

D049800

(Superior Court Case No. GIN035148)

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION ONE

JULIE PUENTES, an individual, KENNETH PUENTES, an individual,
on behalf of themselves, and all others similarly situated,

Plaintiffs/Appellants

v.

WELLS FARGO HOME MORTGAGE, INC.,
a corporation, and DOES 1 TO 100

Defendants/Respondents

On Appeal from the Judgment of the
SAN DIEGO COUNTY SUPERIOR COURT
The Honorable Michael Anello Presiding

Unfair Competition Case – Service on Attorney General and San Diego District
Attorney required by C.R.C. § 8.29 and Bus. & Prof. Code § 17209

**APPELLANTS' ANSWER TO THE BRIEFS OF AMICI
CURIAE CALIFORNIA BANKERS ASSOCIATION AND
MORTGAGE BANKERS ASSOCIATION**

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I. INTRODUCTION AND SUMMARY OF ANSWER

Tellingly, California Bankers Association (hereinafter "CBA") **"will not address any factual issues pertinent to whether Respondent's practices constituted a breach of the underlying agreement."** CBA Br. P. 4.¹ Instead, CBA asserts that banks need not comply with the terms of their own loan contracts where to do so would be "contrary to industry conventions." *Id.* Contrary to CBA's argument, however, industry conventions can never, as a matter of law, trump the express provisions of a loan contract.² Moreover, industry conventions specifically regarding calculation of loan interest are no defense to a UCL action based on violation of the terms of a loan contract. Chern v. Bank of America, 15 Cal. 3d 866, 876 (1976).

Without any supporting evidence, CBA repeats Wells' arguments that a UCL claim based on Wells systematic breach of the loan contract would have dire consequences for Wells and other mortgage lenders. CBA argues (1) that compliance

¹ Mortgage Bankers Association filed an amicus curiae brief on October 10, 2007 that is essentially a joinder in CBA's briefs and makes no additional points. All emphasis added and internal citations omitted unless otherwise states.

² A multitude of decisions hold that the systematic breach of consumer contracts violates the UCL, none of which are rebutted or even addressed by Wells or CBA. See e.g. Smith v. Wells Bank, 135 Cal. App. 4th 1463 (2005); Gibson v. World Savings & Loan Assn., 103 Cal. App. 4th 1291 (2002); State Farm Fire & Casualty Co. v. Superior Court, 45 Cal. App. 4th 1093, 1104 (1996); Allied Grape Growers v. Bronco Wine Co., 203 Cal. App. 3d 432, 449-453 (1988); People v. McKale, 25 Cal. 3d 626, 635 (1979); People v. Custom Craft Carpets, Inc., 159 Cal. App. 3d 676, 683-684 (1984).

with the terms of the note at loan payoff would prevent lenders from selling their loans on the secondary market; and (2) that lenders and servicers would have to develop new procedures. (Brief of CBA at pages 8-10). These arguments are not only pure speculation unsupported by any evidence in the record which have no place in the Appellate Court's review of an order granting summary judgment but are also false and misleading.

CBA simply repeats the arguments in Respondent's Brief, which remain unsupported by any evidence in the record. The true facts are that Wells and other loan originators and servicers have in place computer systems that can compute the correct amount due at loan payoff for a partial year. Moreover, correctly computing the amount due for a partial year would have no net effect on the amount received by the secondary market and therefore would not affect lenders' ability to sell loans. The secondary market and the federal government both direct the loan servicer to comply with the terms of the loan agreement. Given that the Amici have no dispute with the terms of the loan agreement, their unsupported hysteria rings hollow.

Accordingly, CBA's brief adds nothing to Respondent's position and the order granting summary judgment below should be reversed.

II. CBA MISSTATES APPELLANTS' CLAIMS, THE FACTS OF THE CASE, AND THE LAW

CBA misstates Appellants' claims. Appellants claim that Wells breached the express terms of the note when Wells charged Appellants interest at a rate of 6.549%

rather than the stated 6.500% as expressly specified in the terms of their note for the partial year of loan payoff and, as a result thereof, a prepayment penalty of \$71.98 in breach of the terms of the note. This practice of Wells, at loan prepayment, of charging Appellants interest in excess of the note rate for the partial year of payoff and thereby imposing a prepayment penalty is the basis for Appellants' claim.

