March 8, 2022

Sheen v. Wells Fargo Bank, N.A.: The California Supreme Court Delivers a Big Win for Lenders and Loan Servicers

By: Jarrett S. Osborne-Revis and Robert S. McWhorter

On March 7, 2022, the California Supreme Court issued its much-anticipated decision in *Sheen v. Wells Fargo Bank, N.A.*, holding that a lender does not owe a borrower a tort duty of care in considering a loan-modification request.[1] *Sheen*, like many other loan-modification cases resulting from the 2008 recession, arose from a dispute between the plaintiff Kwang K. Sheen ("Kwang") and the defendant Wells Fargo Bank, N.A. ("Wells Fargo") over a failed loan modification. Seven years after Kwang obtained a loan to purchase a home ("Property"), he used the Property as collateral for two more loans ("Second and Third Loans"), both from Wells Fargo.[2] Kwang later defaulted on the Second and Third Loans because of financial difficulties he experienced "in the wake of the global financial crisis."[3] Wells Fargo recorded default notices against the Property and scheduled a foreclosure sale.[4] Seeking to forestall Wells Fargo from exercising its default remedy, Kwang submitted applications to modify the Second and Third Loans.[5]

Though Wells Fargo cancelled the nonjudicial foreclosure proceeding, it allegedly never responded to Sheen's loan-modification requests.[6] Instead, a month and a half later, Wells Fargo sent Kwang two letters accelerating the Second and Third Loans and demanding that he repay both loans.[7] Still Kwang believed Wells Fargo would ultimately modify the Second and Third Loans despite these payment-demand letters.[8] Wells Fargo did not do so; it sold its Second Loan to Mirabella Investment Group, LLC ("Mirabella"), which foreclosed on the Property

---

[1] *Sheen v. Wells Fargo Bank, National Association et al.*, No. S258019, 2022 WL 664722, at *1 (Cal. Supreme Ct. March 7, 2022).
[2] *Sheen*, 2022 WL 664722, at *2.
[3] *Id.*
[4] *Id.*
[5] *Sheen*, 2022 WL 664722, at *2.
[6] *Id.*
[7] *Id.*
[8] *Id.* at * 3.

four years later.[9] Undeterred by the foreclosure, Kwang sued Wells Fargo, asserting a negligence claim for Wells Fargo's alleged failure to "process, review, and respond carefully and completely to his loan modification application."[10]

The trial court sustained Wells Fargo's demurrer to Kwang's negligence claim.[11] Wells Fargo, the trial court found, did not owe Kwang a duty to "respond timely to his request to modify the second trust deed."[12] The Court of Appeal affirmed, joining the majority of courts that have rejected negligence claims premised on a lender's failure to consider a borrower's loan-modification request.[13] The California Supreme Court granted review.

The California Supreme Court confronted this issue from the Court of Appeal's decision: did Wells Fargo owe Kwang a duty to "process, review and respond carefully and completely to [his] loan modification applications" so as to avoid causing him damages.[14] Kwang claimed his loan modification application imposed that legal duty on Wells Fargo. In analyzing Kwang's claim, the *Sheen* Court observed that a lender's tort duty in the loan modification context has divided lower courts.[15] After surveying the lower court split, the *Sheen* Court considered if Kwang could root his legal-duty theory against Wells Fargo in a "statute" or by "operation of the common law."[16]

Quickly dispensing with the first source, the *Sheen* Court found no statute required Wells Fargo to treat Kwang's loan-modification request with due care.[17] Kwang did not challenge that finding either; he acknowledged Wells Fargo owed him no statutory duty of care as a junior lienholder.[18]

The *Sheen* Court then addressed and rejected Kwang's common law duty, the second potential source for plaintiff's negligence claim. Kwang urged the *Sheen* Court to find that Wells Fargo owed him a common law duty in processing his loan-modification request.[19] In analyzing Kwang's common-law-duty claim, the *Sheen* Court adopted the majority of courts' no-duty rule,

---

[9] *Id.* at * 3-4. Wells Fargo cancelled its Third Loan in March 2014 and informed Kwang it cancelled that loan. *Id.* at * 3 n.1.

[10] *Id.* at *4. Kwang also asserted promissory estoppel, intentional infliction of emotional distress, and unfair competition law (Bus. & Prof. Code, § 17200) claims against Mirabella and its loan servicer FCI Lender Services, Inc. *Id.* The Supreme Court's opinion focuses solely on Kwang's negligence claim against Wells Fargo.

[11] *Id.*

[12] *Id.*

[13] *Sheen*, 2022 WL 664722, at *4.

[14] *Id.*

[15] *Id.*

[16] *Id.* at * 5 (citing *J'Aire Corp. v. Gregory*, 24 Cal.3d 799, 803 (1979)).

[17] *Sheen*, 2022 WL 664722, at *6.

[18] *Id.* at *5.

[19] *Id.* at *6.

citing three justifications.

