




CALIFORNIA
BANKERS
ASSOCIATION

Legislative Update

Jason Lane, SVP & Director of Government Relations

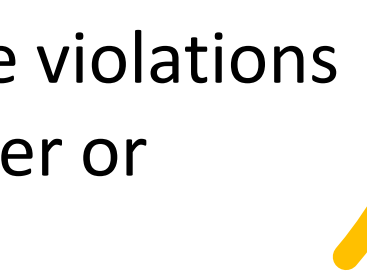
Vanessa Lugo, Senior Legislative Advocate

Legislative Session Status

- August 31 – Legislature adjourns
 - September 30 – Governor's signature/veto
 - November 5 – Presidential general election
 - December 2 – Legislative org. session
- 

Financial Abuse of Elder and Dependent Adults

SB 278 (Dodd)

- Requires establishment of an emergency financial contact program and outreach when financial abuse is suspected
 - Mandates a delay on certain transactions for three business days
 - Significant penalties for multiple violations involving the same accountholder or reckless disregard
- 

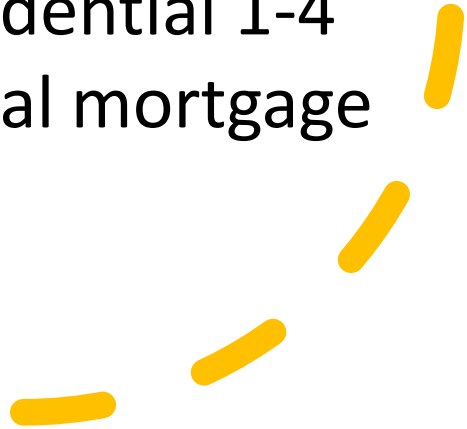
Foreclosure - Equity Sales

AB 2424 (Schiavo)

- Allows a borrower to establish a trusted contact at loan origination or during pre-foreclosure due diligence
- Delays a trustee's sale by 45 days if a borrower submits a valid listing agreement and 45 days if there is a bona fide purchase agreement
- Requires an initial trustee's sale to establish sales price @ 2/3rds of value

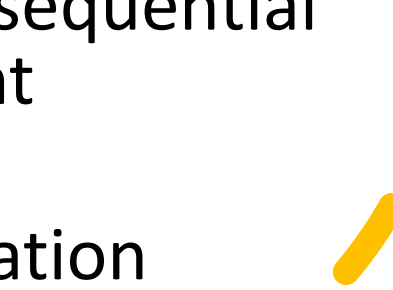
Loan Assumption - Dissolution of Marriage

AB 3100 (Low)

- Codifies GSE servicing guidelines for loan assumptions for dissolution of marriage
 - Starting 1.1.27 must include a provision allowing co-borrower assumption
 - Applies to owner-occupied, residential 1-4 real property with a conventional mortgage
- 

Automated Decision Tools

AB 2930 (Bauer-Kahan)

- Requires annual impact assessments to be conducted by developers and deployers
 - Applies to various activities and industries, including financial services
 - Subsequently narrowed to consequential decisions involving employment
 - Prohibits algorithmic discrimination
- 

Frontier Artificial Intelligence

SB 1047 (Wiener)

- Requires AI model developers and those training models to establish safeguards that prevent critical harms
- Establishes a state entity to oversee the development of these models
- Requires a developer to submit a statement of compliance to the AG

California Privacy Rights Act

- CPPA rulemaking effort underway on cyber audits, risk assessments and ADS
- Board meeting on 11.8.24
- Awaiting approval and submission to OAL



Client Trust Account Reporting

AB 3279 (Judiciary)

- Requires annual reporting by FIs on client trust accounts starting 3.1.26
- Includes data points, like attorney license number, account balance as of 12.31, etc.
- FIs must collect attorney license number on new CTAs established on or after 1.1.26
- Immunity for discharging or failing to discharge duties

Employer Communication – Intimidation

SB 399 (Wahab)

- Prohibits an employer from subjecting an employee to discharge, discrimination, retaliation because the employee declines to attend an employer-sponsored meeting about employer's opinion on religious or political matters
- Excludes communicating information that the employer is required by law to communicate and information necessary to perform job duties

Thank you!



