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Supreme Court of California
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IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

KWANG K. SHEEN,

Plaintiff and Appellant,

v.

WELLS FARGO BANK, N.A.,

Defendant and Respondent.

Case No. S258019

California Court of Appeal,
Second District, Division Eight, No. B289003

Los Angeles Superior Court, No. BC631510
The Honorable Robert L. Hess, Judge

ANSWERING BRIEF ON THE MERITS

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INTRODUCTION

This case presents the question whether a lender has a general duty of care to avoid causing economic loss to a borrower with whom it is in contractual privity, when that borrower seeks to renegotiate their loan contract. Petitioner Kwang Sheen asked Respondent Wells Fargo Bank, N.A. to renegotiate the terms of such a contract, by considering a mortgage modification application. Wells Fargo chose not to agree to a modification, as Sheen concedes was its right. But Sheen contends that Wells Fargo failed to exercise due care in the process, sending him letters that did not state (but nonetheless led him to believe) that nobody would ever foreclose on the house securing the loan. Years later, long after Wells Fargo sold Sheen's defaulted loan, the new owners of the loan foreclosed.

That is the story of an unsuccessful contract negotiation in an intensely regulated field. Were the facts otherwise, it might have been the story of a regulatory violation, or negligent misrepresentations, or even promises made, relied upon, and later broken. Causes of action exist to remedy such wrongs, but Sheen did not assert them against Wells Fargo. Instead, he asks for something novel and additional: A general duty of care by a lender to avoid causing economic loss to a borrower.

No such duty exists. The reason is a simple and settled feature of the economic loss rule: When parties have a contract, that contract governs their rights and obligations with respect to the contract. Layering negligence law over contractual promises upsets the contract's allocations of risks and responsibilities.

Moreover, much of the supposed reform Sheen seeks already exists in detailed regulations that balance competing considerations such as protecting homeowners, preserving access to mortgage lending, ensuring lenders' solvency, and respecting private agreements. This field is an unusually poor candidate for regulation-by-tort because expert policymakers have shown the ability and willingness to make clear rules and hard policy judgments based on empirical evidence—and to revise them as circumstances warrant. Courts and tort juries are not well-situated to second-guess those judgments. Indeed, recognizing an open-ended duty of care here could very well harm rather than help homeowners, because a lender's surest way to avoid liability for negligence in negotiating a loan modification is to not negotiate loan modifications at all.

The areas where this Court has recognized concurrent tort and contract liability are few and far between. Sometimes, the tort is unrelated to the contract. That is impossible here, because the supposed tort occurred in renegotiating the loan contract itself. Other times, the Court has recognized a tort to underscore the special social harm that comes from certain breaches of contract, such as fiduciaries' failures to perform professionally or insurance companies' bad faith denials of coverage. But lenders are not borrowers' fiduciaries, nor their insurers; they are simply ordinary creditors of ordinary debtors. That is why, as the Court of Appeal put it, "the overwhelming supermajority of states" would reject Sheen's tort claim. (C.A. Op. 13.)

Sheen bucks this common law consensus. He argues that mortgage modification practices suffer from a lack of care, criticizing various practices and shortcomings of loan servicers (none of which actually transpired here). But other causes of action already address many of these issues. What Sheen calls gaps in those causes of action are actually vital limitations that this Court should not paint over with a broad-brush negligence duty.

Sheen further argues that *Biakanja v. Irving* (1958) 49 Cal.2d 647, nonetheless requires recognizing a duty here, as an exception to the economic loss rule. His reliance on *Biakanja* is triply misplaced. First, *Biakanja* helps identify when a third party is sufficiently close to a transaction that the defendant owes that stranger a duty of care. The test is about parties *without* a direct relationship; this Court has never treated it as a justification for adjusting the duties of two parties (like Sheen and Wells Fargo) that *do* have a direct relationship. Second, *Biakanja* concerns the negligent performance of a preexisting obligation—say, a contract or statutory duty—not the judicial invention of new obligations. Here, Sheen points to no preexisting obligation that Wells Fargo failed to perform. And third, apart from these categorical limits and even accepting that the *Biakanja* factors applied, they would weigh decisively against recognizing a duty. The painful foreclosure Sheen experienced was disconnected from Wells Fargo's conduct as a matter of policy and as a matter of fact. No basis exists to recognize the new negligence duty that Sheen proposes.

STATEMENT OF FACTS

1. Sheen alleges as follows: In December 1998, he purchased a house financed with a loan secured by the property (First Loan). (Second Am. Compl. (SAC) ¶6.) That loan is not at issue in this case, and, contrary to Sheen's statement to this Court (Br. 11), was not a Wells Fargo loan. Rather, in 2005, years after Sheen had purchased the property, he chose to borrow against his home equity through two loans from Wells Fargo (the Second Loan and Third Loan). (SAC ¶¶7-8.)

In the wake of the 2008 financial crisis, Sheen's financial difficulties caused him to miss payments on the Second and Third Loans. (SAC ¶9.) In 2009, Wells Fargo recorded a notice of default on the Second Loan and scheduled a foreclosure sale for February 3, 2010. (SAC ¶¶9-10.)

In late January 2010, Sheen (with legal assistance) contacted Wells Fargo about cancelling the foreclosure sale so that his loans could be considered for modification. (SAC ¶11.) On January 28, 2010, Wells Fargo emailed Sheen's representative that it "is aware of the Feb. 3 foreclosure sale date and is currently working on this matter." (*Ibid.*) The next day, Sheen submitted applications to modify the Second and Third Loans. (SAC ¶12.) The February 3 foreclosure sale was cancelled. (SAC ¶13.) Although Sheen's brief in this Court suggests otherwise (*e.g.*, Br. 11), the operative complaint does not allege that Wells Fargo accepted or agreed to consider Sheen's loan modification applications, or that it would enter into modification negotiations. (*See* SAC ¶¶14, 18.)

Sheen next heard from Wells Fargo on March 17, 2010, in letters regarding the Second Loan and Third Loan, stating that "[d]ue to the severe delinquency of your account, it has been charged off" (SAC ¶¶15-16), *i.e.*, that Wells Fargo had reclassified it as a bad debt (*see* Office of the Comptroller of the Currency, *Dictionary of Banking Terms and Phrases* s.v. Charge-off, https://www.helpwithmybank.gov/dictionary). The letters further stated that "the entire balance has been accelerated" such that "your entire balance is now due and owing." (SAC ¶¶15-16.) The letters continued that "[a]s a result of your account's charged off status," Wells Fargo would "proceed with whatever action is deemed necessary to protect our interests," including "referring your account to an Attorney." (*Ibid.*) The letters requested that Sheen call immediately with questions. (*Ibid.*)

Sheen allegedly interpreted these letters as approvals of his applications for a mortgage modification. (SAC ¶19.) He allegedly believed these letters meant "that Wells Fargo was not permitted to sell the Property at a non-judicial foreclosure sale" (SAC ¶20) and "that the Property would never be sold at a foreclosure auction in connection with either the Second or Third Loan" (SAC ¶19). Sheen allegedly interpreted a subsequent similar letter in the same way. (*See* SAC ¶¶23-24.) The operative complaint does not allege that the letters expressly stated anything about future foreclosure (nor does it attach the letters).

Also in March 2010, a bank representative spoke with Sheen's wife. Consistent with Wells Fargo's cancellation of the

February 3 sale, the representative told Ms. Sheen "that there would be no more foreclosure sale." (SAC ¶22.) Although Sheen's brief in this Court suggests otherwise, the operative complaint does not allege that the representative "promised him that he and his wife would *never* lose their house" or "said the home would never be sold" (Sheen Br. 11, 47).

Wells Fargo sold its interest in the Second Loan in November 2010. (SAC ¶28.) Separately, it discharged Sheen's debt on the Third Loan in March 2014. (SAC ¶¶25, 29.) As of mid-2014, Mirabella Investments Group, LLC (Mirabella) was the beneficial owner and FCI Lender Services, LLC (FCI) the servicer on the Second Loan. (SAC ¶¶29-30, 35.) During 2014, Sheen submitted additional applications for a mortgage modification to Mirabella and FCI. (SAC ¶¶34, 36, 37, 39, 41.) The Second Loan was never modified. Mirabella recorded a notice of default (SAC ¶¶31-32), and Sheen's property was sold at a trustee's sale in October 2014 (SAC ¶49).

2. Sheen sued Wells Fargo, Mirabella, and FCI. The operative complaint alleges three causes of action against Wells Fargo: negligence, intentional infliction of emotional distress, and violation of Bus. & Prof. Code, § 17200 *et seq*. The trial court sustained Wells Fargo's demurrer.

3. The Court of Appeal (per Wiley, J.) affirmed, holding that "a lender does not owe a borrower a common law duty to offer, consider, or approve a loan modification." (C.A. Op. 16.) It "beg[an] by noting the claims Sheen did *not* bring": six possible statutory claims, and common-law claims for breach of contract, negligent misrepresentation, promissory estoppel, and fraud. (C.A. Op. 7.) The Court understood the absence of such claims to reflect counsel's view that they "did not or could not offer [Sheen] the type of relief he wanted." (*Id.* at 7-8.)

Analyzing the negligence claim, the Court of Appeal noted disagreement over whether lenders owe borrowers a general duty of care under California law when negotiating a loan modification. (*See* C.A. Op. at 8-9.) The Court explained that those disparate results arose from divergent applications of *Biakanja*. (*See ibid.*) The Court concluded that courts finding no duty in this context had "correctly analyzed the *Biakanja* factors." (*Id.* at 9.) But "[r]ather than rely on this debatable test alone," the Court of Appeal sought guidance from this Court's "latest word" on tort duties in *Southern California Gas Leak Cases* (2019) 7 Cal.5th 391 (*SoCalGas*). (C.A. Op. 9.)

"One fundamental consideration" in *SoCalGas* "was that economic losses flowing from 'a financial transaction gone awry' are 'primarily the domain of contract and warranty law or the law of fraud, rather than of negligence.'" (C.A. Op. 9 [quoting *SoCalGas*, *supra*, 7 Cal.5th at p. 402].) That described this case: Sheen's purely economic injuries, the Court of Appeal explained, allegedly flowed from "a financial transaction gone awry and nothing more." (*Id.* at 10.)

