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IN THE UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

WELLS FARGO BANK, N.A., and WELLS FARGO HOME MORTGAGE, INC., Plaintiffs, vs. DEMETRIOS A. BOUTRIS, in his official capacity as Commissioner of the California Department of Corporations, Defendant.	Civil Action No. S-03-0157 GEB JFM DEFENDANT'S MEMORANDUM OF POINTS AND AUTHORITIES IN OPPOSITION TO PLAINTIFFS' EX PARTE MOTION FOR TEMPORARY RESTRAINING ORDERS

I. NO TEMPORARY RESTRAINING ORDER SHOULD ISSUE

This Court should abstain from issuing temporary restraining orders to stay the administrative proceedings against plaintiff Wells Fargo Home Mortgage, Inc. (WFHMI) and allow the issues to be addressed through appropriate state court channels. Plaintiffs have not demonstrated that they will suffer irreparable harm and that they are likely to succeed at the time of trial in their federal action. Rather than abide by the laws under which WFHMI voluntarily obtained a license during the pendency of this federal litigation, plaintiffs are asking this Court to restrain a California

administrative action to revoke WFHMI's licenses based on plaintiff's failure to comply with state laws. In fact, plaintiffs are also requesting this Court sanction lawlessness on their behalf and approve the duplicity perpetrated on California consumers when WFHMI holds itself out as a licensee of the state, yet refuses to comply with the laws by which all other licensees are compelled to abide.

The inherent injustice in not allowing the Commissioner to proceed with a hearing to determine whether WFHMI violated the California Residential Mortgage Act (CRMLA) and the California Finance Lenders Law (CFLL) leaves the Commissioner in the position of having granted a license to a lender who because of a recent change in federal regulations, now claims: 1) it is above California law; 2) it does not need the licenses but still holds itself out as a licensee; 3) it will not surrender the licenses; and 4) it wants to keep the licenses andat the same time block the Commissioner's only remaining remedy to protect California consumers: revocation of the licenses.

While plaintiffs attempt to focus the Court's attention on the alleged harm they might suffer should the administrative hearing go forward, plaintiffs argument fails to acknowledge the serious consequences to California consumers from the issuance of a temporary restraining order. Not only will such an order provide sanction to WFHMI's continuing violation of California law pending the outcome of this federal action, but also allow it to affirmatively mislead California consumers into believing it is complying with the CRMLA and CFLL when it is not. The California Legislature enacted these provisions as consumer protection measures, contemplating compliance with all the laws in order to maintain a license.[1] There is no dispute that WFHMI, even before it could claim preemption based on the federal regulations effective August 1, 2001, was violating these consumer protection laws, yet it has refused to make the California consumers whole. Further, violations after the August 1, 2001, effective date were discovered and WFHMI has made no effort to comply with the law or make those consumers whole. Rather than complying with the law, which it concedes the

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[1] The California Legislature also envisioned exceptions to the requirement of licensing, such as for a national bank. Cal. Fin. Code §§50002-50003; Cal. Fin. Code §22050 et. seq.

OCC would have jurisdiction to enforce[2], WFHMI asks this Court to interfere with a state administrative action.

II. THIS COURT MAY NOT INTERFERE WITH THE PENDING STATE ADMINISTRATIVE ACTION

Federal courts may not enjoin or otherwise interfere with pending state actions, including administrative matters. *Younger v. Harris*, 401 U.S. 37, 49-53 (1971) and *Ohio Civil Rights Commission v. Dayton Christian Schools, Inc.*, 477 U.S. 619, 627 (1986). *Younger* sets forth the policy behind abstention of federal courts in state matters as follows:

> "This underlying reason for restraining courts of equity from interfering with criminal prosecutions is reinforced by an even more vital consideration, the notion of "comity," that is, a proper respect for state functions, a recognition of the fact that the entire country is made up of a Union of separate state governments, and a continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways."

Younger v. Harris, 401 U.S. at 44-45.