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October ____, 2024

Critical Case Law: Recent Case Law Shaping the Banking Industry

Robert S. McWhorter



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Welcome and Introduction



➤ Program Overview

- **Economic Loss Rule/Fraudulent Concealment**
- **Preemption under National Bank Act (State laws re: interest on Escrow Accounts)**
- **Hacking and Intercepted Wire Transfers**
- **Default Interest Update**



Rattagan v. Uber Technologies, Inc.
(Aug. 22, 2024, No. S272113) ____ Cal.5th ____
[2024 Cal. LEXIS 4639]



➤ *Rattagan v. Uber Technologies, Inc.* (Aug. 22, 2024, No. S272113) ____ Cal.5th ____ [2024 Cal. LEXIS 4639]

Key Facts

- **2013-2015:** Rattagan, a lawyer, provided legal services for Uber's Dutch subsidiaries and acted as their legal representative in Argentina, exposing him to legal risks under a contract that included an indemnity clause protecting him from liabilities arising from his role as Uber's legal representative.
- **April 2016:** Uber launched its ridesharing platform in Buenos Aires without informing Rattagan, despite knowing it would violate local regulations.
- **Consequences:** Rattagan faced criminal charges, media backlash, and reputational harm.
- **Lawsuit:** Rattagan sued Uber for fraudulent concealment, claiming Uber intentionally withheld information that could have prevented his legal and reputational issues.



➤ ***(Rattagan v. Uber Technologies, Inc. (Aug. 22, 2024, No. S272113)***
___Cal.5th___ [2024 Cal. LEXIS 4639].)

Issue: Whether a plaintiff may assert a tort claim for fraudulent concealment arising from or related to the performance of a contract?

Answer: Qualified Yes.

Holding:

A plaintiff may assert a fraudulent concealment cause of action based on conduct occurring in the course of a contractual relationship **if**

- (1) the elements of the claim can be established independently of the parties' contractual rights and obligations, and
- (2) the tortious conduct exposes the plaintiff to a risk of harm beyond the reasonable contemplation of the parties when they entered into the contract.

➤ *Rattagan v. Uber Technologies, Inc.* (Aug. 22, 2024, No. S272113) ____ Cal.5th ____ [2024 Cal. LEXIS 4639]

- **Economic Loss Rule:**

- ✓ **General Rule:** bars recovery in tort for purely economic losses that arise from a breach of contract, limiting the plaintiff to contractual remedies.
- ✓ **Exception:** Rule does not bar tort claims for fraudulent concealment if the tortious conduct is independent of the contract and exposes the plaintiff to risks beyond those reasonably contemplated when the contract was formed.
- ✓ If the fraud leads to unanticipated harm, fraudulent concealment claim can be brought.

- **Implications**

- ✓ Banks may face litigation for fraudulent concealment during loan agreements or other contractual relationships
- ✓ Banks cannot rely solely on the economic duress rule to protect them against tort claims.



Cantero v. Bank of Am., N.A. (2024)
____ U.S. ____ [144 S.Ct. 1290, 218 L.Ed.2d 664]



➤ *Cantero v. Bank of Am., N.A.* (2024) ____ U.S. ____ [144 S.Ct. 1290, 218 L.Ed.2d 664]

The Facts

Factual Background

- Petitioners obtained home mortgage loans from Bank of America in New York and were required to maintain escrow accounts for paying property taxes and insurance.
- New York General Obligations Law § 5-601 mandates that banks pay a minimum of 2% interest on escrow account balances.
- Bank of America did not pay interest on the petitioners' escrow accounts, asserting that federal law, specifically the National Bank Act, preempted the New York requirement.

Procedural Background

- ✓ **District Court:** Ruled in favor of the petitioners, finding no preemption.
- ✓ **Second Circuit Court of Appeals:** Reversed the decision, holding that the New York law was preempted as it interfered with the federal powers of national banks.



➤ *Cantero v. Bank of Am., N.A. (2024)* ____ U.S. ____ [144 S.Ct. 1290, 218 L.Ed.2d 664]

Ruling

- The U.S. Supreme Court (9-0) vacated the Second Circuit's ruling and remanded the case for further analysis.
- The Court ruled:
 - ✓ The Second Circuit failed to properly apply the standard set forth in *Barnett Bank of Marion County, N. A. v. Nelson* (1996) ("Barnett")
 - ✓ Not all state laws are preempted under the NBA unless they significantly interfere with national bank powers even if they touch upon areas regulated by federal law. The key is whether state law "prevents or significantly interferes with" a national bank's federally granted powers as required under Barnett.
 - ✓ Preemption requires a detailed, practical assessment of the actual impact of the state law on national bank operations
 - ✓ Advised that avoid categorical rulings of preemption.



