

**CALIFORNIA SUPREME COURT HOLDS THAT BORROWERS
HAVE STANDING TO CHALLENGE AN ALLEGEDLY VOID
ASSIGNMENT OF THE NOTE AND DEED OF TRUST IN AN
ACTION FOR WRONGFUL FORECLOSURE**

Yesterday, the California Supreme Court held in *Yvanova v. New Century Mortgage Corp*, Case No. S218973 (Cal. Sup. Ct. February 18, 2016) that borrowers have standing to challenge an allegedly void assignment of a note and deed of trust in an action for wrongful foreclosure. In reaching this decision, the Court reversed the rule followed by the overwhelming majority of California courts that borrowers lacked such standing. The Court's decision may have broad ramifications for lenders, investors, and servicers of California loans.

The Court's Holding

In *Yvanova*, the borrower challenged the validity of her foreclosure on the ground that her loan was assigned into a securitized trust after the trust closing date set forth in the applicable pooling and servicing agreement, allegedly rendering the assignment void. To date, California courts have rejected hundreds of similar claims. In *Yvanova*, the Court held that "a borrower who has suffered a nonjudicial foreclosure does not lack standing to sue for wrongful foreclosure based on an allegedly void assignment merely because he or she was in default on the loan and was not a party to the challenged assignment." Slip. Op. at 2. The Court's ruling thus breathes new life into this favorite theory of the foreclosure defense bar.

The Court's Reasoning

The Court acknowledged that the majority of California courts have held that borrowers do not have standing to challenge an allegedly void assignment because they are neither parties to, nor intended beneficiaries of, the assignment. Rather than adopt the majority approach, the Court based much of its decision on *Glaski v. Bank of America*, 218 Cal.App.4th 1079 (2013), in which the Fifth District Court of Appeal, on substantially similar facts, held that the question of standing turned on whether the alleged defect in the assignment, if proven, would render the assignment void altogether or merely voidable. Slip. Op. at 12. The parties to a voidable assignment have the power to ratify the defective assignment; parties to a void assignment have no such power. *Id.*, at 10. In the former case, the Court would deny

standing because the borrower would be asserting interests belonging solely to the parties to the assignment: only they have the power to ratify the assignment. *Id.* In the latter case, involving an allegedly void assignment, there would be no power of ratification, and thus the borrower would not be “asserting the interests of parties to the assignment; she [would be] asserting her own interest in limiting foreclosure on her property to those with legal authority to order a foreclosure sale.” *Id.*, at 21.

Potential Impact of the Court’s Decision

Although a borrower’s standing to challenge an allegedly void assignment now appears settled under California law, the full impact of the decision will likely take some time to discern. By recognizing standing to challenge allegedly void assignments, the Court has clearly invited a substantial amount of wrongful foreclosure litigation. The statute of limitations for wrongful foreclosure is at least three years and, possibly longer, if a borrower can invoke the discovery rule or equitable tolling. *See* Cal. Code of Civ. Proc. § 338(d). Given the large number of securitized loans that have been foreclosed upon in California within the last several years, the number of possible claimants is potentially very large.

It remains to be seen whether California’s trial courts will be receptive on the merits to wrongful foreclosure suits based on the now reinvigorated void-assignment theory. **There are a number of key legal and factual questions that the California Supreme Court expressly left unanswered.**

The California Supreme Court explicitly did not decide whether a transfer of a note and deed of trust into a securitized trust in violation of the trust instrument renders the assignment void or voidable under governing New York law. Importantly, the Court acknowledged a conflict between *Glaski*’s construction of New York law on this issue and a decision of the United States Court of Appeals for the Second Circuit in *Rajamin v. Deutsche Bank Nat’l Trust Co.*, 757 F.2d 79 (2d Cir. 2014). Slip. Op. at 27. In *Glaski*, the Court of Appeal found that the alleged violation of the trust instrument, if proven, would render the assignment void. *Rajamin* considered and expressly rejected *Glaski*’s construction of New York law. Nevertheless, **the California Supreme Court, in *Yvanova*, left it to California’s lower courts to determine whether to follow *Glaski* or *Rajamin*. If the lower California courts follow *Rajamin* then the uptick in wrongful foreclosure cases will likely prove short-lived and muted.** Also important

will be how California courts resolve similar issues under Delaware law, which, like New York law, governs many securitization trusts. Given this split in appellate authority under New York law, certification of the question to the New York Court of Appeals may prove an efficient way to address the uncertainty created by *Yvanova*. See New York Court of Appeals Rule 500.27 (authorizing New York Court of Appeals to hear determinative questions of New York law in cases pending before federal courts or the highest court of another state).

The Court also left for future development whether borrowers bringing a wrongful foreclosure action can obtain an order setting aside a completed foreclosure based on the void-assignment theory and whether borrowers will be required to allege tender of the outstanding loan balance to state a cause of action for wrongful foreclosure. Slip. Op. at 9 n. 4. Numerous California decisions hold that tender is required to set aside a completed foreclosure. If the lower courts continue to enforce the tender requirement, then the impact of *Yvanova* may be lessened.

Another significant question that no doubt will arise is whether borrowers can bring pre-foreclosure actions to enjoin ongoing nonjudicial foreclosures based on void assignment allegations. **The Court explicitly left undisturbed, as “not within the scope of review,” a lower court decision “disallowing the use of a lawsuit to preempt a nonjudicial foreclosure.”** *Id.*, at 16-17 (citing *Jenkins*, 216 Cal.App.4th at 513). However, a number of courts have carved out exceptions to the rule disallowing judicial preemption of ongoing nonjudicial foreclosure proceedings. It remains to be seen whether *Yvanova* will provide an impetus to broaden these exceptions.

Finally, **under California’s Homeowner Bill of Rights, borrowers must be given notice that they are entitled to request “a copy of any assignment, if applicable, of the borrower’s mortgage or deed of trust required to demonstrate the right of the mortgage servicer to foreclose.”** Cal. Civ. Code § 2923.55(B)(iii). *Yvanova* will likely inspire a substantial increase in such requests. And that may lead to an increased number of wrongful foreclosure claims.

What Happens Next

Apart from preparing to defend against the expected increase in volume of wrongful foreclosure litigation, servicers and investors may wish to consider steps to reduce their exposure to *Yvanova* and further unfavorable developments in the law. Depending on the volume of wrongful foreclosure litigation that *Yvanova* creates and whether California's trial courts begin enjoining ongoing foreclosures based on this theory, lenders, investors, and **servicers may need to consider revising their foreclosure processes to focus on possession of the note at the relevant time and thereby render irrelevant the validity of the assignment of the deed of trust. Further, lenders, investors and servicers may wish to explore the use of estoppel certificates obtained from borrowers in loan modification or other loss mitigation relief, where permissible, to establish authority to foreclose.**