Younger involved a criminal matter where the defendant was indicted for violating the California Criminal Syndicalism Act in California state court. Defendant filed a complaint in federal district court requesting the court enjoin the district attorney from prosecuting him on the basis the state law was unconstitutional on its face and restricted his rights of free speech. Even where criminal statutes could be declared unconstitutional, the Supreme Court found that the district court should refrain from issuing an injunction because the injury to plaintiff was only that which was "incidental to every criminal proceeding brought lawfully and in good faith. (citations

[2] Plaintiffs adopt a position in their Reply Memorandum In Support of Plaintiff's Motion For Preliminary Injunction at page 6, lines 3-9, from which it may be concluded that if the Depository Institutions Deregulation Monetary Control Act (DIDMCA) does not preempt the California per diem statute, but the Office of the Comptroller of the Currency (OCC) is deemed to have jurisdiction over WFHMI, WFHMI will have been permitted by this Court to continue to violate a law during the pendency of the federal action. Further, only if plaintiffs prevail on both the claim that DIDMCA preempts the per diem statute *and* that the OCC has exclusive visitorial powers, could plaintiffs be entitled to claim they are not subject to the state laws.

omitted)" *Id.* at 46-47. "'No citizen or member of the community is immune from prosecution, in good faith, for his alleged criminal acts. The imminence of such a prosecution even though alleged to be unauthorized and hence unlawful is not alone ground for relief in equity which exerts its extraordinary powers only to prevent irreparable injury to the plaintiff who seeks its aid.' (citations omitted)." *Id.* at 46.

Here, while plaintiffs are not being subjected to a criminal prosecution, WFHMI is subject to the consequences incidental to its failure to comply with the CRMLA and CFLL, even if some portion of the law were determined by this Court to be preempted as to plaintiffs by federal regulations. However, even if WFHMI were granted some federally protected status, that does not mean that WFHMI has not violated provisions of the CRMLA and CFLL and should not be subject to the lawful consequences of the state administrative action: revocation of its license.

In *Ohio Civil Rights Commission v. Dayton Christian Schools, Inc.*, 477 U.S. 619, 627 (1986) the Supreme Court observed that "we thought that it was 'perfectly natural for our cases to repeat time and time again that the *normal* thing to do when federal courts are asked to enjoin pending proceedings in state courts is not to issue such injunctions.'"(emphasis added) *Id.*

It is also well settled that the *Younger* abstention doctrine applies to state administrative actions, even when the constitutional claims involved may only be decided on judicial review of the administrative decision. *Ohio Civil Rights Commission v. Dayton Christian Schools, Inc*., 477 U.S. at 627. In the *Ohio Civil Rights Commission* case, the Court held that an administrative sexual discrimination case could proceed against a Christian school, even though there were First Amendment implications, so long as the issues could be fully litigated. *Id.* at 628-629.

Decisions in the last ten years of the Ninth Circuit Court of Appeals where a Younger abstention motion was considered will not support plaintiffs' position. *See Montclair Parkowners Ass'n v. City of Montclair*, 264 F.3d 829 (9th Cir. 2001); *Green v. City of Tucson*, 255 F.3d 1086 (9th Cir. 2001*); Doe & Assocs. Law Offices v. Napolitano*, 252 F. 3d 1026 (9th Cir. 2001). For example in *Mullins v. Oregon*, 57 F.3d 789, 793 at fn. 4 (9th Cir. 1995), the court would not consider a Younger abstention argument because unlike here there were no ongoing state proceedings.

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Thus, a determination in the state administrative arena, where a state court appellate process is available to participants, is sufficient under *Younger* and *Ohio Civil Rights Commission* to adequately protect WFHMI's interests as to its licenses.

The Ninth Circuit Court of Appeals has identified three requirements that must be satisfied before a federal court may properly invoke the Younger abstention doctrine: "(1) ongoing state judicial proceedings; (2) implication of an important state interest in the proceedings; and (3) an adequate opportunity to raise federal questions in the proceedings. [Citations]" *Lebbos v. Judges of the Superior Court*, 883 F.2d 810, 814 (9th Cir. 1989) (citing *Middlesex County Ethics Comm. v. Garden State Barr Ass'n*, 457 U.S. 423, 432 (1982).).

