**" It stated further, "The beneficiary of this Security Instrument is MERS (solely as nominee for Lender and Lender's successors and assigns) and the successors and assigns of MERS," and "Borrower understands and agrees that MERS holds only legal title to the interests granted by Borrower in this Security Instrument, but, if necessary to comply with law or custom, MERS (as nominee for Lender and Lender's successors and assigns) has the right to exercise any or all of those interests, including, but not limited to, the right to foreclose and sell the Property, and to take any action required of Lender including, but not limited to, releasing and canceling this Security Instrument."

QLS recorded a notice of default and election to sell under deed of trust on March 24, 2010. The notice of default stated that QLS was acting as agent for the beneficiary. A Corporate Assignment of Deed of Trust was recorded on April 28, 2010, stating that MERS was assigning to Deutsche Bank the deed of trust "[t]ogether with the note or notes therein described or referred to . . . . " Deutsche Bank executed a substitution of trustee in May 2010 naming QLS as the new trustee, and the document was recorded on May 19, 2010. QLS recorded a notice of trustee's sale on August 19, 2010.

The trustee's sale was postponed and apparently has not occurred to this date.

2. *Trial Court Proceedings*

The Siligas filed a complaint in February 2011 and filed a first amended complaint against MERS, QLS and Deutsche Bank in May 2011. They allege in pertinent part that (1) MERS as nominee for the lender had no authority to assign the deed of trust and the note to Deutsche Bank; (2) Deutsche Bank had no authority to commence a nonjudicial foreclosure because it was never validly assigned and did not possess the promissory note; (3) the defendants failed to comply with the statutory requirement of attempting to contact the borrower in person or by telephone to assess the borrower's financial situation and explore options to avoid foreclosure before recording a notice of default (Civ. Code, § 2923.5, subd. (a)(2)); (4) the notice of trustee's sale was recorded before the expiration of the 90-day waiting period required under former Civil Code section 2923.52, subdivision (a); and (5) QLS failed to timely post a notice of trustee's sale on the property and failed to timely notify them of the sale.

The Siligas plead counts for (1) breach of contract, alleging that QLS breached the deed of trust by recording a notice of default before it was appointed as trustee; (2) violation of statutory duties, alleging that the defendants' acts and omissions set forth above violated numerous statutory requirements; (3) unfair business practices, alleging that the same acts and omissions constituted unlawful or unfair business practices under the unfair competition law (Bus. & Prof. Code, § 17200 et seq.); and (4) quiet title, seeking to invalidate all adverse claims of interest in the property. They filed an ex parte application for a temporary restraining order at the time they filed their first amended complaint. The trial court denied the application.[1]

Deutsche Bank and MERS filed a general demurrer to each count alleged in the first amended complaint. They argued that the Siligas failed to state any valid cause of action because they failed to allege that they had tendered the amount due. They also argued, among other things, that (1) the Siligas' attacks on the defendants' authority to act in connection with the foreclosure were groundless; (2) the declaration in the notice of default satisfied Civil Code section 2923.5, subdivision (a)(2); (3) former Civil Code

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[1] We affirmed the denial in an unpublished opinion (*Siliga v. Mortgage Electronic Registration Systems, Inc.* (Feb. 9, 2012, B233000)).

section 2923.52 was inapplicable; (4) the Siligas had suffered no injury and therefore lacked standing under the unfair competition law; and (5) the Siligas were not entitled to quiet title. They filed a request for judicial notice of certain recorded documents in support of their demurrer. The Siligas opposed the demurrer and also requested judicial notice of certain documents.[2]

The trial court filed a signed order ruling on the demurrer on July 14, 2011. It stated that the Siligas' first, third and fourth counts and part of their second count were based on the allegation that MERS had no authority to assign the deed of trust to Deutsche Bank. It noted the language in the deed of trust that " 'MERS (as nominee for Lender and Lender's successors and assigns) has the right to exercise any or all of those interests, including, but not limited to, the right to foreclose . . . . ' " Citing *Gomes v. Countrywide Home Loans, Inc.* (2011) 192 Cal.App.4th 1149, 1157 (*Gomes*), for the proposition that MERS as nominee for the lender has the authority to initiate a nonjudicial foreclosure as stated in the deed of trust, the court concluded that MERS also had the authority to assign the deed of trust. The court therefore sustained the demurrer without leave to amend as to the entire complaint with the exception of that part of the second count alleging the violation of Civil Code section 2923.5.

The order stated further that notwithstanding the sustaining of the demurrer to most of the complaint, the trial court would discuss each count further "to determine

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[2] No ruling on the requests for judicial notice appears in the record on appeal.

what the outcome of their pleading *would have been* had that cause of action not been barred." The order then proceeded to discuss each count.

The Siligas filed a request for the dismissal without prejudice of their second count as to the alleged violation of Civil Code section 2923.5. The trial court clerk entered a dismissal on January 25, 2012, as requested. The court entered a signed order on March 27, 2012, dismissing the remainder of the complaint with prejudice in accordance with its ruling on the demurrer.[3] The Siligas timely appealed the judgment.

CONTENTIONS

The Siligas contend (1) MERS had no authority to assign the deed of trust and the note; (2) the provision in the deed of trust granting authority to MERS is unconscionable; (3) the notice of default is invalid because QLS had no authority to record it; (4) they are entitled to leave to amend their complaint to allege damages for breach of contract more specifically; (5) they are entitled to leave to amend their count for unfair business practices; and (6) they have adequately alleged a count for quiet title.

DISCUSSION

1. *Standard of Review*

A demurrer tests the legal sufficiency of the factual allegations in a complaint. We independently review the sustaining of a demurrer and determine de novo whether the complaint alleges facts sufficient to state a cause of action or discloses a complete defense. (*McCall v. PacifiCare of Cal., Inc.* (2001) 25 Cal.4th 412, 415.) We assume

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[3] A signed order of dismissal is an appealable judgment. (Code Civ. Proc., §§ 581d., 904.1, subd.(a)(1).)

the truth of the properly pleaded factual allegations, facts that reasonably can be inferred from those expressly pleaded and matters of which judicial notice has been taken. (*Schifando v. City of Los Angeles* (2003) 31 Cal.4th 1074, 1081.) We construe the pleading in a reasonable manner and read the allegations in context. (*Ibid.*) We must affirm the judgment if the sustaining of a general demurrer was proper on any of the grounds stated in the demurrer, regardless of the trial court's stated reasons. (*Aubry v. Tri-City Hospital Dist.* (1992) 2 Cal.4th 962, 967.)

It is an abuse of discretion to sustain a demurrer without leave to amend if there is a reasonable probability that the defect can be cured by amendment. (*Schifando v. City of Los Angeles, supra*, 31 Cal.4th at p. 1082.) The burden is on the plaintiff to demonstrate how the complaint can be amended to state a valid cause of action. (*Ibid.*) The plaintiff can make that showing for the first time on appeal. (*Careau & Co. v. Security Pacific Business Credit, Inc.* (1990) 222 Cal.App.3d 1371, 1386.)

2. *The Siligas Cannot Maintain a Preemptive Judicial Action Challenging the Defendants' Authority to Foreclose*

"California's nonjudicial foreclosure scheme is set forth in Civil Code sections 2924 through 2924k, which 'provide a comprehensive framework for the regulation of a nonjudicial foreclosure sale pursuant to a power of sale contained in a deed of trust.' (*Moeller v. Lien* (1994) 25 Cal.App.4th 822, 830 [30 Cal.Rptr.2d 777] (*Moeller*).) 'These provisions cover every aspect of exercise of the power of sale contained in a deed of trust.' (*I. E. Associates v. Safeco Title Ins. Co.* (1985) 39 Cal.3d 281, 285 [216 Cal.Rptr. 438, 702 P.2d 596].) 'The purposes of this comprehensive scheme are threefold: (1) to provide the creditor/beneficiary with a quick, inexpensive and efficient remedy against a defaulting debtor/trustor; (2) to protect the debtor/trustor from wrongful loss of the property; and (3) to ensure that a properly conducted sale is final between the parties and conclusive as to a bona fide purchaser.' (*Moeller*, at p. 830.) 'Because of the exhaustive nature of this scheme, California appellate courts have refused to read any additional requirements into the non-judicial foreclosure statute.' (*Lane v. Vitek Real Estate Industries Group* (E.D.Cal. 2010) 713 F.Supp.2d 1092, 1098; see also *Moeller*, at p. 834 ['It would be inconsistent with the comprehensive and exhaustive statutory scheme regulating nonjudicial foreclosures to incorporate another unrelated cure provision into statutory nonjudicial foreclosure proceedings.'].)" (*Gomes, supra*, 192 Cal.App.4th at p. 1154.)

California courts have refused to allow trustors to delay the nonjudicial foreclosure process by pursuing preemptive judicial actions challenging the authority of a foreclosing "beneficiary" or beneficiary's "agent." (*Jenkins v. JPMorgan Chase Bank, N.A.* (2013) 216 Cal.App.4th 497, 511 (*Jenkins*); *Gomes*, *supra*, 192 Cal.App.4th at pp. 1154-1156 & fn. 5.) Such an action is "preemptive" if the plaintiff alleges no "specific factual x" for the claim that the foreclosure was not initiated by the correct person. (*Jenkins*, *supra*, at p. 512.) A preemptive suit does not seek a remedy for specified misconduct in the nonjudicial foreclosure process, which may provide a basis for a valid cause of action. Instead, a preemptive suit seeks to create an additional requirement for the foreclosing party, apart from the comprehensive statutory requirements, by requiring the foreclosing party to demonstrate in court that it is authorized to initiate a foreclosure. (*Ibid.*) "[A]llowing a trustor-debtor to pursue such an action, absent a '*specific factual basis* for alleging that the foreclosure was not initiated by the correct party' would unnecessarily 'interject the courts into [the] comprehensive nonjudicial scheme' created by the Legislature, and 'would be inconsistent with the policy behind nonjudicial foreclosure of providing a quick, inexpensive and efficient remedy. [Citation.]' " (*Id.* at p. 512; italics in original.)

3. *The Siligas Fail to Adequately Allege that MERS Lacked Authority to Assign the Deed of Trust and the Note*

The Siligas argue that MERS had no authority to assign the deed of trust and the note essentially for three reasons. First, they argue that any authority given to MERS by Accredited as the lender lapsed when Accredited went out of business. Second, they argue that MERS had no authority to assign the note, and an assignment of a deed of trust without an assignment of the note is invalid as a matter of law. Third, they argue that MERS required Accredited's written authorization to assign the deed of trust and the note in order to satisfy the statute of frauds, and there is no evidence that MERS had such written authorization.

Fontenot v. Wells Fargo Bank, N.A. (2011) 198 Cal.App.4th 256, 267 (*Fontenot*), explained: "MERS is a private corporation that administers a national registry of real estate debt interest transactions. Members of the MERS System assign limited interests in the real property to MERS, which is listed as a grantee in the official records of local governments, but the members retain the promissory notes and mortgage servicing rights. The notes may thereafter be transferred among members without requiring recordation in the public records. [Citation.] [¶] Ordinarily, the owner of a promissory note secured by a deed of trust is designated as the beneficiary of the deed of trust. [Citation.] Under the MERS System, however, MERS is designated as the beneficiary in deeds of trust, acting as 'nominee' for the lender and granted the authority to exercise legal rights of the lender."

California courts have held that a trustor who agreed under the terms of the deed of trust that MERS, as the lender's nominee, has the authority to exercise all of the rights and interests of the lender, including the right to foreclose, is precluded from maintaining a cause of action based on the allegation that MERS has no authority to exercise those rights. (*Gomes*, *supra*, 192 Cal.App.4th at p. 1157; *Herrera v. Federal National Mortgage Assn.* (2012) 205 Cal.App.4th 1495, 1505 (*Herrera*).) The deed of trust itself, attached to the Siligas' complaint, establishes as a factual matter that MERS has the authority to exercise all of the rights and interests of the lender.[4] (*Gomes*, *supra*, at p. 1157; *Herrera*, *supra*, at p. 1505.) The authority to exercise all of the rights and interests of the lender necessarily includes the authority to assign the deed of trust. (*Herrera*, *supra*, at p. 1505.)

The Siligas cite Civil Code section 2356, subdivision (a)(2) and (3), which states that an agent's authority terminates upon the death of the principal or the principal's

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[4] The facts alleged in the complaint and those judicially noticeable fail to establish that the provision in the deed of trust granting MERS the authority to foreclose is unconscionable. Contrary to the Siligas' argument, this provision does not purport to authorize MERS to initiate a foreclosure in violation of the law, is not "unfairly one-sided" or " ' " 'overly harsh' " ' " (*Little v. Auto Stiegler, Inc.* (2003) 29 Cal.4th 1064, 1071), and therefore is not substantively unconscionable.

incapacity to contract unless the agent's power is coupled with an interest in the subject of the agency. They argue that MERS's authority was terminated upon Accredited's going out of business and filing for bankruptcy protection. But they do not allege in their complaint that Accredited has gone out of business, dissolved or suffered either death or an incapacity to contract in any manner. Accredited's chapter 11 bankruptcy petition, which we have judicially noticed at the Siligas' request, relates to a reorganization and shows neither the company's death nor an incapacity to contract. The Siligas have not alleged facts showing any lapse in MERS's authority to assign the deed of trust and the note on this basis; nor do they argue, if given the opportunity, that they could do so.

The Siligas also fail to allege facts supporting the conclusion that MERS lacked authority to assign the note. "The extent of MERS's authority as a nominee was defined by its agency agreement with the lender, and whether MERS had the authority to assign the lender's interest in the note must be determined by reference to that agreement. [Citations.] Accordingly, the allegation that MERS was merely a nominee is insufficient to demonstrate that MERS lacked authority to make a valid assignment of the note on behalf of the original lender." (*Fontenot*, *supra*, 198 Cal.App.4th at pp. 270-271.) The Siligas allege that "MERS did not and could not have assigned the Promissory Note to DEUTSCHE BANK," but they allege no specific factual basis for this claim. Absent a specific factual basis, this claim amounts to a preemptive claim seeking to require the foreclosing party to demonstrate in court its authority to initiate a foreclosure. Such a claim is invalid and subject to demurrer.[5] (*Jenkins*, *supra*, 216 Cal.App.4th at pp. 511-513; *Gomes*, *supra*, 192 Cal.App.4th at pp. 1154-1156 & fn. 5.) Similarly, the claim that there is no evidence that MERS had written authorization to assign the deed of trust and the note is merely a challenge to the foreclosing party to prove in court its authority to initiate a foreclosure. This claim fails for the same reason.

4. *QLS Had the Authority to Record the Notice of Default*

The Siligas contend QLS had no authority to record the notice of default because it was not the trustee at the time. A notice of default may be recorded by a "trustee, mortgagee, or beneficiary, or any of their authorized agents." (Civ. Code, § 2924, subd. (a)(1).) The notice of default stated that QLS recorded the notice of default not as trustee but as agent for the beneficiary. This was proper, and the Siligas have shown no error in this regard.

5. *The Siligas Fail to Adequately Allege any Prejudice Resulting from an Alleged Irregularity in the Foreclosure Process*

Separate and apart from the foregoing, the Siligas fail to allege any facts showing that they suffered prejudice as a result of any lack of authority of the parties participating in the foreclosure process. The Siligas do not dispute that they are in

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[5] We reject the argument that MERS as nominee of the original lender could not assign the note because it did not possess the note. The Siligas allege no factual basis for this argument, and there is no legal basis. (*Fontenot, supra,* 198 Cal.App.4th at pp. 270-271.) Similarly, there is no legal basis for the claim that the foreclosing party must possess the original note. Nothing in the foreclosure statutes imposes such a requirement. (*Debrunner v. Deutsche Bank National Trust Co.* (2012) 204 Cal.App.4th 433, 440.)

default under the note. The assignment of the deed of trust and the note did not change the Siligas' obligations under the note, and there is no reason to believe that Accredited as the original lender would have refrained from foreclosure in these circumstances. Absent any prejudice, the Siligas have no standing to complain about any alleged lack of authority or defective assignment. (*Herrera*, *supra*, 205 Cal.App.4th at pp. 1507-1508; *Fontenot*, *supra*, 198 Cal.App.4th at p. 272.)

6. *The Siligas Have Shown No Prejudicial Error as to the Sustaining of the Demurrer to the Counts for Breach of Contract, Unfair Business Practices and Quiet Title*

The Siligas contend they are entitled to leave to amend their counts for breach of contract and unfair business practices and contend they have adequately alleged a count for quiet title. These contentions are based on the discussion in the latter part of the order ruling on the demurrer. The trial court, however, expressly did not rely on that discussion in sustaining the demurrer to those counts without leave to amend. Instead, the order stated that the discussion explained as to each count "what the outcome of their pleading *would have been* had that cause of action not been barred." We conclude that the discussion in the latter part of the order was not part of the trial court's decision and that the Siligas have shown no prejudicial error based on that discussion.

DISPOSITION

The judgment is affirmed. Defendants shall recover their costs on appeal.

CERTIFIED FOR PUBLICATION

CROSKEY, J.

WE CONCUR:

KLEIN, P. J.

KITCHING, J.

Filed 9/19/13

CERTIFIED FOR PUBLICATION

COURT OF APPEAL, FOURTH APPELLATE DISTRICT

DIVISION ONE

STATE OF CALIFORNIA

ANGELICA CHAVEZ, Plaintiff and Appellant, v. INDYMAC MORTGAGE SERVICES et al., Defendants and Respondents.	D061997 (Super. Ct. No. 37-2010-00105461-CU-OR-CTL)

APPEAL from a judgment of the Superior Court of San Diego County, Lorna Alksne, Judge. Reversed.

Law Offices of Frank De Santis, Frank De Santis and Valorie E. Ryan for Plaintiff and Appellant.

Kent Qian for National Housing Law Project; Elizabeth Letcher for Housing and Economic Rights Advocates; Law Office of Eric Andrew Mercer and Eric Mercer as Amici Curiae on behalf of Plaintiff and Appellant.

Malcolm Cisneros, William G. Malcolm and Brian S. Thomley for Defendants and Respondents.

In this case, a lender mailed a homeowner a loan modification agreement under the Home Affordable Mortgage Program (HAMP). The homeowner signed, returned and performed under the loan modification agreement. The lender, however, never mailed the homeowner a signed copy of the loan modification agreement. We conclude the homeowner sufficiently alleged equitable estoppel to preclude the lender's reliance on the statute of frauds defense. We also conclude that the homeowner sufficiently alleged a cause of action for wrongful foreclosure. Accordingly, the judgment entered after the court sustained the lender's demurrer without leave to amend is reversed.

FACTUAL AND PROCEDURAL BACKGROUND

In accordance with the principles governing our review of a ruling sustaining a demurrer, the following factual recitation is taken from the allegations of the third amended complaint filed by Angelica Chavez and from documents cognizable by judicial notice. (Code Civ. Proc., § 430.30, subd. (a); *Moore v. Regents of University of California* (1990) 51 Cal.3d 120, 125.)

In 1999, Chavez purchased residential real property located in San Diego, California (the property). In 2006, she refinanced the property which she occupied as the owner. In connection with the refinance, Chavez executed a promissory note, promising to pay SBMC Mortgage the principal amount of $380,000.00, plus interest. The promissory note was secured by a deed of trust encumbering the property. The deed of trust was later assigned to OneWest Bank, F.S.B. and Indymac Mortgage Services (together Defendants).

In November 2009, a notice of default and election to sell under deed of trust was executed and recorded. The notice stated that Chavez was in default on the promissory note and that the amount in arrears, as of October 29, 2009, was $10,603.65. In December 2009, Chavez entered into negotiations with Defendants for a loan modification. In January 2010, Defendants offered Chavez a "Home Affordable Modification Trial Period Plan (Step One of Two-Step Documentation Process)" (the Trial Period Plan) under HAMP. (Undesignated year references are to 2010.) The Trial Period Plan required her to make three monthly payments of $1,167.46 in February, March, and April.

The Trial Period Plan stated that "[i]f I am in compliance with this Trial Period Plan . . . then the lender will provide me with a Home Affordable Modification Agreement." Chavez alleged that she fully complied with all the terms of the Trial Period Plan and in May, Defendants mailed her a "Home Affordable Modification Agreement (Step Two of Two-Step Documentation Process)" (the Modification Agreement) which stated, in part, that after she signed and returned two copies of the Modification Agreement to Defendants, Defendants "will send me a signed copy of this Agreement." It further provided that if her material representations, which included her residency in the property, were true in all material respects and if the preconditions to the modification have been met, "the Loan Documents will automatically become modified on 7/1/2010."

Chavez timely returned the Modification Agreement in June, fully complied with all the requirements of the Modification Agreement and continued making her payments on time by personal check. She believed that her loan had been permanently modified. In September, Defendants returned her check for the October payment because "the check [was] not certified." The Trial Period Plan and Modification Agreement, however, do not contain such a requirement. On October 15, the property was sold at auction below fair market value. After the sale took place, Chavez learned that her home had been sold at foreclosure even though she had never received a notice of default or notice of trustee sale from Defendants. In November, Chavez was served with an unlawful detainer summons and was forced to move from her residence in February 2011 due to the wrongful foreclosure on her home.

Chavez filed this action alleging breach of the Modification Agreement and wrongful foreclosure. The trial court sustained Defendants' demurrer, without leave to amend, and entered judgment in favor of Defendants. Chavez timely appealed. We granted an application by the National Housing Law Project, Housing and Economic Rights Advocates and Eric Mercer to file an amicus brief.

DISCUSSION

I. *Standard of Review*

We review an order sustaining a demurrer without leave to amend de novo (*Blank v. Kirwan* (1985) 39 Cal.3d 311, 318), assuming the truth of all properly pleaded facts as well as facts inferred from the pleadings, and give the complaint a reasonable interpretation by reading it as a whole and its parts in context. (*Palacin v. Allstate Ins.*

Co. (2004) 119 Cal.App.4th 855, 861.) However, we give no credit to allegations that merely set forth contentions or legal conclusions. (*Financial Corp. of America v. Wilburn* (1987) 189 Cal.App.3d 764, 768–769.) A complaint will be construed "liberally . . . with a view to substantial justice between the parties." (Code Civ. Proc., § 452.) If the complaint states any possible legal theory, the trial court's order sustaining the demurrer must be reversed. (*Palestini v. General Dynamics Corp.* (2002) 99 Cal.App.4th 80, 86.) Also, "if there is a reasonable possibility the defect in the complaint could be cured by amendment, it is an abuse of discretion to sustain a demurrer without leave to amend." (*City of Atascadero v. Merrill Lynch, Pierce, Fenner & Smith* (1998) 68 Cal.App.4th 445, 459.) Whether a plaintiff will be able to prove its allegations is not relevant. (*Alcorn v. Anbro Engineering, Inc.* (1970) 2 Cal.3d 493, 496.)

II. *Analysis*

A. Breach of Contract

Chavez alleges that Defendants breached the Modification Agreement by refusing to accept her October payment, erroneously claiming she did not qualify for the Modification Agreement because she did not live at the property, and by foreclosing on the property. As a result of these breaches, Chavez claims she was forced to move from her home and suffered monetary damages. Defendants demurred to this claim arguing that the statute of frauds barred enforcement of the contract. The trial court sustained Defendants' demurrer to this claim without leave to amend on the ground Chavez failed to plead around the statute of frauds. As explained below, we conclude the trial court erred in sustaining the demurrer because the language of the Trial Period Plan and the

Modification Agreement, combined with the facts alleged in the complaint, support a claim that Defendants should be equitably estopped to assert the statute of frauds.

"A contract coming within the statute of frauds is invalid unless it is memorialized by a writing subscribed by the party to be charged or by the party's agent." (*Secrest v. Security Nat. Mortg. Loan Trust 2002-2* (2008) 167 Cal.App.4th 544, 552 (*Secrest*).) The signature of the party to be charged "need not be manually affixed, but may in some cases be printed, stamped or typewritten." (*Marks v. Walter G. McCarty Corp.* (1949) 33 Cal.2d 814, 820.) An agreement to modify a contract that is subject to the statute of frauds is also subject to the statute of frauds. (Civ. Code, § 1698.) Thus, California courts have held that forbearance agreements altering a mortgage are covered by the statute of frauds. (*Secrest*, *supra*, at p. 552.)

Courts, however, "have the power to apply equitable principles to prevent a party from using the statute of frauds where such use would constitute fraud." (*Juran v. Epstein* (1994) 23 Cal.App.4th 882, 895.) "Without the qualifying doctrine of estoppel in a proper case the statute would encourage rather than prevent the perpetration of frauds." (*Wilk v. Vencill* (1947) 30 Cal.2d 104, 108.) Accordingly, equitable estoppel may preclude the use of a statute of frauds defense. (*Byrne v. Laura* (1997) 52 Cal.App.4th 1054, 1068 (*Byrne*).) " 'The doctrine of estoppel has been applied where an unconscionable injury would result from denying enforcement after one party has been induced to make a serious change of position in reliance on the contract or where unjust enrichment would result if a party who has received the benefits of the other's performance were allowed to invoke the statute.' " (*Redke v. Silvertrust* (1971) 6 Cal.3d

94, 101.) Generally, "four elements must be present in order to apply the doctrine of equitable estoppel: (1) the party to be estopped must be apprised of the facts; (2) he must intend that his conduct shall be acted upon, or must so act that the party asserting the estoppel had a right to believe it was so intended; (3) the other party must be ignorant of the true state of facts; and (4) he must rely upon the conduct to his injury." (*Driscoll v. City of Los Angeles* (1967) 67 Cal.2d 297, 305.) Whether a party is precluded from using the statute of frauds defense in a given case is generally a question of fact. (*Byrne, supra*, at p. 1068.)

Our analysis begins with review of the Trial Period Plan and the Modification Agreement. As a general matter, contracts must be interpreted to make them "lawful, operative, definite, reasonable, and capable of being carried into effect, if it can be done without violating the intention of the parties." (Civ. Code, § 1643.) Additionally, courts " ' "must avoid an interpretation which will make a contract extraordinary, harsh, unjust, or inequitable." ' " (*Barroso v. Ocwen Loan Servicing, LLC* (2012) 208 Cal.App.4th 1001, 1012-1013.)

The Trial Period Plan stated that: "If [the borrower is] in compliance with this Trial Period Plan (the 'Plan') and [her] representations in Section 1 continue to be true in all material respects, then the Lender *will provide* [the borrower] with a Home Affordable Modification Agreement ('Modification Agreement'), as set forth in Section 3." (Italics added.) The introductory paragraph of the Trial Period Plan set forth the understanding of the parties that "after [the borrower] sign[s] and return[s] two copies of this Plan to the Lender, the Lender *will send me a signed copy of this Plan if I qualify for the Offer or* *will send me written notice that I do not qualify for the Offer.* This Plan will not take effect unless and until both the Lender and I sign it and the Lender provides me with a copy of this Plan with the Lender's signature." (Italics added.)

The Trial Period Plan further explained at paragraph 3 that "[i]f (1) [the borrower's] representations in Section 1 were and continue to be true in all material respects; (2) [the borrower] compl[ies] with the requirements in Section 2; (3) [the borrower] provide[s] the Lender with all required information and documentation; and (4) the Lender determines that I qualify, the Lender *will send* [her] a Modification Agreement for [her] signature which *will modify* [her] Loan Documents as necessary to reflect this new payment amount." (Italics added.)

As a threshold matter, we note that the language of the Trial Period Plan stating it does not take effect "unless and until both the Lender and I sign it and the Lender provides me with a copy of this Plan with the Lender's signature" essentially nullifies other express provisions of the Trial Period Plan. Namely, the introductory paragraph and paragraph 3, whereby Defendants promised it would "send [Chavez]" a Modification Agreement that would "modify [her] Loan Documents" if she "compl[ied] with the requirements" of the Trial Period Plan and if her "representations … continue to be true in all material respects."

Here, Chavez alleged she sent Defendants all required information, timely made all payments under the Trial Period Plan, and that Defendants accepted the payments and mailed her the Modification Agreement. Based on the language of the Trial Period Plan, Defendants were *required* to either send Chavez a signed copy of the Trial Period Plan if she qualified for the offer, or send her a notice that she did not qualify for the offer. Defendants did neither; rather, they sent Chavez a copy of the Modification Agreement. This action, when considered with the language of the Trial Period Plan, suggests Defendants concluded that Chavez qualified for a permanent modification despite the fact they did not send Chavez a signed copy of the Trial Period Plan. This interpretation gives effect to all provisions in the Trial Period Plan and does not render an otherwise straightforward offer into an illusion. (*Corvello v. Wells Fargo Bank, NA* (Cal. 9th Cir. 2013) ___ F.3d ___ [2013 U.S. App. LEXIS 16415, *13] ["The more natural and fair interpretation of the [Trial Period Plan] is that the servicer must send a signed Modification Agreement offering to modify the loan once borrowers meet their end of the bargain."].)

The Modification Agreement received by Chavez stated, in part, that after she signed and returned two copies to Defendants, Defendants "*will send me* a signed copy of this Agreement." (Italics added.) Thereafter, the Modification Agreement provided that if Chavez's representations continued to be true and all preconditions to modifications have been satisfied "the Loan Documents *will automatically become modified* on 7/1/2010 (the 'Modification Effective Date') and all unpaid late charges that remain unpaid will be waived." (Italics added.) By this language, defendants expressed their intent to be bound by the Modification Agreement.

The language of the Modification Agreement, however, allowed Defendants to control contract formation by stating elsewhere "that the Loan Documents will not be modified unless and until (i) I receive from the Lender a copy of this Agreement signed by the Lender . . . ." This language suggests that, even if Chavez satisfied all other conditions, Defendants had no obligation to permanently modify Chavez's loan unless they in fact mailed Chavez a signed copy of the Modification Agreement. This provision, however, conflicts with Defendants' promises that (1) it would send Chavez a signed copy of the Modification Agreement once she signed and returned two copies of the Modification Agreement to Defendants and (2) "the Loan Documents [would] automatically become modified on 7/1/2010" if Chavez's representations continued to be true and all preconditions to modifications have been satisfied.

Under Defendants' proposed reading of the Modification Agreement, Chavez could do everything required of her to be entitled to a permanent modification, but Defendants could avoid the contract by refusing to send Chavez a signed copy of the Modification Agreement for any reason whatsoever. We reject this interpretation as we must determine the objective intent of the parties based on reading the Modification Agreement as a whole. (Civ. Code, § 1641 ["The whole of a contract is to be taken together, so as to give effect to every part, if reasonably practicable, each clause helping to interpret the other."].) Here, the language of the Trial Period Plan and the Modification Agreement taken together suggest Defendants concluded that Chavez qualified for a permanent modification when it sent her the Modification Agreement, and assuming Chavez's representations continued to be true and all preconditions to modifications have been satisfied, that Chavez's original loan documents would automatically be modified on the date stated in the Modification Agreement. (Civ. Code,

§ 1642 ["Several contracts relating to the same matters, between the same parties, and made as parts of substantially one transaction, are to be taken together."].)

Chavez alleges that after Defendants sent her the Modification Agreement, she timely returned the signed agreement and fully complied with the terms of the Modification Agreement, including making the payments required under it. Defendants accepted Chavez's payments for several months until it returned her check with a letter stating that it did not accept personal checks and payments had to be certified. The Trial Period Plan and the Modification Agreement, however, do not contain a clause requiring that payments be certified. Thereafter, Defendants sold Chavez's home by foreclosure without notice and ultimately forced her to move after serving her with an unlawful detainer summons and complaint.

Liberally construed, the complaint sufficiently alleged facts supporting a claim that Defendants should be equitably estopped to rely on the statute of frauds defense. First, Defendants provided the Modification Agreement which is ambiguous at best and illusory at worse. (*Victoria v. Superior Court* (1985) 40 Cal.3d 734, 739 [ambiguity in a standard form contract is generally resolved against the drafter].) The words of the Modification Agreement and Defendants' conduct after Chavez sent Defendants a signed copy of the agreement suggest Defendants intended to stand by the agreement. Defendants' conduct, combined with the language of the Modification Agreement that Chavez's original loan documents would "automatically" be modified on a date certain could be construed as an implied representation that the statute of frauds would not be relied upon.

The question whether Chavez adequately pleaded facts to allege equitable estoppel to rely on the statute of frauds defense is a close one. In *Secrest*, the appellate court found that a homeowner's mere payment of money, a down payment in reliance on a forbearance agreement not signed by the party to be charged, was insufficient to raise an estoppel to assert the statute of frauds defense. (*Secrest*, *supra*, 167 Cal.App.4th at pp. 548, 557.) Defendants rely on *Secrest* to argue that Chavez did not sufficiently allege an estoppel because she merely made payments she was already obligated to make under the Trial Period Plan.

In deciding this issue, however, we must look at the Trial Period Plan and the Modification Agreement together. As we discussed, Defendants' conduct of sending Chavez the Modification Agreement, even though they had not sent her a signed copy of the Trial Period Plan suggests Defendants concluded that Chavez qualified for a permanent loan modification. Chavez then detrimentally changed her position by completing and signing the Modification Agreement. The Modification Agreement provided that Chavez agreed that unpaid and deferred interest, fees, escrow advances and other costs would be added to the outstanding principal balance and would accrue interest and that interest would accrue on the unpaid interest "which would not happen without this Agreement." Thus, Chavez incurred additional costs and fees in excess of the amounts she had been obligated to pay under her original loan agreement or the Trial Period Plan. This detrimental change in position is sufficient to allege that Defendants should be estopped from asserting the statute of frauds.

Although Chavez has not alleged that Defendants were unjustly enriched, discovery may show unjust enrichment. (See generally, Diane E. Thompson, *Foreclosing Modifications: How Servicer Incentives Discourage Loan Modifications* (2011) 86 Wash. L.Rev. 755, 777 [Noting that servicers can make more money from foreclosing than from modifying and "the true sweet spot lies in stretching out a delinquency without either a modification or a foreclosure."].) Additionally, we are at the pleading stage and discovery may reveal that Defendants signed the Modification Agreement or sent the Modification Agreement with a cover letter that contained a stamped or typewritten name that qualifies as the necessary signature. (*Marks v. Walter G. McCarty Corp.*, *supra*, 33 Cal.2d at p. 820 [signature of the party to be charged need not be at end of writing and be placed at the end of the writing relied upon if a proper signature be found may be printed, stamped or typewritten].)

Finally, we note that Chavez argues the Modification Agreement is not subject to the statute of frauds because it does not modify the loan documents. In making this argument, Chavez cites to a portion of the Trial Period Plan, which provided: "I understand that this Plan is not a modification of the Loan Documents. . . ." While Chavez is correct that the Trial Period Plan did not modify her original loan documents and thus would not be subject to the statute of frauds, she has not alleged a breach of the Trial Period Plan. We express no opinion on whether Chavez can allege a valid claim for breach of the Trial Period Plan. We leave this issue to the trial court should Chavez seek leave to amend to add such a claim.

B. Wrongful Foreclosure

To obtain the equitable set aside of a trustee's sale or maintain a wrongful foreclosure claim, a plaintiff must allege that (1) defendants caused an illegal, fraudulent, or willfully oppressive sale of the property pursuant to a power of sale in a mortgage or deed of trust; (2) plaintiff suffered prejudice or harm; and (3) plaintiff tendered the amount of the secured indebtedness or were excused from tendering. (*Lona v. Citibank, N.A.* (2011) 202 Cal.App.4th 89, 112 (*Lona*).) Recognized exceptions to the tender rule include when: (1) the underlying debt is void, (2) the foreclosure sale or trustee's deed is void on its face, (3) a counterclaim offsets the amount due, (4) specific circumstances make it inequitable to enforce the debt against the party challenging the sale, or (5) the foreclosure sale has not yet occurred. (*Id.* at pp. 112-113 [outlining the first four exceptions]; *Pfeifer v. Countrywide Home Loans, Inc.* (2012) 211 Cal.App.4th 1250, 1280-1281 [recognizing the fifth exception].)

The trial Court sustained Defendants' demurrer to this claim finding that to the extent it was based on breach of the Modification Agreement, the claim failed because the Modification Agreement did not comply with the statute of frauds, and to the extent the claim was based on Defendants' failure to serve the requisite notices, Chavez did not plead that she could tender the indebtedness. Chavez argues that she alleged a valid claim for breach of the Modification Agreement and she was not required to allege tender. We agree.

As discussed above, Chavez properly alleged a cause of action for breach of the Modification Agreement. Under the terms of the Modification Agreement, all late charges were waived and the modified principal balance included any past due amounts and arrearages. Chavez alleged the existence of an enforceable agreement to modify her loan and the payment of all sums due under that agreement until Defendants allegedly breached the agreement by failing to accept her payment. Chavez sufficiently alleged an exception to the tender rule that the foreclosure sale was void because Defendants lacked a contractual basis to exercise the power of sale as Chavez's original loan had been modified under the Modification Agreement and Chavez fully performed under the Modification Agreement until Defendants breached the agreement by refusing payment. (*Bank of America, N.A. v. La Jolla Group II* (2005) 129 Cal.App.4th 706, 710, 711-712 [trustee's sale invalid where "the trustor and beneficiary entered into an agreement to cure the default"]; *Bisno v. Sax* (1959) 175 Cal.App.2d 714, 724 ["Speaking generally, the acceptance of payment of a delinquent installment of principal or interest cures that particular default and precludes a foreclosure sale based upon such preexisting delinquency. The same is true of a tender which has been made and rejected."].) Because Chavez sufficiently alleged a recognized exception to the tender rule, the trial court erred by sustaining the demurrer to her wrongful foreclosure cause of action.

Chavez also alleged improper notice of the trustee's sale, thereby making the sale voidable and subject to the tender requirement. (*Lona*, *supra*, 202 Cal.App.4th at p. 112 ["[A]s a condition precedent to an action by the borrower to set aside the trustee's sale on the ground that the sale is voidable because of irregularities in the sale notice or procedure, the borrower must offer to pay the full amount of the debt for which the property was security."].) This additional allegation, however, does not invalidate the remainder of this properly pled cause of action. (*Financial Corp. of America v. Wilburn*, *supra*, 189 Cal.App.3d at p. 778 [a general demurrer does not lie to only part of a cause of action].)

C. Promissory Estoppel

Promissory estoppel is an equitable doctrine that allows enforcement of a promise that would otherwise be unenforceable based on lack of consideration. (*US Ecology, Inc. v. State of California* (2005) 129 Cal.App.4th 887, 901-902.) Chavez contends the trial court erred in not allowing her leave to amend to add a cause of action for promissory estoppel because she reasonably relied on the promises in the Modification Agreement to her detriment by not seeking help elsewhere to save her home. We need not address this issue as we concluded Chavez alleged a valid claim for breach of the Modification Agreement. Nonetheless, we note that Chavez's proposed allegation that she did not seek help elsewhere to save her home provides additional detrimental reliance supporting Chavez's claim that Defendants should be equitably estopped to rely on the statute of frauds defense.

Nothing in this opinion prohibits Chavez from seeking leave to amend to add new allegations, assert alternative theories of recovery or add new theories of liability.

DISPOSITION

The judgment is reversed. Plaintiff is entitled to recover her costs on appeal.

McINTYRE, J.

WE CONCUR:

NARES, Acting P. J.

McDONALD, J.

FILED
United States Court of Appeals
Tenth Circuit

September 11, 2012

Elisabeth A. Shumaker
Clerk of Court

UNITED STATES COURT OF APPEALS

TENTH CIRCUIT

UNITED STATES OF AMERICA, Plaintiff-Counter-Defendant - Appellee, v. MARVIN M. BRANDT, Trustee of the Marvin M. Brandt Revocable Trust, MARVIN M. BRANDT REVOCABLE TRUST, Defendants-Counter-Claimants - Appellants, and DANIEL K. MCNIERNEY, SUSAN MCNIERNEY; GINNY L OTTERSTEIN; LAWRENCE R OTTERSTEIN; NORMA J. BREAZEALE, Defendants-Counter-Claimants, and WYOMING AND COLORADO RAILROAD COMPANY, INC.; GARY WILLIAMS; JOAN WILLIAMS; GLENNA MARRS; KENNETH R. LANKFORD, II; KENNETH R. LANKFORD, SR.; PATRICK R RINKER; PATRICIA A. RINKER; RONDAL WAYNE; EDMUND L GRUBER; KATHLYNN A. LAMBERT; DAVID M. PEARCE;	No. 09-8047 (D.C. No. 2:06-CV-00184-ABJ) (D. Wyo.)

DOROTHY M. PEARCE; ROBERT S. PEARCE; STEVEN M. PEARCE; TOBIN L. RATLIFF; LYNDA L. RINKER; PATRICK R RINKER; JANIS A. TAFFEE; STEVEN P. TAFFEE,

Defendants.

RAILS TO TRAILS CONSERVANCY,

Amicus Curiae.

ORDER AND JUDGMENT*

Before **KELLY**, **O'BRIEN**, and **HOLMES**, Circuit Judges.

The Marvin M. Brandt Revocable Trust and Mr. Brandt, Trustee, appeal from the district court's judgment quieting title in the United States to certain property that crosses the trust's property. United States v. Marvin M. Brandt Revocable Trust, 2008 WL 7185272 (D. Wyo. 2008). The parties are familiar with the facts and we need not restate them here. Suffice it to say that the subject property is part of an abandoned right-of-way granted a railroad pursuant to the

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* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. It may be cited, however, for its persuasive value consistent with Fed. R. App. P. 32.1 and 10th Cir. R. 32.1.

General Railroad Right-of-Way Act of 1875, 43 U.S.C. § 934 ("1875 Act") and a nearby government road, Forest Service Road 512.

A. The Railroad Right-of-Way

The trust argues that the 1908 right-of-way granted to the railroad (pursuant to the 1875 Act) is like an ordinary easement that has been extinguished. It reasons as follows. The 1976 patent issued to the trust's predecessors-in-interest did not reserve to the United States any interest in this easement; it merely provided that the property was subject to the easement for railroad purposes.[1]

[1] The pertinent portions provide:

> EXCEPTING AND RESERVING TO THE UNITED STATES from the land granted a right-of-way thereon for ditches or canals constructed by the authority of the United States; and
>
> RESERVING TO the United States, and its assigns, a right-of-way for the existing Platte Access Road No. 512 over and across Tract No. 37 . . . containing 3.30 acres, more or less; and
>
> RESERVING TO the United States, and its assigns, a right-of-way for the existing Dry Park Road No. 517, over and across Tract 37 . . . containing 0.71 acres, more or less.
>
> Provided, that if for a period of five years, the United States, or its assigns, shall cease to use the above roads, or any segment thereof, for the purposes reserved, or if at any time the Regional Forester determines that the roads, or any segment thereof, is no longer needed for the purposes reserved, the easement traversed thereby shall terminate. In the event of such nonuse or such determination by the Regional Forester, the Regional Forester shall furnish to the patentees or, their heirs or assigns, a statement in recordable form evidencing termination.

Thus, when the railroad administratively abandoned the easement (by notifying the Surface Transportation Board ("STB") on January 15, 2004 that it would exercise its authority to abandon the line), the easement was extinguished and the trust's property was disencumbered. Because the United States lacked any ownership interest (as of October 4, 1988) in the right-of-way, it could not claim through 16 U.S.C. § 1248(c) which generally provides that the United States retains rights in abandoned or forfeited railroad grants. Nor could the United States claim through 43 U.S.C. § 912, which generally provided that the interest in the right-of-way went to the adjacent landowner given abandonment decreed by a court of competent jurisdiction or an Act of Congress. The trust argues that the district court should have quieted title in it, not the United States.

Much of the trust's argument is foreclosed by circuit precedent which we are bound to follow. See United States v. Spedalieri, 910 F.2d 707, 709 n.2, 710 n.3 (10th Cir. 1990). In Marshall v. Chicago & Northwestern Transportation Co., 31 F.3d 1028, 1030–32 (10th Cir. 1994), we held that § 912 applies to grants under the 1875 Act. Relying upon Idaho v. Oregon Short Line R.R., 617 F. Supp. 207 (D. Idaho 1985), we concluded that the United States retained an implied

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> SUBJECT TO those rights for railroad purposes as have been granted to the Laramie Hahn's Peak & Pacific Railway Company, its successors or assigns by permit Cheyenne 04128 under the Act of March 3, 1875, 43 U.S.C. 934–939.

Aplt. App. 92–93.

reversionary interest. Marshall, 31 F.3d at 1032. We subsequently applied § 912 on the issue of whether a railroad had abandoned its right-of-way such that adjacent landowners would take in Phillips Co. v. Denver & Rio Grande Western R.R., 97 F.3d 1375 (10th Cir. 1996). And we have recognized that § 912 was modified by 16 U.S.C. § 1248(c) to provide that, as of October 4, 1988, interests in abandoned railroad rights-of-way generally revert to the United States rather than adjacent landowners. See Nicodemus v. Union Pac. Corp., 440 F.3d 1227, 1236 n.9 (10th Cir. 2006); Phillips, 97 F.3d at 1376 n.4. We are unpersuaded by the remainder of the trust's other arguments and efforts to distinguish and limit the obvious contrary precedent. Though we recognize that the Seventh Circuit, the Federal Circuit and the Court of Federal Claims have concluded that the United States did not retain any reversionary interest in these railroad rights-of-way, we are bound by our precedent. See Samuel C. Johnson 1988 Tr. v. Bayfield County, 649 F.3d 799, 803–04 (7th Cir. 2011); Hash v. United States, 403 F.3d 1308, 1317 (Fed. Cir. 2005); Beres v. United States, 64 Fed. Cl. 403, 427–28 (2005). But see Darwin P. Roberts, The Legal History of Federally Granted Railroad Rights-of-Way and the Myth of Congress's "1871 Shift", 82 U. Colo. L. Rev. 85, 150–64 (2011) (criticizing this interpretation). Thus, the district court correctly held that the interest in the abandoned railroad right-of-way belongs to the United States.

B. Forest Service Road 512

The trust argues that the 1976 patent reserved a certain right-of-way in Road 512 and provided that it would terminate if the United States ceased to use the road or any segment. See supra n.1. The trust argues that it made a conclusive showing that an obliterated segment of the Road 512 easement had not been used for five years and therefore, title should have been quieted in the trust, not the United States. Aplt. Br. 48; Aplt. Reply Br. 25. The trust relies upon the following: (1) the Forest Service published a decision memorandum closing and obliterating a portion of the road and removed the road surface, leveled the area, and planted grass on a smaller portion, and (2) Mr. Brandt declared that, to the best of his knowledge, the Forest Service had not used any part of the easement for five years and took issue with certain statements of Forest Service personnel about some of the claimed use. Aplt. App. 101; Aplee. Supp. App. 1–2. The trust argues that the United States failed to present any evidence that the obliterated portion had been used, and therefore the entire Road 512 easement terminated.

The district court considered the trust's argument that non-use of Road 512 terminated the easements for Roads 512 and 517. Marvin M. Brandt Revocable Trust, 2008 WL 7185272 at *16 & *17–18. That is precisely the argument the trust made in response to the United States' motion for summary judgment. 2:06-cv-00184-ABJ, ECF Doc. 147 at 25–26. In its own motion for summary judgment, the trust argued, consistent with its counterclaim, that non-use of Road 512 terminated the easement for only Road 512. Aplt. App. 72;

2:06-cv-00184-ABJ, ECF Doc. 140 at 22–23.

The district court held that the trust could not create a genuine issue of material fact as to non-use of Road 512 based upon Mr. Brandt's affidavit that the Forest Service did not use the closed portion of Road 512. Marvin M. Brandt Revocable Trust, 2008 WL 7185272 at *17–18. The trust admits that Road 512 has been used as a private road and Mr. Brandt allows the Forest Service, law enforcement, and emergency personnel to enter through a gate at the south end. Aplt. App. 71; Aplee. Supp. App. 2; Aplt. Reply Br. 24–25. Instead, the trust argues that the evidence submitted by the United States, Aplt. App. 151–56, listing over 30 incidents of use simply does not establish that the obliterated segment of Road 512 was used from 1996–2003.

Even assuming that the trust could create a genuine issue of material fact as to use of the obliterated portion of Road 512,[2] we would reject the contention that non-use of part of the road is sufficient to terminate the entire easement, be it Road 512 or Road 517, or both. The meaning of "the easement traversed thereby," which defines what terminates upon non-use, is the operative language. So as to give effect to all of the terms, "the easement traversed thereby" refers

[2] We reject the trust's contention that the United States failed to provide any evidence of use of the obliterated portion. See Aplt. App. 151–56; Aplee. Supp. App. 8–11. Such a conclusion would be particularly anomalous given summary judgment standards which require that the evidence be viewed in the light most favorable to the non-movant. Ricci v. DeStefano, 557 U.S. 557, 586 (2009).

back to non-use of “the above roads [Road 512 or 517], <u>or</u> “any segment thereof.” The trust’s reading essentially eliminates “any segment thereof.” Moreover, the language refers to easement in the singular which is completely at odds with the argument the district court considered: that non-use of one of the roads, or a segment thereof, results in termination of both easements, no matter the use being made of each. We note that the trust did not contend (either in its counterclaim or in the briefing) that non-use of a segment of Road 512 results in the termination of the easement in that segment, and we do not address it. <u>See</u> <u>Somerlott v. Cherokee Nation Distribs. Inc.</u>, 686 F.3d 1144, 1151–52 (10th Cir. 2012).

AFFIRMED.

Entered for the Court

Per Curiam

09-8047 *United States v. Brandt*

O'BRIEN, J. concurring.

I join the Order and Judgment. I write separately for a collateral reason. After oral argument I was designated as author. Recently, because he was concerned with the delay in disposition, Judge Kelly reassigned the case and prepared the Order and Judgment. I am solely responsible for, and deeply regret, all delay in resolving this matter.

Filed 7/31/13; pub. order 8/8/13 (see end of opn.)

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIFTH APPELLATE DISTRICT

THOMAS A. GLASKI,

Plaintiff and Appellant,

v.

BANK OF AMERICA, NATIONAL ASSOCIATION et al.

Defendants and Respondents.

F064556

(Super. Ct. No. 09CECG03601)

OPINION

APPEAL from a judgment of the Superior Court of Fresno County. Alan M. Simpson, Judge.

Law Offices of Richard L. Antognini and Richard L. Antognini; Law Offices of Catarina M. Benitez and Catarina M. Benitez, for Plaintiff and Appellant.

AlvaradoSmith, Theodore E. Bacon, and Mikel A. Glavinovich, for Defendants and Respondents.

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INTRODUCTION

Before Washington Mutual Bank, FA (WaMu) was seized by federal banking regulators in 2008, it made many residential real estate loans and used those loans as collateral for mortgage-backed securities.[1] Many of the loans went into default, which led to nonjudicial foreclosure proceedings. Some of the foreclosures generated lawsuits, which raised a wide variety of claims. The allegations that the instant case shares with some of the other lawsuits are that (1) documents related to the foreclosure contained forged signatures of Deborah Brignac and (2) the foreclosing entity was not the true owner of the loan because its chain of ownership had been broken by a defective transfer of the loan to the securitized trust established for the mortgage-backed securities. Here, the specific defect alleged is that the attempted transfers were made *after the closing date* of the securitized trust holding the pooled mortgages and therefore the transfers were ineffective.

In this appeal, the borrower contends the trial court erred by sustaining defendants' demurrer as to all of his causes of action attacking the nonjudicial foreclosure. We conclude that, although the borrower's allegations are somewhat confusing and may contain contradictions, he nonetheless has stated a wrongful

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[1] Mortgage-backed securities are created through a complex process known as "securization." (See Levitin & Twomey, *Mortgage Servicing* (2011) 28 Yale J. on Reg. 1, 13 ["a mortgage securitization transaction is extremely complex"].) In simplified terms, "securitization" is the process where (1) many loans are bundled together and transferred to a passive entity, such as a trust, and (2) the trust holds the loans and issues investment securities that are repaid from the mortgage payments made on the loans. (Oppenheim & Trask-Rahn, *Deconstructing the Black Magic of Securitized Trusts: How the Mortgage-Backed Securitization Process is Hurting the Banking Industry's Ability to Foreclose and Proving the Best Offense for a Foreclosure Defense* (2012) 41 Stetson L.Rev. 745, 753-754 (hereinafter, *Deconstructing Securitized Trusts*).) Hence, the securities issued by the trust are "mortgage-backed." For purposes of this opinion, we will refer to such a trust as a "securitized trust."

foreclosure claim under the lenient standards applied to demurrers. We conclude that a borrower may challenge the securitized trust's chain of ownership by alleging the attempts to transfer the deed of trust to the securitized trust (which was formed under New York law) occurred after the trust's closing date. Transfers that violate the terms of the trust instrument are void under New York trust law, and borrowers have standing to challenge void assignments of their loans even though they are not a party to, or a third party beneficiary of, the assignment agreement.

We therefore reverse the judgment of dismissal and remand for further proceedings.

FACTS

<u>The Loan</u>

Thomas A. Glaski, a resident of Fresno County, is the plaintiff and appellant in this lawsuit. The operative second amended complaint (SAC) alleges the following: In July 2005, Glaski purchased a home in Fresno for $812,000 (the Property). To finance the purchase, Glaski obtained a $650,000 loan from WaMu. Initial monthly payments were approximately $1,700. Glaski executed a promissory note and a deed of trust that granted WaMu a security interest in the Property (the Glaski deed of trust). Both documents were dated July 6, 2005. The Glaski deed of trust identified WaMu as the lender and the beneficiary, defendant California Reconveyance Company (California Reconveyance) as the trustee, and Glaski as the borrower.

Paragraph 20 of the Glaski deed of trust contained the traditional terms of a deed of trust and states that the note, together with the deed of trust, can be sold one or more times without prior notice to the borrower. In this case, a number of transfers purportedly occurred. The validity of attempts to transfer Glaski's note and deed of trust to a securitized trust is a fundamental issue in this appeal.

Paragraph 22—another provision typical of deeds of trust—sets forth the remedies available to the lender in the event of a default. Those remedies include (1) the lender's right to accelerate the debt after notice to the borrower and (2) the lender's right to "invoke the power of sale" after the borrower has been given written notice of default and of the lender's election to cause the property to be sold. Thus, under the Glaski deed of trust, it is the lender-beneficiary who decides whether to pursue nonjudicial foreclosure in the event of an uncured default by the borrower. The trustee implements the lender-beneficiary's decision by conducting the nonjudicial foreclosure.[2]

Glaski's loan had an adjustable interest rate, which caused his monthly loan payment to increase to $1,900 in August 2006 and to $2,100 in August 2007. In August 2008, Glaski attempted to work with WaMu's loan modification department to obtain a modification of the loan. There is no dispute that Glaski defaulted on the loan by failing to make the monthly installment payments.

<u>Creation of the WaMu Securitized Trust</u>

In late 2005, the WaMu Mortgage Pass-Through Certificates Series 2005-AR17 Trust was formed as a common law trust (WaMu Securitized Trust) under New York law. The corpus of the trust consists of a pool of residential mortgage notes purportedly secured by liens on residential real estate. La Salle Bank, N.A., was the original trustee for the WaMu Securitized Trust.[3] Glaski alleges that the WaMu Securitized Trust has no

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[2] Civil Code section 2924, subdivision (a)(1) states that a "trustee, mortgagee, or beneficiary, or any of their authorized agents" may initiate the nonjudicial foreclosure process. This statute and the provision of the Glaski deed of trust are the basis for Glaski's position that the nonjudicial foreclosure in this case was *wrongful*—namely, that the power of sale in the Glaski deed of trust was invoked by an entity that was not the true beneficiary.

[3] Glaski's pleading does not allege that LaSalle Bank was the original trustee when the WaMu Securitized Trust was formed in late 2005, but filings with the Securities and Exchange Commission identify LaSalle Bank as the original trustee. We provide this

continuing duties other than to hold assets and to issue various series of certificates of investment. A description of the certificates of investment as well as the categories of mortgage loans is included in the prospectus filed with the Securities and Exchange Commission (SEC) on October 21, 2005. Glaski alleges that the investment certificates issued by the WaMu Securitized Trust were duly registered with the SEC.

The closing date for the WaMu Securitized Trust was December 21, 2005, or 90 days thereafter. Glaski alleges that the attempt to assign his note and deed of trust to the WaMu Securitized Trust was made after the closing date and, therefore, the assignment was ineffective. (See fn. 12, *post*.)

WaMu's Failure and Transfers of the Loan

In September 2008, WaMu was seized by the Office of Thrift Supervision and the Federal Deposit Insurance Corporation (FDIC) was appointed as a receiver for WaMu. That same day, the FDIC, in its capacity as receiver, sold the assets and liabilities of WaMu to defendant JPMorgan Chase Bank, N.A., (JP Morgan). This transaction was documented by a "PURCHASE AND ASSUMPTION AGREEMENT WHOLE BANK" (boldface and underlining omitted) between the FDIC and JP Morgan dated as of September 25, 2008. If Glaski's loan was not validly transferred to the WaMu Securitized Trust, it is possible, though not certain, that JP Morgan acquired the Glaski deed of trust when it purchased WaMu assets from the FDIC.[4] JP Morgan also might have acquired the right to service the loans held by the WaMu Securitized Trust.

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information for background purposes only and it plays no role in our decision in this appeal.

4 Another possibility, which was acknowledged by both sides at oral argument, is that the true holder of the note and deed of trust cannot be determined at this stage of the proceedings. This lack of certainty regarding who holds the deed of trust is not uncommon when a securitized trust is involved. (See Mortgage and Asset Backed Securities Litigation Handbook (2012) § 5:114 [often difficult for securitized trust to

In September 2008, Glaski spoke to a representative of defendant Chase Home Finance LLC (Chase),[5] which he believed was an agent of JP Morgan, and made an oral agreement to start the loan modification process. Glaski believed that Chase had taken over loan modification negotiations from WaMu.

On December 9, 2008, two documents related to the Glaski deed of trust were recorded with the Fresno County Recorder: (1) an "ASSIGNMENT OF DEED OF TRUST" and (2) a "NOTICE OF DEFAULT AND ELECTION TO SELL UNDER DEED OF TRUST" (boldface omitted; hereinafter the NOD). The assignment stated that JP Morgan transferred and assigned all beneficial interest under the Glaski deed of trust to "LaSalle Bank NA as trustee for WaMu [Securitized Trust]" together with the note described in and secured by the Glaski deed of trust.[6]

Notice of Default and Sale of the Property

The NOD informed Glaski that (1) the Property was in foreclosure because he was behind in his payments[7] and (2) the Property could be sold without any court action.

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prove ownership by showing a chain of assignments of the loan from the originating lender].)

[5] It appears this company is no longer a separate entity. The certificate of interested entities filed with the respondents' brief refers to "JPMorgan Chase Bank, N.A. as successor by merger to Chase Home Finance, LLC."

[6] One controversy presented by this appeal is whether this court should consider the December 9, 2008, assignment of deed of trust, which is not an exhibit to the SAC. Because the trial court took judicial notice of the existence and recordation of the assignment earlier in the litigation, we too will consider the assignment, but will not presume the matters stated therein are true. (See pt. IV.B, *post*.) For instance, we will not assume that JP Morgan actually held any interests that it could assign to LaSalle Bank. (See *Herrera v. Deutsche Bank National Trust Co.* (2011) 196 Cal.App.4th 1366, 1375 [taking judicial notice of a recorded assignment does not establish assignee's ownership of deed of trust].)

[7] Specifically, the notice stated that his August 2008 installment payment and all subsequent installment payments had not been made.

The NOD also stated that "the present beneficiary under" the Glaski deed of trust had delivered to the trustee a written declaration and demand for sale. According to the NOD, all sums secured by the deed of trust had been declared immediately due and payable and that the beneficiary elected to cause the Property to be sold to satisfy that obligation.

The NOD stated the amount of past due payments was $11,200.78 as of December 8, 2008.[8] It also stated: "To find out the amount you must pay, or to arrange for payment to stop the foreclosure, … contact: JPMorgan Chase Bank, National Association, at 7301 BAYMEADOWS WAY, JACKSONVILLE, FL 32256, (877) 926-8937."

Approximately three months after the NOD was recorded and served, the next official step in the nonjudicial foreclosure process occurred. On March 12, 2009, a "NOTICE OF TRUSTEE'S SALE" was recorded by the Fresno County Recorder (notice of sale). The sale was scheduled for April 1, 2009. The notice stated that Glaski was in default under his deed of trust and estimated the amount owed at $734,115.10.

The notice of sale indicated it was signed on March 10, 2009, by Deborah Brignac, as Vice President for *California Reconveyance*. Glaski alleges that Brignac's signature was forged to effectuate a fraudulent foreclosure and trustee's sale of his primary residence.

Glaski alleges that from March until May 2009, he was led to believe by his negotiations with Chase that a loan modification was in process with JP Morgan.

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[8] The signature block at the end of the NOD indicated it was signed by Colleen Irby as assistant secretary for California Reconveyance. The first page of the notice stated that recording was requested by California Reconveyance. Affidavits of mailing attached to the SAC stated that the declarant mailed copies of the notice of default to Glaski at his home address and to Bank of America, care of Custom Recording Solutions, at an address in Santa Ana, California. The affidavits of mailing are the earliest documents in the appellate record indicating that Bank of America had any involvement with Glaski's loan.

Despite these negotiations, a nonjudicial foreclosure sale of the Property was conducted on May 27, 2009. Bank of America, as successor trustee for the WaMu Securitized Trust and beneficiary under the Glaski deed of trust, was the highest bidder at the sale.

On June 15, 2009, another "ASSIGNMENT OF DEED OF TRUST" was recorded with the Fresno County Recorder. This assignment, like the assignment recorded in December 2008, identified JP Morgan as the assigning party. The entity receiving all beneficial interest under the Glaski deed of trust was identified as Bank of America, "as successor by merger to 'LaSalle Bank NA as trustee for WaMu [Securitized Trust] .…"[9] The assignment of deed of trust indicates it was signed by Brignac, as *Vice President for JP Morgan*. Glaski alleges that Brignac's signature was forged.

The very next document filed by the Fresno County Recorder on June 15, 2009, was a "TRUSTEE'S DEED UPON SALE." (Boldface omitted.) The trustee's deed upon sale stated that California Reconveyance, as the duly appointed trustee under the Glaski deed of trust, granted and conveyed to Bank of America, as successor by merger to La Salle NA as trustee for the WaMu Securitized Trust, all of its right, title and interest to the Property. The trustee's deed upon sale stated that the amount of the unpaid debt and costs was $738,238.04 and that the grantee, paid $339,150 at the trustee's sale, either in lawful money or by credit bid.

PROCEEDINGS

In October 2009, Glaski filed his original complaint. In August 2011, Glaski filed the SAC, which alleged the following numbered causes of action:

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[9] Bank of America took over La Salle Bank by merger in 2007.

(1) Fraud against JPMorgan and California Reconveyance for the alleged forged signatures of Deborah Brignac as vice president for California Reconveyance and then as vice president of JPMorgan;

(2) Fraud against all defendants for their failure to timely and properly transfer the Glaski loan to the WaMu Securitized Trust and their representations to the contrary;

(3) Quiet title against Bank of America, Chase, and California Reconveyance based on the broken chain of title caused by the defective transfer of the loan to the WaMu Securitized Trust;

(4) Wrongful foreclosure against all defendants, based on the forged signatures of Deborah Brignac and the failure to timely and properly transfer the Glaski loan to the WaMu Securitized Trust;

(5) Declaratory relief against all defendants, based on the above acts by defendants;

(8) Cancellation of various foreclosure documents against all defendants, based on the above acts by the defendants; and

(9) Unfair practices under California Business and Professions Code section 17200, et seq., against all defendants.

Among other things, Glaski raised questions regarding the chain of ownership, by contending that the defendants were not the lender or beneficiary under his deed of trust and, therefore, did not have the authority to foreclose.

In September 2011, defendants filed a demurrer that challenged each cause of action in the SAC on the grounds that it failed to state facts sufficient to constitute a claim for relief. With respect to the wrongful foreclosure cause of action, defendants argued that Glaski failed to allege (1) any procedural irregularity that would justify setting aside the presumptively valid trustee's sale and (2) that he could tender the amount owed if the trustee's sale were set aside.

To support their demurrer to the SAC, defendants filed a request for judicial notice concerning (1) Order No. 2008-36 of the Office of Thrift Supervision, dated September 25, 2008, appointing the FDIC as receiver of Washington Mutual Bank and (2) the Purchase and Assumption Agreement Whole Bank between the FDIC and JP Morgan dated as of September 25, 2008, concerning the assets, deposits and liabilities of Washington Mutual Bank.[10]

Glaski opposed the demurrer, arguing that breaks in the chain of ownership of his deed of trust were sufficiently alleged. He asserted that Brignac's signature was forged and the assignment bearing that forgery was void. His opposition also provided a more detailed explanation of his argument that his deed of trust had not been effectively transferred to the WaMu Securitized Trust that held the pool of mortgage loans. Thus, in Glaski's view, Bank of America's claim as the successor trustee is flawed because the trust never held his loan.

On November 15, 2011, the trial court heard argument from counsel regarding the demurrer. Counsel for Glaski argued, among other things, that the possible ratification of the allegedly forged signatures of Brignac presented an issue of fact that could not be resolved at the pleading stage.

Later that day, the court filed a minute order adopting its tentative ruling. As background for the issues presented in this appeal, we will describe the trial court's ruling on Glaski's two fraud causes of action and his wrongful foreclosure cause of action.

The ruling stated that the first cause of action for fraud was based on an allegation that defendants misrepresented material information by causing a forged signature to be

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[10] The trial court did not explicitly rule on defendants' request for judicial notice of these documents, but referred to matters set forth in these documents in its ruling. Therefore, for purposes of this appeal, we will infer that the trial court granted the request.

placed on the June 2009 assignment of deed of trust. The ruling stated that if the signature of Brignac was forged, California Reconveyance "ratified the signature by treating it as valid." As an additional rationale, the ruling cited *Gomes v. Countrywide Home Loans, Inc.* (2011) 192 Cal.App.4th 1149 (*Gomes*) for the proposition that the exhaustive nature of California's nonjudicial foreclosure scheme prohibited the introduction of additional requirements challenging the authority of the lender's nominee to initiate nonjudicial foreclosure.

As to the second cause of action for fraud, the ruling noted the allegation that the Glaski deed of trust was transferred to the WaMu Securitized Trust after the trust's closing date and summarized the claim as asserting that the Glaski deed of trust had been improperly transferred and, therefore, the assignment was void *ab initio*. The ruling rejected this claim, stating: "[T]o reiterate, *Gomes v. Countrywide,* supra holds that there is no legal basis to challenge the authority of the trustee, mortgagee, beneficiary, or any of their authorized agents to initiate the foreclosure process citing Civil Code § 2924, subd. (a)(1)."

The ruling stated that the fourth cause of action for wrongful foreclosure was "based upon the invalidity of the foreclosure sale conducted on May 27, 2009 due to the 'forged' signature of Deborah Brignac and the failure of Defendants to 'provide a chain of title of the note and the mortgage.'" The ruling stated that, as explained earlier, "these contentions are meritless" and sustained the general demurrer to the wrongful foreclosure claim without leave to amend.

Subsequently, a judgment of dismissal was entered and Glaski filed a notice of appeal.

DISCUSSION

I. STANDARD OF REVIEW

The trial court sustained the demurrer to the SAC on the ground that it did "not state facts sufficient to constitute a cause of action." (Code Civ. Proc., § 430.10, subd. (e).) The standard of review applicable to such an order is well settled. "[W]e examine the complaint de novo to determine whether it alleges facts sufficient to state a cause of action under any legal theory …." (*McCall v. PacifiCare of Cal., Inc.* (2001) 25 Cal.4th 412, 415.)

When conducting this de novo review, "[w]e give the complaint a reasonable interpretation, reading it as a whole and its parts in their context. [Citation.] Further, we treat the demurrer as admitting all material facts properly pleaded, but do not assume the truth of contentions, deductions or conclusions of law. [Citations.]" (*City of Dinuba v. County of Tulare* (2007) 41 Cal.4th 859, 865.) Our consideration of the facts alleged includes "those evidentiary facts found in recitals of exhibits attached to a complaint." (*Satten v. Webb* (2002) 99 Cal.App.4th 365, 375.) "We also consider matters which may be judicially noticed." (*Serrano v. Priest* (1971) 5 Cal.3d 584, 591; see Code Civ. Proc., § 430.30, subd. (a) [use of judicial notice with demurrer].) Courts can take judicial notice of the existence, content and authenticity of public records and other specified documents, but do not take judicial notice of the truth of the factual matters asserted in those documents. (*Mangini v. R.J. Reynolds Tobacco Co.* (1994) 7 Cal.4th 1057, 1063, overruled on other grounds in *In re Tobacco Cases II* (2007) 41 Cal.4th 1257, 1262.)

We note "in passing upon the question of the sufficiency or insufficiency of a complaint to state a cause of action, it is wholly beyond the scope of the inquiry to ascertain whether the facts stated are true or untrue" as "[t]hat is always the ultimate question to be determined by the evidence upon a trial of the questions of fact." (*Colm v. Francis* (1916) 30 Cal.App. 742, 752.))

II. FRAUD

A. Rules for Pleading Fraud

The elements of a fraud cause of action are (1) misrepresentation, (2) knowledge of the falsity or scienter, (3) intent to defraud—that is, induce reliance, (4) justifiable reliance, and (5) resulting damages. (*Lazar v. Superior Court* (1996) 12 Cal.4th 631, 638.) These elements may not be pleaded in a general or conclusory fashion. (*Id*. at p. 645.) Fraud must be pled specifically—that is, a plaintiff must plead *facts* that show with particularity the elements of the cause of action. (*Ibid*.)

In their demurrer, defendants contended facts establishing detrimental reliance were not alleged.

B. First Cause of Action for Fraud, Lack of Specific Allegations of Reliance

Glaski's first cause of action, which alleges a fraud implemented through forged documents, alleges that defendants' act "caused Plaintiff to rely on the recorded documents and ultimately lose the property which served as his primary residence, and caused Plaintiff further damage, proof of which will be made at trial."

This allegation is a general allegation of reliance and damage. It does not identify the particular acts Glaski took because of the alleged forgeries. Similarly, it does not identify any acts that Glaski did not take because of his reliance on the alleged forgeries. Therefore, we conclude that Glaski's conclusory allegation of reliance is insufficient under the rules of law that require fraud to be pled specifically. (*Lazar v. Superior Court, supra*, 12 Cal.4th at p. 645.)

The next question is whether the trial court abused its discretion in sustaining the demurrer to the first fraud cause of action without leave to amend.

In March 2011, the trial court granted Glaski leave to amend when ruling on defendants' motion for judgment on the pleadings. The court indicated that Glaski's complaint had jumbled together many different statutes and theories of liability and directed Glaski to avoid "chain letter" allegations in his amended pleading.

Glaski's first amended complaint set forth two fraud causes of action that are similar to those included in the SAC.

Defendants demurred to the first amended complaint. The trial court's minute order states: "Plaintiff is advised **for the last time** to plead each cause of action such that only the essential **elements** for the claim are set forth without reincorporation of lengthy 'general allegations'. In other words, the 'facts' to be pleaded are those upon which liability depends (i.e., 'the facts constituting the cause of action')."

After Glaski filed his SAC, defendants filed a demurrer. Glaski then filed an opposition that asserted he had properly alleged detrimental reliance. He did not argue he could amend to allege specifically the action he took or did not take because of his reliance on the alleged forgeries.

Accordingly, Glaski failed to carry his burden of demonstrating he could allege with the requisite specificity the elements of justifiable reliance and damages resulting from that reliance. (See *Blank v. Kirwan* (1985) 39 Cal.3d 311, 318 [the burden of articulating how a defective pleading could be cured is squarely on the plaintiff].) Therefore, we conclude that the trial court did not abuse its discretion when it denied leave to amend as to the SAC's first cause of action for fraud.

C. Second Fraud Cause of Action, Lack of Specific Allegations of Reliance

Glaski's second cause of action for fraud alleged that WaMu failed to transfer his note and deed of trust into the WaMu Securitized Trust back in 2005. Glaski further alleged, in essence, that defendants attempted to rectify WaMu's failure by engaging in a fraudulent scheme to assign his note and deed of trust into the WaMu Securitized Trust. The scheme was implemented in 2008 and 2009 and its purpose was to enable defendants to fraudulently foreclosure against the Property.

The second cause of action for fraud attempts to allege detrimental reliance in the following sentence: "Defendants, and each of them, also knew that the act of recording the Assignment of Deed of trust without the authorization to do so would cause Plaintiff to rely **upon Defendants' actions** by attempting to negotiate a loan modification with representatives of Chase Home Finance, LLC, agents of JP MORGAN." The assignment mentioned in this allegation is the assignment of deed of trust recorded in June 2009—no other assignment of deed of trust is referred to in the second cause of action.

The allegation of reliance does not withstand scrutiny. The act of recording the allegedly fraudulent assignment occurred in June 2009, after the trustee's sale of the Property had been conducted. If Glaski was induced to negotiate a loan modification at that time, it is unclear how negotiations occurring after the May 2009 trustee's sale could have diverted him from stopping the trustee's sale. Thus, Glaski's allegation of reliance is not connected to any detriment or damage.

Because Glaski has not demonstrated how this defect in his fraud allegations could be cured by amendment, we conclude that the trial court did not abuse its discretion in denying leave to amend the second cause of action in the SAC.

