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Shuster v. BAC Home Loans Servicing, LP

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Shuster v. BAC Home Loans Servicing, LP, 2012 WL 5984222 (Court of Appeal of California, November 29, 2012)

SYNOPSIS: Omission of trustee from deed of trust did not preclude enforcement through nonjudicial foreclosure where beneficiary substituted trustee prior to commencing foreclosure; mortgagors had to allege tender of balance due to assert cause of action alleging foreclosure irregularities.

FACTS: In 2006, Daniel and Yvette Shuster borrowed $670,000 from WMC Mortgage Corp. (WMC) to buy a home, executing a deed of trust that named MERS as beneficiary but did not name a trustee. WMC transferred the note to BAC Home Loans Servicing (BAC). In 2010, the Shusters defaulted. MERS substituted ReconTrust as trustee, and assigned its beneficial interest in the deed of trust to BAC. ReconTrust recorded a notice of default, claiming arrearages over $90,000 which the Shusters failed to cure. ReconTrust then recorded a notice of trustee's sale. BAC assigned its beneficial interest in the deed of trust to Arch Bay Holdings, LLC—Series 2010B, which purchased the home at the trustee's sale.

The Shusters then filed a complaint against ReconTrust, BAC, and Arch Bay, for quiet title, wrongful foreclosure and breach of contract. The complaint alleged that the defendants had no right to foreclose under the deed of trust, and an amended complaint sought to have the deed of trust cancelled for lack of a named trustee. The defendants filed a demurrer, arguing that the deed of trust was valid and properly foreclosed; the defendants further argued that the Shusters could not challenge any ostensible imperfections in the foreclosure sale because they had not tendered the unpaid balance of the debt. The trial court concluded that the omission of a named trustee in the deed of trust was "no impediment to enforcement of the Trust Deed" and sustained the demurrer of BAC and ReconTrust, dismissing the complaint against them without leave to amend. Likewise, the trial court sustained the demurrer of Arch Bay demurrer (with leave to amend), concluding that Arch Bay had purchased the home pursuant to a properly noticed trustee's sale. The Shusters filed another amended complaint against Arch Bay, which the trial court also dismissed because it pleaded no additional material facts.

On appeal, the Shusters raised two arguments. First, analogizing to prior cases holding that a deed is void if it fails to name a grantee, the Shusters argued that a deed of trust

that fails to name a trustee must likewise fail for want of someone to receive a transfer. Second, they argued that if a deed of trust fails to designate a trustee, it was transformed into a mortgage, which in California could only be foreclosed through judicial foreclosure. The Shusters thus argued that the trustee's sale of the home was invalid.

Addressing the first argument, the court noted that this was an issue of first impression in California. However, the court rejected the Shusters' argument and affirmed the judgment of the trial court, noting that prior decisions in Arizona, Missouri, and Virginia had rejected similar arguments. See *In re Bisbee*, 754 P.2d 1135 (Ariz. 1988) (deed of trust creates valid lien notwithstanding the failure to designate a trustee); *In re Burche*, 249 B.R. 518 (Bankr.W.D.Mo. 2000) (deed of trust not invalid for want of trustee if beneficiary reserves right to name a successor); *New York Life Ins. Co. v. Kennedy*, 135 S.E. 882 (Va. 1926) (named trustee not essential to validity of deed of trust).

Citing Bisbee, the court noted that a trustee under a deed of trust serves "as a type of common agent" for both borrower and lender, and thus concluded that the mere failure to designate a trustee did not render the deed of trust invalid as between the borrower and lender: "the naming of the trustee is irrelevant to the creation of the deed of trust, so long as a trustee is named prior to the foreclosure." [quoting *Bisbee*, 754 P.2d at 1137.] Thus, the court concluded that because MERS appointed a trustee before the foreclosure commenced, the deed of trust was valid and was properly foreclosed.

The court also agreed that the Shusters' claims failed because the Shusters' complaint did not allege tender of the balance due on the loan. The court upheld the principle (well-established in California) that a debtor cannot set aside a foreclosure based on irregularities in the sale without also alleging tender of the amount of the secured debt. The court acknowledged that an exception to the tender rule might be justified where the borrower challenges the validity of the underlying debt, asserts a counterclaim or set-off against the beneficiary, or demonstrates the deed of trust is void on its face, but noted that the Shusters' complaint did not implicate any of these established exceptions.

COMMENT 1: While it is well-established that a deed is void for lack of a grantee, it would make no sense to apply the same principle to a deed of trust given the circumscribed role and limited interest of the trustee. The court's decision to treat the deed of trust as valid despite the omission of a named trustee seems appropriate, at least where the deed of trust explicitly authorizes the beneficiary to appoint a trustee. Likewise, the argument by the Shusters that the omission "converted" the deed of trust into a mortgage seems dubious. Prior California decisions do establish that a deed of trust without a power of sale constitutes only a mortgage that must be foreclosed judicially—but there is no question here that the deed of trust unquestionably contained an explicit power of sale.

COMMENT 2: California courts have long embraced the principle that a mortgagor seeking to set aside a foreclosure sale must tender the mortgage debt as a condition precedent to equitable relief. This requirement has traditionally been "rationalized by the maxim that doing equity is a pre-condition to obtaining equitable relief." 2 Grant Nelson & Dale Whitman, Real Estate Finance § 7.22, at 880 (5th ed.). Nelson & Whitman have questioned the soundness of the tender requirement:

> The mortgagor is, by hypothesis, in default, and is probably in serious financial straits. The fundamental concept of foreclosure is that, despite his economic condition he is entitled to an orderly liquidation of the security in a manner consistent with law. It is plainly a violation of this concept to enjoin a wrongful foreclosure only if he can tender the balance owing on the debt; if he could do so, it is likely that no foreclosure would have been necessary. Of course, if the debtor wishes to redeem by tendering, that is his right, but he should not be compelled to exercise it in order to prevent an illegal foreclosure sale. [Id. at § 7.22, at 879.]

Further, even prior California court decisions have treated tender as unnecessary where the mortgagor's complaint is that the defect rendered the sale void, rather than voidable. *Dimock v. Emerald Properties LLC*, 81 Cal. App. 4th 868, 97 Cal. Rptr. 2d 255 (2000). Here, the Shusters did allege in their complaint that the defect rendered the deed of trust (and thus the foreclosure) void. Moreover, even though the court ultimately rejected their argument, it did acknowledge that the issue was one of first impression in California. As such, it seems dubious for the court to use the Shusters' lack of tender as an independent basis for dismissing their complaint.