Following *SoCalGas*, the Court of Appeal also looked to other jurisdictions' approaches and the Restatement of Torts. "[A]t least 23 states have refused to impose tort duties on lenders about loan modifications" (C.A. Op. 10; *see id.* at 10-12 [collecting cases]), while at most two States—Arizona and Mississippi—might impose a duty in this context (*see id.* at 12-13 [noting "uncertainty" about even these States]). The Restatement likewise counseled against imposing a duty: "'[T]here can be no liability in tort for economic loss caused by negligence in the performance or *negotiation* of a contract between its parties.'" (*Ibid.* [quoting Rest.3d Torts, Liability for Economic Harm (Tent. Draft No. 1, Apr. 4, 2012), § 3].) "Logic," the Court added, "points to the same conclusion": It would be "'strange to impose a negligence duty on lenders to carefully review modification applications when there is no such tort duty to *approve* applications as a result of that review.' [citation]." (*Id.* at 15.)

Finally, the Court of Appeal noted that *SoCalGas* had relied on "the ability of legislatures to craft remedies beyond the ken of courts." (C.A. Op. 16.) "Legislatures have been active" in this field, the Court explained, but have created regulations that are "designedly limited in time and scope" to avoid increasing costs or decreasing the availability of mortgages or modifications. (*Ibid.*) Future legislatures can both "craft broadly acceptable compromises and…experimental pilot programs" and "adjust policy swiftly in the face of change and experience." (*Ibid.*) "Courts," by contrast, "can do none of these things well." (*Ibid.*)

STANDARD OF REVIEW

"The existence of a duty…is a question of law" reviewed de novo. (*Wiener v. Southcoast Childcare Centers, Inc.* (2004) 32 Cal.4th 1138, 1146.)

ARGUMENT

"[L]iability in negligence for purely economic losses…is the exception, not the rule." (*SoCalGas*, *supra*, 7 Cal.5th at p. 400.) Departing from that rule is unwarranted here for three reasons that are deeply rooted in both doctrine and policy. *First*, Wells Fargo and Sheen had a loan contract, and that contract should govern their rights and obligations. Courts have long been very reluctant to layer a general duty of care atop contract duties, because doing so would disrupt contracts' predictability and frustrate parties' expectations. *Second*, legislatures and regulators have been unusually attentive to the complex and technical mortgage-modification field. Their efforts, along with recognized common-law causes of action other than negligence, are calibrated to protect borrowers while remaining sensitive to competing policy concerns, such as ensuring access to mortgage lending. The general duty Sheen seeks would upset those fine balances. *Third*, considering the challenged conduct, that conduct's connection to Sheen's injury, and the consequences of recognizing a duty, the policy balance weighs decisively against imposing a duty.

I. General Negligence Principles Do Not Govern Mortgage Modification Because the Relationship Between Borrower and Lender Is Contractual

A. Under the economic loss rule, a borrower's rights and obligations related to a loan are determined by contract, not tort

1. Parties to a contract are generally barred from pursuing a tort action for economic loss related to the subject matter of the contract. (*See* Rest.3d Torts, Liab. for Econ. Harm

§ 3 (*Restatement*) [subject to enumerated exceptions, "there is no liability in tort for economic loss caused by negligence in the performance or negotiation of a contract between the parties"].) This principle is one strand of the so-called "economic loss rule." (*See infra*, pp. 30-32.)

As a leading commentator explains, the rule recognizes that, when two parties enter into a contract, their contract "allocat[es] the relevant economic risks." (Dobbs, Law of Torts (2d ed. 2019) § 608 (*Dobbs*).) That contract, accordingly, determines whether and how liability follows when such risks are realized. Superimposing "tort liability for those risks would undermine the parties' contractual ordering of responsibilities." (*Ibid.*) Indeed, such tort liability strikes at the very premise of contract law—that parties generally should be free to reach voluntary agreements about their rights and obligations. Thus, the economic loss rule "protects the bargain the parties have made," allowing them "to make dependable allocations of financial risk without fear that tort law will be used to undo them later." (*Restatement* § 3, com. b.) More broadly, the rule "prevents the law of contract and the law of tort from dissolving one into the other." (*Robinson Helicopter Co. v. Dana Corp.* (2004) 34 Cal.4th 979, 988 [citation and alteration omitted]; *Restatement* § 3, com. b ["[T]he rule prevents the erosion of contract doctrines by the use of tort law to work around them."].)

This rule gives way only when a party violates a duty "independent" of the contract. (*Cf. Erlich v. Menezes* (1999) 21 Cal.4th 543, 551.) Contract law "protect[s] the interest in having promises performed," while tort law "protect[s] the interest in freedom from various kinds of harm." (*Freeman & Mills, Inc. v. Belcher Oil Co.* (1995) 11 Cal.4th 85, 105 [citation omitted].) What harm tort protects against is determined "based primarily on social policy," rather than the parties' agreement. (*Ibid.*) As explained below (*see infra*, pp. 26-30), simple negligence in negotiating the modification of a loan contract does not violate any such social policy.

2. Applying those principles here, a borrower can (if the facts warrant) pursue a contract claim, but not a negligence claim. When Sheen chose to borrow against his property by taking out the Second Loan, he made a contract with Wells Fargo. That contract "allocat[ed] the relevant economic risks" (*Dobbs* § 608) between the parties. In particular, Wells Fargo accepted the risk that Sheen might not repay the loan. Conversely, Sheen accepted the risk of foreclosure under that circumstance. Ultimately, Sheen's failure to perform led to foreclosure. Absent an independent duty—one that is both independent of the loan contract yet governs negotiations to modify it—longstanding doctrine cuts sharply against frustrating the parties' bargain by bringing tort law to bear here.

The same result would follow even if Wells Fargo had not been the original lender (as in the fact patterns of some other cases confronting the issue presented here). Loan agreements typically permit the originating lender to assign its beneficial interest or its servicing obligations to others (as Wells Fargo eventually did here (SAC ¶28)). Under those circumstances, the successor would assume the relevant rights and obligations of the originating lender (*see* 1 Witkin, *Summary of California Law* (11th ed. 2019) Contracts § 763) or be treated as the agent of the original lender (*see* Civ. Code, § 2920.5, subd. (a); *Daniels v. Select Portfolio Servicing, Inc.* (2016) 246 Cal.App.4th 1150, 1172). Either way, the borrower could continue to enforce contractual promises, and the reason for prohibiting tort recovery remains: The borrower and lender had an opportunity to determine what risks each would accept under the loan agreement.

3. Sheen agrees that the economic loss rule "generally bars extra-contractual recovery of economic losses where there is privity of contract between the parties *and* the plaintiffs' losses arise solely out of a contractual breach." (Sheen Br. 52.) But he denies the rule's application here because "he does *not* claim" Wells Fargo's conduct "violated any contractual duty." (*Ibid.*)

Such an approach—heads-I-sue-in-contract, tails-I-sue-in-tort—would gut the economic loss rule. Sheen does not explain why a lender like Wells Fargo that has *fulfilled* its contractual promises should face greater liability than a lender that has *breached* them. The policy of the rule is to prevent tort's "interference with an allocation of risk made by the parties." (*Restatement* § 3, com. c.) That policy is served—regardless of whether the contract is performed or breached—by barring any "tort claim [that] creates a risk of interference with an allocation of risk made by the parties." (*Ibid.*)

Sheen's approach would be especially unworkable because contractual "silence may itself serve as an allocation" of risk. (*Restatement* § 3, com. c.) Parties bargain both by *including* obligations in their contract and by *omitting* them. As Dean Ward Farnsworth, the Reporter for the *Restatement*, explains, "[p]arties wrangle over integration clauses to make clear that their obligations are the ones stated in the contract and nothing else; the point of bothering about such matters becomes unclear if a disappointed party can later invoke an outside set of obligations that are imposed on the promisor and defined by the law of tort." (Farnsworth, *The Economic Loss Rule* (2016) 50 Val. U. L.Rev. 545, 553-554 (Farnsworth); *see Applied Equip. Corp. v. Litton Saudi Arabia Ltd.* (1994) 7 Cal.4th 503, 517 ["When two parties make a contract, …it is appropriate to enforce only such obligations as each party voluntarily assumed, and to give him only such benefits as he expected to receive; this is the function of contract law." [citation and alteration omitted]].)

Sheen's claim plainly falls within "the contract's scope" (*Restatement* § 3, com. c). Parties entering a loan contract with definite promises have quite obviously *omitted* a commitment to scrap those promises and replace them with unspecified future terms. The relatively few contracts that contemplate renegotiations when certain contingencies arise are explicit; for example, a loan contract could expressly require a lender to evaluate modifications under specified circumstances and with a particular level of care. Such a promise could be breached, and could be enforced through a contract claim by a borrower against a lender. But here, Wells Fargo undertook no such obligation, and Sheen cannot instead require compliance with that same obligation through tort.

For that reason, Sheen is mistaken in attempting to distinguish some of the cases cited below on the ground that they involved contractual duties (*see* Sheen Br. 58-59). As the Court of Appeal recognized, those cases support Wells Fargo because they correctly reason that any claims related to mortgage servicing necessarily fall within the scope of the loan contract. (*See Wigod v. Wells Fargo Bank, N.A.* (7th Cir. 2012) 673 F.3d 547, 568 ["To the extent Wells Fargo had a duty to service [the] home loan responsibly and with competent personnel, that duty emerged solely out of its contractual obligations."]; *Srok v. Bank of Am.* (E.D.Wis. Nov. 6, 2015, No. 15-CV-239) 2015 WL 6828078, at *8 [explaining that any "duty of care in accepting and processing [plaintiffs'] loan modification paperwork…emerged solely out of [the lender's] contractual obligations"]; *Henderson v. Wells Fargo Bank, N.A.* (N.D.Tex. 2013) 974 F.Supp.2d 993, 1011 [holding that "negligence claim fails because [the] only alleged injury is the economic loss to the subject matter of the contract at issue"].)

In short, Sheen's proposed duty in negligence would impose new obligations on how Wells Fargo performed in its contractual relationship with Sheen—obligations that it did not undertake in contract. That duty would "affirmatively interfere" with that contract, making it "a less dependable instrument for settling commercial relations with finality." (Farnsworth, *supra*, at p. 553.) The economic loss rule thus bars that proposed duty.

B. Negligence in renegotiating loan terms does not violate any duty independent of the loan contract

Courts have, of course, recognized certain duties "independent" of contract that exist between parties to a contract. But a survey of the duties recognized by this Court reveals nothing remotely resembling a duty to negotiate or process a loan modification to avoid purely economic harm.