III. WRONGFUL FORECLOSURE BY NONHOLDER OF THE DEED OF TRUST

A. Glaski's Theory of Wrongful Foreclosure

Glaski's theory that the foreclosure was wrongful is based on (1) the position that paragraph 22 of the Glaski deed of trust authorizes only the lender-beneficiary (or its assignee) to (a) accelerate the loan after a default and (b) elect to cause the Property to be sold and (2) the allegation that a nonholder of the deed of trust, rather than the true beneficiary, instructed California Reconveyance to initiate the foreclosure.[11]

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[11] The claim that a foreclosure was conducted by or at the direction of a nonholder of mortgage rights often arises where the mortgage has been securitized. (Buchwalter, *Cause of Action in Tort for Wrongful Foreclosure of Residential Mortgage*,

In particular, Glaski alleges that (1) the corpus of the WaMu Securitized Trust was a pool of residential mortgage notes purportedly secured by liens on residential real estate; (2) section 2.05 of "the Pooling and Servicing Agreement" required that all mortgage files transferred to the WaMu Securitized Trust be delivered to the trustee or initial custodian of the WaMu Securitized Trust before the closing date of the trust (which was allegedly set for December 21, 2005, or 90 days thereafter); (3) the trustee or initial custodian was required to identify all such records as being held by or on behalf of the WaMu Securitized Trust; (4) Glaski's note and loan were not transferred to the WaMu Securitized Trust prior to its closing date; (5) the assignment of the Glaski deed of trust did not occur by the closing date in December 2005; (6) the transfer to the trust attempted by the assignment of deed of trust recorded on June 15, 2009, occurred long after the trust was closed; and (7) the attempted assignment was ineffective as the WaMu Securitized Trust could not have accepted the Glaski deed of trust after the closing date because of the pooling and servicing agreement and the statutory requirements applicable to a Real Estate Mortgage Investment Conduit (REMIC) trust.[12]

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52 Causes of Action Second (2012) 119, 149 [§ 11 addresses foreclosure by a nonholder of mortgage rights].)

[12] This allegation comports with the following view of pooling and servicing agreements and the federal tax code provisions applicable to REMIC trusts. "Once the bundled mortgages are given to a depositor, the [pooling and servicing agreement] and IRS tax code provisions require that the mortgages be transferred to the trust within a certain time frame, usually ninety dates from the date the trust is created. After such time, the trust closes and any subsequent transfers are invalid. The reason for this is purely economic for the trust. If the mortgages are properly transferred within the ninety-day open period, and then the trust properly closes, the trust is allowed to maintain REMIC tax status." (*Deconstructing Securitized Trusts, supra,* 41 Stetson L.Rev. at pp. 757-758.)

B. Wrongful Foreclosure by a Nonholder of the Deed of Trust

The theory that a foreclosure was wrongful because it was initiated by a nonholder of the deed of trust has also been phrased as (1) the foreclosing party lacking standing to foreclose or (2) the chain of title relied upon by the foreclosing party containing breaks or defects. (See *Scott v. JPMorgan Chase Bank, N.A.* (2013) 214 Cal.App.4th 743, 764; *Herrera v. Deutsche Bank National Trust Co.*, *supra*, 196 Cal.App.4th 1366 [Deutsche Bank not entitled to summary judgment on wrongful foreclosure claim because it failed to show a chain of ownership that would establish it was the true beneficiary under the deed of trust]; *Guerroro v. Greenpoint Mortgage Funding, Inc.* (9th Cir. 2010) 403 Fed.Appx. 154, 156 [rejecting a wrongful foreclosure claim because, among other things, plaintiffs "have not pleaded any facts to rebut the unbroken chain of title"].)

In *Barrionuevo v. Chase Bank, N.A.* (N.D.Cal. 2012) 885 F.Supp.2d 964, the district court stated: "Several courts have recognized the existence of a valid cause of action for wrongful foreclosure where a party alleged not to be the true beneficiary instructs the trustee to file a Notice of Default and initiate nonjudicial foreclosure." (*Id.* at p. 973.) We agree with this statement of law, but believe that properly alleging a cause of action under this theory requires more than simply stating that the defendant who invoked the power of sale was not the true beneficiary under the deed of trust. Rather, a plaintiff asserting this theory must allege facts that show the defendant who invoked the power of sale was not the true beneficiary. (See *Herrera v. Federal National Mortgage Assn.* (2012) 205 Cal.App.4th 1495, 1506 [plaintiff failed to plead specific facts demonstrating the transfer of the note and deed of trust were invalid].)

C. Borrower's Standing to Raise a Defect in an Assignment

One basis for claiming that a foreclosing party did not hold the deed of trust is that the assignment relied upon by that party was ineffective. When a borrower asserts an assignment was ineffective, a question often arises about the borrower's standing to challenge the assignment of the loan (note and deed of trust)—an assignment to which the borrower is not a party. (E.g., *Conlin v. Mortgage Electronic Registration Systems, Inc.* (6th Cir. 2013) 714 F.3d 355, 361 [third party may only challenge an assignment if that challenge would render the assignment absolutely invalid or ineffective, or void]; *Culhane v. Aurora Loan Services of Nebraska* (1st Cir. 2013) 708 F.3d 282, 291 [under Massachusetts law, mortgagor has standing to challenge a mortgage assignment as invalid, ineffective or void]; *Gilbert v. Chase Home Finance, LLC* (E.D.Cal., May 28, 2013, No. 1:13-CV-265 AWI SKO) 2013 WL 2318890.)[13]

California's version of the principle concerning a third party's ability to challenge an assignment has been stated in a secondary authority as follows:

> "Where an assignment is merely voidable at the election of the assignor, third parties, and particularly the obligor, cannot … successfully challenge the validity or effectiveness of the transfer." (7 Cal.Jur.3d (2012) Assignments, § 43.)

This statement implies that a borrower can challenge an assignment of his or her note and deed of trust if the defect asserted would *void* the assignment. (See *Reinagel v. Deutsche Bank National Trust Co.* (5th Cir. 2013) ___ F.3d ___ [2013 WL 3480207 at p. *3] [following majority rule that an obligor may raise any ground that renders the assignment void, rather than merely voidable].) We adopt this view of the law and turn to the question whether Glaski's allegations have presented a theory under which the challenged assignments are void, not merely voidable.

We reject the view that a borrower's challenge to an assignment must fail once it is determined that the borrower was not a party to, or third party beneficiary of, the

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13 "Although we may not rely on unpublished California cases, the California Rules of Court do not prohibit citation to unpublished federal cases, which may properly be cited as persuasive, although not binding, authority." (*Landmark Screens, LLC v. Morgan, Lewis & Bockius, LLP* (2010) 183 Cal.App.4th 238, 251, fn. 6, citing Cal. Rules of Court, rule 8.1115.)

assignment agreement. Cases adopting that position "paint with too broad a brush." (*Culhane v. Aurora Loan Services of Nebraska, supra,* 708 F.3d at p. 290.) Instead, courts should proceed to the question whether the assignment was void.

D. Voidness of a Post-Closing Date Transfers to a Securitized Trust

Here, the SAC includes a broad allegation that the WaMu Securitized Trust "did not have standing to foreclosure on the … Property, as Defendants cannot provide the entire chain of title of the note and the [deed of trust]."[14]

More specifically, the SAC identifies two possible chains of title under which Bank of America, as trustee for the WaMu Securitized Trust, could claim to be the holder of the Glaski deed of trust and alleges that each possible chain of title suffers from the same defect—a transfer that occurred after the closing date of the trust.

First, Glaski addresses the possibility that (1) Bank of America's chain of title is based on its status as successor trustee for the WaMu Securitized Trust and (2) the Glaski deed of trust became part of the WaMu Securitized Trust's property when the securitized trust was created in 2005. The SAC alleges that WaMu did not transfer Glaski's note and deed of trust into the WaMu Securitized Trust prior to the closing date established by the pooling and servicing agreement. If WaMu's attempted transfer was void, then Bank of America could not claim to be the holder of the Glaski deed of trust simply by virtue of being the successor trustee of the WaMu Securitized Trust.

Second, Glaski addresses the possibility that Bank of America acquired Glaski's deed of trust from JP Morgan, which may have acquired it from the FDIC. Glaski

[14] Although this allegation and the remainder of the SAC do not explicitly identify the trustee of the WaMu Securitized Trust as the entity that invoked the power of sale, it is reasonable to interpret the allegation in this manner. Such an interpretation is consistent with the position taken by Glaski's attorney at the hearing on the demurrer, where she argued that the WaMu Securitized Trust did not obtain Glaski's loan and thus was precluded from proceeding with the foreclosure.

contends this alternate chain of title also is defective because JP Morgan's attempt to transfer the Glaski deed of trust to Bank of America, as trustee for the WaMu Securitized Trust, occurred after the trust's closing date. Glaski specifically alleges JP Morgan's attempted assignment of the deed of trust to the WaMu Securitized Trust in June 2009 occurred long after the WaMu Securitized Trust closed (i.e., 90 days after December 21, 2005).

Based on these allegations, we will address whether a post-closing date transfer into a securitized trust is the type of defect that would render the transfer void. Other allegations relevant to this inquiry are that the WaMu Securitized Trust (1) was formed in 2005 under New York law and (2) was subject to the requirements imposed on REMIC trusts (entities that do not pay federal income tax) by the Internal Revenue Code.

The allegation that the WaMu Securitized Trust was formed under New York law supports the conclusion that New York law governs the operation of the trust. New York Estates, Powers & Trusts Law section 7-2.4, provides: "If the trust is expressed in an instrument creating the estate of the trustee, every sale, conveyance or other act of the trustee in contravention of the trust, except as authorized by this article and by any other provision of law, is void."[15]

Because the WaMu Securitized Trust was created by the pooling and servicing agreement and that agreement establishes a closing date after which the trust may no longer accept loans, this statutory provision provides a legal basis for concluding that the trustee's attempt to accept a loan after the closing date would be void as an act in contravention of the trust document.

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[15] The statutory purpose is "to protect trust beneficiaries from unauthorized actions by the trustee." (Turano, Practice Commentaries, McKinney's Consolidated Laws of New York, Book 17B, EPTL § 7-2.4.)

We are aware that some courts have considered the role of New York law and rejected the post-closing date theory on the grounds that the New York statute is not interpreted literally, but treats acts in contravention of the trust instrument as merely *voidable*. (*Calderon v. Bank of America, N.A.* (W.D.Tex., Apr. 23, 2013, No. SA:12-CV-00121-DAE) ___ F.Supp.2d ___, [2013 WL 1741951 at p. *12] [transfer of plaintiffs' note, if it violated PSA, would merely be voidable and therefore plaintiffs do not have standing to challenge it]; *Bank of America National Association v. Bassman FBT, L.L.C.* (Ill.Ct.App. 2012) 981 N.E.2d 1, 8 [following cases that treat *ultra vires* acts as merely voidable].)

Despite the foregoing cases, we will join those courts that have read the New York statute literally. We recognize that a literal reading and application of the statute may not always be appropriate because, in some contexts, a literal reading might defeat the statutory purpose by harming, rather than protecting, the beneficiaries of the trust. In this case, however, we believe applying the statute to void the attempted transfer is justified because it protects the beneficiaries of the WaMu Securitized Trust from the potential adverse tax consequence of the trust losing its status as a REMIC trust under the Internal Revenue Code. Because the literal interpretation furthers the statutory purpose, we join the position stated by a New York court approximately two months ago: "Under New York Trust Law, every sale, conveyance or other act of the trustee in contravention of the trust is void. EPTL § 7-2.4. Therefore, the acceptance of the note and mortgage by the trustee after the date the trust closed, would be void." (*Wells Fargo Bank, N.A. v. Erobobo* (Apr. 29, 2013) 39 Misc.3d 1220(A), 2013 WL 1831799, slip opn. p. 8; see Levitin & Twomey, *Mortgage Servicing*, *supra*, 28 Yale J. on Reg. at p. 14, fn. 35 [under New York law, any transfer to the trust in contravention of the trust documents is void].) Relying on *Erobobo*, a bankruptcy court recently concluded "that under New York law, assignment of the Saldivars' Note after the start up day is void *ab initio*. As such, none of the Saldivars' claims will be dismissed for lack of standing." (*In re Saldivar* (Bankr.S.D.Tex., Jun. 5, 2013, No. 11-10689) 2013 WL 2452699, at p. *4.)

We conclude that Glaski's factual allegations regarding post-closing date attempts to transfer his deed of trust into the WaMu Securitized Trust are sufficient to state a basis for concluding the attempted transfers were void. As a result, Glaski has a stated cognizable claim for wrongful foreclosure under the theory that the entity invoking the power of sale (i.e., Bank of America in its capacity as trustee for the WaMu Securitized Trust) was not the holder of the Glaski deed of trust.[16]

We are aware that that some federal district courts sitting in California have rejected the post-closing date theory of invalidity on the grounds that the borrower does not have standing to challenge an assignment between two other parties. (*Aniel v. GMAC Mortgage, LLC* (N.D.Cal., Nov. 2, 2012, No. C 12-04201 SBA) 2012 WL 5389706 [joining courts that held borrowers lack standing to assert the loan transfer occurred outside the temporal bounds prescribed by the pooling and servicing agreement]; *Almutarreb v. Bank of New York Trust Co., N.A.* (N.D.Cal., Sept. 24, 2012, No. C 12-

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[16] Because Glaski has stated a claim for relief in his wrongful foreclosure action, we need not address his alternate theory that the foreclosure was void because it was implemented by forged documents. (*Genesis Environmental Services v. San Joaquin Valley Unified Air Pollution Control Dist.* (2003) 113 Cal.App.4th 597, 603 [appellate inquiry ends and reversal is required once court determines a cause of action was stated under any legal theory].) We note, however, that California law provides that ratification generally is an affirmative defense and must be specially pleaded by the party asserting it. (See *Reina v. Erassarret* (1949) 90 Cal.App.2d 418, 424 [ratification is an affirmative defense and the defendant ordinarily bears the burden of proof]; 49A Cal.Jur.3d (2010) Pleading, § 186, p. 319 [defenses that must be specially pleaded include waiver, estoppel and ratification].) Also, "[w]hether there has been ratification of a forged signature is ordinarily a question of fact." (*Common Wealth Ins. Systems, Inc. v. Kersten* (1974) 40 Cal.App.3d 1014, 1026; see *Brock v. Yale Mortg. Corp.* (Ga. 2010) 700 S.E.2d 583, 588 [ratification may be expressed or implied from acts of principal and "is usually a fact question for the jury"; wife had forged husband's signature on quitclaim deed].)

3061 EMC) 2012 WL 4371410.) These cases are not persuasive because they do not address the principle that a borrower may challenge an assignment that is void and they do not apply New York trust law to the operation of the securitized trusts in question.

E. Application of *Gomes*

The next question we address is whether Glaski's wrongful foreclosure claim is precluded by the principles set forth in *Gomes*, *supra*, 192 Cal.App.4th 1149, a case relied upon by the trial court in sustaining the demurrer. *Gomes* was a pre-foreclosure action brought by a borrower against the lender, trustee under a deed and trust, and MERS, a national electronic registry that tracks the transfer of ownership interests and servicing rights in mortgage loans in the secondary mortgage market. (*Id.* at p. 1151.) The subject trust deed identified MERS as a nominee for the lender and that MERS is the beneficiary under the trust deed. After initiation of a nonjudicial forclosure, borrower sued for wrongful initiation of foreclosure, alleging that the current owner of the note did not authorize MERS, the nominee, to proceed with the foreclosure. The appellate court held that California's nonjudicial foreclosure system, outlined in Civil Code sections 2924 through 2924k, is a "'comprehensive framework for the regulation of a nonjudicial foreclosure sale'" that did not allow for a challenge to the authority of the person initiating the foreclosure. (*Gomes, supra,* at p. 1154.)

In *Naranjo v. SBMC Mortgage* (S.D.Cal., Jul. 24, 2012, No. 11-CV-2229-L(WVG)) 2012 WL 3030370 (*Naranjo*), the district court addressed the scope of *Gomes*, stating:

> "In *Gomes*, the California Court of Appeal held that a plaintiff does not have a right to bring an action to determine the nominee's authorization to proceed with a nonjudicial foreclosure on behalf of a noteholder. [Citation.] The nominee in *Gomes* was MERS. [Citation.] Here, Plaintiff is not seeking such a determination. The role of the nominee is not central to this action as it was in *Gomes*. Rather, Plaintiff alleges that the transfer of rights to the WAMU Trust is improper, thus Defendants consequently

> lack the legal right to either collect on the debt or enforce the underlying security interest." (*Naranjo*, *supra*, 2012 WL 3030370, at p. *3.)

Thus, the court in *Naranjo* did not interpret *Gomes* as barring a claim that was essentially the same as the post-closing date claim Glaski is asserting in this case.

Furthermore, the limited nature of the holding in *Gomes* is demonstrated by the *Gomes* court's discussion of three federal cases relied upon by Mr. Gomes. The court stated that the federal cases were not on point because none recognized a cause of action requiring the noteholder's nominee to prove its authority to initiate a foreclosure proceeding. (*Gomes, supra,* 192 Cal.App.4th at p. 1155.) The *Gomes* court described one of the federal cases by stating that "the plaintiff alleged wrongful foreclosure on the ground that assignments of the deed of trust had been improperly backdated, and thus the wrong party had initiated the foreclosure process. [Citaiton.] No such infirmity is alleged here." (*Ibid*.; see *Lester v. J.P. Morgan Chase Bank* (N.D.Cal., Feb. 20, 2013) ___ F.Supp.2d____, [2013 WL 633333, p. *7] [concluding *Gomes* did not preclude the plaintiff from challenging JP Morgan's authority to foreclose].) The *Gomes* court also stated it was significant that in each of the three federal cases, "the plaintiff's complaint identified a *specific factual basis* for alleging that the foreclosure was not initiated by the correct party." (*Gomes, supra*, at p. 1156.)

The instant case is distinguishable from *Gomes* on at least two grounds. First, like *Naranjo*, Glaski has alleged that the entity claiming to be the noteholder was not the true owner of the note. In contrast, the principle set forth in *Gomes* concerns the authority of the *noteholder's nominee*, MERS. Second, Glaski has alleged specific grounds for his theory that the foreclosure was not conducted at the direction of the correct party.

In view of the limiting statements included in the *Gomes* opinion, we do not interpret it as barring claims that challenge a foreclosure based on specific allegations that an attempt to transfer the deed of trust was void. Our interpretation, which allows borrowers to pursue questions regarding the chain of ownership, is compatible with

Herrera v. Deutsche Bank National Trust Co., *supra*, 196 Cal.App.4th 1366. In that case, the court concluded that triable issues of material fact existed regarding alleged breaks in the chain of ownership of the deed of trust in question. (*Id*. at p. 1378.) Those triable issues existed because Deutsche Bank's motion for summary judgment failed to establish it was the beneficiary under that deed of trust. (*Ibid*.)

F. Tender

Defendants contend that Glaski's claims for wrongful foreclosure, cancellation of instruments and quiet title are defective because Glaski failed to allege that he made a valid and viable tender of payment of the indebtedness. (See *Karlsen v. American Sav. & Loan Assn.* (1971) 15 Cal.App.3d 112, 117 ["valid and viable tender of payment of the indebtedness owing is essential to an action to cancel a voidable sale under a deed of trust"].)

Glaski contends that he is not required to allege he tendered payment of the loan balance because (1) there are many exceptions to the tender rule, (2) defendants have offered no authority for the proposition that the absence of a tender bars *a claim for damages*,[17] and (3) the tender rule is a principle of equity and its application should not be decided against him at the pleading stage.

Tender is not required where the foreclosure sale is void, rather than voidable, such as when a plaintiff proves that the entity lacked the authority to foreclose on the property. (*Lester v. J.P. Morgan Chase Bank*, *supra*, ___ F.Supp.2d____, [2013 WL 633333, p. *8]; 4 Miller & Starr, Cal. Real Estate (3d ed. 2003) Deeds of Trust, § 10:212, p. 686.)

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[17] See generally, Annotation, *Recognition of Action for Damages for Wrongful Foreclosure—Types of Action* (2013) 82 A.L.R.6th 43 (claims that a foreclosure is "wrongful" can be tort-based, statute-based, and contract-based).

Accordingly, we cannot uphold the demurrer to the wrongful foreclosure claim based on the absence of an allegation that Glaski tendered the amount due under his loan. Thus, we need not address the other exceptions to the tender requirement. (See e.g., *Onofrio v. Rice* (1997) 55 Cal.App.4th 413, 424 [tender may not be required where it would be inequitable to do so].)

G. Remedy of Setting Aside Trustee's Sale

Defendants argue that the allegedly ineffective transfer to the WaMu Securitized Trust was a mistake that occurred outside the confines of the statutory nonjudicial foreclosure proceeding and, pursuant to *Nguyen v. Calhoun* (2003) 105 Cal.App.4th 428, 445, that mistake does not provide a basis for invalidating the trustee's sale.

First, this argument does not negate the possibility that other types of relief, such as damages, are available to Glaski. (See generally, Annot., *Recognition of Action for Damages for Wrongful Foreclosure—Types of Action*, *supra*, 82 A.L.R.6th 43.)

Second, "where a plaintiff alleges that the entity lacked authority to foreclose on the property, the foreclosure sale would be void. [Citation.]" (*Lester v. J.P. Morgan Chase Bank*, *supra*, ___ F.Supp.2d____, [2013 WL 633333, p. *8].)

Consequently, we conclude that *Nguyen v. Calhoun*, *supra*, 105 Cal.App.4th 428 does not deprive Glaski of the opportunity to prove the foreclosure sale was void based on a lack of authority.

H. Causes of Action Stated

Based on the foregoing, we conclude that Glaski's fourth cause of action has stated a claim for wrongful foreclosure. It follows that Glaski also has stated claims for quiet title (third cause of action), declaratory relief (fifth cause of action), cancellation of instruments (eighth cause of action), and unfair business practices under Business and Professions Code section 17200 (ninth cause of action). (See *Susilo v. Wells Fargo Bank*, *N.A.* (C.D.Cal. 2011) 796 F.Supp.2d 1177, 1196 [plaintiff's wrongful foreclosure claims served as predicate violations for her UCL claim].)

IV. JUDICIAL NOTICE

A. Glaski's Request for Judicial Notice

When Glaski filed his opening brief, he also filed a request for judicial notice of (1) a Consent Judgment entered on April 4, 2012, by the United States District Court of the District of Columbia in *United States v. Bank of America Corp.* (D.D.C. No. 12-CV-00361); (2) the Settlement Term Sheet attached to the Consent Judgment; and (3) the federal and state release documents attached to the Consent Judgment as Exhibits F and G.

Defendants opposed the request for judicial notice on the ground that the request violated the requirements in California Rules of Court, rule 8.252 because it was not filed with a separate proposed order, did not state why the matter to be noticed was relevant to the appeal, and did not state whether the matters were submitted to the trial court and, if so, whether that court took judicial notice of the matters.

The documents included in Glaski's request for judicial notice may provide background information and insight into robo-signing[18] and other problems that the lending industry has had with the procedures used to foreclose on defaulted mortgages. However, these documents do not directly affect whether the allegations in the SAC are sufficient to state a cause of action. Therefore, we deny Glaski's request for judicial notice.

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[18] Claims of misrepresentation or fraud related to robo-signing of foreclosure documents is addressed in Buchwalter, *Cause of Action in Tort for Wrongful Foreclosure of Residential Mortgage,* 52 Causes of Action Second, *supra*, at pages 147 to 149.

B. Defendants' Request for Judicial Notice of Assignment

The "ASSIGNMENT OF DEED OF TRUST" recorded on December 9, 2008, that stated JP Morgan transferred and assigned all beneficial interest under the Glaski deed of trust to "LaSalle Bank NA as trustee for WaMu [Securitized Trust]" together with the note described in and secured by the Glaski deed of trust was not attached to the SAC as an exhibit. That document is part of the appellate record because the respondents' appendix includes a copy of defendants' request for judicial notice that was filed in June 2011 to support a motion for judgment on the pleadings.

In ruling on defendants' request for judicial notice, the trial court stated that it could only take judicial notice that certain documents in the request, including the assignment of deed of trust, had been recorded, but it could not take judicial notice of factual matters stated in those documents. This ruling is correct and unchallenged on appeal. Therefore, like the trial court, we will take judicial notice of the existence and recordation of the December 2008 assignment, but we "do not take notice of the truth of matters stated therein." (*Herrera v. Deutsche Bank National Trust Co.*, *supra*, 196 Cal.App.4th at p. 1375.) As a result, the assignment of deed of trust does not establish that JP Morgan was, in fact, the holder of the beneficial interest in the Glaski deed of trust that the assignment states was transferred to LaSalle Bank. Similarly, it does not establish that LaSalle Bank in fact became the owner or holder of that beneficial interest.

Because the document does not establish these facts for purposes of this demurrer, it does not cure either of the breaks in the two alternate chains of ownership challenged in the SAC. Therefore, the December 2008 assignment does not provide a basis for sustaining the demurrer.

DISPOSITION

The judgment of dismissal is reversed. The trial court is directed to vacate its order sustaining the general demurrer and to enter a new order overruling that demurrer as to the third, fourth, fifth, eighth and ninth causes of action.

Glaski's request for judicial notice filed on September 25, 2012, is denied.

Glaski shall recover his costs on appeal.

Franson, J.

WE CONCUR:

Wiseman, Acting P.J.

Kane, J.

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIFTH APPELLATE DISTRICT

THOMAS A. GLASKI, Plaintiff and Appellant, v. BANK OF AMERICA, NATIONAL ASSOCIATION et al. Defendants and Respondents.	F064556 (Super. Ct. No. 09CECG03601) **ORDER GRANTING REQUEST FOR PUBLICATION**

As the nonpublished opinion filed on July 31, 2013, in the above entitled matter hereby meets the standards for publication specified in the California Rules of Court, rule 8.1105(c), it is ordered that the opinion be certified for publication in the Official Reports.

FRANSON, J.

I CONCUR:

KANE, J.

Filed 8/14/13

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION SEVEN

MICHAEL G. KING et al. Plaintiffs and Appellants, v. CHUNG H. WU et al. Defendants and Respondents.	B239801 (Los Angeles County Super. Ct. No. YC060847)

APPEAL from a judgment of the Superior Court of Los Angeles County, Dudley W. Gray II, Judge. Reversed.

Hennelly & Grossfeld and Michael G. King for Plaintiffs and Appellants.

Law Offices of Bennett A. Rheingold and Bennett A. Rheingold for Defendants and Respondents.

Michael and Linda King brought action to quiet title over a strip of land on their neighbors' property over which they claimed to have obtained a prescriptive easement. The trial court granted their neighbors' summary adjudication motion. We reverse.

FACTUAL AND PROCEDURAL BACKGROUND

Fred and Viola Fluckiger bought their property on June 24, 1960. Shortly thereafter they poured a concrete driveway partly encroaching on the neighboring property. The strip of driveway on the neighboring property ("prescriptive strip") is approximately eight inches wide and ninety feet long. The Kings bought the Fluckiger lot in July 1994. They used the concrete driveway for ingress and egress to their garage and for parking in the rear of the driveway.

On March 29, 1963, Chung H. Wu, Cindy Wu, and Yu Tsen Wu, as Trustee of the Chung Han Wu Revocable Trust of 1993 (the "Wus") became the owners of the property neighboring the Fluckigers. On October 16, 2009, they began constructing a metal guardrail over the prescriptive strip. Three days later the Kings filed a complaint seeking to quiet title over the prescriptive strip and asserting claims for trespass and declaratory relief. The Wus' answer claimed in an affirmative defense that the Wus had not had a possessory interest in their property until 2008. The Wus also filed a cross-complaint seeking injunctive relief and damages for trespass.

On June 17, 2011, the Wus moved for summary adjudication on the Kings' prescriptive easement and declaratory relief claims. To establish their affirmative defense, the Wus presented declarations by Yu Tsen Wu and accountant Keith Schulberg. Yu Tsen Wu declared that when she married her husband on June 9, 1966, the property was already rented out. According to her, the property was "continuously rented out" to a number of tenants with some "brief vacancies" of less than one year between June 1966 and August 2008. Schulberg opined that the Wu property was not rented for a period of one year, 10 and a half months between March 29, 1963, and mid-February 1965, and that it was continuously rented thereafter.

On September 9, 2011, the trial court granted the summary adjudication motion. The court concluded that the Wus had established an affirmative defense because they or their predecessors had not been in possession of the property for five continuous years during the Kings' and Fluckigers' 49-year use. The Kings voluntarily dismissed their trespass claim with prejudice, and the Wus dismissed their injunctive relief claim with prejudice. The Wus' remaining cross-claim was heard in October 2011, and a final judgment resolving all claims was entered in January 2012. The Kings filed a timely appeal on March 13, 2012.

DISCUSSION

We review the grant of summary adjudication *de novo*. (*West Shield Investigations & Security Consultants v. Superior Court* (2000) 82 Cal.App.4th 935, 946.)

A motion for summary adjudication can be granted "only if it completely disposes of a cause of action, an affirmative defense, a claim for damages, or an issue of duty." (Code of Civ. Pro., § 437c (f)(1).) The moving party bears the initial burden of production to make a prima facie showing that no triable issue of material fact exists. (*Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826, 850.) A defendant can meet his or her burden if he or she shows that one or more elements of the cause of action cannot be established or that an affirmative defense bars that action. (Code of Civ. Pro., § 437c (p)(2).) If so, the burden shifts to the plaintiff to demonstrate a triable issue of material fact. (*Ibid*.)

The Wus failed to meet their burden of proof because they could neither establish an affirmative defense nor demonstrate that the Kings had not obtained a prescriptive easement. To obtain a prescriptive easement, the Kings or their predecessors must have used the property "for the statutory period of five years, which use has been (1) open and notorious; (2) continuous and uninterrupted; (3) hostile to the true owner; and (4) under claim of right." (*Mehdizadeh v. Mincer* (1996) 46 Cal.App.4th 1296, 1305.) The Wus made no attempt to prove that any of these elements was unsatisfied. Instead, they argued that they had an affirmative defense because they and their predecessors had not been in continuous possession of the Wu property for five years.

California law does not require the actual owners of the adversely used land to have been in continuous possession for five years. (See *Gartlan v. C.A. Hooper & Co.* (1918) 177 Cal. 414, 428-429.) If at any point during the adverse use an owner or a landlord has been in possession, including constructively at the expiration of a renewable lease, he or she could and should have taken action to interrupt such use. (*Id.* at p. 428.) As a result, the fact that a prescriptive right cannot arise against an owner or landlord who has no possessory interest in the property during the period of adverse use, does not impact this case. (*Dieterich Internat. Truck Sales, Inc. v. J. S. & J. Services Inc.* (1992) 3 Cal.App.4th 1601; Civ. Code, §741 [an action obtained solely against a landlord's tenants cannot affect his or her rights].)

The Wus' own evidence demonstrates that the current case does not fall within the *Dieterich* limitation. The Wus were in actual possession of their property for nearly two years between 1963 and 1965 and for a period of almost a year between 1966 and 2008. Additionally, Yu Tsen Wu declared that the Wus had a number of tenants over the years. As a result, the Wus had constructive possession at the expiration of each of the various leases.

Because the Wus did not provide any evidence that the Kings could not satisfy an element of the prescriptive easement claim and because they did not establish a valid affirmative defense, the Wus did not meet their burden. Therefore, the summary adjudication should not have been granted.

DISPOSITION

The judgment is reversed. The Kings shall recover their costs on appeal.

ZELON, J.

We concur:

PERLUSS, P. J.

SEGAL, J.*

* Judge of the Los Angeles Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

Filed 9/20/13; pub. order 10/11/13 (see end of opn.)

COURT OF APPEAL, FOURTH APPELLATE DISTRICT

DIVISION ONE

STATE OF CALIFORNIA

THOMAS WILLIAM SELF et al., Plaintiffs, Cross-defendants and Respondents, v. SHAHRAM SHARAFI et al., Defendants, Cross-complainants and Appellants.	D061181 (Super. Ct. No. 37-2010-00101291-CU-OR-CTL)

APPEAL from a judgment of the Superior Court of San Diego County, Jeffrey B. Barton, Judge. Reversed with directions.

Dillon & Gerardi, Timothy P. Dillon and Sunjina Ahuja for Defendants, Cross-complainants and Appellants.

Boudreau Williams and Jon R. Williams for Plaintiffs, Cross-defendants and Respondents.

Defendants and cross-complainants Shahram Sharafi and Fatemeh Falahat-Pisheh (the Sharafis)[1] appeal from a judgment entered after the trial court granted summary judgment in favor of plaintiffs and cross-defendants Thomas William Self and Linda P. Self as co-trustees of the Thomas William Self and Linda P. Self Family Trust, executed May 10, 1995 (the Selfs) on the Selfs' first amended complaint for quiet title and declaratory relief and the Sharafis' cross-complaint for declaratory relief.

The first amended complaint and cross-complaint concern adjoining parcels of real property owned by the Selfs and the Sharafis, respectively. In granting the Selfs' motion for summary judgment, the court ruled that a building restriction contained in a 1946 deed, by which the prior common owner of the adjoining parcels conveyed the parcel the Sharafis now own and retained the parcel the Selfs now own, was a personal covenant that is not enforceable against the Selfs. The Sharafis contend the building restriction is enforceable as a covenant running with the land and as an equitable servitude. We conclude the building restriction is enforceable as a covenant running with the land under Civil Code[2] section 1462 and, accordingly, reverse with directions to enter judgment in favor of the Sharafis.

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1 Defendants refer to themselves collectively as the Sharafis in their appellate briefs.

2 Unless otherwise indicated, all further statutory references are to the Civil Code.

I

FACTUAL AND PROCEDURAL BACKGROUND

In 1945 Elizabeth Fleet purchased a parcel of real property described as "Lot 4 in Block 'I' of the Resubdivision of a portion of Villa Tract, La Jolla Park, in the City of San Diego." In November 1946, Fleet conveyed a portion of Lot 4 to Jay M. and Nita Donovan by a grant deed, which provided that she was conveying "[a]ll of Lot 4 EXCEPTING the following described property in Block 'I' . . . :" The deed then set forth the legal description of the portion of Lot 4 that Fleet retained.[3] Under the heading "Restriction[,]" the deed stated: "A consideration of this sale is that no buildings will be erected now or at any future date on the [property retained]."

In 1989, the Selfs purchased from successors in interest of Fleet the portion of Lot 4 that Fleet retained as well as some adjacent property. Although the grant deed conveying the Lot 4 property to the Selfs does not refer to the building restriction, the Selfs were made aware of the restriction *before* they purchased the property.[4] The Selfs

3 The 1946 grant deed sets forth the legal description of the retained portion as follows: "Beginning at the most Northerly corner of Lot 4, being also the Southerly line of Pepita Way: thence South 41° 19' West along the Northerly line of Lot 4, a distance of 60 feet to the Northwest corner of Lot 4; thence South 38° 32' East along the Westerly line of Lot 4 to the most Westerly prolongation of a line that would be the Southerly line of Lot 7; thence Easterly to the Easterly line of Lot 4 and also the most Southwesterly corner of said Lot 7 in said Block 'I'; thence North 30° 54' West, a distance of 118.42 feet to the most Northerly corner of Lot 4."

4 The building restriction was specifically noted in the sellers' Real Estate Transfer Disclosure Statement, which the Selfs signed to acknowledge their receipt of a copy of that document about a month before they completed the purchase of the property.

later transferred the property to their family trust. In October 2010, the Sharafis obtained title to the portion of Lot 4 that Fleet sold to the Donovans, and an adjoining lot.

In January 2011, the Selfs filed a verified first amended complaint against the Sharafis for quiet title and declaratory relief, seeking an adjudication that they held title to their Lot 4 property free of the building restriction contained in the 1946 grant deed and that the building restriction is invalid and unenforceable. In March 2011, the Sharafis filed a cross-complaint for declaratory relief, seeking an adjudication that the building restriction is "binding, valid and enforceable against the Self's [*sic*] as the owners of the Restricted Property and as against all subsequent owners of the Restricted Property."

The Selfs and the Sharafis both filed motions for summary judgment. The Selfs argued in their motion that, as a matter of law, the building restriction is not enforceable as a covenant running with the land or as an equitable servitude. The Sharafis argued the building restriction is enforceable as a covenant running with the land under two different statutes that define such covenants — section 1462 and former section 1468. They additionally argued that the building restriction is enforceable as an equitable servitude, and as a negative easement. The court granted the Selfs' motion and entered judgment in favor of the Selfs and against the Sharafis, ruling the building restriction is not a covenant running with the land, an equitable servitude, or a negative easement.

II

DISCUSSION

Because the material facts are undisputed, the legal significance of those facts presents a question of law, which we review de novo. (*Hill v. San Jose Family Housing Partners, LLC* (2011) 198 Cal.App.4th 764, 774; *Oxford v. Foster Wheeler LLC* (2009) 177 Cal.App.4th 700, 707.)

A. *Statutory Scheme for Covenants Running with the Land*

Section 1460 provides: "Certain covenants, contained in grants of estates in real property, are appurtenant to such estates, and pass with them, so as to bind the assigns of the covenantor and to vest in the assigns of the covenantee, in the same manner as if they had personally entered into them. Such covenants are said to run with the land." Section 1461 provides: "The only covenants which run with the land are those specified in this Title, and those which are incidental thereto." A covenant can run with the land under either section 1462 or section 1468. (*Monterey/Santa Cruz County Bldg. etc. Trades Council v. Cypress Marina Heights LP* (2011) 191 Cal.App.4th 1500, 1517.) To run with the land, a covenant must touch and concern land, which means it must affect the parties as owners of the particular estates in land or relate to the use of land. (*Anthony v. Brea Glenbrook Club* (1976) 58 Cal.App.3d 506, 510 (*Anthony*).) "The primary characteristic of a covenant running with the land is that both liability upon it and enforceability of it pass with the transfer of the estate. The benefits or burdens pass by implication of law rather than under principles of contract." (*Ibid*.)

B. *The Building Restriction Is Not a Covenant Running with the Land Under Section 1468*

The former version of section 1468 that was effective in 1946 provided: "A covenant made by the owner of land with the owner of other land to do or refrain from doing some act on his own land, which doing or refraining is expressed to be for the benefit of the land of the covenantee, and which is made by the covenantor expressly for his assigns or to the assigns of the covenantee, runs with both of such parcels of land." (Stats. 1905, ch. 450, § 1, p. 610.) The Legislature amended section 1468 in 1968 and 1969 to make covenants that run with the land analytically closer to equitable servitudes and to make the statute applicable to covenants between a grantor and grantee, as well as between separate landowners. (*Citizens for Covenant Compliance v. Anderson* (1995) 12 Cal.4th 345, 354 (*Citizens*).) However, those amendments "have been held to apply only to covenants postdating their enactment." (*Ibid.*) Accordingly, our determination of whether the building restriction at issue in this case is a covenant running with the land under section 1468 is governed by the former version of section 1468 in effect in 1946.

We conclude that the building restriction is not a covenant running with the land under the former version of section 1468 because that statute "only applied to a covenant 'made by the owner of land with the owner of other land,' and not to a covenant between a grantor and a grantee." (*Citizens*, *supra*, 12 Cal.4th at p. 353; *Marra v. Aetna Construction Co.* (1940) 15 Cal.2d 375, 377-378 (*Marra*).) Although Fleet and the Donovans were adjoining landowners before Fleet severed Lot 4 and conveyed a portion of it to the Donovans, the subject building restriction is contained in the grant deed by which Fleet made that conveyance. The building restriction was not a covenant concerning other parcels that Fleet and the Donovans owned before or after that conveyance. Because the covenant at issue in this case is contained in a grant of real property and predates the amendments to the original version of section 1468, it is governed *exclusively* by section 1462. (*Marra*, at p. 377 ["Covenants . . . contained in a grant in fee of real property, are governed solely by section 1462 . . . ."].)

C. *The Building Restriction Is a Covenant Running with the Land Under Section 1462*

Section 1462 provides: "Every covenant contained in a grant of an estate in real property, which is made for the direct benefit of the property, or some part of it then in existence, runs with the land." "The decisions have interpreted [section 1462] to mean that a burdensome covenant contained in a deed which in no way benefits the property conveyed is not binding at law upon the transferees of the grantee." (*Marra*, *supra*, 15 Cal.2d at p. 378.) Conversely, when a covenant benefits, and does not burden, the property conveyed, it runs with the land under section 1462 and is binding on transferees of the grantee. (*Citizens*, *supra*, 12 Cal.4th at pp. 353, 368.) Whether a covenant in a grant of real property benefits the conveyed property so as to run with the land under section 1462 is determined in light of the conditions existing at the time of the grant. (*Robertson v. Nichols* (1949) 92 Cal.App.2d 201, 205.) The fact that the covenant does not mention "assigns" is immaterial; the question must be determined from the nature of the covenant itself. (*Sacramento Suburban Fruit Lands Co. v. Whaley* (1920) 50 Cal.App. 125, 133 (*Sacramento Suburban Fruit*).)

The general test for determining whether a covenant runs with the land under section 1462 is whether the covenant "is 'made for the direct benefit of the property.' The phrase 'made for the direct benefit of the property' means, among other things, 'any covenant which affects the title to real property or any interest or estate therein of the covenantee. . . . [I]f the covenant is one which concerns the land itself, or in any manner or measure affects its title or any interest therein, then it is, within the meaning of . . . section 1462, "made for the direct benefit of the real property" to which it relates.'" (*Carlson v. Lindauer* (1953) 119 Cal.App.2d 292, 304-305.) The meaning of the phrase "direct benefit to the property" is not restricted to physical benefit that directly accrues to the land from the covenant. (*Richardson v. Callahan* (1931) 213 Cal. 683, 689; *Sacramento Suburban Fruit*, *supra*, 50 Cal.App. at p. 130.) Courts interpreting section 1462 "'have uniformly adopted the view that if the covenant tends to enhance or increase the value of the land, it is a direct benefit within the meaning of the [statute] and therefore runs with the land.'" (*Anthony*, *supra*, 53 Cal.App.3d at p. 511.)

The building restriction in the present case touches and concerns the land because it relates to the use of the restricted land. (*Anthony*, *supra*, 58 Cal.App.3d at p. 510.) The restriction directly benefits the Sharafis' property that Fleet conveyed to the Donovans in 1946 because it is the type of restriction that naturally enhances the market value of any property adjoining the restricted property. (*Mock v. Shulman* (1964) 226 Cal.App.2d 263, 266 [restriction imposed against all lots in a tract against growing any hedge over six feet in height within 15 feet of boundary line of adjoining lot was for the mutual benefit of the entire tract and the owners of the separate lots therein]; *Whitinsville Plaza, Inc. v.*

Kotseas (Mass. 1979) 390 N.E.2d 243, 247 [the purpose of all building restrictions is to enhance the market value of the promisee's land].)

The Selfs argue that the building restriction is not a covenant running with the land under section 1462 because it burdens their portion of Lot 4, citing the rule that "[u]nder section 1462, a [covenant] that *benefits* the property may run with the land, but not one that *burdens* the property." (*Citizens*, *supra*, 12 Cal.4th at p. 353.) However, "the property" referenced in the *Citizens* court's articulation of the rule is the property *conveyed* by the grant containing the covenant, *not property retained by the grantor*. Section 1462 states that "[e]very covenant contained in a *grant of an estate in real property*, which is made for the direct benefit of *the property*, or some part of it then in existence, runs with the land." (Italics added.) The property referenced in the phrase "which is made for the direct benefit of the property" can only be the property *granted* (i.e., *conveyed*) referenced in section 1462's opening clause because the statute does not refer to any other property. "It is . . . 'generally presumed that when a word is used in a particular sense in one part of a statute, it is intended to have the same meaning if it appears in another part of the same statute.'" (*Delaney v. Baker* (1999) 20 Cal.4th 23, 41.)

Thus, on its face, section 1462 applies when the covenant contained in a grant deed directly benefits the *conveyed* property. Nothing in the statute defeats its application where a covenant benefitting the conveyed property correspondingly burdens property retained by the grantor or some other property. As the Supreme Court stated in *Marra*, "[t]he decisions have interpreted [section 1462] to mean that a burdensome covenant contained in a deed which in no way benefits *the property conveyed* is not binding at law upon the transferees of the grantee." (*Marra*, *supra*, 15 Cal.2d at p. 378, italics added; *Taormina Theosophical Community, Inc. v. Silver* (1983) 140 Cal.App.3d 964, 972 ["Only the benefit of a covenant runs; covenants which burden *the covenantee/grantee's land* will not bind subsequent transferees." (Italics added.)]; *Standard Oil Co. v. Slye* (1913) 164 Cal. 435, 442 [covenant in a lease to renew the lease for an additional term runs with the land under section 1462 "because obviously a covenant for a renewal of a lease is for the direct benefit of *the estate granted*" (italics added)]; *Los Angeles Terminal Land Co. v. Muir* (1902) 136 Cal. 36, 41-42 (*Muir*) [covenant did not run with the land under section 1462 because it "was not made for the benefit of the lot *conveyed*, but purported to impose a burden thereon by restricting its use" (italics added)].)

The rule that a covenant does not run under section 1462 if it burdens "the property" does not apply to the building restriction at issue in this case because the restriction burdens only the land that Fleet *retained*; it does not burden the land she *conveyed* by the deed containing the building restriction. The building restriction is a covenant running with the land under section 1462 because it is contained in a grant of real property and directly benefits the land conveyed.[5]

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5 In *Oceanside Community Assn. v. Oceanside Land Co.* (1983) 147 Cal.App.3d 166 (*Oceanside*), a developer of 932 residences on individual lots recorded CC&R's restricting property it owned adjacent to the residential development to be used as a golf course. (*Id.* at p. 172.) This court decided the golf-course restriction was enforceable as a covenant running with the land under the current version of section 1468 as to some

The Selfs argue that the building restriction is not enforceable as a covenant running with the land because it does not describe the dominant tenement — i.e., the property benefitted by the restriction. Among other authority, the Selfs cite the *Citizens* court's statement that in light of the statute of frauds, for restrictions to be enforceable "there '"'should be some *written* evidence'"' indicating what property was affected by the restrictions." (*Citizens*, *supra*, 12 Cal.4th at p. 358.) The Selfs also cite *MacDonald Properties, Inc. v. Bel-Air Country Club* (1977) 72 Cal.App.3d 693 (*MacDonald*) for the proposition that a deed restriction cannot be enforced as a covenant running with the land if the deed contains no particular description of the dominant tenement to be benefitted.[6]

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homeowners and as an equitable servitude as to others. (*Oceanside*, at pp. 174-175.) In light of that determination, it was unnecessary for the *Oceanside* court to address whether the restriction was also a covenant running with the land under section 1462. Nevertheless, the court opined that the restriction was not enforceable under section 1462 because although it benefited the homeowners' properties, it burdened the developer's property. (*Oceanside*, at p. 174.) The court cited *Marra*, *supra*, 15 Cal.2d 375, and *Muir*, *supra*, 136 Cal. 36, for the proposition that a covenant does not run with the land under section 1462 if it burdens property. (*Oceanside*, at p. 174.) However, both *Marra* and *Muir* involved covenants that burdened only land *conveyed* by a grant deed and not land *retained* by the grantor. Neither case supports the *Oceanside* court's apparent view that a restriction in a grant deed cannot be a covenant running with the land under section 1462 if it burdens any other property. Because the *Oceanside* court's cursory analysis of the applicability of section 1462 was unnecessary to its decision, and its cited authority does not support its conclusion on that point, we do not view *Oceanside* as persuasive authority for the proposition that a covenant in a grant of real property that directly benefits the conveyed property does not run under section 1462 if it correspondingly burdens property the grantor retains.

6 Although the *MacDonald* court stated that the plaintiffs in that case were "technically correct at law" in arguing that the covenant in question did not particularly describe the property benefitted by the covenant, it nevertheless decided the covenant was enforceable as an equitable servitude. (*MacDonald*, *supra*, 72 Cal.App.3d at pp. 699-701.)

However, the requirement addressed in *MacDonald* that the instrument containing a covenant must particularly describe the land benefitted (and the land burdened) by the covenant is a requirement under the current version of section 1468, subdivision (a); it is not a requirement under section 1462. (*MacDonald*, at p. 699.)[7]

In any event, we conclude that the 1946 grant from Fleet to the Donovans satisfies the requirement that "there '"'should be some *written* evidence'"' indicating what property was affected by the restrictions." (*Citizens*, *supra*, 12 Cal.4th at p. 358.) The 1946 grant deed specifically described the portion of Lot 4 retained by Fleet and burdened by the building restriction, and sufficiently described the portion of Lot 4 being conveyed. Although the building restriction did not specifically state that the conveyed

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7 Before the current version of section 1468 was enacted, the courts in *Chandler v. Smith* (1959) 170 Cal.App.2d 118 and *Berryman v. Hotel Savoy Co.* (1911) 160 Cal. 559 decided that building restrictions imposed on the land *conveyed* in original grant deeds were not covenants running with the land *in part* because the deeds did not describe land to be benefitted by the covenants. However, these cases are inapposite. Unlike the building restriction at issue in the present case, the restrictions in *Berryman* burdened, rather than benefitted, the land of the grantee, and nothing in the deed gave notice to subsequent purchasers that the original grantor owned other property to be benefitted by the restrictions. Consequently, a subsequent purchaser was entitled to read the restrictions as not creating a covenant or servitude that would pass with the land. (*Berryman*, at pp. 564-565.) Similarly, the restrictions in *Chandler* burdened rather than benefitted the property conveyed, and it did not "appear that the restrictions . . . were inserted for the benefit of grantors' adjoining land." (*Chandler*, at p. 120.) In addition, the deed in *Chandler* expressly provided that title would not be forfeited or impaired for violation of the restrictions. Based on those facts, the *Chandler* court concluded that "the deed created a mere personal burden adhering exclusively to the original covenantor." (*Ibid.*) Unlike the deeds in *Berryman* and *Chandler*, the recorded 1946 deed in this case gives notice to subsequent purchasers of the property burdened by the building restriction (the property that Fleet retained) that Fleet conveyed adjoining property to be benefitted by the restriction.

portion of Lot 4 was the property intended to be benefitted by the building restriction, this intent is reasonably clear from the fact that the only properties referenced in the deed are the portion of Lot 4 retained and burdened by the building restriction and the portion of Lot 4 conveyed. We construe the building restriction as conferring a direct benefit on the parcel conveyed, which the Sharafis now own.

The Selfs additionally argue that the building restriction is not a covenant running with the land because the 1946 grant deed does not express a joint intention that the restriction be binding on the grantor's and grantees' successors or assigns. The Selfs cite *Oceanside* for the proposition that a baseline requirement for a restrictive covenant to run with the land is an expression in the instrument in question that the restriction will be binding on the parties' successors and assigns. However, as the *Oceanside* court noted, the requirement a "covenant must state it is binding on the assigns of the covenantor" is a requirement under the former version of section 1468. (*Oceanside, supra*, 147 Cal.App.3d at pp. 174-175 & fn. 4.)[8] It is not a requirement under section 1462.[9]

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8 As noted, the original version of section 1468 provided: "A covenant made by the owner of land with the owner of other land to do or refrain from doing some act on his own land, which doing or refraining is expressed to be for the benefit of the land of the covenantee, and *which is made by the covenantor expressly for his assigns or to the assigns of the covenantee*, runs with both of such parcels of land." (Stats. 1905, ch. 450, § 1, p. 610, italics added.)

9 At oral argument, the Selfs argued that a covenant under section 1462 must also state it is binding on heirs and assigns (i.e., future owners) of the covenantor, citing *Citizens, supra*, 12 Cal.4th at pp. 353-354. However, *Citizens* does not support that argument. On page 353, the Supreme Court set forth general background information about covenants running with the land. Regarding section 1462, the court noted that before the amendments to section 1468 in 1968 and 1969, section 1462 and 1468 "were

We conclude the building restriction in the 1946 deed is a covenant running with the land under section 1462.[10] As a statutory covenant running with the land, by operation of section 1460 the building restriction "bind[s] the assigns of the covenantor and . . . vest[s] in the assigns of the covenantee, in the same manner as if they had personally entered into them." (§ 1460.) Accordingly, it is enforceable against the portion of Lot 4 that the Selfs now own. Where, as here, it appears from the record that there is only one proper judgment on undisputed facts, we may direct the trial court to enter that judgment. (Code Civ. Proc., § 43; *Conley v. Matthes* (1997) 56 Cal.App.4th 1453, 1459, fn. 7.)

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written and interpreted very narrowly." (*Citizens*, at p. 353.) The *Citizens* court went on to note that "[u]nder section 1462, a [covenant] that *benefits* the property may run with the land, but not one that *burdens* the property." (*Ibid.*) The *Citizens* court noted that the covenants (CC&R's) at issue in that case were not enforceable as covenants under section 1462 because they burdened as well as benefitted the property conveyed. (*Citizens*, at p. 368.) The *Citizens* court did not address whether a covenant under section 1462 must state that it binds later owners, nor did it address that requirement in former section 1468. Regarding future owners, in its general background discussion the *Citizens* court simply noted, in accordance with section 1460, that "[a] covenant is said to run with the land if it binds not only the person who entered into it, but also later owners and assigns who did not personally enter into it." (*Citizens*, *supra*, 12 Cal.4th at p. 353, citing § 1460 and *Scaringe v. J.C.C. Enterprises, Inc.* (1988) 205 Cal.App.3d 1536, 1543.)

10 In light of our conclusion that the building restriction is a covenant running with the land under section 1462, we need not consider whether it is also enforceable as an equitable servitude.

DISPOSITION

The judgment in favor of respondents is reversed. The trial court is directed to enter judgment in favor of appellants on their cross-complaint and against respondents on their first amended complaint. Appellants are awarded their costs on appeal.

IRION, J.

WE CONCUR:

NARES, Acting P.J.

MCDONALD, J.

Filed 10/11/13

COURT OF APPEAL, FOURTH APPELLATE DISTRICT

DIVISION ONE

STATE OF CALIFORNIA

THOMAS WILLIAM SELF et al., Plaintiffs, Cross-defendants and Respondents, v. SHAHRAM SHARAFI et al., Defendants, Cross-complainants and Appellants.	D061181 (Super. Ct. No. 37-2010-00101291-CU-OR-CTL) ORDER CERTIFYING OPINION FOR PUBLICATION

THE COURT:

The opinion filed September 20, 2013, is ordered certified for publication.

NARES, Acting P.J.

Copies to: All parties

FIRST LIEN LETTER

Date:	Commitment Number:	Loan Number:
10/23/13	[redacted]	[redacted]

Borrower(s): [redacted]

Lender: Quicken Loans Inc.
1050 Woodward Ave
Detroit, MI 48226-1906

Property Address: [redacted]

In connection with property covered by the captioned title insurance commitment, we wish to advise that we have closed and completely disbursed the 930 - FHA 30 Yr Fixed mortgage in the amount of $ 83,460.00 .

This mortgage is a valid first lien on the property, subject only to those encumbrances shown in Schedule B of the captioned commitment. All taxes and special assessments which presently constitute a valid lien on the subject property have been paid in full.

Very truly yours,

Closing Agent Northern California Title Company

We have been instructed to record your deed of trust in first position. Escrow is a service to facilitate a real estate transaction and cannot guarantee or insure title, express or implied. This is a function of title insurance.

Do you instruct us to record your transaction with the following instruction

RECORDING INSTRUCTIONSAND
INSTRUCTIONS TO ISSUE TITLE INSURANCE

TO: [BLANK] TITLE CO

Your order no:
Our loan no:

Enclosed herewith are the following documents:
1.
2.
3.
4.

You are authorized and instructed to record the above mentioned items when you can issue a 2006 ALTA extended coverage policy in the amount of ________________________, insuring ______________________

The following numbered exceptions shown on the preliminary report dated___________ are to show on the policy of title insurance which our loan will be subject to:

The following endorsements are to be issued:

You are to record upon confirming email

Mail title policy to:

Assembly Bill No. 116

CHAPTER 62

An act to amend Section 65961 of, and to add Section 66452.24 to, the Government Code, relating to land use, and declaring the urgency thereof, to take effect immediately.

[Approved by Governor July 11, 2013. Filed with Secretary of State July 11, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 116, Bocanegra. Land use: subdivision maps: expiration dates.

(1) The Subdivision Map Act vests the authority to regulate and control the design and improvement of subdivisions in the legislative body of a local agency, and sets forth procedures governing the local agency's processing, approval, conditional approval or disapproval, and filing of tentative, final, and parcel maps, and the modification thereof. The act generally requires a subdivider to file a tentative map or vesting tentative map with the local agency, as specified, and the local agency, in turn, to approve, conditionally approve, or disapprove the map within a specified time period. The act requires an approved tentative map or vesting tentative map to expire 24 months after its approval, or after an additional period of time prescribed by local ordinance, not to exceed 12 months. However, the act extends the expiration date of certain approved tentative maps and vesting tentative maps, as specified.

This bill would extend by 24 months the expiration date of any approved tentative map or vesting tentative map that was approved on or after January 1, 2000. The bill would additionally require the extension of an approved or conditionally approved tentative map or vesting tentative map, or parcel map for which a tentative map or vesting tentative map was approved on or before December 31, 1999, upon application by the subdivider at least 90 days prior to the expiration of the map, as specified. By adding to the procedures that local agency officials must follow, this bill would impose a state-mandated local program.

(2) The Permit Streamlining Act prohibits a local agency, after its approval of a tentative map for a subdivision of single- or multiple-family residential units, from requiring conformance with, or the performance of, any conditions that the local agency could have lawfully imposed as a condition to the previously approved tentative or parcel map, as a condition to the issuance of any building permit or equivalent permit upon approval of that subdivision, during a 5-year period following the recordation of the final map or parcel map for that subdivision. The act also prohibits a local agency from refusing to issue a building permit or equivalent permit for a subdivider's failure to conform with or perform those conditions. However,

the act also provides that this 5-year period is a 3-year period for a tentative map extended pursuant to a specified provision of law, and the local agency is not prohibited from levying a fee, or imposing a condition that requires the payment of a fee upon the issuance of a building permit, with respect to the underlying units.

This bill would provide that a tentative map extended pursuant to its provisions is also subject to the truncated 3-year period described above, and that the local agency is not prohibited from levying a fee, as specified, or imposing a condition that requires the payment of a fee upon the issuance of a building permit, with respect to the underlying units. By adding to the procedures that local agency officials must follow, this bill would impose a state-mandated local program.

(3) The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

(4) This bill would declare that it is to take effect immediately as an urgency statute.

The people of the State of California do enact as follows:

SECTION 1. Section 65961 of the Government Code is amended to read:

65961. Notwithstanding any other provision of law, except as provided in subdivisions (e) and (f), upon approval or conditional approval of a tentative map for a subdivision of single- or multiple-family residential units, or upon recordation of a parcel map for such a subdivision for which no tentative map was required, during the five-year period following recordation of the final map or parcel map for the subdivision, a city, county, or city and county shall not require as a condition to the issuance of any building permit or equivalent permit for such single- or multiple-family residential units, conformance with or the performance of any conditions that the city or county could have lawfully imposed as a condition to the previously approved tentative or parcel map. Nor shall a city, county, or city and county withhold or refuse to issue a building permit or equivalent permit for failure to conform with or perform any conditions that the city, county, or city and county could have lawfully imposed as a condition to the previously approved tentative or parcel map. However, the provisions of this section shall not prohibit a city, county, or city and county from doing any of the following:

(a) Imposing conditions or requirements upon the issuance of a building permit or equivalent permit which could have been lawfully imposed as a condition to the approval of a tentative or parcel map if the local agency finds it necessary to impose the condition or requirement for any of the following reasons:

(1) A failure to do so would place the residents of the subdivision or of the immediate community, or both, in a condition perilous to their health or safety, or both.

(2) The condition is required in order to comply with state or federal law.

(b) Withholding or refusing to issue a building permit or equivalent permit if the local agency finds it is required to do so in order to comply with state or federal law.

(c) Assuring compliance with the applicable zoning ordinance.

(d) This section shall also apply to a city or city and county which incorporates on or after January 1, 1985, and which includes within its boundaries any areas included in the tentative or parcel map described in this section.

When the incorporation includes areas included in the tentative or parcel map described in this section, "a condition that the city could have lawfully imposed as a condition to the previously approved tentative or parcel map," as used in this section, refers to conditions the county could have imposed had there been no incorporation.

(e) For purposes only of a tentative subdivision map or parcel map that is extended pursuant to Section 66452.22, 66452.23, or 66452.24, the five-year period described in this section shall be three years.

(f) For purposes only of a tentative subdivision map or parcel map that is extended pursuant to Section 66452.22, 66452.23, or 66452.24, this section does not prohibit a city, county, or city and county from levying a fee or imposing a condition that requires the payment of a fee in the amount in effect upon the issuance of a building permit, including an adopted fee that is not included within an applicable zoning ordinance, upon the issuance of a building permit, including, but not limited to, a fee defined in Section 66000.

SEC. 2. Section 66452.24 is added to the Government Code, to read:

66452.24. (a) The expiration date of any tentative map, vesting tentative map, or parcel map for which a tentative map or vesting tentative map, as the case may be, that was approved on or after January 1, 2000, and that has not expired on or before the effective date of the act that added this section, shall be extended by 24 months.

(b) Upon application of the subdivider filed at least 90 days prior to the expiration of the approved or conditionally approved tentative map or vesting tentative map, or parcel map for which the tentative map or vesting tentative map, as the case may be, that was approved on or before December 31, 1999, the time at which the map expires shall be extended by the legislative body or by an advisory agency authorized to approve or conditionally approve tentative maps, for a period of 24 months upon a determination that the map is consistent with the applicable zoning and general plan requirements in effect when the application is filed. If the map is determined not to be consistent with applicable zoning and general plan requirements in effect when the application is filed, the legislative body or advisory agency may deny or conditionally approve an extension for a period of 24 months. Prior to the expiration of an approved or conditionally approved tentative map, upon an application by the subdivider to extend that map, the map shall automatically be extended for 60 days or until the application for the extension is approved, conditionally approved, or denied, whichever occurs last. If the advisory agency denies a subdivider's application for an extension, the subdivider may appeal to the legislative body within 15 days after the advisory agency has denied the extension.

(c) The extension provided by subdivisions (a) and (b) shall be in addition to any extension of the expiration date provided for in Section 66452.6, 66452.11, 66452.13, 66452.21, 66452.22, 66452.23, or 66463.5.

(d) Any legislative, administrative, or other approval by any state agency that pertains to a development project included in a map that is extended pursuant to subdivisions (a) and (b) shall be extended by 24 months if this approval has not expired on or before the effective date of the act that added this section. This extension shall be in addition to any extension provided for in Sections 66452.13, 66452.21, 66452.22, and 66452.23.

(e) The provisions of Section 65961 relating to conditions that may be imposed upon or after a building permit for a subdivision of single- or multiple-family residential units or a parcel map for a subdivision for which no tentative map was required, are modified as set forth in subdivisions (e) and (f) of Section 65961 for tentative maps extended pursuant to this section.

SEC. 3. No reimbursement is required by this act pursuant to Section 6 of Article XIII B of the California Constitution because a local agency or school district has the authority to levy service charges, fees, or assessments sufficient to pay for the program or level of service mandated by this act, within the meaning of Section 17556 of the Government Code.

SEC. 4. This act is an urgency statute necessary for the immediate preservation of the public peace, health, or safety within the meaning of Article IV of the Constitution and shall go into immediate effect. The facts constituting the necessity are:

In order to permit cities, counties, and cities and counties to preserve development applications that are set to expire and that cannot be processed presently due to prevailing adverse economic conditions in the construction industry, it is necessary that this act take effect immediately.

O

Senate Bill No. 426

CHAPTER 65

An act to amend Sections 580b and 580d of the Code of Civil Procedure, relating to deficiency judgments.

[Approved by Governor July 11, 2013. Filed with Secretary of State July 11, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 426, Corbett. Civil procedure: deficiency judgments.

Existing law provides that no deficiency judgment shall lie following a judicial foreclosure with respect to certain enumerated circumstances, including, among others, after a sale of real property or an estate for years therein for failure of the purchaser to complete his or her contract of sale. Existing law prohibits a judgment to be rendered for a deficiency on a note secured by a deed of trust or mortgage on real property or an estate for years therein, as specified.

This bill would prohibit a deficiency from being owed or collected following a judicial foreclosure with respect to the enumerated circumstances. The bill also would prohibit a deficiency from being owed or collected for a deficiency on a note secured by a deed of trust or mortgage on real property or an estate for years therein, as specified, and would make nonsubstantive changes to these provisions. The bill also would express the intent of the Legislature that these provisions would not impact existing law regarding the liability of a guarantor, pledgor, or other surety with respect to a deficiency, nor existing law regarding other collateral pledged to secure the obligation that is the subject of a deficiency.

The people of the State of California do enact as follows:

SECTION 1. The Legislature finds and declares that this measure is not intended to and does not impact existing law regarding the liability a guarantor, pledgor or other surety may have with respect to a deficiency, nor does it impact existing law regarding other collateral pledged to secure an obligation that is the subject of a deficiency.

SEC. 2. Section 580b of the Code of Civil Procedure is amended to read:

580b. (a) Except as provided in subdivision (c), no deficiency shall be owed or collected, and no deficiency judgment shall lie, for any of the following:

(1) After a sale of real property or an estate for years therein for failure of the purchaser to complete his or her contract of sale.

(2) Under a deed of trust or mortgage given to the vendor to secure payment of the balance of the purchase price of that real property or estate for years therein.

(3) Under a deed of trust or mortgage on a dwelling for not more than four families given to a lender to secure repayment of a loan that was used to pay all or part of the purchase price of that dwelling, occupied entirely or in part by the purchaser. For purposes of subdivision (b), a loan described in this paragraph is a "purchase money loan."

(b) No deficiency shall be owed or collected, and no deficiency judgment shall lie, on a loan, refinance, or other credit transaction (collectively, a "credit transaction") that is used to refinance a purchase money loan, or subsequent refinances of a purchase money loan, except to the extent that in a credit transaction the lender or creditor advances new principal (hereafter "new advance") that is not applied to an obligation owed or to be owed under the purchase money loan, or to fees, costs, or related expenses of the credit transaction. A new credit transaction shall be deemed to be a purchase money loan except as to the principal amount of a new advance. For purposes of this section, any payment of principal shall be deemed to be applied first to the principal balance of the purchase money loan, and then to the principal balance of a new advance, and interest payments shall be applied to any interest due and owing. This subdivision applies only to credit transactions that are executed on or after January 1, 2013.

(c) The fact that no deficiency shall be owed or collected under the circumstances set forth in subdivisions (a) and (b) does not affect the liability that a guarantor, pledgor or other surety might otherwise have with respect to the deficiency, or that might otherwise be satisfied in whole or in part from other collateral pledged to secure the obligation that is the subject of the deficiency.

(d) When both a chattel mortgage and a deed of trust or mortgage have been given to secure payment of the balance of the combined purchase price of both real and personal property, no deficiency judgment shall lie under any one thereof if no deficiency judgment would lie under the deed of trust or mortgage on the real property or estate for years therein.

SEC. 3. Section 580d of the Code of Civil Procedure is amended to read:

580d. (a) Except as provided in subdivision (b), no deficiency shall be owed or collected, and no deficiency judgment shall be rendered for a deficiency on a note secured by a deed of trust or mortgage on real property or an estate for years therein executed in any case in which the real property or estate for years therein has been sold by the mortgagee or trustee under power of sale contained in the mortgage or deed of trust.

(b) The fact that no deficiency shall be owed or collected under the circumstances set forth in subdivision (a) does not affect the liability that a guarantor, pledgor or other surety might otherwise have with respect to the deficiency, or that might otherwise be satisfied in whole or in part from other collateral pledged to secure the obligation that is the subject of the deficiency.

(c) This section does not apply to a deed of trust, mortgage, or other lien given to secure the payment of bonds or other evidences of indebtedness authorized or permitted to be issued by the Commissioner of Corporations, or which is made by a public utility subject to the Public Utilities Act (Part 1 (commencing with Section 201) of Division 1 of the Public Utilities Code).

O

Assembly Bill No. 464

CHAPTER 78

An act to amend Sections 1188 and 1195 of the Civil Code, to amend Section 103526 of the Health and Safety Code, and to amend Section 210 of the Probate Code, relating to vital records.

[Approved by Governor August 12, 2013. Filed with Secretary of State August 12, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 464, Daly. Vital records.

Under existing law, a certified copy of a birth, death, marriage or military service record may only be supplied by the State Registrar, local registrar, or county recorder to an authorized person, as defined, who submits a written or faxed request accompanied by a notarized statement sworn under penalty of perjury that the applicant is an authorized person.

This bill would additionally authorize the request and the notarized statement to be a digitized image, as defined. The bill would remove the application of these provisions to requests for certified copies of a military service record as requests for certified copies of those records are also subject to different provisions of existing law.

Existing law authorizes proof of the execution of an instrument by certain persons and prescribes the form for that proof. Existing law authorizes the use of a specified form as a certificate for proof of execution of an instrument.

This bill would instead require the specified form to be used as a certificate for proof of execution of an instrument, and would make several changes to the form.

Existing law authorizes, if title to real property is affected by the death of a person, any person to record evidence of the death in the county in which the property is located by providing specified documents, which may include, among other things, a certified copy of a record of the death, as specified.

This bill would provide that a certified copy of a record of death includes a certified copy or informational certified copy issued by the State Registrar, local registrar, or county recorder pursuant to specified provisions.

The people of the State of California do enact as follows:

SECTION 1. Section 1188 of the Civil Code is amended to read:

1188. An officer taking the acknowledgment of an instrument shall endorse thereon or attach thereto a certificate pursuant to Section 1189.

SEC. 2. Section 1195 of the Civil Code is amended to read:

1195. (a) Proof of the execution of an instrument, when not acknowledged, may be made by any of the following:

(1) By the party executing it, or either of them.

(2) By a subscribing witness.

(3) By other witnesses, in cases mentioned in Section 1198.

(b) (1) Proof of the execution of a power of attorney, grant deed, mortgage, deed of trust, quitclaim deed, security agreement, or any instrument affecting real property is not permitted pursuant to Section 27287 of the Government Code, though proof of the execution of a trustee's deed or deed of reconveyance is permitted.

(2) Proof of the execution for any instrument requiring a notary public to obtain a thumbprint from the party signing the document in the notary public's journal is not permitted.

(c) Any certificate for proof of execution taken within this state shall be in the following form:

State of California } ss.
County of __________ }

On ____ (date), before me, _____ (name and title of officer), personally appeared ____ (name of subscribing witness), proved to me to be the person whose name is subscribed to the within instrument, as a witness thereto, on the oath of ____ (name of credible witness), a credible witness who is known to me and provided a satisfactory identifying document. ____ (name of subscribing witness), being by me duly sworn, said that he/she was present and saw/heard ____ (name[s] of principal[s]), the same person(s) described in and whose name(s) is/are subscribed to the within or attached instrument in his/her/their authorized capacity(ies) as (a) party(ies) thereto, execute or acknowledge executing the same, and that said affiant subscribed his/her name to the within or attached instrument as a witness at the request of ____ (name[s] of principal[s]).

WITNESS my hand and official seal.
Signature____ (Seal)

SEC. 3. Section 103526 of the Health and Safety Code is amended to read:

103526. (a) (1) If the State Registrar, local registrar, or county recorder receives a written, faxed, or digitized image of a request for a certified copy of a birth, death, or marriage record pursuant to Section 103525 that is accompanied by a notarized statement sworn under penalty of perjury, or a faxed copy or digitized image of a notarized statement sworn under penalty of perjury, that the requester is an authorized person, as defined in this section, that official may furnish a certified copy to the applicant pursuant to Section 103525. A faxed or digitized image of the notary acknowledgment accompanying a faxed request received pursuant to this subdivision for a certified copy of a birth, death, or marriage record shall be legible and, if the notary's seal is not photographically reproducible, show the name of the notary, the county of the notary's principal place of business, the notary's telephone number, the notary's registration number, and the notary's commission expiration date typed or printed in a manner that is photographically reproducible below, or immediately adjacent to, the notary's signature in the acknowledgment. If a request for a certified copy of a birth, death, or marriage record is made in person, the official shall take a statement sworn under penalty of perjury that the requester is signing his or her own legal name and is an authorized person, and that official may then furnish a certified copy to the applicant.

(2) For purposes of this subdivision, "digitized image" means an image of an original paper request for a certified copy of a birth, death, or marriage record.

(b) (1) If the person requesting a certified copy of a birth, death, or nonconfidential marriage record is not an authorized person or is an authorized person who is otherwise unable to satisfy the requirements of subdivision (a), the certified copy provided to the applicant shall be an informational certified copy and shall display a legend that states "INFORMATIONAL, NOT A VALID DOCUMENT TO ESTABLISH IDENTITY." The legend shall be placed on the certificate in a manner that will not conceal information.

(2) If the person requesting a certified copy of a confidential marriage record is not an authorized person or is an authorized person who is otherwise unable to satisfy the requirements of subdivision (a), the official shall not release a certified copy of the confidential marriage record unless otherwise authorized by law.

(c) For purposes of this section, an "authorized person" means:

(1) For purposes of requests for certified copies of confidential marriage records, only a party to the confidential marriage.

(2) For purposes of requests for certified copies of birth, death, or nonconfidential marriage records, a person who is any of the following:

(A) The registrant or a parent or legal guardian of the registrant.

(B) A party entitled to receive the record as a result of a court order, or an attorney or a licensed adoption agency seeking the birth record in order to comply with the requirements of Section 3140 or 7603 of the Family Code.