Kivett v. Flagstar Bank (9th Cir. Aug. 22, 2024, No. 21-15667) 2024 U.S. App. LEXIS 21222



➤ *(Kivett v. Flagstar Bank (9th Cir. Aug. 22, 2024, No. 21-15667) 2024 U.S. App. LEXIS 21222.)*

Factual Background

- Borrowers sued Flagstar Bank claiming that it failed to pay 2% interest on escrow accounts, as required by California Civil Code § 2954.8(a) which states:
 - (a) Every financial institution that makes loans upon the security of real property containing only a one- to four-family residence and located in this state or purchases obligations secured by such property and that receives money in advance for payment of taxes and assessments on the property, for insurance, or for other purposes relating to the property, shall pay interest on the amount so held to the borrower. The interest on such amounts shall be at the rate of at least 2 percent simple interest per annum. Such interest shall be credited to the borrower's account annually or upon termination of such account, whichever is earlier.
- Flagstar argued that this state law was preempted by the National Bank Act



➤ (*Kivett v. Flagstar Bank* (9th Cir. Aug. 22, 2024, No. 21-15667) 2024 U.S. App. LEXIS 21222.)

Ruling

- Court relied upon *Cantero v. Bank of America, N.A.*
- Confirms that state laws requiring escrow interest payments are not preempted by the NBA under Dodd-Frank.
- Dodd-Frank requires compliance with state laws that do not "prevent or significantly interfere" with national bank operations.
- Payment of interest does not interfere with operations



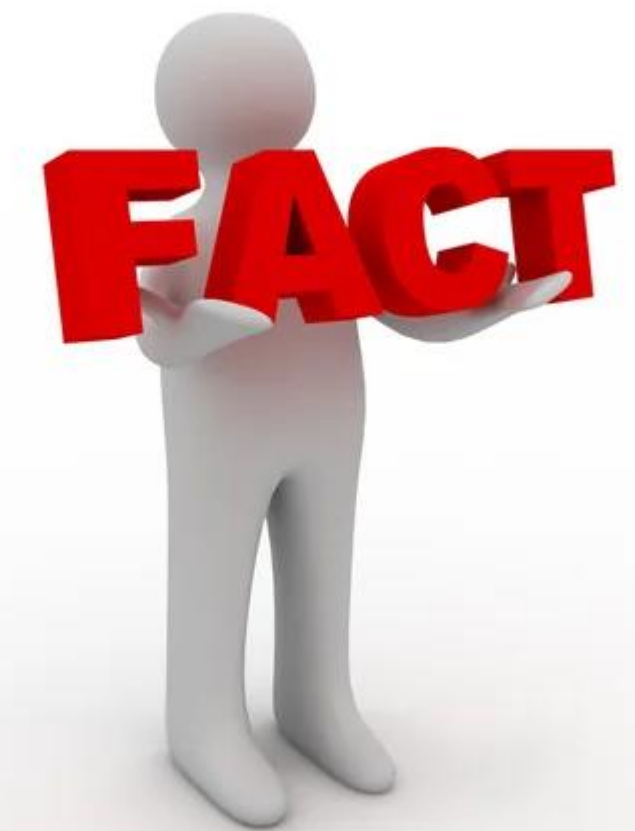
*Approved Mortg. Corp. v. Truist Bank
(7th Cir. 2024) 106 F.4th 582*



➤ *Approved Mortg. Corp. v. Truist Bank (7th Cir. 2024) 106 F.4th 582*

The Facts

- Approved Mortgage received wire transfer instructions from two customers altered by unknown hackers, substituting Truist Bank (formerly SunTrust Bank) for Huntington Mortgage Company
- Approved Mortgage initiated over \$550,000 in wire transfers through MVP Title to Truist Bank
- Truist Bank accepted wire transfers and applied the funds to an account at Truist matching the account number on the altered wire instructions, belonging to AER Operations, LLC, which did not match the other information provided in these instructions.
- Funds were subsequently withdrawn via cashier's checks and converted to cryptocurrency.
- Truist had signs of suspicious activity previously stopped wire transfers to AER account on suspicion of fraud and “other irregularities”
- Approved Mortgage sued Truist Bank asserting
 - 4A-207 Claim
 - Negligence



➤ *Approved Mortg. Corp. v. Truist Bank (7th Cir. 2024) 106 F.4th 582*

Legal Issue - UCC 4A-207: Misdescription of Beneficiary

- **Nonexistent/Unidentifiable Beneficiary (§ 4A-207(a))**
 - ✓ If the beneficiary's name or account number refers to a nonexistent or unidentifiable person, no one has rights as a beneficiary. Acceptance of the payment order cannot occur in such cases.
- **Inconsistent Name and Account Number (§ 4A-207(b))**
 - ✓ If the name and account number identify different persons, the beneficiary's bank can rely on the account number unless it knows of the discrepancy.
 - ✓ If the bank pays the wrong person based on the name, the correct payee (if entitled) is the only one with rights.
- **Obligations of the Originator (§ 4A-207(c))**
 - ✓ **If** the originator is a bank, it is obliged to pay the order.
 - ✓ If the originator is not a bank and the payment was made to an incorrect beneficiary, the originator is not obliged to pay unless they had prior notice that the bank could rely solely on the account number.
- **Recovery Rights (§ 4A-207(d)).**
 - ✓ Recovery of misdirected funds is governed by law on mistake and restitution

