UNITED STATES BANKRUPTCY COURT
Eastern District of California

Honorable Michael S. McManus
Bankruptcy Judge
Sacramento, California

January 21, 2014 at 10:30 a.m.

---

1. 10-51694-A-13 MERCEDITA/RUEL PALMERA — CONTINUED TRIAL RE: AMENDED COMPLAINT
12-2202 — 6-12-12 [11]
PALMERA ET AL V. WASHINGTON MUTUAL BANK ET AL

Tentative Ruling: The parties have stipulated that the court may determine the facts and apply the apply based on the written record they have presented to the court. Based on that record judgment for JPMorgan Chase Bank will be entered.

"[O]n or about October 1, 2005, the plaintiffs obtained a revolving home equity line of credit from Washington Mutual Bank in the maximum amount of $200,000. Ex. 2 to Johnston Decl. ¶ 1. The plaintiffs executed a loan agreement with WaMu, promising to repay 'all advances from the Credit Line' and other fees charges and expenses. Ex. 2 to Johnston Decl. ¶ 1. The loan was assigned a loan number ending on 2371. Ex. 2 to Johnston Decl.

"The loan agreement provided for, and was secured by, a deed of trust on the property. Ex. 2 to Johnston Decl. ¶ 3; Ex. 3 to Johnston Decl. ¶ 2. The plaintiffs executed the deed of trust on October 15, 2005. Ex. 3 to Johnston Decl. The deed was recorded on October 27, 2005. Ex. 3 to Johnston Decl.

"The loan agreement says that the plaintiffs 'may obtain advances from the Credit Line up to the Credit Limit, repay any portion of the amounts advanced and obtain additional advances up to the Credit Limit.' Ex. 2 to Johnston Decl. ¶ 2. The agreement allowed the plaintiffs to have two types of advances under the equity line, variable rate advances and fixed rate loans. Ex. 2 to Johnston Decl. ¶¶ 1, 4. It provided that the plaintiffs must make one monthly payment for the variable rate advances and another, separate monthly payment for the fixed rate loan(s). Ex. 2 to Johnston Decl. ¶ 4.

"The plaintiffs requested their first fixed rate loan under the agreement on October 1, 2005. The amount was $100,000. The fixed rate loan option confirmation contains the equity line loan/account number, 2371, as well as a fixed rate loan option number, ending on 2389. Ex. 4 to Johnston Decl.

"The confirmation states: 'This will serve as confirmation that you have exercised the Fixed Rate Loan Option (FRLO) under your WaMu Equity Plus line of credit. This FRLO is subject to the WaMU Equity Plus Agreement and Disclosure (Agreement) between you and Washington Mutual Bank [ ] (the Bank) and is secured by a security instrument (Security Instrument) evidencing the Bank's security interest in your property.' It states also: 'By signing below, you confirm your request for a FRLO subject to the above-stated terms and you acknowledge and agree that this FRLO will be subject to the terms and conditions of the Agreement and Security Instrument.' Ex. 4 to Johnston Decl.

"The plaintiffs requested their second fixed rate loan under the agreement on December 19, 2006. The amount was $64,999.98. The fixed rate loan option confirmation contains the equity line loan/account number, 2371, as well as a fixed rate loan option number, ending on 2881. This confirmation contains the identical language as the confirmation evidencing the plaintiffs' prior fixed rate loan option. Ex. 5 to Johnston Decl.

"Since taking over WaMu, JPMorgan Chase Bank has continued to abide to the terms of the equity line agreement, honoring the terms of the plaintiffs' fixed rate loan options. Ex. 7 to Johnston Decl."

Docket 89 at 2.

The plaintiffs' amended complaint (Docket 11), filed on June 12, 2012, naming JPMorgan Chase Bank and WaMu as defendants, contains the following claims:

(1) A claim disputing the defendant's interest in the property; the first amended complaint says that the defendant's claim is not secured by the plaintiffs' real property on Levant Court in Elk Grove, California, "other than as to WaMu account #[XXXXXX2371]," asking the court to declare the remaining loans held by the defendant as a general unsecured claim.

(2) A claim asking the court to quiet title of the real property.

(3) A claim for fraud in the formation of the "WaMu Equity Plus" contract with the plaintiffs.

(4) A claim for negligent misrepresentation in the formation of the "WaMu Equity Plus" contract with the plaintiffs.