(C) A member of a law enforcement agency or a representative of another governmental agency, as provided by law, who is conducting official business.

(D) A child, grandparent, grandchild, sibling, spouse, or domestic partner of the registrant.

(E) An attorney representing the registrant or the registrant's estate, or any person or agency empowered by statute or appointed by a court to act on behalf of the registrant or the registrant's estate.

(F) An agent or employee of a funeral establishment who acts within the course and scope of his or her employment and who orders certified copies of a death certificate on behalf of any individual specified in paragraphs (1) to (5), inclusive, of subdivision (a) of Section 7100.

(d) A person who asks the agent or employee of a funeral establishment to request a death certificate on his or her behalf warrants the truthfulness of his or her relationship to the decedent, and is personally liable for all damages occasioned by, or resulting from, a breach of that warranty.

(e) Notwithstanding any other law:

(1) A member of a law enforcement agency or a representative of a state or local government agency, as provided by law, who orders a copy of a record to which subdivision (a) applies in conducting official business shall not be required to provide the notarized statement required by subdivision (a).

(2) An agent or employee of a funeral establishment who acts within the course and scope of his or her employment and who orders death certificates on behalf of individuals specified in paragraphs (1) to (5), inclusive, of subdivision (a) of Section 7100 shall not be required to provide the notarized statement required by subdivision (a).

(f) Informational certified copies of birth and death certificates issued pursuant to subdivision (b) shall only be printed from the single statewide database prepared by the State Registrar and shall be electronically redacted to remove any signatures for purposes of compliance with this section. Local registrars and county recorders shall not issue informational certified copies of birth and death certificates from a source other than the statewide database prepared by the State Registrar. This subdivision shall become operative on July 1, 2007, but only after the statewide database becomes operational and the full calendar year of the birth and death indices and images is entered into the statewide database and is available for the respective year of the birth or death certificate for which an informational copy is requested. The State Registrar shall provide written notification to local registrars and county recorders as soon as a year becomes available for issuance from the statewide database.

SEC. 4. Section 210 of the Probate Code is amended to read:

210. If title to real property is affected by the death of a person, any person may record in the county in which the property is located any of the following documents establishing the fact of the death:

(a) An affidavit of death executed by a person having knowledge of the facts. The affidavit shall include a particular description of the real property and an attested or certified copy of a record of the death made and filed in a designated public office as required by law. For purposes of this subdivision, a certified copy issued in this state shall include any copy issued pursuant to Section 103525 of, subdivision (a) of Section 103526 of, or paragraph (1) of subdivision (b) of Section 103526 of, the Health and Safety Code.

(b) A certified copy of a court order that determines the fact of death made pursuant to Chapter 1 (commencing with Section 200) or pursuant to another statute that provides for a determination of the fact of death.

O

Assembly Bill No. 727

CHAPTER 104

An act to add Section 6707 to the Public Resources Code, relating to public trust lands.

[Approved by Governor August 13, 2013. Filed with Secretary of State August 13, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 727, Stone. Public trust lands: dredging: notice and leases.

Existing law authorizes the State Lands Commission to enter into an exchange, with any person or private entity, of filled or reclaimed tidelands and submerged lands or beds of navigable waterways, or interests in those lands, if the commission finds that specified conditions are met.

This bill would require that a local trustee of tide and submerged lands or an applicant for dredging on granted tide and submerged lands that intends to commence dredging on granted public trust lands, upon which any right to minerals on those lands is reserved by the state, to notify the commission, in writing, no later than 120 days prior to the time dredging is commenced, and would require that the written notice contain specified information.

The bill would specify that if that written notice is provided to the commission, a local trustee or applicant for dredging may presume that a dredging lease is not required if prescribed conditions are met. The bill would authorize the commission, if any dredging on granted tide and submerged lands wherein minerals are reserved to the state does not meet those prescribed conditions, to require a lease from the commission for that dredging. The bill would require the commission, if it determines that a lease is required, to provide the grantee or applicant for dredging with written notification of that determination within 30 days after the commission receives notification of the proposed dredging. The bill would require that any revenue that is earned by a local trustee from the dredging of granted lands be held or spent in a manner consistent with the trustee's existing obligations under the public trust and the specific terms of its grant of lands. The bill would make the above requirements applicable only to dredging operations that are commenced on or after January 1, 2014.

The people of the State of California do enact as follows:

SECTION 1. It is the intent of the Legislature to streamline the process of dredging on granted tide and submerged lands wherein mineral deposits are reserved to the state when consistent with the preservation and promotion of tideland trust activities, and to preserve tideland trust revenue within the corpus of the trust. To this end, it is also the intent of the Legislature that dredging on granted tide and submerged lands wherein mineral deposits are reserved to the state does not require a dredging lease from the State Lands Commission when the dredging is conducted strictly for the purposes of maintaining or enhancing maritime or water-dependent commerce, navigation, fishing, or other public trust activities required under the granting statute.

SEC. 2. The Legislature finds and declares all of the following:

(a) As part of its fiduciary duty, a local trustee of granted tide and submerged lands is required to take reasonable steps under the circumstances to take and keep control of, and preserve property for, public trust purposes on behalf of the state for the benefit of all the people of California.

(b) All local trustees of tide and submerged lands that were granted for the establishment, improvement, or conduct of a harbor and for the construction, maintenance, and operation of the public trust lands in a manner that is necessary or convenient for the promotion and accommodation of commerce and navigation should, from time to time, deepen and maintain depths of their berths, harbors, and navigable waterways within their grants to further the trust purposes for which the local trustee holds tide and submerged lands.

(c) Dredging activity on granted tide and submerged lands typically requires multiple approvals and permits from various local, state, and federal regulators, and must comply with the environmental requirements prescribed under the California Environmental Quality Act (Division 13 (commencing with Section 21000) of the Public Resources Code).

(d) When the rights to mineral deposits are reserved to the state in any grant of tide and submerged lands, the state should reserve the right to require that any dredging on those granted lands be carried out pursuant to a lease entered into by a local trustee and the State Lands Commission.

SEC. 3. Section 6707 is added to the Public Resources Code, to read:

6707. (a) The Legislature finds and declares that to promote and accommodate public trust uses, including commerce, navigation, and fisheries, proper management of granted public trust lands may require the local trustee to conduct dredging of navigational channels and vessel berths on granted lands, including on those granted lands in which the state reserves mineral interests, and that those dredging activities are consistent with the public trust.

(b) A local trustee of tide and submerged lands or an applicant for dredging on granted tide and submerged lands that intends to commence dredging on granted public trust lands, upon which any right to minerals on those lands is reserved by the state, shall notify the commission, in writing, no later than 120 days prior to the time dredging is commenced.

The notice shall contain all of the following information:

(1) A description of the dredging to be conducted on those lands, including a map and land description showing the area and project site.

(2) A description of the amount of material to be dredged, disposal amount, location, and means of disposal, if available.

(3) The time and manner in which dredging is to occur.

(4) The relevant permits, authorizations, and approvals that exist or must be obtained to complete dredging, or, if applicable, demonstration of compliance with a dredged materials management office plan that is administered by the United States Army Corps of Engineers.

(5) A declaration that the dredging is necessary for the proper management of the grant consistent with the public trust for commerce, navigation, and fisheries, or a statement of why the dredging is necessary to be undertaken for other purposes and a declaration that the dredging is consistent with the statutory grant.

(6) A statement with supporting documents that explains whether the trustee anticipates receipt of any revenues from the materials to be dredged, and, if so, in what amounts.

(c) After submission of the written notice required by this section, a local trustee or applicant for dredging may presume that a dredging lease is not required if all of the following conditions are met:

(1) The dredging is maintenance dredging consistent with the proper management of the granted lands.

(2) The dredged material is not sold or used for a private benefit.

(3) The dredged material is disposed of at an approved onshore or offshore disposal site.

(d) The commission may require a lease for any dredging on granted tide and submerged lands wherein the right to minerals is reserved to the state if the proposed dredging does not meet the conditions set forth in subdivision (c). The commission may delegate the authority to determine whether a lease is necessary to its executive officer. If the commission determines that a lease is required, the commission shall provide the grantee or applicant for dredging with written notification of that determination within 30 days after the commission receives notification of the proposed dredging. All applicable reimbursement costs shall be submitted with the application for a lease, if a lease is necessary.

(e) This section shall apply only to dredging operations that are commenced on or after January 1, 2014.

(f) This section does not exempt a local trustee of tide and submerged lands or other person or entity dredging on those lands from any permit or other approval necessary to carry out dredging operations that may be required by another local, state, or federal law.

(g) (1) Any revenue that is earned by a local trustee from the dredging of granted lands shall be held or spent in a manner consistent with the trustee's existing obligations under the public trust and the specific terms of its grant of lands.

(2) If a local trustee receives any revenue from the dredged materials not otherwise disclosed in the notice required by this section, the local trustee shall immediately notify the commission in writing. The commission may require the grantee to pay a reasonable royalty and enter into a lease for the dredging. If a grantee fails to notify the commission, the commission may require the local trustee to remit all revenues to the state.

(h) Nothing in this section shall be construed to limit the authority of the commission to enter into a lease, at its discretion, for dredging activity on granted tide and submerged lands wherein the right to minerals is reserved to the state.

O

Assembly Bill No. 379

CHAPTER 137

An act to amend Section 18551 of the Health and Safety Code, relating to manufactured housing.

[Approved by Governor August 26, 2013. Filed with Secretary of State August 26, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 379, Brown. Manufactured housing: removal.

Existing law requires the installation of a manufactured home, mobilehome, or commercial modular as a fixture or improvement to real property to comply with specified provisions. Existing law requires an enforcement agency to record with the county recorder of the county where real property is situated, on the same day that the certificate of occupancy for a manufactured home, mobilehome, or commercial modular is issued by the appropriate enforcement agency, that the real property has been installed upon, a document naming the owner of the real property, describing the real property with certainty, and stating that a manufactured home, mobilehome, or commercial modular has been affixed to the real property by installation on a foundation system, as specified.

This bill would instead require that recordation to occur within 5 business days of the issuance of the certificate of occupancy.

Existing law provides that once installed on a foundation system in compliance with these provisions, a manufactured home, mobilehome, or commercial modular shall be deemed a fixture and a real property improvement to the real property to which it is affixed and physical removal of the manufactured home, mobilehome, or commercial modular shall thereafter be prohibited without the consent of all persons or entities who, at the time of removal, have title to any estate or interest in the real property to which it is affixed.

The bill would also make other technical, nonsubstantive, and clarifying changes.

The people of the State of California do enact as follows:

SECTION 1. Section 18551 of the Health and Safety Code is amended to read:

18551. The department shall establish regulations for manufactured home, mobilehome, and commercial modular foundation systems that shall be applicable throughout the state. When established, these regulations supersede any ordinance enacted by any city, county, or city and county applicable to manufactured home, mobilehome, and commercial modular foundation systems. The department may approve alternate foundation systems to those provided by regulation if the department is satisfied of equivalent performance. The department shall document approval of alternate systems by its stamp of approval on the plans and specifications for the alternate foundation system. A manufactured home, mobilehome, or commercial modular may be installed on a foundation system as either a fixture or improvement to the real property, in accordance with subdivision (a), or a manufactured home or mobilehome may be installed on a foundation system as a chattel, in accordance with subdivision (b).

(a) Notwithstanding any other law, prior to a manufactured home, mobilehome, or commercial modular being deemed a fixture or improvement to the real property, the installation shall comply with all of the following:

(1) Prior to installation of a manufactured home, mobilehome, or commercial modular on a foundation system, the manufactured home, mobilehome, or commercial modular owner or a licensed contractor shall obtain a building permit from the appropriate enforcement agency. To obtain a permit, the owner or contractor shall provide the following:

(A) Written evidence acceptable to the enforcement agency that the manufactured home, mobilehome, or commercial modular owner owns, holds title to, or is purchasing the real property where the mobilehome is to be installed on a foundation system. A lease held by the manufactured home, mobilehome, or commercial modular owner, that is transferable, for the exclusive use of the real property where the manufactured home, mobilehome, or commercial modular is to be installed, shall be deemed to comply with this paragraph if the lease is for a term of 35 years or more, or if less than 35 years, for a term mutually agreed upon by the lessor and lessee, and the term of the lease is not revocable at the discretion of the lessor except for cause, as described in subdivisions 2 to 5, inclusive, of Section 1161 of the Code of Civil Procedure.

(B) Written evidence acceptable to the enforcement agency that the registered owner owns the manufactured home, mobilehome, or commercial modular free of any liens or encumbrances or, in the event that the legal owner is not the registered owner, or liens and encumbrances exist on the manufactured home, mobilehome, or commercial modular, written evidence provided by the legal owner and any lienors or encumbrancers that the legal owner, lienor, or encumbrancer consents to the attachment of the manufactured home, mobilehome, or commercial modular upon the discharge of any personal lien, that may be conditioned upon the satisfaction by the registered owner of the obligation secured by the lien.

(C) Plans and specifications required by department regulations or a department-approved alternate for the manufactured home, mobilehome, or commercial modular foundation system.

(D) The manufactured home, mobilehome, or commercial modular manufacturer's installation instructions, or plans and specifications signed by a California-licensed architect or engineer covering the installation of an individual manufactured home, mobilehome, or commercial modular in the absence of the manufactured home, mobilehome, or commercial modular manufacturer's instructions.

(E) Building permit fees established by ordinance or regulation of the appropriate enforcement agency.

(F) A fee payable to the department in the amount of eleven dollars ($11) for each transportable section of the manufactured home, mobilehome, or commercial modular, that shall be transmitted to the department at the time the certificate of occupancy is issued with a copy of the building permit and any other information concerning the manufactured home, mobilehome, or commercial modular that the department may prescribe on forms provided by the department.

(2) (A) Within five business days of the issuance of the certificate of occupancy for the manufactured home, mobilehome, or commercial modular by the appropriate enforcement agency, the enforcement agency shall record a document naming the owner of the real property, describing the real property with certainty, and stating that a manufactured home, mobilehome, or commercial modular has been affixed to that real property by installation on a foundation system pursuant to this subdivision. The document shall be recorded with the county recorder of the county where the real property, upon which the manufactured home, mobilehome, or commercial modular that has been installed, is situated.

(B) When recorded, the document referred to in subparagraph (A) shall be indexed by the county recorder to the named owner and shall be deemed to give constructive notice as to its contents to all persons thereafter dealing with the real property.

(C) Fees received by the department pursuant to subparagraph (F) of paragraph (1) shall be deposited in the Mobilehome-Manufactured Home Revolving Fund established under subdivision (a) of Section 18016.5.

(3) The certification of title and other indicia of registration shall be surrendered to the department pursuant to regulations adopted by the department providing for the cancellation of registration of a manufactured home, mobilehome, or commercial modular that is permanently attached to the ground on a foundation system pursuant to subdivision (a). For the purposes of this subdivision, permanent affixation to a foundation system shall be deemed to have occurred on the day a certificate of occupancy is issued to the manufactured home, mobilehome, or commercial modular owner and the document referred to in subparagraph (A) of paragraph (2) is recorded. Cancellation shall be effective as of that date and the department shall enter the cancellation on its records upon receipt of a copy of the certificate of occupancy. This subdivision shall not be construed to affect the application of existing laws, or the department's regulations or procedures with regard to the cancellation of registration, except as to the requirement therefor and the effective date thereof.

(4) Once installed on a foundation system in compliance with this subdivision, a manufactured home, mobilehome, or commercial modular shall be deemed a fixture and a real property improvement to the real property to which it is affixed. Physical removal of the manufactured home,

mobilehome, or commercial modular shall thereafter be prohibited without the consent of all persons or entities who, at the time of removal, have title to any estate or interest in the real property to which the manufactured home, mobilehome, or commercial modular is affixed.

(5) For the purposes of this subdivision:

(A) "Physical removal" shall include, without limitation, the unattaching of the manufactured home, mobilehome, or commercial modular from the foundation system, except for temporary purposes of repair or improvement thereto.

(B) Consent to removal shall not be required from the owners of rights-of-way or easements or the owners of subsurface rights or interests in or to minerals, including, but not limited to, oil, gas, or other hydrocarbon substances.

(6) At least 30 days prior to a legal removal of the manufactured home, mobilehome, or commercial modular from the foundation system and transportation away from the real property to which it was formerly affixed, the manufactured home, mobilehome, or commercial modular owner shall notify the department and the county assessor of the intended removal of the manufactured home, mobilehome, or commercial modular. The department shall require written evidence that the necessary consents have been obtained pursuant to this section and shall require application for either a transportation permit or manufactured home, mobilehome, or commercial modular registration, as the department may decide is appropriate to the circumstances. Immediately upon removal, as defined in this section, the manufactured home, mobilehome, or commercial modular shall be deemed to have become personal property and subject to all laws governing the same as applicable to a manufactured home, mobilehome, or commercial modular.

(b) The installation of a manufactured home or a mobilehome on a foundation system as chattel shall be in accordance with Section 18613 and shall be deemed to meet or exceed the requirements of Section 18613.4. This subdivision shall not be construed to affect the application of sales and use or property taxes. No provisions of this subdivision are intended, nor shall they be construed, to affect the ownership interest of any owner of a manufactured home or mobilehome.

(c) Once installed on a foundation system, a manufactured home, mobilehome, or commercial modular shall be subject to state-enforced health and safety standards for manufactured homes, mobilehomes, or commercial modulars enforced pursuant to Section 18020.

(d) No local agency shall require that any manufactured home, mobilehome, or commercial modular currently on private property be placed on a foundation system.

(e) No local agency shall require that any manufactured home or mobilehome located in a mobilehome park be placed on a foundation system.

(f) No local agency shall require, as a condition for the approval of the conversion of a rental mobilehome park to a resident-owned park, including, but not limited to, a subdivision, cooperative, or condominium for mobilehomes, that any manufactured home or mobilehome located there be placed on a foundation system. This subdivision shall only apply to the conversion of a rental mobilehome park that has been operated as a rental mobilehome park for a minimum period of five years.

O

Assembly Bill No. 625

CHAPTER 159

An act to amend Section 1185 of the Civil Code, relating to notaries public.

[Approved by Governor August 27, 2013. Filed with Secretary of State August 27, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 625, Quirk. Notaries public: acceptance of identification.

Existing law relating to property transfers specifies certain documents as allowable forms of identification for a credible witness, who, by oath or affirmation, attests to the identity of an individual executing a written instrument in the presence of, and acknowledged by, a notary public. Existing law specifies that an inmate identification card that is current or has been issued within 5 years by the Department of Corrections and Rehabilitation if the inmate is in custody is an allowable form of identification, for purposes of these provisions, if it contains certain identifying information, including a photograph and description of the person named on it, is signed by the person, and has a serial or other identifying number.

This bill would recast those provisions to make an inmate identification card that is current or has been issued within 5 years by the department, if the inmate is in custody in prison, an allowable form of identification for a credible witness to prove the identity of an individual who executes a written instrument, and to delete the requirement that the card have the additional identifying information.

The people of the State of California do enact as follows:

SECTION 1. The Legislature finds and declares the following:

(a) The state and its counties have a financial and public safety interest in ensuring the children of people convicted of felonies and sentenced to state prison time have access to appropriate schooling and medical treatment. Eighty percent of imprisoned women are mothers and the vast majority were the primary care provider of minor children at the time of their arrest and imprisonment. These minor children's access to school and medical treatment may be unnecessarily interrupted should their incarcerated parent lack timely and affordable access to a notary necessary for them to complete paperwork to establish temporary guardianship for their children.

(b) The state and its counties have a financial and public safety interest in ensuring people convicted of felonies and sentenced to state prison time are able to successfully reenter their communities upon completion of their sentences and live a crime-free life. Evidence-based research demonstrates a clear connection between decreased recidivism rates and strength of familial bonds during periods of incarceration. These bonds are weakened when minor children are unnecessarily prevented from visiting incarcerated parents due merely to the incarcerated parents' lack of timely and affordable access to a notary public required to complete required visitation forms.

(c) The state has taken significant measures to ensure due process and accuracy in determining the identity of people convicted of felonies and held in control of the Department of Corrections and Rehabilitation, and in tracking these individuals' appropriate identity through issuance and monitoring of state inmate identification cards.

SEC. 2. Section 1185 of the Civil Code is amended to read:

1185. (a) The acknowledgment of an instrument shall not be taken unless the officer taking it has satisfactory evidence that the person making the acknowledgment is the individual who is described in and who executed the instrument.

(b) For purposes of this section, "satisfactory evidence" means the absence of information, evidence, or other circumstances that would lead a reasonable person to believe that the person making the acknowledgment is not the individual he or she claims to be and any one of the following:

(1) (A) The oath or affirmation of a credible witness personally known to the officer, whose identity is proven to the officer upon presentation of a document satisfying the requirements of paragraph (3) or (4), that the person making the acknowledgment is personally known to the witness and that each of the following are true:

(i) The person making the acknowledgment is the person named in the document.

(ii) The person making the acknowledgment is personally known to the witness.

(iii) That it is the reasonable belief of the witness that the circumstances of the person making the acknowledgment are such that it would be very difficult or impossible for that person to obtain another form of identification.

(iv) The person making the acknowledgment does not possess any of the identification documents named in paragraphs (3) and (4).

(v) The witness does not have a financial interest in the document being acknowledged and is not named in the document.

(B) A notary public who violates this section by failing to obtain the satisfactory evidence required by subparagraph (A) shall be subject to a civil penalty not exceeding ten thousand dollars ($10,000). An action to impose this civil penalty may be brought by the Secretary of State in an administrative proceeding or a public prosecutor in superior court, and shall be enforced as a civil judgment. A public prosecutor shall inform the secretary of any civil penalty imposed under this subparagraph.

(2) The oath or affirmation under penalty of perjury of two credible witnesses, whose identities are proven to the officer upon the presentation of a document satisfying the requirements of paragraph (3) or (4), that each statement in paragraph (1) is true.

(3) Reasonable reliance on the presentation to the officer of any one of the following, if the document is current or has been issued within five years:

(A) An identification card or driver's license issued by the Department of Motor Vehicles.

(B) A passport issued by the Department of State of the United States.

(C) An inmate identification card issued by the Department of Corrections and Rehabilitation, if the inmate is in custody in prison.

(4) Reasonable reliance on the presentation of any one of the following, provided that a document specified in subparagraphs (A) to (E), inclusive, shall either be current or have been issued within five years and shall contain a photograph and description of the person named on it, shall be signed by the person, shall bear a serial or other identifying number, and, in the event that the document is a passport, shall have been stamped by the United States Citizenship and Immigration Services of the Department of Homeland Security:

(A) A passport issued by a foreign government.

(B) A driver's license issued by a state other than California or by a Canadian or Mexican public agency authorized to issue driver's licenses.

(C) An identification card issued by a state other than California.

(D) An identification card issued by any branch of the Armed Forces of the United States.

(E) An employee identification card issued by an agency or office of the State of California, or by an agency or office of a city, county, or city and county in this state.

(c) An officer who has taken an acknowledgment pursuant to this section shall be presumed to have operated in accordance with the provisions of law.

(d) A party who files an action for damages based on the failure of the officer to establish the proper identity of the person making the acknowledgment shall have the burden of proof in establishing the negligence or misconduct of the officer.

(e) A person convicted of perjury under this section shall forfeit any financial interest in the document.

O

Senate Bill No. 551

CHAPTER 176

An act to amend Sections 683.140 and 699.510 of the Code of Civil Procedure, relating to enforcement of judgments.

[Approved by Governor August 27, 2013. Filed with Secretary of State August 27, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 551, Gaines. Renewal and execution of judgments: judgment debtor.

Existing law provides that the period of enforceability of a money judgment or a judgment for possession or sale of property may be extended by renewal of the judgment upon application by the judgment creditor to the court in which the judgment was entered. Existing law requires that the application for renewal of the judgment be executed under oath and include, along with other items, the name and address of the judgment creditor and the name and last known address of the judgment debtor.

Existing law requires that, after entry of a money judgment, a writ of execution be issued by the clerk of the court upon application by the judgment creditor, and directed to the levying officer in the county where the levy is to be made and to any registered process server. Existing law requires that the writ of execution be issued in the name of the judgment debtor as listed on the judgment.

This bill would require the judgment creditor to omit the name of a judgment debtor from the application for renewal of the judgment and the application for a writ of execution if the liability of that judgment debtor has ceased with regard to the judgment, which would include the judgment debtor obtaining a discharge of the judgment pursuant to specified federal bankruptcy statutes or the judgment creditor filing an acknowledgment of satisfaction of judgment with regard to the judgment debtor, as specified.

The people of the State of California do enact as follows:

SECTION 1. Section 683.140 of the Code of Civil Procedure is amended to read:

683.140. The application for renewal of the judgment shall be executed under oath and shall include all of the following:

(a) The title of the court where the judgment is entered and the cause and number of the action.

(b) The date of entry of the judgment and of any renewals of the judgment and where entered in the records of the court.

(c) The name and address of the judgment creditor and the name and last known address of the judgment debtor. However, the judgment creditor shall omit the name of a judgment debtor from the application for a writ of execution if the liability of that judgment debtor has ceased with regard to the judgment, including either of the following occurrences:

(1) The judgment debtor has obtained a discharge of the judgment pursuant to Title 11 of the United States Code and notice thereof has been filed with the court.

(2) The judgment creditor files an acknowledgment of satisfaction of judgment with regard to the judgment debtor pursuant to Chapter 1 (commencing with Section 724.010) of Division 5.

(d) In the case of a money judgment, the information necessary to compute the amount of the judgment as renewed. In the case of a judgment for possession or sale of property, a description of the performance remaining due.

SEC. 2. Section 699.510 of the Code of Civil Procedure is amended to read:

699.510. (a) Subject to subdivision (b), after entry of a money judgment, a writ of execution shall be issued by the clerk of the court, upon application of the judgment creditor, and shall be directed to the levying officer in the county where the levy is to be made and to any registered process server. The clerk of the court shall give priority to the application for, and issuance of, writs of execution on orders or judgments for child support and spousal support. A separate writ shall be issued for each county where a levy is to be made. Writs may be issued successively until the money judgment is satisfied, except that a new writ may not be issued for a county until the expiration of 180 days after the issuance of a prior writ for that county unless the prior writ is first returned.

(b) If the judgment creditor seeks a writ of execution to enforce a judgment made, entered, or enforceable pursuant to the Family Code, in addition to the requirements of this article, the judgment creditor shall satisfy the requirements of any applicable provisions of the Family Code.

(c) (1) The writ of execution shall be issued in the name of the judgment debtor as listed on the judgment, except that the judgment creditor shall omit the name of a judgment debtor from the application for a writ of execution if the liability of that judgment debtor has ceased with regard to the judgment, including either of the following occurrences:

(A) The judgment debtor has obtained a discharge of the judgment pursuant to Title 11 of the United States Code and notice thereof has been filed with the court.

(B) The judgment creditor files an acknowledgment of satisfaction of judgment with regard to the judgment debtor pursuant to Chapter 1 (commencing with Section 724.010) of Division 5.

(2) The writ of execution shall include the additional name or names, and the type of legal entity, by which the judgment debtor is known, as set forth in the affidavit of identity, as defined in Section 680.135, filed by the judgment creditor with the application for issuance of the writ of execution.

Prior to the clerk of the court issuing a writ of execution containing any additional name or names by which the judgment debtor is known that are not listed on the judgment, the court shall approve the affidavit of identity. If the court determines, without a hearing or a notice, that the affidavit of identity states sufficient facts upon which the judgment creditor has identified the additional names of the judgment debtor, the court shall authorize the issuance of the writ of execution with the additional name or names.

(d) In any case where the writ of execution lists any name other than that listed on the judgment, the person in possession or control of the levied property, if other than the judgment debtor, shall not pay to the levying officer the amount or deliver the property being levied upon until being notified to do so by the levying officer. The levying officer may not require the person, if other than the judgment debtor, in possession or control of the levied property to pay the amount or deliver the property levied upon until the expiration of 15 days after service of notice of levy.

(e) If a person who is not the judgment debtor has property erroneously subject to an enforcement of judgment proceeding based upon an affidavit of identity, the person shall be entitled to the recovery of reasonable attorney's fees and costs from the judgment creditor incurred in releasing the person's property from a writ of execution, in addition to any other damages or penalties to which an aggrieved person may be entitled to by law, including Division 4 (commencing with Section 720.010).

O

Senate Bill No. 692

CHAPTER 219

An act to amend Sections 6588, 53313, 53316.2, 53317, 53328.1, 53340, 53350, and 53363.9 of, and to add Section 53357.1 to, the Government Code, relating to local government.

[Approved by Governor September 6, 2013. Filed with Secretary of State September 6, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 692, Hancock. Local government: community facilities districts.

(1) The Mello-Roos Community Facilities Act of 1982 authorizes the legislative bodies of 2 or more local agencies, at any time prior to the adoption of the resolution of formation creating a community facilities district or a resolution of change to alter a district, or a resolution or resolutions authorizing issuance of bonds, to enter into a joint community facilities agreement or into a joint exercise of powers agreement, pursuant to the Joint Exercise of Powers Act, to exercise any power authorized by the Mello-Roos Community Facilities Act of 1982 with respect to the community facilities district being created or changed if the legislative body of each entity adopts a resolution declaring that the joint agreement would be beneficial to the residents of that entity.

This bill would specify that this authorization is not intended to limit the ability of a joint powers authority created pursuant to the Joint Exercise of Powers Act to exercise powers authorized by the Marks-Roos Local Bond Pooling Act of 1985.

(2) Under the Mello-Roos Community Facilities Act of 1982, after a community facilities district has been created and authorized to levy specified special taxes, the legislative body may, by ordinance, levy the special taxes at the rate and apportion them in the manner specified in the resolution forming the community facilities district. The act also authorizes the annexation of territory to the community facilities district by unanimous approval of the owner or owners following the formation of that district.

This bill would authorize the legislative body, in the case of a community facilities district that includes property proposed to be annexed to the district at a future date by unanimous approval, to, by ordinance, provide for the imposition of special taxes on that property, as specified.

(3) The Mello-Roos Community Facilities Act of 1982 authorizes the legislative body to, by resolution, designate a portion or portions of the district as one or more improvement areas for purposes of the financing of, or contributing to the financing of, specified public facilities, as specified, and following the designation, authorizes all proceedings for purposes of a bond election and for the purpose of levying special taxes for payment of

the bonds, or for any other change, to apply only to the improvement area for those specified facilities.

This bill would authorize the legislative body to designate a parcel or parcels of property included in a community facilities district by unanimous approval, as specified, as an improvement area without additional hearings or procedures, as specified. The bill would specify that following the designation, all proceedings for approval of the appropriations limit, the rate and method of apportionment and manner of collection of special taxes, and the authorization to incur bonded indebtedness for the parcel or parcels applies only within the improvement area.

(4) The Mello-Roos Community Facilities Act of 1982 authorizes the legislative body to incur bonded indebtedness, as specified, and authorizes any refunding bonds issued to be exchanged for the bonds to be refunded on such basis as the legislative body determines is for the benefit of the district. The legislative body is also authorized to sell the refunding bonds at public or private sale, and to place the proceeds of any sale of refunding bonds for cash in the "refunding fund" in the treasury of the local agency. The funds in the "revolving account" are required to be secured and may be invested in accordance with any other laws applicable to the funds of the local agency. Existing law requires the proceeds and investments in the "refunding fund" at the time of issuance of the refunding bonds, as certified by a certified public accountant, to be in an amount sufficient to pay the principal, interest, and redemption premiums, if any, on the refunded bonds as they become due or at designated dates prior to maturity and the designated costs of issuance of the refunding bonds, or to pay the principal, interest, and redemption premiums, if any, on the refunding bonds prior to the maturity of the bonds to be refunded or prior to a designated date or dates before the maturity of the bonds to be refunded, the principal and any redemption premiums due on the refunded bonds at maturity or upon that designated date or dates, and the designated costs of issuance of the refunding bonds.

This bill would, with regard to the proceeds and any other cash in the "refunding fund," require those funds to be held uninvested or invested in noncallable obligations of, or obligations guaranteed as to principal and interest by, the United States of America or any agency or instrumentality thereof, when those obligations are backed by the full faith and credit of the United States of America, and requires those proceeds to be in an amount sufficient to pay the principal, interest, and redemption premiums, if any, on the refunded bonds as they become due or at designated dates prior to maturity, in which case certification of a certified public accountant is not required. The bill would authorize a local agency to execute and record in the office of the county recorder of the county in which a community facilities district is located, a notice of the owner's agreement to disclose certain information and a notice of termination of that obligation, as specified. The bill would subject a subsequent transferee of the property to the disclosure obligation.

(5) The Joint Exercise of Powers Act authorizes the legislative or other governing bodies of 2 or more public agencies to jointly exercise by agreement any power common to the contracting parties, as specified, and authorizes that joint powers authority to exercise various powers, including, among others, the power to take title to, and sell by installment sale or otherwise, lands, structures, real or personal property, rights, rights-of-way, franchises, easements, and other interests in lands that are located within the state that the authority determines are necessary or convenient for the financing of public capital improvements, or any portion thereof.

This bill would additionally authorize the joint powers authority to lease lands, structures, real or personal property, rights, rights-of-way, franchises, easements, and other interests in lands that are located within the state that the authority determines are necessary or convenient for the financing of public capital improvements, or any portion thereof.

(6) The Mello-Roos Community Facilities Act of 1982 authorizes a community facilities district to finance various services, including, but not limited to, police protection services and maintenance and lighting of parks, parkways, streets, roads, and open space.

This bill would also authorize the financing of the maintenance and operation of any real property or other tangible property, with an estimated useful life of 5 years or more, that is owned by the local agency or by another local agency, as specified.

(7) Existing law specifies the requirements for the establishment of a community facilities district, including, among other things, a petition, a hearing, the establishment of the boundaries of the community facilities district, and an election on the question of establishment. Existing law authorizes a separate procedure for establishing a community facilities district where, with the unanimous approval of parcel owners, the district initially consists solely of territory proposed for annexation to the community facilities district in the future, as specified, and, for a district so established, provides for an alternate procedure for establishing a district appropriations limit, applying special taxes, and incurring bonded indebtedness.

This bill would also exclude a legislative body from being obligated to specify in the resolution of intention the conditions under which the obligation to pay the specified special tax may be prepaid and permanently satisfied, and would instead authorize a prepayment provision to be included in the unanimous approval, as specified. The bill would authorize, as an alternate and independent procedure for making changes to authorized facilities and services, the unanimous approval of the owner or owners of the parcel or parcels that will be affected by the change together with the written consent of the local agency, as specified.

The people of the State of California do enact as follows:

SECTION 1. Section 6588 of the Government Code is amended to read:

6588. In addition to other powers specified in an agreement pursuant to Article 1 (commencing with Section 6500) and Article 2 (commencing with Section 6540), the authority may do any or all of the following:

(a) Adopt bylaws for the regulation of its affairs and the conduct of its business.

(b) Sue and be sued in its own name.

(c) Issue bonds, including, at the option of the authority, bonds bearing interest, to pay the cost of any public capital improvement, working capital, or liability or other insurance program. In addition, for any purpose for which an authority may execute and deliver or cause to be executed and delivered certificates of participation in a lease or installment sale agreement with any public or private entity, the authority, at its option, may issue or cause to be issued bonds, rather than certificates of participation, and enter into a loan agreement with the public or private entity.

(d) Engage the services of private consultants to render professional and technical assistance and advice in carrying out the purposes of this article.

(e) As provided by applicable law, employ and compensate bond counsel, financial consultants, and other advisers determined necessary by the authority in connection with the issuance and sale of any bonds.

(f) Contract for engineering, architectural, accounting, or other services determined necessary by the authority for the successful development of a public capital improvement.

(g) Pay the reasonable costs of consulting engineers, architects, accountants, and construction, land-use, recreation, and environmental experts employed by any sponsor or participant if the authority determines those services are necessary for the successful development of public capital improvements.

(h) Take title to, sell by installment sale or otherwise, or lease lands, structures, real or personal property, rights, rights-of-way, franchises, easements, and other interests in lands that are located within the state that the authority determines are necessary or convenient for the financing of public capital improvements, or any portion thereof.

(i) Receive and accept from any source, loans, contributions, or grants, in either money, property, labor, or other things of value, for, or in aid of, the construction financing, or refinancing of public capital improvement, or any portion thereof or for the financing of working capital or insurance programs, or for the payment of the principal of and interest on bonds if the proceeds of those bonds are used for one or more of the purposes specified in this section.

(j) Make secured or unsecured loans to any local agency in connection with the financing of capital improvement projects, working capital or insurance programs in accordance with an agreement between the authority and the local agency. However, no loan shall exceed the total cost of the public capital improvements, working capital or insurance needs of the local agency as determined by the local agency and by the authority.

(k) Make secured or unsecured loans to any local agency in accordance with an agreement between the authority and the local agency to refinance indebtedness incurred by the local agency in connection with public capital improvements undertaken and completed.

(*l*) Mortgage all or any portion of its interest in public capital improvements and the property on which any project is located, whether owned or thereafter acquired, including the granting of a security interest in any property, tangible or intangible.

(m) Assign or pledge all or any portion of its interests in mortgages, deeds of trust, indentures of mortgage or trust, or similar instruments, notes, and security interests in property, tangible or intangible, of a local agency to which the authority has made loans, and the revenues therefrom, including payment or income from any interest owned or held by the authority, for the benefit of the holders of bonds issued to finance public capital improvements. The pledge of moneys, revenues, accounts, contract rights, or rights to payment of any kind made by or to the authority pursuant to the authority granted in this part shall be valid and binding from the time the pledge is made for the benefit of the pledgees and successors thereto, against all parties irrespective of whether the parties have notice of the claim.

(n) Lease the public capital improvements being financed to a local agency, upon terms and conditions that the authority deems proper; charge and collect rents therefor; terminate any lease upon the failure of the lessee to comply with any of the obligations of the lease; include in any lease provisions that the lessee shall have options to renew the lease for a period or periods, and at rents as determined by the authority; purchase or sell by an installment agreement or otherwise any or all of the public capital improvements; or, upon payment of all the indebtedness incurred by the authority for the financing or refinancing of the public capital improvements, the authority may convey any or all of the project to the lessee or lessees.

(o) Charge and apportion to local agencies that benefit from its services the administrative costs and expenses incurred in the exercise of the powers authorized by this article. These fees shall be set at a rate sufficient to recover, but not exceed, the authority's costs of issuance and administration. The fee charged to each local obligation acquired by the pool shall not exceed that obligation's proportionate share of those costs. The level of these fees shall be disclosed to the California Debt and Investment Advisory Commission pursuant to Section 6599.1.

(p) Issue, obtain, or aid in obtaining, from any department or agency of the United States or of the state, or any private company, any insurance or guarantee to, or for, the payment or repayment of interest or principal, or both, or any part thereof, on any loan, lease, or obligation or any instrument evidencing or securing the same, made or entered into pursuant to this article.

(q) Notwithstanding any other provision of this article, enter into any agreement, contract, or any other instrument with respect to any insurance or guarantee; accept payment in the manner and form as provided therein in the event of default by a local agency; and assign any insurance or guarantee that acts as security for the authority's bonds.

(r) Enter into any agreement or contract, execute any instrument, and perform any act or thing necessary, convenient, or desirable to carry out any power authorized by this article.

(s) Invest any moneys held in reserve or sinking funds, or any moneys not required for immediate use or disbursement, in obligations that are authorized by law for the investment of trust funds.

(t) At the request of affected local agencies, combine and pledge revenues to public capital improvements for repayment of one or more series of bonds issued pursuant to this article.

(u) Delegate to any of its individual parties or other responsible individuals the power to act on its behalf subject to its general direction, guidelines, and oversight.

(v) Purchase, with the proceeds of its bonds or its revenue, bonds issued by any local agency at public or negotiated sale. Bonds purchased pursuant to this subdivision may be held by the authority or sold to public or private purchasers at public or negotiated sale, in whole or in part, separately or together with other bonds issued by the authority.

(w) Purchase, with the proceeds of its bonds or its revenue, VLF receivables sold to the authority pursuant to Section 6588.5. VLF receivables so purchased may be pledged to the payment of bonds issued by the authority or may be resold to public or private purchasers at public or negotiated sale, in whole or in part, separately or together with other VLF receivables purchased by the authority.

(x) (1) Purchase, with the proceeds of its bonds or its revenue, Proposition 1A receivables pursuant to Section 6588.6. Proposition 1A receivables so purchased may be pledged to the payment of bonds issued by the authority or may be resold to public or private purchasers at public or negotiated sales, in whole or in part, separately or together with other Proposition 1A receivables purchased by the authority.

(2) (A) All entities subject to a reduction of ad valorem property tax revenues required under Section 100.06 of the Revenue and Taxation Code pursuant to the suspension set forth in Section 100.05 of the Revenue and Taxation Code shall be afforded the opportunity to sell their Proposition 1A receivables to the authority.

(B) If these entities offer Proposition 1A receivables to the authority for purchase and duly authorize the sale of the Proposition 1A receivable pursuant to documentation approved by the authority, the authority shall purchase all Proposition 1A receivables so offered to the extent it can sell bonds therefor. If the authority does not purchase all Proposition 1A receivables offered, it shall purchase a pro rata share of each entity's offered Proposition 1A receivables.

(C) The authority may establish a deadline, no earlier than November 3, 2009, by which these entities shall offer their Proposition 1A receivables for sale to the authority and complete the application required by the authority.

(3) For purposes of meeting costs incurred in performing its duties relative to the purchase and sale of Proposition 1A receivables, the authority shall

be authorized to charge a fee to each entity from which it purchases a Proposition 1A receivable. The fee shall be computed based on the percentage value of the Proposition 1A receivable purchased from each entity, in relation to the value of all Proposition 1A receivables purchased by the authority. The amount of the fee shall be paid from the proceeds of the bonds and shall be included in the principal amount of the bonds.

(4) Terms and conditions of any and all fees and expenses charged by the authority, or those it contracts with, and the terms and conditions of sales of Proposition 1A receivables and bonds issued pursuant to this subdivision, including the terms of optional early redemption provisions, if any, shall be approved by the Treasurer and the Director of Finance, who shall not unreasonably withhold their approval. The aggregate principal amount of all bonds issued pursuant to this subdivision shall not exceed two billion two hundred fifty million dollars ($2,250,000,000), and the rate of interest paid on those bonds shall not exceed 8 percent per annum. The authority shall exercise its best efforts to obtain the lowest cost financing possible. Any and all premium obtained shall be used for either of the following:

(A) Applied to pay the costs of issuance of the bonds.

(B) Deposited in a trust account that is pledged to bondholders and used solely for the payment of interest on, or for repayment of, the bonds.

(5) (A) In connection with any financing backed by Proposition 1A receivables, the Treasurer may retain financial advisors, legal counsel, and other consultants to assist in performing the duties required by this chapter and related to that financing.

(B) Notwithstanding any other law, none of the following shall apply to any agreements entered into by the Treasurer pursuant to subparagraph (A) in connection with any Proposition 1A financing:

(i) Section 11040 of the Government Code.

(ii) Section 10295 of the Public Contract Code.

(iii) Article 3 (commencing with Section 10300) and Article 4 (commencing with Section 10335) of, Chapter 2 of Part 2 of Division 2 of the Public Contract Code, except for the authority of the Department of Finance under Section 10336 of the Public Contract Code to direct a state agency to transmit to it a contract for review, and except for Section 10348.5 of the Public Contract Code.

(C) Any costs incurred by the Treasurer in connection with any Proposition 1A financing shall be reimbursed out of the proceeds of the financing.

(y) Set any other terms and conditions on any purchase or sale pursuant to this section as it deems by resolution to be necessary, appropriate, and in the public interest, in furtherance of the purposes of this article.

SEC. 2. Section 53313 of the Government Code is amended to read:

53313. A community facilities district may be established under this chapter to finance any one or more of the following types of services within an area:

(a) Police protection services, including, but not limited to, criminal justice services. However, criminal justice services shall be limited to providing services for jails, detention facilities, and juvenile halls.

(b) Fire protection and suppression services, and ambulance and paramedic services.

(c) Recreation program services, library services, maintenance services for elementary and secondary schoolsites and structures, and the operation and maintenance of museums and cultural facilities. A special tax may be levied for any of the services specified in this subdivision only upon approval of the registered voters as specified in subdivision (b) of Section 53326. An election to enact a special tax for recreation program services, library services, and the operation and maintenance of museums and cultural facilities may be conducted pursuant to subdivision (c) of Section 53326.

(d) Maintenance and lighting of parks, parkways, streets, roads, and open space.

(e) Flood and storm protection services, including, but not limited to, the operation and maintenance of storm drainage systems, plowing and removal of snow, and sandstorm protection systems.

(f) Services with respect to removal or remedial action for the cleanup of any hazardous substance released or threatened to be released into the environment. As used in this subdivision, the terms “remedial action” and “removal” shall have the meanings set forth in Sections 25322 and 25323, respectively, of the Health and Safety Code, and the term “hazardous substance” shall have the meaning set forth in Section 25281 of the Health and Safety Code. Community facilities districts shall provide the State Department of Health Services and local health and building departments with notification of any cleanup activity pursuant to this subdivision at least 30 days prior to commencement of the activity.

(g) Maintenance and operation of any real property or other tangible property with an estimated useful life of five or more years that is owned by the local agency or by another local agency pursuant to an agreement entered into under Section 53316.2.

A community facilities district tax approved by vote of the landowners of the district may only finance the services authorized in this section to the extent that they are in addition to those provided in the territory of the district before the district was created. The additional services shall not supplant services already available within that territory when the district was created.

Bonds shall not be issued pursuant to this chapter to fund any of the services specified in this section, although bonds may be issued to fund capital facilities to be used in providing these services.

SEC. 3. Section 53316.2 of the Government Code is amended to read:

53316.2. (a) A community facilities district may finance facilities to be owned or operated by a public agency other than the agency that created the district, or services to be provided by a public agency other than the agency that created the district, or any combination, only pursuant to a joint community facilities agreement or a joint exercise of powers agreement adopted pursuant to this section. A joint community facilities agreement or a joint exercise of powers agreement with a state or federal agency shall not be required if the local agency that created the district is the agency that would, in the absence of the district, enter into an agreement with the state or federal agency for the provision of the facilities or services, or if the local agency that created the district enters into a joint agreement with the public agency that would, in the absence of the district, enter into an agreement with the state or federal agency for the provision of the facilities or services.

(b) At any time prior to the adoption of the resolution of formation creating a community facilities district or a resolution of change to alter a district, or a resolution or resolutions authorizing issuance of bonds pursuant to Section 53356, the legislative bodies of two or more local agencies may enter into a joint community facilities agreement pursuant to this section and Sections 53316.4 and 53316.6 or into a joint exercise of powers agreement pursuant to the Joint Exercise of Powers Act (Chapter 5 (commencing with Section 6500) of Division 7 of Title 1) to exercise any power authorized by this chapter with respect to the community facilities district being created or changed if the legislative body of each entity adopts a resolution declaring that the joint agreement would be beneficial to the residents of that entity. This subdivision shall not be construed to limit the ability of a joint powers authority created pursuant to the Joint Exercise of Powers Act to exercise the powers authorized by the Joint Exercise of Powers Act.

(c) Notwithstanding the Joint Exercise of Powers Act, a contracting party may use the proceeds of any special tax or charge levied pursuant to this chapter or, in the case of facilities, of any bonds or other indebtedness issued pursuant to this chapter to provide facilities or services which that contracting party is otherwise authorized by law to provide, even though another contracting party does not have the power to provide those facilities or services.

(d) Notwithstanding subdivision (b), nothing in this section shall prevent entry into or amendment of a joint community facilities agreement or a joint exercise of powers agreement at any time, if the new agreement or amendment is necessary, as determined by the legislative body, for either of the following reasons:

(1) To allow an orderly transition of governmental facilities and finances in the case of any change in governmental organization approved pursuant to the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Division 3 (commencing with Section 56000) of Title 5) or other law governing the reorganization of any agency that is a party to the agreement.

(2) To allow participation in the agreement by a state or federal agency, including, but not limited to, the California Department of Transportation. Participation in an agreement by a state or federal agency is purely optional.

(e) Notwithstanding any other provision of this chapter, no local agency that is party to a joint exercise of powers agreement or joint community facilities agreement shall have primary responsibility for formation of a district, or for an extension of authorized facilities and services or a change in special taxes pursuant to Article 3 (commencing with Section 53330), unless that local agency is one or more of the following:

(1) A city, a county, or a city and county.

(2) An agency created pursuant to a joint powers agreement that is separate from the parties to the agreement, is responsible for the administration of the agreement, and is subject to the notification requirement of Section 6503.5.

(3) An agency that is reasonably expected to have responsibility for providing facilities or services to be financed by a larger share of the proceeds of special taxes and bonds of the district or districts created or changed pursuant to the joint exercise of powers agreement or the joint community facilities agreement than any other local agency.

SEC. 4. Section 53317 of the Government Code is amended to read:

53317. Unless the context otherwise requires, the definitions contained in this article shall govern the construction of this chapter.

(a) "Clerk" means the clerk of the legislative body of a local agency.

(b) "Community facilities district" means a legally constituted governmental entity established pursuant to this chapter for the sole purpose of financing facilities and services.

(c) "Cost" means the expense of constructing or purchasing the public facility and of related land, right-of-way, easements, including incidental expenses, and the cost of providing authorized services, including incidental expenses.

(d) "Debt" means any binding obligation to pay or repay a sum of money, including obligations in the form of bonds, certificates of participation, long-term leases, loans from government agencies, or loans from banks, other financial institutions, private businesses, or individuals, or long-term contracts.

(e) "Incidental expense" includes all of the following:

(1) The cost of planning and designing public facilities to be financed pursuant to this chapter, including the cost of environmental evaluations of those facilities.

(2) The costs associated with the creation of the district, issuance of bonds, determination of the amount of taxes, collection of taxes, payment of taxes, or costs otherwise incurred in order to carry out the authorized purposes of the district.

(3) Any other expenses incidental to the construction, completion, and inspection of the authorized work.

(f) "Landowner" or "owner of land" means any person shown as the owner of land on the last equalized assessment roll or otherwise known to be the owner of the land by the legislative body. The legislative body has no obligation to obtain other information as to the ownership of the land, and its determination of ownership shall be final and conclusive for the purposes of this chapter. A public agency is not a landowner or owner of land for purposes of this chapter, unless one of the following exists:

(1) The land owned by a public agency would be subject to a special tax pursuant to Section 53340.1.

(2) The public agency has acquired the property by purchase or negotiation in connection with foreclosure of a special tax lien and it is intended that the property will be transferred to private ownership.

(3) The public agency states in the proceedings that its land is intended to be transferred to private ownership and provides in the proceedings that its land will be subject to the special tax on the same basis as private property within the district and affirmatively waives any defense based on the fact of public ownership, to any action to foreclose on the property in the event of nonpayment of the special tax.

(4) The land owned by a public agency is within the territory of a military base that is closed or is being closed.

(g) “Legislative body” means the legislative body or governing board of any local agency.

(h) “Local agency” means any city or county, whether general law or chartered, special district, school district, joint powers entity created pursuant to Chapter 5 (commencing with Section 6500) of Division 7 of Title 1, redevelopment agency, or any other municipal corporation, district, or political subdivision of the state.

(i) “Rate” means a single rate of tax or a schedule of rates.

(j) “Services” means the provision of categories of services identified in Section 53313. “Services” includes the performance by employees of functions, operations, maintenance, and repair activities. “Services” does not include activities or facilities identified in Section 53313.5. “Maintenance” shall include replacement, and the creation and funding of a reserve fund to pay for a replacement.

SEC. 5. Section 53328.1 of the Government Code is amended to read:

53328.1. (a) As an alternate and independent procedure for forming a community facilities district, the legislative body may form a community facilities district that initially consists solely of territory proposed for annexation to the community facilities district in the future, with the condition that a parcel or parcels within that territory may be annexed to the community facilities district and subjected to the special tax only with the unanimous approval of the owner or owners of the parcel or parcels at the time that the parcel or parcels are annexed. In that case, the legislative body shall follow the procedures set forth in this article for the formation of a community facilities district, with the following exceptions:

(1) The legislative body shall not be obligated to specify the rate or rates of special tax in the resolution of intention or the resolution of formation, provided that both of the following are met:

(A) The resolution of intention and the resolution of formation include a statement that the rate shall be established in an amount required to finance or refinance the authorized improvements and to pay the district’s administrative expenses.

(B) The maximum rate of special tax applicable to a parcel or parcels shall be specified in the unanimous approval described in this section relating to the parcel or parcels.

(2) The legislative body shall not be obligated to specify in the resolution of intention the conditions under which the obligation to pay the specified special tax may be prepaid and permanently satisfied. Instead, a prepayment provision may be included in the unanimous approval of the owner or owners of each parcel or parcels at the time that the parcel or parcels are annexed to the community facilities district.

(3) In lieu of approval pursuant to an election held in accordance with the procedures set forth in Sections 53326, 53327, 53327.5, and 53328, the appropriations limit for the community facilities district, the applicable rate of the special tax and the method of apportionment and manner of collection of that tax, and the authorization to incur bonded indebtedness for the community facilities district shall be specified and be approved by the unanimous approval of the owner or owners of each parcel or parcels at the time that the parcel or parcels are annexed to the community facilities district. No additional hearings or procedures are required, and the unanimous approval shall be deemed to constitute a unanimous vote in favor of the appropriations limit for the community facilities district, the authorization to levy the special tax on the parcel or parcels, and the authorization to incur bonded indebtedness for the community facilities district.

(4) Notwithstanding Section 53324, this paragraph establishes the applicable protest provisions in the event a local agency forms a community facilities district pursuant to the procedures set forth in this section. If 50 percent or more of the registered voters, or six registered voters, whichever is more, residing within the territory proposed to be annexed to the community facilities district in the future, or if the owners of one-half or more of the area of land proposed to be annexed in the future and not exempt from the special tax, file written protests against establishment of the community facilities district, and protests are not withdrawn so as to reduce the protests to less than a majority, no further proceedings to form the community facilities district shall be undertaken for a period of one year from the date of decision of the legislative body on the issues discussed at the hearing. If the majority protests of the registered voters or of the landowners are only against the furnishing of a specified type or types of facilities or services within the district, or against levying a specified special tax, those types of facilities or services or the specified special tax shall be eliminated from the resolution of formation.

(5) The legislative body shall not record a notice of special tax lien against any parcel or parcels in the community facilities district until the owner or owners of the parcel or parcels have given their unanimous approval of the parcel's or parcels' annexation to the community facilities district, at which time the notice of special tax lien shall be recorded against the parcel or parcels as set forth in Section 53328.3.

(b) Notwithstanding the provisions of Section 53340, after adoption of the resolution of formation for a community facilities district described in subdivision (a), the legislative body may, by ordinance, provide for the levy of the special taxes on parcels that will annex to the community facilities district at the rate or rates to be approved unanimously by the owner or owners of each parcel or parcels to be annexed to the community facilities district and for apportionment and collection of the special taxes in the manner specified in the resolution of formation. No further ordinance shall be required even though no parcels may then have annexed to the community facilities district.

(c) The local agency may bring an action to determine the validity of any special taxes levied pursuant to this chapter and authorized pursuant to the procedures set forth in this section pursuant to Chapter 9 (commencing with Section 860) of Title 10 of Part 2 of the Code of Civil Procedure. Notwithstanding Section 53359, if an action is brought by an interested person pursuant to Section 863 of the Code of Civil Procedure to determine the validity of any special taxes levied against a parcel pursuant to this chapter and authorized pursuant to the procedures set forth in this section, the action shall be brought pursuant to Chapter 9 (commencing with Section 860) of Title 10 of Part 2 of the Code of Civil Procedure, but shall, notwithstanding the time limits specified in Section 860 of the Code of Civil Procedure, be commenced within 15 days after the date on which the notice of special tax lien is recorded against the parcel. Any appeal from a judgment in any action or proceeding described in this subdivision shall be commenced within 30 days after entry of judgment.

(d) A community facilities district formed pursuant to this section may only finance facilities pursuant to subdivision (*l*) of Section 53313.5.

(e) In connection with formation of a community facilities district and annexation of a parcel or parcels to the community facilities district pursuant to this section, and the conduct of an election on the proposition to authorize bonded indebtedness pursuant to the alternate procedures set forth in Section 53355.5, the local agency may, without additional hearings or procedures, designate a parcel or parcels as an improvement area within the community facilities district. After the designation of a parcel or parcels as an improvement area, all proceedings for approval of the appropriations limit, the rate and method of apportionment and manner of collection of special tax and the authorization to incur bonded indebtedness for the parcel or parcels shall apply only to the improvement area.

(f) In connection with a community facilities district formed under this section, as an alternate and independent procedure for making the changes described in Section 53330.7, the changes may be made with the unanimous approval of the owner or owners of the parcel or parcels that will be affected by the change and with the written consent of the local agency. No additional hearings or procedures are required, and the unanimous approval shall be deemed to constitute a unanimous vote in favor of the proposed changes. If the proceeds of a special tax are being used to retire any debt incurred pursuant to this chapter and the unanimous approval relates to the reduction of the special tax rate, the unanimous approval shall recite that the reduction or termination of the special tax will not interfere with the timely retirement of that debt.

SEC. 6. Section 53340 of the Government Code is amended to read:

53340. (a) After a community facilities district has been created and authorized to levy specified special taxes pursuant to Article 2 (commencing with Section 53318), Article 3 (commencing with Section 53330), or Article 3.5 (commencing with Section 53339), the legislative body may, by ordinance, levy the special taxes at the rate and apportion them in the manner specified in the resolution adopted pursuant to Article 2 (commencing with Section 53318), Article 3 (commencing with Section 53330), or Article 3.5 (commencing with Section 53339). After creation of a community facilities district that includes territory proposed for annexation in the future by unanimous approval as described in subdivision (b) of Section 53339.3, the legislative body may, by ordinance, provide for the levy of special taxes on parcels that will be annexed to the community facilities district at the rate or rates to be approved unanimously by the owner or owners of each parcel or parcels to be annexed to the community facilities district and for apportionment and collection of the special taxes in the manner specified in the resolution of formation.

(b) The legislative body may provide, by resolution, for the levy of the special tax in the current tax year or future tax years at the same rate or at a lower rate than the rate provided by the ordinance, if the resolution is adopted and a certified list of all parcels subject to the special tax levy including the amount of the tax to be levied on each parcel for the applicable tax year, is filed by the clerk or other official designated by the legislative body with the county auditor on or before the 10th day of August of that tax year. The clerk or other official designated by the legislative body may file the certified list after the 10th of August but not later than the 21st of August if the clerk or other official obtains prior written consent of the county auditor.

(c) Properties or entities of the state, federal, or local governments shall, except for properties that a local agency is a landowner of within the meaning of subdivision (f) of Section 53317, or except as otherwise provided in Section 53317.3, be exempt from the special tax. No other properties or entities are exempt from the special tax unless the properties or entities are expressly exempted in the resolution of formation to establish a district adopted pursuant to Section 53325.1 or in a resolution of consideration to levy a new special tax or special taxes or to alter the rate or method of apportionment of an existing special tax as provided in Section 53334.

(d) The proceeds of any special tax may only be used to pay, in whole or part, the cost of providing public facilities, services, and incidental expenses pursuant to this chapter.

(e) The special tax shall be collected in the same manner as ordinary ad valorem property taxes are collected and shall be subject to the same penalties and the same procedure, sale, and lien priority in case of delinquency as is provided for ad valorem taxes, unless another procedure has been authorized in the resolution of formation establishing the district and adopted by the legislative body.

(f) (1) Notwithstanding subdivision (e), the legislative body of the district may waive all or any specified portion of the delinquency penalties and redemption penalties if it makes all of the following determinations:

(A) The waivers shall apply only to parcels delinquent at the time of the determination.

(B) The waivers shall be available only with respect to parcels for which all past due and currently due special taxes and all other costs due are paid in full within a limited period of time specified in the determination.

(C) The waivers shall be available only with respect to parcels sold or otherwise transferred to new owners unrelated to the owner responsible for the delinquency.

(D) The waivers are in the best interest of the debtholders.

(2) The charges with penalties to be waived shall be removed from the tax roll pursuant to Section 53356.2 and local administrative procedures, and any distributions made to the district prior to collection pursuant to Chapter 3 (commencing with Section 4701) of Part 8 of Division 1 of the Revenue and Taxation Code shall be repaid by the district prior to granting the waiver.

(g) The tax collector may collect the special tax at intervals as specified in the resolution of formation, including intervals different from the intervals determining when the ordinary ad valorem property taxes are collected. The tax collector may deduct the reasonable administrative costs incurred in collecting the special tax.

(h) All special taxes levied by a community facilities district shall be secured by the lien imposed pursuant to Section 3115.5 of the Streets and Highways Code. This lien shall be a continuing lien and shall secure each levy of special taxes. The lien of the special tax shall continue in force and effect until the special tax obligation is prepaid, permanently satisfied, and canceled in accordance with Section 53344 or until the special tax ceases to be levied by the legislative body in the manner provided in Section 53330.5. If any portion of a parcel is encumbered by a lien pursuant to this chapter, the entirety of the parcel shall be encumbered by that lien.

SEC. 7. Section 53350 of the Government Code is amended to read:

53350. (a) For purposes of financing of, or contributing to the financing of, specified public facilities, the legislative body may by resolution designate a portion or portions of the district as one or more improvement areas. An area shall be known as “Improvement Area No. ____” of “Community Facilities District ____.” After the designation of an improvement area, all proceedings for purposes of a bond election and for the purpose of levying special taxes for payment of the bonds, or for any other change pursuant to Article 3 (commencing with Section 53330), shall apply only to the improvement area for those specified facilities.

(b) In connection with the annexation by unanimous approval to a community facilities district of a parcel that was included in territory proposed for annexation in the future to the community facilities district, as described in Section 53329.6, the local agency may designate a parcel or parcels as an improvement area within the community facilities district.

The designation of a parcel or parcels as an improvement area shall be specified and approved by the unanimous approval of the owner or owners of each parcel or parcels at the time that the parcel or parcels are annexed to the community facilities district. No additional hearings or procedures are required. After the designation of a parcel or parcels as an improvement area, all proceedings for approval of the appropriations limit, the rate and method of apportionment and manner of collection of special taxes, and the authorization to incur bonded indebtedness for the parcel or parcels shall apply only to the improvement area.

SEC. 8. Section 53357.1 is added to the Government Code, to read:

53357.1. (a) In connection with the issuance of bonds in which a property owner agrees, by written consent, to disclose certain information on a continuous basis through the Municipal Securities Rulemaking Board's Electronic Municipal Market Access, or successor information depository, the local agency may execute and record in the office of the county recorder, in which the community facilities district is located, a notice of the owner's disclosure agreement for the purpose of providing notice to a subsequent transferee. The owner's written consent shall be attached to the notice.

(b) A subsequent transferee of the property shall be subject to the disclosure obligation. Upon the termination of the disclosure obligation, the local agency may cause a notice of termination to be recorded with the office of the county recorder in which the original notice was recorded.

(c) Notwithstanding Sections 6103 and 27383, the county recorder may charge an appropriate fee for the expense incurred in recording the notices provided for in this section.

SEC. 9. Section 53363.9 of the Government Code is amended to read:

53363.9. (a) The proceeds and investments in the "refunding fund" shall be in an amount sufficient to meet either the requirements of paragraph (1) or paragraph (2) at the time of issuance of the refunding bonds, as certified by a certified public accountant licensed to practice in this state.

(1) The proceeds and investments, together with any interest or other gain to be derived from any such investment, shall be in an amount sufficient to pay the principal, interest, and redemption premiums, if any, on the refunded bonds as they become due or at designated dates prior to maturity and the designated costs of issuance of the refunding bonds.

(2) The proceeds and investments, together with any interest or other gain to be derived from any such investment, shall be in an amount sufficient to pay the principal, interest, and redemption premiums, if any, on the refunding bonds prior to the maturity of the bonds to be refunded or prior to a designated date or dates before the maturity of the bonds to be refunded, the principal and any redemption premiums due on the refunded bonds at maturity or upon that designated date or dates, and the designated costs of issuance of the refunding bonds.

(b) The proceeds and any other cash in the "refunding fund" shall be held uninvested or shall be invested in noncallable obligations of, or obligations guaranteed as to principal and interest by, the United States of America or any agency or instrumentality thereof, when those obligations are backed by the full faith and credit of the United States of America, and shall be in an amount sufficient to pay the principal, interest, and redemption premiums, if any, on the refunded bonds as they become due or at designated dates prior to maturity, in which case certification of a certified public accountant licensed to practice in this state shall not be required.

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Senate Bill No. 310

CHAPTER 251

An act to add Section 2924.26 to, and to add and repeal Section 2924.25 of, the Civil Code, relating to mortgages.

[Approved by Governor September 6, 2013. Filed with Secretary of State September 6, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 310, Calderon. Mortgages: foreclosure notices: title companies.

Existing law requires a mortgage servicer, mortgagee, trustee, beneficiary, or authorized agent to, among other things, contact the borrower prior to filing a notice of default to explore options for the borrower to avoid foreclosure, as specified. Existing law, until January 1, 2018, prohibits a mortgage servicer, mortgagee, trustee, beneficiary, or authorized agent from recording a notice of default if a foreclosure prevention alternative is approved in writing prior to the recordation of a notice of default under certain circumstances. Existing law, operative January 1, 2018, prohibits a mortgage servicer, trustee, mortgagee, beneficiary, or authorized agent from recording a notice of sale or conducting a trustee's sale while a foreclosure prevention alternative application submitted by the borrower is pending, as specified. Existing law, until January 1, 2018, prohibits a mortgage servicer, trustee, mortgagee, beneficiary, or authorized agent from recording a notice of default, notice of sale, or conducting a trustee's sale while a complete first lien loan modification application submitted by the borrower is pending, as specified. Existing law, until January 1, 2018, authorizes a borrower to bring an action for injunctive relief to enjoin a material violation of certain of these provisions if a trustee's deed of sale has not been recorded.

This bill would exempt a licensed title company or underwritten title company, except when it is acting as a trustee, from liability for a violation of those provisions if it records or causes to record a notice of default or notice of sale at the request of a trustee, substitute trustee, or beneficiary, in good faith and in the normal course of its business activities.

The people of the State of California do enact as follows:

SECTION 1. Section 2924.25 is added to the Civil Code, to read:

2924.25. (a) Unless acting in the capacity of a trustee, a licensed title company or underwritten title company shall not be liable for a violation of Section 2923.5, 2923.55, 2923.6, 2924.11, 2924.18, or 2924.19 if it records or causes to record a notice of default or notice of sale at the request of a trustee, substitute trustee, or beneficiary, in good faith and in the normal course of its business activities.

(b) This section shall remain in effect only until January 1, 2018, and as of that date is repealed, unless a later enacted statute, that is enacted before January 1, 2018, deletes or extends that date.

SEC. 2. Section 2924.26 is added to the Civil Code, to read:

2924.26. (a) Unless acting in the capacity of a trustee, a licensed title company or underwritten title company shall not be liable for a violation of Section 2923.5 or 2924.11 if it records or causes to record a notice of default or notice of sale at the request of a trustee, substitute trustee, or beneficiary, in good faith and in the normal course of its business activities.

(b) This section shall become operative on January 1, 2018.

SEC. 3. Sections 2924.25 and 2924.26 shall not be construed to affect the liability of a trustee, substitute trustee, or beneficiary that requests a licensed title company or underwritten title company to record a notice of default or notice of sale.

CORRECTIONS:
Date—Page 1.

O

Assembly Bill No. 1169

CHAPTER 380

An act to add and repeal Chapter 3.6 (commencing with Section 1785.28) of Title 1.6 of Part 4 of Division 3 of the Civil Code, relating to escrow agent credit.

[Approved by Governor September 27, 2013. Filed with Secretary of State September 27, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 1169, Daly. Escrow agent rating service: escrow agents.

Existing law, the Consumer Credit Reporting Agencies Act, requires every consumer credit reporting agency, upon request and proper identification of any consumer, to allow the consumer to visually inspect all files maintained regarding that consumer at the time of the request. Existing law requires every consumer reporting agency to advise the consumer of the agency's obligation to provide a decoded written version of the file. Existing law grants the consumer the right to request and receive a decoded written version of the file. Existing law requires a consumer credit reporting agency to disclose the recipients of any consumer credit report on the consumer which the consumer credit reporting agency has furnished, as specified.

Under existing law, a consumer credit reporting agency is required to furnish a consumer credit report only under certain circumstances, including in accordance with the written instructions of the consumer to whom it relates. Existing law prohibits a consumer credit reporting agency from making any consumer credit report containing specified information. Existing law requires every consumer credit reporting agency to maintain reasonable procedures designed to avoid disclosing certain information and to limit the furnishing of consumer credit reports to specified purposes. If the completeness or accuracy of any item of information in a consumer's file is disputed by the consumer, existing law requires the consumer credit reporting agency to reinvestigate and record the current status of the disputed information within a specified period of time. Existing law requires each consumer credit reporting agency that compiles and reports items of information that are matters of public record to specify the source from which that information was obtained. Existing law requires a person that procures a consumer credit report for the purpose of reselling the report to take specified actions.

Existing law authorizes any consumer suffering damages as a result of a violation of the Consumer Credit Reporting Agencies Act by any person to bring a court action for damages or injunctive relief, as specified.

This bill would, until January 1, 2017, require an escrow agent rating service, as defined, to comply with the provisions described above. The bill would make an escrow agent rating service subject to the requirements applicable to a reseller of credit information if it acts in that capacity, as specified. The bill would also require an escrow agent rating service to establish policies and procedures to protect the personal information it obtains from escrow agents. The bill would authorize an escrow agent, as defined, who suffers damages as a result of the failure of an escrow agent rating service to comply with these provisions to bring a court action for specified damages.

The people of the State of California do enact as follows:

SECTION 1. Chapter 3.6 (commencing with Section 1785.28) is added to Title 1.6 of Part 4 of Division 3 of the Civil Code, to read:

Chapter 3.6. Escrow Agent Rating Service

1785.28. (a) For the purposes of this section, the following definitions shall apply:

(1) Escrow means any transaction in which one person, for the purpose of effecting the sale, transfer, encumbering, or leasing of real or personal property to another person, delivers any written instrument, money, evidence of title to real or personal property, or other thing of value to a third person to be held by that third person until the happening of a specified event or the performance of a prescribed condition, when it is then to be delivered by that third person to a grantee, grantor, promisee, promisor, obligee, obligor, bailee, bailor, or any agent or employee of any of the latter.

(2) An escrow agent is any of the following:

(A) A natural person who performs escrow services for an entity licensed pursuant to the Escrow Law contained in Division 6 (commencing with Section 17000) of the Financial Code.

(B) A natural person performing escrow services for a title insurer admitted pursuant to Article 3 (commencing with Section 699) of Chapter 1 of Part 2 of Division 1 of the Insurance Code or an underwritten title company licensed pursuant to Article 3.7 (commencing with Section 12389) of Chapter 1 of Part 6 of Division 2 of the Insurance Code.

(C) A natural person performing escrow services for a controlled escrow company, as defined in Section 12340.6 of the Insurance Code.

(D) A natural person licensed pursuant to Division 4 (commencing with Section 10000) of the Business and Professions Code, who performs escrow services, in accordance with Section 17006 of the Financial Code.

(3) An escrow agent rating service is a person or entity that prepares a report, for compensation or in expectation of compensation, for use by a creditor in evaluating the capacity of an escrow agent to perform escrow

services in connection with an extension of credit. An escrow agent rating service does not include either of the following:

(A) A creditor or an employee of a creditor evaluating an escrow agent in connection with an extension of credit by that creditor.

(B) An entity described in paragraph (2) for which a natural person performs escrow services as an employee or an independent contractor.

(4) An escrow agent rating service shall be considered a reseller of credit information within the meaning of Section 1785.22 if it assembles and merges information contained in the database or databases maintained by a consumer credit reporting agency.

(5) "Consumer" also means escrow agent.

(b) An escrow agent rating service shall comply with and be subject to the following sections of this title applicable to a consumer credit reporting agency:

(1) Subdivision (a) of Section 1785.10.

(2) Subdivision (b) of Section 1785.10, limited to the obligation to advise a consumer of his or her right to a decoded written version of a file.

(3) Subdivision (d) of Section 1785.10.

(4) Paragraph (2) of subdivision (a) of Section 1785.11.

(5) Section 1785.13.

(6) Section 1785.14.

(7) Paragraph (1) of subdivision (a) of Section 1785.15, limited to the right to request and receive a decoded written version of the file.

(8) Section 1785.16.

(9) Section 1785.18.

(c) An escrow agent rating service that acts as a reseller of credit information as described in paragraph (4) of subdivision (a) shall comply with and be subject to Section 1785.22.

(d) An escrow agent rating service shall establish policies and procedures reasonably intended to safeguard from theft or misuse any personally identifiable information it obtains from an escrow agent.

(e) An escrow agent who suffers damages as a result of the failure of an escrow agent rating service to comply with subdivision (b), (c), or (d) may bring an action in a court of competent jurisdiction pursuant to Section 1785.31 of the Civil Code.

(f) If an escrow agent rating service is also a consumer credit reporting agency as defined in subdivision (d) of Section 1785.3, nothing in this section shall be construed to suggest that an escrow agent reporting service that is also a consumer credit reporting agency is not otherwise required to comply with other provisions of this title applicable to consumer credit reporting agencies.