Under settled case law, this systematic breach of the form contract is an unfair business practice within the meaning of Business & Professions Code § 17200 *et seq.* ("UCL"). Smith v. Wells Bank, *supra*, 135 Cal. App. 4th 1463; Gibson v. World Savings & Loan Assn., *supra*, 103 Cal. App. 4th 1291; State Farm Fire & Casualty Co. v. Superior Court, 45 Cal. App. 4th at 1104; Allied Grape Growers v. Bronco Wine Co., *supra*, 203 Cal. App. 3d at 449-453; People v. McKale, *supra*, 25 Cal. 3d at 635; People v. Custom Craft Carpets, Inc., *supra*, 159 Cal. App. 3d at 683-684. Further, because this practice is never disclosed, the practice is also deceptive.

CBA erroneously asserts that Regulation Z, requires Wells to charge Appellants interest in excess of the note rate and a prepayment penalty in the event of an early loan payoff. **This argument grossly misreads Regulation Z which is a disclosure law.**³ Indeed, Regulation Z expressly provides that "[t]he purpose of this regulation is to promote the informed use of consumer credit by requiring disclosures about its terms and cost... ..**The regulation does not govern charges for consumer**

³ Wells's own expert admitted that Regulation Z says nothing about loan prepayment. (Deposition of Thomas Lambert, p. 40, ln.2-7, at AA0512).

credit.” 12 C.F.R. § 226.1(b). TILA itself instructs borrowers to “see your contract documents for any additional information about nonpayment, default, any required repayment before the scheduled date, prepayment refunds and penalties, and creditor’s policy regarding assumption of the obligation.” (AA0661).

In fact, the federal agencies regulating lenders agree that this payoff amount is controlled by the terms of the note and applicable state contract law. (AA0639 and AA0671). In response to borrower complaints, the very agency responsible for Regulation Z, does not respond by stating that Regulation Z requires a certain payoff interest calculation. Instead, the agency directs the consumer to consult the “loan contract” and “state laws” to determine the appropriate method of calculating payoff interest. (AA0639). Appellants’ action based upon the loan contract and state contract case law is therefore fully consistent with Regulation Z and the views of the federal agencies.

CBA also ignores that Appellants’ claim involves early prepayment of a loan, which is not covered by the TILA payment schedule disclosed at loan inception or by Regulation Z. Wells charged Appellants interest for the partial year of payoff that exceeds the interest rate allowed by the terms of the note and thereby imposed a prepayment penalty. No federal agency or regulation requires, condones or excuses this breach of the loan contract. CBA fails to address these crucial facts and claims in this case.

III. CBA'S ASSERTIONS THAT CALIFORNIA LENDERS WOULD BE REQUIRED TO CHANGE THEIR COMPUTER SYSTEMS AND BE PRECLUDED FROM THE SECONDARY MARKET ARE UNSUPPORTED BY, AND CONTRARY TO, THE RECORD

CBA speculates about facts wholly outside of or contradicted by the record.

This is an appeal of summary judgment, and as such, only the record is relevant to determine whether Respondent established the absence of a triable issue of fact.

Appellate courts do not consider matters outside the record. Doers v. Golden Gate Bridge etc. Dist., 23 Cal.3d 180, 184, fn. 1 (1979); Kinney v. Overton, 153 Cal. App. 4th 482, 497 (2007). California Rules of Court rule 8.204(a), which requires citation to the record, applies to parties and amici alike. Because CBA fails to support their assertions with any citation to the record at all, CBA's arguments are waived and must be ignored as pure unsupported speculation. Id.

CBA argues that if Wells were required to comply with the terms of the contract, lenders and servicers would have to develop new procedures in California that would not conform with the practices in other states. There is no evidence in the record concerning the practices of lenders in calculating interest due on loan payoffs in other states and CBA cites no statute or case law from any other state which requires loan payoff interest to be calculated differently than as provided under Wells' mortgage contract and California law.