(5) A claim for constructive fraud in the formation of the "WaMu Equity Plus" contract with the plaintiffs.

(6) A claim for breach of contract in the formation of the loan contracts between WaMu and the plaintiffs.

The first amended complaint does not ask for monetary relief. It asks only for a declaration that the plaintiffs are owners of the property and that the defendant has a security interest in the property, only "as to WaMu account #[XXXXXX2371]." The first amended complaint also asks for an order sustaining the objection to the secured status of the defendant's claim.

On August 9, 2012, the court entered an order dismissing the plaintiffs' claims for: quiet title of the property, actual fraud, constructive fraud, negligent misrepresentation, and breach of contract. This leaves the plaintiffs' cause of action seeking a declaration that the defendant's claim is not secured by the property. Dockets 37 & 40.

The plaintiffs' trial brief asserts: "The contract provision preventing any division of the first and second claim is [an] unconscionable term and should therefore allow for a contract interpretation that allows for two claims." The court rejects this assertion for two reasons.

First, the plaintiffs' amended complaint does not say anything about an unconscionable term of contract between the parties. There is no cause of action based on unconscionability in the amended complaint. The plaintiffs had asserted a claim for breach of contract, which the court dismissed on August 9,

2012. The court will not allow the plaintiffs to assert this new cause of action on the eve of trial.

Second, as the court ruled on JPMorgan Chase Bank's motion to dismiss the amended complaint:

"Under the agreement with the FDIC, the defendant has not assumed 'any liability associated with borrower claims for payment of or liability to any borrower for monetary relief, or that provide for any other form of relief to any borrower, whether or not such liability is reduced to judgment, liquidated or unliquidated, fixed or contingent, matured or unmatured, disputed or undisputed, legal or equitable, judicial or extra-judicial, secured or unsecured, whether asserted affirmatively or defensively, related in any way to any loan or commitment to lend made by [WaMu] prior to failure (September 25,2008) . . . or otherwise arising in connection with [WaMu's] lending or loan purchase activities.' Such liabilities 'are specifically not assumed by [the defendant].' See Ex. F to RJN at 9."

Docket 37.

In other words, seeking any form of relief against the defendant, including a request for declaration that one of the terms of the contract between the plaintiffs and WaMu is unconscionable, is barred by the defendant's agreement with the FDIC.

Finally, the provision is not unconscionable and there is no rational explanation from the plaintiffs as to why this provision in the contract is unconscionable.

Accordingly, the court will dismiss the plaintiffs' unconscionability claim.

Turning to the remainder of the amended complaint, on April 29, 2013, the court adjudicated the defendant JPMorgan Chase Bank's summary judgment motion, concluding that:

"Based on the unrefuted facts in the defendant's motion and statement of undisputed facts, the debt incurred by the plaintiffs under both options is secured by the same deed of trust the plaintiffs executed in connection with the equity line agreement. There is no genuine issue of material fact as to this.

. . .

"Fourth, the court's determination that the debt incurred by the plaintiffs under the fixed rate loan options is secured by the deed of trust executed by them in connection with the equity line agreement does not resolve this adversary proceeding in its entirety. The court agrees with the plaintiffs that the next important issue is whether the debt incurred under the two fixed rate loan options represents one or two loans for purposes of allowing the plaintiffs to strip off the debt incurred under the latter of the two fixed rate loan options. See 11 U.S.C. § 506(a)(1) (providing that a secured claim is a secured claim only to the extent of the creditor's interest in the estate's interest in the collateral)."

Docket 89 at 3, 4.

The issue left for this court to decide is whether the debt incurred under the

two fixed rate loan options represents one or two claims for purposes of allowing the plaintiffs to strip off under 11 U.S.C. § 506(a)(1) the debt incurred under the latter of the two fixed rate loan options.

In the Bankruptcy Code, the term "claim" is broadly defined as "(A) right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured." 11 U.S.C. § 101(5).

The Ninth Circuit has identified the above definition as the "broadest possible definition" of claim. "This 'broadest possible definition' of 'claim' is designed to ensure that 'all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the bankruptcy case.'" California Dept. of Health Servs. v. Jensen (In re Jensen), 995 F.2d 925, 929-30 (9th Cir. 1993) (citing to H.R.Rep. No. 595, 95th Cong., 2d Sess. 1, 309 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6266; S.Rep. No. 598, 95th Cong., 2d Sess. 1, 22, reprinted in 1978 U.S.C.C.A.N. 5787, 5808).

