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TO REMOVE OR NOT TO REMOVE: THAT IS THE QUESTION – THEN WHAT HAPPENS?

By *Spencer Scheer, Esq., Scheer Law Group, LLP*

OVERVIEW

With the recent flood of consumer borrower lawsuits against lenders, establishing state or federal jurisdiction via removal¹ and remand has become a strategically important consideration that may often determine the direction and resolution of the case. Counsel that fail to consider and plan for this may be doing their clients a big disservice.

While borrower/lender lawsuits differ, there are common themes emerging from the more recent wave² of consumer-borrower/lender lawsuits.³ Generally, borrowers' counsel will seek to avoid federal court, and lender's counsel want to get the case there. Federal courts appear ready and willing to "weed out" claims at the pleading stage that appear to be frivolous or ill conceived. Utilization of the "incorporation by reference" doctrine⁴ in the context of a motion to dismiss in federal court can bring a quick end to a case that might otherwise drag on. This is often not the case in state courts where the standard for reviewing pleadings is less flexible and judges appear more reluctant to resolve or cut back cases at the pleading stage.

The recent case of *Destfino v. Reiswig*, 630 F.3d 952 (9th Cir. Cal. 2011), provides a good overview of the strategic and practical consideration related to removing a case, and the authority of the federal court to retain jurisdiction over the case, even when the original basis for federal jurisdiction is taken away.

FACTUAL BACKGROUND OF THE DESTFINO CASE

The Plaintiffs filed a law suit in state court against forty defen-

dants. One of the defendants ("First Removing Defendant") removed the case to the federal district court and the Plaintiff moved to remand, asserting that the removal was procedurally defective. While the Plaintiff's motion to remand was pending, the FDIC (as successor to IndyMac Bank) ("FDIC") removed the case to federal court on independent grounds⁵. The federal court then denied Plaintiffs' motion to remand the case against the First Removing Defendant, because of the FDIC involvement.

To escape this, Plaintiffs then dismissed IndyMac and the FDIC and eventually dismissed the federal claims, and asserted that there was no further basis for federal jurisdiction. The district court refused to remand, asserting that it had latitude to determine whether or not to continue to exercise jurisdiction over the state law claims, and that the removal by the First Removing Defendant was sufficient to establish jurisdiction (assuming the procedural defect related to that removal was cured).

Eventually the District Court ruled on motions to dismiss filed by some of the Defendants and dismissed the Complaint against those defendants. Plaintiff appealed the dismissals of the claims. In supporting the authority of the District Court to exercise removal jurisdiction and enter judgment, the Ninth Circuit Court of appeals also established the following removal review guidelines that must be noted by any practitioner or party seeking to remove or defend against removal of an action.

REMOVAL MUST BE TIMELY

A defendant seeking to remove from state to federal court must file a notice of removal within thirty days of receiving a copy of

“*The recent case of In re Reggie Ong, could change things dramatically for credit unions and may generally assist all lenders in limiting the rights of bankruptcy judges to throw out reaffirmation agreements they do not like.*”

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defense against the lenders' foreclosure efforts. But the season is long, and the lenders' efforts are not going unnoticed. Several challenges to the Foreclosure Mediation Program are pending, including cases challenging the courts' right to modify a loan and challenges to the constitutional administration of the program.

In the meantime, lender representatives will want to huddle up to ensure that preparation for mediation is air-tight. Making sure you have the proper pages in your playbook is the only way to succeed on mediation day. Good luck this season.

1. 127 Nev., Adv. Op. 39 (July 7, 2011).
2. A recent decision in Washoe County, Nevada analyzes that strict compliance is mandated as to the statutory language of NRS 107.086. However, strict compliance may not be necessary as to the Foreclosure Mediation Rules, so long as the purported violation is not a violation of NRS 107.086. In such an instance, substantial compliance would be sufficient. This analysis has not been adopted by the Supreme Court of Nevada. (See, *Hermesen v. Deutsche Bank National Trust Company, as Trustee, et al.*, Second Judicial District Court, Case No. CV11-01811, Order dated August 10, 2011.)
3. 127 Nev., Adv. Op. 40 (July 7, 2011)
4. 2011 WL 2671546 (Nev. 2011).
5. At the time this article was submitted for publication, the matter remained pending before the District Court on remand.