 *Approved Mortg. Corp. v. Truist Bank (7th Cir. 2024) 106 F.4th 582*

Legal Analysis: 4A-207

- The Seventh Circuit analyzed whether Truist Bank had a duty to verify the match between the beneficiary's name and account number.
- The court ruled that under UCC 4A-207, Truist Bank was not required to ensure the names matched as long as the account number provided was correct.
- The court emphasized the importance of the account number in the payment process.
- The court held dismissed Truist finding no liability.
- Privity Requirement: The court upheld that privity is necessary under 4A-402(d) for a refund.
- Section 402(d) provides a “money-back guarantee” but is limited to the sender-receiver bank relationship. A receiving bank must refund its sender, even if it will not receive a refund from its receiving bank.



Legal Analysis: Negligence

•Negligence Claim:

- ✓ **Claim by Plaintiff:** Approved Mortgage Corp. argued that Truist Bank was negligent in processing the wire transfer, leading to financial loss due to the mismatch between the beneficiary name and account number.
- ✓ **Standard of Care:** The court examined whether Truist Bank breached a duty of care in handling the wire transfer.

•**Ruling:** The court determined that Truist Bank's reliance on the account number, as permitted by UCC 4A-207, did not constitute negligence. Since UCC 4A-207 allows banks to process transfers based on account numbers without verifying the beneficiary name, Truist Bank was not negligent.



*Honchariw v. FJM Private Mortgage Fund,
LLC (2022) 83 Cal.App.5th 893
& Default Interest Update*



➤ Default Interest

Honchariw v. FJM Private Mortgage Fund, LLC (2022) 83 Cal.App.5th 893

- **Background:**

- ✓ Husband and wife received a \$5.6 million **commercial** loan with an 8.5% interest rate.
- ✓ They missed **one** payment, triggering a late fee and a 9.99% default interest on the entire unpaid principal.
- ✓ They sued bank claiming that late fee and default interest were unlawful penalties per Civil Code § 1671
- ✓ **Loan documents acknowledged that it would be difficult to estate expense as a result of default**



➤ Default Interest

Honchariw v. FJM Private Mortgage Fund, LLC (2022) 83 Cal.App.5th 893

- **Court Ruling:**

- ✓ “[L]iquidated damages in the form of a penalty assessed during the lifetime of a partially matured note against the entire outstanding loan amount are unlawful penalties.”
- ✓ “Late charges [and default interest] based on the entire unpaid [principal] balance for failure to pay an installment was punitive and was not rationally calculated to merely compensate the injured lender.”
- ✓ Loan document found be insufficient to show that the parties “attempted to estimate their damages in the amount of breach and that the late fee [and default interest] represents the reasoned outcome of such an attempt.”
- ✓ Late fees and default interest on matured loan is presumed valid

➤ Default Interest

Laser Pro's Response to *Honchariw*

_____ INCREASED POST-MATURITY RATE. You have selected to provide for an increased interest rate following default in the Interest After Default policy component for this California loan. Our California counsel has advised that a California court recently found that liquidated damages in the form of an increased interest rate assessed against the entire outstanding balance of an unmatured loan qualified as an unlawful penalty under California law. Therefore, when California law applies and your financial institution has chosen an increased post-default rate in Standard Policy for the loan, the Interest After Default paragraph provides only for application of the increased interest rate on a fully matured note. Additionally, our California counsel advised that since increased interest after default provisions have been scrutinized by California courts, and since this is a developing area of the law, it is possible that a court may even find that default interest applied to the principal balance upon maturity, or upon acceleration of the loan (which is an issue that has not yet been clearly addressed by California courts), may not be enforceable in certain situations. Consult your legal counsel if you have questions. _____

Problems:

- (1) “California counsel has advised us. . .”
- (2) Take broadest view



Cases Post- *Honchariu*

- *Cohen & Assocs. Invs., LLC v. Luther Burbank Sav.*, 2023 Cal. Super. LEXIS 99490 (LA Superior Court – December 11, 2023):
 - Facts: Cohen alleged that LBS illegally imposed a 10% default interest rate upon default, significantly increasing monthly payments by 356%.
 - Upon default, LBS accelerated the loan, demanding full payment of the remaining balance plus default interest.
 - Cohen sued LBS for breach of contract and negligent misrepresentation related to the default interest and acceleration provisions.
 - Court denied finding that the legality of the default interest rate provisions remains a factual issue

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QUESTIONS?