In fact, the evidence in the record belies CBA's claim that charging a borrower no more than the amount of interest actually due under a contract at loan payoff would be unduly burdensome to the lender. The evidence is that Wells already adjusts

the interest due and owing at payoff using the actual number of days elapsed for certain loans without disrupting the mortgage market or its ability to sell the loans to the secondary market. (AA 0529). As Wells' designated deponent testified, in such a case, **"We can expense our own cost on behalf of the borrower to pay the investor what is due..."** (Depo of Leo, p.22 AA0529).

CBA's argument that Wells and other lenders would have to acquire expensive new systems to calculate interest at loan payoff, is also unsupported by any evidence in the record is simply not true. Wells could not even make this argument in either in Wells' summary judgment motion or Respondents brief because Wells knows that Wells' current computers are already equipped to correctly calculate interest due at loan payoff.

CBA further argues that charging interest on loan prepayments as required by the loan contracts would expose Wells to claims by other borrowers who are currently undercharged as the result of Wells practices. (Brief of CBA at page 7). Respectfully, this is completer nonsense. Wells could incur no liability with respect to any borrowers if Wells were to honor the express terms of the loan contracts and charge the correct amount due on loan payoffs as required by the loan contracts. No borrower could complain simply because they would no longer receive an unearned windfall as the result of being undercharged.

CBA also asserts that if Appellants are allowed to sue Wells for breaching the express terms of the loan contract and Wells were required to comply with these

contractual obligations to borrowers, California lenders would be shut out from the secondary market. CBA, here again, parrots Wells' argument without any supporting evidence. Like Wells, CBA fails to cite any evidence that compliance with the terms of the Note would make the secondary market unavailable. That argument was pure speculation, without any evidentiary support, when raised by Wells and remains equally so when repeated by CBA.

CBA's speculation is also flatly refuted by Wells' own admission that in certain circumstances, Wells correctly calculates loan interest at payoff when the payoff occurs in early March. (Depo of Leo, p.22 AA0529) Wells' own practice with loans closing in early of March deviates from Wells' practice with other loans and the industry practice advocated by CBA. (AA 0529). Yet the secondary market still accepts Wells' loans and Wells' relationship with the secondary market is unaffected by such practices.

CBA's speculation also defies common sense because Wells' compliance with requirements of Wells' loan contracts would have no net effect on the secondary market. In other words, because loans are sold in bulk on the secondary market, any differences in payoff interest for individual loans would be netted out and the value of the loans to the secondary market purchaser would remain exactly the same in the event of a proper accounting.

In addition, the secondary market guidelines expressly permit lender's to adjust either their practices or their documents to insure compliance with all rules and

regulations. (AA0494-504). In fact, the secondary market guidelines recognize and expressly approve of variations in lending and servicing practices resulting from the need to comply with the applicable state laws:

We expect all Fannie Mae-approved lenders to be aware of, and in full compliance with, any and all federal, state or local jurisdictional regulations that apply to any of their selling or servicing business practices.

("Fannie Mae Guidelines", at p.156 , AA0494).

In some cases, the mortgage forms may have to be adapted to meet the lender's or local jurisdictional requirements.

("Fannie Mae Guidelines", at p.404, AA0496).

The FNMA/FHLMC Uniform Instruments provide for this amortization method, unless a different method is specifically required by the law of the State where the Mortgaged Premises are located.

("Freddie Mac Guidelines", at p.75-8, AA0504).

Finally, the Federal Reserve Board itself has stated in an official letter to a complaining borrower that the question of whether a payoff calculation was permissible is an issue of state law and is based upon the terms of the loan contract.

(AA0639 and AA0671).

IV. APPELLANTS DO NOT ASSERT THAT ANY PARTICULAR INTEREST CALCULATION IS REQUIRED FOR LOANS, ONLY THAT THE LENDER COMPLY WITH THE TERMS OF THE NOTE AT LOAN PAYOFF

Contrary to CBA's rhetoric, this case does not involve an attempt to have the trial court impose the court's own notions of fairness on banking practices or tell

banks how much interest they can charge and how the interest must be calculated. To the contrary, Wells is free to dictate the language in the loan contracts governing the interest rate and calculation of interest for loan prepayments and specify the interest rate and method of calculation. Wells, like everyone else however must comply with the terms of the written contract. Trial courts routinely enforce contractual obligations every day and such enforcement presents no novel policy issue as CBA asserts.