A. No Federal Court Action On The Merits Has Taken Place.

Commissioner Boutris began his examination of WFHMI under its CRMLA license in April of 2001, before there was any claim of preemption and before any federal regulations were promulgated. That examination disclosed violations and a follow-up examination was conducted in April of 2002, covering the prior calendar year. At no time until nearly two months after the Commissioner demanded that WFHMI make California consumers whole by conducting an audit and refunding overcharges based on CRMLA violations, did WFHMI ever raise the issue of preemption.

Only upon notice that WFHMI claimed it was no longer covered by the California laws under which it had been licensed for several years and would not be making refunds to California consumers, did Commissioner Boutris move forward with a revocation action.[3] Even "where state criminal proceedings are begun against the federal plaintiffs after the federal complaint is filed but before any proceedings of substance on the merits have taken place in the federal court, the principles of *Younger* v. *Harris* should apply in full force." *Hicks v. Miranda*, 422 U.S. 332 (1975) The Ninth Circuit has even recognized that where a county prosecutor filed a state action only two days prior to the preliminary injunction hearing in federal district, there was a 'pending" state

[3] Plaintiffs never requested this Court stay any administrative action the Commissioner could lawfully take until after the hearing WFHMI requested was set so close in time to the hearing on the preliminary injunction.

proceeding that satisfied the first prong of the *Younger* requirement. *Ploykoff v. Collins,* 816 F.2d 1326, 1332 (9th Cir. 1987).

In the matter before this Court, although the plaintiffs filed a case in federal court before the Commissioner sent them a notice of the intent to revoke the license, the administrative examination and proceedings predated the federal lawsuit and the action to revoke the licenses of WFHMI are currently pending. Thus, this Court should abstain and await the outcome of the state administrative proceeding and any subsequent appeals on the issues.

B. Consumer Protection Is An Important State Interest.

In this case, protecting the consumers of the State of California is an important state interest. The California Legislature vested in the Commissioner the power to revoke the license of any person that violates the consumer protection laws of California. Cal. Fin. Code §§ 22714, 50327. The Commissioner is required to enforce laws under his jurisdiction and must insure that WFHMI follows the laws established to protect borrowers from lenders who fail to comply with licensure requirements. In order to accomplish this and his Constitutional mandate, the Commissioner instituted revocation proceedings. WFHMI has requested a hearing, and may seek judicial review in California state courts of any final order or decision following the administrative hearing. Cal. Fin.Code § 50332

A wide variety of state interests qualify as "important" state interests for purposes of *Younger* abstention. In *Delta Dental Plan of California, Inc. v. Mendoza*, 139 F.3d 1289 (9th Cir. 1998), the Court found that important state interests included low-cost, high quality health care for California citizens and adequate information so that they could make informed choices. *Id*. at 1295. *See also Ohio Civil Rights Commission v. Dayton Christian Schools, Inc*., 477 U.S. 619, 628 (1986) where the court held that the elimination of prohibited sex discrimination was an important state interest. Further, in *Middlesex County Ethics Comm. v. Garden State Barr Ass'n*, 457 U.S. 423 (1982), the Court found that "New Jersey has an extremely important interest in maintaining and assuring the professional conduct of the attorneys it licenses." *Id.* at p. 435.

Accordingly, the federal court should abstain from enjoining the administrative proceedings.

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C. WFHMI Will Have The Opportunity To Raise Federal Questions In The Administrative Proceedings And The State Court Appeals.

WFHMI will have adequate opportunity to raise federal questions in the administrative proceeding. Any argument that WFHMI cannot raise such issues during the administrative process is overcome by the availability of raising these claims in the state-court judicial review of the administrative proceeding.

Younger requires that the federal plaintiff, here WFHMI, "have a full and fair opportunity to litigate his constitutional claim" in the course of the state proceedings. *Ohio Civil Rights Comm'n v. Dayton Christian Schools, Inc*. 477 U.S. 619, 627(1986). And, "[m]inimal respect for the state processes, of course, precludes any presumption that the state courts will not safeguard federal constitutional rights." *Middlesex County Ethics Comm. v. Garden State Bar Ass'n*, 457 U.S. 423, 431 (1982).

