Equitable Subrogation

A Shield to Protect the Lender's Interest

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There is a reoccurring story that plays out in the courts again and again arising out of real estate scams aiming to defraud the lender. The story, or some a variation of it, is all too familiar. The basic story line evolves along the lines of a recent California Court of Appeal decision, *Branscomb v. JPMorgan Chase Bank, N.A.*[1] While the lender has numerous potential remedies and defenses to claims sounding in fraud, the *Branscomb* decision reminds litigators that arguably one of the most powerful positions to be advanced by the lender is its right of equitable subrogation.

In *Branscomb v. JPMorgan Chase Bank, N.A.*, the Court of Appeal found that the lender was entitled to lien priority under the doctrine of equitable subrogation.[2] By way of background, in 2005, Navjot obtained a $5.1 million dollar refinance loan from Washington Mutual Bank (WaMu) secured by a first priority deed of trust encumbering his property.[3] In 2006, he obtained a $1.1 million dollar loan from MMB secured by a second priority lien.[4] In May 2007, Navjot obtained a $500,000 loan from Branscomb. The loan was negotiated through Branscomb's agent, Kirtikumar Monon, and was intended to be secured by a junior lien.[5] Due to Menon's negligence is preparing the documents, the deed

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to the resolution of a claim. See, *Insurance Code* Section 790.03 (h) (3) and *Fair Claims Settlement Process Regulations* Section 2695.7(d).

While the failure to notify a primary level insurer of a claim or potential claim will not operate to bar coverage *unless* the insurer has been substantially prejudiced thereby, it is better not to give the insurer any ammunition to deny your claim. Time passes rapidly – and only to the detriment of the insured.

In addition, if the title insurer accepts your claim, Section 2695.7(h) (2) of the *California Fair Claims Settlement Practices Regulations* requires, in pertinent part, that "[u]pon acceptance of the claim in whole or in part and, when necessary, upon receipt of a properly executed release, every insurer . . . shall immediately, but in no event more than thirty (30) calendar days later, tender payment or otherwise take action to perform its claim obligation . . . (2) Any insurer issuing a title insurance policy shall either tender payment pursuant to subsection 2695.7(h) or take action to resolve the problem which gave rise to the claim immediately upon, but in no event more than thirty (30) calendar days after, acceptance of the claim."

The earlier your claim is tendered, the earlier your claim may be accepted and the insurer required to resolve your claim.

What To Do If Your Claim Is Denied

If a title insurance claim is denied, do not take "no" for an answer. Experienced coverage counsel may be able to convince the title insurer that its denial was wrongful or in bad faith and that coverage should be afforded. If the title insurer changes its coverage determination, the insurer is liable to its insured for the attorneys' fees and costs incurred by the insured post-tender. *See, Hogan v. Midland National Ins. Co.* (1970) 3 Cal.3d 553, 558 (holding that an insurer that breaches its duty to defend its insured is liable to its insured for all costs and attorneys' fees incurred).

If the title insurer does not change its coverage determination, a lawsuit should immediately be filed against the insurer. An insurer that, in bad faith, withholds policy benefits due to its insured, is liable for the insured's attorneys' fees and litigation expenses which are reasonably incurred in obtaining those benefits. *See, Brandt v. Superior Court* (1985) 37 Cal.App.3d 813, 819 and *White v. Western Title Insurance Company* (1985) 40 Cal.3d 870, 890.

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of trust erroneously specified the amount as $100,000 and was not recorded until August 30, 2007.[6] In December 2007, Navjot refinanced with WaMu and the proceeds paid off the existing first priority deed of trust.[7] This was consistent with WaMu's instructions that its deed of trust be a first priority lien and MMB's agreement that its deed of trust would remain in a second position.[8] Through the refinance escrow, Branscomb's agent, Menon, provided escrow with a zero balance pay-off demand , reconveyance of the deed of trust as well as the original promissory note and deed of trust.[9] Based on these documents, escrow closed without paying any monies to Branscomb.[10] Evidentially, Menon forged Branscomb's name on the pay-off demand and reconveyance. A lawsuit followed in which Branscomb sought to enforce his deed of trust as a senior lien with priority over WaMu