Where, as here, a borrower's claim is based on the lender's violation of a loan contract, the only obligations being enforced by the court are those voluntarily assumed by the parties. These voluntarily assumed contractual obligations are routinely enforced by the courts against banks. See e.g., Chern, supra, 15 Cal. 3d 866; .Smith v. Wells Bank, supra, 135 Cal. App. 4th 1463; Gibson v. World Savings & Loan Assn., supra, 103 Cal. App. 4th 1291.

Appellants' only claim is that they are entitled to payoff their loan, without a prepayment penalty, and without being charged more than the specified interest rate specified by their note. CBA attempts to justify Wells' interest overcharge by re-writing the terms of the Appellants' note in asserting that depending on the specific payoff date, the interest rate charged may be more than the yearly rate, the same as the yearly rate, or less. (Brief of CBA at page 7). **CBA thus admits that the Appellants are being charged a prepayment penalty "depending on the specific payoff date."**

According to the express terms of the Appellants' note, the interest charged may not exceed the specified rate of 6.5% and Appellants' may not be charged a prepayment penalty, regardless of the specific payoff date. The enforcement of the express terms of the contract should be the focus of the Court's decision as required by Chern, supra, 15 Cal. 3d 866.

Wells remains free to prospectively change the provisions of a new loan contract to provide for the interest calculation method Wells now uses and to disclose this method to its future borrowers. CBA, like Wells, loses sight of the important fact that this case does not seek to impose any new obligations on Wells but only seeks recovery of overcharges that violate contractual obligations Wells has elected to voluntarily include in the loan contract.

V. CONCLUSION

CBA's brief adds nothing to this appeal and provides no basis for affirming the trial court's ruling. Accordingly, Appellants respectfully submit that the order granting summary judgment should be reversed.

DATED: November 21, 2007

BLUMENTHAL & NORDREHAUG

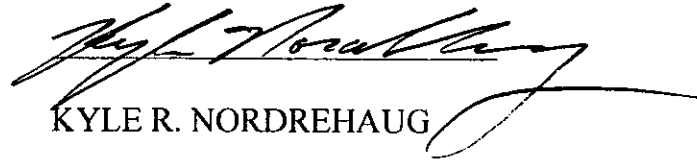
By: 

Norman B. Blumenthal
Attorneys for Appellants

CERTIFICATE OF WORD COUNT

The text of this brief consists of 2505 words as counted by the Corel WordPerfect version X3 word-processing program used to generate the brief.

Dated: November 21, 2007


KYLE R. NORDREHAUG

CERTIFICATE OF SERVICE

I, Kyle R. Nordrehaug, declare as follows:

I am employed in the County of San Diego, State of California. I am over the age of 18 and not a party to the within action. My business address is 2255 Calle Clara, La Jolla, California 92037.

On November 21, 2007, I served a copy of the following:

(1) APPELLANTS' ANSWER TO BRIEF OF AMICUS CURIAE BY
CALIFORNIA BANKERS ASSOCIATION AND MORTGAGE
BANKERS ASSOCIATION

X (BY U.S. MAIL): I caused each such envelope, with postage thereon fully prepaid, to be placed in the United States mail at San Diego, California. I am readily familiar with this firm's business practice for collection and processing of correspondence for mailing with the U.S. Postal Service pursuant to which practice the correspondence will be deposited with the U.S. Postal Service this same day in the ordinary course of business:

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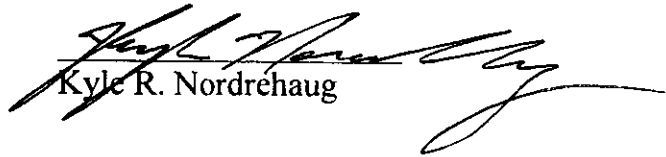
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I declare under penalty of perjury under the laws of the State of California that
the above is true and correct. Executed on November 21, 2007 at La Jolla, California.


Kyle R. Nordrehaug