1. Tort law presumptively imposes a duty of care to avoid causing "traditionally compensable forms of injury—like physical harm to person or property." (*SoCalGas*, *supra*, 7 Cal.5th at p. 398.) Thus, when a "breach of contract also involves physical injury…the action will generally sound in tort." (*Freeman*, *supra*, 11 Cal.4th at p. 107.)

Sheen alleges no harm to person or property.

2. Tort law also imposes an obligation to refrain from intentional wrongful conduct. Thus, where a contract "breach is accompanied by a traditional common law tort, such as fraud or conversion" or "the means used to breach the contract are tortious, involving deceit or undue coercion," courts have recognized a tort claim despite the existence of a contract. (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 990.) "Focusing on intentional conduct gives substance to the proposition that a breach of contract is tortious only when some independent duty arising from tort law is violated." (*Erlich*, *supra*, 21 Cal.4th at p. 554.) By contrast, "[i]f every negligent breach of a contract g[ave] rise to tort damages the limitation would be meaningless, as would the statutory distinction between tort and contract remedies." (*Ibid.*)

Sheen's negligence claim implicates no intentional conduct that would trigger this exception.

3. Courts have recognized certain "special relationships" that support a tort action for economic damages despite the existence of a contractual relationship. This Court has held that in certain *direct* relationships (often involving particular types of contracts), a "special relationship" exists such that public policy dictates heightened obligations regardless of the parties' agreement. (*See, e.g.*, *Erlich*, *supra*, 21 Cal.4th at pp. 552-553 [discussing insurer-insured relationship]; *Foley v. Interactive Data Corp.* (1988) 47 Cal.3d 654, 682-685 [same].) Significantly, this Court has also used the term "special relationship" in a different context, to describe the relationship between a party to a transaction and a *third* party who brings suit as "an intended beneficiary of [the] particular transaction." (*SoCalGas*, *supra*, 7 Cal.5th at p. 400 [citing *Biakanja*].) But these two different uses come from two different contexts and are not interchangeable. (*See Foley*, *supra*, at pp. 684-685 [analyzing whether parties in direct relationship had "special relationship" without reference to *Biakanja*]; *Erlich*, *supra*, at pp. 552-553 [same].)

Sheen ignores cases like *Foley* and *Erlich*, instead invoking *Biakanja* to argue that he and Wells Fargo are in a "special relationship" justifying an independent duty. But that argument is wordplay: It conflates the two different meanings of "special relationship" noted above, when, under this Court's cases, only the former has relevance for parties in a direct relationship. Neither logic nor precedent supports transplanting the test from one area into the other merely because the Court has happened to use the same shorthand in both contexts.

No independent duty based on a special relationship exists here. The most familiar relationships justifying an independent duty are contracts for professional services, often with fiduciary characteristics: When a client hires a professional, such as an attorney, doctor, or accountant, the client's contract is no bar to a malpractice action. (*See Restatement* § 4; *Neel v. Magana, Olney, Levy, Cathcart & Gelfand* (1971) 6 Cal.3d 176, 181 ["legal malpractice generally constitutes both a tort and a breach of contract"].) Similarly, this Court has recognized that features of the relationship between insurer and insured favor allowing an insured to pursue a tort action where the insurer breaches the implied covenant of good faith and fair dealing. (*See Foley*, *supra*, 47 Cal.3d at p. 684.) But this was "a major departure from traditional principles of contract law." (*Id.* at 690.)

Wells Fargo and Sheen do not have a special relationship. To begin, the recognized examples of special relationships are distinguishable because in each, the premise of the tort is that there is *also* a contractual breach: In the insurance context, "a bad faith claim cannot be maintained unless policy benefits are due." (*Waller v. Truck Ins. Exch., Inc.* (1995) 11 Cal.4th 1, 36 [quoting this principle with approval in context of contract claim]; *Foley*, *supra*, 47 Cal.3d. at p. 684 [same for tort].) In the professional negligence context, an individual hiring a professional to perform a task "invariably" contracts for performance with due care, and that failure is a breach. (*See* Farnsworth, *supra*, at p. 560-561; *Restatement* § 4, com. a.) Given the nature of such professional relationships, there is a "social interest" in recognizing that obligation (Farnsworth, *supra*, at p. 560), allowing it to be brought as either a contract or a tort claim. But the underlying obligation still coincides with the contract. Here, by contrast, Sheen admits that he got what he contracted for. Indeed, it was Sheen, not Wells Fargo, who breached the contract when he defaulted on his payments.

More generally, there is nothing "special" about the relationship between a lender and a borrower seeking to modify a debt. "No fiduciary duty exists between a borrower and lender in an arm's length transaction." (*Ragland v. U.S. Bank Nat'l Ass'n* (2012) 209 Cal.App.4th 182, 206.) Unlike a fiduciary, which must "subordinate its interests to act on behalf of and for the benefit of another," a bank "is entitled to pursue its own economic interests in a loan transaction." (*Nymark v. Heart Fed. Sav. & Loan Assn.* (1991) 231 Cal.App.3d 1089, 1093 n.1; *see Downey v. Humphreys* (1951) 102 Cal.App.2d 323, 332 ["A debt is not a trust and there is not a fiduciary relation between debtor and creditor as such."].) The banking system would seize up if creditors owed fiduciary-like tort duties to debtors seeking to modify their ordinary debts.

For this reason, a lender owes no extra-contractual duty of care when its "involvement in the loan transaction does not exceed the scope of its conventional role as a mere lender of money." (*Nymark*, *supra*, 231 Cal.App.3d at p. 1096; *see ibid.*

[“Liability to a borrower for negligence arises only when the lender ‘actively participates’ in the financed enterprise ‘beyond the domain of the usual money lender.’” [citation omitted]]; *Wagner v. Benson* (1980) 101 Cal.App.3d 27, 35.) Deciding whether to adjust the terms of an existing loan has long been one of the mortgagee’s ordinary roles. (*See* Congressional Oversight Panel, December Oversight Report: A Review of Treasury’s Foreclosure Prevention Programs (Dec. 2010) pp. 6-7.)

C. *Biakanja* is not a basis for imposing new duties on parties to a contract

Sheen’s principal argument for an exception to the economic loss rule relies on this Court’s six-factor test from *Biakanja*. Although that argument fails on its own terms (*see infra*, pp. 54-66), it is unsound for a more fundamental reason: *Biakanja*’s test is irrelevant here because this Court neither created it, nor has used it, as an exception to the aspect of the economic loss rule that respects bilateral contractual bargains.

1. The “economic loss rule” bundles together several “discrete doctrines that regulate the ability of a plaintiff to recover in tort for pure money losses caused by negligence.” (Farnsworth, *supra*, at p. 546.) Because those different doctrines have different rationales, “it is important to distinguish [between] two patterns.” (*Dobbs* § 608.)

First is the so-called “contract rule” explained above: When two parties *do* have a contract, that contract generally controls any liability for economic loss. Second is the so-called “stranger rule”: Because recognizing tort liability for economic loss as between two “strangers” who *do not* have a contract “may involve concerns about unpredictable and limitless liabilities," there is generally no tort duty to avoid causing such harm. (*Dobbs* § 608; *SoCalGas*, *supra*, 7 Cal.5th at p. 401 [explaining that, unlike with respect to physical harm, "mere foreseeability" does not "set[] meaningful limits on liability" in cases of economic harm].) These two principles end in the same place (no tort duty for economic loss), but they begin with diametrically opposite fact patterns (where the plaintiff and defendant either do or do not have a contract).

With different rationales, these doctrines have different exceptions. The contract rule posits that contracts appropriately allocate economic risk. If that is doubtful—for example, where the contract was fraudulently induced or reflects a fiduciary relationship (*see supra*, pp. 27-28)—then the contract rule may give way. The stranger rule, by contrast, is wary of boundless and unforeseeable liability. If that concern is absent—for example, where the "stranger" has intimate ties to a particular transaction—then the stranger rule may give way.

But these exceptions are not mix-and-match. It would make no sense to ask whether a contract sufficiently allocates risks between an alleged tortfeasor and a stranger—they have no contract. And conversely, the contract rule would be swallowed up by an exception triggered by the truism that permitting a tort action between two contracting parties would not risk "countless people" bringing "vast numbers of suits" causing "limitless financial exposure" (*SoCalGas*, *supra*, 7 Cal.5th at pp. 401-402 [citation omitted]).

In short, "attempts to generate a single rationale for [applications of the economic loss rule and its exceptions] run the risk of oversimplifying the policy concerns at stake." (Rabin, *Respecting Boundaries and the Economic Loss Rule in Tort* (2006) 48 Ariz. L.Rev. 857, 859.) Consequently, "conventional rationales for the economic loss rule" developed in one context should not "be[] imported" into cases involving the other. (Sharkey, *In Search of the Cheapest Cost Avoider: Another View of the Economic Loss Rule* (2018) 85 U. Cin. L.Rev. 1017, 1018; *see id.* at 1034 [explaining how the "stranger paradigm" and "consensual paradigm start[] from…very different premise[s]"]; Dobbs, *An Introduction to Non-Statutory Economic Loss Claims* (2006) 48 Ariz. L.Rev. 713, 733 [emphasizing need to distinguish between contracting and non-contracting parties in economic loss cases].)

2. *Biakanja* is an exception to the stranger rule—not the contract rule. It therefore says nothing about duties between parties who, like Sheen and Wells Fargo, have a contract.

Biakanja itself says so, explaining that its factors gauge whether, as "a matter of policy," a "defendant will be held liable *to a third person not in privity*." (*Biakanja*, *supra*, 49 Cal.2d at p. 651 [emphasis added].) This Court has consistently described *Biakanja* as supplying the relevant test where parties are *not* in privity.[1] And, indeed, when this Court has used *Biakanja* factors

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[1] *See Goonewardene v. ADP, LLC* (2019) 6 Cal.5th 817, 838 (*Biakanja* supplies "factors that may properly be considered in deciding whether to recognize a tort duty of care to a third party in the absence of privity of contract"); *Centinela Freeman*

to assess whether a defendant owes a duty to avoid causing economic loss, the parties have *not* been in privity.[2]

Emergency Medical Assocs. v. Health Net of California, Inc. (2016) 1 Cal.5th 994, 1013 (*Biakanja* supplies a "test for determining the existence of…an exceptional duty [to prevent purely economic loss] to third parties"); *Beacon Residential Community Assn. v. Skidmore, Owings & Merrill LLP* (2014) 59 Cal.4th 568, 578 ("*Biakanja* set forth a list of factors that inform whether a duty of care exists between a plaintiff and defendant in the absence of privity"); *Borissoff v. Taylor & Faust* (2004) 33 Cal.4th 523, 529 (*Biakanja* "articulat[es] the circumstances under which someone not a party to a contract may sue to enforce it as a third party beneficiary"); *Bily v. Arthur Young & Co.* (1992) 3 Cal.4th 370, 397 ("We have employed a checklist of factors to consider in assessing legal duty in the absence of privity of contract between a plaintiff and a defendant.").