(g) Nothing in this section shall be construed to authorize a person, who was not otherwise legally authorized to perform escrow services prior to the effective date of this section, to legally perform escrow services.

(h) Nothing in this section is intended to alter the provisions of Section 17420 of the Financial Code, including the legal authority of an escrow agent to compensate an escrow agent rating service for a report prepared pursuant to paragraph (3) of subdivision (a).

1785.28.6. This chapter shall remain in effect only until January 1, 2017, and as of that date is repealed, unless a later enacted statute, that is enacted before January 1, 2017, deletes or extends that date.

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Senate Bill No. 46

CHAPTER 396

An act to amend Sections 1798.29 and 1798.82 of the Civil Code, relating to personal information.

[Approved by Governor September 27, 2013. Filed with Secretary of State September 27, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 46, Corbett. Personal information: privacy.

Existing law requires any agency, and any person or business conducting business in California, that owns or licenses computerized data that includes personal information, as defined, to disclose in specified ways, any breach of the security of the system or data, as defined, following discovery or notification of the security breach, to any California resident whose unencrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person. Existing law defines "personal information" for these purposes, to include an individual's first name and last name, or first initial and last name, in combination with one or more designated data elements relating to, among other things, social security numbers, driver's license numbers, financial accounts, and medical information.

This bill would revise certain data elements included within the definition of personal information, by adding certain information that would permit access to an online account.

This bill would impose additional requirements on the disclosure of a breach of the security of the system or data in situations where the breach involves personal information that would permit access to an online or email account.

This bill would incorporate additional changes to Section 1798.29 of the Civil Code proposed by AB 1149 that would become operative if this bill and AB 1149 are enacted and this bill is enacted last.

The people of the State of California do enact as follows:

SECTION 1. Section 1798.29 of the Civil Code is amended to read:

1798.29. (a) Any agency that owns or licenses computerized data that includes personal information shall disclose any breach of the security of the system following discovery or notification of the breach in the security of the data to any resident of California whose unencrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person. The disclosure shall be made in the most expedient time possible and without unreasonable delay, consistent with the legitimate needs of law enforcement, as provided in subdivision (c), or any measures necessary to determine the scope of the breach and restore the reasonable integrity of the data system.

(b) Any agency that maintains computerized data that includes personal information that the agency does not own shall notify the owner or licensee of the information of any breach of the security of the data immediately following discovery, if the personal information was, or is reasonably believed to have been, acquired by an unauthorized person.

(c) The notification required by this section may be delayed if a law enforcement agency determines that the notification will impede a criminal investigation. The notification required by this section shall be made after the law enforcement agency determines that it will not compromise the investigation.

(d) Any agency that is required to issue a security breach notification pursuant to this section shall meet all of the following requirements:

(1) The security breach notification shall be written in plain language.

(2) The security breach notification shall include, at a minimum, the following information:

(A) The name and contact information of the reporting agency subject to this section.

(B) A list of the types of personal information that were or are reasonably believed to have been the subject of a breach.

(C) If the information is possible to determine at the time the notice is provided, then any of the following: (i) the date of the breach, (ii) the estimated date of the breach, or (iii) the date range within which the breach occurred. The notification shall also include the date of the notice.

(D) Whether the notification was delayed as a result of a law enforcement investigation, if that information is possible to determine at the time the notice is provided.

(E) A general description of the breach incident, if that information is possible to determine at the time the notice is provided.

(F) The toll-free telephone numbers and addresses of the major credit reporting agencies, if the breach exposed a social security number or a driver’s license or California identification card number.

(3) At the discretion of the agency, the security breach notification may also include any of the following:

(A) Information about what the agency has done to protect individuals whose information has been breached.

(B) Advice on steps that the person whose information has been breached may take to protect himself or herself.

(4) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (g) for an online account, and no other personal information defined in paragraph (1) of subdivision (g), the agency may comply with this section by providing the security breach notification in electronic or other form that directs the person whose personal information has been breached to promptly change his or her

password and security question or answer, as applicable, or to take other steps appropriate to protect the online account with the agency and all other online accounts for which the person uses the same user name or email address and password or security question or answer.

(5) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (g) for login credentials of an email account furnished by the agency, the agency shall not comply with this section by providing the security breach notification to that email address, but may, instead, comply with this section by providing notice by another method described in subdivision (i) or by clear and conspicuous notice delivered to the resident online when the resident is connected to the online account from an Internet Protocol address or online location from which the agency knows the resident customarily accesses the account.

(e) Any agency that is required to issue a security breach notification pursuant to this section to more than 500 California residents as a result of a single breach of the security system shall electronically submit a single sample copy of that security breach notification, excluding any personally identifiable information, to the Attorney General. A single sample copy of a security breach notification shall not be deemed to be within subdivision (f) of Section 6254 of the Government Code.

(f) For purposes of this section, “breach of the security of the system” means unauthorized acquisition of computerized data that compromises the security, confidentiality, or integrity of personal information maintained by the agency. Good faith acquisition of personal information by an employee or agent of the agency for the purposes of the agency is not a breach of the security of the system, provided that the personal information is not used or subject to further unauthorized disclosure.

(g) For purposes of this section, “personal information” means either of the following:

(1) An individual’s first name or first initial and last name in combination with any one or more of the following data elements, when either the name or the data elements are not encrypted:

(A) Social security number.

(B) Driver’s license number or California identification card number.

(C) Account number, credit or debit card number, in combination with any required security code, access code, or password that would permit access to an individual’s financial account.

(D) Medical information.

(E) Health insurance information.

(2) A user name or email address, in combination with a password or security question and answer that would permit access to an online account.

(h) (1) For purposes of this section, “personal information” does not include publicly available information that is lawfully made available to the general public from federal, state, or local government records.

(2) For purposes of this section, “medical information” means any information regarding an individual’s medical history, mental or physical condition, or medical treatment or diagnosis by a health care professional.

(3) For purposes of this section, “health insurance information” means an individual’s health insurance policy number or subscriber identification number, any unique identifier used by a health insurer to identify the individual, or any information in an individual’s application and claims history, including any appeals records.

(i) For purposes of this section, “notice” may be provided by one of the following methods:

(1) Written notice.

(2) Electronic notice, if the notice provided is consistent with the provisions regarding electronic records and signatures set forth in Section 7001 of Title 15 of the United States Code.

(3) Substitute notice, if the agency demonstrates that the cost of providing notice would exceed two hundred fifty thousand dollars ($250,000), or that the affected class of subject persons to be notified exceeds 500,000, or the agency does not have sufficient contact information. Substitute notice shall consist of all of the following:

(A) Email notice when the agency has an email address for the subject persons.

(B) Conspicuous posting of the notice on the agency’s Internet Web site page, if the agency maintains one.

(C) Notification to major statewide media and the Office of Information Security within the Department of Technology.

(j) Notwithstanding subdivision (i), an agency that maintains its own notification procedures as part of an information security policy for the treatment of personal information and is otherwise consistent with the timing requirements of this part shall be deemed to be in compliance with the notification requirements of this section if it notifies subject persons in accordance with its policies in the event of a breach of security of the system.

SEC. 1.5. Section 1798.29 of the Civil Code is amended to read:

1798.29. (a) Any agency that owns or licenses computerized data that includes personal information shall disclose any breach of the security of the system following discovery or notification of the breach in the security of the data to any resident of California whose unencrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person. The disclosure shall be made in the most expedient time possible and without unreasonable delay, consistent with the legitimate needs of law enforcement, as provided in subdivision (c), or any measures necessary to determine the scope of the breach and restore the reasonable integrity of the data system.

(b) Any agency that maintains computerized data that includes personal information that the agency does not own shall notify the owner or licensee of the information of any breach of the security of the data immediately following discovery, if the personal information was, or is reasonably believed to have been, acquired by an unauthorized person.

(c) The notification required by this section may be delayed if a law enforcement agency determines that the notification will impede a criminal investigation. The notification required by this section shall be made after the law enforcement agency determines that it will not compromise the investigation.

(d) Any agency that is required to issue a security breach notification pursuant to this section shall meet all of the following requirements:

(1) The security breach notification shall be written in plain language.

(2) The security breach notification shall include, at a minimum, the following information:

(A) The name and contact information of the reporting agency subject to this section.

(B) A list of the types of personal information that were or are reasonably believed to have been the subject of a breach.

(C) If the information is possible to determine at the time the notice is provided, then any of the following: (i) the date of the breach, (ii) the estimated date of the breach, or (iii) the date range within which the breach occurred. The notification shall also include the date of the notice.

(D) Whether the notification was delayed as a result of a law enforcement investigation, if that information is possible to determine at the time the notice is provided.

(E) A general description of the breach incident, if that information is possible to determine at the time the notice is provided.

(F) The toll-free telephone numbers and addresses of the major credit reporting agencies, if the breach exposed a social security number or a driver's license or California identification card number.

(3) At the discretion of the agency, the security breach notification may also include any of the following:

(A) Information about what the agency has done to protect individuals whose information has been breached.

(B) Advice on steps that the person whose information has been breached may take to protect himself or herself.

(4) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (g) for an online account, and no other personal information defined in paragraph (1) of subdivision (g), the agency may comply with this section by providing the security breach notification in electronic or other form that directs the person whose personal information has been breached to promptly change his or her password and security question or answer, as applicable, or to take other steps appropriate to protect the online account with the agency and all other online accounts for which the person uses the same user name or email address and password or security question or answer.

(5) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (g) for login credentials of an email account furnished by the agency, the agency shall not comply with this section by providing the security breach notification to that email address, but may, instead, comply with this section by providing notice by another method described in subdivision (i) or by clear and conspicuous notice delivered to the resident online when the resident is connected to the

online account from an Internet Protocol address or online location from which the agency knows the resident customarily accesses the account.

(e) Any agency that is required to issue a security breach notification pursuant to this section to more than 500 California residents as a result of a single breach of the security system shall electronically submit a single sample copy of that security breach notification, excluding any personally identifiable information, to the Attorney General. A single sample copy of a security breach notification shall not be deemed to be within subdivision (f) of Section 6254 of the Government Code.

(f) For purposes of this section, “breach of the security of the system” means unauthorized acquisition of computerized data that compromises the security, confidentiality, or integrity of personal information maintained by the agency. Good faith acquisition of personal information by an employee or agent of the agency for the purposes of the agency is not a breach of the security of the system, provided that the personal information is not used or subject to further unauthorized disclosure.

(g) For purposes of this section, “personal information” means either of the following:

(1) An individual’s first name or first initial and last name in combination with any one or more of the following data elements, when either the name or the data elements are not encrypted:

(A) Social security number.

(B) Driver’s license number or California identification card number.

(C) Account number, credit or debit card number, in combination with any required security code, access code, or password that would permit access to an individual’s financial account.

(D) Medical information.

(E) Health insurance information.

(2) A user name or email address, in combination with a password or security question and answer that would permit access to an online account.

(h) (1) For purposes of this section, “personal information” does not include publicly available information that is lawfully made available to the general public from federal, state, or local government records.

(2) For purposes of this section, “medical information” means any information regarding an individual’s medical history, mental or physical condition, or medical treatment or diagnosis by a health care professional.

(3) For purposes of this section, “health insurance information” means an individual’s health insurance policy number or subscriber identification number, any unique identifier used by a health insurer to identify the individual, or any information in an individual’s application and claims history, including any appeals records.

(i) For purposes of this section, “notice” may be provided by one of the following methods:

(1) Written notice.

(2) Electronic notice, if the notice provided is consistent with the provisions regarding electronic records and signatures set forth in Section 7001 of Title 15 of the United States Code.

(3) Substitute notice, if the agency demonstrates that the cost of providing notice would exceed two hundred fifty thousand dollars ($250,000), or that the affected class of subject persons to be notified exceeds 500,000, or the agency does not have sufficient contact information. Substitute notice shall consist of all of the following:

(A) Email notice when the agency has an email address for the subject persons.

(B) Conspicuous posting of the notice on the agency's Internet Web site page, if the agency maintains one.

(C) Notification to major statewide media and the Office of Information Security within the Department of Technology.

(j) Notwithstanding subdivision (i), an agency that maintains its own notification procedures as part of an information security policy for the treatment of personal information and is otherwise consistent with the timing requirements of this part shall be deemed to be in compliance with the notification requirements of this section if it notifies subject persons in accordance with its policies in the event of a breach of security of the system.

(k) Notwithstanding the exception specified in paragraph (4) of subdivision (b) of Section 1798.3, for purposes of this section, "agency" includes a local agency, as defined in subdivision (a) of Section 6252 of the Government Code.

SEC. 2. Section 1798.82 of the Civil Code is amended to read:

1798.82. (a) Any person or business that conducts business in California, and that owns or licenses computerized data that includes personal information, shall disclose any breach of the security of the system following discovery or notification of the breach in the security of the data to any resident of California whose unencrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person. The disclosure shall be made in the most expedient time possible and without unreasonable delay, consistent with the legitimate needs of law enforcement, as provided in subdivision (c), or any measures necessary to determine the scope of the breach and restore the reasonable integrity of the data system.

(b) Any person or business that maintains computerized data that includes personal information that the person or business does not own shall notify the owner or licensee of the information of any breach of the security of the data immediately following discovery, if the personal information was, or is reasonably believed to have been, acquired by an unauthorized person.

(c) The notification required by this section may be delayed if a law enforcement agency determines that the notification will impede a criminal investigation. The notification required by this section shall be made after the law enforcement agency determines that it will not compromise the investigation.

(d) Any person or business that is required to issue a security breach notification pursuant to this section shall meet all of the following requirements:

(1) The security breach notification shall be written in plain language.

(2) The security breach notification shall include, at a minimum, the following information:

(A) The name and contact information of the reporting person or business subject to this section.

(B) A list of the types of personal information that were or are reasonably believed to have been the subject of a breach.

(C) If the information is possible to determine at the time the notice is provided, then any of the following: (i) the date of the breach, (ii) the estimated date of the breach, or (iii) the date range within which the breach occurred. The notification shall also include the date of the notice.

(D) Whether notification was delayed as a result of a law enforcement investigation, if that information is possible to determine at the time the notice is provided.

(E) A general description of the breach incident, if that information is possible to determine at the time the notice is provided.

(F) The toll-free telephone numbers and addresses of the major credit reporting agencies if the breach exposed a social security number or a driver's license or California identification card number.

(3) At the discretion of the person or business, the security breach notification may also include any of the following:

(A) Information about what the person or business has done to protect individuals whose information has been breached.

(B) Advice on steps that the person whose information has been breached may take to protect himself or herself.

(4) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (h) for an online account, and no other personal information defined in paragraph (1) of subdivision (h), the person or business may comply with this section by providing the security breach notification in electronic or other form that directs the person whose personal information has been breached promptly to change his or her password and security question or answer, as applicable, or to take other steps appropriate to protect the online account with the person or business and all other online accounts for which the person whose personal information has been breached uses the same user name or email address and password or security question or answer.

(5) In the case of a breach of the security of the system involving personal information defined in paragraph (2) of subdivision (h) for login credentials of an email account furnished by the person or business, the person or business shall not comply with this section by providing the security breach notification to that email address, but may, instead, comply with this section by providing notice by another method described in subdivision (j) or by clear and conspicuous notice delivered to the resident online when the resident is connected to the online account from an Internet Protocol address or online location from which the person or business knows the resident customarily accesses the account.

(e) A covered entity under the federal Health Insurance Portability and Accountability Act of 1996 (42 U.S.C. Sec. 1320d et seq.) will be deemed to have complied with the notice requirements in subdivision (d) if it has complied completely with Section 13402(f) of the federal Health Information Technology for Economic and Clinical Health Act (Public Law 111-5). However, nothing in this subdivision shall be construed to exempt a covered entity from any other provision of this section.

(f) Any person or business that is required to issue a security breach notification pursuant to this section to more than 500 California residents as a result of a single breach of the security system shall electronically submit a single sample copy of that security breach notification, excluding any personally identifiable information, to the Attorney General. A single sample copy of a security breach notification shall not be deemed to be within subdivision (f) of Section 6254 of the Government Code.

(g) For purposes of this section, "breach of the security of the system" means unauthorized acquisition of computerized data that compromises the security, confidentiality, or integrity of personal information maintained by the person or business. Good faith acquisition of personal information by an employee or agent of the person or business for the purposes of the person or business is not a breach of the security of the system, provided that the personal information is not used or subject to further unauthorized disclosure.

(h) For purposes of this section, "personal information" means either of the following:

(1) An individual's first name or first initial and last name in combination with any one or more of the following data elements, when either the name or the data elements are not encrypted:

(A) Social security number.

(B) Driver's license number or California identification card number.

(C) Account number, credit or debit card number, in combination with any required security code, access code, or password that would permit access to an individual's financial account.

(D) Medical information.

(E) Health insurance information.

(2) A user name or email address, in combination with a password or security question and answer that would permit access to an online account.

(i) (1) For purposes of this section, "personal information" does not include publicly available information that is lawfully made available to the general public from federal, state, or local government records.

(2) For purposes of this section, "medical information" means any information regarding an individual's medical history, mental or physical condition, or medical treatment or diagnosis by a health care professional.

(3) For purposes of this section, "health insurance information" means an individual's health insurance policy number or subscriber identification number, any unique identifier used by a health insurer to identify the individual, or any information in an individual's application and claims history, including any appeals records.

(j) For purposes of this section, "notice" may be provided by one of the following methods:

(1) Written notice.

(2) Electronic notice, if the notice provided is consistent with the provisions regarding electronic records and signatures set forth in Section 7001 of Title 15 of the United States Code.

(3) Substitute notice, if the person or business demonstrates that the cost of providing notice would exceed two hundred fifty thousand dollars ($250,000), or that the affected class of subject persons to be notified exceeds 500,000, or the person or business does not have sufficient contact information. Substitute notice shall consist of all of the following:

(A) Email notice when the person or business has an email address for the subject persons.

(B) Conspicuous posting of the notice on the Internet Web site page of the person or business, if the person or business maintains one.

(C) Notification to major statewide media.

(k) Notwithstanding subdivision (j), a person or business that maintains its own notification procedures as part of an information security policy for the treatment of personal information and is otherwise consistent with the timing requirements of this part, shall be deemed to be in compliance with the notification requirements of this section if the person or business notifies subject persons in accordance with its policies in the event of a breach of security of the system.

SEC. 3. Section 1.5 of this bill incorporates amendments to Section 1798.29 of the Civil Code proposed by both this bill and Assembly Bill 1149. It shall only become operative if (1) both bills are enacted and become effective on or before January 1, 2014, (2) each bill amends Section 1798.29 of the Civil Code, and (3) this bill is enacted after Assembly Bill 1149, in which case Section 1 of this bill shall not become operative.

O

Assembly Bill No. 551

CHAPTER 406

An act to add Chapter 6.3 (commencing with Section 51040) to Part 1 of Division 1 of Title 5 of the Government Code, and to amend Section 402.1 of, and to add Section 422.7 to, the Revenue and Taxation Code, relating to local government.

[Approved by Governor September 28, 2013. Filed with Secretary of State September 28, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 551, Ting. Local government: urban agriculture incentive zones.

(1) Existing law, the Williamson Act, authorizes a city or county to enter into 10-year contracts with owners of land devoted to agricultural use, whereby the owners agree to continue using the property for that purpose, and the city or county agrees to value the land accordingly for purposes of property taxation. Existing law authorizes the parties to a Williamson Act contract to mutually agree to rescind a contract under the act in order to simultaneously enter into an open-space easement for a certain period of years.

This bill would enact the Urban Agriculture Incentive Zones Act and would authorize, under specified conditions and until January 1, 2019, a city, county, or city and county and a landowner to enter into a contract to enforceably restrict the use of vacant, unimproved, or otherwise blighted lands for small-scale production of agricultural crops and animal husbandry. The bill would require a contract entered into pursuant to these provisions to, among other things, be for a term of no less than 5 years and to enforceably restrict property that is at least 0.10 acres in size.

(2) Existing law requires the county assessor to consider, when valuing real property for property taxation purposes, the effect of any enforceable restrictions to which the use of the land may be subjected. Under existing law these restrictions include, but are not limited to, zoning, recorded contracts with governmental agencies, and various other restrictions imposed by governments.

This bill would require the county assessor to value property that is enforceably restricted by a contract entered into pursuant to the Urban Agriculture Incentive Zones Act at the rate based on the average per-acre value of irrigated cropland in California, adjusted proportionally to reflect the acreage of the property under contract, as most recently published by the National Agricultural Statistics Service of the United States Department of Agriculture. The bill would also require the State Board of Equalization to post the per-acre land value as published by the National Agricultural Statistics Service of the United States Department of Agriculture on its

Internet Web site within 30 days of publication, and to provide the rate to county assessors no later than January 1 of each assessment year.

The people of the State of California do enact as follows:

SECTION 1. Chapter 6.3 (commencing with Section 51040) is added to Part 1 of Division 1 of Title 5 of the Government Code, to read:

Chapter 6.3. Urban Agriculture Incentive Zones

51040. This chapter shall be known, and may be cited, as the Urban Agriculture Incentive Zones Act.

51040.1. The Legislature finds and declares that it is in the public interest to promote sustainable urban farm enterprise sectors in urban centers.

The Legislature further finds and declares the small-scale, active production of marketable crops and animal husbandry, including, but not limited to, foods, flowers, and seedlings, in urban centers is consistent with, and furthers, the purposes of this act.

51040.3. For purposes of this chapter, the following terms have the following meanings:

(a) "Urban" means an area within the boundaries of an urbanized area, as that term is used by the United States Census Bureau, that includes at least 250,000 people.

(b) "Urban Agriculture Incentive Zone" means an area within a county or a city and county that is comprised of individual properties designated as urban agriculture preserves by the county or the city and county for farming purposes.

(c) "Agricultural use" means farming in all its branches including, but not limited to, the cultivation and tillage of the soil, the production, cultivation, growing, and harvesting of any agricultural or horticultural products, the raising of livestock, bees, fur-bearing animals, dairy-producing animals, and poultry, agricultural education, the sale of produce through field retail stands or farms stands as defined by Article 5 (commencing with Section 47030) of Chapter 10.5 of Division 17 of the Food and Agricultural Code, and any practices performed by a farmer or on a farm as an incident to or in conjunction with farming operations. For purposes of this chapter, the term "agricultural use" does not include timber production.

51042. (a) (1) (A) A county or city and county may, after a public hearing, establish by ordinance an Urban Agriculture Incentive Zone within its boundaries for the purpose of entering into enforceable contracts with landowners, on a voluntary basis, for the use of vacant, unimproved, or blighted lands for small-scale agricultural use.

(B) A city may, after a public hearing and approval from the board of supervisors of the county in which the city is located, establish by ordinance an Urban Agriculture Incentive Zone within its boundaries for the purpose of entering into enforceable contracts with landowners, on a voluntary basis, for the use of vacant, unimproved, or blighted lands for small-scale agricultural use.

(2) Following the adoption of the ordinance pursuant to paragraph (1), a city, county, or city and county that has established an Urban Agriculture Incentive Zone within its boundaries may adopt rules and regulations consistent with the city, county, or city and county's zoning and other ordinances, for the implementation and administration of the Urban Agriculture Incentive Zone and of contracts related to that Urban Agriculture Incentive Zone.

(A) The city, county, or city and county may impose a fee upon contracting landowners for the reasonable costs of implementing and administering contracts.

(B) The city, county, or city and county shall impose a fee equal to the cumulative value of the tax benefit received during the duration of the contract upon landowners for cancellation of any contract prior to the expiration of the contract, unless the city, county, or city and county makes a determination that the cancellation was caused by extenuating circumstances despite the good faith effort by the landowner.

(b) Following the adoption of the ordinance as required by subdivision (a), a city, county, or a city and county may enter into a contract with a landowner to enforceably restrict the use of the land subject to the contract to uses consistent with urban agriculture. Any contract entered into pursuant to this chapter shall include, but is not limited to, all of the following provisions:

(1) An initial term of not less than five years.

(2) A restriction on property that is at least 0.10 acres, and not more than three acres.

(3) A requirement that the entire property subject to the contract shall be dedicated toward commercial or noncommercial agricultural use.

(4) A prohibition against any dwellings on the property while under contract.

(5) A notification that if a landowner cancels a contract, a city, county, or city and county is required to assess a cancellation fee, pursuant to subparagraph (B) of paragraph (2) of subdivision (a).

(c) A contract entered into pursuant to this chapter shall not prohibit the use of structures that support agricultural activity, including, but not limited to, toolsheds, greenhouses, produce stands, and instructional space.

(d) A contract entered into pursuant to this chapter that includes a prohibition on the use of pesticide or fertilizers on properties under contract shall permit those pesticides or fertilizers allowed by the United States Department of Agriculture's National Organic Program.

(e) A city, county, or city and county shall not enter into a new contract, or renew an existing contract pursuant to this chapter after January 1, 2019. Any contract entered into pursuant to this chapter on or before January 1, 2019, shall be valid and enforceable for the duration of the contract.

(f) Property subject to a contract entered into pursuant to this chapter shall be assessed pursuant to Section 422.7 of the Revenue and Taxation Code during the term of the contract.

(g) A county or a city and county shall not establish an Urban Agriculture Incentive Zone within any portion of the spheres of influence of a city unless the legislative body of the city has consented to the establishment of the Urban Agriculture Incentive Zone.

(h) A city, county, or city and county shall not establish an Urban Agriculture Incentive Zone in any area that is currently subject to, or has been subject to within the previous three years, a contract pursuant to the Williamson Act (Article 1 (commencing with Section 51200) of Chapter 7 of Part 1 of Division 1 of Title 5).

SEC. 2. Section 402.1 of the Revenue and Taxation Code is amended to read:

402.1. (a) In the assessment of land, the assessor shall consider the effect upon value of any enforceable restrictions to which the use of the land may be subjected. These restrictions shall include, but are not limited to, all of the following:

(1) Zoning.

(2) Recorded contracts with governmental agencies other than those provided in Sections 422, 422.5, and 422.7.

(3) Permit authority of, and permits issued by, governmental agencies exercising land use powers concurrently with local governments, including the California Coastal Commission and regional coastal commissions, the San Francisco Bay Conservation and Development Commission, and the Tahoe Regional Planning Agency.

(4) Development controls of a local government in accordance with any local coastal program certified pursuant to Division 20 (commencing with Section 30000) of the Public Resources Code.

(5) Development controls of a local government in accordance with a local protection program, or any component thereof, certified pursuant to Division 19 (commencing with Section 29000) of the Public Resources Code.

(6) Environmental constraints applied to the use of land pursuant to provisions of statutes.

(7) Hazardous waste land use restriction pursuant to Section 25240 of the Health and Safety Code.

(8) A recorded conservation, trail, or scenic easement, as described in Section 815.1 of the Civil Code, that is granted in favor of a public agency, or in favor of a nonprofit corporation organized pursuant to Section 501(c)(3) of the Internal Revenue Code that has as its primary purpose the preservation, protection, or enhancement of land in its natural, scenic, historical, agricultural, forested, or open-space condition or use.

(9) A solar-use easement pursuant to Chapter 6.9 (commencing with Section 51190) of Part 1 of Division 1 of Title 5 of the Government Code.

(b) There is a rebuttable presumption that restrictions will not be removed or substantially modified in the predictable future and that they will substantially equate the value of the land to the value attributable to the legally permissible use or uses.

(c) Grounds for rebutting the presumption may include, but are not necessarily limited to, the past history of like use restrictions in the jurisdiction in question and the similarity of sales prices for restricted and unrestricted land. The possible expiration of a restriction at a time certain shall not be conclusive evidence of the future removal or modification of the restriction unless there is no opportunity or likelihood of the continuation or renewal of the restriction, or unless a necessary party to the restriction has indicated an intent to permit its expiration at that time.

(d) In assessing land with respect to which the presumption is unrebutted, the assessor shall not consider sales of otherwise comparable land not similarly restricted as to use as indicative of value of land under restriction, unless the restrictions have a demonstrably minimal effect upon value.

(e) In assessing land under an enforceable use restriction wherein the presumption of no predictable removal or substantial modification of the restriction has been rebutted, but where the restriction nevertheless retains some future life and has some effect on present value, the assessor may consider, in addition to all other legally permissible information, representative sales of comparable lands that are not under restriction but upon which natural limitations have substantially the same effect as restrictions.

(f) For the purposes of this section the following definitions apply:

(1) "Comparable lands" are lands that are similar to the land being valued in respect to legally permissible uses and physical attributes.

(2) "Representative sales information" is information from sales of a sufficient number of comparable lands to give an accurate indication of the full cash value of the land being valued.

(g) It is hereby declared that the purpose and intent of the Legislature in enacting this section is to provide for a method of determining whether a sufficient amount of representative sales information is available for land under use restriction in order to ensure the accurate assessment of that land. It is also hereby declared that the further purpose and intent of the Legislature in enacting this section and Section 1630 is to avoid an assessment policy which, in the absence of special circumstances, considers uses for land that legally are not available to the owner and not contemplated by government, and that these sections are necessary to implement the public policy of encouraging and maintaining effective land use planning. This statute shall not be construed as requiring the assessment of any land at a value less than as required by Section 401 or as prohibiting the use of representative comparable sales information on land under similar restrictions when this information is available.

SEC. 3. Section 422.7 is added to the Revenue and Taxation Code, to read:

422.7. (a) For purposes of this section, the term "open-space land" includes land subject to contract for an urban agricultural incentive zone, as defined in subdivision (b) of Section 51040.3 of the Government Code.

For purposes of this section, open-space land is enforceably restricted within the meaning of Section 8 of Article XIII of the California Constitution if it is subject to an urban agriculture incentive zone contract.

(b) (1) Open-space land subject to contract for an urban agricultural incentive zone pursuant to Section 52010.3 shall be valued for assessment at the rate based on the average per-acre value of irrigated cropland in California, adjusted proportionally to reflect the acreage of the property under contract, as most recently published by the National Agricultural Statistics Service of the United States Department of Agriculture.

(2) Notwithstanding the published rate, the valuation resulting from the section shall not exceed the lesser of either the valuation that would have resulted by a calculation under Section 110, or the valuation that would have resulted by a valuation under Section 110.1, as though the property was not subject to an enforceable restriction in the base year.

(c) The State Board of Equalization shall post the per-acre land value as published by the National Agricultural Statistics Service of the United States Department of Agriculture on its Internet Web site within 30 days of publication, and shall provide the rate to county assessors no later than January 1 of each assessment year.

O

Senate Bill No. 652

CHAPTER 431

An act to amend Section 1102.6 of the Civil Code, relating to real property.

[Approved by Governor September 30, 2013. Filed with Secretary of State September 30, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 652, DeSaulnier. Real property disclosures: construction defect litigation.

Existing law requires the transferor of residential property to make certain disclosures to a prospective transferee and requires these disclosures to be made on a specified form.

This bill would revise the transfer disclosure form to additionally disclose to a potential transferee specified claims for damages by the seller.

The bill would make its provisions operative on July 1, 2014.

The people of the State of California do enact as follows:

SECTION 1. Section 1102.6 of the Civil Code is amended to read:

1102.6. (a) The disclosures required by this article pertaining to the property proposed to be transferred are set forth in, and shall be made on a copy of, the following disclosure form:

REAL ESTATE TRANSFER DISCLOSURE STATEMENT

THIS DISCLOSURE STATEMENT CONCERNS THE REAL PROPERTY SITUATED IN THE CITY OF ____________, COUNTY OF ______________, STATE OF CALIFORNIA, DESCRIBED AS ____ ____. THIS STATEMENT IS A DISCLOSURE OF THE CONDITION OF THE ABOVE DESCRIBED PROPERTY IN COMPLIANCE WITH SECTION 1102 OF THE CIVIL CODE AS OF ____________________, 20___. IT IS NOT A WARRANTY OF ANY KIND BY THE SELLER(S) OR ANY AGENT(S) REPRESENTING ANY PRINCIPAL(S) IN THIS TRANSACTION, AND IS NOT A SUBSTITUTE FOR ANY INSPECTIONS OR WARRANTIES THE PRINCIPAL(S) MAY WISH TO OBTAIN.

I

COORDINATION WITH OTHER DISCLOSURE FORMS

This Real Estate Transfer Disclosure Statement is made pursuant to Section 1102 of the Civil Code. Other statutes require disclosures, depending upon the details of the particular real estate transaction (for example: special study zone and purchase-money liens on residential property).

Substituted Disclosures: The following disclosures and other disclosures required by law, including the Natural Hazard Disclosure Report/Statement that may include airport annoyances, earthquake, fire, flood, or special assessment information, have or will be made in connection with this real estate transfer, and are intended to satisfy the disclosure obligations on this form, where the subject matter is the same:

☐ Inspection reports completed pursuant to the contract of sale or receipt for deposit.

☐ Additional inspection reports or disclosures:

____

____

____

II

SELLER'S INFORMATION

The Seller discloses the following information with the knowledge that even though this is not a warranty, prospective Buyers may rely on this information in deciding whether and on what terms to purchase the subject property. Seller hereby authorizes any agent(s) representing any principal(s) in this transaction to provide a copy of this statement to any person or entity in connection with any actual or anticipated sale of the property.

THE FOLLOWING ARE REPRESENTATIONS MADE BY THE SELLER(S) AND ARE NOT THE REPRESENTATIONS OF THE AGENT(S), IF ANY. THIS INFORMATION IS A DISCLOSURE AND IS NOT INTENDED TO BE PART OF ANY CONTRACT BETWEEN THE BUYER AND SELLER:

Seller __is __is not occupying the property.

A. The subject property has the items checked below (read across):*

__Range	__Oven	__Microwave
__Dishwasher	__Trash Compactor	__Garbage Disposal
__Washer/Dryer Hookups		__Rain Gutters
__Burglar Alarms	__Carbon Monoxide Device(s)	__Fire Alarm
__TV Antenna		__Intercom
__Central Heating	__Satellite Dish	__Evaporator Cooler(s)
__Wall/Window Air Cndtng.	__Central Air Cndtng.	__Public Sewer System
__Septic Tank	__Sprinklers	__Water Softener
__Patio/Decking	__Sump Pump	__Gazebo
__Sauna	__Built-in Barbecue	
__Hot Tub__Locking Safety Cover	__Pool __Child Resistant Barrier	__Spa__Locking Safety Cover
__Security Gate(s)	__Automatic Garage Door Opener(s)	__Number Remote Controls
Garage:__Attached	__Not Attached	__Carport
Pool/Spa Heater: __Gas	__Solar	__Electric
Water Heater: __Gas		__Private Utility or Other________
Water Supply: __City	__Well	__Water-conserving plumbing fixtures
Gas Supply: __Utility	__Bottled	
__Window Screens	__Window Security Bars__Quick-Release Mechanism on Bedroom Windows	

Exhaust Fan(s) in ________ 220 Volt Wiring in ________ Fireplace(s) in ________
Gas Starter ________ Roof(s): Type: ________ Age: ________ (approx.)
Other: ________

Are there, to the best of your (Seller's) knowledge, any of the above that are not in operating condition? __Yes __No. If yes, then describe.
(Attach additional sheets if necessary): ________

B. Are you (Seller) aware of any significant defects/malfunctions in any of the following? __Yes __No. If yes, check appropriate space(s) below.
__Interior Walls __Ceilings __Floors __Exterior Walls __Insulation __Roof(s) __Windows __Doors __Foundation __Slab(s) __Driveways __Sidewalks __Walls/Fences __Electrical Systems __Plumbing/Sewers/Septics __Other Structural Components (Describe: ________)

If any of the above is checked, explain. (Attach additional sheets if necessary): ________

* Installation of a listed appliance, device, or amenity is not a precondition of sale or transfer of the dwelling. The carbon monoxide device, garage door opener, or child-resistant pool barrier may not be in compliance with the safety standards relating to, respectively, carbon monoxide device standards of Chapter 8 (commencing with Section 13260) of Part 2 of Division 12 of, automatic reversing device standards of Chapter 12.5 (commencing with Section 19890) of Part 3 of Division 13 of, or the pool safety standards of Article 2.5 (commencing with Section 115920) of Chapter 5 of Part 10 of Division 104 of, the Health and Safety Code. Window security bars may not have quick-release mechanisms in compliance with the 1995 edition of the California Building Standards Code. Section 1101.4 of the Civil Code requires all single-family residences built on or before January 1, 1994, to be equipped with water-conserving plumbing fixtures after January 1, 2017. Additionally, on and after January 1, 2014, a single-family residence built on or before January 1, 1994, that is altered or improved is required to be equipped with water-conserving plumbing fixtures as a condition of final approval. Fixtures in this dwelling may not comply with Section 1101.4 of the Civil Code.

C. Are you (Seller) aware of any of the following:

1. Substances, materials, or products which may be an environmental hazard such as, but not limited to, asbestos, formaldehyde, radon gas, lead-based paint, mold, fuel or chemical storage tanks, and contaminated soil or water on the subject property .... __Yes __No
2. Features of the property shared in common with adjoining landowners, such as walls, fences, and driveways, whose use or responsibility for maintenance may have an effect on the subject property .... __Yes __No
3. Any encroachments, easements or similar matters that may affect your interest in the subject property .... __Yes __No
4. Room additions, structural modifications, or other alterations or repairs made without necessary permits .... __Yes __No
5. Room additions, structural modifications, or other alterations or repairs not in compliance with building codes .... __Yes __No
6. Fill (compacted or otherwise) on the property or any portion thereof .... __Yes __No
7. Any settling from any cause, or slippage, sliding, or other soil problems .... __Yes __No
8. Flooding, drainage or grading problems .... __Yes __No
9. Major damage to the property or any of the structures from fire, earthquake, floods, or landslides .... __Yes __No
10. Any zoning violations, nonconforming uses, violations of "setback" requirements .... __Yes __No
11. Neighborhood noise problems or other nuisances .... __Yes __No
12. CC&Rs or other deed restrictions or obligations .... __Yes __No
13. Homeowners' Association which has any authority over the subject property .... __Yes __No
14. Any "common area" (facilities such as pools, tennis courts, walkways, or other areas co-owned in undivided interest with others) .... __Yes __No
15. Any notices of abatement or citations against the property .... __Yes __No
16. Any lawsuits by or against the Seller threatening to or affecting this real property, claims for damages by the Seller pursuant to Section 910 or 914 threatening to or affecting this real property, claims for breach of warranty pursuant to Section 900 threatening to or affecting this real property, or claims for breach of an enhanced protection agreement pursuant to Section 903 threatening to or affecting this real property, including any lawsuits or claims for damages pursuant to Section 910 or 914 alleging a defect or deficiency in this real property or "common areas" (facilities such as pools, tennis courts, walkways, or other areas co-owned in undivided interest with others) .... __Yes __No

If the answer to any of these is yes, explain. (Attach additional sheets if necessary.): ____________________

____

____

D. 1. The Seller certifies that the property, as of the close of escrow, will be in compliance with Section 13113.8 of the Health and Safety Code by having operable smoke detectors(s) which are approved, listed, and installed in accordance with the State Fire Marshal's regulations and applicable local standards.

2. The Seller certifies that the property, as of the close of escrow, will be in compliance with Section 19211 of the Health and Safety Code by having the water heater tank(s) braced, anchored, or strapped in place in accordance with applicable law.

Seller certifies that the information herein is true and correct to the best of the Seller's knowledge as of the date signed by the Seller.

Seller ______________________________ Date ________________
Seller ______________________________ Date ________________

III

AGENT'S INSPECTION DISCLOSURE

(To be completed only if the Seller is represented by an agent in this transaction.)

THE UNDERSIGNED, BASED ON THE ABOVE INQUIRY OF THE SELLER(S) AS TO THE CONDITION OF THE PROPERTY AND BASED ON A REASONABLY COMPETENT AND DILIGENT VISUAL INSPECTION OF THE ACCESSIBLE AREAS OF THE PROPERTY IN CONJUNCTION WITH THAT INQUIRY, STATES THE FOLLOWING:

☐ Agent notes no items for disclosure.

☐ Agent notes the following items:

____
____
____
____

Agent (Broker
Representing Seller) ________________ By ____________ Date ________
(Please Print) (Associate Licensee or Broker Signature)

IV

AGENT'S INSPECTION DISCLOSURE

(To be completed only if the agent who has obtained the offer is other than the agent above.)

THE UNDERSIGNED, BASED ON A REASONABLY COMPETENT AND DILIGENT VISUAL INSPECTION OF THE ACCESSIBLE AREAS OF THE PROPERTY, STATES THE FOLLOWING:

☐ Agent notes no items for disclosure.

☐ Agent notes the following items:

____

____

____

____

Agent (Broker
Obtaining the Offer) ______________________ By ______________ Date __________
(Please Print) (Associate Licensee or Broker Signature)

V

BUYER(S) AND SELLER(S) MAY WISH TO OBTAIN PROFESSIONAL ADVICE AND/OR INSPECTIONS OF THE PROPERTY AND TO PROVIDE FOR APPROPRIATE PROVISIONS IN A CONTRACT BETWEEN BUYER(S) AND SELLER(S) WITH RESPECT TO ANY ADVICE/INSPECTIONS/DEFECTS.

I/WE ACKNOWLEDGE RECEIPT OF A COPY OF THIS STATEMENT.

Seller ________________ Date _________ Buyer________________ Date _________
Seller ________________ Date _________ Buyer________________ Date _________

Agent (Broker
Representing Seller) ______________________ By ______________ Date __________
(Please Print) (Associate Licensee or Broker Signature)

Agent (Broker
Obtaining the Offer) ______________________ By ______________ Date __________
(Please Print) (Associate Licensee or Broker Signature)

SECTION 1102.3 OF THE CIVIL CODE PROVIDES A BUYER WITH THE RIGHT TO RESCIND A PURCHASE CONTRACT FOR AT LEAST THREE DAYS AFTER THE DELIVERY OF THIS DISCLOSURE IF DELIVERY OCCURS AFTER THE SIGNING OF AN OFFER TO PURCHASE. IF YOU WISH TO RESCIND THE CONTRACT, YOU MUST ACT WITHIN THE PRESCRIBED PERIOD.

A REAL ESTATE BROKER IS QUALIFIED TO ADVISE ON REAL ESTATE.
IF YOU DESIRE LEGAL ADVICE, CONSULT YOUR ATTORNEY.

(b) The amendments to this section by the act adding this subdivision shall become operative on July 1, 2014.

O

Assembly Bill No. 253

CHAPTER 432

An act to amend Section 11010.9 of, and to add Section 11010.85 to, the Business and Professions Code, and to amend Sections 66427.4 and 66428.1 of, and to add Section 66427.6 to, the Government Code, relating to floating home marinas.

[Approved by Governor September 30, 2013. Filed with Secretary of State September 30, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 253, Levine. Floating home marinas: conversion: subdivision map requirements.

(1) Existing law, the Subdivision Map Act, generally requires that a tentative and final map shall be required for all subdivisions creating 5 or more condominiums, as defined, with specified exceptions. Existing law requires a subdivider, at the time of filing a tentative or parcel map for a subdivision to be created from the conversion of a mobilehome park to another use, to file a report on the impact of the conversion upon the displaced residents of the mobilehome park to be converted, addressing the availability of adequate replacement space in mobilehome parks. Existing law exempts from these requirements the conversion of a rental mobilehome park to resident ownership, and instead requires a subdivider for that conversion to avoid the economic displacement of nonpurchasing residents, as specified, and file a report on the impact of the conversion upon the displaced residents of the mobilehome park to be converted. Existing law also subjects the subdivider of a rental mobilehome park to resident ownership to a hearing regarding the impact of the conversion upon the displaced residents of the park, and requires the subdivider to offer each existing tenant the option to purchase his or her condominium unit to be created by the conversion.

This bill would extend the same requirements to the conversion of floating home marinas. The bill would require a subdivider, at the time of filing a tentative or parcel map for a subdivision to be created from the conversion of a floating home marina to another use, to file a report on the impact of the conversion upon the displaced residents of the floating home marina to be converted, addressing the availability of adequate replacement space in floating home marinas. The bill would exempt from these requirements the conversion of a rental floating home marina to resident ownership, and would instead require a subdivider for that conversion to avoid the economic displacement of nonpurchasing residents, as specified, and file a report on the impact of the conversion upon the displaced residents of the floating home marina to be converted. The bill would also require the local agency to consider the results of the survey in making its decision to approve, conditionally approve, or disapprove the map, and would authorize the agency to disapprove the map if it finds that the results of the survey have not demonstrated the support of at least a majority of the park's homeowners. The bill would authorize local legislative bodies to enact local regulations to implement the survey requirements. The bill would further subject the subdivider of a rental floating home marina to resident ownership to a hearing regarding the impact of the conversion upon the displaced residents of the marina, and would require the subdivider to offer each existing tenant the option to purchase his or her condominium unit to be created by the conversion.

(2) Existing law exempts mobilehome parks from the requirement of the filing of a tentative and final map for all subdivisions creating 5 or more condominiums, if at least $^2\!/_3$ of the owners of mobilehomes who are tenants have applied, as specified, for a waiver, unless specified conditions exist.

This bill would exempt floating home marinas from the requirement of the filing of a tentative and final map for all subdivisions creating 5 or more condominiums, if at least $^2\!/_3$ of the owners of floating homes who are tenants have applied, as specified, for a waiver, unless specified conditions exist.

(3) Existing law, the Subdivided Lands Act, requires any person who intends to offer subdivided lands for sale or lease, as specified, to file with the Department of Real Estate an application for a public report consisting of, among other things, a notice of intention, as specified. Existing law exempts from the notice of intention requirement the purchase of a mobilehome park by a nonprofit corporation, under specified circumstances. Existing law requires the subdivider of a mobilehome park that is proposed to be converted to resident ownership to make a written disclosure, as specified, to homeowners and residents of the park, with regard to the tentative price of the subdivided interest proposed to be sold or leased.

This bill would exempt from the notice of intention requirement the purchase of a floating home marina by a nonprofit corporation, under specified circumstances. The bill would also require the subdivider of a floating home marina that is proposed to be converted to resident ownership to make a specified written disclosure to homeowners and residents of the marina, with regard to the tentative price of the subdivided interest proposed to be sold or leased.

Because this bill would require local agencies to provide a higher level of service, it would impose a state-mandated local program.

The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that no reimbursement is required by this act for a specified reason.

The people of the State of California do enact as follows:

SECTION 1. Section 11010.85 is added to the Business and Professions Code, to read:

11010.85. (a) The requirement that a notice of intention be filed pursuant to Section 11010 is not applicable to the purchase of a floating home marina by a nonprofit corporation if all of the following occur:

(1) A majority of the shareholders or members of the nonprofit corporation constitute a majority of the homeowners of the floating home marina, and a majority of the members of the board of directors of the nonprofit corporation are homeowners of the floating home marina.

(2) All members of the corporation are residents of the floating home marina. Members of the nonprofit corporation may enter into leases with the corporation that are greater than five years in length. “Homeowners” or “residents” of the floating home marina shall include a bona fide secured party who has, pursuant to a security interest in a membership, taken title to the membership by means of foreclosure, repossession, or voluntary repossession, and who is actively attempting to resell the membership to a prospective resident or homeowner of the floating home marina, in accordance with subdivision (f) of Section 7312 of the Corporations Code.

(3) A permit to issue securities under Section 25113 of the Corporations Code is obtained from the Department of Business Oversight, Division of Corporations. In the case of a nonissuer transaction (as defined by Section 25011 of the Corporations Code) involving the offer to resell or the resale of memberships by a bona fide secured party as described in paragraph (2) of this section, a permit is not required where the transaction is exempt from the qualification requirements of Section 25130 of the Corporations Code pursuant to subdivision (e) of Section 25104 of the Corporations Code. The exemption from qualification pursuant to subdivision (e) of Section 25104 of the Corporations Code available to a bona fide secured party does not eliminate the requirement of this section that the nonprofit corporation shall either file a notice of intention pursuant to Section 11010 or obtain a permit pursuant to Section 25113 of the Corporations Code.

(4) All funds of tenants for the purchase of the floating home marina are deposited in escrow until the document transferring title of the floating home marina to the nonprofit corporation is recorded. The escrow also shall include funds of homeowners that shall be available to the homeowners association nonprofit corporation for payment of any and all costs reasonably associated with the processing and conversion of the floating home marina into condominium interests. Payment of these costs may be made from the funds deposited in escrow prior to the close of escrow upon the direction of the homeowners association nonprofit corporation.

(b) The funds described by paragraph (4) of subdivision (a), or any other funds subsequently received from tenants for purposes other than the purchase of a separate subdivided interest in any portion of the floating home marina, are not subject to the requirements of Section 11013.1, 11013.2, or 11013.4.

SEC. 2. Section 11010.9 of the Business and Professions Code is amended to read:

11010.9. (a) Notwithstanding any other provision of law, the subdivider of a mobilehome park or floating home marina that is proposed to be converted to resident ownership, prior to filing a notice of intention pursuant to Section 11010, shall disclose to homeowners and residents of the park or marina, by written notice, the tentative price of the subdivided interest proposed to be sold or leased.

(b) The disclosure notice required by subdivision (a) shall include a statement that the tentative price is not binding, could change between the time of disclosure and the time of governmental approval to commence the actual sale or lease of the subdivided interests in the park or marina, as the result of conditions imposed by the state or local government for approval of the park or marina conversion, increased financing costs, or other factors and, in the absence of bad faith, shall not give rise to a claim for liability against the provider of this information.

(c) The disclosure notice required by subdivision (a) shall not be construed to authorize the subdivider of a mobilehome park or floating home marina that is proposed to be converted to resident ownership to offer to sell or lease, sell or lease, or accept money for the sale or lease of, subdivided interests in the park or marina, or to engage in any other activities that are otherwise prohibited, with regard to subdividing the park or marina into ownership interests, prior to the issuance of a public report pursuant to this chapter.

SEC. 3. Section 66427.4 of the Government Code is amended to read:

66427.4. (a) At the time of filing a tentative or parcel map for a subdivision to be created from the conversion of a mobilehome park or floating home marina to another use, the subdivider shall also file a report on the impact of the conversion upon the displaced residents of the mobilehome park or floating home marina to be converted. In determining the impact of the conversion on displaced mobilehome park or floating home marina residents, the report shall address the availability of adequate replacement space in mobilehome parks or floating home marinas.

(b) The subdivider shall make a copy of the report available to each resident of the mobilehome park or floating home marina at least 15 days prior to the hearing on the map by the advisory agency or, if there is no advisory agency, by the legislative body.

(c) The legislative body, or an advisory agency that is authorized by local ordinance to approve, conditionally approve, or disapprove the map, may require the subdivider to take steps to mitigate any adverse impact of the conversion on the ability of displaced mobilehome park or floating home marina residents to find adequate space in a mobilehome park or floating home marina, respectively.

(d) This section establishes a minimum standard for local regulation of conversions of mobilehome parks and floating home marinas into other uses and shall not prevent a local agency from enacting more stringent measures.

(e) This section shall not be applicable to a subdivision that is created from the conversion of a rental mobilehome park or rental floating home marina to resident ownership.

SEC. 4. Section 66427.6 is added to the Government Code, to read:

66427.6. At the time of filing a tentative or parcel map for a subdivision to be created from the conversion of a rental floating home marina to resident ownership, the subdivider shall avoid the economic displacement of all nonpurchasing residents in the following manner:

(a) The subdivider shall offer each existing tenant an option to either purchase his or her condominium or subdivided unit, which is to be created by the conversion of the marina to resident ownership, or to continue residency as a tenant.

(b) The subdivider shall file a report on the impact of the conversion upon residents of the floating home marina to be converted to a resident-owned subdivided interest.

(c) The subdivider shall make a copy of the report available to each resident of the floating home marina at least 15 days prior to the hearing on the map by the advisory agency or, if there is no advisory agency, by the legislative body.

(d) (1) The subdivider shall obtain a survey of support of residents of the floating home marina for the proposed conversion.

(2) The survey of support shall be conducted in accordance with an agreement between the subdivider and a resident homeowners' association, if any, that is independent of the subdivider or floating home marina owner.

(3) The survey shall be obtained pursuant to a written ballot.

(4) The survey shall be conducted so that each occupied floating home berth has one vote.

(5) The results of the survey shall be submitted to the local agency upon the filing of the tentative or parcel map, to be considered in the agency's decision as to whether to approve, conditionally approve, or disapprove the map, and the agency may disapprove the map if it finds that the results of the survey have not demonstrated the support of at least a majority of the marina's homeowners.

(6) Local legislative bodies may enact local regulations to implement the requirements of this subdivision.

(e) The subdivider shall be subject to a hearing by a legislative body or advisory agency, which is authorized by local ordinance to approve, conditionally approve, or disapprove the map. The scope of the hearing shall be limited to the issue of compliance with this section.

(f) The subdivider shall be required to avoid the economic displacement of all nonpurchasing residents in accordance with the following:

(1) As to nonpurchasing residents who are not lower income households, as defined in Section 50079.5 of the Health and Safety Code, the monthly rent, including any applicable fees or charges for use of any preconversion amenities, may increase from the preconversion rent to market levels, as defined in an appraisal conducted in accordance with nationally recognized

professional appraisal standards, in equal annual increases over a four-year period.

(2) As to nonpurchasing residents who are lower income households, as defined in Section 50079.5 of the Health and Safety Code, the monthly rent, including any applicable fees or charges for use of any preconversion amenities, may increase from the preconversion rent by an amount equal to the average monthly increase in rent in the four years immediately preceding the conversion, except that the monthly rent shall not be increased by an amount greater than the average monthly percentage increase in the Consumer Price Index for the most recently reported period.

SEC. 5. Section 66428.1 of the Government Code is amended to read:

66428.1. (a) When at least two-thirds of the owners of mobilehomes or floating homes who are tenants in the mobilehome park or floating home marina sign a petition indicating their intent to purchase the mobilehome park or the floating home marina for purposes of converting it to resident ownership, and a field survey is performed, the requirement for a parcel map or a tentative and final map shall be waived unless any of the following conditions exists:

(1) There are design or improvement requirements necessitated by significant health or safety concerns.

(2) The local agency determines that there is an exterior boundary discrepancy that requires recordation of a new parcel or tentative and final map.

(3) The existing parcels that exist prior to the proposed conversion were not created by a recorded parcel or final map.

(4) The conversion would result in the creation of more condominium units or interests than the number of tenant lots, spaces, or floating home berths that exist prior to conversion.

(b) The petition signed by owners of mobilehomes in a mobilehome park proposed for conversion to resident ownership pursuant to subdivision (a) shall read as follows:

MOBILEHOME PARK PETITION AND
DISCLOSURE STATEMENT

SIGNING THIS PETITION INDICATES YOUR SUPPORT FOR CONVERSION OF THIS MOBILEHOME PARK TO RESIDENT OWNERSHIP. THIS DISCLOSURE STATEMENT CONCERNS THE REAL PROPERTY SITUATED IN THE CITY OF ____, COUNTY OF ____, STATE OF CALIFORNIA, DESCRIBED AS ____. THE TOTAL COST FOR CONVERSION AND PURCHASE OF THE PARK IS $____ TO $____, EXCLUDING FINANCING COSTS. THE TOTAL COST TO YOU FOR CONVERSION AND PURCHASE OF YOUR OWNERSHIP INTEREST IS $____ TO $____, EXCLUDING FINANCING COSTS. IF TWO-THIRDS OF THE RESIDENTS IN THIS PARK SIGN THIS PETITION INDICATING THEIR INTENT TO PURCHASE THE MOBILEHOME PARK FOR PURPOSES OF CONVERTING IT TO RESIDENT OWNERSHIP, THEN

THE REQUIREMENTS FOR A NEW PARCEL, OR TENTATIVE AND FINAL SUBDIVISION MAP IN COMPLIANCE WITH THE SUBDIVISION MAP ACT MUST BE WAIVED, WITH CERTAIN VERY LIMITED EXCEPTIONS. WAIVING THESE PROVISIONS OF LAW ELIMINATES NUMEROUS PROTECTIONS THAT ARE AVAILABLE TO YOU.

Buyer, unit #, date	Petitioner, date

(c) The petition signed by owners of floating homes in a floating home marina proposed for conversion to resident ownership pursuant to subdivision (a) shall read as follows:

FLOATING HOME MARINA PETITION AND
DISCLOSURE STATEMENT

SIGNING THIS PETITION INDICATES YOUR SUPPORT FOR CONVERSION OF THIS FLOATING HOME MARINA TO RESIDENT OWNERSHIP. THIS DISCLOSURE STATEMENT CONCERNS THE REAL PROPERTY SITUATED IN THE CITY OF ____, COUNTY OF ____, STATE OF CALIFORNIA, DESCRIBED AS ____. THE TOTAL COST FOR CONVERSION AND PURCHASE OF THE PARK IS $____ TO $____, EXCLUDING FINANCING COSTS. THE TOTAL COST TO YOU FOR CONVERSION AND PURCHASE OF YOUR OWNERSHIP INTEREST IS $____ TO $____, EXCLUDING FINANCING COSTS. IF TWO-THIRDS OF THE RESIDENTS IN THIS MARINA SIGN THIS PETITION INDICATING THEIR INTENT TO PURCHASE THE FLOATING HOME MARINA FOR PURPOSES OF CONVERTING IT TO RESIDENT OWNERSHIP, THEN THE REQUIREMENTS FOR A NEW PARCEL, OR TENTATIVE AND FINAL SUBDIVISION MAP IN COMPLIANCE WITH THE SUBDIVISION MAP ACT MUST BE WAIVED, WITH CERTAIN VERY LIMITED EXCEPTIONS. WAIVING THESE PROVISIONS OF LAW ELIMINATES NUMEROUS PROTECTIONS THAT ARE AVAILABLE TO YOU.

Buyer, unit #, date	Petitioner, date

(d) The local agency shall provide an application for waiver pursuant to this section. After the waiver application is deemed complete pursuant to Section 65943, the local agency shall approve or deny the application within 50 days. The applicant shall have the right to appeal that decision to the governing body of the local agency.

(e) If a tentative or parcel map is required, the local agency shall not impose any offsite design or improvement requirements unless these are necessary to mitigate an existing health or safety condition. No other dedications, improvements, or in-lieu fees shall be required by the local agency. In no case shall the mitigation of a health or safety condition have the effect of reducing the number, or changing the location, of existing mobilehome spaces or floating home marina berths.

(f) If the local agency imposes requirements on an applicant to mitigate a health or safety condition, the applicant and the local agency shall enter into an unsecured improvement agreement. The local agency shall not require bonds or other security devices pursuant to Chapter 5 (commencing with Section 66499) for the performance of that agreement. The applicant shall have a period of one year from the date the agreement was executed to complete those improvements.

(g) If the waiver application provided for in this section is denied by the local agency pursuant to the provisions of subdivision (a), the applicant may proceed to convert the mobilehome park or the floating home marina to a tenant-owned, condominium ownership interest, but shall file a parcel map or a tentative and final map. The local agency may not require the applicant to file and record a tentative and final map unless the conversion creates five or more parcels shown on the map. The number of condominium units or interests created by the conversion shall not determine whether the filing of a parcel or a tentative and final map shall be required.

(h) For the purposes of this section, the meaning of "resident ownership" shall be as defined in Section 50781 of the Health and Safety Code.

SEC. 6. No reimbursement is required by this act pursuant to Section 6 of Article XIII B of the California Constitution because a local agency or school district has the authority to levy service charges, fees, or assessments sufficient to pay for the program or level of service mandated by this act, within the meaning of Section 17556 of the Government Code.

O

Senate Bill No. 684

CHAPTER 544

An act to amend Section 5273 of the Business and Professions Code, relating to advertising displays, and declaring the urgency thereof, to take effect immediately.

[Approved by Governor October 4, 2013. Filed with Secretary of State October 4, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 684, Hill. Advertising displays: redevelopment agency project areas.

Existing law, the Outdoor Advertising Act, provides for the regulation by the Department of Transportation of advertising displays, as defined, within view of public highways. The act regulates the placement of off-premises advertising displays along highways that generally advertise business conducted or services rendered or goods produced or sold at a location other than the property upon which the display is located. Under the act, advertising displays advertising businesses and activities within the boundary limits of, and as a part of, an individual redevelopment agency project may, with the consent of the redevelopment agency governing the project, be considered to be on premises, as specified. A violation of these provisions is a misdemeanor.

The Community Redevelopment Law authorizes the establishment of redevelopment agencies in communities to address the effects of blight, as defined. Existing law dissolved redevelopment agencies and community development agencies, as of February 1, 2012, and provides for the designation of successor agencies.

This bill would provide that an advertising display advertising businesses and activities within the boundary limits of, and as a part of, an individual redevelopment agency project, as the project boundaries existed on December 29, 2011, may remain and be considered an on-premises display, until January 1, 2023, if the advertising display meets specified criteria. This bill would authorize, on and after January 1, 2022, the applicable city, county, or city and county to request from the department an extension for good cause, as specified, beyond January 1, 2023, not to exceed the expiration of the redevelopment project area. The bill would require a specified certification of a local agency authorizing one of these advertising displays, and would require the local agency to ensure that the display conforms to the bill's requirements. By imposing a new requirement in that regard on local agencies, the bill would impose a state-mandated local program. By imposing new conditions on a redevelopment project advertising display to remain lawfully erected, a violation of which would constitute a misdemeanor, this bill would also impose a state-mandated local program.

The California Constitution requires the state to reimburse local agencies and school districts for certain costs mandated by the state. Statutory provisions establish procedures for making that reimbursement.

This bill would provide that with regard to certain mandates no reimbursement is required by this act for a specified reason.

With regard to any other mandates, this bill would provide that, if the Commission on State Mandates determines that the bill contains costs so mandated by the state, reimbursement for those costs shall be made pursuant to the statutory provisions noted above.

This bill would declare that it is to take effect immediately as an urgency statute.

The people of the State of California do enact as follows:

SECTION 1. Section 5273 of the Business and Professions Code is amended to read:

5273. (a) Notwithstanding the dissolution of a state redevelopment agency, and subject to subdivision (b), for purposes of this chapter, an advertising display advertising the businesses and activities developed within the boundary limits of, and as a part of, an individual redevelopment agency project, as those boundaries existed on December 29, 2011, may continue to exist and be considered an on-premises display, as defined in Section 5490, if the advertising display meets all of the following conditions:

(1) The advertising display is located within the boundary limits of the project.

(2) The advertising display was constructed on or before January 1, 2012.

(3) The advertising display does not cause the reduction of federal aid highway funds provided pursuant to Section 131 of Title 23 of the United States Code. If an advertising display authorized under this section is subject to a notice from the United States Department of Transportation, the Federal Highway Administration, or any other applicable federal agency to the state that the operation of that display will result in the reduction of federal aid highway funds as provided in Section 131 of Title 23 of the United States Code, the display owner or operator shall remove all advertising copy from the display within 60 days after the date the state notifies the owner or operator, and the applicable city, county, or city and county, by certified mail, of the receipt of the federal notice. Failure to remove the advertising copy pursuant to this paragraph shall result in a civil fine, imposed by the California Department of Transportation, of ten thousand dollars ($10,000) per day until the advertising copy is removed. The department shall not assume any liability in connection with the cessation of operation or removal of an advertising display or advertising copy pursuant to this paragraph. If the name of the owner or operator of the display is not indicated on the

display, the state is only required to send the notice to the applicable city, county, or city and county.

(b) An advertising display described in subdivision (a) may remain until January 1, 2023, after which date the display shall be removed, unless it otherwise qualifies as a lawful advertising display pursuant to this chapter, without the payment of any compensation to the owner or operator. On and after January 1, 2022, the applicable city, county, or city and county may for good cause request from the department an extension beyond January 1, 2023, not to exceed the expiration of the redevelopment project area. "Good cause" for these purposes means all of the following are satisfied: (1) there has been a finding by the applicable city, county, or city and county that the advertising display has had a positive economic impact on the redevelopment project area and provides a public benefit, (2) there have been no violations by the display owner or operator of this section or of any applicable illumination standards in the previous 10 years that have not been corrected within 30 days of the date of mailing of a violation notice to the owner or operator by the department, and (3) there has been compliance by the owner and operator with all other standards adopted by the applicable city, county, or city and county, or by the department.

(c) The applicable city, county, or city and county shall be responsible for ensuring that an advertising display is consistent with this section and provides a public benefit. This provision shall not be construed to preclude any enforcement authority of the department under this chapter.

(d) The applicable city, county, or city and county shall annually, by December 31, certify to the department that the advertising copy of the advertising display is advertising businesses or activities operating within the boundaries of the redevelopment project area and that at least 10 percent of the advertising copy, up to a maximum of 100 square feet, is used to display the address or location or locations of the business or activity, or to identify the route to the business or activity from the nearest freeway offramp. The department may independently review compliance with this certification. An advertising display subject to this section shall be removed if it is in violation of this subdivision more than three times within a 10-year period and the violation has not been corrected within 30 days of the date of mailing of a violation notice to the owner or operator by the department.

(e) The applicable city, county, or city and county authorizing an advertising display placed pursuant to this section shall have primary responsibility for ensuring that the display remains in conformance with all provisions of this section. If the city, county, or city and county fails to do so within 30 days of the date of mailing of a notice to the city, county, or city and county by the department, the city, county, or city and county shall hold the department harmless and indemnify the department for all costs incurred by the department to ensure compliance with this section or to defend actions challenging the authorization of displays pursuant to this section.

SEC. 2. No reimbursement is required by this act pursuant to Section 6 of Article XIII B of the California Constitution for certain costs that may be incurred by a local agency or school district because, in that regard, this act creates a new crime or infraction, eliminates a crime or infraction, or changes the penalty for a crime or infraction, within the meaning of Section 17556 of the Government Code, or changes the definition of a crime within the meaning of Section 6 of Article XIII B of the California Constitution.

However, if the Commission on State Mandates determines that this act contains other costs mandated by the state, reimbursement to local agencies and school districts for those costs shall be made pursuant to Part 7 (commencing with Section 17500) of Division 4 of Title 2 of the Government Code.

SEC. 3. This act is an urgency statute necessary for the immediate preservation of the public peace, health, or safety within the meaning of Article IV of the Constitution and shall go into immediate effect. The facts constituting the necessity are:

As of February 1, 2012, redevelopment agencies have been dissolved and designated successor agencies have been vested with all authority, rights, powers, duties, and obligations previously vested in the former redevelopment agencies, including projects addressing blight in communities. In order that advertising displays can continue to exist within the redevelopment agency projects, and help to fight blight in an affected community, it is necessary that this act take effect immediately.

O

COMMON INTEREST DEVELOPMENTS

▪ COMMERCIAL AND INDUSTRIAL COMMON INTEREST DEVELOPMENT ACT

The Davis-Stirling Common Interest Development Act provides for the creation and regulation of common interest developments, as defined, but exempts common interest developments that are limited to industrial or commercial uses from specified provisions of the act.

This act establishes the Commercial and Industrial Common Interest Development Act, which provides for the creation and regulation of commercial and industrial common interest developments. The act makes various conforming changes.

Amending Sections 10153.2, 11003, 11003.2, 11004.5, 11010.3, 23426.5, and 23428.20 of the Business and Professions Code, amending Sections 714, 714.1, 782, 782.5, 783, 783.1, 1098, 1133, 1633.3, 2924b, 2955.1, 4202, and 4280 of, adding Part 5.3 (commencing with Section 6500) to Division 4 of, and repealing Section 6870 of, the Civil Code, amending Sections 86 and 116.540 of the Code of Civil Procedure, amending Sections 12191, 12956.1, 12956.2, 53341.5, 65008, 66411, 66412, 66424, 66427, 66452.10, and 66475.2 of the Government Code, amending Sections 13132.7, 19850, 25400.22, 25915.2, 33050, 33435, 33436, 35811, 37630, 50955, 51602, and 116048 of the Health and Safety Code, amending Section 790.031 of the Insurance Code, amending Section 2188.6 of the Revenue and Taxation Code, amending Sections 21107.7, 22651, 22651.05, and 22658 of the Vehicle Code, and amending Section 13553 of the Water Code.

Reference

Chapter 605 (SB 752 – Roth)

Senate Bill No. 470

CHAPTER 659

An act to add Part 4 (commencing with Section 52200) to Division 1 of Title 5 of the Government Code, relating to community development.

[Approved by Governor October 8, 2013. Filed with Secretary of State October 8, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 470, Wright. Community development: economic opportunity.

Existing law generally regulates the power of cities, counties, and cities and counties.

This bill would state the intent of the Legislature to promote economic development on a local level so that communities can enact local strategies to increase jobs, create economic opportunity, and generate tax revenue for all levels of government. The bill would define economic opportunity to include certain types of agreements, purposes, and projects, and declare that it is the policy of the state to protect and promote the sound development of economic opportunity in cities and counties, and the general welfare of the inhabitants of those communities through the employment of all appropriate means.

The bill would state that the creation of economic opportunity and the provisions for appropriate continuing land use and construction policies with respect to property acquired, in whole or in part, for economic opportunity constitute public uses and purposes for which public money may be advanced or expended and private property acquired. The bill would provide that before certain returned city, county, or city and county property is sold or leased for development, the sale or lease shall first be approved by the legislative body, as specified. The bill would authorize a city, county, or city and county to establish a program under which it loans funds to owners or tenants for the purpose of rehabilitating commercial buildings or structures and to assist with the financing of facilities or capital equipment as part of an agreement that provides for the development or rehabilitation of property that will be used for industrial or manufacturing purposes, as specified.

The people of the State of California do enact as follows:

SECTION 1. Part 4 (commencing with Section 52200) is added to Division 1 of Title 5 of the Government Code, to read:

PART 4. ECONOMIC OPPORTUNITY

Chapter 1. General Provisions

52200. It is the intent of the Legislature to do all of the following:

(a) Promote economic development on a local level so that communities can enact local strategies to increase jobs, create economic opportunity, and generate tax revenue for all levels of government.

(b) Give local governments tools, at no cost to the state, that allow local governments to use their funds in a manner that promotes economic opportunity.

(c) With the loss of redevelopment funds, cities, counties, and cities and counties need to continue certain powers afforded to redevelopment agencies that were critical to economic development, yet do not have an impact on schools and the state budget.

52200.2. As used in this part "economic opportunity" means any of the following:

(a) Development agreements or other agreements that create, retain, or expand new jobs, in which the legislative body finds that the agreement will create or retain at least one full-time equivalent, permanent job for every thirty-five thousand dollars ($35,000) of city, county, or city and county investment in the project after full capacity and implementation.

(b) Development agreements that increase property tax revenues to all property tax collecting entities, in which the legislative body finds that the agreement will result in an increase of at least 15 percent of total property tax resulting from the project at full implementation when compared to the year prior to the property being acquired by the government entity.

(c) Creation of affordable housing, if a demonstrated affordable housing need exists in the community, as defined in the approved housing element or regional housing needs assessment.

(d) Projects that meet the goals set forth in Chapter 728 of the Statutes of 2008 and have been included in an adopted sustainable communities strategy or alternative planning strategy or a project that specifically implements the goals of those adopted plans.

(e) Transit priority projects, as defined in Section 21155 of the Public Resources Code.

52200.4. It is declared to be the policy of the state:

(a) To protect and promote the sound development of economic opportunity in cities and counties and the general welfare of the inhabitants of those communities through the employment of all appropriate means.

(b) That whenever the creation of economic opportunity in cities and counties cannot be accomplished by private enterprise alone, without public participation and assistance in the acquisition of land, in planning and in the financing of land assembly, in the work of clearance, and in the making of improvements necessary therefor, it is in the public interest to advance or expend public funds for these purposes, and to provide a means by which economic opportunity can be created.

(c) That the creation of economic opportunity and the provisions for appropriate continuing land use and construction policies with respect to property acquired, in whole or in part, for economic opportunity constitute public uses and purposes for which public money may be advanced or expended and private property acquired, and are governmental functions of state concern in the interest of health, safety, and welfare of the people of the state and cities and counties.

(d) That the necessity in the public interest for the provisions of this part is declared to be a matter of legislative determination.

52200.6. This chapter shall not be interpreted to authorize the use of eminent domain for economic development purposes.

Chapter 2. Sales and Leases

52201. (a) (1) Before any city, county, or city and county property that is returned to the city, county, or city and county per the long-range property management plan, pursuant to Section 34191.5 of the Health and Safety Code, is sold or leased for economic development purposes, the sale or lease shall first be approved by the legislative body by resolution after public hearing. Notice of the time and place of the hearing shall be published in a newspaper of general circulation in the community at least once per week for at least two successive weeks, as specified in Section 6066, prior to the hearing.

(2) The city, county, or city and county shall make available, for public inspection and copying at a cost not to exceed the cost of duplication, a report no later than the time of publication of the first notice of the hearing mandated by this section. This report shall contain both of the following:

(A) A copy of the proposed sale or lease.

(B) A summary that describes and specifies all of the following:

(i) The cost of the agreement to the city, county, or city and county, including land acquisition costs, clearance costs, relocation costs, the costs of any improvements to be provided by the city, county, or city and county, plus the expected interest on any loans or bonds to finance the agreements.

(ii) The estimated value of the interest to be conveyed or leased, determined at the highest and best uses permitted under the general plan or zoning.

(iii) The estimated value of the interest to be conveyed or leased, determined at the use and with the conditions, covenants, and development costs required by the sale or lease. The purchase price or present value of the lease payments which the lessor will be required to make during the term of the lease. If the sale price or total rental amount is less than the fair market value of the interest to be conveyed or leased, determined at the highest and best use, then the city, county, or city and county shall provide as part of the summary an explanation of the reasons for the difference.

(iv) An explanation of why the sale or lease of the property will assist in the creation of economic opportunity, with reference to all supporting facts and materials relied upon in making this explanation.