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the initial pleading. 28 U.S.C. § 1446(b).⁶ The court in *Destfino* case first considered the question of whether each defendant gets thirty days to remove or does the clock run on all defendants when one is served?

Noting a split in authority in the 9th Circuit, the Court found that logic and fairness concepts dictated that the time to remove runs separately for each defendant, but that it does not give a defendant whose time has run a new time period. The Court held that:

“We adopt the later-served rule as the wiser and more equitable approach. This rule doesn't go so far as to give already-served defendants a new thirty-day period to remove whenever a new defendant is served, as that could give a defendant more than the statutorily prescribed thirty days to remove. See 28 U.S.C. § 1446(b). Rather, we hold that each defendant is entitled to thirty days to exercise his removal rights after being served. Because Courtesy removed the case within thirty days from when it was served, the removal was timely (*Id.* at Page 956).

A Removal Must be Joined by All Defendants: All defendants who are served must join a petition for removal.⁷The second removal concept examined by the appeals court in *Destfino v. Reiswig* was whether all defendants had to join a petition for removal and when the joinder had to occur. The appeals court found that the district court has flexibility to enforce this requirement and that a defect in obtaining consent/joinder at the onset can be cured later on, and does not provide a basis to negate the removal. See *Destfino v. Reiswig* at page 957.⁸

DOES THE DISMISSAL OF FEDERAL CLAIMS OR A FEDERAL ENTITY AFTER REMAND DIVEST A FEDERAL COURT OF JURISDICTION?

Perhaps most significant portion of the Court's ruling in the *Destfino v. Reiswig* decision is the finding that the federal district court still had latitude to retain jurisdiction to resolve the merits of the state law claims, even though the federal claims (and federally chartered defendant) were dismissed by the Plaintiff.⁹



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The court in *Destfino v. Reiswig* noted a split in the analysis of the Second, Third and Fifth Appellate Circuits when determining the effect of dismissing the FDIC from an action that had been removed. The Court noted that the Second and Fifth Circuits view the inclusion of the FDIC as a party (even if the FDIC becomes a party by virtue of its successor status as receiver of a failed lender originally named as a defendant) sufficient to keep the suit within the original jurisdiction of the district court, even if the Plaintiff subsequently dismisses the FDIC from the action. The Court compared this with the Third Circuit, which viewed dismissal of the FDIC as divesting original jurisdiction of the district court, but allowing the district court to retain jurisdiction based on its authority to exercise supplemental jurisdiction over the state law claims.

This distinction is important because if a district court has original jurisdiction it has no authority to remand the case and if it has supplemental jurisdiction it can exercise discretion. However, the Court in *Destfino* decided not to reconcile the distinction and instead cited the inherent discretion of the district court to exercise latitude and determine whether it had sufficient interest in retaining and resolving the state law claims, and held that:

“We need not take sides in this dispute because, even if the district court had authority to remand, it did not abuse its discretion in failing to do so. The district court here articulated its ongoing interest in the supplemental state claims as “ensuring compliance with its orders” because “the [c]ourt had invested considerable time and effort to decide lengthy motions on complicated pleadings.” See *Harrell v. 20th Century Ins. Co.*, 934 F.2d 203, 205 (9th Cir.1991). *Destfino v. Reiswig*, 2011 U.S. App. LEXIS 1375, ____ F 3d ____.

Having found that the District Court did not abuse its discretion in retaining jurisdiction, the court in *Destfino v. Reiswig* upheld the lower court ruling that the Plaintiff’s second amended complaint would be dismissed **with prejudice**.¹⁰

LESSONS TO BE LEARNED

The difference between bringing or defending a case in federal or state court is significant. Removal is a powerful tool that can

determine the “playing field” and significantly impact or alter the direction and result of a case.

Removal is a technical process. The technicalities must be observed or removal can be challenged and the case remanded. There is significant discretion in the Ninth Circuit to maintain jurisdiction over state law claims, even if the basis for federal jurisdiction is subsequently divested, if there was a proper basis to exercise federal jurisdiction at the onset of the case.