[2] *See Centinela*, *supra*, 1 Cal.5th at page 1016 ("no contractual relationship between the [defendant] plans and the [plaintiff] emergency physicians" [citation and alteration omitted]); *Beacon*, *supra*, 59 Cal.4th at page 576 (addressing "[a]rchitect liability to third parties"); *Summit Fin. Holdings, Ltd. v. Cont'l Lawyers Title Co.* (2002) 27 Cal.4th 705, 715 (applying *Biakanja* factors to determine whether escrow holder had liability to third-party to escrow); *Quelimane Co. v. Stewart Title Guar. Co.* (1998) 19 Cal.4th 26, 58 ("Recognition of a duty to manage business affairs so as to prevent purely economic loss to third parties in their financial transactions is the exception, not the rule, in negligence law."); *Goodman v. Kennedy* (1976) 18 Cal.3d 335, 343-344 ("there is no allegation that plaintiffs had any relationship to defendant's clients"); *J'Aire Corp. v. Gregory* (1979) 24 Cal.3d 799, 803 (plaintiff restaurant had contract with property owner, which in turn had contract with defendant); *Connor v. Great W. Sav. & Loan Ass'n* (1968) 69 Cal.2d 850, 865 (acknowledging that defendant "was not in privity of contract with any of the plaintiffs except as a lender"); *Lucas v. Hamm* (1961) 56 Cal.2d 583, 589 (noting "the lack of privity between plaintiffs and defendant"); *Stewart v. Cox* (1961) 55 Cal.2d 857, 861-862 (addressing "whether a subcontractor…may be liable to the [property] owner,

"Even the most cursory review of [the *Biakanja*] test reveals that it was not intended for application to parties in privity." (*Body Jewelz, Inc. v. Valley Forge Ins. Co.* (C.D.Cal. 2017) 241 F.Supp.3d 1084, 1092-1093.) For example, *Biakanja* asks about "the extent to which the transaction was intended to affect the plaintiff," something that is always true of parties in

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with whom he was not in privity of contract"); *Biakanja*, *supra*, 49 Cal.2d at page 648 ("The principal question is whether defendant was under a duty to exercise due care…even though [defendant and plaintiff] were not in privity of contract."); *see also Goonewardene*, *supra*, 6 Cal.5th at page 838 (defendant "had no contractual relationship" with plaintiff); *Bily*, *supra*, 3 Cal.4th at page 398 (declining to impose duty to "all merely foreseeable third party users of audit reports"); *Barrera v. State Farm Mut. Auto. Ins. Co.* (1969) 71 Cal.2d 659, 674 (addressing duty owed by insurer to "third persons injured by the insured").

In *Aas v. Superior Court* (2000) 24 Cal.4th 627, an "uncertain number of plaintiffs" were in privity with one of several defendants. (*Id.* at 642.) Those in privity argued that their contracts justified recognizing a tort remedy; this Court rejected the invitation, relying on *Erlich* and the "contract rule" described in the text. (*Id.* at 643.) It then went on to consider (and reject) a *Biakanja*-based argument by all plaintiffs (some in privity with a defendant, some not). The Court noted that some lower courts had "expanded" upon this Court's decisions by applying the test "to cases in which privity did exist." (*Id.* at 645.) But the Court never accepted that expansion and, given the presence of parties not in privity and its ultimate rejection of a tort duty, it had no need to resolve the issue in *Aas*.

In *Sabella v. Wisler* (1963) 59 Cal.2d 21, this Court relied on *Biakanja* to evaluate the tort liability of a homebuilder to homeowners with whom it was apparently in privity. But the Court has since explained that "*Sabella* clearly involved property damage" (*Aas*, *supra*, 24 Cal.4th at p. 642), and thus is not a case about purely economic loss.

privity, but which can "serve[] as a bridge between the absence of privity and liability." (*Lichtman v. Siemens Indus. Inc.* (2017) 16 Cal.App.5th 914, 921-922.) Likewise, "the policy of preventing future harm" is a necessary consideration for a third-party plaintiff whose "sole recourse" is against a noncontracting defendant (*Goodman, supra*, 18 Cal.3d at pp. 352-353), for if that injured party cannot sue the stranger defendant, then there may be no liability and no deterrence at all. But that consideration lacks similar force when a plaintiff and defendant are in privity, for their conduct is controlled and enforceable by contract law.

These mismatches arise because the *Biakanja* factors evaluate whether the rationales for the "stranger rule" are sufficiently weak to make an exception to that rule. Asking whether a plaintiff was an intended beneficiary of a transaction and whether there is a sufficiently "close[]…connection between the defendant's conduct and the injury suffered" (*Biakanja*, *supra*, 49 Cal.2d at p. 650) helps ensure that there is "an intimate nexus" between the plaintiff and defendant (Sharkey, *supra*, at 1034 [citation omitted]). In doing so, those factors "set[] meaningful limits on liability" and avoid "limitless financial exposure." (*SoCalGas*, *supra*, 7 Cal.5th at pp. 401-402 [citation omitted].) But those factors do nothing to pinpoint whether imposing a general duty of care would upset parties' contractual expectations and "dissolv[e]" the boundary between tort and contract. (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 988 [citation omitted].) Indeed, because a contract itself creates "an intimate nexus" between parties to the contract, "essentially all" contractual relationships could be "deemed 'special,'" obliterating the economic loss rule as applied to contracting parties. (*Body Jewelz*, *supra*, 241 F.Supp.3d at pp. 1092-1093.)

In short, *Biakanja*'s factors are an analytical guide for evaluating a situation not presented here. Because the parties have a contract, the question is whether there is any basis for displacing the general rule that the contract allocates the economic risks between them. Sheen points to none.

D. The voluntary-undertaking doctrine is not an exception to the economic loss rule

Biakanja aside, Sheen hints at a second theory for why Wells Fargo had a duty here. He concedes that Wells Fargo had no duty to consider or approve his modification application, but claims that, once it supposedly agreed to review the application, Wells Fargo had to do so carefully. That is, he argues that an "actor who undertakes modification negotiations" must "do[] so with ordinary care." (Sheen Br. 49.) This apparent allusion to the voluntary-undertaking doctrine lacks legal or logical support.

Under the voluntary-undertaking doctrine, "a volunteer who, having no initial duty to do so, undertakes to provide protective services to another, will [sometimes] be found to have a duty to exercise due care in the performance of that undertaking." (*Delgado v. Trax Bar & Grill* (2005) 36 Cal.4th 224, 249.)

But that doctrine has no application in cases involving purely economic loss. As the Restatement explains, the voluntary-undertaking duty is "limited…to physical harm." (Rest.3d Torts, Phys. & Emot. Harm § 42, com. a; Rest.2d Torts

§ 323 [undertaking gives rise "to liability…for physical harm"]; *State Ready Mix, Inc. v. Moffatt & Nichol* (2015) 232 Cal.App.4th 1227, 1235 ["The negligent undertaking theory of liability permits damages for personal injury or property damage, not economic losses."].)

The doctrine has not been extended to purely economic loss because it would pervasively disrupt contractual negotiations and performance. This case is an apt example: To the extent Wells Fargo "undertook" to do anything, it undertook to consider *for itself* whether to enter a modified loan agreement with Sheen. But if entertaining an economic transaction is an actionable "voluntary undertaking," then parties to any contract negotiation gone awry will wind up in court, each arguing that the other failed in its undertaking to negotiate with care. (*Contra Quelimane*, *supra*, 19 Cal.4th at p. 58 ["[W]e decline to recognize a duty…to use due care in deciding whether to enter into contractual relations with another."].)

E. Other jurisdictions overwhelmingly would reject a general duty of care in this context

As the Court of Appeal recognized, at least 23 States would reject Sheen's tort claim, while at most two would accept it. (*See* C.A. Op. 10-13.) That "extent of consensus across other jurisdictions confirms" that this Court should not find a duty here. (*SoCalGas*, *supra*, 7 Cal.5th at p. 395.) Sheen identifies no case from another jurisdiction clearly endorsing his proposed tort duty, and fails in his attempts to distinguish the cases on which the Court of Appeal relied. He identifies three groups of cases.

The first group consists of cases that involved "negligent performance of a *contractual* duty." (Sheen Br. 58.) Sheen argues these cases are distinguishable because Wells Fargo did not breach the contract. (*Id.* at 59.) But as explained above (*see supra*, pp. 23-25), that distinction is irrelevant. The economic loss rule bars tort claims that fall within the scope of a contract, regardless of whether they restate a contractual obligation.

Sheen's second group of cases reject a general duty of care because of the parties' contractual relationship. (*See* Sheen Br. 59.) Sheen claims these cases are "fundamentally incompatible with California law," which recognizes a tort where there is "a duty independent of the underlying contract." (Sheen Br. 60.) But the cases he cites are consistent with that principle, and some even expressly respect it. (*See, e.g.*, *Polidori v. Bank of Am., N.A.* (E.D.Mich. 2013) 977 F.Supp.2d 754, 763 ["If no independent duty exists, no tort action based on a contract will lie." [citation omitted]].) They simply rest on the proposition that negligence in negotiating or processing a loan modification does not violate a duty independent of the loan contract.

Sheen's last group of cases are ones that would allow a duty "where there is a special relationship." (Sheen Br. 61.) Sheen's contention that these cases support him mirrors his conflation of "special relationship" used in the *Biakanja* context with "special relationship" used in cases like *Erlich* and *Foley*. (*See supra*, pp. 27-28.) The cases Sheen identifies use "special relationship" not in the *Biakanja* intended-beneficiary sense, but in the *Erlich* and *Foley* independent-duty sense—*i.e.*, to refer to a relationship where public policy requires a heightened duty of care. (*See, e.g.*, *Medici v. JP Morgan Chase Bank, N.A.* (D.Or. Jan. 15, 2014, No. 3:11-CV-00959-HA) 2014 WL 199232, at *4 ["Oregon courts have found that the relationship between creditor and borrower is not a special relationship that imposes a heightened duty of care."].) Those cases correctly conclude that a lender acting in "its conventional role as a mere lender of money" (*Nymark*, *supra*, 231 Cal.App.3d at p. 1096) owes no heightened duty. (*See, e.g.*, *McNeely v. Wells Fargo Bank, N.A.* (S.D.W.Va. Dec. 10, 2014, No. 2:13-CV-25114) 2014 WL 7005598, at *6 [explaining that "a special relationship exists if the loan servicer has 'performed services not normally provided' to a borrower," but that review of a loan modification is a "service[] normally provided to a borrower by a loan servicer" [citation and alteration omitted]].)