The broad definition of a claim in the Bankruptcy Code is not boundless, however. In Jensen, the Ninth Circuit identified four different tests for determining when a claim arises:

(1) the claim arises when the right to payment accrues,

(2) the claim arises when a relationship is established between the debtor and the creditor, *i.e.*, the earliest point in the relationship between the debtor and the creditor,

(3) the claim arises at the time of the debtor's conduct, or

(4) the claim arises from damages that can be fairly contemplated by the parties at the time of the debtor's bankruptcy.

Jensen at 928-31.

First, Jensen rejected and this court also rejects the "right to payment" test because it ignores the scope of the claim definition in 11 U.S.C. § 101(5). By including contingent and unmatured rights to payment, that provision clearly goes beyond the mere right to payment. Jenses at 929.

Second, the court in Jensen was not impressed with the "relationship" test either. The test is over-inclusive as it could easily encompass debt that was not fairly contemplated by the parties.

In addition, Jensen discussed the test mainly in the context of tort claims, where the conduct underlying the claim was committed pre-petition, but it or the resulting injury was not discovered until after the petition date.

Here though, the claim at issue relates to a contractual obligation, and not tortious misconduct. The plaintiffs committed themselves to a contractual obligation to repay a loan.

Third, the "debtor's conduct" test, also mainly applied in the context of tort

claims, provides that the bankruptcy claim arises at the time of the debtor's conduct relating to the misconduct.

The "debtor's conduct" test does not work well in the context of contractual obligations either. Under the test, a contractual right to payment would not be a claim for bankruptcy purposes until the debtor breaches his obligation to pay. Such outcome under the debtor's conduct test does not comport with the scope of the claim definition in 11 U.S.C. § 101(5). As with the "right to payment test," by including contingent and unmatured rights to payment, that provision clearly goes beyond the mere breach of a contractual obligation to pay. See Jenses at 929.

For instance, bankruptcy law does not wait for the debtor to default on ongoing debt so he can obtain a discharge of his personal liability on that debt. The fact that the debtor may be current on an ongoing debt as of the petition date does not prevent him from receiving a bankruptcy discharge.

This is the case with secured debt that goes through bankruptcy, including promissory notes financing the purchase of vehicles and notes and home equity lines of credit financing the purchase of homes. The same is true with respect to unsecured debt, such as credit card debt. The debtor does not have to be in default on a debt in order to receive a discharge.

This leaves the "fair contemplation" test, 11 U.S.C. § 101(5), and the definition of a contingent claim.

"[C]laims are contingent . . . if the debt is one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event which will trigger the liability of the debtor to the alleged creditor and if such triggering event or occurrence was one reasonably contemplated by the debtor and creditor at the time the event giving rise to the claim occurred."

Hexcel at 567 (determining that the bankruptcy court correctly applied the fair contemplation test; quoting Semel v. Dill (In re Dill), 731 F.2d 629, 631 (9th Cir. 1984)).

Claims that are contingent or unmatured under state law are nevertheless claims for bankruptcy purposes, even though not yet ripe for suit. See e.g., Stone Street Services, Inc. V. Granati (In re Granati), 271 B.R. 89, 94 (Bankr. E.D. Va. 2001) (noting that a pre-petition indemnification agreement gives the indemnitee a contingent pre-petition claim, even where the conduct giving rise to the indemnification occurs post-petition; also noting that product defect injuries resulting from a pre-petition installation of the product are a claim even though injury did not manifest itself until after bankruptcy filing).

With the above in mind, the court concludes that the plaintiffs incurred a single contingent claim with WaMu when they executed on October 1, 2005 a revolving home equity line of credit with WaMu in the maximum amount of $200,000. The plaintiffs executed a Loan Agreement with WaMu, promising to repay "all advances from the Credit Line" and other fees charges and expenses.

In other words, at that time, the plaintiffs promised to pay a debt only upon the occurrence or happening of an extrinsic event - when the plaintiffs took advances on the credit line.

Advances to the plaintiffs triggered their liability under the Loan Agreement/Credit Line with WaMu. If the plaintiffs had not obtained advances,

they would have had no liability under the Loan Agreement/Credit Line to WaMu.