The final administrative decision is subject to judicial review. Cal. Gov. § 11523, Cal. Fin. Code §§ 22718, 50332. Thus at the administrative hearing or in any subsequent state court appeals, WFMHI will have full opportunity to litigate its claim.

III. PLAINTIFFS HAVE FAILED TO MEET THE STANDARD REQUIRED TO OBTAIN AN INJUNCTION

A temporary restraining order is a form of injunctive relief and as such, the same standards apply as to a preliminary injunction. *See Hoeschst Diafoil Co. v. Nan Y Plastics Corp.,* 174 F.3d. 411, 422 (4th Cir. 1999). Courts have applied a heightened standard on the moving party when the injunctive relief is sought "to stay governmental action taken in the public interest pursuant to a statutory or regulatory scheme." *Able v. United States,* 44 F.3d 128, 130-31 (2d Cir. 1995) citing *Plaza Health Labs, Inc. v. Perales,* 878 F.2d 577, 580 (2d Cir. 1989). In this line of cases, the moving party must show more than "sufficiently serious questions going to the merits" (also known as the "fair-ground-for litigation" test). *Able,* 44 F.3d at 130. Where the governmental action is based on a statutory scheme to protect the public, such as the CRMLA and CFLL at issue here, plaintiffs must demonstrate (1) irreparable harm should the injunction not be granted and (2) a likelihood of success on the merits. *Id.*

In *Able,* the Second Circuit Court of Appeals reversed and remanded the case to the District Court when it found the lower court abused its discretion by issuing a preliminary injunction based upon the less stringent standard of "sufficiently serious questions going to the merits" rather than the measure of a "likelihood of success on the merits." *Id.* at 131-132. The court expressly found that it would be inappropriate for the court to substitute its own determination of public interest and apply the lesser standard where the government had engaged the democratic process to produce policy in the name of public interest that was embodied in a statute and implementing regulations. *Id.* The statutory and regulatory scheme in *Able* was the much debated "don't ask, don't tell" policy of the military as related to sexual orientation of its personnel. *Id.* at 130.

Plaintiffs' reliance upon *International Jensen, Inc. v. Merrasound U.S.A., Inc.* 4 F.3d 819 (9th Cir. 1993) for the proposition that the Ninth Circuit Court of Appeals has adopted a more lenient standard similar to the standards rejected in *Able, supra,* and *Plaza Health Labs, Inc., supra,* is without merit. *International Jensen* involved a preliminary injunction against a private corporation, not a governmental entity. Therefore, it should be disregarded as irrelevant.

Further, plaintiffs' citation to *National Center for Immigration Rights, Inc. v. INS,* 743 F.2d 1365 (9th Cir. 1984) and its application to the case at bar is also disputed as it was decided prior to the *Able* line of cases. In *National Center for Immigration Rights,* the issue of the appropriate standard for a preliminary injunction to be issued against a governmental entity was not raised, and therefore, never addressed by the court. *Id.* Further, unlike the situation in this case, a newly promulgated regulation was at issue, not a statute or statutory scheme designed to protect the public. *Id.* at 1367.

In *American Bankers Ass'n v. Lockyer,* No. S-02-1138 FCD JFM (E.D. Cal. Dec. 2002), the Eastern District, likewise, never reached the issue of the appropriate standard applicable to the issuance of a preliminary injunction against a governmental entity. In that case, the district court granted plaintiffs motion for summary judgment and permanent injunction and denied the preliminary injunction as moot. *Id.*

In point of fact, the Ninth Circuit has never specifically reached the issue of the applicable standard for issuance of a preliminary injunction against a governmental entity. Although the Ninth

Circuit upheld the district court's issuance of a preliminary injunction in *Bank of America, N.A. v. City and County of San Francisco,* 2000 U.S. Dist. LEXIS 12587 (appeal from *Bank of America, N.A. v. City and County of San Francisco,* 1999 WL 33429989 (N.D. Cal. Nov. 15, 1999) the appellate court never addressed the issue and there is no published appellate court decision from which any conclusions may be drawn with regard to the standard applicable when a party is seeking an injunction against a public entity.