As in *SoCalGas*, this "striking degree of unanimity" in other jurisdictions "cuts sharply against imposing a duty of care." (7 Cal.5th at pp. 403, 407 [citation omitted].)

II. Recognizing a General Duty of Care Is Unnecessary Here Because Other Sources of Law Address the Potential Harms that Plaintiff Identifies

Sheen identifies an array of problems that may arise in mortgage servicing or during the process of negotiating a mortgage modification. Recognized causes of action, he contends, will not always allow a borrower to bring a claim when those problems occur. Accordingly, he continues, this Court should impose a general duty of care, precisely to create liability in cases like his, where the lender's conduct violated no existing law.

But that argument mistakes the deliberate tailoring of existing law for gaps in need of filling. Other areas of law—contract law, misrepresentation torts, promissory estoppel, and a variety of state and federal statues—"have been developed for the specific purpose" of guarding against the kind of harms Sheen catalogs. (*Restatement* § 3, com. b.) Those other laws "provide a more extensive and finely tuned apparatus" for addressing those harms. (*Ibid.*) Indeed, "one reason the general duty of reasonable care…is limited to physical harm is that liability for purely economic harm in commercial cases often raises issues better addressed by contract law or by the tort of misrepresentation." (Rest.3d Torts, Phys. & Emot. Harm § 7, com. d.) The field of mortgage servicing is an especially poor candidate for a new duty in negligence because it is subject to extensive specialized regulatory attention. As this Court recently recognized in *SoCalGas*, the existence of these alternative sources of law—and, in particular, the Legislature's ability to respond to any deficiencies in existing law—shows that no reason exists for this Court to intervene. (*See* 7 Cal.5th at pp. 412-413.)

A. Because mortgage servicing in general, and mortgage modification in particular, is intensely regulated, further obligations should come from the Legislature, not this Court

A web of federal and state law already governs the mortgage modification process. As in some other fields, "[l]egislative competence to act in this area is demonstrated by th[os]e existing statutes." (*Moore v. Regents of Univ. of California* (1990) 51 Cal.3d 120, 147.) Moreover, policymakers have been attentive to evolving issues in this field, which shows they will continue to act when public policy demands it. (*See SoCalGas*, *supra*, 7 Cal.5th at p. 413; *Wolfe v. State Farm Fire & Cas. Ins. Co.* (1996) 46 Cal.App.4th 554, 568 ["The Legislature's expressed intent to address these issues, both now and in the future, mandates judicial restraint as much if not more so than had it refused to do so."].) Judicial intervention through a new tort duty is not only unnecessary, but counterproductive.

1. As Sheen acknowledges, legislators and regulators at the state and federal levels have adopted "increasingly specific rules governing loan servicing and loss mitigation" in recent years, including California's Homeowners Bill of Rights (HBOR). (Sheen Br. 18.)

For example, where they apply, regulations at the federal and state level already provide detailed guidance for loan servicers. Upon receiving certain modification applications, a servicer must acknowledge receipt and notify the borrower of any deficiencies. (Civ. Code, § 2924.10, subd. (a); 12 C.F.R. §§ 1024.41(b)(2)(i)(B), (c)(3).) If the application is complete, the servicer must give the borrower information about the review process, including an estimate of when a decision will be reached. (Civ. Code, § 2924.10, subd. (a).) The servicer must "[e]valuate the borrower for all loss mitigation options available to the borrower." (12 C.F.R. § 1024.41(c)(1); *see* Civ. Code, §§ 2923.6, subd. (c)(1) & (d).) When a servicer denies an application, it must give notice of the reasons for its decision. (Civ. Code, § 2923.6, subd. (f); 12 C.F.R. § 1024.41(d).) And throughout that process, foreclosure cannot proceed. (Civ. Code, § 2923.6, subd. (c); 12 C.F.R. § 1024.41(g).)

Sheen's concerns about servicing transfers—which are not the basis for his claim here—are also addressed by law. Notice must be given to a borrower both before and after a loan is sold, transferred, or assigned. (Civ. Code, § 2937; 15 U.S.C. § 1641(g)(1); 12 U.S.C. § 2605(b)(1).) Any subsequent servicer must honor a modification granted by a previous servicer. (Civ. Code, § 2924.11, subd. (g).) And if servicing is transferred while an application is pending, the new servicer assumes the old servicer's obligations for processing the application. (12 C.F.R. § 1024.41(k).)

2. Sheen has no claim under any of these protections. But that is because they do not apply to the Second Loan, or because Wells Fargo's conduct would not have violated them.[3] For example, most of HBOR's requirements apply only to first-lien mortgages. (*See* Civ. Code, § 2924.15.) Such first-lien mortgages are most commonly used to finance the purchase of a house, in contrast to junior loans, which are often used (as here) to voluntarily borrow money against a property. HBOR therefore would not protect someone like Sheen, who sought to modify a junior loan. But that limited scope was intentional. (*See* Sen. Rules Com., Off. of Sen. Floor Analyses, Conf. Rep. on Sen. Bill 900 (2011-2012 Reg. Sess.) July 2, 2012, p. 29.)

[3] HBOR also happens not to apply to Wells Fargo in this particular case because Wells sold the Second Loan in 2010 and HBOR became effective in 2013.

Likewise, Sheen complains about Wells Fargo's communications. (*See* Sheen Br. 22.) But as explained, HBOR already details what information must be communicated for first-lien modification applications. Similarly, Sheen seeks a common law duty to process modification applications carefully. But HBOR already addresses the risk of errors by creating a statutory right to appeal the denial of a first-lien modification application and "provide evidence that the [denial] was in error." (Civ. Code, § 2923.6, subd. (d); *see* 12 C.F.R. § 1024.41(h).)

The point is not that HBOR *itself* precludes a finding of a duty. (*Cf.* Sheen Br. 19 [citing the preservation of other remedies in Civ. Code, § 2924.12, subd. (g)].) Rather, the point is that the Legislature has proven capable of addressing the issues he raises, and yet he seeks to "circumvent valid [legislative] limitations…by asserting that those very limitations create a gap…that must be filled by the common law." (*United States v. Valdez-Pacheco* (9th Cir. 2001) 237 F.3d 1077, 1080.) This Court should "decline [Sheen's] invitation to do that which the Legislature has left undone." (*Korens v. R. W. Zukin Corp.* (1989) 212 Cal.App.3d 1054, 1059.)

3. Sheen nonetheless contends that regulation in this area evinces a policy interest in "avoiding foreclosure where possible" (Sheen Br. 19) and "protecting homeowners" (*id.* at 49). Increasing lenders' duties would, he says, further this public policy. So, he concludes, this Court should judicially impose requirements that no regulator has in connection with processing loan modification applications. (*See id.* at 49-50.)

Even if Sheen's arguments were correct, they would simply be "a basis for further industry-specific *legislative or regulatory action*." (*SoCalGas*, *supra*, 7 Cal.5th at p. 413 [emphasis added]; *see id.* at 414 ["[W]here gaps persist, the Legislature can act."].) "Deciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice—and it frustrates rather than effectuates legislative intent simplistically to assume that whatever furthers the statute's primary objective must be the law." (*Rodriguez v. United States* (1987) 480 U.S. 522, 525-526.)

Here, legislators and regulators presumably were concerned with the important policies Sheen identifies, but they presumably were also interested in safeguarding access to mortgage financing. (*See* Civ. Code, § 2923.6, subd. (b) [expressing "the intent of the Legislature that the mortgage servicer offer the borrower a loan modification…*if such a modification…is consistent with its contractual…authority*" [emphasis added]]; *cf. City of Spokane v. Fed. Nat. Mortg. Ass'n* (9th Cir. 2014) 775 F.3d 1113, 1116 [discussing national policy behind the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation].) Imposing additional obligations on mortgage lenders could disrupt the mortgage marketplace and make mortgages more expensive and less accessible. Indeed, it is entirely unclear whether imposing a general duty of care in negotiating loan modifications will improve such negotiations, or simply eliminate them altogether—perversely increasing the likelihood of foreclosure, and harming rather than protecting homeowners. (*See Daniels*, *supra*, 246 Cal.App.4th at p. 1183.)

"[T]he democratic process"—not litigation—is the best forum for reconciling these varied and potentially conflicting goals, because "the Legislature can bring to bear a mix of expertise while considering competing concerns to craft a solution in tune with public demands." (*SoCalGas*, *supra*, 7 Cal.5th at p. 413). The policy issues here pose "empirical question[s] of fact," which are "better suited to legislative investigation and determination" than to judicial resolution. (*State Dep't of Health Servs. v. Superior Court* (2003) 31 Cal.4th 1026, 1048.) Legislatures, unlike courts, "have the ability to gather empirical evidence, solicit the advice of experts, and hold hearings at which all interested parties may present evidence and express their views." (*Foley*, *supra*, 47 Cal.3d at p. 694 n.31.) They are thus best positioned to resolve issues implicating "[s]ignificant policy judgments affecting social policies and commercial relationships." (*Id.* at 694; *Aas*, *supra*, 24 Cal.4th at p. 652 ["[T]he many considerations of social policy this case implicates, rather than justifying the imposition of liability…serve instead to emphasize that certain choices are better left to the Legislature."]; *Moore*, *supra*, 51 Cal.3d at p. 147 [rejecting tort liability because, *inter alia*, "[c]omplex policy choices affecting all society are involved" and the "Legislature should make th[e] decision" regarding liability].)

Moreover, in the highly technical and already-regulated field of mortgage lending, legislatures and regulators have a further advantage over courts: They can prospectively announce clear, predictable, detailed, and administrable rules. Here, for example, Sheen urges that a lender must "process and respond carefully and completely" to loan modification applications. (Sheen Br. 24.) That apparently means completing review quickly—though Sheen does not say how quickly (*see id.* at 17). It apparently means providing information about the application's status—though Sheen does not say when or what information must be communicated (*see id.* at 37-38). It apparently means improving customer service offerings—though Sheen offers no specifics (*see id.* at 16-17 & 17 n.3). Imposing such a generalized duty would put every lender in a quandary: Follow its contract and relevant regulations? Or do something different, knowing that years later a jury with understandable sympathy for the borrower's misfortune may second-guess the lender's conduct? These challenges are inherent and insurmountable in a general negligence approach; "finely tuned rules" simply "defy judicial creation." (*SoCalGas*, *supra*, 7 Cal.5th at p. 412.)

