

Ruling Could Shield Lenders Eviction Judgment Offers Protections

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IN ITS MOST SIMPLISTIC TERMS, the principle of “res judicata” or “already judged” means one party cannot sue later over the same claims after they’ve been addressed in a prior lawsuit. A recent court of appeals ruling in California suggests that in certain circumstances, an eviction judgment in the lender’s favor can potentially avoid future foreclosure litigation and protect against subsequent challenges to a lender’s title to the property.

An eviction action is generally limited to the issue of possession. Adjudication of a loan dispute or other title is-sues, other than procedural issues involving the trustee’s sale in conformance with California civil code (Section 2924), is usually not permitted in an unlawful detainer (eviction) action. As a result, a judgment entered by an eviction action has a very limited res judicata effect on a subsequent wrongful foreclosure lawsuit, leaving the evicted borrower free to challenge the foreclosure and related title issues in a subsequent wrongful foreclosure case. A recent court of appeals ruling, however, changes the landscape.

In *Malkoskie v. Option One Mortgage*, a California court of appeals case stemming from a Los Angeles County post-foreclosure eviction action, the Court of Appeals held that the judgment in the eviction proceeding had a “preclusive effect” on the issue of lawful title to the property in a subsequent action seeking to challenge the foreclosure. In other words, the court ruled that the title issues had already been addressed in the eviction proceeding and couldn’t be raised again in the challenge to the foreclosure.

In the Malkoskie case, the lender, Wells Fargo, filed an unlawful detainer action (pursuant to Section 1161a) against the prior borrower, alleging that the foreclosure complied with California’s Civil Code section 2924. On the day of the unlawful detainer trial, the parties stipulated to a judgment giving Wells possession of the property.

After the eviction, the prior borrowers sued Wells Fargo to set aside the foreclosure and the subsequent eviction. Wells Fargo and its loan servicer, Option One, successfully demurred on the grounds that the stipulated judgment in the eviction case barred the borrower’s wrongful foreclosure claims in the new action. On appeal, the borrowers argued that a consent or stipulated judgment arising from a summary unlawful detainer proceeding had limited preclusive effect on the issue of lawful title to the subject property. The appeals court disagreed, finding that the validity of title was conclusively resolved in the unlawful detainer action and affirmed the trial court’s sustaining of the demurrer and judgment of dismissal. The Court of Appeals explained that:

“Plaintiffs’ consent to the stipulated judgment in the un-lawful detainer action conclusively determined the specific factual contentions embraced by the complaint, namely that Wells Fargo had obtained valid record title pursuant to a nonjudicial foreclosure sale that had been duly conducted pursuant to statute...a) stipulated judgment normally concludes or determines all matters put into issue by the pleadings, unless the parties agree to restrict its scope by expressly withdrawing an issue from that judgment.”

Moreover, the Court of Appeals held that Option One, who was sued on the exact same grounds as Wells Fargo, was also entitled to use the stipulated unlawful detainer judgment as a shield, even though it was not a party to the unlawful detainer action.

The Court of Appeals' published decision suggests that a well-drafted stipulation or any favorable judgment in the eviction can potentially avoid future litigation and offer protection against subsequent challenges to a lender's title. On the flip side, a judgment in the borrower's favor could work against the lender in a subsequent wrongful foreclosure action.

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