And, the plaintiffs' obtaining of the advances was reasonably contemplated by the plaintiffs and WaMu at the time the event giving rise to the claim occurred, *i.e.*, when the plaintiffs executed the Loan Agreement/Credit Line on October 1, 2005. The contemplation is evident from and it is reasonable given the fact that the plaintiffs promised in the Loan Agreement/Credit Line "to repay 'all advances from the Credit Line' and other fees charges and expenses." Docket 89 at 2.

It is not the conduct of entering into a loan agreement that must have been fairly contemplated by the parties. It makes no sense to contemplate conduct that has already taken place.

In both Jensen and Hexcel, the contemplation is about what happens in the future. It is "all future response and natural resource damages cost based on pre-petition conduct that can be fairly contemplated by the parties at the time of [d]ebtors' bankruptcy are claims under the [Bankruptcy] Code." Jensen at 930. The contemplation is of the "future response and natural resource damages cost," not the "pre-petition conduct."

Hexcel defines it as the "triggering event or occurrence [that] was . . . reasonably contemplated by the debtor and creditor at the time the event giving rise to the claim occurred." The triggering event and the event giving rise to the claim are different events.

The triggering event is the advances taken by the plaintiffs, while the event giving rise to the claim is the plaintiffs executing the Loan Agreement/Credit Line with WaMu on October 1, 2005.

In short, because the plaintiffs' obtaining advances was reasonably contemplated by them and WaMu at the time the Loan Agreement/Credit Line was executed, on October 1, 2005, on that date the plaintiffs incurred a single claim that was contingent on the plaintiffs obtaining advances.

More, there is no dispute that the plaintiffs requested and obtained two advances from WaMu pursuant to the Loan Agreement/Credit Line. One of the advances was obtained on October 1, 2005 in the amount of $100,000 and the other advance was obtained on December 19, 2006 in the amount of $64,999.98. Docket 89 at 2.

Given the foregoing, the court concludes that JPMorgan Chase Bank holds a single claim secured by the subject property, comprising both advances obtained by the plaintiffs.

The above interpretation of the agreement between the parties is consistent with the fact that all amounts due under the Loan Agreement/Credit Line and subsequent advances obtained by the plaintiffs, are secured by a single deed of trust on the subject real property. The fact that each advance had different terms of repayment, including interest rates and payoff dates, is not sufficient to transform the advances into separate claims for purposes of this bankruptcy case. The fact is that there is one Loan Agreement/Credit Line that establishes and governs a standard set of terms for all anticipated advances to be obtained by the plaintiffs, including how the rates will be calculated, will the rates be fixed or variable, the ceiling for the advance amounts, how often advances may be obtained, the manner in which the advances may be obtained, etc.

For instance, "The Loan Agreement specifically sets forth that any and all advances made on the line of credit, defined as the Credit Line, are governed by the Loan Agreement, and that the Loan Agreement is a promise to pay 'all advances from the Credit Line'. The Loan Agreement also includes the following language: 'all amounts outstanding under the Credit Line that are covered by the Fixed Rate Loan Option described in Section 24 . . .', which makes it clear that any FRLO advances are covered by the Loan Agreement and are part of the Plaintiffs' promise to pay thereunder. Plaintiffs expressly agreed and acknowledged these terms by executing the Loan Agreement, and by executing the FRLO Confirmations which integrate and incorporate the Loan Agreement." Docket 106 at 11.

The plaintiffs have not refuted or explained the foregoing facts.

As the parties' statement of undisputed facts provides, the aggregate amount owed under both advances is $136,601.84 (consisting of the FRLO A advance with a balance of $77,323.06 and the FRLO B advance with a balance of $59,263.82. Docket 98 at 5. The plaintiffs have valued the subject property at $150,000, while there is a first mortgage on the property in favor of U.S. Bank, totaling $81,140.41, which leaves only $68,859.59 of equity in the property. Id.

As the subject property is the plaintiffs' principal residence and there is at least some equity to satisfy JPMorgan Chase Bank's single second mortgage claim on the property, the plaintiffs are not entitled to strip down the claim. See 11 U.S.C. § 1322(b)(2) (the anti-modification in chapter 13 cases).

Judgment will be entered for JPMorgan Chase Bank.

The court will reserve jurisdiction over the award of attorney's fees and costs. In its trial brief, JPMorgan Chase Bank has requested the court to award it attorney's fees and costs for defending this action. The plaintiffs have not addressed the issue of attorney's fees and costs in their trial brief.