(b) The resolution approving the lease or sale shall be adopted by a majority vote unless the legislative body has provided by ordinance for a two-thirds vote for that purpose and shall contain a finding that the sale or lease of the property will assist in the creation of economic opportunity. The resolution shall also contain one of the following findings:

(1) The consideration is not less than the fair market value at its highest and best use.

(2) The consideration is not less than the fair reuse value at the use and with the covenants and conditions and development costs authorized by the sale or lease.

(c) The provisions of this section are an alternative to any other authority granted by law to cities to dispose of city-owned property.

52202. A city, county, or city and county may establish a program under which it loans funds to owners or tenants for the purpose of rehabilitating commercial buildings or structures.

52203. (a) As part of an agreement that provides for the development or rehabilitation of property that will be used for industrial or manufacturing purposes, a city, county, or city and county may assist with the financing of facilities or capital equipment, including, but not necessarily limited to, pollution control devices.

(b) Prior to entering into an agreement for a development that will be assisted pursuant to this section, a city, county, or city and county shall find, after a public hearing, that the assistance is necessary for the economic feasibility of the development and that the assistance cannot be obtained on economically feasible terms in the private market.

O

Assembly Bill No. 1386

CHAPTER 750

An act to amend Section 98.2 of the Labor Code, relating to employment.

[Approved by Governor October 11, 2013. Filed with Secretary of State October 11, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 1386, Committee on Labor and Employment. Employment: employee complaints: final orders.

Existing law vests with the Labor Commissioner the authority to hear employee complaints regarding the payment of wages and other employment-related issues. Existing law requires the Labor Commissioner to file an order, decision, or award within 15 days of hearing an employee complaint. If no party to the action appeals the order, decision, or award within 10 days after its service, existing law provides that the order, decision, or award becomes the final order for the action. The Labor Commissioner is required to file the final order with the clerk of the superior court of the appropriate county within 10 days of the order, decision, or award becoming the final order for the action, unless the parties reach a settlement approved by the Labor Commissioner. Existing law then requires the clerk of the superior court to enter judgment in conformity with the final order, which has the same force and effect as a judgment entered in a civil action.

This bill would provide that, under the above provisions, upon an order becoming final, a lien is created and the Labor Commissioner may record a certificate of lien, as specified, with the county recorder of any county in which the employer's property may be located. The bill would require the certificate to contain specified information. The bill would provide that the lien would continue on the employer's real property until satisfied or released, as provided, or for 10 years, as specified, and would require the county recorder to accept, record, and index the certificate of lien, as specified.

The people of the State of California do enact as follows:

SECTION 1. Section 98.2 of the Labor Code is amended to read:

98.2. (a) Within 10 days after service of notice of an order, decision, or award the parties may seek review by filing an appeal to the superior court, where the appeal shall be heard de novo. The court shall charge the first paper filing fee under Section 70611 of the Government Code to the party seeking review. The fee shall be distributed as provided in Section 68085.3 of the Government Code. A copy of the appeal request shall be served upon the Labor Commissioner by the appellant. For purposes of computing the 10-day period after service, Section 1013 of the Code of Civil Procedure is applicable.

(b) As a condition to filing an appeal pursuant to this section, an employer shall first post an undertaking with the reviewing court in the amount of the order, decision, or award. The undertaking shall consist of an appeal bond issued by a licensed surety or a cash deposit with the court in the amount of the order, decision, or award. The employer shall provide written notification to the other parties and the Labor Commissioner of the posting of the undertaking. The undertaking shall be on the condition that, if any judgment is entered in favor of the employee, the employer shall pay the amount owed pursuant to the judgment, and if the appeal is withdrawn or dismissed without entry of judgment, the employer shall pay the amount owed pursuant to the order, decision, or award of the Labor Commissioner unless the parties have executed a settlement agreement for payment of some other amount, in which case the employer shall pay the amount that the employer is obligated to pay under the terms of the settlement agreement. If the employer fails to pay the amount owed within 10 days of entry of the judgment, dismissal, or withdrawal of the appeal, or the execution of a settlement agreement, a portion of the undertaking equal to the amount owed, or the entire undertaking if the amount owed exceeds the undertaking, is forfeited to the employee.

(c) If the party seeking review by filing an appeal to the superior court is unsuccessful in the appeal, the court shall determine the costs and reasonable attorney's fees incurred by the other parties to the appeal, and assess that amount as a cost upon the party filing the appeal. An employee is successful if the court awards an amount greater than zero.

(d) If no notice of appeal of the order, decision, or award is filed within the period set forth in subdivision (a), the order, decision, or award shall, in the absence of fraud, be deemed the final order.

(e) The Labor Commissioner shall file, within 10 days of the order becoming final pursuant to subdivision (d), a certified copy of the final order with the clerk of the superior court of the appropriate county unless a settlement has been reached by the parties and approved by the Labor Commissioner. Judgment shall be entered immediately by the court clerk in conformity therewith. The judgment so entered has the same force and effect as, and is subject to all of the provisions of law relating to, a judgment in a civil action, and may be enforced in the same manner as any other judgment of the court in which it is entered. Enforcement of the judgment shall receive court priority.

(f) (1) In order to ensure that judgments are satisfied, the Labor Commissioner may serve upon the judgment debtor, personally or by first-class mail at the last known address of the judgment debtor listed with the division, a form similar to, and requiring the reporting of the same information as, the form approved or adopted by the Judicial Council for purposes of subdivision (a) of Section 116.830 of the Code of Civil

Procedure to assist in identifying the nature and location of any assets of the judgment debtor.

(2) The judgment debtor shall complete the form and cause it to be delivered to the division at the address listed on the form within 35 days after the form has been served on the judgment debtor, unless the judgment has been satisfied. In case of willful failure by the judgment debtor to comply with this subdivision, the division or the judgment creditor may request the court to apply the sanctions provided in Section 708.170 of the Code of Civil Procedure.

(g) (1) As an alternative to a judgment lien, upon the order becoming final pursuant to subdivision (d), a lien on real property may be created by the Labor Commissioner recording a certificate of lien, for amounts due under the final order and in favor of the employee or employees named in the order, with the county recorder of any county in which the employer's real property may be located, at the Labor Commissioner's discretion and depending upon information the Labor Commissioner obtains concerning the employer's assets. The lien attaches to all interests in real property of the employer located in the county where the lien is created to which a judgment lien may attach pursuant to Section 697.340 of the Code of Civil Procedure.

(2) The certificate of lien shall include information as prescribed by Section 27288.1 of the Government Code.

(3) The recorder shall accept and record the certificate of lien and shall index it as prescribed by law.

(4) Upon payment of the amount due under the final order, the Labor Commissioner shall issue a certificate of release, releasing the lien created under paragraph (1). The certificate of release may be recorded by the employer at the employer's expense.

(5) Unless the lien is satisfied or released, a lien under this section shall continue until 10 years from the date of its creation.

(h) Notwithstanding subdivision (e), the Labor Commissioner may stay execution of any judgment entered upon an order, decision, or award that has become final upon good cause appearing therefor and may impose the terms and conditions of the stay of execution. A certified copy of the stay of execution shall be filed with the clerk entering the judgment.

(i) When a judgment is satisfied in fact, other than by execution, the Labor Commissioner may, upon the motion of either party or on its own motion, order entry of satisfaction of judgment. The clerk of the court shall enter a satisfaction of judgment upon the filing of a certified copy of the order.

(j) The Labor Commissioner shall make every reasonable effort to ensure that judgments are satisfied, including taking all appropriate legal action and requiring the employer to deposit a bond as provided in Section 240.

(k) The judgment creditor, or the Labor Commissioner as assignee of the judgment creditor, is entitled to court costs and reasonable attorney's fees for enforcing the judgment that is rendered pursuant to this section.

O

Assembly Bill No. 325

CHAPTER 767

An act to amend Sections 65009, 65587, and 65755 of the Government Code, relating to land use.

[Approved by Governor October 12, 2013. Filed with Secretary of State October 12, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

AB 325, Alejo. Land use and planning: cause of actions: time limitations.

The Planning and Zoning Law requires an action or proceeding against local zoning and planning decisions of a legislative body to be commenced and the legislative body to be served within a year of accrual of the cause of action, if it meets certain requirements. Where the action or proceeding is brought in support of, or to encourage or facilitate the development of, housing that would increase the community's supply of affordable housing, a cause of action accrues 60 days after a certain notice is filed or the legislative body takes a final action in response to the notice, whichever occurs first.

This bill would authorize the notice to be filed any time within 180 days after specified zoning and planning decisions, but would set a 270-day period for notice with respect to an adopted or revised housing element that is found to substantially comply with law, and a 2-year period for notice with respect to an adopted or revised housing element that is found not to substantially comply with law. This bill would also establish a 6-month limitations period for the commencement of an action or proceeding arising from a notice subject to the 270-day period, a one-year limitations period for the commencement of an action or proceeding arising from a notice subject to the 2-year period, and a 180-day limitations period for the commencement of an action or proceeding arising from a notice subject to the 180-day period. The bill would declare the intent of the Legislature to modify a specified court opinion. The bill would also provide that in an action or proceeding subject to these provisions, no remedy pursuant to specified provisions of law shall abrogate, impair, or otherwise interfere with the full exercise of the rights and protections granted to a tentative map application or a developer, as prescribed. The bill would make further conforming changes.

The people of the State of California do enact as follows:

SECTION 1. It is the intent of the Legislature in enacting Section 2 of this act to modify the court's opinion in Urban Habitat Program v. City of

Pleasanton (2008) 164 Cal.App.4th 1561, with respect to the interpretation of Section 65009 of the Government Code.

SEC. 2. Section 65009 of the Government Code is amended to read:

65009. (a) (1) The Legislature finds and declares that there currently is a housing crisis in California and it is essential to reduce delays and restraints upon expeditiously completing housing projects.

(2) The Legislature further finds and declares that a legal action or proceeding challenging a decision of a city, county, or city and county has a chilling effect on the confidence with which property owners and local governments can proceed with projects. Legal actions or proceedings filed to attack, review, set aside, void, or annul a decision of a city, county, or city and county pursuant to this division, including, but not limited to, the implementation of general plan goals and policies that provide incentives for affordable housing, open-space and recreational opportunities, and other related public benefits, can prevent the completion of needed developments even though the projects have received required governmental approvals.

(3) The purpose of this section is to provide certainty for property owners and local governments regarding decisions made pursuant to this division.

(b) (1) In an action or proceeding to attack, review, set aside, void, or annul a finding, determination, or decision of a public agency made pursuant to this title at a properly noticed public hearing, the issues raised shall be limited to those raised in the public hearing or in written correspondence delivered to the public agency prior to, or at, the public hearing, except where the court finds either of the following:

(A) The issue could not have been raised at the public hearing by persons exercising reasonable diligence.

(B) The body conducting the public hearing prevented the issue from being raised at the public hearing.

(2) If a public agency desires the provisions of this subdivision to apply to a matter, it shall include in any public notice issued pursuant to this title a notice substantially stating all of the following: "If you challenge the (nature of the proposed action) in court, you may be limited to raising only those issues you or someone else raised at the public hearing described in this notice, or in written correspondence delivered to the (public entity conducting the hearing) at, or prior to, the public hearing."

(3) The application of this subdivision to causes of action brought pursuant to subdivision (d) applies only to the final action taken in response to the notice to the city or clerk of the board of supervisors. If no final action is taken, then the issue raised in the cause of action brought pursuant to subdivision (d) shall be limited to those matters presented at a properly noticed public hearing or to those matters specified in the notice given to the city or clerk of the board of supervisors pursuant to subdivision (d), or both.

(c) (1) Except as provided in subdivision (d), no action or proceeding shall be maintained in any of the following cases by any person unless the action or proceeding is commenced and service is made on the legislative body within 90 days after the legislative body's decision:

(A) To attack, review, set aside, void, or annul the decision of a legislative body to adopt or amend a general or specific plan. This paragraph does not apply where an action is brought based upon the complete absence of a general plan or a mandatory element thereof, but does apply to an action attacking a general plan or mandatory element thereof on the basis that it is inadequate.

(B) To attack, review, set aside, void, or annul the decision of a legislative body to adopt or amend a zoning ordinance.

(C) To determine the reasonableness, legality, or validity of any decision to adopt or amend any regulation attached to a specific plan.

(D) To attack, review, set aside, void, or annul the decision of a legislative body to adopt, amend, or modify a development agreement. An action or proceeding to attack, review, set aside, void, or annul the decisions of a legislative body to adopt, amend, or modify a development agreement shall only extend to the specific portion of the development agreement that is the subject of the adoption, amendment, or modification. This paragraph applies to development agreements, amendments, and modifications adopted on or after January 1, 1996.

(E) To attack, review, set aside, void, or annul any decision on the matters listed in Sections 65901 and 65903, or to determine the reasonableness, legality, or validity of any condition attached to a variance, conditional use permit, or any other permit.

(F) Concerning any of the proceedings, acts, or determinations taken, done, or made prior to any of the decisions listed in subparagraphs (A), (B), (C), (D), and (E).

(2) In the case of an action or proceeding challenging the adoption or revision of a housing element pursuant to this subdivision, the action or proceeding may, in addition, be maintained if it is commenced and service is made on the legislative body within 60 days following the date that the Department of Housing and Community Development reports its findings pursuant to subdivision (h) of Section 65585.

(d) (1) An action or proceeding shall be commenced and the legislative body served after the accrual of the cause of action as provided in this subdivision, if the action or proceeding meets both of the following requirements:

(A) It is brought in support of or to encourage or facilitate the development of housing that would increase the community's supply of housing affordable to persons and families with low or moderate incomes, as defined in Section 50079.5 of the Health and Safety Code, or with very low incomes, as defined in Section 50105 of the Health and Safety Code, or middle-income households, as defined in Section 65008 of this code. This subdivision is not intended to require that the action or proceeding be brought in support of or to encourage or facilitate a specific housing development project.

(B) It is brought with respect to the adoption or revision of a housing element pursuant to Article 10.6 (commencing with Section 65580) of Chapter 3, actions taken pursuant to Section 65863.6, or Chapter 4.2

(commencing with Section 65913), or to challenge the adequacy of an ordinance adopted pursuant to Section 65915.

(2) (A) An action or proceeding challenging the adoption or revision of a housing element that the Department of Housing and Community Development has found to substantially comply with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 shall be commenced, and the legislative body shall be served, within six months after the accrual of the cause of action as provided in this subdivision.

(B) An action or proceeding challenging the adoption or revision of a housing element that the Department of Housing and Community Development has found does not substantially comply with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3, where the legislative body has failed to change the draft element or amendment to substantially comply with the requirements of Article 10.6 or has adopted the draft element or amendment without change and made findings pursuant to subdivision (f) of Section 65585, shall be commenced, and the legislative body shall be served, within one year after the accrual of the cause of action as provided in this subdivision.

(C) An action or proceeding challenging an action taken pursuant to Section 65863.6, or Chapter 4.2 (commencing with Section 65913), or to challenge the adequacy of an ordinance adopted pursuant to Section 65915 shall be served within 180 days after the accrual of the cause of action as provided in this subdivision.

(3) (A) A cause of action brought pursuant to this subdivision shall not be maintained until 60 days have expired following notice to the city or clerk of the board of supervisors by the party bringing the cause of action, or his or her representative, specifying the deficiencies of the general plan, specific plan, zoning ordinance, or other action described in subparagraph (B) of paragraph (1). A cause of action brought pursuant to this subdivision shall accrue 60 days after notice is filed or the legislative body takes a final action in response to the notice, whichever occurs first.

(B) This notice may be filed at any time within 270 days after an action described in subparagraph (A) of paragraph (2), two years after an action described in subparagraph (B) of paragraph (2), or 180 days after an action described in subparagraph (C) of paragraph (2).

(4) A notice or cause of action brought by one party pursuant to this subdivision shall not bar filing of a notice and initiation of a cause of action by any other party.

(5) After the adoption of a housing element covering the current planning period, no action shall be filed pursuant to this subdivision to challenge a housing element covering a prior planning period.

(e) Upon the expiration of the time limits provided for in this section, all persons are barred from any further action or proceeding.

(f) Notwithstanding Sections 65700 and 65803, or any other provision of law, this section shall apply to charter cities.

(g) Except as provided in subdivision (d), this section shall not affect any law prescribing or authorizing a shorter period of limitation than that specified herein.

(h) Except as provided in paragraph (4) of subdivision (c), this section shall be applicable to those decisions of the legislative body of a city, county, or city and county made pursuant to this division on or after January 1, 1984.

SEC. 3. Section 65587 of the Government Code is amended to read:

65587. (a) Each city, county, or city and county shall bring its housing element, as required by subdivision (c) of Section 65302, into conformity with the requirements of this article on or before October 1, 1981, and the deadlines set by Section 65588. Except as specifically provided in subdivision (b) of Section 65361, the Director of Planning and Research shall not grant an extension of time from these requirements.

(b) Any action brought by any interested party to review the conformity with the provisions of this article of any housing element or portion thereof or revision thereto shall be brought pursuant to Section 1085 of the Code of Civil Procedure; the court's review of compliance with the provisions of this article shall extend to whether the housing element or portion thereof or revision thereto substantially complies with the requirements of this article.

(c) If a court finds that an action of a city, county, or city and county, which is required to be consistent with its general plan, does not comply with its housing element, the city, county, or city and county shall bring its action into compliance within 60 days. However, the court shall retain jurisdiction throughout the period for compliance to enforce its decision. Upon the court's determination that the 60-day period for compliance would place an undue hardship on the city, county, or city and county, the court may extend the time period for compliance by an additional 60 days.

(d) (1) If a court finds that a city, county, or city and county failed to complete the rezoning required by subparagraph (A) of paragraph (1) of subdivision (c) of Section 65583, as that deadline may be modified by the extension provided for in subdivision (f) of that section, the court shall issue an order or judgment, after considering the equities of the circumstances presented by all parties, compelling the local government to complete the rezoning within 60 days or the earliest time consistent with public hearing notice requirements in existence at the time the action was filed. The court shall retain jurisdiction to ensure that its order or judgment is carried out. If the court determines that its order or judgment is not carried out, the court shall issue further orders to ensure that the purposes and policies of this article are fulfilled, including ordering, after considering the equities of the circumstances presented by all parties, that any rezoning required by subparagraph (A) of paragraph (1) of subdivision (c) of Section 65583 be completed within 60 days or the earliest time consistent with public hearing notice requirements in existence at the time the action was filed and may impose sanctions on the city, county, or city and county.

(2) Any interested person may bring an action to compel compliance with the deadlines and requirements of paragraphs (1), (2), and (3) of

subdivision (c) of Section 65583. The action shall be brought pursuant to Section 1085 of the Code of Civil Procedure. In any such action, the city, county, or city and county shall bear the burden of proof.

SEC. 4. Section 65755 of the Government Code is amended to read:

65755. (a) The court shall include, in the order or judgment rendered pursuant to Section 65754, one or more of the following provisions for any or all types or classes of developments or any or all geographic segments of the city, county, or city and county until the city, county, or city and county has substantially complied with the requirements of Article 5 (commencing with Section 65300):

(1) Suspend the authority of the city, county, or city and county pursuant to Division 13 (commencing with Section 17910) of the Health and Safety Code, to issue building permits, or any category of building permits, and all other related permits, except that the city, county, or city and county shall continue to function as an enforcement agency for review of permit applications for appropriate codes and standards compliance, prior to the issuance of building permits and other related permits for residential housing for that city, county, or city and county.

(2) Suspend the authority of the city, county, or city and county, pursuant to Chapter 4 (commencing with Section 65800) to grant any and all categories of zoning changes, variances, or both.

(3) Suspend the authority of the city, county, or city and county, pursuant to Division 2 (commencing with Section 66410), to grant subdivision map approvals for any and all categories of subdivision map approvals.

(4) Mandate the approval of all applications for building permits, or other related construction permits, for residential housing where a final subdivision map, parcel map, or plot plan has been approved for the project, where the approval will not impact on the ability of the city, county, or city and county to properly adopt and implement an adequate housing element, and where the permit application conforms to all code requirements and other applicable provisions of law except those zoning laws held to be invalid by the final court order, and changes to the zoning ordinances adopted after such final court order which were enacted for the purpose of preventing the construction of a specific residential development.

(5) Mandate the approval of any or all final subdivision maps for residential housing projects which have previously received a tentative map approval from the city, county, or city and county pursuant to Division 2 (commencing with Section 66410) when the final map conforms to the approved tentative map, the tentative map has not expired, and where approval will not impact on the ability of the city, county, or city and county to properly adopt and implement an adequate housing element.

(6) Mandate that notwithstanding the provisions of Sections 66473.5 and 66474, any tentative subdivision map for a residential housing project shall be approved if all of the following requirements are met:

(A) The approval of the map will not significantly impair the ability of the city, county, or city and county to adopt and implement those elements or portions thereof of the general plan which have been held to be inadequate.

(B) The map complies with all of the provisions of Division 2 (commencing with Section 66410), except those parts which would require disapproval of the project due to the inadequacy of the general plan.

(C) The approval of the map will not affect the ability of the city, county, or city and county to adopt and implement an adequate housing element.

(D) The map is consistent with the portions of the general plan not found inadequate and the proposed revisions, if applicable, to the part of the plan held inadequate.

(b) Any order or judgment of a court which includes the remedies described in paragraphs (1), (2), or (3) of subdivision (a) shall exclude from the operation of that order or judgment any action, program, or project required by law to be consistent with a general or specific plan if the court finds that the approval or undertaking of the action, program, or project complies with both of the following requirements:

(1) That it will not significantly impair the ability of the city, county, or city and county to adopt or amend all or part of the applicable plan as may be necessary to make the plan substantially comply with the requirements of Article 5 (commencing with Section 65300) in the case of a general plan, or Article 8 (commencing with Section 65450) in the case of a specific plan.

(2) That it is consistent with those portions of the plan challenged in the action or proceeding and found by the court to substantially comply with applicable provisions of law.

The party seeking exclusion from any order or judgment of a court pursuant to this subdivision shall have the burden of showing that the action, program, or project complies with paragraphs (1) and (2).

(c) Notwithstanding Section 65754.4 or subdivisions (a) and (b), in any action or proceeding brought pursuant to subdivision (d) of Section 65009, no remedy pursuant to this section or injunction pursuant to Section 65754.5 shall abrogate, impair, or otherwise interfere with the full exercise of the rights and protections granted to (1) an applicant for a tentative map pursuant to Section 66474.2, or (2) a developer pursuant to Sections 65866 and 66498.1.

O

Senate Bill No. 341

CHAPTER 796

An act to amend Section 34176 of, and to add Section 34176.1 to, the Health and Safety Code, relating to redevelopment.

[Approved by Governor October 13, 2013. Filed with Secretary of State October 13, 2013.]

LEGISLATIVE COUNSEL'S DIGEST

SB 341, DeSaulnier. Redevelopment.

(1) Existing law dissolved redevelopment agencies and community development agencies, and provides for the designation of successor agencies that are required to wind down the affairs of the dissolved redevelopment agencies and to, among other things, make payments due for enforceable obligations, as defined. Existing law provides that the city, county, or city and county that authorized the creation of a redevelopment agency may elect to retain the housing assets and functions previously performed by the redevelopment agency. Existing law requires the entity assuming the housing functions of the former redevelopment agency to perform various functions.

This bill would change provisions relating to the functions to be performed by the entity assuming the housing functions of the former redevelopment agency to instead refer to the housing successor.

(2) Existing law provides that any funds transferred to the city, county, or city and county or the entity assuming the housing functions of the former redevelopment agency, together with any funds generated from housing assets, shall be maintained in a separate Low and Moderate Income Housing Asset Fund which shall be used in accordance with applicable housing-related provisions of the Community Redevelopment Law, as specified.

This bill would provide that funds in the Low and Moderate Income Housing Asset Fund shall be used in accordance with applicable housing-related provisions of the Community Redevelopment Law, except as specified. The bill would require the housing successor to expend funds in the Low and Moderate Income Housing Asset Fund, other than those expended to meet enforceable obligations, for the purpose of monitoring and preserving the long-term affordability of units subject to affordability restrictions or covenants entered into by the redevelopment agency or the housing successor, for homeless prevention and rapid rehousing services to individuals and families who are homeless or would be homeless but for this assistance, and for the development of affordable housing, as specified.

(3) Existing law requires that moneys in the Low and Moderate Income Housing Fund be used to assist housing for persons of low income and housing for persons of very low income in at least the same proportion as

the total number of housing units needed for each of those income groups bears to the total number of units needed for persons of moderate, low, and very low income within the community, as specified.

This bill would provide that these provisions shall not apply, and would instead require that if the aggregate number of units of deed-restricted rental housing restricted to seniors and assisted by the housing successor, its former redevelopment agency, and its host jurisdiction within the previous 10 years exceeds 50% of the aggregate number of units of deed-restricted rental housing assisted by the housing successor, its former redevelopment agency, and its host jurisdiction within the same time period, then the housing successor shall not expend these funds to assist additional senior housing units until the housing successor or its host jurisdiction assists, and construction has started on, a number of units available to all persons regardless of age that is equal to 50% of the aggregate number of units of deed-restricted rental housing units assisted by the housing successor, its former redevelopment agency, and its host jurisdiction within the same time period.

(4) Existing law requires that a specified percentage of all taxes that are allocated to a former redevelopment agency be used outside a specified project area upon a resolution of the agency and the legislative body that the use will be of benefit to the project.

This bill would provide that program income a housing successor receives shall not be associated with a project area and may be expended anywhere within the jurisdiction of the housing successor or transferred for the purpose of developing transit priority projects, permanent supportive housing, housing for agricultural employees, or special needs housing, without a finding of benefit to a project area, as specified. The bill would also authorize 2 or more housing successors, as specified, to agree to transfer funds among their respective Low and Moderate Income Housing Asset Funds, as specified.

(5) Existing law provides that if excess surplus accumulates in the Low and Moderate Income Housing Fund, the former redevelopment agency may adopt a plan for expenditure of the moneys. Existing law also requires that upon failure of the former redevelopment agency to expend or encumber excess surplus in the Low and Moderate Income Housing Fund, it shall be required to disburse, expend, or encumber its excess surplus, as specified.

This bill would provide that these provisions shall not apply, and would instead provide that if a housing successor has an excess surplus, the housing successor shall encumber the excess surplus for specified purposes or transfer the funds within 3 fiscal years. The bill would provide that if the housing successor fails to comply with this subdivision, the housing successor, within 90 days of the end of the 3rd fiscal year, shall transfer any excess surplus to the Department of Housing and Community Development for expenditure pursuant to the Multifamily Housing Program or the Joe Serna, Jr. Farmworker Housing Grant Program.

(6) Existing law requires a former redevelopment agency, for each interest in real property acquired using moneys from the Low and Moderate Income

Housing Fund, to, within 5 years from the date it first acquires the property interest for the development of housing affordable to persons and families of low and moderate income, initiate activities consistent with the development of the property for that purpose. Existing law provides that in the event that physical development of the property for this purpose has not begun by the end of a specified time period, or if the former redevelopment agency does not comply with this requirement, the property shall be sold and the moneys from the sale, less reimbursement to the agency for the cost of the sale, shall be deposited in the Low and Moderate Income Housing Fund.

This bill would provide that these provisions shall not apply to interests in real property acquired on or after February 1, 2012, and that with respect to interests in real property acquired by the former redevelopment agency prior to February 1, 2012, the specified time periods shall be deemed to have commenced on the date that the Department of Finance approved the property as a housing asset.

(7) Existing law requires every former redevelopment agency to submit the final report of any audit undertaken and an annual report to its legislative body, as specified. Existing law also requires the Controller to compile and publish annually reports of the financial transactions of each former community redevelopment agency, to make the data available to the Legislature and its agents upon request, and to publish this information for each project area of each redevelopment agency.

This bill would provide that these provisions shall not apply and, instead, would require the housing successor to conduct and provide to its governing body an independent financial audit of the Low and Moderate Income Housing Asset Fund. It would also require the housing successor to post specified information on its Internet Web site.

The people of the State of California do enact as follows:

SECTION 1. Section 34176 of the Health and Safety Code is amended to read:

34176. (a) (1) The city, county, or city and county that authorized the creation of a redevelopment agency may elect to retain the housing assets and functions previously performed by the redevelopment agency. If a city, county, or city and county elects to retain the authority to perform housing functions previously performed by a redevelopment agency, all rights, powers, duties, obligations, and housing assets, as defined in subdivision (e), excluding any amounts on deposit in the Low and Moderate Income Housing Fund and enforceable obligations retained by the successor agency, shall be transferred to the city, county, or city and county.

(2) The housing successor shall submit to the Department of Finance by August 1, 2012, a list of all housing assets that contains an explanation of how the assets meet the criteria specified in subdivision (e). The Department of Finance shall prescribe the format for the submission of the list. The list

shall include assets transferred between February 1, 2012, and the date upon which the list is created. The department shall have up to 30 days from the date of receipt of the list to object to any of the assets or transfers of assets identified on the list. If the Department of Finance objects to assets on the list, the housing successor may request a meet and confer process within five business days of receiving the department objection. If the transferred asset is deemed not to be a housing asset as defined in subdivision (e), it shall be returned to the successor agency and the provision of Section 34178.8 may apply. If a housing asset has been previously pledged to pay for bonded indebtedness, the successor agency shall maintain control of the asset in order to pay for the bond debt.

(3) For purposes of this section and Section 34176.1, "housing successor" means the entity assuming the housing function of a former redevelopment agency pursuant to this section.

(b) If a city, county, or city and county does not elect to retain the responsibility for performing housing functions previously performed by a redevelopment agency, all rights, powers, assets, duties, and obligations associated with the housing activities of the agency, excluding enforceable obligations retained by the successor agency and any amounts in the Low and Moderate Income Housing Fund, shall be transferred as follows:

(1) If there is no local housing authority in the territorial jurisdiction of the former redevelopment agency, to the Department of Housing and Community Development.

(2) If there is one local housing authority in the territorial jurisdiction of the former redevelopment agency, to that local housing authority.

(3) If there is more than one local housing authority in the territorial jurisdiction of the former redevelopment agency, to the local housing authority selected by the city, county, or city and county that authorized the creation of the redevelopment agency.

(c) Commencing on the operative date of this part, the housing successor may enforce affordability covenants and perform related activities pursuant to applicable provisions of the Community Redevelopment Law (Part 1 (commencing with Section 33000)), including, but not limited to, Section 33418.

(d) Except as specifically provided in Section 34191.4, any funds transferred to the housing successor, together with any funds generated from housing assets, as defined in subdivision (e), shall be maintained in a separate Low and Moderate Income Housing Asset Fund which is hereby created in the accounts of the housing successor.

(e) For purposes of this part, "housing asset" includes all of the following:

(1) Any real property, interest in, or restriction on the use of real property, whether improved or not, and any personal property provided in residences, including furniture and appliances, all housing-related files and loan documents, office supplies, software licenses, and mapping programs, that were acquired for low- and moderate-income housing purposes, either by purchase or through a loan, in whole or in part, with any source of funds.

(2) Any funds that are encumbered by an enforceable obligation to build or acquire low- and moderate-income housing, as defined by the Community Redevelopment Law (Part 1 (commencing with Section 33000)) unless required in the bond covenants to be used for repayment purposes of the bond.

(3) Any loan or grant receivable, funded from the Low and Moderate Income Housing Fund, from homebuyers, homeowners, nonprofit or for-profit developers, and other parties that require occupancy by persons of low or moderate income as defined by the Community Redevelopment Law (Part 1 (commencing with Section 33000)).

(4) Any funds derived from rents or operation of properties acquired for low- and moderate-income housing purposes by other parties that were financed with any source of funds, including residual receipt payments from developers, conditional grant repayments, cost savings and proceeds from refinancing, and principal and interest payments from homebuyers subject to enforceable income limits.

(5) A stream of rents or other payments from housing tenants or operators of low- and moderate-income housing financed with any source of funds that are used to maintain, operate, and enforce the affordability of housing or for enforceable obligations associated with low- and moderate-income housing.

(6) (A) Repayments of loans or deferrals owed to the Low and Moderate Income Housing Fund pursuant to subparagraph (G) of paragraph (1) of subdivision (d) of Section 34171, which shall be used consistent with the affordable housing requirements in the Community Redevelopment Law (Part 1 (commencing with Section 33000)).

(B) Loan or deferral repayments shall not be made prior to the 2013–14 fiscal year. Beginning in the 2013–14 fiscal year, the maximum repayment amount authorized each fiscal year for repayments made pursuant to this paragraph and subdivision (b) of Section 34191.4 combined shall be equal to one-half of the increase between the amount distributed to taxing entities pursuant to paragraph (4) of subdivision (a) of Section 34183 in that fiscal year and the amount distributed to taxing entities pursuant to that paragraph in the 2012–13 base year. Loan or deferral repayments made pursuant to this paragraph shall take priority over amounts to be repaid pursuant to subdivision (b) of Section 34191.4.

(f) If a development includes both low- and moderate-income housing that meets the definition of a housing asset under subdivision (e) and other types of property use, including, but not limited to, commercial use, governmental use, open space, and parks, the oversight board shall consider the overall value to the community as well as the benefit to taxing entities of keeping the entire development intact or dividing the title and control over the property between the housing successor and the successor agency or other public or private agencies. The disposition of those assets may be accomplished by a revenue-sharing arrangement as approved by the oversight board on behalf of the affected taxing entities.

(g) (1) (A) The housing successor may designate the use of and commit indebtedness obligation proceeds that remain after the satisfaction of enforceable obligations that have been approved in a Recognized Obligation Payment Schedule and that are consistent with the indebtedness obligation covenants. The proceeds shall be derived from indebtedness obligations that were issued for the purposes of affordable housing prior to January 1, 2011, and were backed by the Low and Moderate Income Housing Fund. Enforceable obligations may be satisfied by the creation of reserves for the projects that are the subject of the enforceable obligation that are consistent with the contractual obligations for those projects, or by expending funds to complete the projects.

(B) The housing successor shall provide notice to the successor agency of any designations of use or commitments of funds specified in subparagraph (A) that it wishes to make at least 20 days before the deadline for submission of the Recognized Obligation Payment Schedule to the oversight board. Commitments and designations shall not be valid and binding on any party until they are included in an approved and valid Recognized Obligation Payment Schedule. The review of these designations and commitments by the successor agency, oversight board, and Department of Finance shall be limited to a determination that the designations and commitments are consistent with bond covenants and that there are sufficient funds available.

(2) Funds shall be used and committed in a manner consistent with the purposes of the Low and Moderate Income Housing Asset Fund. Notwithstanding any other law, the successor agency shall retain and expend the excess housing obligation proceeds at the discretion of the housing successor, provided that the successor agency ensures that the proceeds are expended in a manner consistent with the indebtedness obligation covenants and with any requirements relating to the tax status of those obligations. The amount expended shall not exceed the amount of indebtedness obligation proceeds available and such expenditure shall constitute the creation of excess housing proceeds expenditures to be paid from the excess proceeds. Excess housing proceeds expenditures shall be listed separately on the Recognized Obligation Payment Schedule submitted by the successor agency.

(h) This section shall not be construed to provide any stream of tax increment financing.

SEC. 2. Section 34176.1 is added to the Health and Safety Code, to read:

34176.1. Funds in the Low and Moderate Income Housing Asset Fund described in subdivision (d) of Section 34176 shall be subject to the provisions of the Community Redevelopment Law (Part 1 (commencing with Section 33000)) relating to the Low and Moderate Income Housing Fund, except as follows:

(a) Subdivision (d) of Section 33334.3 and subdivision (a) of Section 33334.4 shall not apply. Instead, funds received from the successor agency for items listed on the Recognized Obligation Payment Schedule shall be expended to meet the enforceable obligations, and the housing successor shall expend all other funds in the Low and Moderate Income Housing Asset Fund as follows:

(1) For the purpose of monitoring and preserving the long-term affordability of units subject to affordability restrictions or covenants entered into by the redevelopment agency or the housing successor and for the purpose of administering the activities described in paragraphs (2) and (3), a housing successor may expend per fiscal year up to an amount equal to 2 percent of the statutory value of real property owned by the housing successor and of loans and grants receivable, including real property and loans and grants transferred to the housing successor pursuant to Section 34176 and real property purchased and loans and grants made by the housing successor. If this amount is less than two hundred thousand dollars ($200,000) for any given fiscal year, the housing successor may expend up to two hundred thousand dollars ($200,000) in that fiscal year for these purposes. The Department of Housing and Community Development shall annually publish on its Internet Web site an adjustment to this amount to reflect any change in the Consumer Price Index for All Urban Consumers published by the federal Department of Labor for the preceding calendar year. For purposes of this paragraph, "statutory value of real property" means the value of properties formerly held by the former redevelopment agency as listed on the housing asset transfer form approved by the Department of Finance pursuant to paragraph (2) of subdivision (a) of Section 34176, the value of the properties transferred to the housing successor pursuant to subdivision (f) of Section 34181, and the purchase price of properties purchased by the housing successor.

(2) Notwithstanding Section 33334.2, if the housing successor has fulfilled all obligations pursuant to Sections 33413 and 33418, the housing successor may expend up to two hundred fifty thousand dollars ($250,000) per fiscal year for homeless prevention and rapid rehousing services for individuals and families who are homeless or would be homeless but for this assistance, including the provision of short-term or medium-term rental assistance, housing relocation and stabilization services including housing search, mediation, or outreach to property owners, credit repair, security or utility deposits, utility payments, rental assistance for a final month at a location, moving cost assistance, and case management, or other appropriate activities for homelessness prevention and rapid rehousing of persons who have become homeless.

(3) (A) The housing successor shall expend all funds remaining in the Low and Moderate Income Housing Asset Fund after the expenditures allowed pursuant to paragraphs (1) and (2) for the development of housing affordable to and occupied by households earning 80 percent or less of the area median income, with at least 30 percent of these remaining funds expended for the development of rental housing affordable to and occupied by households earning 30 percent or less of the area median income and no more than 20 percent of these remaining funds expended for the development of housing affordable to and occupied by households earning between 60 percent and 80 percent of the area median income. A housing successor

shall demonstrate in the annual report described in subdivision (f), for 2019, and every five years thereafter, that the housing successor's expenditures from January 1, 2014, through the end of the latest fiscal year covered in the report comply with the requirements of this subparagraph.

(B) If the housing successor fails to comply with the extremely low income requirement in any five-year report, then the housing successor shall ensure that at least 50 percent of these remaining funds expended in each fiscal year following the latest fiscal year following the report are expended for the development of rental housing affordable to, and occupied by, households earning 30 percent or less of the area median income until the housing successor demonstrates compliance with the extremely low income requirement in an annual report described in subdivision (f).

(C) If the housing successor exceeds the expenditure limit for households earning between 60 percent and 80 percent of the area median income in any five-year report, the housing successor shall not expend any of the remaining funds for households earning between 60 percent and 80 percent of the area median income until the housing successor demonstrates compliance with this limit in an annual report described in subdivision (f).

(D) For purposes of this subdivision, "development" means new construction, acquisition and rehabilitation, substantial rehabilitation as defined in Section 33413, the acquisition of long-term affordability covenants on multifamily units as described in Section 33413, or the preservation of an assisted housing development that is eligible for prepayment or termination or for which within the expiration of rental restrictions is scheduled to occur within five years as those terms are defined in Section 65863.10 of the Government Code. Units described in this subparagraph may be counted towards any outstanding obligations pursuant to Section 33413, provided that the units meet the requirements of that section and are counted as provided in that section.

(b) Subdivision (b) of Section 33334.4 shall not apply. Instead, if the aggregate number of units of deed-restricted rental housing restricted to seniors and assisted individually or jointly by the housing successor, its former redevelopment agency, and its host jurisdiction within the previous 10 years exceeds 50 percent of the aggregate number of units of deed-restricted rental housing assisted individually or jointly by the housing successor, its former redevelopment agency, and its host jurisdiction within the same time period, then the housing successor shall not expend these funds to assist additional senior housing units until the housing successor or its host jurisdiction assists, and construction has commenced, a number of units available to all persons, regardless of age, that is equal to 50 percent of the aggregate number of units of deed-restricted rental housing units assisted individually or jointly by the housing successor, its former redevelopment agency, and its host jurisdiction within the time period described above.

(c) (1) Program income a housing successor receives shall not be associated with a project area and, notwithstanding subdivision (g) of Section 33334.2, may be expended anywhere within the jurisdiction of the housing successor or transferred pursuant to paragraph (2) without a finding of benefit to a project area. For purposes of this paragraph, “program income” means the sources described in paragraphs (3), (4), and (5) of subdivision (e) of Section 34176 and interest earned on deposits in the account.

(2) Two or more housing successors within a county, within a single metropolitan statistical area, within 15 miles of each other, or that are in contiguous jurisdictions may enter into an agreement to transfer funds among their respective Low and Moderate Income Housing Asset Funds for the sole purpose of developing transit priority projects as defined in subdivisions (a) and (b) of Section 21155 of the Public Resources Code, permanent supportive housing as defined in paragraph (2) of subdivision (b) of Section 50675.14, housing for agricultural employees as defined in subdivision (g) of Section 50517.5, or special needs housing as defined in federal or state law or regulation if all of the following conditions are met:

(A) Each participating housing successor has made a finding based on substantial evidence, after a public hearing, that the agreement to transfer funds will not cause or exacerbate racial, ethnic, or economic segregation.

(B) The development to be funded shall not be located in a census tract where more than 50 percent of its population is very low income, unless the development is within one-half mile of a major transit stop or high-quality transit corridor as defined in paragraph (3) of subdivision (b) of Section 21155 of the Public Resources Code.

(C) The completed development shall not result in a reduction in the number of housing units or a reduction in the affordability of housing units on the site where the development is to be built.

(D) A transferring housing successor shall not have any outstanding obligations pursuant to Section 33413.

(E) No housing successor may transfer more than one million dollars ($1,000,000) per fiscal year.

(F) The jurisdictions of the transferring and receiving housing successors each have an adopted housing element that the Department of Housing and Community Development has found pursuant to Section 65585 of the Government Code to be in substantial compliance with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code and have submitted to the Department of Housing and Community Development the annual progress report required by Section 65400 of the Government Code within the preceding 12 months.

(G) Transferred funds shall only assist rental units affordable to, and occupied by, households earning 60 percent or less of the area median income.

(H) Transferred funds not encumbered within two years shall be transferred to the Department of Housing and Community Development for expenditure pursuant to the Multifamily Housing Program or the Joe Serna, Jr. Farmworker Housing Grant Program.

(d) Sections 33334.10 and 33334.12 shall not apply. Instead, if a housing successor has an excess surplus, the housing successor shall encumber the excess surplus for the purposes described in paragraph (3) of subdivision

(a) or transfer the funds pursuant to paragraph (2) of subdivision (c) within three fiscal years. If the housing successor fails to comply with this subdivision, the housing successor, within 90 days of the end of the third fiscal year, shall transfer any excess surplus to the Department of Housing and Community Development for expenditure pursuant to the Multifamily Housing Program or the Joe Serna, Jr. Farmworker Housing Grant Program. For purposes of this subdivision, "excess surplus" shall mean an unencumbered amount in the account that exceeds the greater of one million dollars ($1,000,000) or the aggregate amount deposited into the account during the housing successor's preceding four fiscal years, whichever is greater.

(e) Section 33334.16 shall not apply to interests in real property acquired on or after February 1, 2012. With respect to interests in real property acquired by the former redevelopment agency prior to February 1, 2012, the time periods described in Section 33334.16 shall be deemed to have commenced on the date that the Department of Finance approved the property as a housing asset.

(f) Section 33080.1 of this code and Section 12463.3 of the Government Code shall not apply. Instead, the housing successor shall conduct, and shall provide to its governing body, an independent financial audit of the Low and Moderate Income Housing Asset Fund within six months after the end of each fiscal year, which may be included in the independent financial audit of the host jurisdiction. If the housing successor is a city or county, it shall also include in its report pursuant to Section 65400 of the Government Code and post on its Internet Web site all of the following information for the previous fiscal year. If the housing successor is not a city or county, it shall also provide to its governing body and post on its Internet Web site all of the following information for the previous fiscal year:

(1) The amount deposited to the Low and Moderate Income Housing Asset Fund, distinguishing any amounts deposited for items listed on the Recognized Obligation Payment Schedule from other amounts deposited.

(2) A statement of the balance in the fund as of the close of the fiscal year, distinguishing any amounts held for items listed on the Recognized Obligation Payment Schedule from other amounts.

(3) A description of expenditures from the fund by category, including, but not limited to, expenditures (A) for monitoring and preserving the long-term affordability of units subject to affordability restrictions or covenants entered into by the redevelopment agency or the housing successor and administering the activities described in paragraphs (2) and (3) of subdivision (a), (B) for homeless prevention and rapid rehousing services for the development of housing described in paragraph (2) of subdivision (a), and (C) for the development of housing pursuant to paragraph (3) of subdivision (a).

(4) As described in paragraph (1) of subdivision (a), the statutory value of real property owned by the housing successor, the value of loans and grants receivable, and the sum of these two amounts.

(5) A description of any transfers made pursuant to paragraph (2) of subdivision (c) in the previous fiscal year and, if still unencumbered, in earlier fiscal years and a description of and status update on any project for which transferred funds have been or will be expended if that project has not yet been placed in service.

(6) A description of any project for which the housing successor receives or holds property tax revenue pursuant to the Recognized Obligation Payment Schedule and the status of that project.

(7) For interests in real property acquired by the former redevelopment agency prior to February 1, 2012, a status update on compliance with Section 33334.16. For interests in real property acquired on or after February 1, 2012, a status update on the project.

(8) A description of any outstanding obligations pursuant to Section 33413 that remained to transfer to the housing successor on February 1, 2012, of the housing successor's progress in meeting those obligations, and of the housing successor's plans to meet unmet obligations. In addition, the housing successor shall include in the report posted on its Internet Web site the implementation plans of the former redevelopment agency.

(9) The information required by subparagraph (B) of paragraph (3) of subdivision (a).

(10) The percentage of units of deed-restricted rental housing restricted to seniors and assisted individually or jointly by the housing successor, its former redevelopment agency, and its host jurisdiction within the previous 10 years in relation to the aggregate number of units of deed-restricted rental housing assisted individually or jointly by the housing successor, its former redevelopment agency, and its host jurisdiction within the same time period.

(11) The amount of any excess surplus, the amount of time that the successor agency has had excess surplus, and the housing successor's plan for eliminating the excess surplus.

O

Condition of Title Guarantee (11/07/13)

SUBJECT TO THE LIMITATIONS CONTAINED HEREIN, THE EXCLUSIONS FROM COVERAGE, THE LIMITS OF LIABILITY AND OTHER PROVISIONS OF THE CONDITIONS AND STIPULATIONS HERETO ANNEXED AND MADE A PART OF THIS GUARANTEE,

BLANK TITLE INSURANCE COMPANY
a corporation, herein called the Company,

GUARANTEES

the Assured named in Schedule A against loss not exceeding the liability amount stated in Schedule A which the Assured shall sustain by reason of any incorrectness in the assurance which the Company hereby gives that, according to the public records, as of Date of Guarantee shown in Schedule A:

1. The title to the herein described estate or interest is vested in the vestee named in Schedule A.

2. Except for the matters shown in Schedule B, there are no defects, liens, encumbrances or other matters affecting title to the estate or interest in the land shown in Schedule A, which matters are not necessarily shown in the order of their priority.

[BY ACCEPTANCE OF THIS GUARANTEE, THE ASSURED
(1) RECOGNIZES AND AGREES THAT IT IS EXTREMELY DIFFICULT, IF NOT IMPOSSIBLE, TO DETERMINE THE EXTENT OF SUCH MONETARY LOSS OR DAMAGE THAT WOULD ARISE FROM ERRORS OR OMISSIONS IN THIS GUARANTEE AND THAT THE FEE CHARGED THEREFOR IS NOMINAL IN RELATION TO THE POTENTIAL LOSS OR DAMAGE THAT COULD ARISE FROM SUCH ERRORS OR OMISSIONS, AND
(2) UNDERSTANDS THAT THE COMPANY WOULD NOT ISSUE THIS GUARANTEE FOR SUCH FEE UNLESS THE ASSURED AGREED, AND DOES HEREBY AGREE, AS PART OF THE CONSIDERATION FOR THE ISSUANCE OF THIS GUARANTEE, THAT THE COMPANY'S LIABILITY IS STRICTLY LIMITED AS SET FOR IN SECTION 7 OF THE GUARANTEE CONDITIONS AND STIPULATIONS WHICH, AMONG OTHER PROVISIONS, STATES THAT THE COMPANY'S LIABILITY CANNOT EXCEED THE AMOUNT OF LIABILITY STATED IN SCHEDULE A.]

Schedule A

Order No. ___________________
Liability: $___________________
Fee: ________________________

1. Name of Assured:

2. Date of Guarantee:

3. The estate or interest in the Land which is covered by this Guarantee is:

4. Title to the estate or interest in the Land is vested in:

5. The Land referred to in this Guarantee is described as follows:

Schedule B

Defects, liens, encumbrances or other matters affecting title:

1. Any adverse lien or charge upon title that has attached to title upon its recording in the public records by naming the following vestee(s) shown in Schedule A as debtor or obligor thereunder:

________________________________ [enter name of vestee(s)]

There exist in the public records at Date of Guarantee numerous liens or other charges upon title naming as debtor or obligor persons or entities with the same or similar names as that of such vestee(s), and the Company is unable to determine the effect of such matters without the Assured providing information acceptable to the Company as to the identity of such vestee(s). An acceptable proof of identity would be submission of the Company's Statement of Information completed and signed by each of the above name vestee(s). Upon receipt of such information, the Company, by endorsement to this guarantee, will either delete the foregoing matter or limit its extent to matters determined thereby to affect the interest of the vestee(s) in question or that nonetheless will remain excepted from coverage. **[DELETE IF G.I. MATTERS ARE SHOWN]**

2.

3.

SCHEDULE OF EXCLUSIONS FROM COVERAGE OF THIS GUARANTEE

1. *Except to the extent* that specific assurances are provided in Schedule A of this Guarantee, the Company assumes no liability for loss or damage by reason of the following:

(a) Defects, liens, encumbrances, adverse claims or other matters against the title, whether or not shown by the public records.

(b) (1) Taxes or assessments of any taxing authority that levies taxes or assessments on real property; or, (2) Proceedings by a public agency which may result in taxes or assessments, or notices of such proceedings, whether or not the matters excluded under (1) or (2) are shown by the records of the taxing authority or by the public records.

(c) (1) Unpatented mining claims; (2) reservations or exceptions in patents or in Acts authorizing the issuance thereof; (3) water rights, claims or title to water, whether or not the matters excluded under (1), (2) or (3) are shown by the public records.

2. *Notwithstanding* any specific assurances which are provided in Schedule A of this Guarantee, the Company assumes no liability for loss or damage by reason of the following:

(a) Defects, liens, encumbrances, adverse claims or other matters affecting the title to any property beyond the lines of the land expressly described in the description set forth in Schedule (A), (C) or in Part 2 of this Guarantee, or title to streets, roads, avenues, lanes, ways or waterways to which such land abuts, or the right to maintain therein vaults, tunnels, ramps or any structure or improvements; or any rights or easements therein, unless such property, rights or easements are expressly and specifically set forth in said description.

(b) Defects, liens, encumbrances, adverse claims or other matters, whether or not shown by the public records; (1) which are created, suffered, assumed or agreed to by one or more of the Assureds; (2) which result in no loss to the Assured; or (3) which do not result in the invalidity or potential invalidity of any judicial or non-judicial proceeding which is within the scope and purpose of the assurances provided.

(c) The identity of any party shown or referred to in Schedule A.

(d) The validity, legal effect or priority of any matter shown or referred to in this Guarantee.

GUARANTEE CONDITIONS AND STIPULATIONS

1. Definition of Terms.

The following terms when used in the Guarantee mean:

(a) the "Assured": the party or parties named as the Assured in this Guarantee, or on a supplemental writing executed by the Company.

(b) "land": the land described or referred to in Schedule (A)(C) or in Part 2, and improvements affixed thereto which by law constitute real property. The term "land" does not include any property beyond the lines of the area described or referred to in Schedule (A)(C) or in Part 2, nor any right, title, interest, estate or easement in abutting streets, roads, avenues, alleys, lanes, ways or waterways.

(c) "mortgage": mortgage, deed of trust, trust deed, or other security instrument.

(d) "public records": records established under state statutes at Date of Guarantee for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without knowledge.

(e) "date": the effective date.

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2. Notice of Claim to be Given by Assured Claimant.

An Assured shall notify the Company promptly in writing in case knowledge shall come to an Assured hereunder of any claim of title or interest which is adverse to the title to the estate or interest, as stated herein, and which might cause loss or damage for which the Company may be liable by virtue of this Guarantee. If prompt notice shall not be given to the Company, then all liability of the Company shall terminate with regard to the matter or matters for which prompt notice is required; provided, however, that failure to notify the Company shall in no case prejudice the rights of any Assured under this Guarantee unless the Company shall be prejudiced by the failure and then only to the extent of the prejudice.

3. No Duty to Defend or Prosecute.

The Company shall have no duty to defend or prosecute any action or proceeding to which the Assured is a party, notwithstanding the nature of any allegation in such action or proceeding.

4. Company's Option to Defend or Prosecute Actions; Duty of Assured Claimant to Cooperate.

Even though the Company has no duty to defend or prosecute as set forth in Paragraph 3 above:

(a) The Company shall have the right, at its sole option and cost, to institute and prosecute any action or proceeding, interpose a defense, as limited in (b), or to do any other act which in its opinion may be necessary or desirable to establish the title to the estate or interest as stated herein, or to establish the lien rights of the Assured, or to prevent or reduce loss or damage to the Assured. The Company may take any appropriate action under the terms of this Guarantee, whether or not it shall be liable hereunder, and shall not thereby concede liability or waive any provision of this Guarantee. If the Company shall exercise its rights under this paragraph, it shall do so diligently.

(b) If the Company elects to exercise its options as stated in Paragraph 4(a) the Company shall have the right to select counsel of its choice (subject to the right of such Assured to object for reasonable cause) to represent the Assured and shall not be liable for and will not pay the fees of any other counsel, nor will the Company pay any fees, costs or expenses incurred by an Assured in the defense of those causes of action which allege matters not covered by this Guarantee.

(c) Whenever the Company shall have brought an action or interposed a defense as permitted by the provisions of this Guarantee, the Company may pursue any litigation to final determination by a court of competent jurisdiction and expressly reserves the right, in its sole discretion, to appeal from an adverse judgment or order.

(d) In all cases where this Guarantee permits the Company to prosecute or provide for the defense of any action or proceeding, an Assured shall secure to the Company the right to so prosecute or provide for the defense of any action or proceeding, and all appeals therein, and permit the Company to use, at its option, the name of such Assured for this purpose. Whenever requested by the Company, an Assured, at the Company's expense, shall give the Company all reasonable aid in any action or proceeding, securing evidence, obtaining witnesses, prosecuting or defending the action or lawful act which in the opinion of the Company may be necessary or desirable to establish the title to the estate or interest as stated herein, or to establish the lien rights of the Assured. If the Company is prejudiced by the failure of the Assured to furnish the required cooperation, the Company's obligations to the Assured under the Guarantee shall terminate.

5. Proof of Loss or Damage.

In addition to and after the notices required under Section 2 of these Conditions and Stipulations have been provided to the Company, a proof of loss or damage signed and sworn to by the Assured shall be furnished to the Company within ninety (90) days after the Assured shall ascertain the facts giving rise to the loss or damage. The proof of loss or damage shall describe the matters covered by this Guarantee which constitute the basis of loss or damage and shall state, to the extent possible, the basis of calculating the amount of the loss or damage. If the Company is prejudiced by the failure of the Assured to provide the required proof of loss or damage, the Company's obligation to such assured under the Guarantee shall terminate. In addition, the Assured may reasonably be required to submit to examination under oath by any authorized representative of the Company and shall produce for examination, inspection and copying, at such reasonable times and places as may be designated by any authorized representative of the Company, all records, books, ledgers, checks, correspondence and memoranda, whether bearing a date before or after Date of Guarantee, which reasonably pertain to the loss or damage. Further, if requested by any authorized representative of the Company, the Assured shall grant its permission, in writing, for any authorized representative of the Company to examine, inspect and copy all

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records, books, ledgers, checks, correspondence and memoranda in the custody or control of a third party, which reasonably pertain to the loss or damage. All information designated as confidential by the Assured provided to the Company pursuant to this Section shall not be disclosed to others unless, in the reasonable judgment of the Company, it is necessary in the administration of the claim. Failure of the Assured to submit for examination under oath, produce other reasonably requested information or grant permission to secure reasonably necessary information from third parties as required in the above paragraph, unless prohibited by law or governmental regulation, shall terminate any liability of the Company under this Guarantee to the Assured for that claim.

6. Options to Pay or Otherwise Settle Claims: Termination of Liability.

In case of a claim under this Guarantee, the Company shall have the following additional options:

(a) To Pay or Tender Payment of the Amount of Liability or to Purchase the Indebtedness.

The Company shall have the option to pay or settle or compromise for or in the name of the Assured any claim which could result in loss to the Assured within the coverage of this Guarantee, or to pay the full amount of this Guarantee or, if this Guarantee is issued for the benefit of a holder of a mortgage or a lienholder, the Company shall have the option to purchase the indebtedness secured by said mortgage or said lien for the amount owing thereon, together with any costs, reasonable attorneys' fees and expenses incurred by the Assured claimant which were authorized by the Company up to the time of purchase.

Such purchase, payment or tender of payment of the full amount of the Guarantee shall terminate all liability of the Company hereunder. In the event after notice of claim has been given to the Company by the Assured the Company offers to purchase said indebtedness, the owner of such indebtedness shall transfer and assign said indebtedness, together with any collateral security, to the Company upon payment of the purchase price.

Upon the exercise by the Company of the option provided for in Paragraph (a) the Company's obligation to the Assured under this Guarantee for the claimed loss or damage, other than to make the payment required in that paragraph, shall terminate, including any obligation to continue the defense or prosecution of any litigation for which the Company has exercised its options under Paragraph 4, and the Guarantee shall be surrendered to the Company for cancellation.

(b) To Pay or Otherwise Settle With Parties Other Than the Assured or With the Assured Claimant.

To pay or otherwise settle with other parties for or in the name of an Assured claimant any claim assured against under this Guarantee, together with any costs, attorneys' fees and expenses incurred by the Assured claimant which were authorized by the Company up to the time of payment and which the Company is obligated to pay.

Upon the exercise by the Company of the option provided for in Paragraph (b) the Company's obligation to the Assured under this Guarantee for the claimed loss or damage, other than to make the payment required in that paragraph, shall terminate, including any obligation to continue the defense or prosecution of any litigation for which the Company has exercised its options under Paragraph 4.

7. Determination and Extent of Liability.

This Guarantee is a contract of Indemnity against actual monetary loss or damage sustained or incurred by the Assured claimant who has suffered loss or damage by reason of reliance upon the assurances set forth in this Guarantee and only to the extent herein described, and subject to the Exclusions From Coverage of This Guarantee.

The liability of the Company under this Guarantee to the Assured shall not exceed the least of:

(a) the amount of liability stated in Schedule A or in Part 2;

(b) the amount of the unpaid principal indebtedness secured by the mortgage of an Assured mortgagee, as limited or provided under Section 6 of these Conditions and Stipulations or as reduced under Section 9 of these Conditions and Stipulations, at the time the loss or damage assured against by this Guarantee occurs, together with interest thereon; or

(c) the difference between the value of the estate or interest covered hereby as stated herein and the value of the estate or interest subject to any defect, lien or encumbrance assured against by this Guarantee.

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8. Limitation of Liability.

(a) If the Company establishes the title, or removes the alleged defect, lien or encumbrance, or cures any other matter assured against by this Guarantee in a reasonably diligent manner by any method, including litigation and the completion of any appeals therefrom, it shall have fully performed its obligations with respect to that matter and shall not be liable for any loss or damage caused thereby.

(b) In the event of any litigation by the Company or with the Company's consent, the Company shall have no liability for loss or damage until there has been a final determination by a court of competent jurisdiction, and disposition of all appeals therefrom, adverse to the title, as stated herein.

(c) The Company shall not be liable for loss or damage to any Assured for liability voluntarily assumed by the Assured in settling any claim or suit without the prior written consent of the Company.

9. Reduction of Liability or Termination of Liability.

All payments under this Guarantee, except payments made for costs, attorneys' fees and expenses pursuant to Paragraph 4 shall reduce the amount of liability pro tanto.

10. Payment of Loss.

(a) No payment shall be made without producing this Guarantee for endorsement of the payment unless the Guarantee has been lost or destroyed, in which case proof of loss or destruction shall be furnished to the satisfaction of the Company.

(b) When liability and the extent of loss or damage has been definitely fixed in accordance with these Conditions and Stipulations, the loss or damage shall be payable within thirty (30) days thereafter.

11. Subrogation Upon Payment or Settlement.

Whenever the Company shall have settled and paid a claim under this Guarantee, all right of subrogation shall vest in the Company unaffected by any act of the Assured claimant.

The Company shall be subrogated to and be entitled to all rights and remedies which the Assured would have had against any person or property in respect to the claim had this Guarantee not been issued. If requested by the Company, the Assured shall transfer to the Company all rights and remedies against any person or property necessary in order to perfect this right of subrogation. The Assured shall permit the Company to sue, compromise or settle in the name of the Assured and to use the name of the Assured in any transaction or litigation involving these rights or remedies.

If a payment on account of a claim does not fully cover the loss of the Assured the Company shall be subrogated to all rights and remedies of the Assured after the Assured shall have recovered its principal, interest, and costs of collection.

12. Arbitration.

Unless prohibited by applicable law, either the Company or the Assured may demand arbitration pursuant to the Title Insurance Arbitration Rules of the American Land Title Association. Arbitrable matters may include, but are not limited to, any controversy or claim between the Company and the Assured arising out of or relating to this Guarantee, any service of the Company in connection with its issuance or the breach of a Guarantee provision or other obligation. All arbitrable matters when the Amount of Liability is $2,000,000 or less shall be arbitrated at the option of either the Company or the Assured. All arbitrable matters when the amount of liability is in excess of $2,000,000 shall be arbitrated only when agreed to by both the Company and the Assured. The Rules in effect at Date of Guarantee shall be binding upon the parties. The award may include attorneys' fees only if the laws of the state in which the land is located permits a court to award attorneys' fees to a prevailing party. Judgment upon the award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof.

The law of the situs of the land shall apply to an arbitration under the Title Insurance Arbitration Rules.

A copy of the Rules may be obtained from the Company upon request.

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13. Liability Limited to This Guarantee; Guarantee Entire Contract.

(a) This Guarantee together with all endorsements, if any, attached hereto by the Company is the entire Guarantee and contract between the Assured and the Company. In interpreting any provision of this Guarantee, this Guarantee shall be construed as a whole.

(b) Any claim of loss or damage, whether or not based on negligence, or any action asserting such claim, shall be restricted to this Guarantee.

(c) No amendment of or endorsement to this Guarantee can be made except by a writing endorsed hereon or attached hereto signed by either the President, a Vice President, the Secretary, an Assistant Secretary, or validating officer or authorized signatory of the Company.

14. Notices, Where Sent.

All notices required to be given the Company and any statement in writing required to be furnished the Company shall include the number of this Guarantee and shall be addressed to the Company at _____________________________________.

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R. Therien

From:	Hammann, Paul [phammann@firstam.com]
Sent:	Thursday, September 05, 2013 4:32 PM
To:	Flores, Paul
Cc:	Roger Therien
Subject:	ALTA Forms Committee - Current Draft of Revised Definition of "Public Records"

Paul:

Here is the current draft of the definition of "Public Records" to which I made reference. As I mentioned, this comes from the ALTA Forms Committee's ongoing policy revision project.

"Public Records": Records, excluding any record in any federal, state or local office pertaining to environmental protection, planning, zoning, building, health or public safety matters ~~described in any Exclusion contained in the policy~~, established under state statutes at Date of Policy for the purpose of imparting constructive notice of matters relating to the title to real property to purchasers for value and without Knowledge. With respect to Covered Risk 5(d), "Public Records" shall also include environmental protection liens filed in the records of the clerk of the United States District Court for the district where the Land is located.

Paul

****
This message may contain confidential or proprietary information intended only for the use of the addressee(s) named above or may contain information that is legally privileged. If you are not the intended addressee, or the person responsible for delivering it to the intended addressee, you are hereby notified that reading, disseminating, distributing or copying this message is strictly prohibited. If you have received this message by mistake, please immediately notify us by replying to the message and delete the original message and any copies immediately thereafter.
If you received this email as a commercial message and would like to opt out of future commercial messages, please let us know and we will remove you from our distribution list.
Thank you.~
****
FAFLD

ENDORSEMENT
Attached to Policy No. __________
Issued by
BLANK TITLE INSURANCE COMPANY

1. For purposes of this endorsement only
   a. ”Modification” means the agreement between _______ and ________ dated ________ [and recorded _________ as document number] _______.
   b. ”Date of Endorsement” means ____________.

2. The Amount of Insurance is increased to $_________.

3. Subject to the exclusions in Section[s] 4 [and 5] of this endorsement, the Exclusions from Coverage, the Exceptions contained in Schedule B, and the Conditions contained in the policy, and any exclusion or exception in any prior endorsement, the Company insures as of Date of Endorsement against loss or damage sustained by the Insured by reason of any of the following:
   a. The invalidity or unenforceability of the lien of the Insured Mortgage upon the Title as a result of the Modification;
   b. The lack of priority of the lien of the Insured Mortgage over defects in or liens or encumbrances on the Title, except: [*Specify additional exceptions, if any*];
   c. The failure of the following matters to be subordinate to the lien of the Insured Mortgage: [*Specify matters to be insured as subordinate, if any*].

4. This endorsement does not insure against loss or damage, and the Company will not pay costs, attorneys' fees, or expenses, by reason of any claim that arises out of the transaction creating the Modification by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws that is based on:
   a. the Modification being deemed a fraudulent conveyance or fraudulent transfer; or
   b. the Modification being deemed a preferential transfer except where the preferential transfer results from the failure
      i. to timely record the instrument of transfer; or
      ii. of such recordation to impart notice to a purchaser for value or to a judgment or lien creditor.

[5. This endorsement does not insure against loss or damage, and the Company will not pay costs, attorneys’ fees, or expenses, by reason of *the invalidity, unenforceability or lack of priority of the lien of the Insured Mortgage because all applicable mortgage recording or similar intangible taxes were not paid* at time of recording of the Modification].

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

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BLANK TITLE INSURANCE COMPANY

By: _______________________________________
Authorized Signatory

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ENDORSEMENT

Attached to Policy No. __________

Issued by

BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the exclusion in Section 4 of this endorsement; and the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.
2. For purposes of this endorsement only, “Improvement” means a building on the Land at Date of Policy.
3. The Company insures against loss or damage sustained by the Insured by reason of the enforced removal or alteration of any Improvement resulting from the future exercise of any right existing at Date of Policy to use the surface of the Land for the extraction or development of water excepted from the description of the Land or excepted in Schedule B.
4. This endorsement does not insure against loss or damage (and the Company will not pay costs, attorneys' fees, or expenses) resulting from:
   a. contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence; [or]
   b. negligence by a person or an Entity exercising a right to extract or develop water[; or
   c. the exercise of the rights described in (   )]. *

   * Instructional note: identify the interest excepted from the description of the Land in Schedule A or excepted in Schedule B that you intend to exclude from this coverage.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

By: ______________________________________

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ENDORSEMENT

Attached to Policy No. __________

Issued by

BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the exclusion in Section 4 of this endorsement; and the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.
2. For purposes of this endorsement only, "Improvement" means a building, structure located on the surface of the Land, and any paved road, walkway, parking area, driveway, or curb, affixed to the Land at Date of Policy and that by law constitutes real property, but excluding any crops, landscaping, lawn, shrubbery, or trees.
3. The Company insures against loss or damage sustained by the Insured by reason of the enforced removal or alteration of any Improvement, resulting from the future exercise of any right existing at Date of Policy to use the surface of the Land for the extraction or development of water excepted from the description of the Land or excepted in Schedule B.
4. This endorsement does not insure against loss or damage (and the Company will not pay costs, attorneys' fees, or expenses) resulting from:
   a. contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence; [or]
   b. negligence by a person or an Entity exercising a right to extract or develop water[; or
   c. the exercise of the rights described in (   )]. *

      * Instructional note: identify the interest excepted from the description of the Land in Schedule A or excepted in Schedule B that you intend to exclude from this coverage.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

By: ______________________________________

Authorized Signatory

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ENDORSEMENT

Attached to Policy No. __________

Issued by

BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the exclusion in Section 4 of this endorsement; and the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.
2. For purposes of this endorsement only, "Improvement" means each improvement on the Land at Date of Policy itemized [on the exhibit attached to this endorsement.] [below:]
3. The Company insures against loss or damage sustained by the Insured by reason of the enforced removal or alteration of any Improvement resulting from the future exercise of any right existing at Date of Policy to use the surface of the Land for the extraction or development of water excepted from the description of the Land or excepted in Schedule B.
4. This endorsement does not insure against loss or damage (and the Company will not pay costs, attorneys' fees, or expenses) resulting from:
   a. contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence; [or]
   b. negligence by a person or an Entity exercising a right to extract or develop water[; or
   c. the exercise of the rights described in (   )]. *

   * Instructional note: identify the interest excepted from the description of the Land in Schedule A or excepted in Schedule B that you intend to exclude from this coverage.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

By: ______________________________________
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ENDORSEMENT

Attached to Policy No. __________

Issued by

BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the exclusion in Section 4 of this endorsement; and the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.
2. For purposes of this endorsement only:
   a. "Improvement" means a building, structure located on the surface of the Land, and any paved road, walkway, parking area, driveway, or curb, affixed to the Land at Date of Policy and that by law constitutes real property, but excluding any crops, landscaping, lawn, shrubbery, or trees.
   b. "Future Improvement" means a building, structure, and any paved road, walkway, parking area, driveway, or curb to be constructed on or affixed to the Land in the locations according to the Plans and that by law will constitute real property, but excluding any crops, landscaping, lawn, shrubbery, or trees.
   c. "Plans" means the survey, site and elevation plans or other depictions or drawings prepared by (*insert name of architect or engineer*) dated ________, last revised ________, designated as (*insert name of project or project number*) consisting of ________ sheets.
3. The Company insures against loss or damage sustained by the Insured by reason of the enforced removal or alteration of an Improvement or a Future Improvement, resulting from the future exercise of any right existing at Date of Policy to use the surface of the Land for the extraction or development of water excepted from the description of the Land or excepted in Schedule B.
4. This endorsement does not insure against loss or damage (and the Company will not pay costs, attorneys' fees, or expenses) resulting from:
   a. contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence; [or]
   b. negligence by a person or an Entity exercising a right to extract or develop water[; or
   c. the exercise of the rights described in (   )]. *

   * Instructional note: identify the interest excepted from the description of the Land in Schedule A or excepted in Schedule B that you intend to exclude from this coverage.

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This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

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ENDORSEMENT
Attached to Policy No. __________
Issued by
BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is
   a. subject to the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy, and
   b. only effective if the Land is not improved with a one-to-four family residential dwelling.

2. For the purposes of this endorsement only:
   a. “Lender Group” means a group of lenders owning portions of the Indebtedness. The composition of the Lender Group may change by the addition or withdrawal of Participants during the term of the Insured Mortgage.
   b. “Participant” means a member of the Lender Group, but does not include a non-insured obligor as described in Section 12(c) of the Conditions. A Participant is an Insured under the policy to the extent of its ownership of a portion of the Indebtedness, whether it acquires its portion of the Indebtedness on or after Date of Policy.

3. The Company insures against loss or damage sustained by the Insured by reason of:
   a. The invalidity or unenforceability of the lien of the Insured Mortgage caused by transfers after the Date of Policy of portions of the Indebtedness by the Participants.
   b. Loss of priority of the lien of the Insured Mortgage, which loss of priority is caused by transfers after the Date of Policy of portions of the Indebtedness by the Participants.

4. The Company reserves all rights and defenses as to any Participant that the Company would have had against any other Insured under the policy, unless the Participant acquired its portion of the Indebtedness as a purchaser for value without Knowledge of the asserted defect, lien, encumbrance, or other matter insured against by this policy.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

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ENDORSEMENT
Attached to Policy No. __________
Issued by
BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.

2. For the purposes of this endorsement only:

   a. "Loan Agreement" means [a document governing the terms of the loan or loans secured by the Insured Mortgage at Date of Policy] [the __________ Agreement dated ____________, by and between the Insured and _________________________].

   b. "Revolving Credit Loan" means the portion of the Indebtedness that is a revolving credit facility as more particularly defined in the Loan Agreement.

   c. "Term Loan" means the portion of the Indebtedness that is a term loan facility as more particularly defined in the Loan Agreement.

3. The Company insures against loss or damage sustained by the Insured by reason of the loss of priority of the lien of the Insured Mortgage, as security for the amount of the Indebtedness advanced as the Term Loan, resulting from reductions and subsequent increases of the outstanding principal amount of the Indebtedness payable as the Revolving Credit Loan.

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

By: ____
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AMERICAN LAND TITLE ASSOCIATION

ENDORSEMENT
Attached to Policy No. __________
As Issued by
BLANK TITLE INSURANCE COMPANY

1. The insurance provided by this endorsement is subject to the Exclusions from Coverage, the Exceptions from Coverage contained in Schedule B, and the Conditions in the policy.