B. A new negligence duty is unwarranted because existing torts address misrepresentations

California law recognizes the tort of negligent misrepresentation. Sheen chose not to plead such a claim. (*See* C.A. Op. 7-8.) Nonetheless, he has since reframed the issue presented in this Court as whether "a mortgage servicer owe[s] a borrower a duty of care to refrain from making material misrepresentations" (Sheen Br. 11.) Recognizing an amorphous ordinary negligence claim in addition to the existing tort of negligent misrepresentation is neither necessary nor appropriate.

1. This Court has squarely held that negligent misrepresentations are the proper subject of a negligent misrepresentation claim, but not a general negligence claim. In *Bily*, *supra*, the Court considered whether a company's investors who relied on an erroneous audit report could pursue a claim for negligence or negligent misrepresentation against the authoring auditor. The Court explained that the two torts are "separate" and "[t]he distinction" between them "is important." (*Bily*, *supra*, 3 Cal.4th at 407.) "[A] general negligence charge directs attention to a defendant's level of care," while negligent misrepresentation focuses on a "plaintiff's reliance on a materially false statement made by defendant." (*Id.* at 413.) Where a plaintiff complains about "the audit report, not the audit itself," negligent misrepresentation "more precisely captures the gravamen of the cause of action and more clearly conveys the elements essential to a recovery." (*Ibid.*) Accordingly, the Court held that certain plaintiffs could raise a claim for negligent misrepresentation, but concluded they could not "also recover on a general negligence theory." (*Ibid.*)

The same is true here. As in *Bily*, Sheen's misrepresentation-based arguments center on allegedly "materially false statement[s]"—the letters Wells Fargo sent and the call with Sheen's wife—not on "the manner in which" Wells Fargo processed his applications. (*Bily*, *supra*, 3 Cal.4th at 413.) Accordingly, as in *Bily*, negligent misrepresentation "captures the gravamen" of these allegations better than negligence. (*Ibid.*) *Bily* therefore forbids Sheen from resting an ordinary negligence claim on a misrepresentation foundation.

The distinction between the two torts also reveals why *Lueras v. BAC Home Loans Servicing, LP* (2013) 221 Cal.App.4th 49, does not support Sheen's position. *Lueras* rejected an ordinary negligence claim, holding that a lender owed no general duty of care to consider a loan modification or to "explore foreclosure alternatives." (*Id.* at 67.) But, the court continued, "[t]he law imposes a duty not to make negligent misrepresentations of fact" such that "a lender does owe a duty to a borrower to not make material misrepresentations about the status of an application for a loan modification or about the date, time, or status of a foreclosure sale." (*Id.* at 68.) The court accordingly granted the plaintiff leave to amend "to plead a cause of action *for negligent misrepresentation*." (*Id.* at 69 [emphasis added].) *Lueras* thus echoes *Bily*'s insight that a plaintiff cannot transform a misrepresentation claim into a negligence claim.

2. The distinction between negligent misrepresentation and ordinary negligence makes a big difference. Unlike an ordinary negligence claim, a negligent misrepresentation claim here would require pleading, among other elements: [1] a false representation; [2] that Wells Fargo should have known of the representation's falsity; and [3] that Sheen actually and justifiably relied on the representation. (*See Small v. Fritz Companies, Inc.* (2003) 30 Cal.4th 167, 173-174; *Chapman v. Skype Inc.* (2013) 220 Cal.App.4th 217, 231.) And because a "[c]ause[] of action for…negligent misrepresentation sound[s] in fraud" Sheen would have had to plead each of those elements with specificity. (*Daniels*, *supra*, 246 Cal.App.4th at p. 1166; *see also Small*, *supra*, 30 Cal.4th at p. 184 [stockholder suit].)

Each of those requirements exists for a reason, but Sheen's complaint satisfies none of them. The operative complaint alleges that Wells Fargo's March 2010 letters "suggest[ed]" that the loans had been modified and that the property would not be sold, and that its subsequent call and letters "[c]onfirm[ed]" that interpretation. (SAC ¶55.) But Sheen has never alleged that Wells Fargo made an actually false statement, much less that it should have known of that falsity. (*Compare* SAC ¶¶89, 97 [alleging that other defendants made false statements]; *see Apollo Capital Fund, LLC v. Roth Capital Partners, LLC* (2007) 158 Cal.App.4th 226, 243 [noting that "an omission or an implied assertion or representation is not sufficient" for negligent misrepresentation claim].) Nor could he make such an allegation: Statements that the debt was charged off (*i.e.*, deemed likely uncollectable), that Wells Fargo would pursue appropriate debt collection strategies, and that the February 2010 foreclosure sale would not occur were all accurate. (*See* Tr. Proceedings (June 22, 2017) 12 [trial court noting that "I'm not sure that [Sheen] ha[s] pleaded that [Wells Fargo] said anything that was incorrect"].)

Moreover, Sheen's operative complaint has only conclusory allegations about reliance, yet this is "the indispensab[le]" element of a misrepresentation claim (*Bily*, *supra*, 3 Cal.4th at p. 413). Sheen claims that he would have "submitt[ed] additional applications for mortgage modification" and "pursu[ed] a short sale" absent Wells Fargo's challenged conduct. (SAC ¶59.) But Sheen actually *did* pursue additional modifications. (SAC ¶¶34, 36, 37, 39, 41.) Regardless, he points to no "actions, as distinguished from unspoken and unrecorded thoughts and decisions, that would indicate that [he] actually relied on the misrepresentations." (*Small*, *supra*, 30 Cal.4th at p. 184 [rejecting conclusory reliance allegations].) Nor has Sheen pleaded how the "circumstances…ma[d]e it reasonable" for him to rely. (*OCM Principal Opportunities Fund, L.P. v. CIBC World Markets Corp.* (2007) 157 Cal.App.4th 835, 864-865 [citation omitted].) As the trial court here observed, given Sheen's "experience with loans on this property," Sheen should have known "that he would have to sign papers to modify the loans," so "[t]here is no conceivable way that [Sheen] could believe" that his loan had been modified to be unsecured. (Tr. Proceedings (June 22, 2017) 5, 12.)

The court below stated that Sheen's decision not to bring a negligent misrepresentation claim was "well counseled and not inadvertent." (C.A. Op. 7.) The lack of merit in such a claim is not a reason to create a new tort duty, but rather a reason to resist that invitation and instead reaffirm that misrepresentation plaintiffs plead "the elements essential to a recovery." (*Bily*, *supra*, 3 Cal.4th at p. 413.)

C. A new negligence duty is unnecessary to enforce lenders' promises because promissory estoppel already protects a borrower who detrimentally relies on a lender's promise

Sheen also suggests that a negligence duty would protect borrowers who rely on lenders' promises to their detriment. (*See, e.g.*, Sheen Br. 11, 12.) Here, Sheen asserts in his brief that Wells Fargo "promised"—an allegation absent from the operative complaint—that he would "*never* lose [his] house" (*id.* at 11) "which led to reliance…and resulting damages" (*id.* at 45).

But promissory estoppel, not negligence, exists to remedy such conduct. That doctrine operates when a defendant makes a promise that it "should reasonably expect to induce action or forbearance…and which does induce such action or forbearance" and where "injustice can be avoided only by enforcement of the promise." (*Kajima/Ray Wilson v. Los Angeles Cty. Metro. Transp. Auth.* (2000) 23 Cal.4th 305, 310 [quoting Rest.2d Contracts § 90, subd. (1)].)

Sheen argues that promissory estoppel is inadequate because its "elements are difficult to establish in the mortgage modification context." (Sheen Br. 56.) But he does not explain why the mortgage modification context would be unduly inhospitable to promissory estoppel; such claims have been allowed to proceed. (*See, e.g.*, *Aceves v. U.S. Bank, N.A.* (2011) 192 Cal.App.4th 218, 221-222, 225-231 [plaintiff stated a claim for promissory estoppel where she detrimentally relied on "bank's promise to work with her in reinstating and modifying [her] loan"].) Here, Sheen's allegations would not support a promissory estoppel claim. For example, Sheen argues that Wells Fargo made "suggestions" that his "loan had been modified and that his house was safe from foreclosure," but concedes these were "not sufficiently definite promises to support a promissory estoppel claim." (Sheen Br. 57.)

Because "promissory estoppel is essentially equitable in nature," it allows courts to "enforc[e] a promise which otherwise would be unenforceable" to avoid injustice. (*C & K Eng'g Contractors v. Amber Steel Co.* (1978) 23 Cal.3d 1, 7-8.) The extent and limits of promissory estoppel are thus flexible, but they ultimately reflect the equitable judgment that not every statement—be it an express promise or suggestive conduct—should be enforceable to achieve a just result. No reason exists to use general negligence law to excuse Sheen's inability to come within such a flexible equitable doctrine.

D. When a borrower claims an agreement exists with a lender regarding mortgage modification, contract law rather than tort law governs enforcement of that agreement

Sheen contends that Wells Fargo's duty arose because "Wells…agreed to review Sheen's application to modify the Second Loan." (Sheen Br. 43; *see, e.g.*, *id.* at 33 [describing a "duty to exercise reasonable care…once a servicer agrees to consider a modification"].) But agreements are the domain of contract, not tort. Arguing for a duty arising from an agreement is simply a claim that the parties have a contract. (*See* Rest.2d Contracts § 1 ["A contract is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty."].) Sheen effectively claims that he and Wells Fargo had a contract to renegotiate his loan contract. (*See Copeland v. Baskin Robbins U.S.A.* (2002) 96 Cal.App.4th 1251, 1257 [holding that breach of agreement to negotiate could give rise to contract cause of action].)

Although contracts to negotiate exist, contract law is generally skeptical of them. Ordinarily, "[w]hen two parties, under no compulsion to do so, engage in negotiations to form or modify a contract neither party has any obligation to continue negotiating or to negotiate in good faith." (*Copeland*, *supra*, 96 Cal.App.4th at p. 1260; *see Racine & Laramie, Ltd. v. Dep't of Parks & Recreation* (1992) 11 Cal.App.4th 1026, 1031-1032 [holding that defendant "had no obligation to negotiate new terms" of contract and "that its assumption of an arbitrary stance at some point in the negotiations cannot therefore be a breach of any contract term"].) No reason exists to create tort law that overrides those contract law principles.