Given that many districts courts will resolve the federal claims (via a Motion to Dismiss) and then remand the remaining state law claims, the decision in the *Destfino* case gives lender counsel a firm basis to request that the entire action be resolved in federal court. The Court in *Destfino v. Reiswig* gives a review of the limits of discretion that a court can exercise in maintaining jurisdiction and provides practitioners and their counsel with valuable tools to argue for or against maintenance of jurisdiction.

1. A defendant seeking to remove from state to federal court must file a notice of removal within thirty days of receiving a copy of the initial pleading. 28 U.S.C. § 1446(b).
2. This author views the “wave” as starting from the subprime meltdown in 2007 to the present.
3. Fraud, unfair business practice claims, RESPA, TILA violations, “show me the note” claims and Foreclosure Loss Mitigation Statute violations to name a few.
4. Motions to Dismiss in federal court are often more effective than state court demurrers. Where state courts are limited to examination of the pleadings and taking judicial notice (when applicable), federal courts can review documents that are referred to in the complaint (See e.g. *Marder v. Lopez*, 450 F.3d 445, 448 (9th Cir. 2006)). Some courts have even allowed the incorporation by reference doctrine to apply when the documents are not referred but are essential to the claim raised by the Plaintiff in the action (See *Knievel v. ESPN*, 393 F.3d 1068, 1076 (9th Cir. 2005)).
5. Removal by FDIC pursuant to 12 U.S.C. § 1819(b)(2)(B).
6. If a bankruptcy proceeding is filed different periods may apply, depending on whether state court case was commenced before or after the bankruptcy (See 11 U.S.C. Bankruptcy R 9027). It is also worth noting that the FDIC has 90 days in which to remove a case (See section 1819(b)(2)).
7. See *Soliman v. Philip Morris Inc.*, 311 F.3d 966, 970 (9th Cir.2002)
8. It should be noted that the Court went out of its way to excuse the requirement that all defendants consent or join in removal (either at the onset of the case or later) as to five of the defendants who had not joined or consented, but who had also not been properly served, or served at all, in the action, including one defendant who allegedly filed an answer.
9. It should be noted that in the *Destfino* case that after removal of the case, the Plaintiff dismissed the FDIC and federal claims in an attempt to divest the district court of jurisdiction and sought to remand the remaining state court claims.
10. The primary basis for dismissal was the failure to plead fraud with par-

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ticularity. We will never know if the same thing would have happened via a demurrer in State Court, but in this author's opinion, it would be much less likely.



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BAP discussed two ways in which a party can obtain 'person entitled to enforce the note status.' The first, is a holder of note—meaning the note is payable to the person who possesses the note, or the note is payable to the bearer of the note. To meet this burden, a moving party who is not the original would offer the court the note with proper indorsements or a properly affixed allonge making the note payable to the moving party. The second method is making a showing under UCC § 3-301(ii) that a party has attained the status of a 'nonholder in possession of the [note] who has the rights of a holder.' Under the second method, a party must establish that fact and purpose of delivery. For example, if a party acquires the note through a bulk sale of notes without individual indorsements, that party has obtained the right to enforce the note despite the fact they are not an Article 3 holder of the note. Establishing a showing under this second method is decidedly a grey area in bankruptcy courts and a much riskier method on which to premise standing.

Expanding on the 'person entitled to enforce the note' concept, the purpose of this concept is to provide for the maker note or debtor as is the case in the bankruptcy proceeding, to determine to whom their monetary obligation is owed. As long as the maker/debtor has the ability to make payments on the note which will ultimately discharge his obligations to the extent paid under UCC Section 3-601(a) and the maker/debtor will never be obligated to pay that amount again, it should make absolutely no difference to the debtor who actually owns the note. As the BAP significantly noted in *Veal*, it is irrelevant whether the Note has been fractionalized or securitized. The only relevant information that pertains to the debtor is whether they are paying the person entitled to enforce the note. The debtor has no reason to care who actually owns the note.

In *Veal*, Wells Fargo could have satisfied a showing of prudential standing by proving it had a colorable claim to receive payment pursuant to the note, either under UCC Article 3 or by showing they had some ownership or other property interest in the note. Likewise, AHMSI could have satisfied a showing of prudential standing had it shown it was the person entitled to enforce the note or the agent of such person. While the *Veal* decision clarifies standing issues for motions for relief and proofs of claim, creditors can be assured that debtors will continue to challenge a movant's standing which necessitates the need that motion