2. The Company insures against loss or damage sustained by the Insured by reason of the failure of the Insured Mortgage to have been recorded in the Public Records as set forth in Section 3 below.

3. Paragraph 4 of Schedule A is amended to read as follows:

4. The Insured Mortgage and its assignments, if any, are described as follows:

   Mortgage [Deed of Trust][Deed to Secure Debt]:
   Mortgagor:
   Mortgagee:
   Dated:
   Recorded:
   Recording/Instrument Number:

This endorsement is issued as part of the policy. Except as it expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsements, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance. To the extent a provision of the policy or a previous endorsement is inconsistent with an express provision of this endorsement, this endorsement controls. Otherwise, this endorsement is subject to all of the terms and provisions of the policy and of any prior endorsements.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

By: ____
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EXPANDED COVERAGE RESIDENTIAL LOAN POLICY

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

Any notice of claim and any other notice or statement in writing required to be given to the Company under this Policy must be given to the Company at the address shown in Section 17 of the Conditions.

SUBJECT TO THE EXCLUSIONS FROM COVERAGE, THE EXCEPTIONS FROM COVERAGE CONTAINED IN SCHEDULE B, AND THE CONDITIONS, BLANK TITLE INSURANCE COMPANY, a Blank corporation (the "Company") insures as of Date of Policy and, to the extent stated in Covered Risks 11, 16, 17, 18, 19, 20, 21, 22, 23, 24, 27 and 28, after Date of Policy, against loss or damage, not exceeding the Amount of Insurance, sustained or incurred by the Insured by reason of:

COVERED RISKS

1. Title being vested other than as stated in Schedule A.

2. Any defect in or lien or encumbrance on the Title. This Covered Risk includes but is not limited to insurance against loss from

(a) A defect in the Title caused by

(i) forgery, fraud, undue influence, duress, incompetency, incapacity, or impersonation;

(ii) failure of any person or Entity to have authorized a transfer or conveyance;

(iii) a document affecting Title not properly created, executed, witnessed, sealed, acknowledged, notarized, or delivered;

(iv) failure to perform those acts necessary to create a document by electronic means authorized by law;

(v) a document executed under a falsified, expired, or otherwise invalid power of attorney;

(vi) a document not properly filed, recorded, or indexed in the Public Records including failure to perform those acts by electronic means authorized by law; or

(vii) a defective judicial or administrative proceeding.

(b) The lien of real estate taxes or assessments imposed on the Title by a governmental authority due or payable, but unpaid.

(c) Any encroachment, encumbrance, violation, variation, or adverse circumstance affecting the Title that would be disclosed by an accurate and complete land survey of the Land. The term "encroachment" includes encroachments of existing improvements located on the Land onto adjoining land, and encroachments onto the Land of existing improvements located on adjoining land.

3. Unmarketable Title.

4. No right of access to and from the Land.

5. The violation or enforcement of any law, ordinance, permit, or governmental regulation (including those relating to building and zoning) restricting, regulating, prohibiting, or relating to

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(a) the occupancy, use, or enjoyment of the Land;
(b) the character, dimensions, or location of any improvement erected on the Land;
(c) the subdivision of land; or
(d) environmental protection

if a notice, describing any part of the Land, is recorded in the Public Records setting forth the violation or intention to enforce, but only to the extent of the violation or enforcement referred to in that notice.

6. An enforcement action based on the exercise of a governmental police power not covered by Covered Risk 5 if a notice of the enforcement action, describing any part of the Land, is recorded in the Public Records, but only to the extent of the enforcement referred to in that notice.

7. The exercise of the rights of eminent domain if a notice of the exercise, describing any part of the Land, is recorded in the Public Records.

8. Any taking by a governmental body that has occurred and is binding on the rights of a purchaser for value without Knowledge.

9. The invalidity or unenforceability of the lien of the Insured Mortgage upon the Title. This Covered Risk includes but is not limited to insurance against loss from any of the following impairing the lien of the Insured Mortgage
(a) forgery, fraud, undue influence, duress, incompetency, incapacity, or impersonation;
(b) failure of any person or Entity to have authorized a transfer or conveyance;
(c) the Insured Mortgage not being properly created, executed, witnessed, sealed, acknowledged, notarized, or delivered;
(d) failure to perform those acts necessary to create a document by electronic means authorized by law;
(e) a document executed under a falsified, expired, or otherwise invalid power of attorney;
(f) a document not properly filed, recorded, or indexed in the Public Records including failure to perform those acts by electronic means authorized by law; or
(g) a defective judicial or administrative proceeding.

10. The lack of priority of the lien of the Insured Mortgage upon the Title over any other lien or encumbrance.

11. The lack of priority of the lien of the Insured Mortgage upon the Title
(a) as security for each and every advance of proceeds of the loan secured by the Insured Mortgage over any statutory lien for services, labor, or material arising from construction of an improvement or work related to the Land when the improvement or work is either
  (i) contracted for or commenced on or before Date of Policy; or
  (ii) contracted for, commenced, or continued after Date of Policy if the construction is financed, in whole or in part, by proceeds of the loan secured by the Insured Mortgage that the Insured has advanced or is obligated on Date of Policy to advance;
(b) over the lien of any assessments for street improvements under construction or completed at Date of Policy;
(c) over any defect in or lien or encumbrance on the Title attaching or created before, on or after

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Date of Policy; as to each and every advance of proceeds of the loan secured by the Insured Mortgage, which at Date of Policy the Insured has made or is legally obligated to make; and

(d) over any environmental protection lien that comes into existence before, on or after Date of Policy pursuant to any federal statute in effect at Date of Policy as to each and every advance of proceeds of the loan secured by the Insured Mortgage, which at Date of Policy the Insured has made or is legally obligated to make.

12. The invalidity or unenforceability of any assignment of the Insured Mortgage, provided the assignment is shown in Schedule A, or the failure of the assignment shown in Schedule A to vest title to the Insured Mortgage in the named Insured assignee free and clear of all liens.

13. The failure of the Land

(a) to have the street address shown in Schedule A, and the failure of the map, if any, attached to this policy to show the correct location and dimensions of the Land according to the Public Record.

(b) to be improved with a one-to-four family residential structure or, if stated in the description of the Land, a residential condominium unit.

(c) to be zoned to permit a one-to-four family residential structure or, if stated in the description of the Land, a residential condominium unit.

(d) to be a lawfully created one-to-four family residential parcel according to state statutes and local ordinances governing subdivision of land.

14. The forced removal, modification or replacement of any existing one-to-four family residential structure or residential condominium unit located on the Land resulting from the violation of any of the following requirements of any applicable zoning ordinance: Area or dimensions of the Land as a building site; floor space area of the structure; height of the structure; or distance of the structure from the boundary lines of the Land.

15. The assessment or taxation of the Land by governmental authority as part of a larger parcel.

16. The failure of the existing one-to-four family residential structure or residential condominium unit or a portion or a future modification or replacement to have been constructed with a valid building permit from the appropriate local government issuing office or agency.

17. The inability to use the existing one-to-four family residential structure or residential condominium unit or a portion of it or a future modification or replacement to it for one-to-four family residential purposes because that use violates a restriction shown in Schedule B.

18. Damage to improvements, lawns, shrubbery or trees constructed or planted on the Land before, on or after Date of Policy resulting from the future exercise of any right to use the surface of the Land for the extraction or development of minerals, water or any other substance.

19. The encroachment onto the Land of an improvement constructed after Date of Policy.

20. Encroachment of improvements constructed on the Land after Date of Policy onto adjoining property or over any easement or building setback line on the Land.

21. Forgery after Date of Policy of

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AMERICAN LAND TITLE ASSOCIATION

(a) any instrument purporting to subordinate, assign, release or reconvey the Insured Mortgage; and

(b) any instrument purporting to convey or encumber the Title.

22. The invalidity, unenforceability or lack of priority of the lien of the Insured Mortgage as to Advances made or changes in the rate of interest charged subsequent to any modification of the terms of the Insured Mortgage made after Date of Policy which are secured by the terms of the Insured Mortgage as modified.

23. Damage to improvements, lawns, shrubbery or trees constructed or planted on the Land before, on or after Date of Policy occasioned by the exercise of the right to use or maintain any easement referred to in Schedule B.

24. Interference with the use for one-to-four family residential purposes of the improvements constructed on the Land before, on or after Date of Policy occasioned by the exercise of the right to use or maintain any easement referred to in Schedule B.

25. Supplemental real estate taxes, including those caused by construction or a change of ownership or use, that occurred before Date of Policy, not previously assessed against the Land for any period before Date of Policy.

26. The invalidity or unenforceability of the lien of the Insured Mortgage upon the Title based upon a violation of the usury laws of the state where the Land is located if no other Mortgage is shown as an exception in Schedule B.

27. The invalidity, unenforceability, lack of priority, or avoidance of the lien of the Insured Mortgage upon the Title

(a) resulting from the avoidance in whole or in part, or from a court order providing an alternative remedy, of any transfer of all or any part of the title to or any interest in the Land occurring prior to the transaction creating the lien of the Insured Mortgage because that prior transfer constituted a fraudulent or preferential transfer under federal bankruptcy, state insolvency, or similar creditors' rights laws; or

(b) because the Insured Mortgage constitutes a preferential transfer under federal bankruptcy, state insolvency, or similar creditors' rights laws by reason of the failure of its recording in the Public Records

(i) to be timely, or

(ii) to impart notice of its existence to a purchaser for value or to a judgment or lien creditor.

28. Any defect in or lien or encumbrance on the Title or other matter insured against by this Policy that has been created or attached or has been filed or recorded in the Public Records subsequent to Date of Policy and prior to the recording of the Insured Mortgage in the Public Records.

Unless stated to the contrary in Schedule B, the Company incorporates the following American Land Title Association endorsements into this policy by this reference as if these endorsements had been attached to this policy

(a) ALTA Form [4-06] [4.1-06] (Condominium), if a condominium unit is referred to in the description of the Land;

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(b) ALTA Form [5-06] [5.1-06] (Planned Unit Development);
(c) ALTA Form 6-06 (Variable Rate Mortgage);
(d) ALTA Form 6.2-06 (Variable Rate Mortgage - Negative Amortization); and
(e) ALTA Form 8.1-06 (Environmental Protection Lien) subject to the statutes, if any, shown in Schedule B specifically for this endorsement.
(f) ALTA Form 9.3-06 (Restrictions, Encroachments, Minerals).

The Company will also pay the costs, attorneys' fees, and expenses incurred in defense of any matter insured against by this policy, but only to the extent provided in the Conditions.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

BY:___________________________________
PRESIDENT

BY:___________________________________
SECRETARY

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EXCLUSIONS FROM COVERAGE

The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorneys' fees or expenses which arise by reason of:

1. (a) Any law, ordinance, permit, or governmental regulation (including those relating to building and zoning) restricting, regulating, prohibiting, or relating to

(i) the occupancy, use, or enjoyment of the Land;

(ii) the character, dimensions, or location of any improvement erected on the Land;

(iii) the subdivision of land; or

(iv) environmental protection;

or the effect of any violation of these laws, ordinances, or governmental regulations. This Exclusion 1(a) does not modify or limit the coverage provided under Covered Risk 5, 6, 13(c), 13(d), 14 or 16.

(b) Any governmental police power. This Exclusion 1(b) does not modify or limit the coverage provided under Covered Risk 5, 6, 13(c), 13(d), 14 or 16.

2. Rights of eminent domain. This Exclusion does not modify or limit the coverage provided under Covered Risk 7 or 8.

3. Defects, liens, encumbrances, adverse claims, or other matters

(a) created, suffered, assumed, or agreed to by the Insured Claimant;

(b) not Known to the Company, not recorded in the Public Records at Date of Policy, but Known to the Insured Claimant and not disclosed in writing to the Company by the Insured Claimant prior to the date the Insured Claimant became an Insured under this policy;

(c) resulting in no loss or damage to the Insured Claimant;

(d) attaching or created subsequent to Date of Policy (however, this does not modify or limit the coverage provided under Covered Risk 11, 16, 17, 18, 19, 20, 21, 22, 23, 24, 27 or 28); or

(e) resulting in loss or damage that would not have been sustained if the Insured Claimant had paid value for the Insured Mortgage.

4. Unenforceability of the lien of the Insured Mortgage because of the inability or failure of an Insured to comply with applicable doing-business laws of the state where the Land is situated.

5. Invalidity or unenforceability in whole or in part of the lien of the Insured Mortgage that arises out of the transaction evidenced by the Insured Mortgage and is based upon usury, or any consumer credit protection or truth-in-lending law. This Exclusion does not modify or limit the coverage provided in Covered Risk 26.

6. Any claim of invalidity, unenforceability or lack of priority of the lien of the Insured Mortgage as to Advances or modifications made after the Insured has Knowledge that the vestee shown in Schedule A is no longer the owner of the estate or interest covered by this policy. This Exclusion does not modify or limit the coverage provided in Covered Risk 11.

7. Any lien on the Title for real estate taxes or assessments imposed by governmental authority and created or attaching subsequent to Date of Policy. This Exclusion does not modify or limit the

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coverage provided in Covered Risk 11(b) or 25.

8. The failure of the residential structure, or any portion of it, to have been constructed before, on or after Date of Policy in accordance with applicable building codes. This Exclusion does not modify or limit the coverage provided in Covered Risk 5 or 6.

9. Any claim, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that the transaction creating the lien of the Insured Mortgage, is

(a) a fraudulent conveyance or fraudulent transfer, or

(b) a preferential transfer for any reason not stated in Covered Risk 27(b) of this policy.

10. Contamination, explosion, fire, flooding, vibration, fracturing, earthquake, or subsidence.

11. Negligence by a person or an Entity exercising a right to extract or develop minerals, water, or any other substances.

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AMERICAN LAND TITLE ASSOCIATION

EXPANDED COVERAGE RESIDENTIAL LOAN POLICY
For a one-to-four family residence
Issued By
BLANK TITLE INSURANCE COMPANY

SCHEDULE A

Name and Address of Title Insurance Company:

[File No.:] Policy No.:
Loan No.:
Street Address of the Land:
Policy Amount: $ [Premium: $]
Date of Policy: [at a.m./p.m.]

1. Name of Insured:

2. The estate or interest in the Land that is encumbered by the Insured Mortgage is:

3. Title is vested in:

4. The Insured Mortgage and its assignments, if any, are described as follows:

5. The Land referred to in this policy is described as follows:

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EXPANDED COVERAGE RESIDENTIAL LOAN POLICY
For a one-to-four family residence
Issued By
BLANK TITLE INSURANCE COMPANY

SCHEDULE B - PART I

File No. Policy No.

EXCEPTIONS FROM COVERAGE

This policy does not insure against loss or damage (and the Company will not pay costs, attorneys' fees or expenses) that arise by reason of:

[**1.** The following state statutes, reference to which are made part of the ALTA 8.1-06 Environmental Protection Lien Endorsement incorporated into this Policy:]

SCHEDULE B - PART II

In addition to the matters set forth in Part I of this Schedule, the Title is subject to the following matters, and the Company insures against loss or damage sustained in the event that they are not subordinate to the lien of the Insured Mortgage:

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CONDITIONS

1. DEFINITION OF TERMS

The following terms when used in this policy mean:

(a) "Advances": Disbursements of Indebtedness made after the Date of Policy as provided by the Insured Mortgage.

(b) "Amount of Insurance": One hundred twenty-five percent (125%) of the Policy Amount stated in Schedule A, as may be increased or decreased by endorsement to this policy, increased by Section 8(b) or decreased by Section 10 of these Conditions.

(c) "Date of Policy": The date designated as "Date of Policy" in Schedule A.

(d) "Entity": A corporation, partnership, trust, limited liability company, or other similar legal entity.

(e) "Indebtedness": The obligation secured by the Insured Mortgage including one evidenced by electronic means authorized by law, and if that obligation is the payment of a debt, the Indebtedness is the sum of

(i) the amount of the principal disbursed as of Date of Policy;

(ii) the amount of the principal disbursed subsequent to Date of Policy;

(iii) the construction loan advances made subsequent to Date of Policy for the purpose of financing in whole or in part the construction of an improvement to the Land or related to the Land that the Insured was and continued to be obligated to advance at Date of Policy and at the date of the Advance;

(iv) interest on the loan;

(v) the prepayment premiums, exit fees, and other similar fees or penalties allowed by law;

(vi) the expenses of foreclosure and any other costs of enforcement;

(vii) the amounts advanced to assure compliance with laws or to protect the lien or the priority of the lien of the Insured Mortgage before the acquisition of the estate or interest in the Title;

(viii) the amounts to pay taxes and insurance; and

(ix) the reasonable amounts expended to prevent deterioration of improvements;

but the Indebtedness is reduced by the total of all payments and by any amount forgiven by an Insured.

(f) "Insured": The Insured named in Schedule A.

(i) The term "Insured" also includes

(A) the owner of the Indebtedness and each successor in ownership of the Indebtedness, whether the owner or successor owns the Indebtedness for its own account or as a trustee or other fiduciary, except a successor who is an obligor under the provisions of Section 12(c) of these Conditions;

(B) the person or Entity who has "control" of the "transferable record," if the Indebtedness is evidenced by a "transferable record," as these terms are defined by applicable electronic transactions law;

(C) successors to an Insured by dissolution, merger, consolidation, distribution, or reorganization;

(D) successors to an Insured by its conversion to another kind of Entity;

(E) a grantee of an Insured under a deed delivered without payment of actual valuable consideration conveying the Title

(1) if the stock, shares, memberships, or other equity interests of the grantee are wholly-owned by the named Insured,

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(2) if the grantee wholly owns the named Insured, or

(3) if the grantee is wholly-owned by an affiliated Entity of the named Insured, provided the affiliated Entity and the named Insured are both wholly-owned by the same person or Entity;

(F) any government agency or instrumentality that is an insurer or guarantor under an insurance contract or guaranty insuring or guaranteeing the Indebtedness secured by the Insured Mortgage, or any part of it, whether named as an Insured or not;

(ii) With regard to (A), (B), (C), (D), and (E) reserving, however, all rights and defenses as to any successor that the Company would have had against any predecessor Insured, unless the successor acquired the Indebtedness as a purchaser for value without Knowledge of the asserted defect, lien, encumbrance, or other matter insured against by this policy.

(g) "Insured Claimant": An Insured claiming loss or damage.

(h) "Insured Mortgage": The Mortgage described in paragraph 4 of Schedule A.

(i) "Knowledge" or "Known": Actual knowledge, not constructive knowledge or notice that may be imputed to an Insured by reason of the Public Records or any other records that impart constructive notice of matters affecting the Title.

(j) "Land": The land described in Schedule A, and affixed improvements that by law constitute real property. The term "Land" does not include any property beyond the lines of the area described in Schedule A, nor any right, title, interest, estate, or easement in abutting streets, roads, avenues, alleys, lanes, ways, or waterways, but this does not modify or limit the extent that a right of access to and from the Land is insured by this policy.

(k) "Mortgage": Mortgage, deed of trust, trust deed, or other security instrument, including one evidenced by electronic means authorized by law.

(l) "Public Records": Records established under state statutes at Date of Policy for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without Knowledge. With respect to Covered Risk 5(d), "Public Records" shall also include environmental protection liens filed in the records of the clerk of the United States District Court for the district where the Land is located.

(m) "Title": The estate or interest described in Schedule A.

(n) "Unmarketable Title": Title affected by an alleged or apparent matter that would permit a prospective purchaser or lessee of the Title or lender on the Title or a prospective purchaser of the Insured Mortgage to be released from the obligation to purchase, lease, or lend if there is a contractual condition requiring the delivery of marketable title.

2. CONTINUATION OF INSURANCE

The coverage of this policy shall continue in force as of Date of Policy in favor of an Insured after acquisition of the Title by an Insured or after conveyance by an Insured, but only so long as the Insured retains an estate or interest in the Land, or holds an obligation secured by a purchase money Mortgage given by a purchaser from the Insured, or only so long as the Insured shall have liability by reason of warranties in any transfer or conveyance of the Title. This policy shall not continue in force in favor of any purchaser from the Insured of either (i) an estate or interest in the Land, or (ii) an obligation secured by a purchase money Mortgage given to the Insured.

3. NOTICE OF CLAIM TO BE GIVEN BY INSURED CLAIMANT

The Insured shall notify the Company promptly in writing (i) in case of any litigation as set forth in Section 5(a) of these Conditions, (ii) in case Knowledge shall come to an Insured of any claim of title or interest that is adverse to the Title or the lien of the Insured Mortgage, as insured, and that

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might cause loss or damage for which the Company may be liable by virtue of this policy, or (iii) if the Title or the lien of the Insured Mortgage, as insured, is rejected as Unmarketable Title. If the Company is prejudiced by the failure of the Insured Claimant to provide prompt notice, the Company's liability to the Insured Claimant under the policy shall be reduced to the extent of the prejudice.

4. PROOF OF LOSS

In the event the Company is unable to determine the amount of loss or damage, the Company may, at its option, require as a condition of payment that the Insured Claimant furnish a signed proof of loss. The proof of loss must describe the defect, lien, encumbrance, or other matter insured against by this policy that constitutes the basis of loss or damage and shall state, to the extent possible, the basis of calculating the amount of the loss or damage.

5. DEFENSE AND PROSECUTION OF ACTIONS

(a) Upon written request by the Insured, and subject to the options contained in Section 7 of these Conditions, the Company, at its own cost and without unreasonable delay, shall provide for the defense of an Insured in litigation in which any third party asserts a claim covered by this policy adverse to the Insured. This obligation is limited to only those stated causes of action alleging matters insured against by this policy. The Company shall have the right to select counsel of its choice (subject to the right of the Insured to object for reasonable cause) to represent the Insured as to those stated causes of action. It shall not be liable for and will not pay the fees of any other counsel. The Company will not pay any fees, costs, or expenses incurred by the Insured in the defense of those causes of action that allege matters not insured against by this policy.

(b) The Company shall have the right, in addition to the options contained in Section 7 of these Conditions, at its own cost, to institute and prosecute any action or proceeding or to do any other act that in its opinion may be necessary or desirable to establish the Title or the lien of the Insured Mortgage, as insured, or to prevent or reduce loss or damage to the Insured. The Company may take any appropriate action under the terms of this policy, whether or not it shall be liable to the Insured. The exercise of these rights shall not be an admission of liability or waiver of any provision of this policy. If the Company exercises its rights under this subsection, it must do so diligently.

(c) Whenever the Company brings an action or asserts a defense as required or permitted by this policy, the Company may pursue the litigation to a final determination by a court of competent jurisdiction, and it expressly reserves the right, in its sole discretion, to appeal any adverse judgment or order.

6. DUTY OF INSURED CLAIMANT TO COOPERATE

(a) In all cases where this policy permits or requires the Company to prosecute or provide for the defense of any action or proceeding and any appeals, the Insured shall secure to the Company the right to so prosecute or provide defense in the action or proceeding, including the right to use, at its option, the name of the Insured for this purpose. Whenever requested by the Company, the Insured, at the Company's expense, shall give the Company all reasonable aid (i) in securing evidence, obtaining witnesses, prosecuting or defending the action or proceeding, or effecting settlement, and (ii) in any other lawful act that in the opinion of the Company may be necessary or desirable to establish the Title, the lien of the Insured Mortgage, or any other matter as insured. If the Company is prejudiced by the failure of the Insured to furnish the required cooperation, the Company's obligations to the Insured under the policy shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation, with regard to the matter or matters requiring such cooperation.

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(b) The Company may reasonably require the Insured Claimant to submit to examination under oath by any authorized representative of the Company and to produce for examination, inspection, and copying, at such reasonable times and places as may be designated by the authorized representative of the Company, all records, in whatever medium maintained, including books, ledgers, checks, memoranda, correspondence, reports, e-mails, disks, tapes, and videos whether bearing a date before or after Date of Policy, that reasonably pertain to the loss or damage. Further, if requested by any authorized representative of the Company, the Insured Claimant shall grant its permission, in writing, for any authorized representative of the Company to examine, inspect, and copy all of these records in the custody or control of a third party that reasonably pertain to the loss or damage. All information designated as confidential by the Insured Claimant provided to the Company pursuant to this Section shall not be disclosed to others unless, in the reasonable judgment of the Company, it is necessary in the administration of the claim. Failure of the Insured Claimant to submit for examination under oath, produce any reasonably requested information, or grant permission to secure reasonably necessary information from third parties as required in this subsection, unless prohibited by law or governmental regulation, shall terminate any liability of the Company under this policy as to that claim.

7. OPTIONS TO PAY OR OTHERWISE SETTLE CLAIMS; TERMINATION OF LIABILITY

In case of a claim under this policy, the Company shall have the following additional options:

(a) To Pay or Tender Payment of the Amount of Insurance or to Purchase the Indebtedness.

(i) To pay or tender payment of the Amount of Insurance under this policy together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment or tender of payment and that the Company is obligated to pay; or

(ii) To purchase the Indebtedness for the amount of the Indebtedness on the date of purchase, together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of purchase and that the Company is obligated to pay.

When the Company purchases the Indebtedness, the Insured shall transfer, assign, and convey to the Company the Indebtedness and the Insured Mortgage, together with any collateral security.

Upon the exercise by the Company of either of the options provided for in subsections (a)(i) or (ii), all liability and obligations of the Company to the Insured under this policy, other than to make the payment required in those subsections, shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation.

(b) To Pay or Otherwise Settle With Parties Other Than the Insured or With the Insured Claimant.

(i) to pay or otherwise settle with other parties for or in the name of an Insured Claimant any claim insured against under this policy. In addition, the Company will pay any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment and that the Company is obligated to pay; or

(ii) to pay or otherwise settle with the Insured Claimant the loss or damage provided for under this policy, together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment and that the Company is obligated to pay.

Upon the exercise by the Company of either of the options provided for in subsections (b)(i) or (ii), the Company's obligations to the Insured under this policy for the claimed loss or damage, other than the payments required to be made, shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation.

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8. DETERMINATION AND EXTENT OF LIABILITY

This policy is a contract of indemnity against actual monetary loss or damage sustained or incurred by the Insured Claimant who has suffered loss or damage by reason of matters insured against by this policy.

(a) The extent of liability of the Company for loss or damage under this policy shall not exceed the least of

(i) the Amount of Insurance,

(ii) the Indebtedness,

(iii) the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy, or

(iv) if a government agency or instrumentality is the Insured Claimant, the amount it paid in the acquisition of the Title or the Insured Mortgage in satisfaction of its insurance contract or guaranty.

(b) If the Company pursues its rights under Section 5 of these Conditions and is unsuccessful in establishing the Title or the lien of the Insured Mortgage, as insured,

(i) the Amount of Insurance shall be increased by 10%, and

(ii) the Insured Claimant shall have the right to have the loss or damage determined either as of the date the claim was made by the Insured Claimant or as of the date it is settled and paid.

(c) In the event the Insured has acquired the Title in the manner described in Section 2 of these Conditions or has conveyed the Title, then the extent of liability of the Company shall continue as set forth in Section 8(a) of these Conditions.

(d) In addition to the extent of liability under (a), (b), and (c), the Company will also pay those costs, attorneys' fees, and expenses incurred in accordance with Sections 5 and 7 of these Conditions.

9. LIMITATION OF LIABILITY

(a) If the Company establishes the Title, or removes the alleged defect, lien, or encumbrance, or cures the lack of a right of access to or from the Land, or cures the claim of Unmarketable Title, or establishes the lien of the Insured Mortgage, all as insured, in a reasonably diligent manner by any method, including litigation and the completion of any appeals, it shall have fully performed its obligations with respect to that matter and shall not be liable for any loss or damage caused to the Insured.

(b) In the event of any litigation, including litigation by the Company or with the Company's consent, the Company shall have no liability for loss or damage until there has been a final determination by a court of competent jurisdiction, and disposition of all appeals, adverse to the Title or to the lien of the Insured Mortgage, as insured.

(c) The Company shall not be liable for loss or damage to the Insured for liability voluntarily assumed by the Insured in settling any claim or suit without the prior written consent of the Company.

10. REDUCTION OF INSURANCE; REDUCTION OR TERMINATION OF LIABILITY

(a) All payments under this policy, except payments made for costs, attorneys’ fees, and expenses, shall reduce the Amount of Insurance by the amount of the payment. However, any payments made prior to the acquisition of Title as provided in Section 2 of these Conditions shall not reduce the Amount of Insurance afforded under this policy except to the extent that the payments reduce the Indebtedness.

(b) The voluntary satisfaction or release of the Insured Mortgage shall terminate all liability of the

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Company except as provided in Section 2 of these Conditions.

11. PAYMENT OF LOSS

When liability and the extent of loss or damage have been definitely fixed in accordance with these Conditions, the payment shall be made within 30 days.

12. RIGHTS OF RECOVERY UPON PAYMENT OR SETTLEMENT

(a) The Company's Right to Recover

Whenever the Company shall have settled and paid a claim under this policy, it shall be subrogated and entitled to the rights of the Insured Claimant in the Title or Insured Mortgage and all other rights and remedies in respect to the claim that the Insured Claimant has against any person or property, to the extent of the amount of any loss, costs, attorneys' fees, and expenses paid by the Company. If requested by the Company, the Insured Claimant shall execute documents to evidence the transfer to the Company of these rights and remedies. The Insured Claimant shall permit the Company to sue, compromise, or settle in the name of the Insured Claimant and to use the name of the Insured Claimant in any transaction or litigation involving these rights and remedies.

If a payment on account of a claim does not fully cover the loss of the Insured Claimant, the Company shall defer the exercise of its right to recover until after the Insured Claimant shall have recovered its loss.

(b) The Insured's Rights and Limitations

(i) The owner of the Indebtedness may release or substitute the personal liability of any debtor or guarantor, extend or otherwise modify the terms of payment, release a portion of the Title from the lien of the Insured Mortgage, or release any collateral security for the Indebtedness, if it does not affect the enforceability or priority of the lien of the Insured Mortgage.

(ii) If the Insured exercises a right provided in (b)(i), but has Knowledge of any claim adverse to the Title or the lien of the Insured Mortgage insured against by this policy, the Company shall be required to pay only that part of any losses insured against by this policy that shall exceed the amount, if any, lost to the Company by reason of the impairment by the Insured Claimant of the Company's right of subrogation.

(c) The Company's Rights Against Noninsured Obligors

The Company’s right of subrogation includes the Insured’s rights against non-insured obligors including the rights of the Insured to indemnities, guarantees, other policies of insurance, or bonds, notwithstanding any terms or conditions contained in those instruments that address subrogation rights.

The Company's right of subrogation shall not be avoided by acquisition of the Insured Mortgage by an obligor (except an obligor described in Section 1(f)(i)(F) of these Conditions) who acquires the Insured Mortgage as a result of an indemnity, guarantee, other policy of insurance, or bond, and the obligor will not be an Insured under this policy.

13. ARBITRATION

Either the Company or the Insured may demand that the claim or controversy shall be submitted to arbitration pursuant to the Title Insurance Arbitration Rules of the American Land Title Association (“Rules”). Except as provided in the Rules, there shall be no joinder or consolidation with claims or controversies of other persons. Arbitrable matters may include, but are not limited to, any controversy or claim between the Company and the Insured arising out of or relating to this policy, any service in connection with its issuance or the breach of a policy provision, or to any other controversy or claim arising out of the transaction giving rise to this policy. All arbitrable matters

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when the Amount of Insurance is $2,000,000 or less shall be arbitrated at the option of either the Company or the Insured. All arbitrable matters when the Amount of Insurance is in excess of $2,000,000 shall be arbitrated only when agreed to by both the Company and the Insured. Arbitration pursuant to this policy and under the Rules shall be binding upon the parties. Judgment upon the award rendered by the Arbitrator(s) may be entered in any court of competent jurisdiction.

14. LIABILITY LIMITED TO THIS POLICY; POLICY ENTIRE CONTRACT

(a) This policy together with all endorsements, if any, attached to it by the Company is the entire policy and contract between the Insured and the Company. In interpreting any provision of this policy, this policy shall be construed as a whole.

(b) Any claim of loss or damage that arises out of the status of the Title or lien of the Insured Mortgage or by any action asserting such claim shall be restricted to this policy.

(c) Any amendment of or endorsement to this policy must be in writing and authenticated by an authorized person, or expressly incorporated by Schedule A of this policy.

(d) Each endorsement to this policy issued at any time is made a part of this policy and is subject to all of its terms and provisions. Except as the endorsement expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsement, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance.

15. SEVERABILITY

In the event any provision of this policy, in whole or in part, is held invalid or unenforceable under applicable law, the policy shall be deemed not to include that provision or such part held to be invalid, but all other provisions shall remain in full force and effect.

16. CHOICE OF LAW; FORUM

(a) Choice of Law: The Insured acknowledges the Company has underwritten the risks covered by this policy and determined the premium charged therefor in reliance upon the law affecting interests in real property and applicable to the interpretation, rights, remedies, or enforcement of policies of title insurance of the jurisdiction where the Land is located.

Therefore, the court or an arbitrator shall apply the law of the jurisdiction where the Land is located to determine the validity of claims against the Title or the lien of the Insured Mortgage that are adverse to the Insured and to interpret and enforce the terms of this policy. In neither case shall the court or arbitrator apply its conflicts of law principles to determine the applicable law.

(b) Choice of Forum: Any litigation or other proceeding brought by the Insured against the Company must be filed only in a state or federal court within the United States of America or its territories having appropriate jurisdiction.

17. NOTICES, WHERE SENT

Any notice of claim and any other notice or statement in writing required to be given to the Company under this policy must be given to the Company at [fill in].

NOTE: Bracketed [ ] material optional

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EXPANDED COVERAGE RESIDENTIAL LOAN POLICY
For a one-to-four family residence
Issued By
BLANK TITLE INSURANCE COMPANY

Any notice of claim and any other notice or statement in writing required to be given to the Company under this Policy must be given to the Company at the address shown in Section 17 of the Conditions.

SUBJECT TO THE EXCLUSIONS FROM COVERAGE, THE EXCEPTIONS FROM COVERAGE CONTAINED IN SCHEDULE B, AND THE CONDITIONS, BLANK TITLE INSURANCE COMPANY, a Blank corporation (the “Company”) insures as of Date of Policy and, to the extent stated in Covered Risks 11, 16, 17, 18, 19, 20, 21, 22, 23, 24, 27 and 28, after Date of Policy, against loss or damage, not exceeding the Amount of Insurance, sustained or incurred by the Insured by reason of:

COVERED RISKS

1. Title being vested other than as stated in Schedule A.

2. Any defect in or lien or encumbrance on the Title. This Covered Risk includes but is not limited to insurance against loss from
- (a) A defect in the Title caused by
  - (i) forgery, fraud, undue influence, duress, incompetency, incapacity, or impersonation;
  - (ii) failure of any person or Entity to have authorized a transfer or conveyance;
  - (iii) a document affecting Title not properly created, executed, witnessed, sealed, acknowledged, notarized, or delivered;
  - (iv) failure to perform those acts necessary to create a document by electronic means authorized by law;
  - (v) a document executed under a falsified, expired, or otherwise invalid power of attorney;
  - (vi) a document not properly filed, recorded, or indexed in the Public Records including failure to perform those acts by electronic means authorized by law; or
  - (vii) a defective judicial or administrative proceeding.
- (b) The lien of real estate taxes or assessments imposed on the Title by a governmental authority due or payable, but unpaid.
- (c) Any encroachment, encumbrance, violation, variation, or adverse circumstance affecting the Title that would be disclosed by an accurate and complete land survey of the Land. The term “encroachment” includes encroachments of existing improvements located on the Land onto adjoining land, and encroachments onto the Land of existing improvements located on adjoining land.

3. Unmarketable Title.

4. No right of access to and from the Land.

5. The violation or enforcement of any law, ordinance, permit, or governmental regulation (including those relating to building and zoning) restricting, regulating, prohibiting, or relating to

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AMERICAN LAND TITLE ASSOCIATION

(a) the occupancy, use, or enjoyment of the Land;

(b) the character, dimensions, or location of any improvement erected on the Land;

(c) the subdivision of land; or

(d) environmental protection

if a notice, describing any part of the Land, is recorded in the Public Records setting forth the violation or intention to enforce, but only to the extent of the violation or enforcement referred to in that notice.

6. An enforcement action based on the exercise of a governmental police power not covered by Covered Risk 5 if a notice of the enforcement action, describing any part of the Land, is recorded in the Public Records, but only to the extent of the enforcement referred to in that notice.

7. The exercise of the rights of eminent domain if a notice of the exercise, describing any part of the Land, is recorded in the Public Records.

8. Any taking by a governmental body that has occurred and is binding on the rights of a purchaser for value without Knowledge.

9. The invalidity or unenforceability of the lien of the Insured Mortgage upon the Title. This Covered Risk includes but is not limited to insurance against loss from any of the following impairing the lien of the Insured Mortgage

(a) forgery, fraud, undue influence, duress, incompetency, incapacity, or impersonation;

(b) failure of any person or Entity to have authorized a transfer or conveyance;

(c) the Insured Mortgage not being properly created, executed, witnessed, sealed, acknowledged, notarized, or delivered;

(d) failure to perform those acts necessary to create a document by electronic means authorized by law;

(e) a document executed under a falsified, expired, or otherwise invalid power of attorney;

(f) a document not properly filed, recorded, or indexed in the Public Records including failure to perform those acts by electronic means authorized by law; or

(g) a defective judicial or administrative proceeding.

10. The lack of priority of the lien of the Insured Mortgage upon the Title over any other lien or encumbrance.

11. The lack of priority of the lien of the Insured Mortgage upon the Title

(a) as security for each and every advance of proceeds of the loan secured by the Insured Mortgage over any statutory lien for services, labor, or material arising from construction of an improvement or work related to the Land when the improvement or work is either

 (i) contracted for or commenced on or before Date of Policy; or

 (ii) contracted for, commenced, or continued after Date of Policy if the construction is financed, in whole or in part, by proceeds of the loan secured by the Insured Mortgage that the Insured has advanced or is obligated on Date of Policy to advance;

(b) over the lien of any assessments for street improvements under construction or completed at Date of Policy;

(c) over any defect in or lien or encumbrance on the Title attaching or created before, on or after

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Date of Policy; as to each and every advance of proceeds of the loan secured by the Insured Mortgage, which at Date of Policy the Insured has made or is legally obligated to make; and

(d) over any environmental protection lien that comes into existence before, on or after Date of Policy pursuant to any federal statute in effect at Date of Policy as to each and every advance of proceeds of the loan secured by the Insured Mortgage, which at Date of Policy the Insured has made or is legally obligated to make.

12. The invalidity or unenforceability of any assignment of the Insured Mortgage, provided the assignment is shown in Schedule A, or the failure of the assignment shown in Schedule A to vest title to the Insured Mortgage in the named Insured assignee free and clear of all liens.

13. The failure of the Land

(a) to have the street address shown in Schedule A, and the failure of the map, if any, attached to this policy to show the correct location and dimensions of the Land according to the Public Record.

(b) to be improved with a one-to-four family residential structure or, if stated in the description of the Land, a residential condominium unit.

(c) to be zoned to permit a one-to-four family residential structure or, if stated in the description of the Land, a residential condominium unit.

(d) to be a lawfully created one-to-four family residential parcel according to state statutes and local ordinances governing subdivision of land.

14. The forced removal, modification or replacement of any existing one-to-four family residential structure or residential condominium unit located on the Land resulting from the violation of any of the following requirements of any applicable zoning ordinance: Area or dimensions of the Land as a building site; floor space area of the structure; height of the structure; or distance of the structure from the boundary lines of the Land.

15. The assessment or taxation of the Land by governmental authority as part of a larger parcel.

16. The failure of the existing one-to-four family residential structure or residential condominium unit or a portion or a future modification or replacement to have been constructed with a valid building permit from the appropriate local government issuing office or agency.

17. The inability to use the existing one-to-four family residential structure or residential condominium unit or a portion of it or a future modification or replacement to it for one-to-four family residential purposes because that use violates a restriction shown in Schedule B.

18. Damage to improvements, lawns, shrubbery or trees constructed or planted on the Land before, on or after Date of Policy resulting from the future exercise of any right to use the surface of the Land for the extraction or development of minerals, water or any other substance.

19. The encroachment onto the Land of an improvement constructed after Date of Policy.

20. Encroachment of improvements constructed on the Land after Date of Policy onto adjoining property or over any easement or building setback line on the Land.

21. Forgery after Date of Policy of

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(a) any instrument purporting to subordinate, assign, release or reconvey the Insured Mortgage; and

(b) any instrument purporting to convey or encumber the Title.

22. The invalidity, unenforceability or lack of priority of the lien of the Insured Mortgage as to Advances made or changes in the rate of interest charged subsequent to any modification of the terms of the Insured Mortgage made after Date of Policy which are secured by the terms of the Insured Mortgage as modified.

23. Damage to improvements, lawns, shrubbery or trees constructed or planted on the Land before, on or after Date of Policy occasioned by the exercise of the right to use or maintain any easement referred to in Schedule B.

24. Interference with the use for one-to-four family residential purposes of the improvements constructed on the Land before, on or after Date of Policy occasioned by the exercise of the right to use or maintain any easement referred to in Schedule B.

25. Supplemental real estate taxes, including those caused by construction or a change of ownership or use, that occurred before Date of Policy, not previously assessed against the Land for any period before Date of Policy.

26. The invalidity or unenforceability of the lien of the Insured Mortgage upon the Title based upon a violation of the usury laws of the state where the Land is located if no other Mortgage is shown as an exception in Schedule B.

27. The invalidity, unenforceability, lack of priority, or avoidance of the lien of the Insured Mortgage upon the Title

(a) resulting from the avoidance in whole or in part, or from a court order providing an alternative remedy, of any transfer of all or any part of the title to or any interest in the Land occurring prior to the transaction creating the lien of the Insured Mortgage because that prior transfer constituted a fraudulent or preferential transfer under federal bankruptcy, state insolvency, or similar creditors' rights laws; or

(b) because the Insured Mortgage constitutes a preferential transfer under federal bankruptcy, state insolvency, or similar creditors' rights laws by reason of the failure of its recording in the Public Records

(i) to be timely, or

(ii) to impart notice of its existence to a purchaser for value or to a judgment or lien creditor.

28. Any defect in or lien or encumbrance on the Title or other matter insured against by this Policy that has been created or attached or has been filed or recorded in the Public Records subsequent to Date of Policy and prior to the recording of the Insured Mortgage in the Public Records.

Unless stated to the contrary in Schedule B, the Company incorporates the following American Land Title Association endorsements into this policy by this reference as if these endorsements had been attached to this policy

(a) ALTA Form [4-06] [4.1-06] (Condominium), if a condominium unit is referred to in the description of the Land;

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(b) ALTA Form [5-06] [5.1-06] (Planned Unit Development);

(c) ALTA Form 6-06 (Variable Rate Mortgage);

(d) ALTA Form 6.2-06 (Variable Rate Mortgage - Negative Amortization); and

(e) ALTA Form 8.1-06 (Environmental Protection Lien) subject to the statutes, if any, shown in Schedule B specifically for this endorsement.

(f) ALTA Form 9.3-06 (Restrictions, Encroachments, Minerals).

The Company will also pay the costs, attorneys' fees, and expenses incurred in defense of any matter insured against by this policy, but only to the extent provided in the Conditions.

[Witness clause optional]

BLANK TITLE INSURANCE COMPANY

BY:___________________________________
PRESIDENT

BY:___________________________________
SECRETARY

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EXCLUSIONS FROM COVERAGE

The following matters are expressly excluded from the coverage of this policy and the Company will not pay loss or damage, costs, attorneys' fees or expenses which arise by reason of:

1. (a) Any law, ordinance, permit, or governmental regulation (including those relating to building and zoning) restricting, regulating, prohibiting, or relating to
(i) the occupancy, use, or enjoyment of the Land;
(ii) the character, dimensions, or location of any improvement erected on the Land;
(iii) the subdivision of land; or
(iv) environmental protection;

or the effect of any violation of these laws, ordinances, or governmental regulations. This Exclusion 1(a) does not modify or limit the coverage provided under Covered Risk 5, 6, 13(c), 13(d), 14 or 16.

(b) Any governmental police power. This Exclusion 1(b) does not modify or limit the coverage provided under Covered Risk 5, 6, 13(c), 13(d), 14 or 16.

2. Rights of eminent domain. This Exclusion does not modify or limit the coverage provided under Covered Risk 7 or 8.

3. Defects, liens, encumbrances, adverse claims, or other matters
(a) created, suffered, assumed, or agreed to by the Insured Claimant;
(b) not Known to the Company, not recorded in the Public Records at Date of Policy, but Known to the Insured Claimant and not disclosed in writing to the Company by the Insured Claimant prior to the date the Insured Claimant became an Insured under this policy;
(c) resulting in no loss or damage to the Insured Claimant;
(d) attaching or created subsequent to Date of Policy (however, this does not modify or limit the coverage provided under Covered Risk 11, 16, 17, 18, 19, 20, 21, 22, 23, 24, 27 or 28); or
(e) resulting in loss or damage that would not have been sustained if the Insured Claimant had paid value for the Insured Mortgage.

4. Unenforceability of the lien of the Insured Mortgage because of the inability or failure of an Insured to comply with applicable doing-business laws of the state where the Land is situated.

5. Invalidity or unenforceability in whole or in part of the lien of the Insured Mortgage that arises out of the transaction evidenced by the Insured Mortgage and is based upon usury, or any consumer credit protection or truth-in-lending law. This Exclusion does not modify or limit the coverage provided in Covered Risk 26.

6. Any claim of invalidity, unenforceability or lack of priority of the lien of the Insured Mortgage as to Advances or modifications made after the Insured has Knowledge that the vestee shown in Schedule A is no longer the owner of the estate or interest covered by this policy. This Exclusion does not modify or limit the coverage provided in Covered Risk 11.

7. Any lien on the Title for real estate taxes or assessments imposed by governmental authority and created or attaching subsequent to Date of Policy. This Exclusion does not modify or limit the

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coverage provided in Covered Risk 11(b) or 25.

8. The failure of the residential structure, or any portion of it, to have been constructed before, on or after Date of Policy in accordance with applicable building codes. This Exclusion does not modify or limit the coverage provided in Covered Risk 5 or 6.

9. Any claim, by reason of the operation of federal bankruptcy, state insolvency, or similar creditors' rights laws, that the transaction creating the lien of the Insured Mortgage, is

(a) a fraudulent conveyance or fraudulent transfer, or

(b) a preferential transfer for any reason not stated in Covered Risk 27(b) of this policy.

10. Contamination, explosion, fire, flooding, vibration, fracturing, earthquake, or subsidence.

11. Negligence by a person or an Entity exercising a right to extract or develop minerals, water, or any other substances.

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EXPANDED COVERAGE RESIDENTIAL LOAN POLICY
For a one-to-four family residence
Issued By
BLANK TITLE INSURANCE COMPANY

SCHEDULE A

Name and Address of Title Insurance Company:

[File No.:] Policy No.:
Loan No.:
Street Address of the Land:
Policy Amount: $ [Premium: $]
Date of Policy: [at a.m./p.m.]

1. Name of Insured:

2. The estate or interest in the Land that is encumbered by the Insured Mortgage is:

3. Title is vested in:

4. The Insured Mortgage and its assignments, if any, are described as follows:

5. The Land referred to in this policy is described as follows:

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EXPANDED COVERAGE RESIDENTIAL LOAN POLICY
For a one-to-four family residence
Issued By
BLANK TITLE INSURANCE COMPANY

SCHEDULE B - PART I

File No. Policy No.

EXCEPTIONS FROM COVERAGE

This policy does not insure against loss or damage (and the Company will not pay costs, attorneys' fees or expenses) that arise by reason of:

[**1.** The following state statutes, reference to which are made part of the ALTA 8.1-06 Environmental Protection Lien Endorsement incorporated into this Policy:]

SCHEDULE B - PART II

In addition to the matters set forth in Part I of this Schedule, the Title is subject to the following matters, and the Company insures against loss or damage sustained in the event that they are not subordinate to the lien of the Insured Mortgage:

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CONDITIONS

1. DEFINITION OF TERMS

The following terms when used in this policy mean:

(a) "Advances": Disbursements of Indebtedness made after the Date of Policy as provided by the Insured Mortgage.

(b) "Amount of Insurance": One hundred twenty-five percent (125%) of the Policy Amount stated in Schedule A, as may be increased or decreased by endorsement to this policy, increased by Section 8(b) or decreased by Section 10 of these Conditions.

(c) "Date of Policy": The date designated as "Date of Policy" in Schedule A.

(d) "Entity": A corporation, partnership, trust, limited liability company, or other similar legal entity.

(e) "Indebtedness": The obligation secured by the Insured Mortgage including one evidenced by electronic means authorized by law, and if that obligation is the payment of a debt, the Indebtedness is the sum of

(i) the amount of the principal disbursed as of Date of Policy;

(ii) the amount of the principal disbursed subsequent to Date of Policy;

(iii) the construction loan advances made subsequent to Date of Policy for the purpose of financing in whole or in part the construction of an improvement to the Land or related to the Land that the Insured was and continued to be obligated to advance at Date of Policy and at the date of the Advance;

(iv) interest on the loan;

(v) the prepayment premiums, exit fees, and other similar fees or penalties allowed by law;

(vi) the expenses of foreclosure and any other costs of enforcement;

(vii) the amounts advanced to assure compliance with laws or to protect the lien or the priority of the lien of the Insured Mortgage before the acquisition of the estate or interest in the Title;

(viii) the amounts to pay taxes and insurance; and

(ix) the reasonable amounts expended to prevent deterioration of improvements;

but the Indebtedness is reduced by the total of all payments and by any amount forgiven by an Insured.

(f) "Insured": The Insured named in Schedule A.

(i) The term "Insured" also includes

(A) the owner of the Indebtedness and each successor in ownership of the Indebtedness, whether the owner or successor owns the Indebtedness for its own account or as a trustee or other fiduciary, except a successor who is an obligor under the provisions of Section 12(c) of these Conditions;

(B) the person or Entity who has "control" of the "transferable record," if the Indebtedness is evidenced by a "transferable record," as these terms are defined by applicable electronic transactions law;

(C) successors to an Insured by dissolution, merger, consolidation, distribution, or reorganization;

(D) successors to an Insured by its conversion to another kind of Entity;

(E) a grantee of an Insured under a deed delivered without payment of actual valuable consideration conveying the Title

(1) if the stock, shares, memberships, or other equity interests of the grantee are wholly-owned by the named Insured,

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(2) if the grantee wholly owns the named Insured, or

(3) if the grantee is wholly-owned by an affiliated Entity of the named Insured, provided the affiliated Entity and the named Insured are both wholly-owned by the same person or Entity;

(F) any government agency or instrumentality that is an insurer or guarantor under an insurance contract or guaranty insuring or guaranteeing the Indebtedness secured by the Insured Mortgage, or any part of it, whether named as an Insured or not;

(ii) With regard to (A), (B), (C), (D), and (E) reserving, however, all rights and defenses as to any successor that the Company would have had against any predecessor Insured, unless the successor acquired the Indebtedness as a purchaser for value without Knowledge of the asserted defect, lien, encumbrance, or other matter insured against by this policy.

(g) "Insured Claimant": An Insured claiming loss or damage.

(h) "Insured Mortgage": The Mortgage described in paragraph 4 of Schedule A.

(i) "Knowledge" or "Known": Actual knowledge, not constructive knowledge or notice that may be imputed to an Insured by reason of the Public Records or any other records that impart constructive notice of matters affecting the Title.

(j) "Land": The land described in Schedule A, and affixed improvements that by law constitute real property. The term "Land" does not include any property beyond the lines of the area described in Schedule A, nor any right, title, interest, estate, or easement in abutting streets, roads, avenues, alleys, lanes, ways, or waterways, but this does not modify or limit the extent that a right of access to and from the Land is insured by this policy.

(k) "Mortgage": Mortgage, deed of trust, trust deed, or other security instrument, including one evidenced by electronic means authorized by law.

(l) "Public Records": Records established under state statutes at Date of Policy for the purpose of imparting constructive notice of matters relating to real property to purchasers for value and without Knowledge. With respect to Covered Risk 5(d), "Public Records" shall also include environmental protection liens filed in the records of the clerk of the United States District Court for the district where the Land is located.

(m) "Title": The estate or interest described in Schedule A.

(n) "Unmarketable Title": Title affected by an alleged or apparent matter that would permit a prospective purchaser or lessee of the Title or lender on the Title or a prospective purchaser of the Insured Mortgage to be released from the obligation to purchase, lease, or lend if there is a contractual condition requiring the delivery of marketable title.

2. CONTINUATION OF INSURANCE

The coverage of this policy shall continue in force as of Date of Policy in favor of an Insured after acquisition of the Title by an Insured or after conveyance by an Insured, but only so long as the Insured retains an estate or interest in the Land, or holds an obligation secured by a purchase money Mortgage given by a purchaser from the Insured, or only so long as the Insured shall have liability by reason of warranties in any transfer or conveyance of the Title. This policy shall not continue in force in favor of any purchaser from the Insured of either (i) an estate or interest in the Land, or (ii) an obligation secured by a purchase money Mortgage given to the Insured.

3. NOTICE OF CLAIM TO BE GIVEN BY INSURED CLAIMANT

The Insured shall notify the Company promptly in writing (i) in case of any litigation as set forth in Section 5(a) of these Conditions, (ii) in case Knowledge shall come to an Insured of any claim of title or interest that is adverse to the Title or the lien of the Insured Mortgage, as insured, and that

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might cause loss or damage for which the Company may be liable by virtue of this policy, or (iii) if the Title or the lien of the Insured Mortgage, as insured, is rejected as Unmarketable Title. If the Company is prejudiced by the failure of the Insured Claimant to provide prompt notice, the Company's liability to the Insured Claimant under the policy shall be reduced to the extent of the prejudice.

4. PROOF OF LOSS

In the event the Company is unable to determine the amount of loss or damage, the Company may, at its option, require as a condition of payment that the Insured Claimant furnish a signed proof of loss. The proof of loss must describe the defect, lien, encumbrance, or other matter insured against by this policy that constitutes the basis of loss or damage and shall state, to the extent possible, the basis of calculating the amount of the loss or damage.

5. DEFENSE AND PROSECUTION OF ACTIONS

(a) Upon written request by the Insured, and subject to the options contained in Section 7 of these Conditions, the Company, at its own cost and without unreasonable delay, shall provide for the defense of an Insured in litigation in which any third party asserts a claim covered by this policy adverse to the Insured. This obligation is limited to only those stated causes of action alleging matters insured against by this policy. The Company shall have the right to select counsel of its choice (subject to the right of the Insured to object for reasonable cause) to represent the Insured as to those stated causes of action. It shall not be liable for and will not pay the fees of any other counsel. The Company will not pay any fees, costs, or expenses incurred by the Insured in the defense of those causes of action that allege matters not insured against by this policy.

(b) The Company shall have the right, in addition to the options contained in Section 7 of these Conditions, at its own cost, to institute and prosecute any action or proceeding or to do any other act that in its opinion may be necessary or desirable to establish the Title or the lien of the Insured Mortgage, as insured, or to prevent or reduce loss or damage to the Insured. The Company may take any appropriate action under the terms of this policy, whether or not it shall be liable to the Insured. The exercise of these rights shall not be an admission of liability or waiver of any provision of this policy. If the Company exercises its rights under this subsection, it must do so diligently.

(c) Whenever the Company brings an action or asserts a defense as required or permitted by this policy, the Company may pursue the litigation to a final determination by a court of competent jurisdiction, and it expressly reserves the right, in its sole discretion, to appeal any adverse judgment or order.

6. DUTY OF INSURED CLAIMANT TO COOPERATE

(a) In all cases where this policy permits or requires the Company to prosecute or provide for the defense of any action or proceeding and any appeals, the Insured shall secure to the Company the right to so prosecute or provide defense in the action or proceeding, including the right to use, at its option, the name of the Insured for this purpose. Whenever requested by the Company, the Insured, at the Company's expense, shall give the Company all reasonable aid (i) in securing evidence, obtaining witnesses, prosecuting or defending the action or proceeding, or effecting settlement, and (ii) in any other lawful act that in the opinion of the Company may be necessary or desirable to establish the Title, the lien of the Insured Mortgage, or any other matter as insured. If the Company is prejudiced by the failure of the Insured to furnish the required cooperation, the Company's obligations to the Insured under the policy shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation, with regard to the matter or matters requiring such cooperation.

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(b) The Company may reasonably require the Insured Claimant to submit to examination under oath by any authorized representative of the Company and to produce for examination, inspection, and copying, at such reasonable times and places as may be designated by the authorized representative of the Company, all records, in whatever medium maintained, including books, ledgers, checks, memoranda, correspondence, reports, e-mails, disks, tapes, and videos whether bearing a date before or after Date of Policy, that reasonably pertain to the loss or damage. Further, if requested by any authorized representative of the Company, the Insured Claimant shall grant its permission, in writing, for any authorized representative of the Company to examine, inspect, and copy all of these records in the custody or control of a third party that reasonably pertain to the loss or damage. All information designated as confidential by the Insured Claimant provided to the Company pursuant to this Section shall not be disclosed to others unless, in the reasonable judgment of the Company, it is necessary in the administration of the claim. Failure of the Insured Claimant to submit for examination under oath, produce any reasonably requested information, or grant permission to secure reasonably necessary information from third parties as required in this subsection, unless prohibited by law or governmental regulation, shall terminate any liability of the Company under this policy as to that claim.

7. OPTIONS TO PAY OR OTHERWISE SETTLE CLAIMS; TERMINATION OF LIABILITY

In case of a claim under this policy, the Company shall have the following additional options:

(a) To Pay or Tender Payment of the Amount of Insurance or to Purchase the Indebtedness.

(i) To pay or tender payment of the Amount of Insurance under this policy together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment or tender of payment and that the Company is obligated to pay; or

(ii) To purchase the Indebtedness for the amount of the Indebtedness on the date of purchase, together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of purchase and that the Company is obligated to pay.

When the Company purchases the Indebtedness, the Insured shall transfer, assign, and convey to the Company the Indebtedness and the Insured Mortgage, together with any collateral security.

Upon the exercise by the Company of either of the options provided for in subsections (a)(i) or (ii), all liability and obligations of the Company to the Insured under this policy, other than to make the payment required in those subsections, shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation.

(b) To Pay or Otherwise Settle With Parties Other Than the Insured or With the Insured Claimant.

(i) to pay or otherwise settle with other parties for or in the name of an Insured Claimant any claim insured against under this policy. In addition, the Company will pay any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment and that the Company is obligated to pay; or

(ii) to pay or otherwise settle with the Insured Claimant the loss or damage provided for under this policy, together with any costs, attorneys' fees, and expenses incurred by the Insured Claimant that were authorized by the Company up to the time of payment and that the Company is obligated to pay.

Upon the exercise by the Company of either of the options provided for in subsections (b)(i) or (ii), the Company's obligations to the Insured under this policy for the claimed loss or damage, other than the payments required to be made, shall terminate, including any liability or obligation to defend, prosecute, or continue any litigation.

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8. DETERMINATION AND EXTENT OF LIABILITY

This policy is a contract of indemnity against actual monetary loss or damage sustained or incurred by the Insured Claimant who has suffered loss or damage by reason of matters insured against by this policy.

(a) The extent of liability of the Company for loss or damage under this policy shall not exceed the least of

(i) the Amount of Insurance,

(ii) the Indebtedness,

(iii) the difference between the value of the Title as insured and the value of the Title subject to the risk insured against by this policy, or

(iv) if a government agency or instrumentality is the Insured Claimant, the amount it paid in the acquisition of the Title or the Insured Mortgage in satisfaction of its insurance contract or guaranty.

(b) If the Company pursues its rights under Section 5 of these Conditions and is unsuccessful in establishing the Title or the lien of the Insured Mortgage, as insured,

(i) the Amount of Insurance shall be increased by 10%, and

(ii) the Insured Claimant shall have the right to have the loss or damage determined either as of the date the claim was made by the Insured Claimant or as of the date it is settled and paid.

(c) In the event the Insured has acquired the Title in the manner described in Section 2 of these Conditions or has conveyed the Title, then the extent of liability of the Company shall continue as set forth in Section 8(a) of these Conditions.

(d) In addition to the extent of liability under (a), (b), and (c), the Company will also pay those costs, attorneys' fees, and expenses incurred in accordance with Sections 5 and 7 of these Conditions.

9. LIMITATION OF LIABILITY

(a) If the Company establishes the Title, or removes the alleged defect, lien, or encumbrance, or cures the lack of a right of access to or from the Land, or cures the claim of Unmarketable Title, or establishes the lien of the Insured Mortgage, all as insured, in a reasonably diligent manner by any method, including litigation and the completion of any appeals, it shall have fully performed its obligations with respect to that matter and shall not be liable for any loss or damage caused to the Insured.

(b) In the event of any litigation, including litigation by the Company or with the Company's consent, the Company shall have no liability for loss or damage until there has been a final determination by a court of competent jurisdiction, and disposition of all appeals, adverse to the Title or to the lien of the Insured Mortgage, as insured.

(c) The Company shall not be liable for loss or damage to the Insured for liability voluntarily assumed by the Insured in settling any claim or suit without the prior written consent of the Company.

10. REDUCTION OF INSURANCE; REDUCTION OR TERMINATION OF LIABILITY

(a) All payments under this policy, except payments made for costs, attorneys' fees, and expenses, shall reduce the Amount of Insurance by the amount of the payment. However, any payments made prior to the acquisition of Title as provided in Section 2 of these Conditions shall not reduce the Amount of Insurance afforded under this policy except to the extent that the payments reduce the Indebtedness.

(b) The voluntary satisfaction or release of the Insured Mortgage shall terminate all liability of the

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Company except as provided in Section 2 of these Conditions.

11. PAYMENT OF LOSS

When liability and the extent of loss or damage have been definitely fixed in accordance with these Conditions, the payment shall be made within 30 days.

12. RIGHTS OF RECOVERY UPON PAYMENT OR SETTLEMENT

(a) The Company's Right to Recover

Whenever the Company shall have settled and paid a claim under this policy, it shall be subrogated and entitled to the rights of the Insured Claimant in the Title or Insured Mortgage and all other rights and remedies in respect to the claim that the Insured Claimant has against any person or property, to the extent of the amount of any loss, costs, attorneys' fees, and expenses paid by the Company. If requested by the Company, the Insured Claimant shall execute documents to evidence the transfer to the Company of these rights and remedies. The Insured Claimant shall permit the Company to sue, compromise, or settle in the name of the Insured Claimant and to use the name of the Insured Claimant in any transaction or litigation involving these rights and remedies.

If a payment on account of a claim does not fully cover the loss of the Insured Claimant, the Company shall defer the exercise of its right to recover until after the Insured Claimant shall have recovered its loss.

(b) The Insured's Rights and Limitations

(i) The owner of the Indebtedness may release or substitute the personal liability of any debtor or guarantor, extend or otherwise modify the terms of payment, release a portion of the Title from the lien of the Insured Mortgage, or release any collateral security for the Indebtedness, if it does not affect the enforceability or priority of the lien of the Insured Mortgage.

(ii) If the Insured exercises a right provided in (b)(i), but has Knowledge of any claim adverse to the Title or the lien of the Insured Mortgage insured against by this policy, the Company shall be required to pay only that part of any losses insured against by this policy that shall exceed the amount, if any, lost to the Company by reason of the impairment by the Insured Claimant of the Company's right of subrogation.

(c) The Company's Rights Against Noninsured Obligors

The Company’s right of subrogation includes the Insured’s rights against non-insured obligors including the rights of the Insured to indemnities, guarantees, other policies of insurance, or bonds, notwithstanding any terms or conditions contained in those instruments that address subrogation rights.

The Company's right of subrogation shall not be avoided by acquisition of the Insured Mortgage by an obligor (except an obligor described in Section 1(f)(i)(F) of these Conditions) who acquires the Insured Mortgage as a result of an indemnity, guarantee, other policy of insurance, or bond, and the obligor will not be an Insured under this policy.

13. ARBITRATION

Either the Company or the Insured may demand that the claim or controversy shall be submitted to arbitration pursuant to the Title Insurance Arbitration Rules of the American Land Title Association (“Rules”). Except as provided in the Rules, there shall be no joinder or consolidation with claims or controversies of other persons. Arbitrable matters may include, but are not limited to, any controversy or claim between the Company and the Insured arising out of or relating to this policy, any service in connection with its issuance or the breach of a policy provision, or to any other controversy or claim arising out of the transaction giving rise to this policy. All arbitrable matters

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when the Amount of Insurance is $2,000,000 or less shall be arbitrated at the option of either the Company or the Insured. All arbitrable matters when the Amount of Insurance is in excess of $2,000,000 shall be arbitrated only when agreed to by both the Company and the Insured. Arbitration pursuant to this policy and under the Rules shall be binding upon the parties. Judgment upon the award rendered by the Arbitrator(s) may be entered in any court of competent jurisdiction.

14. LIABILITY LIMITED TO THIS POLICY; POLICY ENTIRE CONTRACT

(a) This policy together with all endorsements, if any, attached to it by the Company is the entire policy and contract between the Insured and the Company. In interpreting any provision of this policy, this policy shall be construed as a whole.

(b) Any claim of loss or damage that arises out of the status of the Title or lien of the Insured Mortgage or by any action asserting such claim shall be restricted to this policy.

(c) Any amendment of or endorsement to this policy must be in writing and authenticated by an authorized person, or expressly incorporated by Schedule A of this policy.

(d) Each endorsement to this policy issued at any time is made a part of this policy and is subject to all of its terms and provisions. Except as the endorsement expressly states, it does not (i) modify any of the terms and provisions of the policy, (ii) modify any prior endorsement, (iii) extend the Date of Policy, or (iv) increase the Amount of Insurance.

15. SEVERABILITY

In the event any provision of this policy, in whole or in part, is held invalid or unenforceable under applicable law, the policy shall be deemed not to include that provision or such part held to be invalid, but all other provisions shall remain in full force and effect.

16. CHOICE OF LAW; FORUM

(a) Choice of Law: The Insured acknowledges the Company has underwritten the risks covered by this policy and determined the premium charged therefor in reliance upon the law affecting interests in real property and applicable to the interpretation, rights, remedies, or enforcement of policies of title insurance of the jurisdiction where the Land is located.

Therefore, the court or an arbitrator shall apply the law of the jurisdiction where the Land is located to determine the validity of claims against the Title or the lien of the Insured Mortgage that are adverse to the Insured and to interpret and enforce the terms of this policy. In neither case shall the court or arbitrator apply its conflicts of law principles to determine the applicable law.

(b) Choice of Forum: Any litigation or other proceeding brought by the Insured against the Company must be filed only in a state or federal court within the United States of America or its territories having appropriate jurisdiction.

17. NOTICES, WHERE SENT

Any notice of claim and any other notice or statement in writing required to be given to the Company under this policy must be given to the Company at [fill in].

NOTE: Bracketed [ ] material optional

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HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

OWNER'S INFORMATION SHEET

Your Title Insurance Policy is a legal contract between You and Us.

It applies only to a one-to-four family residence and only if each insured named in Schedule A is a Natural Person. If the Land described in Schedule A of the Policy is not an improved residential lot on which there is located a one-to-four family residence, or if each insured named in Schedule A is not a Natural Person, contact Us immediately.

The Policy insures You against actual loss resulting from certain Covered Risks. These Covered Risks are listed beginning on page of the Policy. The Policy is limited by:

- Provisions of Schedule A
- Exceptions in Schedule B
- Our Duty To Defend Against Legal Actions On Page _____
- Exclusions on page __
- Conditions on pages __ and __.

You should keep the Policy even if You transfer Your Title to the Land. It may protect against claims made against You by someone else after You transfer Your Title.

IF YOU WANT TO MAKE A CLAIM, **SEE SECTION 3 UNDER CONDITIONS ON PAGE** __.

The premium for this Policy is paid once. No additional premium is owed for the Policy.

This sheet is not Your insurance Policy. It is only a brief outline of some of the important Policy features. The Policy explains in detail Your rights and obligations and Our rights and obligations. Since the Policy--and not this sheet--is the legal document,

YOU SHOULD READ THE POLICY VERY CAREFULLY.

If You have any questions about Your Policy, contact:

BLANK TITLE INSURANCE COMPANY

____

____

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AMERICAN LAND TITLE ASSOCIATION

HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

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HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

As soon as You Know of anything that might be covered by this Policy, You must notify Us promptly in writing at the address shown in Section 3 of the Conditions.

OWNER'S COVERAGE STATEMENT

This Policy insures You against actual loss, including any costs, attorneys' fees and expenses provided under this Policy. The loss must result from one or more of the Covered Risks set forth below. This Policy covers only Land that is an improved residential lot on which there is located a one-to-four family residence and only when each insured named in Schedule A is a Natural Person.

Your insurance is effective on the Policy Date. This Policy covers Your actual loss from any risk described under Covered Risks if the event creating the risk exists on the Policy Date or, to the extent expressly stated in Covered Risks, after the Policy Date.

Your insurance is limited by all of the following:

- The Policy Amount
- For Covered Risk 16, 18, 19 and 21, Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A
- The Exceptions in Schedule B
- Our Duty To Defend Against Legal Actions
- The Exclusions on page
- The Conditions on pages and .

COVERED RISKS

The Covered Risks are:

1. Someone else owns an interest in Your Title.
2. Someone else has rights affecting Your Title because of leases, contracts, or options.
3. Someone else claims to have rights affecting Your Title because of forgery or impersonation.
4. Someone else has an Easement on the Land.
5. Someone else has a right to limit Your use of the Land.

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6. Your Title is defective. Some of these defects are:

    a. Someone else's failure to have authorized a transfer or conveyance of your Title.
    b. Someone else's failure to create a valid document by electronic means.
    c. A document upon which Your Title is based is invalid because it was not properly signed, sealed, acknowledged, delivered or recorded.
    d. A document upon which Your Title is based was signed using a falsified, expired, or otherwise invalid power of attorney.
    e. A document upon which Your Title is based was not properly filed, recorded, or indexed in the Public Records.
    f. A defective judicial or administrative proceeding.

7. Any of Covered Risks 1 through 6 occurring after the Policy Date.

8. Someone else has a lien on Your Title, including a:

    a. lien of real estate taxes or assessments imposed on Your Title by a governmental authority that are due or payable, but unpaid;
    b. Mortgage;
    c. judgment, state or federal tax lien;
    d. charge by a homeowner's or condominium association; or
    e. lien, occurring before or after the Policy Date, for labor and material furnished before the Policy Date.

9. Someone else has an encumbrance on Your Title.

10. Someone else claims to have rights affecting Your Title because of fraud, duress, incompetency or incapacity.

11. You do not have actual vehicular and pedestrian access to and from the Land, based upon a legal right.

12. You are forced to correct or remove an existing violation of any covenant, condition or restriction affecting the Land, even if the covenant, condition or restriction is excepted in Schedule B. However, You are not covered for any violation that relates to:

    a. any obligation to perform maintenance or repair on the Land; or
    b. environmental protection of any kind, including hazardous or toxic conditions or substances

    unless there is a notice recorded in the Public Records, describing any part of the Land, claiming a violation exists. Our liability for this Covered Risk is limited to the extent of the violation stated in that notice.

13. Your Title is lost or taken because of a violation of any covenant, condition or restriction, which occurred before You acquired Your Title, even if the covenant, condition or restriction is excepted in Schedule B.

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14. The violation or enforcement of those portions of any law or government regulation concerning:

    a. building;
    b. zoning;
    c. land use;
    d. improvements on the Land;
    e. land division; or
    f. environmental protection,

    if there is a notice recorded in the Public Records, describing any part of the Land, claiming a violation exists or declaring the intention to enforce the law or regulation. Our liability for this Covered Risk is limited to the extent of the violation or enforcement stated in that notice.

15. An enforcement action based on the exercise of a governmental police power not covered by Covered Risk 14 if there is a notice recorded in the Public Records, describing any part of the Land, of the enforcement action or intention to bring an enforcement action. Our liability for this Covered Risk is limited to the extent of the enforcement action stated in that notice.

16. Because of an existing violation of a subdivision law or regulation affecting the Land:

    a. You are unable to obtain a building permit;
    b. You are required to correct or remove the violation; or
    c. someone else has a legal right to, and does, refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it.

    The amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

17. You lose Your Title to any part of the Land because of the right to take the Land by condemning it, if:

    a. there is a notice of the exercise of the right recorded in the Public Records and the notice describes any part of the Land; or
    b. the taking happened before the Policy Date and is binding on You if You bought the Land without Knowing of the taking.

18. You are forced to remove or remedy Your existing structures, or any part of them - other than boundary walls or fences - because any portion was built without obtaining a building permit from the proper government office. The amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

19. You are forced to remove or remedy Your existing structures, or any part of them, because they violate an existing zoning law or zoning regulation. If You are required to remedy any portion of Your existing structures, the amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

20. You cannot use the Land because use as a single-family residence violates an existing zoning law or zoning regulation. 21. You are forced to remove Your existing structures because they encroach onto Your neighbor's land. If the encroaching structures are boundary walls or fences, the amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

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22. Someone else has a legal right to, and does, refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it because Your neighbor's existing structures encroach onto the Land.

23. You are forced to remove Your existing structures which encroach onto an Easement or over a building set-back line, even if the Easement or building set-back line is excepted in Schedule B.