Instructive to this Court, however, is the Northern District of California case that recently followed the heightened standard established by the Second Circuit. *Ft. Funsten Dog Walkers v. Babbitt*, 96 F. Supp.2d 1021 (N.D. Cal. 2000). There the court acknowledged the "alternative standard" as the standard for the Ninth Circuit, but nevertheless held that "[a] strong showing or entitlement to a preliminary injunction is required where the moving party seeks to enjoin governmental action taken in the public interest pursuant to a statutory or regulatory scheme. In such cases, the moving party must establish both irreparable injury and a probability of success on the merits." *Id.* at 1032 (cite omitted).

The CMRLA and CFLL challenged by Plaintiffs are statutory schemes developed to provide consumer protection in lending transactions and, therefore, under the rationale as set forth in *Able* and subsequent cases, require the application of more stringent burdens before a temporary restraining order will issue. Plaintiffs must therefore establish, to the satisfaction of this court, both irreparable injury and a likelihood of success on the merits, because they are seeking to stay governmental action taken in the public interest pursuant to a statutory or regulatory scheme. Plaintiffs cannot meet this burden.

A. WFHMI Will Not Suffer Irreparable Harm Should The Administrative Hearing Proceed.

WFHMI presently possesses multiple licenses from the State of California. WFHMI advertises its licensure to potential and existing California consumers. It advertises through mailings and its website, claiming that it is licensed under the CRMLA. At the same time, WFHMI is disregarding the provisions of those statutes designed by the California Legislature to afford

consumer protection from lenders overcharging them or understating finance charges, such as the California per diem interest statute..

Despite WFHMI's contention to the contrary, the California public is being harmed if WFHMI is allowed to continue its business because it is misleading California consumers into believing that the protections afforded under the CRMLA would apply to their loans if they seek their residential mortgage loan through WFHMI. Plaintiffs' argument that going forward with the administrative proceeding will cause irreparable harm to California's economy overlooks the provisions contained in the CRMLA that allows for a reasonable time to transfer loans and servicing obligations so that California consumers will not be injured. Cal. Fin. Code §50310, 50311. It is mere speculation on the part of Plaintiffs, and not appropriate basis for a temporary restraining order, to claim that they will be forced to cease operations in California if they are unable to maintain a CRMLA license.

B. Plaintiffs Have Failed To Show Their Likelihood Of Success On The Merits

Even if the federal court were to rule that Plaintiffs' business is preempted from regulation, which the Commissioner does not concede, it would only make the Commissioner's argument stronger that the licenses need to be revoked because Plaintiffs would not be required to follow the law. If the federal court decides there is no preemption, then the per diem and the disclosure violations, as well as the matter of Plaintiffs' failure to comply with the law, would still need to be decided. Essentially, Plaintiffs want the best of both worlds. They want to maintain a license under California law that they have used as a marketing tool, but they do not want to comply with California law.

Regardless of the federal court's decision on preemption, the administrative hearing must be allowed to go forward. Even were the Commissioner prevented from holding the administrative hearing, WFHMI may well still be in violation of California law and its licenses should be revoked.

IV. PLAINTIFFS HAVE FAILED TO ADDRESS THE SECURITY REQUIREMENT AND NO TEMPORARY RESTRAINING ORDERS SHOULD BE ISSUED

"No restraining order or preliminary injunction shall issue, except upon the giving of security by the applicant, in such sum as the court deems proper. . ." Fed. R. Civ. Proc. 65(c). Further, local

rule 65.231(c)(6) requires the proposed order to include the bond, unless impossible under the circumstances. Plaintiff's proposed order does not provide for a bond and no declaration addresses the absence of this required element. Therefore, a temporary restraining order should not be issued.

CONCLUSION

This Court should abstain from restraining in any way the administrative procedure to revoke the licenses of Wells Fargo Home Mortgage, Inc. Plaintiffs have failed to demonstrate the requisite harm or a likelihood of success such as to warrant an invasion into the state's ability to oversee its licensees. Further, this Court may even want to await the outcome of the state administrative actions and any state court appeals that may follow before ruling on the preliminary injunction.

Dated: March 3, 2003

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