Here, of course, no enforceable contract to negotiate exists. The operative complaint neither specifies the terms of the agreement, nor explains when or how Wells Fargo manifested its agreement to negotiate for a modification. (*See generally Secrest v. Sec. Nat'l Mortgage Loan Trust 2002-2* (2008) 167 Cal.App.4th 544 [loan forbearance agreement is subject to the Statute of Frauds]; Rest.2d Contracts, §§ 18-23 [manifestation of assent]; *id.* §§ 50-70 [acceptance of offers].) Using tort duties to create the facsimile of an enforceable contract where none exists frustrates both the policies behind contract law and parties' reliance on those well-settled rules.

III. Even If *Biakanja* Supplied the Proper Test Here, It Would Counsel Against Recognizing a Duty

For the reasons above, the *Biakanja* framework has no place in this case. But, even if this Court were to collapse the distinction between contracting parties and strangers and apply *Biakanja* to determine duties between contracting parties, there would still be no basis for finding a duty here.

Sheen argues principally that the *Biakanja* framework counsels imposing on Wells Fargo a general duty of care to avoid economic loss to him. *Biakanja* permits a plaintiff to recover for economic losses arising from "a contracting party's negligent performance of a contract" where policy factors dictate that "a tort duty of care should be recognized." (*Goonewardene*, *supra*, 6 Cal.5th at p. 838; *see Aas*, *supra*, 24 Cal.4th at p. 638 ["*Biakanja* held that the negligent performance of a contractual obligation, resulting in damage to the property or economic interests of a person not in privity, could support recovery if the defendant was under a duty to protect those interests."].) The *Biakanja* framework thus involves two steps: [1] identifying the obligation that the defendant "negligent[ly] perform[ed]," and [2] weighing policy factors to assess whether the defendant had a duty *to the plaintiff* to perform that obligation with care. Here, Sheen cannot satisfy either step: Sheen cannot point to any obligation that Wells Fargo improperly discharged. And even if he could, the policy factors this Court identified in *Biakanja* and *Bily* dictate that Wells Fargo owed no duty to Sheen here.

A. Wells Fargo violated no preexisting obligation regarding handling loan modifications

1. A premise of applying *Biakanja*'s factors is that the defendant had some obligation that it failed to perform with care. Depending on the factors, the defendant may therefore be liable to the plaintiff for losses caused by that failure.

Biakanja itself dealt with the "negligent performance of a contract" (49 Cal.2d at p. 649): The notary public defendant had contracted to prepare the plaintiff's brother's will; the notary's error in preparing that will caused economic loss to the plaintiff. (*See id.* at 648.) *Biakanja* concluded, as a matter of policy, that the plaintiff could sue the notary for negligently preparing the will—that is, the plaintiff could enforce in tort the notary's preexisting contractual obligation to the plaintiff's brother.

Similarly, in every subsequent case where this Court has found *Biakanja* dictates a duty to avoid causing economic loss, the plaintiff alleged the defendant had failed to properly perform some preexisting obligation. Often, that obligation was reflected in the defendant's contractual agreement to perform a particular task.[4] In a few cases, a statute or other source of law imposed the

[4] *See Beacon*, *supra*, 59 Cal.4th at page 571 (hired to provide design services); *J'Aire*, *supra*, 24 Cal.3d at page 803 (contractual obligation to complete construction on time); *Connor*, *supra*, 69 Cal.2d at page 864 (development financer's obligation to investors "to prevent the construction of defective homes"); *Lucas*, *supra*, 56 Cal.2d at page 591 ("implied[] agree[ment] to use such skill, prudence, and diligence as lawyers of ordinary skill and capacity commonly possess and exercise"); *Stewart*, *supra*, 55 Cal.2d at page 860 (subcontract to install concrete).

obligation that the defendant allegedly failed to fulfill.[5] And even where the Court ultimately found no duty after discussing the *Biakanja* factors, the premise of the Court's analysis was that defendant had a preexisting obligation.[6]

The requirement of a preexisting obligation makes perfect sense. As one Court of Appeal observed, "[i]f defendant had no obligation to manage [certain] funds, obviously, it had no duty to exercise ordinary care in the performance of such an obligation." (*Gill v. Mission Sav. & Loan Ass'n* (1965) 236 Cal.App.2d 753, 757.) The requirement also vindicates the rule that there is generally "no duty to prevent financial loss to others." (*Quelimane*, *supra*, 19 Cal.4th at p. 59.) When a defendant has *already* agreed to perform an obligation, the defendant is fairly on notice of its obligations and can plausibly be held liable for the

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[5] *See Centinela*, *supra*, 1 Cal.5th at 1001 (statutory obligation "to reimburse the emergency service provider for necessary emergency medical services and care"); *Barrera*, *supra*, 71 Cal.2d at page 668 ("'quasi-public' nature of the insurance business [fn. omitted] and the public policy underlying [a state statute]" create duty "to conduct a reasonable investigation of insurability within a reasonable time").

[6] *See Summit*, *supra*, 27 Cal.4th at pages 715-716 (escrow holder had contractual obligations relating to disbursement of escrowed funds, though had complied with those obligations); *Aas*, *supra*, 24 Cal.4th at page 632 (developer, contractor, and subcontractors undertook to build dwellings); *Quelimane*, *supra*, 19 Cal.4th at page 57 ("common law duty of nondiscrimination"); *Goodman*, *supra*, 18 Cal.3d at page 339 (attorney has obligation to properly advise his clients); *see also Goonewardene*, *supra*, 6 Cal.5th at page 839 (defendant payroll company "obligated to act with due care" under its contract with plaintiff's employer); *Bily*, *supra,* 3 Cal.4th at page 406 (duty to client "in the conduct of an audit").

economic consequences of failing to perform them with care. But untethered from that preexisting obligation, *Biakanja* would become a general mandate to exercise care to avoid economic loss to all foreseeably affected parties, swallowing the ordinary rule.

The preexisting-obligation requirement is especially important where, as here, contract negotiations are at issue. Parties negotiating a contract are expected to protect their own interests. For that reason, "the amount of care they are expected to show for *each other's* interests will often be unclear or significantly less than the care expected in a situation involving strangers or the risk of physical injury." (Rest.3d Torts § 3, com. d [emphasis added]; *cf.* Rest.3d Torts, Phys. & Emot. Harm § 5, com. a [noting that even *intentionally* causing economic loss may not give rise to liability].) Negotiating a mortgage modification is no different: No doubt, *Sheen* sought a modification to retain ownership of his property. But *Wells Fargo* would have a different motivation, because loan modification "at its core is an attempt by a money lender to salvage a troubled loan." (*Armstrong v. Chevy Chase Bank, FSB* (N.D.Cal. Oct. 3, 2012, No. 5:11-CV-05664 EJD) 2012 WL 4747165, at *4; *see Daniels*, *supra*, 246 Cal.App.4th at p. 1182.) So long as a lender acts within the limits of existing law, no basis exists for using *Biakanja* "to create broad tort duties in arms-length business dealings." (*Stop Loss Ins. Brokers, Inc. v. Brown & Toland Med. Grp.* (2006) 143 Cal.App.4th 1036, 1042.)

2. Sheen proceeds directly to applying the *Biakanja* factors, without identifying what preexisting obligation Wells

Fargo allegedly violated. No suitable preexisting obligation exists. Certainly, Wells Fargo has obligations that govern its conduct with respect to mortgage modifications. But Sheen does not claim any such obligation was violated. Sheen also contends that Wells Fargo "agree[d] to review" his mortgage modification application. (Sheen Br. 11.) But such a direct voluntary agreement would be a matter for contract law or promissory estoppel, not tort. (*See supra*, pp. 51-54.)

Because Wells Fargo violated no preexisting obligation, no duty exists under *Biakanja*. (*See, e.g.*, *Pac. Rim Mech. Contractors, Inc. v. Aon Risk Ins. Servs. W., Inc.* (2012) 203 Cal.App.4th 1278, 1291-1292 [*Biakanja* "inapplicable" because "[plaintiff] does not assert [defendant] breached any contract"]; *Mark Tanner Constr. v. Hub Int'l Ins. Servs.* (2014) 224 Cal.App.4th 574, 587 [similar]; *Stop Loss*, *supra*, 143 Cal.App.4th at p. 1042 [similar].)

B. The *Biakanja* and *Bily* factors weigh against recognizing a general duty of care here

In all events, consideration of the *Biakanja* and *Bily* factors shows Wells Fargo owed Sheen no duty here.

1. The *Biakanja* factors consider "[1] the extent to which the transaction was intended to affect the plaintiff, [2] the foreseeability of harm to him, [3] the degree of certainty that the plaintiff suffered injury, [4] the closeness of the connection between the defendant's conduct and the injury suffered, [5] the moral blame attached to the defendant's conduct, and [6] the policy of preventing future harm." (*Biakanja*, *supra*, 49 Cal.2d at p. 650.)

Biakanja requires a "determination whether *in a specific case* the defendant will be held liable to a third person." (*Biakanja*, *supra*, 49 Cal.2d at p. 650 [emphasis added].) Sheen nonetheless contends that this Court should, instead, "conduct[] the duty analysis 'at a relatively broad level of factual generality.'" (Sheen Br. 38 [quoting *Kesner v. Superior Court* (2015) 1 Cal.5th 1132, 1144, (quoting in turn *Cabral v. Ralphs Grocery Co.* (2011) 51 Cal.4th 764, 770)].) But *Kesner* and *Cabral* (both physical harm cases) are inapposite because they considered whether to recognize an *exception* to the general duty rule in cases of physical harm. Conducting a high-level analysis prevented "usurping the jury's proper function of deciding what reasonable prudence dictates under th[e] particular circumstances." (*Cabral*, *supra*, 51 Cal.4th at p. 774.) But here, the situation is reversed: The presumption is against recognizing a duty to prevent economic loss, and the question is whether to *create* a new duty. Analyzing that question at too high a level would abdicate to juries the policy-bound duty determination, "which is for the *court* to make." (*Id.* at 772.) In the *Biakanja* context, "[e]xceptions [to the no-duty rule] have been recognized only rarely, and then only when the specific facts of the case" warrant. (*Borissoff*, *supra*, 33 Cal.4th at p. 530.)