24. Your existing structures are damaged because of the exercise of a right to maintain or use any Easement affecting the Land, even if the Easement is excepted in Schedule B.

25. Your existing improvements (or a replacement or modification made to them after the Policy Date), including lawns, shrubbery or trees, are damaged because of the future exercise of a right to use the surface of the Land for the extraction or development of minerals, water or any other substance, even if those rights are excepted or reserved from the description of the Land or excepted in Schedule B.

26. Someone else tries to enforce a discriminatory covenant, condition or restriction that they claim affects Your Title which is based upon race, color, religion, sex, handicap, familial status, or national origin.

27. A taxing authority assesses supplemental real estate taxes not previously assessed against the Land for any period before the Policy Date because of construction or a change of ownership or use that occurred before the Policy Date.

28. Your neighbor builds any structures after the Policy Date -- other than boundary walls or fences -- which encroach onto the Land.

29. Your Title is unmarketable, which allows someone else to refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it.

30. Someone else owns an interest in Your Title because a court order invalidates a prior transfer of the title under federal bankruptcy, state insolvency, or similar creditors' rights laws.

31. The residence with the address shown in Schedule A is not located on the Land at the Policy Date.

32. The map, if any, attached to this Policy does not show the correct location of the Land according to the Public Records.

OUR DUTY TO DEFEND AGAINST LEGAL ACTIONS

We will defend Your Title in any legal action only as to that part of the action which is based on a Covered Risk and which is not excepted or excluded from coverage in this Policy. We will pay the costs, attorneys' fees, and expenses We incur in that defense.

We will not pay for any part of the legal action which is not based on a Covered Risk or which is excepted or excluded from coverage in this Policy.

We can end Our duty to defend Your Title under Section 4 of the Conditions.

THIS POLICY IS NOT COMPLETE WITHOUT SCHEDULES A AND B.

[Witness clause optional]

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BLANK TITLE INSURANCE COMPANY

BY:______________________________________
PRESIDENT

BY:______________________________________
SECRETARY

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EXCLUSIONS

In addition to the Exceptions in Schedule B, You are not insured against loss, costs, attorneys' fees, and expenses resulting from:

1. Governmental police power, and the existence or violation of those portions of any law or government regulation concerning:

   a. building;
   b. zoning;
   c. land use;
   d. improvements on the Land;
   e. land division; and
   f. environmental protection.

   This Exclusion does not limit the coverage described in Covered Risk 8.a., 14, 15, 16, 18, 19, 20, 23 or 27.

2. The failure of Your existing structures, or any part of them, to be constructed in accordance with applicable building codes. This Exclusion does not limit the coverage described in Covered Risk 14 or 15.

3. The right to take the Land by condemning it. This Exclusion does not limit the coverage described in Covered Risk 17.

4. Risks:

   a. that are created, allowed, or agreed to by You, whether or not they are recorded in the Public Records;
   b. that are Known to You at the Policy Date, but not to Us, unless they are recorded in the Public Records at the Policy Date;
   c. that result in no loss to You; or
   d. that first occur after the Policy Date - this does not limit the coverage described in Covered Risk 7, 8.e., 25, 26, 27 or 28.

5. Failure to pay value for Your Title.

6. Lack of a right:

   a. to any land outside the area specifically described and referred to in paragraph 3 of Schedule A; and
   b. in streets, alleys, or waterways that touch the Land.

   This Exclusion does not limit the coverage described in Covered Risk 11 or 21.

7. The transfer of the Title to You is invalid as a preferential transfer or as a fraudulent transfer or conveyance under federal bankruptcy, state insolvency, or similar creditors' rights laws.

8. Contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence.

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9. Negligence by a person or an Entity exercising a right to extract or develop minerals, water, or any other substances.

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HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

CONDITIONS

1. DEFINITIONS

   a. Easement - the right of someone else to use the Land for a special purpose.

   b. Estate Planning Entity - a legal entity or Trust established by a Natural Person for estate planning.

   c. Known - things about which You have actual knowledge. The words "Know" and "Knowing" have the same meaning as Known.

   d. Land - the land or condominium unit described in paragraph 3 of Schedule A and any improvements on the Land which are real property.

   e. Mortgage - a mortgage, deed of trust, trust deed or other security instrument.

   f. Natural Person - a human being, not a commercial or legal organization or entity. Natural Person includes a trustee of a Trust even if the trustee is not a human being.

   g. Policy Date - the date and time shown in Schedule A. If the insured named in Schedule A first acquires the interest shown in Schedule A by an instrument recorded in the Public Records later than the date and time shown in Schedule A, the Policy Date is the date and time the instrument is recorded.

   h. Public Records - records that give constructive notice of matters affecting Your Title, according to the state statutes where the Land is located.

   i. Title - the ownership of Your interest in the Land, as shown in Schedule A.

   j. Trust - a living trust established by a Natural Person for estate planning.

   k. We/Our/Us - Blank Title Insurance Company.

   l. You/Your - the insured named in Schedule A and also those identified in Section 2.b. of these Conditions.

2. CONTINUATION OF COVERAGE

   a. This Policy insures You forever, even after You no longer have Your Title. You cannot assign this Policy to anyone else.

   b. This Policy also insures:

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(1) anyone who inherits Your Title because of Your death;

(2) Your spouse who receives Your Title because of dissolution of Your marriage;

(3) the trustee or successor trustee of Your Trust or any Estate Planning Entity created for You to whom or to which You transfer Your Title after the Policy Date;

(4) the beneficiaries of Your Trust upon Your death; or

(5) anyone who receives Your Title by a transfer effective on Your death as authorized by law.

c. We may assert against the insureds identified in Section 2.b. any rights and defenses that We have against any previous insured under this Policy.

3. HOW TO MAKE A CLAIM

a. Prompt Notice Of Your Claim

(1) As soon as You Know of anything that might be covered by this Policy, You must notify Us promptly in writing.

(2) Send Your notice to **Blank Title Insurance Company**, , Attention: Claims Department. Please include the Policy number shown in Schedule A , and the county and state where the Land is located. Please enclose a copy of Your policy, if available.

(3) If You do not give Us prompt notice, Your coverage will be reduced or ended, but only to the extent Your failure affects Our ability to resolve the claim or defend You.

b. Proof Of Your Loss

(1) We may require You to give Us a written statement signed by You describing Your loss which includes:

(a) the basis of Your claim;

(b) the Covered Risks which resulted in Your loss;

(c) the dollar amount of Your loss; and

(d) the method You used to compute the amount of Your loss.

(2) We may require You to make available to Us records, checks, letters, contracts, insurance policies and other papers which relate to Your claim. We may make copies of these papers.

(3) We may require You to answer questions about Your claim under oath.

(4) If you fail or refuse to give Us a statement of loss, answer Our questions under oath, or make available to Us the papers We request, Your coverage will be reduced or ended, but only to the extent Your failure or refusal affects Our ability to resolve the claim or defend You.

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4. OUR CHOICES WHEN WE LEARN OF A CLAIM

a. After We receive Your notice, or otherwise learn, of a claim that is covered by this Policy, Our choices include one or more of the following:

(1) Pay the claim;

(2) Negotiate a settlement;

(3) Bring or defend a legal action related to the claim;

(4) Pay You the amount required by this Policy;

(5) End the coverage of this Policy for the claim by paying You Your actual loss resulting from the Covered Risk, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

(6) End the coverage described in Covered Risk 16, 18, 19 or 21 by paying You the amount of Your insurance then in force for the particular Covered Risk, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

(7) End all coverage of this Policy by paying You the Policy Amount then in force, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

(8) Take other appropriate action.

b. When We choose the options in Sections 4.a. (5), (6) or (7), all Our obligations for the claim end, including Our obligation to defend, or continue to defend, any legal action.

c. Even if We do not think that the Policy covers the claim, We may choose one or more of the options above. By doing so, We do not give up any rights.

5. HANDLING A CLAIM OR LEGAL ACTION

a. You must cooperate with Us in handling any claim or legal action and give Us all relevant information.

b. If You fail or refuse to cooperate with Us, Your coverage will be reduced or ended, but only to the extent Your failure or refusal affects Our ability to resolve the claim or defend You.

c. We are required to repay You only for those settlement costs, attorneys' fees and expenses that We approve in advance.

d. We have the right to choose the attorney when We bring or defend a legal action on Your behalf. We can appeal any decision to the highest level. We do not have to pay Your claim until the legal action is finally decided.

e. Whether or not We agree there is coverage, We can bring or defend a legal action, or take other appropriate action under this Policy. By doing so, We do not give up any rights.

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6. LIMITATION OF OUR LIABILITY

   a. After subtracting Your Deductible Amount if it applies, We will pay no more than the least of:

      (1) Your actual loss;

      (2) Our Maximum Dollar Limit of Liability then in force for the particular Covered Risk, for claims covered only under Covered Risk 16, 18, 19 or 21; or

      (3) the Policy Amount then in force.

      and any costs, attorneys' fees and expenses that We are obligated to pay under this Policy.

   b. If We pursue Our rights under Sections 4.a.(3) and 5.e. of these Conditions and are unsuccessful in establishing the Title, as insured:

      (1) the Policy Amount then in force will be increased by 10% of the Policy Amount shown in Schedule A, and

      (2) You shall have the right to have the actual loss determined on either the date the claim was made by You or the date it is settled and paid.

   c. (1) If We remove the cause of the claim with reasonable diligence after receiving notice of it, all Our obligations for the claim end, including any obligation for loss You had while We were removing the cause of the claim.

      (2) Regardless of 6.c.(1) above, if You cannot use the Land because of a claim covered by this Policy:

         (a) You may rent a reasonably equivalent substitute residence and We will repay You for the actual rent You pay, until the earlier of:

            (i) the cause of the claim is removed; or

            (ii) We pay You the amount required by this Policy. If Your claim is covered only under Covered Risk 16, 18, 19 or 21, that payment is the amount of Your insurance then in force for the particular Covered Risk.

         (b) We will pay reasonable costs You pay to relocate any personal property You have the right to remove from the Land, including transportation of that personal property for up to twenty-five (25) miles from the Land, and repair of any damage to that personal property because of the relocation. The amount We will pay You under this paragraph is limited to the value of the personal property before You relocate it.

   d. All payments We make under this Policy reduce the Policy Amount then in force, except for costs, attorneys' fees and expenses. All payments We make for claims which are covered only under Covered Risk 16, 18, 19 or 21 also reduce Our Maximum Dollar Limit of Liability for the particular Covered Risk, except for costs, attorneys' fees and expenses.

   e. If We issue, or have issued, a Policy to the owner of a Mortgage that is on Your Title and We have not given You any coverage against the Mortgage, then:

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(1) We have the right to pay any amount due You under this Policy to the owner of the Mortgage, and any amount paid shall be treated as a payment to You under this Policy, including under Section 4.a. of these Conditions;

(2) Any amount paid to the owner of the Mortgage shall be subtracted from the Policy Amount then in force ; and

(3) If Your claim is covered only under Covered Risk 16, 18, 19 or 21, any amount paid to the owner of the Mortgage shall also be subtracted from Our Maximum Dollar Limit of Liability for the particular Covered Risk.

f. If You do anything to affect any right of recovery You may have against someone else, We can subtract from Our liability the amount by which You reduced the value of that right.

7. TRANSFER OF YOUR RIGHTS TO US

a. When We settle Your claim, We have all the rights and remedies You have against any person or property related to the claim. You must not do anything to affect these rights and remedies. When We ask, You must execute documents to evidence the transfer to Us of these rights and remedies. You must let Us use Your name in enforcing these rights and remedies.

b. We will not be liable to You if We do not pursue these rights and remedies or if We do not recover any amount that might be recoverable.

c. We will pay any money We collect from enforcing these rights and remedies in the following order:

(1) to Us for the costs, attorneys' fees and expenses We paid to enforce these rights and remedies;

(2) to You for Your loss that You have not already collected;

(3) to Us for any money We paid out under this Policy on account of Your claim; and

(4) to You whatever is left.

d. If You have rights and remedies under contracts (such as indemnities, guaranties, bonds or other policies of insurance) to recover all or part of Your loss, then We have all of those rights and remedies, even if those contracts provide that those obligated have all of Your rights and remedies under this Policy.

8. THIS POLICY IS THE ENTIRE CONTRACT

This Policy, with any endorsements, is the entire contract between You and Us. To determine the meaning of any part of this Policy, You must read the entire Policy and any endorsements. Any changes to this Policy must be agreed to in writing by Us. Any claim You make against Us must be made under this Policy and is subject to its terms.

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9. INCREASED POLICY AMOUNT

The Policy Amount then in force will increase by ten percent (10%) of the Policy Amount shown in Schedule A each year for the first five years following the Policy Date shown in Schedule A, up to one hundred fifty percent (150%) of the Policy Amount shown in Schedule A. The increase each year will happen on the anniversary of the Policy Date shown in Schedule A.

10. SEVERABILITY

If any part of this Policy is held to be legally unenforceable, both You and We can still enforce the rest of this Policy.

11. ARBITRATION

a. If permitted in the state where the Land is located, You or We may demand arbitration.

b. The law used in the arbitration is the law of the state where the Land is located.

c. The arbitration shall be under the Title Insurance Arbitration Rules of the American Land Title Association ("Rules"). You can get a copy of the Rules from Us.

d. Except as provided in the Rules, You cannot join or consolidate Your claim or controversy with claims or controversies of other persons.

e. The arbitration shall be binding on both You and Us. The arbitration shall decide any matter in dispute between You and Us.

f. The arbitration award may be entered as a judgment in the proper court.

12. CHOICE OF LAW

The law of the state where the Land is located shall apply to this policy.

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HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

SCHEDULE A

Name and Address of Title Insurance Company:

Policy No.: [Premium: $_______________] Policy Amount: $ Policy Date [and Time]:

Deductible Amounts and Maximum Dollar Limits of Liability
For Covered Risk 16, 18, 19 and 21:

	Your Deductible Amount	Our Maximum Dollar Limit of Liability
Covered Risk 16:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 18:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 19:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 21:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$

Street Address of the Land:

1. Name of Insured:

2. Your interest in the Land covered by this Policy is:

3. The Land referred to in this Policy is described as:

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HOMEOWNER'S POLICY OF TITLE INSURANCE

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BLANK TITLE INSURANCE COMPANY

SCHEDULE B

EXCEPTIONS

In addition to the Exclusions, You are not insured against loss, costs, attorneys' fees, and expenses resulting from:

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HOMEOWNER'S POLICY OF TITLE INSURANCE

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OWNER'S INFORMATION SHEET

Your Title Insurance Policy is a legal contract between You and Us.

It applies only to a one-to-four family residence and only if each insured named in Schedule A is a Natural Person. If the Land described in Schedule A of the Policy is not an improved residential lot on which there is located a one-to-four family residence, or if each insured named in Schedule A is not a Natural Person, contact Us immediately.

The Policy insures You against actual loss resulting from certain Covered Risks. These Covered Risks are listed beginning on page   of the Policy. The Policy is limited by:

- Provisions of Schedule A
- Exceptions in Schedule B
- Our Duty To Defend Against Legal Actions On Page _____
- Exclusions on page __
- Conditions on pages __ and __.

You should keep the Policy even if You transfer Your Title to the Land. It may protect against claims made against You by someone else after You transfer Your Title.

IF YOU WANT TO MAKE A CLAIM, **SEE SECTION 3 UNDER CONDITIONS ON PAGE** __.

The premium for this Policy is paid once. No additional premium is owed for the Policy.

This sheet is not Your insurance Policy. It is only a brief outline of some of the important Policy features. The Policy explains in detail Your rights and obligations and Our rights and obligations. Since the Policy--and not this sheet--is the legal document,

YOU SHOULD READ THE POLICY VERY CAREFULLY.

If You have any questions about Your Policy, contact:

BLANK TITLE INSURANCE COMPANY

____

____

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HOMEOWNER'S POLICY OF TITLE INSURANCE

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HOMEOWNER'S POLICY OF TITLE INSURANCE

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As soon as You Know of anything that might be covered by this Policy, You must notify Us promptly in writing at the address shown in Section 3 of the Conditions.

OWNER'S COVERAGE STATEMENT

This Policy insures You against actual loss, including any costs, attorneys' fees and expenses provided under this Policy. The loss must result from one or more of the Covered Risks set forth below. This Policy covers only Land that is an improved residential lot on which there is located a one-to-four family residence and only when each insured named in Schedule A is a Natural Person.

Your insurance is effective on the Policy Date. This Policy covers Your actual loss from any risk described under Covered Risks if the event creating the risk exists on the Policy Date or, to the extent expressly stated in Covered Risks, after the Policy Date.

Your insurance is limited by all of the following:

- The Policy Amount
- For Covered Risk 16, 18, 19 and 21, Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A
- The Exceptions in Schedule B
- Our Duty To Defend Against Legal Actions
- The Exclusions on page
- The Conditions on pages and .

COVERED RISKS

The Covered Risks are:

1. Someone else owns an interest in Your Title.
2. Someone else has rights affecting Your Title because of leases, contracts, or options.
3. Someone else claims to have rights affecting Your Title because of forgery or impersonation.
4. Someone else has an Easement on the Land.
5. Someone else has a right to limit Your use of the Land.

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6. Your Title is defective. Some of these defects are:

    a. Someone else's failure to have authorized a transfer or conveyance of your Title.
    b. Someone else's failure to create a valid document by electronic means.
    c. A document upon which Your Title is based is invalid because it was not properly signed, sealed, acknowledged, delivered or recorded.
    d. A document upon which Your Title is based was signed using a falsified, expired, or otherwise invalid power of attorney.
    e. A document upon which Your Title is based was not properly filed, recorded, or indexed in the Public Records.
    f. A defective judicial or administrative proceeding.

7. Any of Covered Risks 1 through 6 occurring after the Policy Date.

8. Someone else has a lien on Your Title, including a:

    a. lien of real estate taxes or assessments imposed on Your Title by a governmental authority that are due or payable, but unpaid;
    b. Mortgage;
    c. judgment, state or federal tax lien;
    d. charge by a homeowner's or condominium association; or
    e. lien, occurring before or after the Policy Date, for labor and material furnished before the Policy Date.

9. Someone else has an encumbrance on Your Title.

10. Someone else claims to have rights affecting Your Title because of fraud, duress, incompetency or incapacity.

11. You do not have actual vehicular and pedestrian access to and from the Land, based upon a legal right.

12. You are forced to correct or remove an existing violation of any covenant, condition or restriction affecting the Land, even if the covenant, condition or restriction is excepted in Schedule B. However, You are not covered for any violation that relates to:

    a. any obligation to perform maintenance or repair on the Land; or
    b. environmental protection of any kind, including hazardous or toxic conditions or substances

    unless there is a notice recorded in the Public Records, describing any part of the Land, claiming a violation exists. Our liability for this Covered Risk is limited to the extent of the violation stated in that notice.

13. Your Title is lost or taken because of a violation of any covenant, condition or restriction, which occurred before You acquired Your Title, even if the covenant, condition or restriction is excepted in Schedule B.

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14. The violation or enforcement of those portions of any law or government regulation concerning:

    a. building;
    b. zoning;
    c. land use;
    d. improvements on the Land;
    e. land division; or
    f. environmental protection,

    if there is a notice recorded in the Public Records, describing any part of the Land, claiming a violation exists or declaring the intention to enforce the law or regulation. Our liability for this Covered Risk is limited to the extent of the violation or enforcement stated in that notice.

15. An enforcement action based on the exercise of a governmental police power not covered by Covered Risk 14 if there is a notice recorded in the Public Records, describing any part of the Land, of the enforcement action or intention to bring an enforcement action. Our liability for this Covered Risk is limited to the extent of the enforcement action stated in that notice.

16. Because of an existing violation of a subdivision law or regulation affecting the Land:

    a. You are unable to obtain a building permit;
    b. You are required to correct or remove the violation; or
    c. someone else has a legal right to, and does, refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it.

    The amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

17. You lose Your Title to any part of the Land because of the right to take the Land by condemning it, if:

    a. there is a notice of the exercise of the right recorded in the Public Records and the notice describes any part of the Land; or
    b. the taking happened before the Policy Date and is binding on You if You bought the Land without Knowing of the taking.

18. You are forced to remove or remedy Your existing structures, or any part of them - other than boundary walls or fences - because any portion was built without obtaining a building permit from the proper government office. The amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

19. You are forced to remove or remedy Your existing structures, or any part of them, because they violate an existing zoning law or zoning regulation. If You are required to remedy any portion of Your existing structures, the amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

20. You cannot use the Land because use as a single-family residence violates an existing zoning law or zoning regulation. 21. You are forced to remove Your existing structures because they encroach onto Your neighbor's land. If the encroaching structures are boundary walls or fences, the amount of Your insurance for this Covered Risk is subject to Your Deductible Amount and Our Maximum Dollar Limit of Liability shown in Schedule A.

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22. Someone else has a legal right to, and does, refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it because Your neighbor's existing structures encroach onto the Land.

23. You are forced to remove Your existing structures which encroach onto an Easement or over a building set-back line, even if the Easement or building set-back line is excepted in Schedule B.

24. Your existing structures are damaged because of the exercise of a right to maintain or use any Easement affecting the Land, even if the Easement is excepted in Schedule B.

25. Your existing improvements (or a replacement or modification made to them after the Policy Date), including lawns, shrubbery or trees, are damaged because of the future exercise of a right to use the surface of the Land for the extraction or development of minerals, water or any other substance, even if those rights are excepted or reserved from the description of the Land or excepted in Schedule B.

26. Someone else tries to enforce a discriminatory covenant, condition or restriction that they claim affects Your Title which is based upon race, color, religion, sex, handicap, familial status, or national origin.

27. A taxing authority assesses supplemental real estate taxes not previously assessed against the Land for any period before the Policy Date because of construction or a change of ownership or use that occurred before the Policy Date.

28. Your neighbor builds any structures after the Policy Date -- other than boundary walls or fences -- which encroach onto the Land.

29. Your Title is unmarketable, which allows someone else to refuse to perform a contract to purchase the Land, lease it or make a Mortgage loan on it.

30. Someone else owns an interest in Your Title because a court order invalidates a prior transfer of the title under federal bankruptcy, state insolvency, or similar creditors' rights laws.

31. The residence with the address shown in Schedule A is not located on the Land at the Policy Date.

32. The map, if any, attached to this Policy does not show the correct location of the Land according to the Public Records.

OUR DUTY TO DEFEND AGAINST LEGAL ACTIONS

We will defend Your Title in any legal action only as to that part of the action which is based on a Covered Risk and which is not excepted or excluded from coverage in this Policy. We will pay the costs, attorneys' fees, and expenses We incur in that defense.

We will not pay for any part of the legal action which is not based on a Covered Risk or which is excepted or excluded from coverage in this Policy.

We can end Our duty to defend Your Title under Section 4 of the Conditions.

THIS POLICY IS NOT COMPLETE WITHOUT SCHEDULES A AND B.

[Witness clause optional]

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AMERICAN LAND TITLE ASSOCIATION

BLANK TITLE INSURANCE COMPANY

BY:______________________________________
PRESIDENT

BY:______________________________________
SECRETARY

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EXCLUSIONS

In addition to the Exceptions in Schedule B, You are not insured against loss, costs, attorneys' fees, and expenses resulting from:

1. Governmental police power, and the existence or violation of those portions of any law or government regulation concerning:

   a. building;
   b. zoning;
   c. land use;
   d. improvements on the Land;
   e. land division; and
   f. environmental protection.

   This Exclusion does not limit the coverage described in Covered Risk 8.a., 14, 15, 16, 18, 19, 20, 23 or 27.

2. The failure of Your existing structures, or any part of them, to be constructed in accordance with applicable building codes. This Exclusion does not limit the coverage described in Covered Risk 14 or 15.

3. The right to take the Land by condemning it. This Exclusion does not limit the coverage described in Covered Risk 17.

4. Risks:

   a. that are created, allowed, or agreed to by You, whether or not they are recorded in the Public Records;
   b. that are Known to You at the Policy Date, but not to Us, unless they are recorded in the Public Records at the Policy Date;
   c. that result in no loss to You; or
   d. that first occur after the Policy Date - this does not limit the coverage described in Covered Risk 7, 8.e., 25, 26, 27 or 28.

5. Failure to pay value for Your Title.

6. Lack of a right:

   a. to any land outside the area specifically described and referred to in paragraph 3 of Schedule A; and
   b. in streets, alleys, or waterways that touch the Land.

   This Exclusion does not limit the coverage described in Covered Risk 11 or 21.

7. The transfer of the Title to You is invalid as a preferential transfer or as a fraudulent transfer or conveyance under federal bankruptcy, state insolvency, or similar creditors' rights laws.

8. Contamination, explosion, fire, flooding, vibration, fracturing, earthquake or subsidence.

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9. Negligence by a person or an Entity exercising a right to extract or develop minerals, water, or any other substances.

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HOMEOWNER'S POLICY OF TITLE INSURANCE

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BLANK TITLE INSURANCE COMPANY

CONDITIONS

1. DEFINITIONS

   a. Easement - the right of someone else to use the Land for a special purpose.

   b. Estate Planning Entity - a legal entity or Trust established by a Natural Person for estate planning.

   c. Known - things about which You have actual knowledge. The words "Know" and "Knowing" have the same meaning as Known.

   d. Land - the land or condominium unit described in paragraph 3 of Schedule A and any improvements on the Land which are real property.

   e. Mortgage - a mortgage, deed of trust, trust deed or other security instrument.

   f. Natural Person - a human being, not a commercial or legal organization or entity. Natural Person includes a trustee of a Trust even if the trustee is not a human being.

   g. Policy Date - the date and time shown in Schedule A. If the insured named in Schedule A first acquires the interest shown in Schedule A by an instrument recorded in the Public Records later than the date and time shown in Schedule A, the Policy Date is the date and time the instrument is recorded.

   h. Public Records - records that give constructive notice of matters affecting Your Title, according to the state statutes where the Land is located.

   i. Title - the ownership of Your interest in the Land, as shown in Schedule A.

   j. Trust - a living trust established by a Natural Person for estate planning.

   k. We/Our/Us - Blank Title Insurance Company.

   l. You/Your - the insured named in Schedule A and also those identified in Section 2.b. of these Conditions.

2. CONTINUATION OF COVERAGE

   a. This Policy insures You forever, even after You no longer have Your Title. You cannot assign this Policy to anyone else.

   b. This Policy also insures:

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(1) anyone who inherits Your Title because of Your death;

(2) Your spouse who receives Your Title because of dissolution of Your marriage;

(3) the trustee or successor trustee of ~~a~~Your Trust or any Estate Planning Entity created for You to whom or to which You transfer Your Title after the Policy Date;

(4) the beneficiaries of Your Trust upon Your death; or

(5) anyone who receives Your Title by a transfer effective on Your death as authorized by law.

c. We may assert against the insureds identified in Section 2.b. any rights and defenses that We have against any previous insured under this Policy.

3. HOW TO MAKE A CLAIM

a. Prompt Notice Of Your Claim

(1) As soon as You Know of anything that might be covered by this Policy, You must notify Us promptly in writing.

(2) Send Your notice to **Blank Title Insurance Company**, , Attention: Claims Department. Please include the Policy number shown in Schedule A , and the county and state where the Land is located. Please enclose a copy of Your policy, if available.

(3) If You do not give Us prompt notice, Your coverage will be reduced or ended, but only to the extent Your failure affects Our ability to resolve the claim or defend You.

b. Proof Of Your Loss

(1) We may require You to give Us a written statement signed by You describing Your loss which includes:

(a) the basis of Your claim;

(b) the Covered Risks which resulted in Your loss;

(c) the dollar amount of Your loss; and

(d) the method You used to compute the amount of Your loss.

(2) We may require You to make available to Us records, checks, letters, contracts, insurance policies and other papers which relate to Your claim. We may make copies of these papers.

(3) We may require You to answer questions about Your claim under oath.

(4) If you fail or refuse to give Us a statement of loss, answer Our questions under oath, or make available to Us the papers We request, Your coverage will be reduced or ended, but only to the extent Your failure or refusal affects Our ability to resolve the claim or defend You.

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4. OUR CHOICES WHEN WE LEARN OF A CLAIM

   a. After We receive Your notice, or otherwise learn, of a claim that is covered by this Policy, Our choices include one or more of the following:

      (1) Pay the claim;

      (2) Negotiate a settlement;

      (3) Bring or defend a legal action related to the claim;

      (4) Pay You the amount required by this Policy;

      (5) End the coverage of this Policy for the claim by paying You Your actual loss resulting from the Covered Risk, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

      (6) End the coverage described in Covered Risk 16, 18, 19 or 21 by paying You the amount of Your insurance then in force for the particular Covered Risk, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

      (7) End all coverage of this Policy by paying You the Policy Amount then in force, and those costs, attorneys' fees and expenses incurred up to that time which We are obligated to pay;

      (8) Take other appropriate action.

   b. When We choose the options in Sections 4.a. (5), (6) or (7), all Our obligations for the claim end, including Our obligation to defend, or continue to defend, any legal action.

   c. Even if We do not think that the Policy covers the claim, We may choose one or more of the options above. By doing so, We do not give up any rights.

5. HANDLING A CLAIM OR LEGAL ACTION

   a. You must cooperate with Us in handling any claim or legal action and give Us all relevant information.

   b. If You fail or refuse to cooperate with Us, Your coverage will be reduced or ended, but only to the extent Your failure or refusal affects Our ability to resolve the claim or defend You.

   c. We are required to repay You only for those settlement costs, attorneys' fees and expenses that We approve in advance.

   d. We have the right to choose the attorney when We bring or defend a legal action on Your behalf. We can appeal any decision to the highest level. We do not have to pay Your claim until the legal action is finally decided.

   e. Whether or not We agree there is coverage, We can bring or defend a legal action, or take other appropriate action under this Policy. By doing so, We do not give up any rights.

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AMERICAN LAND TITLE ASSOCIATION

6. LIMITATION OF OUR LIABILITY

a. After subtracting Your Deductible Amount if it applies, We will pay no more than the least of:

(1) Your actual loss;

(2) Our Maximum Dollar Limit of Liability then in force for the particular Covered Risk, for claims covered only under Covered Risk 16, 18, 19 or 21; or

(3) the Policy Amount then in force.

and any costs, attorneys' fees and expenses that We are obligated to pay under this Policy.

b. If We pursue Our rights under Sections 4.a.(3) and 5.e. of these Conditions and are unsuccessful in establishing the Title, as insured:

(1) the Policy Amount then in force will be increased by 10% of the Policy Amount shown in Schedule A, and

(2) You shall have the right to have the actual loss determined on either the date the claim was made by You or the date it is settled and paid.

c. (1) If We remove the cause of the claim with reasonable diligence after receiving notice of it, all Our obligations for the claim end, including any obligation for loss You had while We were removing the cause of the claim.

(2) Regardless of 6.c.(1) above, if You cannot use the Land because of a claim covered by this Policy:

(a) You may rent a reasonably equivalent substitute residence and We will repay You for the actual rent You pay, until the earlier of:

(i) the cause of the claim is removed; or

(ii) We pay You the amount required by this Policy. If Your claim is covered only under Covered Risk 16, 18, 19 or 21, that payment is the amount of Your insurance then in force for the particular Covered Risk.

(b) We will pay reasonable costs You pay to relocate any personal property You have the right to remove from the Land, including transportation of that personal property for up to twenty-five (25) miles from the Land, and repair of any damage to that personal property because of the relocation. The amount We will pay You under this paragraph is limited to the value of the personal property before You relocate it.

d. All payments We make under this Policy reduce the Policy Amount then in force, except for costs, attorneys' fees and expenses. All payments We make for claims which are covered only under Covered Risk 16, 18, 19 or 21 also reduce Our Maximum Dollar Limit of Liability for the particular Covered Risk, except for costs, attorneys' fees and expenses.

e. If We issue, or have issued, a Policy to the owner of a Mortgage that is on Your Title and We have not given You any coverage against the Mortgage, then:

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AMERICAN LAND TITLE ASSOCIATION

(1) We have the right to pay any amount due You under this Policy to the owner of the Mortgage, and any amount paid shall be treated as a payment to You under this Policy, including under Section 4.a. of these Conditions;

(2) Any amount paid to the owner of the Mortgage shall be subtracted from the Policy Amount then in force ; and

(3) If Your claim is covered only under Covered Risk 16, 18, 19 or 21, any amount paid to the owner of the Mortgage shall also be subtracted from Our Maximum Dollar Limit of Liability for the particular Covered Risk.

f. If You do anything to affect any right of recovery You may have against someone else, We can subtract from Our liability the amount by which You reduced the value of that right.

7. <u>TRANSFER OF YOUR RIGHTS TO US</u>

a. When We settle Your claim, We have all the rights and remedies You have against any person or property related to the claim. You must not do anything to affect these rights and remedies. When We ask, You must execute documents to evidence the transfer to Us of these rights and remedies. You must let Us use Your name in enforcing these rights and remedies.

b. We will not be liable to You if We do not pursue these rights and remedies or if We do not recover any amount that might be recoverable.

c. We will pay any money We collect from enforcing these rights and remedies in the following order:

(1) to Us for the costs, attorneys' fees and expenses We paid to enforce these rights and remedies;

(2) to You for Your loss that You have not already collected;

(3) to Us for any money We paid out under this Policy on account of Your claim; and

(4) to You whatever is left.

d. If You have rights and remedies under contracts (such as indemnities, guaranties, bonds or other policies of insurance) to recover all or part of Your loss, then We have all of those rights and remedies, even if those contracts provide that those obligated have all of Your rights and remedies under this Policy.

8. <u>THIS POLICY IS THE ENTIRE CONTRACT</u>

This Policy, with any endorsements, is the entire contract between You and Us. To determine the meaning of any part of this Policy, You must read the entire Policy and any endorsements. Any changes to this Policy must be agreed to in writing by Us. Any claim You make against Us must be made under this Policy and is subject to its terms.

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9. INCREASED POLICY AMOUNT

The Policy Amount then in force will increase by ten percent (10%) of the Policy Amount shown in Schedule A each year for the first five years following the Policy Date shown in Schedule A, up to one hundred fifty percent (150%) of the Policy Amount shown in Schedule A. The increase each year will happen on the anniversary of the Policy Date shown in Schedule A.

10. SEVERABILITY

If any part of this Policy is held to be legally unenforceable, both You and We can still enforce the rest of this Policy.

11. ARBITRATION

a. If permitted in the state where the Land is located, You or We may demand arbitration.

b. The law used in the arbitration is the law of the state where the Land is located.

c. The arbitration shall be under the Title Insurance Arbitration Rules of the American Land Title Association ("Rules"). You can get a copy of the Rules from Us.

d. Except as provided in the Rules, You cannot join or consolidate Your claim or controversy with claims or controversies of other persons.

e. The arbitration shall be binding on both You and Us. The arbitration shall decide any matter in dispute between You and Us.

f. The arbitration award may be entered as a judgment in the proper court.

12. CHOICE OF LAW

The law of the state where the Land is located shall apply to this policy.

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AMERICAN LAND TITLE ASSOCIATION

HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

SCHEDULE A

Name and Address of Title Insurance Company:

Policy No.: [Premium: $_______________] Policy Amount: $ Policy Date [and Time]:

Deductible Amounts and Maximum Dollar Limits of Liability
For Covered Risk 16, 18, 19 and 21:

	Your Deductible Amount	Our Maximum Dollar Limit of Liability
Covered Risk 16:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 18:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 19:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$
Covered Risk 21:	% of Policy Amount Shown in Schedule A or $ (whichever is less)	$

Street Address of the Land:

1. Name of Insured:

2. Your interest in the Land covered by this Policy is:

3. The Land referred to in this Policy is described as:

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HOMEOWNER'S POLICY OF TITLE INSURANCE

For a one-to-four family residence

Issued By

BLANK TITLE INSURANCE COMPANY

SCHEDULE B

EXCEPTIONS

In addition to the Exclusions, You are not insured against loss, costs, attorneys' fees, and expenses resulting from:

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DIVISION ONE
FILED: 9/19/2013
RUTH A. WILLINGHAM, CLERK
BY: mjt

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

CENTENNIAL DEVELOPMENT GROUP, LLC, an Arizona limited liability company, Plaintiff/Appellant, v. LAWYER'S TITLE INSURANCE CORPORATION, Defendant/Appellee.	No. 1 CA-CV 12-0080 DEPARTMENT A **O P I N I O N**

Appeal from the Superior Court in Navajo County

Cause No. S0900CV20090348

The Honorable John N. Lamb, Judge

AFFIRMED IN PART; REVERSED IN PART; REMANDED

Holland Law Firm PLLC — Snowflake
By Joseph E. Holland
Attorneys for Plaintiff/Appellant

Fidelity National Law Group — Phoenix
By Patrick J. Davis
David M. LaSpaluto
Attorneys for Defendant/Appellee

J O H N S E N, Chief Judge

¶1 Centennial Development Group, LLC sued Lawyer's Title Insurance Corporation after the latter's title commitment failed to disclose an easement. We affirm the superior court's holding on summary judgment that Arizona Revised Statutes ("A.R.S.") section 20-1562 (West 2013) bars Centennial's claim for negligence.[1] We reverse the dismissal of Centennial's contract claim, however, because although the title policy that Lawyer's Title issued only covers damages sustained while the insured owns the affected property, the "continuation of insurance" provision of the policy does not bar a claim for such damages made after the property is sold.

FACTS AND PROCEDURAL BACKGROUND

¶2 Centennial contracted to buy 75 acres in Snowflake. It made a down payment of $50,000 toward the purchase price of $1,500,000 and gave the seller two notes and deeds of trust to secure its obligation to pay the balance. In connection with its purchase, Centennial obtained a title commitment and a title insurance policy from Transnation Title Insurance Company, now Lawyer's Title. Roughly a year after closing, Centennial discovered a roadway and utility easement across its property that the commitment had not disclosed. Believing the easement substantially diminished the value of its property, Centennial unsuccessfully tried to sell the property, then defaulted on its carry-back loan from the seller. In lieu of foreclosure,

[1] Absent material revision after the relevant date, we cite a statute's current version.

Centennial reconveyed all but one acre to the prior owner through a warranty deed subject to all easements of record. The easement at issue does not burden the single acre Centennial retained.

¶3 Centennial sued Lawyer's Title, alleging negligence and breach of contract. The superior court granted summary judgment in favor of Lawyer's Title on both claims. We have jurisdiction of Centennial's timely appeal pursuant to Article 6, Section 9, of the Arizona Constitution, and A.R.S. §§ 12-120.21(A)(1) (West 2013) and -2101(A) (West 2013).

DISCUSSION

A. Standard of Review.

¶4 Arizona Rule of Civil Procedure 56(a) allows a court to enter summary judgment when "there is no genuine dispute as to any material fact and the moving party is entitled to judgment as a matter of law." We review a summary judgment *de novo*, viewing the facts and inferences drawn from those facts in the light most favorable to the party against which judgment was entered. *Brookover v. Roberts Enters., Inc.*, 215 Ariz. 52, 55, ¶ 8, 156 P.3d 1157, 1160 (App. 2007). We will affirm if the summary judgment is correct for any reason. *City of Tempe v. Outdoor Sys., Inc.*, 201 Ariz. 106, 111, ¶ 14, 32 P.3d 31, 36 (App. 2001). The interpretation of an insurance contract is a question of law we review *de novo*. *First Am. Title Ins. Co. v.*

Action Acquisitions, LLC, 218 Ariz. 394, 397, ¶ 8, 187 P.3d 1107, 1110 (2008).

B. The Negligence Claim.

¶5 Centennial's negligence claim alleged Lawyer's Title misrepresented the condition of title by omitting the easement from the report of exceptions attached to the policy. Centennial alleged the omission of the easement constituted a negligent misrepresentation on which it reasonably relied in deciding to buy the property. The superior court granted summary judgment against Centennial based on A.R.S. § 20-1562, reasoning the statute bars an insured from relying on information contained in a report of exceptions attached to a title insurance policy. *See* A.R.S. § 20-1562(5).

¶6 Before a title insurer issues a policy, it reviews public records for defects, then issues a title commitment that lists exceptions to coverage. *Action Acquisitions*, 218 Ariz. at 398, ¶ 11, 187 P.3d at 1111. The insurance policy to which the list of exceptions is attached is not a promise that no other exceptions or encumbrances exist. Rather, the policy is a contract under which the insurer agrees to indemnify the insured for losses caused by claims arising from encumbrances not identified in the insurer's commitment. *See Swanson v. Safeco Title Ins. Co.*, 186 Ariz. 637, 641, 925 P.2d 1354, 1358 (App. 1995) ("Title insurance does not guarantee perfect title;

instead, it pays damages, if any, caused by any defects to title that the title company should have discovered but did not."); *see also Action Acquisitions*, 218 Ariz. at 398, ¶ 11, 187 P.3d at 1107; *Siegel v. Fidelity Nat'l Title Ins. Co.*, 54 Cal. Rptr. 2d 84, ___ (App. 1996) ("[T]he function of title insurance is to protect against the possibility that liens and other items not found in the search or disclosed in the preliminary report exist.").

¶7 Before A.R.S. § 20-1562 was amended in 1992, an insurer could be liable in Arizona for issuing a title commitment that negligently failed to disclose an encumbrance of record. *See Moore v. Title Ins. Co. of Minn.*, 148 Ariz. 408, 412, 714 P.2d 1303, 1307 (App. 1985). Jurisdictions were divided on this issue, and Arizona was among several that equated a title insurer's duty with that owed by an abstractor, which may be liable for negligence if it fails to include liens of record in the abstract. *Id.* at 411, 714 P.2d at 1306; *see also U.S. Bank, N.A. v. Integrity Land Title Corp.*, 929 N.E.2d 742, 746-47 (Ind. 2010) (collecting cases).

¶8 But a 1992 amendment to A.R.S. § 20-1562 changed that rule by effectively barring a common-law claim against an insurer whose title commitment fails to identify a cloud on title. *See generally State v. Rios*, 225 Ariz. 292, 298, ¶ 21, 237 P.3d 1052, 1058 (App. 2010) (when a statute conflicts with common law, the statute prevails). The amendment added definitions for three new terms, "Abstract of title," "Preliminary report" and "Title insurance policy." 1992 Ariz. Sess. Laws, ch. 203, § 8 (2d Reg. Sess.). As amended, the statute draws a clear distinction between an abstract and a title commitment:

> 1. "Abstract of title" means a written representation . . . that is *intended to be relied on* by the person who has contracted for the receipt of the representation. The abstract of title shall include all recorded conveyances, instruments or documents that impart constructive notice with respect to the chain of title to the real property described in the abstract. An abstract of title is not a title insurance policy.
>
> * * *
>
> 5. "Preliminary report", "commitment" or "binder" means a report that is furnished in connection with an application for title insurance and that offers to issue a title insurance policy subject to the stated exceptions set forth in the report . . . . *The reports are not abstracts of title and the rights, duties and responsibilities relating to the preparation and issuance of an abstract of title do not apply to the issuance of a report. The report is not a representation as to the condition of title to real property* but does constitute a statement of the terms and conditions on which the issuer is willing to issue its title insurance policy if the offer is accepted.

A.R.S. § 20-1562(1), (5) (emphasis added).

¶9 Under the plain language of the amended statute, the title commitment that Lawyer's Title issued in connection with its policy was not a representation of the condition of the title to the property. Nor did the insurer's issuance of the commitment subject it to "the rights, duties and responsibilities relating to the preparation and issuance of an abstract of title." A.R.S. § 20-1562(5). Because the commitment was "not a representation as to the condition of title" to the property, it cannot form the basis of a claim by Centennial for negligent misrepresentation.

¶10 Centennial argues § 20-1562 does not protect a title insurer from liability pursuant to Restatement (Second) of Torts § 552 (1977) for failing to exercise reasonable care in supplying information in the course of its business. But we do not follow the Restatement when it conflicts with an Arizona statute. *See Ocotillo W. Joint Venture v. Schwartz*, 173 Ariz. 486, 489, 844 P.2d 653, 656 (App. 1992). Our statute controls here: As a matter of law, no rights, duties or responsibilities arose with Lawyer's Title's issuance of the commitment, and the commitment was not a "representation as to the condition of title" on which Centennial could rely. A.R.S. § 20-1562(5).[2]

[2] California courts similarly hold that the California legislature's enactment in 1981 of nearly identical provisions precludes a tort action against an insurer based on information

Thus, the superior court correctly entered summary judgment for Lawyer's Title on Centennial's negligence claim.

C. The Contract Claim.

¶11 The policy insures Centennial "against loss or damage . . . sustained or incurred . . . by reason of . . . [a]ny defect in or lien or encumbrance on the title." That grant of coverage, however, is subject to the following condition:

> 2. CONTINUATION OF INSURANCE AFTER CONVEYANCE OF TITLE.
>
> The coverage of this policy shall continue in force as of Date of Policy in favor of an insured only so long as the insured retains an estate or interest in the land, . . . or only so long as the insured shall have liability by reason of covenants of warranty made by the insured in any transfer or conveyance of the estate or interest.

In entering summary judgment against Centennial on its contract claim, the superior court concluded that under this provision, Lawyer's Title owed no obligation to Centennial with respect to the 74 acres Centennial had reconveyed to the prior owner. And because the single acre Centennial retained was not affected by the undisclosed easement, the court held Lawyer's Title owed no

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in a title commitment. *See* Cal. Insurance Code §§ 12340.10, 12340.11 (West 2013); *Siegel v. Fidelity Nat'l Title Ins. Co.*, 54 Cal. Rptr. 2d 84, ___ (App. 1996); *Southland Title Corp. v. Superior Court*, 282 Cal. Rptr. 425, 429-30 (App. 1991). *See also Barstad v. Stewart Title Guar. Co., Inc.*, 39 P.3d 984, 991 (Wash. 2002) ("majority of state courts in Ninth Circuit . . . have held that title insurance companies have no general disclosure duty in preliminary commitments").

duty to cover the loss Centennial alleged it incurred when it discovered the easement.

¶12 The policy condition recited above plainly provides that coverage continues only so long as the insured owns the affected property. Put differently, once the insured's interest in the land terminates, coverage under the policy terminates as to that interest. *See Chicago Title Ins. Co. v. 100 Inv. Ltd. P'ship*, 355 F.3d 759, 763 (4th Cir. 2004) (under quoted provision, policy is effective during "the period running from the effective date of the policy until the insured conveys away its interest in the land"). After Centennial conveyed 74 of the 75 acres back to the prior owner, the policy no longer "continue[d] in force" as to the 74 acres, given that the conveyance was made subject to all easements of record. *See Point of Rocks Ranch, L.L.C. v. Sun Valley Title Ins. Co.*, 146 P.3d 677, 679 (Idaho 2006) ("Because the deed excluded easements from the covenants of warranty, the [insured] . . . did not have any liability for the breach of such covenants due to the existence of the easement.").

¶13 Centennial's damage theory, however, is that it paid too much for the property because it was unaware of the easement, and ultimately had to give back the property because it is not worth the purchase price. Thus, Centennial alleges it incurred damages while it owned the property, within the "continuation of coverage" condition of the policy. *See Swanson*, 186 Ariz. at 641-42, 925 P.2d at 1358-59 (damages valued as of the date title defect is discovered).

¶14 We are not persuaded by Lawyer's Title's argument that, as a matter of law, Centennial's reconveyance of the affected property bars its claim for damages. Lawyer's Title cites no policy language that requires the insured own the affected property at the time it makes a claim. While the policy makes plain that *coverage* continues only so long as the insured owns the property, it contains no similar restriction on when an insured may file a claim. *See* Burke*, Law of Title Insurance* § 5.02 (3d. ed. Supp. 2012) (a "post-coverage claim" may be made on a title insurance policy "so long as the damages were sustained during coverage.").

¶15 Each side argues *Chicago Title* resolves the issue in its favor. The insured in that case owned 300 acres, including a one-acre parcel called the Miller tract. *Chicago Title*, 355 F.3d at 761. After the insured sold the Miller tract by special warranty deed, it discovered a competing conveyance by which a third party claimed to have owned the tract. *Id.* at 761-62. Seeking to clear title for the benefit of the party to which it had sold the Miller tract, the insured bought back the tract from the other purported owner. The third-party owner then sued the insured, alleging trespass during the prior period the insured had purported to own the tract. *Id.* The insured made a claim on its title insurance policy, demanding the insurer both indemnify it for the cost of repurchasing the tract and defend it in the trespass litigation. *Id.*

¶16 Applying Maryland law, the Fourth Circuit Court of Appeals examined a "continuation of insurance" provision similar to the one at issue here. The court explained:

> A natural reading of this policy language evinces the intent of the parties to limit the scope of title protection to the period running from the effective date of the policy until the insured conveys away its interest in the land, unless, in the conveyance, the insured gives warranties to the grantee. If the insured does give a warranty to the grantee, coverage extends to protect the insured's obligation under that warranty. But if it does not, then title insurance for that land ends, and any risk of loss for defective title becomes the problem of the new owner.
>
> The allocation of risk by this agreement gives title insurance coverage to the insured during the period when the insured purportedly owns the property, when most of the adverse consequences due to a defective title would occur. If a preexisting defect in title were to remain after the insured conveyed the land, the risk inherent in that defect would pass to the purchaser and the insured would no longer have risk, nor coverage. Of course, if the insured were to warrant the property against title defects, then the insured would be retaining the risk of a defective title, and coverage would continue for that risk. Thus, if the conveyance were accomplished by a deed containing a special warranty, the insured would be conveying no more than what it

> received from its grantor, and coverage would end with the conveyance.

Id. at 763-64.

¶17 Applying those principles, the court held there was no coverage for the cost the insured incurred in trying to clear title to the Miller tract because under the special warranty deed by which the insured had conveyed the tract, upon the sale, the title defect became the new owner's problem. *Id.* at 74. But the court came to a different conclusion about the insured's demand that the insurer defend it in the trespass action. The court held the insurer was obligated to defend because the alleged trespass occurred during the time the insured owned the Miller tract. *Id.* at 765. It did not matter that the insured no longer owned the property by the time the insured made the claim for coverage; the relevant date was the date of the claimed injury. *Id.* at 765-66.

¶18 The same is true here. As relevant, the policy generally only covers loss or damage incurred during the period of ownership, but it does not require the insured to make such a claim before it sells the affected property. *Id.* at 766 ("The policy, rather than providing insurance for any 'claim' asserted during the policy period, provides that it covers any 'loss or damage during the policy period.'"). Moreover, contrary to Lawyer's Title's argument, it is irrelevant that Centennial's demand for coverage was not triggered by a third-party trespass or other title claim. The policy insures "against loss or damage" caused by an "encumbrance on the title." It does not require that Centennial be sued or subjected to a threat of suit.

¶19 Cases interpreting similar "continuation of insurance" provisions make clear the distinction between the two holdings by the *Chicago Title* court. Unless the insured remains subject to liability under a warranty deed, coverage does not continue in force for damages incurred from defects discovered after the insured conveys the property. *See Chicago Title*, 355 F.3d at 764-65; *Point of Rock Ranch,* 146 P.3d at 680 ("the [insureds] are not entitled to recover under the policy for the easement discovered *after* they had conveyed the real property"); *Gebhardt Family Inv., L.L.C. v. Nations Title Ins. of New York, Inc.*, 752 A.2d 1222, 1227 (Md. Spec. App. 2000) (any loss would be suffered by the new owner because the property was conveyed by special warranty deed).

¶20 Here, however, the loss Centennial alleges was sustained when it discovered the defect in title, at a time when it owned all 75 acres. Because Centennial owned the property at the time it allegedly incurred the loss, its damage claim is not barred by the "continuation in force" provision of the policy. *See generally Sandler v. New Jersey Realty Title Ins. Co.*, 178

A.2d 1, 6 (N.J. 1962) ("Where the insured had an insurable interest at the time of making the contract, a change of title to the property insured does not automatically void the policy, if at the time of loss the insured has such an insurable interest. Such a result is attained only by a policy provision to that effect.").

¶21 The cases Lawyer's Title cites are inapposite. In *Gebhardt*, the insureds sold the property, then sued the insurer for failing to resolve a cloud on title discovered prior to the sale. 752 A.2d at 1223. Although the insureds argued they suffered the loss before they conveyed the property, they conceded on appeal that they had not yet suffered any monetary damages. *Id.* at 1227. Likewise, in *Willow Ridge Ltd. Partnership v. Stewart Title Guaranty Co.*, 706 F. Supp. 477 (S.D. Miss. 1988), the trial court rejected the property owner's contention that the insurer was liable for damage incurred when the property was foreclosed upon; the court held that contrary to the owner's argument, the foreclosure was caused by the insured's failure to service the debt, not by any cloud on title. *Id.* at 484-85. And in *Point of Rocks Ranch,* the insureds' claim was based on a cloud on title they did not discover until after they had sold the property. 146 P.3d at 678, 680. By contrast to this case, the insureds there did not contend they suffered any damages while the policy continued in force.[3]

¶22 We hold that under the "continuation of insurance" provision of the policy, Centennial's sale of the affected property does not bar its claim for damages it alleges it incurred prior to the sale. The parties' summary judgment briefing did not address Centennial's ability to prove the damages it alleges or its obligation to mitigate those damages; nor did the briefing address any other policy defenses Lawyer's Title might raise (including the timeliness of Centennial's claim) to coverage. We do not express any view on any of these issues, which the parties may raise on remand.

CONCLUSION

¶23 For the foregoing reasons, we affirm summary judgment in Lawyer's Title's favor as to the negligence claim, but reverse and remand for further proceedings the judgment in favor of Lawyer's Title on Centennial's claim for breach of contract. We also reverse the superior court's order awarding Lawyer's

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[3] Lawyer's Title also cites *Resolution Trust Corp. v. American Title Insurance Company*, 901 F. Supp. 1122 (M.D. La. 1995), in which the court granted summary judgment to a title insurer on a claim brought by a former note holder. The note holder had argued that a cloud on title prevented it from being able to foreclose. Although the court held the plaintiff's claim was barred because it was no longer an insured under the policy, the court did not address whether a claim could be made for damages allegedly suffered while the policy continued in force.

Title attorney's fees and costs pursuant to A.R.S. § 12-341.01 (West 2013). We decline to grant attorney's fees or costs to either party on appeal. *See Chapman v. The Westerner*, 220 Ariz. 52, 55, ¶ 15, 202 P.3d 517, 521 (App. 2008). The superior court, however, may consider the fees incurred in this appeal in determining whether and how much to award the prevailing party at the close of the case. *See Lennar Corp. v. Transamerica Ins. Co.*, 227 Ariz. 238, 247, ¶ 32, 256 P.3d 635, 644 (App. 2011).

_______________/S/________________
DIANE M. JOHNSEN, Chief Judge

CONCURRING:

_______________/S/___________________________
MARGARET H. DOWNIE, Acting Presiding Judge

_______________/S/________________
JOHN C. GEMMILL, Judge

THIRD DIVISION
August 30, 2013

No. 1-12-3510

CHICAGO TITLE INSURANCE COMPANY, as Subrogee of WATERSIDE PARTNERS, LLC,	)	Appeal from the Circuit Court of Cook County
Plaintiff-Appellant,	)	
v.	)	No. 12 L 4228
AURORA LOAN SERVICES, LLC,	)	Honorable John C. Griffin,
Defendant-Appellee.	)	Judge Presiding.

JUSTICE PIERCE delivered the judgment of the court, with opinion.
Presiding Justice Neville and Justice Hyman concurred in the judgment and opinion.

OPINION

¶ 1 Plaintiff, Chicago Title Insurance Company, appealed the circuit court's order granting defendant's motion to dismiss the complaint with prejudice pursuant to section 2-619 of the Code of Civil Procedure (Code). 735 ILCS 5/2-619 (West 2010). For the reasons that follow, we affirm the circuit court's order.

¶ 2 BACKGROUND

¶ 3 Plaintiff filed a one-count verified complaint on April 20, 2010, for breach of special warranty deed. According to plaintiff's complaint, Aurora Loan Services, LLC (Aurora), conveyed the subject property located at 201 N. Westshore Drive, Unit 2603, in Chicago, Illinois, to Waterside Partners, LLC (Waterside), by special warranty deed on February 23, 2010. The special warranty deed was recorded on March 11, 2010. Chicago Title Insurance Company (Chicago Title) issued an owner's policy of title insurance for the subject property on March 11, 2010. Plaintiff alleged that Aurora breached its special warranty that it did not do anything or suffer anything to be done to encumber the property when Aurora: (1) failed to redeem a tax sale that was held prior to Aurora's ownership of the subject property; and (2) did not notify Waterside of a pending tax deed proceeding that ultimately divested Waterside of its interest in the property.

¶ 4 The following facts are agreed to by the parties. Pursuant to a judicial sale resulting from a foreclosure action, Aurora Loan Services obtained title to the property from Intercounty Judicial Sales Corporation on September 9, 2008. Prior to Aurora receiving the deed, however, delinquent special assessment taxes were purchased by the Salta Group, Inc. (Salta), on June 22, 2007. Salta recorded a *lis pendens* notice against the property. On February 22, 2010, Salta filed a petition for a tax deed under the June 22, 2007 tax sale. On February 23, 2010, Aurora conveyed the property to Waterside by special warranty deed. The tax sale was redeemable until June 21, 2010. Aurora did not redeem the 2007 tax sale although it did pay the special assessment taxes in 2009 and 2010. Aurora did not notify Waterside of the 2007 tax sale.

¶ 5 On March 2, 2010, Salta served Aurora with notice of a petition for issuance of a tax deed. Aurora did not notify Waterside of the petition for a tax deed. On October 29, 2010, a tax deed issued and Salta obtained title to the property. The tax deed was recorded on November 17, 2010. Waterside was then divested of its interest in the property. On December 6, 2010, Chicago

Title paid its insured, Waterside, the policy limit and appraised value of the property, $290,000. Chicago Title, as Waterside's subrogee, thereafter filed this lawsuit.

¶ 6 The special warranty deed executed by Aurora provided that Aurora "does covenant, promise and agree, to and with [Waterside], their heirs and assigns, that it has not done or suffered to be done anything whereby the said premises hereby granted are, or may be, in any manner encumbered or charged." Plaintiff alleged that the title insurance policy was issued without an exception for the 2007 tax sale and Waterside suffered a full title loss because of the issuance of the tax deed to Salta. Plaintiff alleged that defendant breached its special warranty in that it allowed the encumbrance of the *lis pendens* notice to remain on the property on the day the special warranty deed was delivered and recorded.

¶ 7 Defendant moved to dismiss the complaint pursuant to sections 2-603 and 2-619 of the Code. 735 ILCS 5/2-603, 2-619 (West 2010). Defendant argued that the complaint should be dismissed pursuant to section 2-619 of the Code because it cannot be held liable for Waterside's loss under the terms of the special warranty deed. Specifically, defendant argued that the plain language of the special warranty was limited to actions done or suffered to be done by Aurora which created an encumbrance. Defendant argued that the encumbrance predated Aurora's ownership of the property and, therefore, was not within the scope of the special warranty made to Waterside. Aurora argues that the property was sold for unpaid taxes on June 22, 2007 and it did not obtain title to the property until September 9, 2008. Thus, the prior owner of the property, and not Aurora, caused the tax sale to occur on June 22, 2007. Therefore, defendant argued, under the terms of the special warranty deed, Aurora did not "do or suffer to be done" anything to cause the tax sale encumbrance and it cannot be held liable for an encumbrance caused by the prior owner.

¶ 8 Plaintiff argued in response that under the special warranty deed, defendant had (1) a duty to notify Waterside of the existence of the tax sale; and (2) defendant breached the covenant against encumbrances by (a) failing to redeem the property from the tax sale; and (b) failing to notify Waterside of the petition for a tax deed. Plaintiff argued that defendant's inaction encumbered the property by creating a defect in title.

¶ 9 On October 25, 2012 after full briefing and a hearing on the motion, the circuit court granted the section 2-619 motion to dismiss with prejudice. The circuit court found that because the delinquent special assessment tax encumbrance predated Aurora's ownership of the property, the encumbrance did not occur while Aurora held title and Aurora did not cause the encumbrance, therefore, Aurora did not breach the special warranty deed. The circuit court also found that Aurora did not breach the special warranty deed for failing to notify Waterside of the existence of the tax deed petition.

¶ 10 ANALYSIS

¶ 11 Plaintiff argues that the circuit court erred in granting defendant's motion and dismissing the complaint with prejudice pursuant to section 2-619 of the Code. A section 2-619 motion for involuntary dismissal admits the legal sufficiency of the complaint, but raises defects, defenses, or other affirmative matter which avoids the legal effect or defeats a plaintiff's claim. 735 ILCS 5/2-619(a)(9) (West 2010); *Mauvais-Jarvis v. Wong*, 2013 IL App (1st) 120070, ¶ 64. The purpose of a section 2-619 motion to dismiss is to "provide litigants with a method of disposing of issues of law and easily proved issues of fact —relating to the affirmative matter— early in the litigation." (Emphasis omitted.) *Reynolds v. Jimmy John's Enterprises LLC*, 2013 IL App (4th) 120139, ¶ 30. Affirmative matter is "something in the nature of a defense that negates the cause of action completely or refutes crucial conclusions of law or conclusions of material fact contained in or inferred from the complaint." *In re Estate of Schlenker*, 209 Ill. 2d 456, 461 (2004); *Illinois Graphics Co. v. Nickum*, 159 Ill. 2d, 469, 486 (1994). When a defendant has initially satisfied the burden of presenting an affirmative matter, the burden then shifts to plaintiff "to establish that the defense is unfounded or requires the resolution of an essential element of material fact before it is proven." (Internal quotation marks omitted.) *Schroeder v. RGIS, Inc.*, 2013 IL App (1st) 122483, ¶ 24 (quoting *Reilly v. Wyeth*, 377 Ill. App. 3d 20, 36 (2007)).

¶ 12 In reviewing a section 2-619 motion, the court accepts as true all well-pleaded facts and all reasonable inferences that may be drawn from those facts, construing them in the light most favorable to the nonmovant. *Porter v. Decatur Memorial Hospital*, 227 Ill. 2d 343, 352 (2008); *Sandholm v. Kuecker*, 2012 IL 111443, ¶ 55. Our review of a section 2-619 dismissal of a complaint is *de novo*. *Mauvais-Jarvis*, 2013 IL App (1st) 120070, ¶ 64.

¶ 13 The gist of plaintiff's breach of special warranty theory is that, although defendant did not cause the encumbrance, defendant failed to remove the encumbrance when warranting that it did not do anything or suffer anything to be done to encumber the property. Plaintiff argues that defendant breached the special warranty in one or all of three ways: (1) it conveyed title subject only to taxes "not yet due or payable" even though there had been a prior sale for delinquent taxes; (2) it conveyed title even though there had been a prior sale for delinquent taxes with a *lis* *pendens* recorded against the property; and (3) after it was served with notice of the tax deed proceeding, Aurora (a) failed to redeem the property or (b) notify Waterside of Salta's tax deed petition. Plaintiff argues that the circuit court erred in finding that the encumbrance was caused by acts of the owner before Aurora, therefore, Aurora did not breach the special warranty deed, negating plaintiff's claim. We affirm, and find the circuit court did not err in dismissing plaintiff's complaint with prejudice.

¶ 14 The primary goal in construing a deed is to ascertain the intent of the parties. *Diaz v. Home Federal Savings & Loan Ass'n of Elgin*, 337 Ill. App. 3d 722, 727 (2002). "[I]f language contained in an instrument has a well known meaning and significance in law, it will be presumed such meaning was in the minds of the parties using it, unless a contrary intent is made manifest by other language in the deed." *Tallman v. Eastern Illinois & Peoria R.R. Co.*, 379 Ill. 441, 444 (1942).

¶ 15 "A warranty deed is a stipulation by the grantor in which he guarantees to the grantee that title to the property at issue will be good and that the grantor's possession is undisturbed." *Midfirst Bank v. Abney*, 365 Ill. App. 3d 636, 644 (2006). A special warranty deed is "[a] deed in which the grantor covenants to defend the title against only those claims and demands of the grantor and those claiming by and under the grantor." Black's Law Dictionary 477 (9th ed. 2009). A special warranty is a limited form of warranty and recovery is only available if the defect in title occurs because of an act of the grantor. 20 Am. Jur. 2d *Covenants, Conditions, & Restrictions* § 62 (2005). This limited warranty "does not render the grantor liable for defects in the title based on events that transpired when the property was in the hands of a prior titleholder."

Id. Professor Richard A. Powell notes:

> "If the grantor covenants to warrant and defend title to the property against all claims whatsoever, regardless of their source, the covenant is a general warranty. However, if the grantor covenants to warrant and defend the title only against claims arising by, through or under the grantor, it is a special warranty. Under a special warranty, if the claim arose under, or due to the actions of, a prior owner of the land, the covenantor has no liability. However, under a general warranty, if a claim is validly asserted against the property, regardless of who is responsible for its existence, the covenantor is liable." 14 Richard R. Powell, Powell on Real Property § 81A.06(2)(d)(iii), at 81A-122-23 (Michael Allan Wolf ed., 2000).

¶ 16 In considering this appeal, we found no Illinois case law that provides insight into the nature of a special warranty deed. Jurisdictions that frequently employ special warranty deeds inform our analysis of the issues. Courts have found that the grantor of a special warranty deed, unlike a general warranty deed, "does not warrant against defects in the title that existed before grantor was deeded the property." (Internal quotation marks omitted.) *Morello v. Land Reutilization Comm'n*, 659 N.W.2d 310, 314 (Neb. 2003). The Florida district court discussed the use of special warranty deeds observing:

> "Special warranty deeds are used when the grantor is unwilling to warrant against possible defects arising before he acquired title. Frequently, tax title holders, particularly those claiming through an administrative tax deed, who have not prosecuted a quiet title action against the former owners, convey by special warranty deed. A special warranty

> deed is, of course, effective to convey all the title and estate of the grantor. The covenants as such have no operative effect; they simply define the scope of the liability of the grantor for breach of covenant if less than an indefeasible title is passed." (Internal quotation marks omitted.) *Harris v. Sklarew*, 166 So. 2d 164, 166 (Fla. 3d Dist. Ct. App. 1964).

¶ 17 A special warranty against title or encumbrances "is breached only if the grantor's own conduct creates an encumbrance on the title." *ASK Realty II Corp. v. First American Title Insurance Co.*, 2004 WL 1254005, at *18 (D. Md. June 7, 2004). The nature of a special warranty deed does not require a grantor to extinguish all encumbrances on a property in existence at the time the property is conveyed through a special warranty deed. *Woolf v. 1417 Spruce Associates, L.P.*, 68 F. Supp. 2d 569, 572 (E.D. Pa. 1999). This would render the distinction between a general warranty and a special warranty meaningless. *Id.* The superior court of Delaware observed:

> "A covenant of special warranty is one the operation of which is limited or restricted to certain persons or claims. As a general rule, where a vendee receives a special warranty or quitclaim conveyance, he takes the estate subject to all the disadvantages that it was liable to in the hands of the vendor, and the law will presume notice of all encumbrances, either legal or equitable. The fact that a vendor refuses to make a full and complete assurance of title is said to be sufficient to excite suspicion and put the party upon inquiry." *Indian Harbor, Inc. v. Sea & Pines, Inc.*, 1987 WL 12424, at *3 (Del. Super. Ct. June 10, 1987).

¶ 18 In view of the foregoing, we find the special warranty made by Aurora defined the scope of its liability and placed Waterside on notice that it warranted only against title defects that were caused or created by its own conduct and that it was not responsible for defects arising before it acquired title and it was not required to extinguish all encumbrances on the property at the time of conveyance through the use of a special warranty deed.

¶ 19 The special warranty deed at issue provides that Aurora "does covenant, promise and agree, to and with [Waterside], their heirs and assigns, that it has not done or suffered to be done anything whereby the said premises hereby granted are, or may be, in any manner encumbered or charged."

¶ 20 An encumbrance is "any right to, or interest in, land which may subsist in a third party to the diminution of the value of the estate, but consistent with the passing of the fee by conveyance." (Internal quotation marks omitted.) *Inland Real Estate Corp. v. Oak Park Trust & Savings Bank*, 127 Ill. App. 3d 535, 541 (1983). In *Rhone v. First American Title Insurance Co.*, 401 Ill. App. 3d 802, 808 (2010), we discussed various aspects of encumbrances and noted:

> "It [an encumbrance] may include any right to, or interest in, land which may subsist in a third party to the diminution of the value of the estate, but consistent with the passing of the fee by conveyance. [citations.] Encumbrances include not merely liens such as mortgages, judgment liens, [or] taxes *** but also attachments, leases, inchoate dower rights, water rights, easements, restrictions on use, or any right in a third party which diminishes the value or limits the use of the land granted." (Internal quotation marks omitted.)

¶ 21 In construing the word "suffer," we find particularly instructive a treatise addressing its use in a special warranty deed where unpaid property taxes are at issue:

> " 'Suffered' in this context doesn't mean 'tolerated.' It means 'caused to be placed.' Consider the case of a property owner not paying property taxes. Eventually, the state will assert a lien against the property for unpaid taxes. It would be incorrect to say that the grantor 'created' the lien; the state did. But the grantor 'suffered' it to be created by failing to pay. If, however, the present owner paid the taxes but the predecessor didn't, and that is why the lien arose, the owner has no implied obligation to cure it, or any other flaw in title the owner didn't create." 11 George Lefcoe, Thompson on Real Property § 94.07 (1994).

¶ 22 Under the plain meaning of the special warranty deed at issue, Aurora warranted that it did not do anything to cause the property to be encumbered. The scope of Aurora's special warranty includes only encumbrances Aurora caused and does not include any preexisting encumbrances which remained against the property through the time of the conveyance to Waterside.

¶ 23 Here, plaintiff argues that, at the time of the conveyance to Waterside, the earlier tax sale encumbered the property and defendant, which chose the language of the special warranty deed, did not except the tax sale from the special warranty. Rather, defendant only excluded from the special warranty "taxes due and owing" and, therefore, defendant is liable for the 2007 tax sale encumbrance. We find this argument unpersuasive.

¶ 24 It is clear from the record that Aurora did not do anything to cause the encumbrance: the tax sale. The tax sale was caused because a prior owner did not pay the special assessment tax. Contrary to plaintiff's assertion, the *lis pendens* notice is not an encumbrance: it is a recorded notice that there exists a proceeding that may affect good title to the property and, if conveyed, the grantee may be adversely affected by that proceeding. *Knodle v. Jeffrey*, 189 Ill. App. 3d 877, 888 (1989). Nothing in the record suggests Aurora knew about the tax sale before it conveyed the property to Waterside. Even assuming Aurora knew of this tax delinquency and knew the non-payment would result in a tax sale, the special warranty limited Aurora's exposure to only those encumbrances Aurora created or that existed because of something Aurora did. A tax sale occurs only because there are unpaid taxes. Thus, the tax lien, not the tax sale, is the encumbrance. Aurora did not permit or allow the tax sale to occur. Aurora did not receive title to the property until 2008. The 2007 tax sale occurred prior to Aurora's ownership and, therefore, was not warranted against by Aurora in the special warranty deed.

¶ 25 Plaintiff argues that Aurora's failure to redeem the tax sale after it received notice of Salta's petition for a tax deed, and/or its failure to notify Waterside of the Salta's petition constituted a breach of the special warranty deed. First, we note that plaintiff failed to provide this court with relevant legal authority to support its contention that defendant had a duty to either redeem the property or inform plaintiff of the petition for the tax deed as required by Illinois Supreme Court Rule 341(h)(7) (eff. July 1, 2008). The failure to cite relevant authority to support a legal argument can result in its waiver. *Midfirst Bank*, 365 Ill. App. 3d at 650. Illinois Supreme Court Rule 341 is not a limitation on the court's jurisdiction, however, and we may consider the issue in the interest of finding a just result. *Kic v. Bianucci*, 2011 IL App (1st) 100622, ¶ 23. Acknowledging that there is a lack of precedent on the issue presented by plaintiff, we will address plaintiff's argument.

¶ 26 The circuit court rejected this argument, finding: (1) defendant did not breach the special warranty deed because at the time the warranty was made, defendant did not receive notice of the tax deed petition; (2) plaintiff failed to explain why the title examination did not discover the tax sale when performing its due diligence; and (3) case law from other jurisdictions has held that the conveyance of a property through a special warranty deed "puts the grantee on constructive notice of certain defects that may cloud title."

¶ 27 We affirm the circuit court's finding that plaintiff's allegation of breach arising from any action or inaction by Aurora after the conveyance is negated as a matter of law.

¶ 28 A covenant that land is free from encumbrances is a personal covenant not running with the land. *Firebaugh v. Wittenberg*, 309 Ill. 536, 543 (1923). A covenant against encumbrances is breached at the moment it is made, when the deed is delivered. *Id.*; *Inland Real Estate Corp. v. Oak Park Trust & Savings Bank*, 127 Ill. App. 3d 535, 541 (1983). Therefore, any claim for breach of Aurora's warranty under its terms, must have existed at the time of the delivery of the deed. *Firebaugh v. Wittenberg*, 309 Ill. 536, 543 (1923). Plaintiff's argument for breach premised on any action or inaction after the conveyance cannot serve as a basis of breach of the special warranty deed. Aurora's covenant against encumbrances was made when the deed was delivered and the basis of any alleged breach of this warranty can only be supported by events occurring when it was warranted, not later in time. See *Firebaugh v. Wittenberg*, 309 Ill. 536, 543 (1923).