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and MMB.[11] The trial court denied the lender's equitable subrogation rights.[12]

The Court of Appeal reversed and, in doing so, provided an overview of the application of the doctrine of equitable subrogation.[13] As the name implies, the relief sounds in equity. Equitable subrogation exists not to vindicate a wrong, but to prevent unconscionable and inequitable assertion of rights resulting in unjust enrichment.[14] At its essence, the doctrine of equitable subrogation permits a lender who pays off a prior existing encumbrance to protect its interest, with the intention that the lender's lien will assume the bargained-for priority position, to assume the same priority position as the holder of that prior existing encumbrance in the event its security is deemed invalid or inferior.[15] The prerequisites for equitable subrogation can be generally summarized as follows: (1) payment must have been made by the subrogee to protect his own interest; (2) the subrogee must not have acted as a volunteer; (3) the debt paid must be one for which the subrogee was not primarily liable; (4) the entire debt must have been paid; and (5) subrogation must not work any injustice to the rights of others.[16]

Furthermore, in exercising its equitable jurisdiction, courts will look to the intentions of the parties.[17] To that end, equitable liens are looked upon with favor by the courts where equity will generally "give a lender the security for which he bargained in the situation where there is a mistake or fraud with respect to an intervening right which cuts off a preexisting encumbrance which has been satisfied by the loan proceeds."[18] Of caution, however, the lender's equitable subrogation rights may be comprised if the lender is found to be chargeable with culpable and inexcusable neglect.[19]

In confirming WaMu's equitable subrogation rights, the court held that the application of the equitable subrogation doctrine gave the parties "what they expected."[20] WaMu expected to receive a first priority lien which was a prerequisite to its loan, and Branscomb's lien continued to occupy a junior position which is what he bargained for when he made the loan.[21] The court found that WaMu's reliance on the purportedly forged zero pay-off demand and reconveyance did not establish "culpable and inexcusable neglect by the lender defendants that would justify denial of equitable subrogation."[22] A victory for the lender thanks to the court's exercise of its equitable jurisdiction.

1 No. A137140, A138144, 2014 WL 346621 (Cal. Ct. App. January 31, 2014).
2 *Id.* at *4.
3 *Id.* at *1.
4 *Id.*
5 *Id.*
6 *Id.*
7 *Id.* at *2.
8 *Id.*
9 *Id.*
10 *Id.*
11 *Id.*
12 *Id.* at *2.
13 *Id.* at *2-3.
14 *Id.* at *3; *Farmers Ins. Exchange v. Smith* (1999) 71 Cal.App.4th 660; *Mortgage Guarantee Co. v. Hammond Lumber Co.* (1936) 13 Cal.App.2d 538; *Jones v. Sacramento Savings and Loan* (1968) 248 Cal. App.2d 522.
15 Civ. Code § 2876; *Branscomb, supra,* at *3; *JPMorgan Chase Bank, N.A. v. Banc of America Practice Solutions, Inc.* (2012) 209 Cal.App.4th 855, 860; *Katsivalis v. Serrano Reconveyance Company* (1977) 70 Cal. App.3d 200, 210; *Smith v. State Savings and Loan Association* (1985) 175 Cal.App.3d 1092, 1096; *Han v. United States of America* (1991) 944 F.2d 526, 528.
16 *Branscomb, supra,* *3; *Caito v. United California Bank* (1978) 20 Cal.3d 694, 704.
17 *Branscomb, supra,* at *6; *JPMorgan Chase Bank, N.A., supra,* 209 Cal.App.4th at 862.
18 *Branscomb, supra,* at *6; *JPMorgan Chase Bank, N.A., supra,* 209 Cal.App.4th at p. 861; *Katsivalis v. Serrano Reconveyance Co., supra,* 70 Cal.App.3d at p. 211.
19 *Branscomb, supra,* at *3, 5; *JPMorgan Chase Bank, N.A., supra,* 209 Cal.App.4th at 860; *Simon Newman Co. v. Fink* (1928) 206 Cal. 143, 146; *Lawyers Title v. Feldsher* (1996) 42 Cal.App.4th 41.
20 *Branscomb, supra,* *5.
21 *Id.*
22 *Id.*