2. Here, Sheen urges that Wells Fargo had a duty "to refrain from making material misrepresentations about the status of a foreclosure sale" (Sheen Br. 11) and the specific facts underlying that claim are Wells Fargo's letters and phone call (*see id.* at 21-23). Starting with the first *Biakanja* factor, those specific facts reflect Wells Fargo's announcement that it intended to pursue methods of recovering Sheen's debt besides immediate foreclosure. Those communications were not intended to affect Sheen (except in the sense of exhorting him to cure his default). Sheen confuses the relevant inquiry in arguing that modification negotiations "determine whether foreclosure will take place." (Sheen Br. 40.) When two parties in a contract discuss modifying that contract, their actions *always* "affect" each other. But that is a feature of contract negotiations generally, not the specific conduct here. Because the *Biakanja* analysis focuses on "the specific conduct by [Wells Fargo] that [Sheen] claims was negligent" (*Jolley v. Chase Home Fin., LLC* (2013) 213 Cal.App.4th 872, 899), the question is not about the general "goal[s] of loan modification" (Sheen Br. 40), but instead the intended effect of the particular challenged conduct.

Second, it was not foreseeable that Wells Fargo's communications would cause Sheen harm. Most borrowers would react to the information communicated—that Sheen was in default and that Wells Fargo would attempt to collect the amounts he owed—by pursuing other forms of relief. And indeed, Sheen alleges he continued to seek loan modifications. (SAC ¶¶34, 36, 37, 39, 41.) Again, Sheen is arguing someone else's case when he asserts that it is "utterly predictable" that a borrower will be harmed if a lender "mishandl[es] a loan modification" or if there is "extended delay" in processing. (Sheen Br. 41-42.) This case is about specific, truthful communications.

On the third and fourth factors, Sheen suffered the injury of losing his house (albeit under contractual terms he had agreed to). But that injury was not closely connected to Wells Fargo's conduct. Perhaps he "would have pursued alternatives to cure his default" (SAC ¶59), but there are no allegations about why any "missed…opportunity to save the home" (Sheen Br. 44) would have succeeded. Sheen correctly recognizes that Wells Fargo had no duty to actually grant him a loan modification (*see* Sheen Br. 34; Civ. Code, § 2923.4), and he has never claimed that Wells Fargo would have modified his loan had Sheen continued to pursue that course. He thus fails to allege that "but for [Wells Fargo's] negligence" he would have avoided foreclosure or that his injury "was directly caused by [Wells Fargo's] conduct." (*Biakanja*, *supra*, 49 Cal.2d at pp. 650-651.)

Moreover, Sheen did not suffer his claimed injury until four years after Wells Fargo's challenged conduct when a different actor foreclosed on the property. (*See* SAC ¶¶28-30, 35, 45 [Wells Fargo assigned rights to Dove Creek, which assigned rights to CC Drake, LLC, which assigned rights to Mirabella, which assigned servicing to FCI].) Indeed, Sheen himself contends that subsequent actions by *those* entities led to foreclosure. (*See, e.g.*, SAC ¶¶70, 74.) The significant interval between the conduct and the foreclosure, and Wells Fargo's total lack of involvement in that foreclosure, make the connection here anything but close.

Sheen's contention that Wells Fargo's conduct led him to "refrain[] from taking action to prevent the foreclosure sale" (Sheen Br. 43) is unavailing. *Aas*, *supra*, explains that a plaintiff proceeding under *Biakanja* must show an "appreciable, nonspeculative, present injury." (24 Cal.4th at p. 646.) A "loss of opportunity to save [one's] home" (Sheen Br. 43) "do[es] not comfortably fit the definition of 'appreciable harm'" (*Aas*, *supra*, 24 Cal.4th at p. 646 [citation omitted]). That mere "loss of opportunity" theory is especially misplaced because "courts that have accepted lost opportunity as cognizable harm have almost universally limited its recognition to medical-malpractice cases." (Rest.3d Torts, Phys. & Emot. Harm § 26, com. n.) Thus, in the economic realm, this Court has rejected claims for "speculative expectancies" and demanded instead a "sufficient degree of certainty that the plaintiff…would have received the anticipated benefits." (*Roy Allan Slurry Seal, Inc. v. Am. Asphalt S., Inc.* (2017) 2 Cal.5th 505, 518 [citations and quotation marks omitted].) That "degree of certainty" is lacking here because Sheen cannot even show that the foreclosure was "close[ly]… connect[ed] [to] [Wells Fargo's] conduct." (*Biakanja*, *supra*, 49 Cal.2d at p. 650.)

Fifth, Wells Fargo's communications regarding Sheen's default are not morally blameworthy. Sheen "needed a loan modification to avoid defaulting, and that…need was not a product of [Wells Fargo's] conduct." (*Daniels*, *supra*, 246 Cal.App.4th at p. 1183; *see Lueras*, *supra*, 221 Cal.App.4th at p. 67 ["If the lender did not place the borrower in a position creating a need for a loan modification, then no moral blame would be attached to the lender's conduct."].) Perhaps macroeconomic forces beyond Wells Fargo's or Sheen's control played a part in

Sheen's misfortune. But it was ultimately Sheen who borrowed against his property and defaulted—and thus it was Sheen rather than Wells Fargo who "exercised greater control over the risks at issue." (Sheen Br. 45 [quoting *Kesner*, *supra*, 1 Cal.5th at p. 1151].) No moral blame should attach when a defendant, under no obligation to do so, engages in discussions aimed at allowing the plaintiff to cure his own default.

Sheen argues that Wells Fargo is blameworthy because of the "stark power disparity" between banks and borrowers. (Sheen Br. 46.) Certainly, exploiting a power imbalance may be morally blameworthy. Thus, if Wells Fargo had intentionally "misinform[ed] [or] under-inform[ed]" Sheen (*Alvarez v. BAC Home Loans Servicing, L.P.* (2014) 228 Cal.App.4th 941, 949), this factor would surely weigh in favor of a duty. But Wells Fargo conveyed truthful information. (*See* SAC ¶¶15, 23.) Wells Fargo does not deserve moral blame for Sheen's misunderstanding of those communications.

Sixth, imposing a general duty of care here is unlikely to prevent future harm. Lenders already have strong incentives and regulatory obligations to work toward reasonable modifications. Foreclosure is costly to administer, and is especially likely to cause a loss to junior lienholders like Wells Fargo was here. A general duty of care can add nothing significant to those incentives and rules, and it may well make borrowers worse off. "Absent a duty in the first place to modify a loan or even to evaluate such an application under objective standards limiting the lender's discretion, imposing negligence liability for the mishandling of loan modification applications could be a disincentive to lenders from ever offering modification." (*Daniels*, *supra*, 246 Cal.App.4th at p. 1183 [citation omitted].) That result is particularly likely given the nebulous nature of the duty here. An abstract instruction to "act with care" in this highly technical and regulated field will give lenders every reason to fear how a future jury will judge their conduct in hindsight, but no clear guidance today about how to conform their conduct to the law. Yet avoiding that trap is easy and lawful—simply summarily deny modification applications. A tort duty that makes mortgage modifications less likely is not one that prevents future harm.

3. Each of the *Bily* factors also weighs against a duty: holding Wells Fargo liable [1] would result in liability out of proportion to its fault, [2] would be unnecessary in light of the prospect of private ordering, and [3] would have an adverse effect on the availability of mortgage modifications. (*See Bily*, *supra*, 3 Cal.4th at p. 398.)

First, it would be unfair to hold Wells Fargo liable for all the economic consequences of a foreclosure it did not put into motion and did not carry out. Wells Fargo did not create the situation calling for a modification or foreclosure—Sheen's default did. (*See Bily*, *supra*, 3 Cal.4th at p. 400 [finding this factor weighed against duty where "regardless of the efforts of [the defendant]," another party had "effective primary control"].) Despite the attenuation between Wells Fargo's actions and the injury Sheen suffered (*see supra*, pp. 61-62), Sheen now seeks to hold Wells Fargo responsible for the entire loss of his home. (*See* SAC ¶62.) Such liability would be far out of proportion to any fault.

Second, liability is unnecessary here because Sheen had substantial opportunities to address his own situation. Sheen had more control over his borrowing and default than Wells Fargo. (*See supra*, pp. 62-63.) And even after he defaulted, Sheen had the opportunity to use his "own prudence, diligence, and contracting power, as well as other informational tools" to work with Wells Fargo toward a modification or other forms of relief. (*Bily*, *supra*, 3 Cal.4th at p. 403.) Although Sheen paints himself as "powerless [and] unsophisticated" (Sheen Br. 45 [citation omitted]), he was assisted by counsel in his discussions with Wells Fargo (*see* SAC ¶¶11-12). Moreover, Wells Fargo offered on multiple occasions to have further discussions with Sheen (*see* SAC ¶¶15-16, 23), which Sheen apparently declined. Had Sheen followed up, he could have eliminated any confusion about the status of his loans.

Third, imposing a duty here is likely to adversely affect the availability of mortgage modifications. As explained above, imposing tort liability may create a significant disincentive for lenders to engage in the mortgage modification process. (*See supra*, pp. 63-64.) Indeed, lenders may be especially reluctant to consider modification applications from borrowers with collateral most suitable for foreclosure, "reasoning that they will inevitably be singled out and sued" for damages arising from foreclosure "regardless of the care" they took. (*Bily*, *supra*, 3 Cal.4th at p.

404.) Imposing tort liability could thus lead to the perverse consequence that borrowers most in need of cooperation from a lender are the least likely to get it.

In sum, the only factor that weighs in Sheen's favor is the existence of an injury—and even there he mistakes its connection to Wells Fargo's conduct. Weighed together, the *Biakanja* and *Bily* factors confirm that Wells Fargo did not owe Sheen a duty of care.

CONCLUSION

The judgment of the Court of Appeal should be affirmed.

Respectfully submitted.

Dated: May 15, 2020 By:__________________________

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CERTIFICATE OF COMPLIANCE

Pursuant to California Rules of Court, rules 8.204(b) and 8.520(c)(1), I certify that the foregoing ANSWERING BRIEF ON THE MERITS is produced using 13-point Roman type including footnotes and contains 13,999 words, which is less than the 14,000 words permitted by this rule. Counsel relies on the word count of the computer program used to prepare this brief.

Dated: May 15, 2020

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STATE OF CALIFORNIA, COUNTY OF SAN FRANCISCO

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Susan Ahmadi

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S258019

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