Therefore, plaintiff's allegation that Aurora's failure to redeem or notify, its grantee after the delivery of the deed cannot constitute a breach of the special warranty as a matter of law and negates plaintiff's claim.

¶ 29 Furthermore, the recordation of the *lis pendens* by Salta served as notice to any future purchasers that a deed received after its recording might be affected by the tax sale. *Knodle v. Jeffrey*, 189 Ill. App. 3d 877, 888 (1989). Therefore, the recorded certificate of sale, issued on June 22, 2007, before Aurora purchased the property, put subsequent purchasers, including Waterside, on notice of Salta's interest in the property. *Id*. Plaintiff has failed to provide us with substantive argument and citation to relevant legal authorities to support its contention that defendant had a duty after the conveyance to take any action regarding the tax sale or petition for the tax deed.

¶ 30 In addition, section 21-345 of the Illinois Property Tax Code (Tax Code) governs the right to redeem a property from a tax sale (*In re Application of the County Treasurer & ex officio County Collector*, 394 Ill. App. 3d 111, 119 (2009)) and provides that the right to redeem a property from a tax sale exists "in any owner or person interested in that property." 35 ILCS 200/21-345 (West 2006). A stranger to the property, with no interest in the property, has no right to redeem when the property is sold for delinquent taxes. *In re Application of Du Page County Collector*, 98 Ill. App. 3d 950, 952 (1981).

¶ 31 On February 23, 2010, Aurora conveyed its interest in the subject property to Waterside. Pursuant to section 21-345 of the Tax Code, after the February 23 conveyance only Waterside, and not Aurora, could redeem the property from the tax sale. Because Aurora could not legally redeem the property after the conveyance to Waterside, plaintiff's claim that Aurora breached the special warranty deed in failing to redeem the tax sale after the conveyance to Waterside fails. Therefore, on this basis we find the circuit court property dismissed with prejudice the complaint pursuant to section 2-619(a)(9).

¶ 32 Lastly, plaintiff argues that pursuant to the terms of the deed, defendant excepted from the special warranty deed, only the "taxes not yet due and payable" and, by implication, the unpaid taxes which resulted in the 2007 tax sale were covered by the special warranty. Defendant responds arguing that plaintiff failed to raise this argument in the circuit court and, therefore, it is waived for the purposes of appeal. Plaintiff asserts the argument was raised in its response to the motion to dismiss. The response in pertinent part states:

> "The [d]efendant had a duty to redeem prior to conveying title to the Waterside. Defendant did nothing to cause this encumbrance but if [*sic*] failed to remove the encumbrance. It warranted that there was no such encumbrance when it stated that the [*sic*] by the language in the conveyance and that it was subject only to taxes not yet due and payable."

Plaintiff in its response to the motion to dismiss did not argue that the unpaid taxes which caused the tax sale were within the "taxes not yet due and payable" exception. Rather, plaintiff's argument below was that defendant had warranted there was no prior encumbrance that was excepted from the conveyance. This a different argument than presented by plaintiff on appeal. Therefore, plaintiff's argument that the exception to the conveyance clause for taxes not yet due and payable is waived because it was not asserted in the circuit court and was made for the first time on appeal. *Johnson Press of American, Inc. v. Northern Insurance Co. of New York*, 339 Ill. App. 3d 864, 874 (2003). In addition, we note that plaintiff failed to provide us with relevant legal authority to support its argument, which is made in a conclusory fashion. " 'The appellate court is not a depository in which the appellant may dump the burden of argument and research.' " *In re Marriage of Petrik*, 2012 IL App (2d) 110495, ¶ 38 (quoting *Kic v. Bianucci*, 2011 IL App (1st) 100622, ¶ 23).

¶ 33 In any event, the argument is legally and logically untenable. First, the purpose of selling delinquent taxes is to obtain the tax due through the sale and distribute the sale proceeds to the relevant taxing bodies. When sold, the statutory tax lien shifts from the county to the tax purchaser. 35 ILCS 200/21-240 (West 2006). Effectively, the taxes have been paid, therefore, no taxes are due and owing for that tax period and an encumbrance in favor of the tax buyer remains until redeemed or until a tax deed issues. Second, property taxes are a prior and first lien against the property from January 1 in the year in which they are levied and the lien remains until the taxes are paid or sold. 35 ILCS 200/21-75 (West 2006). In Illinois, current year real estate taxes are billed and payable in the following year. By custom and practice, unless the parties agree otherwise, the land purchaser typically receives a credit at closing for unpaid prior years taxes and the pro-rata share of current year estimated taxes through the date to closing. The exception for "taxes not yet due and payable" clearly applies to taxes levied during 2010 but not yet payable at the time of the conveyance from defendant to Waterside. The special assessment taxes that were sold at the 2007 tax sale took place because they were previously levied, due, payable and delinquent long before defendant conveyed the property to Waterside on February 23, 2010, and, therefore, were not within the special warranty deed exception.

¶ 34 CONCLUSION

¶ 35 For the foregoing reasons we affirm the circuit court's dismissal of plaintiff's complaint with prejudice.

¶ 36 Affirmed.

METROPOLITAN NATIONAL BANK, A NATIONAL BANK, Plaintiff-Respondent,

v.

ROBIN JEMAL; DAVID S. W. VAUGHN; ISRAEL DISCOUNT BANK OF NEW YORK, IDB FACTORS DIVISION; Defendants-Respondents, and BNY MELLON, N.A. Defendant-Appellant.

No. A-0003-12T4.

Superior Court of New Jersey, Appellate Division.

Argued September 10, 2013.
Decided September 23, 2013.

Corrine LaCroix Tighe argued the cause for appellant (Finestein & Malloy L.L.C., attorneys; Ms. LaCroix Tighe and Russell M. Finestein, on the brief).

William C. Sandelands argued the cause for respondent (Sandelands Eyet, LLP, attorneys; Mr. Sandelands, of counsel and on the brief; Maria A. Kershaw, on the brief).

Respondent, Robin Jamal, has not filed a brief.

Respondent, Israel Discount Bank, has not filed a brief.

Respondent, S.W. Vaughn, has not filed a brief.

Before Judges Alvarez and Carroll.

NOT FOR PUBLICATION WITHOUT THE APPROVAL OF THE APPELLATE DIVISION

PER CURIAM.

The narrow issue on appeal in this mortgage foreclosure action involves a dispute between plaintiff, Metropolitan National Bank (Metropolitan), and defendant, BNY Mellon, N.A. (BNY), over the priority of their respective mortgages on the subject property. BNY appeals from October 4, 2011 orders of the trial court determining that the Metropolitan mortgage held priority. We conclude, based on the facts presented, that Metropolitan's receipt of a credit report during its mortgage application process was insufficient to establish notice of BNY's prior, unrecorded mortgage. Accordingly, we affirm.

I.

The essential facts are substantially undisputed. On April 29, 2003, defendants Marvin and Robin Jemal (the Jemals) borrowed $1,300,000 from BNY[1]. BNY secured the 2003 loan with a mortgage on the Jemals' residential property in Allenhurst, New Jersey (the property). Inexplicably, BNY's mortgage was not recorded in the Monmouth County Clerk's Office until November 10, 2010[2].

During the intervening seven-year period between the execution and recording of the BNY mortgage, Robin Jemal (Jemal) applied for, and obtained, a $3,270,000 loan from Metropolitan. The Metropolitan loan was similarly secured by a mortgage on the property, which was dated April 10, 2006, and promptly recorded in the Monmouth County Clerk's Office on April 17, 2006.

In March 2006, as part of its application process, Metropolitan obtained, and reviewed, a Transunion credit report on Jemal. Included in this four-page credit report was a reference to "Alliance Mtg F," an account number, and the notations "4/03," "$1.3M," and "conventional real." It is the significance to be attached to this credit report which frames the priority dispute between the parties.

Prior to closing its loan, Metropolitan also secured a title commitment which, of course, failed to reveal the existence of the unrecorded BNY mortgage. Additionally, Jemal failed to list the BNY mortgage, both in the personal financial statement that she submitted to Metropolitan during the loan application process, and in the affidavit of title that she executed at the 2006 loan closing.

Ultimately, Jemal defaulted on the Metropolitan loan, causing Metropolitan to commence this foreclosure action in November 2010. According to Metropolitan, it first became aware of the BNY mortgage when it ran a foreclosure search preparatory to filing its foreclosure complaint. Metropolitan then amended its complaint in December 2010 to join BNY as a defendant by virtue of its junior lien status. BNY filed a contesting answer, along with a counterclaim asserting that BNY should have first lien status because Metropolitan had actual notice of the 2003 BNY loan at the time Metropolitan closed its 2006 mortgage loan.

Following a period of discovery, BNY moved for partial summary judgment (1) declaring that BNY had a mortgage lien on the property which was superior and prior to any interest of Metropolitan, and (2) dismissing Metropolitan's foreclosure complaint as to BNY. BNY argued that, prior to closing the 2006 mortgage loan, Metropolitan had actual knowledge of the April

2003 BNY mortgage loan, by virtue of having received and reviewed the credit report, which disclosed its existence.

Metropolitan cross-moved for partial summary judgment, asserting that its mortgage had priority because it was recorded first, well prior to the recording of the BNY mortgage. Metropolitan further argued that the credit report was not ordered for the purpose of ascertaining the existence of any liens on the property, nor were the contents of the report sufficient to provide notice of BNY's mortgage. Metropolitan thus sought to strike BNY's contesting answer.

Upon considering the lenders' competing arguments, the motion judge granted summary judgment in favor of Metropolitan, and held that Metropolitan's mortgage had priority over the BNY mortgage. In his oral decision, the judge canvassed jurisprudence involving New Jersey's recording statutes, and the policy underlying the enactment of those statutes. The judge also applied equitable principles and concluded, among other things, that BNY was in the best position to have avoided the loss by timely recording its mortgage. This appeal by BNY follows.

II.

When a party appeals from a trial court order granting or denying a summary judgment motion, we "`employ the same standard [of review] that governs the trial court.'" Henry v. N.J. Dep't of Human Servs., 204 N.J. 320, 330 (2010) (quoting Busciglio v. DellaFave, 366 N.J. Super. 135, 139 (App. Div. 2004)). Thus, we must determine whether there was a genuine issue of material fact, and if not, whether the trial court's ruling on the law was correct. Prudential Prop. & Cas. Ins. Co. v. Boylan, 307 N.J. Super. 162, 167 (App. Div.), certif. denied, 154 N.J. 608 (1998). We review legal conclusions de novo. Henry, supra, 204 N.J. at 330.

We recently recognized that:

> Mortgage priorities are generally governed in New Jersey by our recording statutes. N.J.S.A. 46:26A-1 to-12. New Jersey is a "race-notice" jurisdiction, meaning that when two parties are competing for priority over each other's mortgage, the party that recorded its mortgage first will normally prevail, so long as that party did not have actual knowledge of the other party's previously-acquired interest. Cox v. RKA Corp., 164 N.J. 487, 496 (2000) (citing Palamarg Realty Co. v. Rehac, 80 N.J. 446, 454 (1979)).
>
> [Sovereign Bank v. Gillis, ___ N.J.Super. ___, ___ (App. Div. 2013) (slip op. at 9-10).]

Specifically relevant to our analysis is N.J.S.A. 46:21-1, which provides, in pertinent part, that

> whenever any deed or instrument ... which shall have been or shall be duly acknowledged or proved and certified, shall have been or shall be duly recorded or lodged for record with the county recording officer of the county in which the real estate ... is situate or located such record shall, from that time, be notice to all subsequent ... mortgagees of the execution of the deed or instrument so recorded and of the contents thereof.

Additionally, N.J.S.A. 46:22-1 provides that

> [e]very deed or instrument ... shall, until duly recorded, ... be void and of no effect against ... all subsequent bona fide purchasers and mortgagees for valuable consideration, not having notice thereof, whose deed shall have been first duly recorded or whose mortgage shall have been first duly recorded or registered....
>
> [(Emphasis added).][3]

The principal purpose in enacting these recording statutes "was to protect subsequent judgment creditors, bona fide purchasers, and bona fide mortgagees against the assertion of prior claims to the land based upon any recordable but unrecorded instrument." Cox, supra, 164 N.J. at 507 (citations omitted). "[T]he integrity of the recording scheme is paramount." Id. at 497. "Generally speaking, and absent any unusual equity, a court should decide a question of title ... in the way that will best support and maintain the integrity of the recording system." Palamarg, supra, 80 N.J. at 453. See also Cox, supra, 164 N.J. at 497; Friendship Manor, Inc. v. Greiman, 244 N.J. Super. 104, 113 (App. Div. 1990).

Under our statutory scheme, "as between two competing parties the interest of the party who first records the instrument will prevail so long as that party had no actual knowledge of the other party's previously-acquired interest." Cox, supra, 164 N.J. at 496 (citing Palamarg, supra, 80 N.J. at 454). Here, BNY does not dispute that the Metropolitan mortgage was recorded prior to the recording of the BNY mortgage. Hence, to prevail on its priority claim, BNY must establish that Metropolitan had notice of the unrecorded BNY mortgage prior to or at the time of its loan closing in April 2006.

BNY argues that Metropolitan should be deemed to have had notice of the BNY mortgage by virtue of the credit report that Metropolitan obtained and reviewed prior to closing. This credit report, BNY maintains, referenced the existence of the BNY mortgage, and was sufficient to constitute adequate notice under the recording statutes. We disagree.

Here, based on the undisputed deposition testimony and certification of Metropolitan's vice-president and real estate lending officer, Thomas Mulhall, the lender's sole purpose in obtaining a credit report on a borrower such as Jemal is to examine her credit history and credit score; in short, to establish her creditworthiness. Metropolitan did not obtain or review the credit report to identify liens on the property. Rather, the bank would then procure a title commitment for that purpose after a decision to lend was made. BNY offered no contrary evidence. Nor did BNY support its position with any expert opinion to establish (1) that the information customarily contained in a credit report is current, accurate, or reliable; (2) a standard of care in the industry pertaining to the review of credit reports; or (3) that the credit report is utilized to ascertain the existence of any liens on the property or, minimally, to impart a duty on the lender to inquire further as to the existence of such liens.

BNY also argues that the trial judge erred in failing to take judicial notice that a bank, through its employees, can review and understand credit reports and any coding on a credit report, and asserts that an expert was not necessary for such purpose. We decline to accept that argument, again especially in light of Mulhall's undisputed deposition testimony that he did not know what the codes stood for. Further, we do not conclude that the single, isolated reference in the four-page credit report was sufficient to constitute adequate notice of BNY's mortgage. It identifies the creditor not as BNY, but rather the loan servicer, Alliance Mortgage, and does not identify the property that it relates to. It further bears repeating that it is undisputed that Metropolitan lacked any other indicia of notice, as Jemal failed to disclose the existence of the unrecorded BNY mortgage either in her personal financial statement or her affidavit of title.

We further conclude that the motion judge properly looked to the underlying purpose of the recording statutes and acted in a manner designed to preserve their integrity. The judge recognized the potential chaos that a contrary ruling could visit upon the title insurance industry, which might then be required to canvass not only the public records but also the lender's entire loan file prior to insuring title.

The trial judge also correctly applied equitable principles in rejecting BNY's priority claim. The judge acknowledged the position of another defendant, David S.W. Vaughn, who had also extended a $1,200,000 loan to the Jemals, secured by two mortgages, after the Metropolitan mortgage but prior to the recording of the BNY mortgage. Vaughn too lacked notice of the BNY mortgage due to its unrecorded status. The undisputed evidence was that Vaughn would not have made the loan nor agreed to take a third mortgage position had he been apprised of the BNY mortgage. In balancing the equities, the judge properly concluded that it would be unjust to penalize Vaughn and Metropolitan, when it was BNY that was responsible for failing to timely record its mortgage, and was in the best position to develop procedures to verify the recording of its mortgages.

Affirmed.

[1] The Jemals, the defaulting debtors, have not participated in this appeal.

[2] The mortgage was assigned from the Bank of New York to BNY Mellon, N.A. For purposes of this appeal we refer to both entities collectively as BNY.

[3] These recording statutes have undergone revision since the trial court's decision. N.J.S.A. 4:22-1 was superseded as of May 1, 2012, by N.J.S.A. 46:26A-12, which retains the use of the term "notice." N.J.S.A. 46:26A-12(c) now provides that "[a] claim under a recorded document affecting the title to real property shall not be subject to the effect of a document that was later recorded or was not recorded unless the claimant was on notice of the later recorded or unrecorded document."

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United States District Court,
C.D. California.
Rozik KESHISH and Vartan Keshish, Plaintiffs,
v.
ALLSTATE INSURANCE COMPANY, and Does 1–10, Defendants.

No. CV 12–03818 MMM (JCx).
April 22, 2013.

Background: Homeowners whose residence had been damaged by smoke during wildfire and who disputed value of their insurance claim under homeowners' insurance policy, filed suit against insurer alleging, among other things, breach of the covenant of good faith and fair dealing. Insurer moved for summary judgment.

Holdings: The District Court, Margaret M. Morrow, J., held that:
(1) independent evaluation of damages created genuine dispute as to coverage, precluding insureds' bad faith claim, and
(2) insurer's failure to utilize services of an industrial hygienist in evaluating claim for smoke damage was not bad faith.

Motion granted.

West Headnotes

[1] Contracts 95 0

95 Contracts

California law implies a covenant of good faith and fair dealing in every contract.

[2] Contracts 95 0

95 Contracts

Under California law, the covenant of good faith and fair dealing is implied in contracts to prevent a contracting party from engaging in conduct which, while not technically transgressing the express covenant, frustrates the other party's rights to the benefits of the contract.

[3] Insurance 217 0

217 Insurance

Under California law, the implied covenant of good faith and fair dealing implied in every contract applies to insurance policies just as it does to other types of contracts.

[4] Contracts 95 0

95 Contracts

Under California law, in order to establish an insurer's breach of the implied covenant of good faith and fair dealing, plaintiff must show: (1) benefits due under the policy were withheld, and (2) the reason for withholding benefits was unreasonable or without proper cause.

[5] Contracts 95 0

95 Contracts

Under California law, there can be a breach of the implied covenant of good faith and fair dealing

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even if the express terms of the contract are not breached.

[6] Insurance 217 0

217 Insurance

Under California law, an insurer does not act in bad faith so long as a genuine dispute exists over an insured's coverage.

[7] Insurance 217 0

217 Insurance

Under California insurance law, a "genuine dispute" exists over an insured's coverage, so as to enable insurer to obtain summary adjudication of a bad faith cause of action, only where insurer's position is maintained in good faith and on reasonable grounds.

[8] Insurance 217 0

217 Insurance

Under California insurance law, the "genuine issue rule" in the context of bad faith claims allows a district court to grant summary judgment when it is undisputed or indisputable that the basis for insurer's denial of benefits was reasonable, even when under insured's version of the facts there is a genuine issue as to the insurer's liability under California law.

[9] Insurance 217 0

217 Insurance

Under California law, an insurer may demonstrate the existence of a genuine dispute over an insured's coverage, so as to enable insurer to obtain summary adjudication of a bad faith cause of action, by showing that it relied on opinions from experts while evaluating the insured's claim.

[10] Insurance 217 0

217 Insurance

Under California law, a "genuine dispute" over an insured's coverage can exist, so as to enable insurer to obtain summary adjudication of a bad faith cause of action, if an arbitrator awards substantially lower damages than insured's claims.

[11] Insurance 217 0

217 Insurance

In deciding, under California law, whether there is a genuine dispute over an insured's coverage, so as to enable insurer to obtain summary adjudication of a bad faith cause of action, court does not decide which party is right as to the disputed matter, but only that a reasonable and legitimate dispute actually existed.

[12] Insurance 217 0

217 Insurance

Under California law, although an insurer's reliance on an expert's independent analysis can suffice to show that there was a genuine dispute regarding the amount owed, such reliance will not automatically insulate an insurer from a bad faith claim based on a biased investigation.

[13] Insurance 217 0

217 Insurance

Under California law, even when an insurer has relied on an expert to determine insured's damages,

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court must deny summary judgment on a bad faith claim if evidence shows that insurer dishonestly selected its experts, insurer's experts were unreasonable, or insurer failed to conduct a thorough investigation.

[14] Insurance 217 0

217 Insurance

Independent cleaning and restoration service's report to homeowners' insurer, which estimated smoke damage to insureds' residence following wildfire, and which differed significantly from both insureds' and insurer's initial estimates, created genuine dispute as to coverage, and thus under California law precluded insureds' bad faith claim against insurer based on insufficient coverage.

[15] Insurance 217 0

217 Insurance

Under California law, even a small difference between an insured's estimate of damages and an appraisal award suffices to show the existence of a "genuine dispute," so as to enable insurer to obtain summary adjudication of a bad faith cause of action.

[16] Insurance 217 0

217 Insurance

Under California law, while a significant difference between an insured's claim and an appraisal might render it unnecessary to evaluate the insurer's conduct in investigating a bad faith claim as a matter of law, an insurer who otherwise acted in bad faith should not be insulated from liability simply because insured's estimate of loss was slightly higher than an arbitrator's ultimate award.

[17] Federal Civil Procedure 170A 0

170A Federal Civil Procedure

An expert's conclusory allegations do not defeat summary judgment where the record clearly rebuts the inference the expert suggests. Fed.Rules Civ.Proc.Rule 56(e), 28 U.S.C.A.

[18] Federal Civil Procedure 170A 0

170A Federal Civil Procedure

Expert's conclusory opinion that insurer acted in bad faith, under California law, by failing to meet face to face with insured and his contractor to discuss value of insured's claim resulting from smoke damage to his residence following wildfire, failed to raise a triable issue of fact concerning insurer's bad faith; expert's opinion contained no supporting evidence regarding typical industry standards or customs, and expert failed to identify substantive aspect of insurer's position regarding amount of claim that was unreasonable, in his view. Fed.Rules Civ.Proc.Rule 56(e), 28 U.S.C.A.

[19] Federal Civil Procedure 170A 0

170A Federal Civil Procedure

Generally, an expert witness cannot raise triable issues of fact concerning an insurer's bad faith simply by listing things the insurer could have done differently.

[20] Federal Civil Procedure 170A 0

170A Federal Civil Procedure

Conclusory expert testimony that an insurer act-

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ed in bad faith may be excluded, on motion for summary judgment, on the ground that the opinion is nothing more than a legal conclusion.

[21] Insurance 217 0

217 Insurance

Under California law, the "genuine dispute doctrine" is built around the notion that an insurer need not agree with insured on the scope of coverage or damages before it can be found to have acted in good faith; rather, insurer will be considered to have acted in good faith as long as it has reasonable grounds for disagreeing with insured.

[22] Estoppel 156 0

156 Estoppel

The purpose of the judicial estoppel doctrine is to protect the integrity of the judicial process by prohibiting parties from changing positions as circumstances warrant.

[23] Estoppel 156 0

156 Estoppel

The judicial estoppel doctrine applies when: (1) the same party has taken two positions; (2) the positions were taken in judicial or quasi-judicial administrative proceedings; (3) the party was successful in asserting the first position, i.e., the tribunal adopted the position or accepted it as true; (4) the two positions are totally inconsistent; and (5) the first position was not taken as a result of ignorance, fraud, or mistake.

[24] Estoppel 156 0

156 Estoppel

Under California law, an insurance appraisal is not a "judicial or quasi-judicial proceeding" to which judicial estoppel applies; such appraisals are informal, and appraisers typically conduct independent investigations and base their decisions on their own knowledge, without holding formal hearings.

[25] Insurance 217 0

217 Insurance

Under California law, insurer's failure to utilize services of an industrial hygienist in evaluating homeowners' claim, under homeowners' insurance policy, for smoke damage to residence following wildfire, was not bad faith; independent cleaning and restoration service had already conducted a thorough investigation, so the need for an industrial hygienist's evaluation was not self evident or obvious, no industry standard or requirement existed regarding an insurer's retention of such services when remediating smoke damage, and although insurer ultimately retained an industrial hygienist, it did so only to protect its own interests when it learned that homeowners had obtained their own hygienist evaluation.

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Peter H. Klee, McKenna Long and Aldridge LLP, San Diego, CA, Theona Zhordania, McKenna Long and Aldridge LLP, Los Angeles, CA, for Defendants.

ORDER GRANTING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT

MARGARET M. MORROW, District Judge.

***1** On April 2, 2012, Rozik and Vartan Keshish filed this action against Allstate Insurance Company, alleging claims for breach of contract, breach of the covenant of good faith and fair dealing, elder abuse, violation of the Unruh Civil Rights Act, and violation of California's Unfair Competition Law ("UCL").FN1 The parties thereafter stipulated to dismiss the UCL claim. FN2 On July 30, 2012, the court granted in part and denied in part Allstate's motion for judgment on the pleadings.FN3 Specifically, it granted judgment in Allstate's favor on plaintiffs' Unruh Act claim, but declined to enter judgment on the remaining claims.FN4 The court also determined that plaintiffs' breach of contract claim and breach of the covenant of good faith and fair dealing were entirely duplicative, such that they were not separate claims but rather one claim for breach of the implied covenant. FN5 The parties later stipulated to dismiss plaintiffs' elder abuse claim.FN6 Thus, the claim for breach of the covenant of good faith and fair dealing is the sole remaining cause of action. On February 23, 2013, Allstate filed a motion for summary judgment on this claim.FN7 Plaintiffs oppose the motion.FN8

I. BACKGROUND

This case concerns a homeowners' insurance policy that Allstate issued to plaintiffs.FN9 In late August or early September 2009, a wildfire broke out in the Sunland–Tujunga area near plaintiffs' home.FN10 On October 2, 2009, plaintiffs' attorney submitted a claim for smoke damage to Allstate. FN11 She requested that a home inspection be expedited because Rozik Keshish was a kidney transplant recipient.FN12 To accommodate this request, Allstate assigned plaintiffs' claim to an available claims adjuster. FN13 The adjuster inspected plaintiffs' property on October 5, 2009 to determine the scope of the smoke damage; FN14 he estimated repair costs of $8,582.09, and forwarded this estimate to plaintiffs' attorney.FN15 On October 9, 2009, plaintiffs' attorney called the adjuster to complain that the estimate was too low; FN16 in response, Allstate retained ServiceMaster, an independent contractor, to reevaluate the damage.FN17 Allstate also paid plaintiffs $7,582.09, which represented the amount of the original estimate minus a $1,000 deductible.FN18

On November 10, 2009, after evaluating the property, ServiceMaster submitted an independent estimate to Allstate. It placed the damage at $5,322.97, more than $3,000 less than the adjuster's original estimate.FN19 ServiceMaster opined that this amount was sufficient to complete all necessary cleaning and repairs .FN20 On November 20, 2009, plaintiffs' counsel sent Allstate a letter objecting to ServiceMaster's estimate; she included with the letter the estimates of two contractors plaintiffs had retained; they placed cleaning and repair costs at $81,326.45.FN21 Allstate determined that this estimate was too high, and advised plaintiffs that it would not pay any additional amounts on the claim.FN22 Allstate closed plaintiffs' file on December 28, 2009; it sent a letter instructing them to contact it immediately if they discovered additional damage not accounted for in Allstate's original estimate. FN23

***2** Two months later, plaintiffs retained an independent industrial hygienist to inspect their property and prepare a report regarding the level of smoke damage to the home.FN24 Plaintiffs did not advise Allstate that they had hired a hygienist or that they had an additional evaluation of the property conducted.FN25 From mid-February to May 2010, plaintiffs' attorney sent five letters to Allstate, demanding an appraisal of the loss under the policy's appraisal provision.FN26 None of these letters enclosed a copy of the hygienist's report or mentioned its existence.FN27 The letters were not received by the proper Allstate representatives until June 3, 2010, because they referenced an incorrect claim number.FN28 On June 4, 2010, Allstate responded that it would review any new information plaintiffs had obtained since it had closed its file.FN29 Allstate sent a follow-up letter on June 15, 2010, again requesting any new information plaintiffs had received.FN30 Plaintiffs did not provide the hygienist's report.

Between July 2010 and January 2012, plaintiffs and Allstate exchanged several letters in an attempt to select appraisers and conduct the appraisal process.FN31 The process was delayed several months because plaintiffs did not timely select an umpire.FN32 Once they did, plaintiffs did not immediately pay him, and the umpire refused to participate in the appraisal until he had been compensated.FN33 Finally, on January 17, 2012, Allstate received notice that plaintiffs' umpire anticipated he would be paid and was prepared to engage in the appraisal process.FN34 Allstate also learned for the first time that plaintiffs had retained a hygienist who had prepared a report.FN35 Allstate spoke with its appraiser, who said that the hygienist's report had been prepared in February 2010; he advised Allstate to have a hygienist report prepared and submit it to the appraisers.FN36

Allstate retained a hygienist in late January 2012. Plaintiffs, however, refused to allow Allstate's hygienist to inspect the property. As a consequence, plaintiffs' was the only hygienist report submitted to the appraisers.FN37 In February, 2012, the appraisal panel determined that the value of plaintiffs' loss was $42,950.FN38 This was $34,367.91 more than Allstate's estimate, but $38,826.45 less than plaintiffs' demand. On March 23, 2012, Allstate paid the full amount of the appraisal award.FN39

II. DISCUSSION

A. Standard Governing Motions for Summary Judgment

A motion for summary judgment must be granted when "the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law." FED. R.CIV.PROC. 56. A party seeking summary judgment bears the initial burden of informing the court of the basis for its motion and of identifying those portions of the pleadings and discovery responses that demonstrate the absence of a genuine issue of material fact. See *Celotex Corp. v. Catrett,* 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). Where the moving party will have the burden of proof on an issue at trial, the movant must affirmatively demonstrate that no reasonable trier of fact could find other than for the moving party. On an issue as to which the nonmoving party will have the burden of proof, however, the movant can prevail merely by pointing out that there is an absence of evidence to support the nonmoving party's case. See *id.* If the moving party meets its initial burden, the nonmoving party must set forth, by affidavit or as otherwise provided in Rule 56, "specific facts showing that there is a genuine issue for trial." *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 250, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986); FED.R.CIV.PROC. 56(e)(2). Evidence presented by the parties at the summary judgment stage must be admissible. FED. R.CIV.PROC. 56(e)(1). In reviewing the record, the court does not make credibility determinations or weigh conflicting evidence. Rather, it draws all inferences in the light most favorable to the nonmoving party. See *T.W. Electric Service, Inc. v. Pacific Electric Contractors Ass'n,* 809 F.2d 626, 630–31 (9th Cir.1987).

B. Whether Allstate is Entitled to Summary Judgment on Plaintiffs' Breach of the Covenant of Good Faith and Fair Dealing Claim

***3** [1][2][3][4] California law implies a covenant of good faith and fair dealing in every contract. *Carma Developers (Cal.), Inc. v. Marathon Development California, Inc.,* 2 Cal.4th 342, 371, 6 Cal.Rptr.2d 467, 826 P.2d 710 (1992); see also *Chodos v. West Publishing Co.,* 292 F.3d 992, 996 (9th Cir.2002) (noting that "California law, like the law in most states, provides that a covenant of good faith and fair dealing is an implied term in every contract" (citations omitted)). The covenant is implied "to prevent a contracting party from engaging in conduct which (while not technically transgressing the express covenant) frustrates the other party's rights [to] the benefits of the contract." *Marsu B .V. v. Walt Disney Co.,* 185 F.3d 932, 938 (9th Cir.1999) (citing *Los Angeles Equestrian Ctr., Inc. v. City of Los Angeles,* 17 Cal.App.4th 432, 447, 21 Cal.Rptr.2d 313

(1993)). This principle applies to insurance policies just as it does to other types of contracts. *Kransco v. Am. Empire Surplus Lines Ins. Co.*, 23 Cal.4th 390, 400, 97 Cal.Rptr.2d 151, 2 P.3d 1 (2000). "In order to establish a breach of the implied covenant of good faith and fair dealing under California law, a plaintiff must show: (1) [that] benefits due under the policy were withheld; and (2) [that] the reason for withholding benefits was unreasonable or without proper cause." *Guebara v. Allstate Ins. Co.*, 237 F.3d 987, 992 (9th Cir.2001) (citing *Love v. Fire Ins. Exch.*, 221 Cal.App.3d 1136, 1151, 271 Cal.Rptr. 246 (1990)).

[5] "The implied covenant of good faith and fair dealing acts as a 'supplement to express contractual covenants, to prevent a contracting party from engaging in conduct that frustrates the other party's rights to the benefits of the agreement.' " *Moncada v. Allstate Ins. Co.*, 471 F.Supp.2d 987, 996 (N.D.Cal.2006) (quoting *Waller v. Truck Ins. Exchange, Inc.*, 11 Cal.4th 1, 44, 44 Cal.Rptr.2d 370, 900 P.2d 619 (1995)). There can be a breach of the covenant even if the express terms of the contract are not breached. See *Schwartz v. State Farm Fire and Cas. Co.*, 88 Cal.App.4th 1329, 1339, 106 Cal.Rptr.2d 523 (2001) ("It is well-established that a breach of the implied covenant of good faith is a breach of the contract ... and that breach of a specific provision of the contract is not a necessary prerequisite to a claim for breach of the implied covenant of good faith and fair dealing"). Nonetheless, a necessary prerequisite to such a claim is a showing that benefits due under the policy were withheld unreasonably or without proper cause. Moreover, "[i]t is universally recognized [that] the scope of conduct prohibited by the covenant of good faith is circumscribed by the purposes and express terms of the contract." *Carma Developers*, 2 Cal.4th at 373, 6 Cal.Rptr.2d 467, 826 P.2d 710.

Allstate advances three arguments as to why it is entitled to summary judgment: (1) there was a genuine dispute concerning the value of plaintiffs' insurance claim; (2) plaintiffs concealed the existence of the hygienist's report; and (3) plaintiffs refused to allow Allstate's hygienist access to the property.

1. Whether There Was a Genuine Dispute Regarding the Value of Plaintiffs' Claim

***4** [6][7][8] It is well established that "an insurer does not act in bad faith so long as a 'genuine dispute' exists over an insured's coverage." *Maynard v. State Farm Mut. Auto. Ins. Co.*, 499 F.Supp.2d 1154, 1160 (C.D.Cal.2007) (citing *Rappaport–Scott v. Interinsurance Exchange of Auto. Club*, 146 Cal.App.4th 831, 837, 53 Cal.Rptr.3d 245 (2007). A genuine dispute exists only where "the insurer's position is maintained in good faith and on reasonable grounds." *Wilson v. 21st Century Ins. Co.*, 42 Cal.4th 713, 723, 68 Cal.Rptr.3d 746, 171 P.3d 1082 (2007). "The genuine issue rule in the context of bad faith claims allows a district court to grant summary judgment when it is undisputed or indisputable that the basis for the insurer's denial of benefits was reasonable—for example, where even under the plaintiff's version of the facts there is a genuine issue as to the insurer's liability under California law." *Amadeo v. Principal Mut. Life Ins. Co.*, 290 F.3d 1152, 1161 (9th Cir.2002); see also *Lunsford v. Am. Guar. & Liab. Ins. Co.*, 18 F.3d 653, 656 (9th Cir.1994) ("[A] court can conclude as a matter of law that an insurer's denial of a claim is not unreasonable, so long as there existed a genuine issue as to the insurer's liability").

[9][10] An insurer may demonstrate the existence of a genuine dispute by showing that "it relied on opinions from experts while evaluating the insured's claim." *Maynard*, 499 F.Supp.2d at 1160 (citing *Fraley v. Allstate Ins. Co.*, 81 Cal.App.4th 1282, 1292, 97 Cal.Rptr.2d 386 (2000) ("The 'genuine dispute' doctrine may be applied where the insurer denies a claim based on the opinions of experts")). A genuine dispute can also exist if "an arbitrator awards substantially lower damages than Plaintiff claims." *Id.* (citing *Rappaport–Scott*, 146 Cal.App.4th at 839,

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53 Cal.Rptr.3d 245 ("[T]he vast difference between the $346,732.34 in losses claimed by Rappaport–Scott and the $63,000 in actual losses as determined by the arbitrator demonstrates, *as a matter of law*, that a genuine dispute existed as to the amount payable on the claim" (emphasis original)); *Holland v. Westport Ins. Corp.*, No. C 04–1238 CW, 2007 WL 1456045, *4 (N.D.Cal. May 17, 2007) ("[E]ven if an arbitrator later awards a greater amount than the insurer offered, the amount of that award in comparison to the amount demanded by the insured can establish a lack of bad faith as a matter of law").

[11] In deciding whether there was a genuine dispute, "the court does not decide which party is 'right' as to the disputed matter, but only that a reasonable and legitimate dispute actually existed." *Chateau Chamberay Homeowners Ass'n v. Associated Intern. Ins. Co.*, 90 Cal.App.4th 335, 348, 108 Cal.Rptr.2d 776 (2001). "[T]he reasonableness of the insurer's decisions and actions must be evaluated as of the time that they were made; the evaluation cannot fairly be made in the light of subsequent events that may provide evidence of the insurer's errors." *Id.* at 347, 108 Cal.Rptr.2d 776.

a. Whether Allstate's Reliance on ServiceMaster's Estimate Insulates it From a Bad Faith Claim

***5** [12][13] The gravamen of plaintiffs' claim is that Allstate failed to conduct a good faith review of their property damage claim.[FN40] Allstate argues that its reliance on the ServiceMaster estimate, which was substantially lower than plaintiffs' estimate, precludes a finding that it acted in bad faith in evaluating plaintiffs' claim.[FN41] It is well settled that an insurer's reliance on an expert's independent analysis can suffice to show that there was a genuine dispute regarding the amount owed; such reliance "will not[, however,] *automatically* insulate an insurer from a bad faith claim based on a biased investigation." *Chateau Chamberay*, 90 Cal.App.4th at 348, 108 Cal.Rptr.2d 776. Even where an insurer has relied on an expert, the court must deny summary judgment on a bad faith claim if evidence shows that "the insurer dishonestly selected its experts[,] the insurer's experts were unreasonable[,][or] the insurer failed to conduct a thorough investigation." *Id.* at 348–49, 108 Cal.Rptr.2d 776. See also *Guebara*, 237 F.3d at 996 ("Expert testimony does not automatically insulate insurers from bad faith claims based on biased investigations. Although this list is not exhaustive, we can think of several circumstances where biased investigation claims could go to a jury: (1) the insurer is guilty of misrepresenting the nature of the investigatory proceedings; (2) the insurer's employees lie during the depositions or to the insured; (3) the insurer dishonestly selected its experts; (4) the insurer's experts were unreasonable; and (5) the insurer failed to conduct a thorough investigation").

It is undisputed that, after plaintiffs objected to Allstate's original estimate, the insurer retained ServiceMaster to conduct an independent review. It is further undisputed that ServiceMaster's estimate of the damage was even lower than the original estimate provided by Allstate's adjuster. Despite this, Allstate paid plaintiffs the amount of the higher initial estimate. Plaintiffs proffer no evidence that ServiceMaster's investigation was cursory, biased, or deficient in any way. They also adduce no evidence that Allstate misrepresented to ServiceMaster the scope or focus of the inspection it needed to perform, such that ServiceMaster's evaluation was incomplete or flawed. Rather, based on the record, it appears that ServiceMaster did a thorough review of each room in plaintiffs' home, inspecting the residence's structure and the furniture contained in it.[FN42] The individual who conducted ServiceMaster's evaluation was a certified smoke remediation technician, who specialized in evaluating and remediating smoke damage and had six years experience on the job.[FN43] Plaintiffs proffer no evidence that challenges her expertise or the manner in which she handled the evaluation of the property. Based on the undisputed evidence, therefore, Allstate acted reasonably in relying on ServiceMaster's independent estimate when it denied plaintiffs'

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claim for additional loss amounts.[FN44] See *Adams v. Allstate Insurance Co.*, 187 F.Supp.2d 1207, 1215–17 (C.D.Cal.2002) (granting summary judgment on a bad faith claim where an insurer relied on an expert report from AGRA and "[p]laintiffs submit[ted] no opinion or report by an expert ... alleg[ing that] the nature and quality of AGRA's investigation was somehow incorrect or unreasonable"); see also *Anderson v. USAA Cas. Ins. Co.*, No. C 06–07948 WHA, 2008 WL 619004, *8–9 (N.D.Cal. Mar.4, 2008) (finding a genuine dispute between insured and insured because the insurer "based its decision on expert opinions" and "[n]othing in the record supports the theory of a biased investigation by [the retained experts]"); *Badell v. Celtic Life Ins. Co.*, 159 F.Supp .2d 1186, 1194 (N.D.Cal.2001) ("Plaintiff contends that Celtic acted unreasonably by forwarding insufficient evidence to the [expert].... She offers no authority that suggests why this information [sent to the expert] was so insufficient as to constitute a breach of the implied covenant of good faith and fair dealing"); *Cardiner v. Provident Life & Acc. Ins. Co.*, 158 F.Supp.2d 1088, 1101–02 (C.D.Cal.2001) (granting summary judgment based on existence of a genuine dispute where an insurer relied on the expert opinions of doctors and "[p]laintiff offer[ed] no evidence that the[ ] doctors" performed biased or incomplete evaluations). Plaintiffs have proffered no evidence raising triable issues of fact concerning the bona fide nature of ServiceMaster's independent evaluation of the damage to their home. Nor have they adduced evidence giving rise to an inference that ServiceMaster's estimate reflected anything other than an honest assessment of the damage evident at the time.

***6** The facts here, in fact, are strikingly similar to those in *Fraley.* There, Allstate hired independent contractors to estimate the damage to an insured's property. 81 Cal.App.4th at 1292, 97 Cal.Rptr.2d 386. The contractors submitted estimates of approximately $110,000. *Id.* Plaintiffs' contractor, by contrast, estimated that repairs would cost approximately $230,000. *Id.* After evaluating the estimates, Allstate determined that the minimum repair cost was $199,000, and promptly paid plaintiffs that amount. *Id.* at 1293, 97 Cal.Rptr.2d 386. Plaintiffs sued Allstate for bad faith, seeking to recover the difference between their estimate and the amount paid. The court granted Allstate's motion for summary judgment, finding that a genuine dispute existed at the time plaintiffs submitted their claim; this genuine dispute, the court held, precluded a finding that Allstate had acted in bad faith. It noted:

> "The record reveals that Allstate handled the Fraleys' claim reasonably, by retaining experts and investigating, paying the undisputed actual cash value of the loss and proceeding to appraisal on the disputed portion of the claim, replacement cost. Moreover, Allstate promptly paid the replacement cost appraisal award after the Fraleys purchased another home. We agree with the trial court that their bad faith claim fails as a matter of law." *Id.*

Here, Allstate and plaintiffs each retained an independent expert to evaluate the damage to plaintiffs' home; each expert arrived at a different estimate. Allstate promptly paid plaintiffs $7,582.09, the undisputed amount of plaintiffs' claim. Allstate also honored plaintiffs' request that it engage in the appraisal process, and paid the appraisal award to plaintiffs soon after it was rendered. The fact that plaintiffs' expert estimated the loss at approximately ten times the amount Allstate's adjuster and expert did is insufficient, by itself, to raise triable issues concerning bad faith. See *Guebara*, 237 F.3d at 993 ("Where the parties rely on expert opinions, even a substantial disparity in estimates for the scope and cost of repairs does not, by itself, suggest the insurer acted in bad faith," citing *Fraley*, 81 Cal.App.4th at 1292, 97 Cal.Rptr.2d 386).

[14] Ultimately, "a single, thorough report by an independent expert is sufficient, all other things being equal, to support application of the 'genuine dispute'

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doctrine." *Adams,* 187 F.Supp.2d at 1227–28. It is undisputed that ServiceMaster independently examined plaintiffs' property, and provided an estimate significantly below that of plaintiffs' contractors. Plaintiffs have not raised triable issues of fact regarding the reasonableness of Allstate's reliance on the ServiceMaster estimate in denying their request for additional compensation. Accordingly, the undisputed evidence shows that there was a legitimate, genuine dispute regarding the amount Allstate owed under the policy. This precludes a finding of bad faith.

b. Whether the Difference Between Plaintiffs' Damage Estimate and the Appraisal Award Establishes That There Was a Genuine Dispute

***7** Allstate also argues that the $38,829.45 difference between plaintiffs' damage estimate and the appraisal award demonstrates, as a matter of law, that there was a genuine dispute concerning the amount of insurance proceeds owed. As authority, it cites *Rappaport–Scott,* 146 Cal.App.4th at 833–35, 53 Cal.Rptr.3d 245. In *Rappaport–Scott,* the court determined that a substantial difference between the amount of loss a plaintiff claims and the amount of loss ultimately found by an arbitrator can conclusively determine that a genuine dispute existed. *Id.* at 839, 53 Cal.Rptr.3d 245 ("[T]he vast difference between the $346,732.34 in losses claimed by Rappaport–Scott and the $63,000 in actual losses as determined by the arbitrator demonstrates, *as a matter of law,* that a genuine dispute existed as to the amount payable on the claim" (emphasis original)).

[15] This rule has been applied in a handful of cases since *Rappaport–Scott.* In most, as in *Rappaport–Scott,* the difference between the plaintiff's damage estimate and the amount of loss an arbitrator found was substantial, often in the hundreds of thousands of dollars. See, e.g., *Maynard,* 499 F.Supp.2d at 1162 ("Plaintiff's recovery in the arbitration was an astonishing $414,000 less than what he requested, the difference between $500,000 in claimed damages and $86,000 in damages as determined by the arbitrator"); *Holland,* 2007 WL 1456045 at *4 (finding that a genuine dispute existed as a matter of law because "[t]he $19,000 liability the arbitrator attributed to Westport was significantly less than the $1 million Holland demanded"). At least one court, however, has held that even a small difference between plaintiffs' estimate and an appraisal award suffices to show the existence of a genuine dispute. In *Behnke v. State Farm General Ins. Co.,* 196 Cal.App.4th 1443, 1470, 127 Cal.Rptr.3d 372 (2011), the court concluded that an arbitrator's award that was $16,000 less than plaintiff's demand was sufficient to defeat a claim that the insurer had acted in bad faith. The court concluded:

> "[T]he undisputed facts ... establish that a dispute arose between Behnke (and his Cumis counsel, English & Gloven) on the one hand, and State Farm on the other, over the amount of policy benefits State Farm was obligated to pay for Cumis counsel fees and costs incurred by English & Gloven on Behnke's behalf; that the dispute was properly submitted to mandatory arbitration under section 2860(c); and that the arbitrator, in an award confirmed by the trial court, ordered State Farm to pay an amount [$16,000] less than the amount billed by English & Gloven. These undisputed facts establish as a matter of law that State Farm's conduct in disputing the ... amount of fees and costs billed by English & Gloven was objectively reasonable, and thus Behnke's insurance bad faith claim, which is based on that conduct, fails as a matter of law. *Id.*

Here, the difference between plaintiffs' estimate and the amount of loss found by the appraisal panel is greater than the difference in *Behnke,* but substantially smaller than that in *Rappaport–Scott, Maynard,* or *Holland.* The fact that the arbitration award was approximately 47 per cent lower than plaintiffs' demand is compelling evidence that Allstate had a reasonable basis for believing plaintiffs' loss estimate was too high. This is particularly true here because, unlike Allstate, the appraisal panel had the benefit of reviewing plaintiffs' hygienist report when evaluating damages, and *still* concluded that plaintiffs' estimate was almost double the actual damage suffered. The strongest inference that can reasonably be drawn from this fact is that plaintiffs were not entitled to receive insurance proceeds in the full amount they requested, and thus Allstate's refusal to pay them that amount was not bad faith conduct but rather a legitimate business decision.

***8** Plaintiffs cite *Brehm v. 21st Century Ins. Co.,* 166 Cal.App.4th 1225, 83 Cal.Rptr.3d 410 (2008), as authority for the proposition that the discrepancy between their estimate and the appraisal panel's finding is insufficient to demonstrate a lack of bad faith as a matter of law.FN45 In *Brehm,* however, “the arbitrator awarded [plaintiff] an amount *in excess* of the $90,000 policy limits he demanded.” *Id.* at 1241 n. 7, 83 Cal.Rptr.3d 410 (emphasis added). Given this, the court noted that it could not “hold, at [the pleadings stage], as a matter of law, that a genuine dispute existed as to the amount payable on the claim.” *Id.* While an arbitration award of *more than* plaintiff's claim may raise issues of fact as to whether an offer by the insurer to pay *less than* plaintiff demanded was the product of a genuine dispute, here the appraisal panel awarded substantially less than the amount of plaintiffs' claim. As a consequence, the court finds *Brehm* is inapposite.

[16] Ultimately, the fact that the appraisers determined plaintiffs' loss was roughly half of the damages they claimed, viewed in light of Allstate's reliance on the independent investigation performed by ServiceMaster, strengthens the court's earlier conclusion that the uncontroverted evidence shows there was a genuine dispute regarding Allstate's payment obligation. The court is hesitant, however, to conclude that the discrepancy here is sufficiently substantial, *by itself,* to apply a *per se* rule mandating the entry of summary judgment in Allstate's favor. A plaintiff who only moderately overvalues his loss, in good faith, should not be precluded from adducing other evidence that an insurer acted in bad faith simply because an appraisal panel ultimately awards less than he sought. While a significant difference between an insured's claim and an appraisal might render it unnecessary to evaluate the insurer's conduct in investigating a claim as a matter of law, an insurer who otherwise acted in bad faith should not be insulated from liability simply because the plaintiff's estimate of loss was slightly higher than the arbitrator's ultimate award. The court can conceive of scenarios in which an insurer denies a claim in bad faith, but an appraisal panel award plaintiff less than the amount of his demand. In such an instance, a small discrepancy between plaintiffs' demand and the arbitrator's award should not defeat plaintiff's claim *as a matter of law.*

c. Whether Allstate Failed Thoroughly to Investigate Plaintiffs' Claim

[17] Finally, even if the court concluded as a matter of law that there was not a genuine dispute regarding Allstate's obligations, undisputed evidence in the record demonstrates that there are no triable issues of fact concerning the thoroughness of Allstate's investigation. See, e.g., *Shade Foods, Inc. v. Innovative Products Sales & Marketing, Inc.,* 78 Cal.App.4th 847, 879–80, 93 Cal.Rptr.2d 364 (2000) (“Among the most critical factors bearing on the insurer's good faith is the adequacy of its investigation of the claim. ‘[T]he covenant of good faith and fair dealing implied in all insurance agreements entails a duty to investigate properly submitted claims' ”). It is true that an insurer “cannot reasonably and in good faith deny [benefits] to its insured without thoroughly investigating the foundation for its denial.” *Egan v. Mutual of Omaha Ins. Co.,* 24 Cal.3d 809, 819, 169 Cal.Rptr. 691, 620 P.2d 141 (2007). The only evidence in the record purportedly demonstrating bad faith, however, is the fact that Allstate allegedly failed to meet with plaintiffs' counsel to agree on the scope of coverage Allstate was obligated to provide. FN46 Plaintiffs' expert, Richard Masters, opines “that Allstate violated the covenant of good faith and fair

dealing ... when [it] refused to meet with [plaintiffs' attorney] and the contractors selected by the Keshishes to reach a scope of damages with which all parties could agree." FN47 This opinion does not suffice to raise a triable issue of fact. First, as Allstate notes, the testimony is entirely conclusory. The only support Masters offers for his opinion is the observation that insurance claims manuals state claims adjusters have a duty to attempt to reach an agreed scope of damages, and that he has seen adjusters "reprimanded and even terminated for failing to try in good faith to reach an agreed scope of damages." FN48 Masters provides no facts concerning the other incidents, however, or any information that would permit the court to conclude that the conduct of Allstate's adjuster in this case was similar. He does not even state that the terminated claims adjusters failed to meet with the insureds. Nor does his reference to statements in unspecified claims manuals that adjusters have a duty to attempt to reach agreement on the amount of a claim show that in this instance, the adjuster's failure to have a personal meeting with plaintiffs constituted bad faith. Masters does not state that the claims manuals mandate that an adjuster meet with the insureds in an effort to carry out this duty. Nor does he provide any other context concerning the statements purportedly found in the manuals. Absent additional facts, therefore, his opinion is too conclusory to raise triable issues of fact. See *Harris v. Gates*, 145 F.3d 1338, 1998 WL 337954, *3 (9th Cir. May 26, 1998) (Unpub.Disp.) (" '[I]n the context of a summary judgment, an expert must back up his opinion with specific facts.' The object of Rule 56(e) 'is not to replace conclusory allegations of the complaint or answer with conclusory allegations of an affidavit.' An expert's 'conclusory allegations' do not defeat summary judgment where the record clearly rebuts the inference the expert suggests," quoting *United States v. Various Slot Machines on Guam*, 658 F.2d 697, 700 (9th Cir.1981), and *Lujan v. National Wildlife Federation*, 497 U.S. 871, 888, 110 S.Ct. 3177, 111 L.Ed.2d 695 (1990), and citing *In re Worlds of Wonder Securities Litigation*, 35 F.3d 1407, 1425–27 (9th Cir.1994)); *Various Slot Machines on Guam*, 658 F.2d at 700 ("in the context of a motion for summary judgment, an expert must back up his opinion with specific facts"); see also *Evers v. General Motors Corp.*, 770 F.2d 984, 986 (11th Cir.1985) (a party may not avoid summary judgment solely on the basis of an expert's opinion that fails to provide specific facts from the record to support his conclusory allegations).

***9** [18][19] Masters provides few, if any, details to support his opinion that Allstate failed to negotiate in good faith. Beyond noting that the adjuster declined to have a face to face meeting with plaintiffs and their contractor, FN49 he does not describe how or why Allstate's negotiation positions constituted bad faith. He cites no authority for the proposition that insurance adjusters are required to "meet" with insureds. Indeed, the balance of his testimony reflects only that insurers have a general duty to attempt to reach agreement on a scope of damages. Masters cites no industry standard or custom requiring that the effort to reach agreement involve a face to face meeting. Similarly, he cites no industry standard or custom that requires insurers to meet with their insureds' independent contractor. Beyond a failure to meet, Masters identifies no substantive aspect of Allstate's position regarding the amount of the claim that was unreasonable in his view. His opinion that Allstate acted in bad faith by failing to meet with plaintiffs and their contractor is thus unsupported. An expert witness cannot raise triable issues of fact concerning bad faith simply by listing things the insurer could have done differently. See *Cardiner*, 158 F.Supp.2d at 1105 (granting summary judgment on a bad faith claim because "a mere recitation of actions that an insurer should have taken is not dispositive. Indeed, if this were the case, then most insureds could easily claim bad faith"); *Mitchell v. United Nat. Ins. Co.*, 127 Cal.App.4th 457, 477–78, 25 Cal.Rptr.3d 627 (2005) (affirming both summary judgment and the trial court's exclusion of the conclusory declaration of the insured's expert, which included a "discussion of what the underwriters should have done"); see also *Phelps v. Provident Life & Acc. Ins. Co.*, 60 F.Supp.2d 1014, 1023 (C.D.Cal.1999) ("That Defendant did not exhaust all possible tests is not dispositive. Indeed, an insured would always be able to argue that something else should have been done").

[20] Absent factual support, Masters' conclusion that Allstate "fail[ed] to try in good faith to reach an agreed scope of damages" because it did not meet with plaintiffs or their contractor is too conclusory to raise triable issues of fact and defeat summary judgment.[FN50] Courts frequently exclude conclusory expert testimony that an insurer has acted in bad faith on the ground that the opinion is nothing more than a legal conclusion. See *Montoya Lopez v. Allstate Ins. Co.*, 282 F.Supp.2d 1095, 1105 (D.Ariz.2003) ("Cerf's letter consists primarily of legal conclusions as to the reasonableness of Allstate's actions, which are not proper matters for an expert opinion and are to be disregarded"); *Employers Reinsurance Corp. v. Mid–Continent Cas. Co.*, 202 F.Supp.2d 1212, 1219 (D.Kan.2002) (exc1uding an expert's testimony where the expert opined that an insurer had breached its duty of good faith and fair dealing because such an opinion "constitutes an impermissible attempt to apply the law to the facts of the case to form a legal conclusion"); *Chateau Chamberay*, 90 Cal.App.4th at 349–50, 108 Cal.Rptr.2d 776 (holding that plaintiff's expert's "conclusionary opinions that AIIC (1) had not conducted an adequate and thorough investigation of HOA's loss, (2) had engaged in dilatory claims handling and unreasonable adjusting practices, (3) had arrived at an inadequate initial scope of loss for the structural damage and (4) had failed to obtain all necessary engineering inspections and reports" were not sufficient to demonstrate that an investigation was insufficient). Because he cites no facts supporting the opinion, Masters conclusion that Allstate "fail [ed] to try in good faith to reach an agreed scope of damages" is simply a legal conclusion and does not suffice to raise triable issues of fact.

***10** [21] Finally, Masters' opinion that Allstate acted in bad faith by failing to agree to a scope of damages with plaintiffs is fundamentally inconsistent with case law. The genuine dispute doctrine is built around the notion that an insurer need *not* agree with plaintiffs on the scope of coverage or damages before it can be found to have acted in good faith. Rather, it will be considered to have acted in good faith as long as it has reasonable grounds for disagreeing with the insured. An insurer need not acquiesce in an insured's claim for coverage, because "[w]hile an insurer must give as much consideration to the interests of its insured as it does to its own, it is not required to disregard the interests of its shareholders and other policyholders when evaluating claims." *Love v. Fire Ins. Exchange*, 221 Cal.App.3d 1136, 1148–49, 271 Cal.Rptr. 246 (1990); see also *Chateau Chamberay*, 90 Cal.App.4th at 347, 108 Cal.Rptr.2d 776 ("[A]n insurer is entitled to give its own interests consideration when evaluating the merits of an insured's claim").

This is not a case in which Allstate took no action in the face of its insureds' dispute with its evaluation of the property damage claim. Rather, Allstate hired ServiceMaster to conduct an independent evaluation so that it could determine whether to revise its initial coverage decision. In Masters' parlance, Allstate took this step in an effort to determine the proper scope of damages. While Allstate's ultimate conclusion differed from plaintiffs', that is not evidence of bad faith.[FN51] See *Fraley*, 81 Cal.App.4th at 1292, 97 Cal.Rptr.2d 386. Accordingly, Master's conclusory opinion that Allstate acted in bad faith by failing to reach agreement with plaintiffs concerning the value of the claim is insufficient to defeat Allstate's motion for summary judgment.

Plaintiffs also assert that Allstate should be estopped from arguing that it conducted a thorough investigation because it sought to have an industrial hygienist conduct a follow-up evaluation at the prop-

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erty.FN52 They contend that "[e]ither Allstate's initial investigation was reasonable and in good faith ... or Allstate's initial investigation was neither reasonable nor in good faith ... because Allstate failed to send out a hygienist before [closing the file]." FN53 Plaintiffs assert the doctrine of judicial estoppel bars Allstate from asserting "inconsistent" positions on this issue.

[22][23][24] "Courts uniformly recognize that the purpose of the judicial estoppel doctrine is to protect the integrity of the judicial process by prohibiting parties from changing positions as circumstances warrant." *Milton H. Greene Archives, Inc. v. CMG Worldwide, Inc.*, 568 F.Supp.2d 1152, 1160 (C.D.Cal.2008). The doctrine applies when "(1) the same party has taken two positions; (2) the positions were taken in judicial or quasi-judicial administrative proceedings; (3) the party was successful in asserting the first position (i.e., the tribunal adopted the position or accepted it as true); (4) the two positions are totally inconsistent; and (5) the first position was not taken as a result of ignorance, fraud, or mistake." *Jackson v. County of Los Angeles*, 60 Cal.App.4th 171, 183, 70 Cal.Rptr.2d 96 (1997). Judicial estoppel, however, does not apply, as Allstate has not taken inconsistent positions in judicial or quasi-judicial proceedings. Plaintiffs cite no authority for the proposition that an insurance appraisal is a "quasi-judicial" proceeding, and the court has been unable to find any. See, e.g., *Hartford Lloyd's Ins. Co. v. Teachworth*, 898 F.2d 1058, 1062 (5th Cir.1990) ("an arbitration is a quasi-judicial proceeding, complete with formal hearings, notice to parties, and testimony of witnesses. Appraisals are informal. Appraisers typically conduct independent investigations and base their decisions on their own knowledge, without holding formal hearings"). More fundamentally, Allstate was not successful in asserting its "inconsistent" position during the appraisal; rather, it was required to significantly more than the amount for which it advocated; this shows that the appraisers did not adopt Allstate's position. As a consequence, plaintiffs cannot demonstrate an essential element of judicial estoppel, and the doctrine is inapplicable.

***11** The court is also skeptical that Allstate's positions are wholly inconsistent. The Ninth Circuit has adopted a liberal approach in interpreting this element of judicial estoppel, reflecting its preference that claims be litigated on their merits. See *Admiral Ins. Co. v. Rushmore*, 70 F.3d 1277, 1995 WL 693335, *3 (9th Cir.1995) (Unpub.Disp.) (Noting that "in most cases, [the Ninth Circuit] has declined to preclude the litigants' allegedly inconsistent claims," citing *United States v. Garcia*, 37 F.3d 1359, 1366–67 (9th Cir.1994)). Allstate's argument that it was prejudiced by the fact that plaintiffs unilaterally submitted a hygienist's report to the appraisal panel and denied Allstate's hygienist access to their property is not inconsistent with an argument that it conducted a thorough investigation. Allstate merely asserts that plaintiffs' retention of a hygienist, whose report they did not share with Allstate, and their refusal to permit Allstate's hygienist to visit the property, gave plaintiffs an advantage in the appraisal. Arguing that it was prejudiced by such conduct is not inconsistent with an assertion that Allstate thoroughly investigated plaintiffs' claim.

[25] Moreover, to the extent plaintiffs contend that Allstate's failure to retain a hygienist at the outset is evidence of bad faith, the court disagrees. Plaintiffs proffer no evidence that an insurer conducting a reasonable, good faith investigation would necessarily have understood that evaluation by a hygienist was required. They fail, for example, to adduce a hygienist's or contractor's opinion that the need for a hygienist was obvious or that such a professional must be hired in every case where a structure has suffered smoke damage. Plaintiffs' expert, Masters, provides no opinion on this subject; he fails even to mention the fact that Allstate did not retain a hygienist. Plaintiffs' hygienist, moreover, testified that there is no industry standard or requirement that an insurer must retain an industrial hygienist when remediating

smoke damage.[FN54] In light of this testimony, plaintiffs' failure to adduce any evidence that the smoke damage to their home was such that the services of a hygienist were required defeats their claim that Allstate acted in bad faith because it failed to retain a hygienist before closing plaintiffs' file. Plaintiffs' lack of evidence is particularly glaring as Allstate has adduced evidence that, based on its review, a hygienist was *not* required. Specifically, Allstate has proffered the declaration of the ServiceMaster technician who conducted the independent review. She states that she “did not see any damage that caused [her] to believe that it would be necessary to retain an industrial hygienist to estimate the cost and/or scope of remediating smoke damage at the Keshishes' property.” [FN55] She further states that “[o]ver the past six years, [she has] successfully remediated similar smoke damage claims without the assistance of an industrial hygienist.” [FN56] Plaintiffs proffer no contradictory evidence. Moreover, as discussed, there is no evidence that ServiceMaster's review was deficient. Consequently, plaintiffs have failed to raise triable issues of fact as to whether Allstate's failure to retain an industrial hygienist prior to closing its file on plaintiffs' claim shows that Allstate acted in bad faith. See *Adams* 187 F.Supp.2d at 1227–28) (“The Court concludes that under existing law, *a single, thorough report* by an independent expert is sufficient, all other things being equal, to support application of the ‘genuine dispute’ doctrine” (emphasis added)).[FN57]

***12** The fact that Allstate subsequently sought to have a hygienist review the property does not demonstrate that Allstate knew its initial review was not thorough. It simply shows that once Allstate learned plaintiffs had retained a hygienist and submitted her report to the appraisal panel, it sought to protect its interests by having a comparable report prepared. As noted, an insurer is entitled to protect its own legitimate interests when investigating claims. *Chateau Chamberay*, 90 Cal.App.4th at 347, 108 Cal.Rptr.2d 776 (“[A]n insurer is entitled to give its own interests consideration when evaluating the merits of an insured's claim”). Absent evidence that a hygienist should have been retained before Allstate closed its filed, the fact that it felt it advisable to obtain a hygienist's report for purposes of the appraisal does not raise triable issues of fact as to whether its investigation prior to that time was inadequate and undertaken in bad faith.

In short, plaintiffs have failed to adduce evidence that raises triable issues as to whether Allstate investigated their claim in bad faith.[FN58]

III. CONCLUSION

In conclusion, Allstate's motion for summary judgment is granted.

JUDGMENT FOR DEFENDANT

On April 22, 2013, the court entered an order granting defendant's motion for summary judgment. Accordingly,

IT IS ORDERED AND ADJUDGED

1. That plaintiffs take nothing by way of their complaint; and

2. That the action be, and it hereby is, dismissed.

FN1. Removal, Docket No. 1 (May 2, 2012), Exh. A (“Complaint”).

FN2. Stipulation to Dismiss Fifth Claim for Relief, Docket No. 9 (May 22, 2012).

FN3. Order Granting in Part and Denying in Part Motion for Judgment on the Pleadings, Docket No. 18 (July 30, 2012).

FN4. *Id.* at 21.

FN5. *Id.* at 8 (“[T]he breach of contract claim is duplicative of the breach of implied covenant claim, since the plaintiff can recover contract damages in addition to tort damages on the latter”).

FN6. Stipulation to Dismiss Third Claim for Relief for Elder Abuse, Docket No. 26 (Nov. 7, 2012).

FN7. Motion for Summary Judgment (“Motion”), Docket No. 38 (Feb. 23, 2013); Reply in Support of Motion for Summary Judgment (“Reply”), Docket No. 43 (March 25, 2013).

FN8. Opposition to Motion for Summary Judgment (“Opp.”), Docket No. 41 (March 18, 2013).

FN9. Statement of Uncontroverted Facts (“SUF”), Docket no. 39 (Feb. 23, 2013), ¶ 1; Statement of Genuine Issues (“SGI”), Docket No. 41 (March 18, 2013), ¶ 1.

FN10. SUF, ¶ 2; SGI, ¶ 2.

FN11. SUF, ¶ 3; SGI, ¶ 3.

FN12. SUF, ¶ 3; SGI, ¶ 3.

FN13. SUF, ¶ 4; SGI, ¶ 4.

FN14. SUF, ¶ 5; SGI, ¶ 5.

FN15. SUF, ¶¶ 6–7; SGI, ¶¶ 6–7.

FN16. SUF, ¶ 8; SGI, ¶ 8.

FN17. SUF, ¶ 9; SGI, ¶ 9.

FN18. SUF, ¶ 10; SGI, ¶ 10.

FN19. SUF, ¶ 12; SGI, ¶ 12.

FN20. SUF, ¶ 13; SGI, ¶ 13.

FN21. SUF, ¶ 14; SGI, ¶ 14.

FN22. SUF, ¶ 16; SGI, ¶ 16.

FN23. SUF, ¶ 17; SGI, ¶ 17.

FN24. SUF, ¶ 18; SGI, ¶ 18.

FN25. SUF, ¶ 20; SGI, ¶ 20.

FN26. SUF, ¶ 21; SGI, ¶ 21. The appraisal provision in the policy gives the insured a right to request an independent appraisal in the event the insured and Allstate disagree regarding the amount of loss. Under the policy, each party is to select a disinterested umpire; together, the umpires must then conduct an informal evaluation of the insured's claim. Each umpire is to be paid by the party who selected him or her. (Exhibits to Motion for Summary Judgment (“Exhibits”), Docket No. 40 (Feb. 23, 2013), Exh. 1 (“Policy”) at 28.

FN27. SUF, ¶ 22; SGI, ¶ 22.

FN28. SUF, ¶ 23; SGI, ¶ 23.

FN29. SUF, ¶ 24; SGI, ¶ 24.

FN30. SUF, ¶ 26; SGI, ¶ 26.

FN31. SUF, ¶¶ 29–51; SGI, ¶¶ 29–51.

FN32. SUF, ¶ 36; SGI, ¶ 36.

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FN33. SUF, ¶ 50; SGI, ¶ 50.

FN34. SUF, ¶ 51; SGI, ¶ 51.

FN35. SUF, ¶ 51; SGI, ¶ 51.

FN36. SUF, ¶ 52; SGI, ¶ 52.

FN37. SUF, ¶ 57; SGI, ¶ 57.

FN38. SUF, ¶ 60; SGI, ¶ 60.

FN39. SUF, ¶ 61; SGI, ¶ 61.

FN40. Opp. at 19. Plaintiffs devote a substantial portion of their opposition to a discussion of California's arbitration rules and the level of deference courts must give arbitration awards. (See Opp. at 11–16). Plaintiffs argue that Allstate's motion is a collateral attack on the arbitration award and should not be permitted. The court fails to see, however, how Allstate's motion is in any manner an attack on the appraisal award. Allstate has paid the money it owed under the award, and is not seeking restitution or reimbursement. Rather, it is trying to avoid *additional* liability, beyond that it has already incurred as a result of the appraisal. The court therefore finds plaintiffs' discussion of the arbitration rules inapposite.

FN41. Motion at 17.

FN42. (Declaration of Ari Moss ("Moss Decl."), Docket No. 42 (March 18, 2013), Exh. 3 (ServiceMaster Estimate). The estimate is comprised of several pages of specific, detailed cost breakdowns for cleaning and repairing both the structural components of the home and the furniture in each room.

FN43. Declaration of Sonyia Rouel ("Rouel Decl."), Docket No. 38 (Feb. 23, 2013).

FN44. The only argument plaintiffs offer regarding the substance of the ServiceMaster report is that it failed to determine how far plaintiffs' property was from the "fire-line." (Opp. at 8). Plaintiffs do not explain the relevance of this fact; presumably, however, they argue that this piece of information was a necessary component of a reasonable insurance evaluation, and that the closer the distance, the greater the damage that was likely. Even if this is correct, the evidence cited by plaintiffs in support of their argument does not demonstrate that ServiceMaster failed to determine the distance between the property and the fire-line. At his deposition, ServiceMaster's CEO testified that while the distance was not "precisely known," his company determined that the fire-line was approximately "half a mile away from the residence." (Moss Decl., Exh. 10 at 133:2–4). The CEO also stated that ServiceMaster took this fact into account in valuing plaintiffs' loss. (*Id.* at 134:7–14 ("Knowing that it was a half mile from the fire, based on our experience, there was a stronger likelihood that that household had fire particulates in there than a household on the coast.... These are the things that I'm looking at during the fire—wildfire assessment period"). Thus, plaintiffs argument that ServiceMaster failed to consider the distance between the house and the fire-line is unavailing. As a consequence, they cannot raise triable issues of fact concerning the reasonableness of ServiceMaster's investigation on this basis.

FN45. Opp. at 22–23.

FN46. Declaration of Anahid Barsegian ("Barsegian Decl."), Docket No. 41 (March 18, 2013), ¶ 11.

FN47. Declaration of Richard Masters ("Masters Decl."), Docket No. 41 (March 18, 2013), ¶ 8.

FN48. *Id.*, ¶ 9.

FN49. *Id.*, ¶ 8.

FN50. *Id.*, ¶ 9.

FN51. As Allstate notes, allowing a bad faith claim to proceed beyond summary judgment based only on evidence that an insurer failed to reach agreement with its insured regarding the value of a claim would allow insureds to raise triable issues of fact in every case in which an insurer disagrees with the insured's estimate of the loss, whether or not the insurer's valuation was reasonable. (Reply at 5). This is inconsistent with the well-established genuine dispute doctrine.

FN52. Opp. at 20

FN53. *Id.* at 22.

FN54. Supplemental Declaration of Theona Zhordania, Docket No. 43 (Mar. 25, 2013), Exh. 1 at 123:5–12 ("Q. Are you aware of any standard or guidelines that requires an insurance company to use an industrial hygienist in every fire or smoke damage claim? A. I'm not aware of any. That would probably be their own policy. I would assume that. Q. Not anything that the industry imposes on them; correct? A. No, not that I'm aware of").

FN55. Rouel Decl., ¶ 6.

FN56. *Id.*

FN57. Plaintiffs' assertion that Allstate failed to investigate their claim thoroughly because it did not retain a hygienist is also disingenuous. It is undisputed that when Allstate advised plaintiffs it was closing their claim, it invited them to submit additional evidence if they felt the evidence warranted a reevaluation of the loss. It is also undisputed that plaintiffs failed to inform Allstate that they had had a hygienist inspect the property and prepare a report. Plaintiffs, in fact, *never* told Allstate they had had a hygienist report prepared; it was only through the appraisers that Allstate discovered this fact, more than a year after plaintiffs' hygienist had inspected the property. It is further undisputed that, once Allstate learned of the hygienist report, plaintiffs denied Allstate's hygienist access to their property to conduct an additional inspection. Plaintiffs' claim that Allstate acted in bad faith by failing to retain a hygienist when they did not communicate to Allstate their view that the services of a hygienist were required, and prevented Allstate from obtaining a hygienist's opinion when it asked to do so, is thus, at a minimum, suspect.

FN58. As the court has determined that a genuine dispute existed regarding the amount of insurance proceeds Allstate was required to pay, the court does not address Allstates' additional arguments regarding plaintiffs' failure to disclose the hygienist report. The court notes, however, that the

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undisputed fact that Allstate did not discover the existence of the report until the eve of appraisal bolsters the conclusion that, based on the evidence it had before it, Allstate acted reasonably and in good faith when it initially concluded that plaintiffs' estimate was too high.

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