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THE CALIFORNIA COURT OF APPEAL NARROWLY INTERPRETS THE PERATA MORTGAGE RELIEF ACT

On June 4, 2010, the California Court of Appeal issued its first important decision on the scope of California's Perata Mortgage Relief Act, passed into law in 2008 and codified at California Civil Code Sections 2923.5 and 2923.6. *See Mabry v. Superior Court* (Case No. G042911, June 4, 2010) ---Cal.App.4th---, 2010 WL 2180530.

Though the Court held that plaintiffs have a private right of action under the PMRA, it also held that the PMRA does not require lenders to modify loans, but only to contact (or attempt to contact) borrowers about possible options to potentially avoid foreclosure. The Court's other holdings also limit the impact of the PMRA, eviscerating the claims of many plaintiffs seeking to halt or unwind foreclosure sales in the wake of the mortgage crises.

In 2006, Plaintiffs Terry and Michael Mabry refinanced the loan on their home, borrowing about $700,000. In September of 2008, Plaintiffs stopped making their payments. In June of 2009, the lender recorded a notice of default. In October of 2009, Plaintiffs filed a class action complaint claiming that the lender failed to contact them to explore loan modification or other options prior to foreclosure. The lender disputed Plaintiff's contention. The trial court initially granted a temporary restraining order, then later vacated the order, holding that the PMRA (1) does not bestow any private right of action and (2) is preempted by federal law. Plaintiffs petitioned the appellate court for a writ of mandate.

The Court of Appeal disagreed with the rulings of the trial court, and held that the PMRA may be enforced by a private right of action. The Court noted that Section 2923.5 is silent as to a private right of action, but that it requires lenders to contact borrowers prior to foreclosure to explore possible options to potentially avoid foreclosure. The Court held that, to have any meaning, a private right of action must be implied, and that exclusive enforcement by the Attorney General's office would not be sufficient. *Id.* at *9-*11.

The Court also held that federal banking law does not preempt the PMRA, but only because of the limited reach of the state law. "There is nothing in section 2923.5 that requires the lender to rewrite or modify the loan." *Id.* at *1. We "are able to come to our conclusion that section 2923.5 is not preempted by federal banking regulations because it *is* . . . very narrow. As mentioned above, there is no *right*, for example, under the statute, to a loan modification." *Id.* at *12. As for Section 2923.6, it "does *not* operate substantively. Section 2923.6 merely expresses the *hope* that lenders will offer loan modifications on certain

terms." *Id.* at *6 (emphasis in original). To have "*required* loan modifications would have run afoul of federal law." *Id.* (emphasis in original).

These holdings are significant to the current wave of mortgage litigation for two reasons. First, the Court's decision eviscerates the claims of many plaintiffs that California law requires lenders and loan servicers to modify loans prior to foreclosure. Second, it provides further support for the proposition that federal banking law preempts any state law that attempts to impose loan terms or related requirements on lenders or servicers.

The Court's decision significantly narrowed the claims of plaintiffs in mortgage cases in other ways as well. To comply with the PMRA, a lender must merely contact the borrower prior to foreclosure about options to possibly avoid foreclosure. In doing so, a lender must "assess" the borrower's situation. Any "'assessment' must necessarily be simple—something on the order of, 'why can't you make your payments?" *Id.* at *12. "The statute cannot require the lender to consider a whole new loan application or take detailed loan information over the phone." *Id.* Exploring options to avoid foreclosure, "must necessarily be limited to the traditional ways that foreclosure can be avoided." *Id.* The PMRA does not require a lender "to engage in a process that would be functionally indistinguishable from taking a loan application in the first place." *Id.* The lender "does not have any duty to become a loan counselor itself." *Id.* Moreover, where the borrower is not cooperative, it is sufficient if the lender tried with due diligence to contact the borrower as required by the statute.

The Court also held that the, "*only* remedy provided is a postponement of the sale before it happens." *Id.* at *14. If foreclosure has already taken place, there is no remedy. The "Legislature did nothing to affect the rule regarding foreclosure sales as final." *Id.* at *1. "There is nothing in section 2923.5 that even hints that noncompliance with the statute would cause any cloud on title after an otherwise properly conducted foreclosure sale." *Id.* at *14. The Court also affirmed the rule that a plaintiff must tender loan proceeds prior to setting aside a foreclosure for irregularities in the sale, but that this rule did not apply here because a plaintiff cannot set aside a foreclosure sale based on a violation of the PMRA. *Id.* at *8.

Section 2923.5 also requires that any notice of default include a declaration of compliance with the PMRA. The Court held that this declaration need not be made under oath. *Id.* at *13.

Section 2923.5 also requires that the declaration contain certain other information about the type and substance of the notice, and identifies certain alternative notification language. The Court held that it is sufficient that the declaration "track the language of the statute itself." The declaration can be a form notice listing all the alternative ways that the lender might have complied with the PMRA, even if some of the language is inapplicable to the specific facts. The notice does not need to be "custom drafted." *Id.* at *14.

Finally, the Court held that in most circumstances claims under the PMRA would be unsuitable for class treatment. Section 2923.5 "contemplates highly-individualized facts" about how a lender contacts a borrower prior to foreclosure and what a lender says or writes about possible options to potentially avoid foreclosure. The Court commented that a class action "might" be appropriate only if a lender had a "clean, systematic *policy*" uniformly applied. For example, ignoring the statute all together might give rise to a class action, though the Court specifically declined to state whether it would. *Id.* at *15.

In sum, a plaintiff may enforce rights under the PMRA, but those rights are very narrow and exist only prior to foreclosure. If successful, a plaintiff can merely delay foreclosure until a lender has complied with the statute.

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