First, the *Sheen* Court determined Kwang's negligence claim clashed with California's longstanding economic loss rule.[20] Succinctly summarizing that rule, the *Sheen* Court noted it bars tort recovery for negligently inflicted "purely economic losses" in deference to a contract between litigating parties.[21] Kwang's negligence claim arose from his mortgage contract with Wells Fargo, specifying its rights regarding the loan and collateral securing the loan.[22] Consistent with California law, the contract permitted Wells Fargo to "seize and sell the property in satisfaction of the debt should plaintiff stop making payments on the loan."[23] Wells Fargo did not agree that should Kwang default and seek a loan modification, Wells Fargo would forgo foreclosure until after it "process[ed], review[ed] and respond[ed] carefully and completely to…" Kwang's loan-modification requests.[24] A contrary duty in tort would create obligations "unnegotiated or agreed to by the parties" – and worse, it would dictate terms contradicting the parties' allocation of rights and responsibilities.[25]

Second, along with the parties' agreement, the *Sheen* Court supported its no-duty rule with another principle of California law from *Nymark v. Hear Fed. Sav. & Loan Ass'n*, 231 Cal. App. 3d 1089 (1991).[26] *Nymark* announced a general rule that "a financial institution owes no duty of care to a borrower when the institution's involvement in the loan transaction does not exceed the scope of its conventional role as a mere lender of money."[27] The *Sheen* Court recognized a lender's handling of a loan modification fits perfectly into *Nymark's* general rule. As the *Sheen* Court explained, "a lender's involvement in the loan modification… is part and parcel of its assessment regarding how best to recoup the money it is owed."[28] *Nymark* too supported the conclusion that a lender owes no duty to a borrower in its processing of a loan modification application.[29]

Lastly, the *Sheen* Court rejected Kwang's doom-and-gloom plea for relief. Kwang argued that if he could not pursue a negligence claim, he would be left "without any remedy at all."[30] Not so. Kwang had other claims to address Wells Fargo's alleged mishandling of his loan-modification request (negligent misrepresentation and promissory estoppel), but he did not bring those

---

[20] *Sheen*, 2022 WL 664722, at *7.
[21] *Id.* at *6 (citing *Erlich v. Menezes*, 21 Cal. 4th 543, 550-51 (1999).
[22] *Sheen*, 2022 WL 664722, at *7.
[23] *Id.* (citing *Trustors Sec. Serv. v. Title Recon Tracking Serv.*, 49 Cal. App. 4th 592, 595 (1996) superseded by statute as stated in *Ricketts v. McMormack*, 177 Cal. App. 4th 1324 (2009)).
[24] *Sheen*, 2022 WL 664722, at *7.
[25] *Id.*
[26] *Sheen*, 2022 WL 664722, at *9.
[27] *Id.* (citing *Nymark*, 231 Cal. App. 3d at 1096).
[28] *Sheen*, 2022 WL 664722, at *10.
[29] *Id.*
[30] *Sheen*, 2022 WL 664722, at *19.

claims against Wells Fargo.[31] Concerned too about creating an ill-defined and amorphous tort remedy by "judicial fiat," the *Sheen* Court expressed its preference for a legislative response to this recurring lender-borrower dispute.[32] Congress and the California Legislature, the *Sheen* Court felt, are best suited to pass legislation prescribing "the obligations of lenders who handle mortgage modification applications."[33]

Although *Sheen* upheld the majority no-duty rule, and overruled four contrary lower court decisions, financial institutions and loan services should take *Sheen* with cautious optimism.[34] *Sheen* has now squarely foreclosed general negligence claims against a lender for mishandling a borrower's loan modification. But as *Sheen* cautioned, a borrower upset with a lender's loan modification review can circumvent the no-duty rule with other tort-based claims challenging the lender's conduct.

Jarrett S. Osborne-Revis
Attorney
(916) 945-5190
josbornerevis@buchalter.com

Robert S. McWhorter
Shareholder
(916) 945-5188
rmcwhorter@buchalter.com

This communication is not intended to create or constitute, nor does it create or constitute, an attorney-client or any other legal relationship. No statement in this communication constitutes legal advice nor should any communication herein be construed, relied upon, or interpreted as legal advice. This communication is for general information purposes only regarding recent legal developments of interest, and is not a substitute for legal counsel on any subject matter. No reader should act or refrain from acting on the basis of any information included herein without seeking appropriate legal advice on the particular facts and circumstances affecting that reader. For more information, visit www.buchalter.com.

[31] *Id.* at *19-20.
[32] *Id.* at *20.
[33] *Sheen*, 2022 WL 664722, at *20.
[34] Sheen overruled *Weimer v. Nationstar Mortg.*, LLC 47 Cal. App. 5th 341 (2020), *Rossetta v. CitiMortg., Inc.*, 18 Cal. App. 5th 628 (2017), *Daniels v. Select Portfolio Servicing, Inc.*, 246 Cal. App. 4th 1150 (2016), and *Alvarez v. BAC Homes Loans Servicing, L.P.*, 228 Cal. App. 4th 941 (2014). *Sheen*, 2022 WL 664722, at *22 n.12.