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NOTES, TRUST DEEDS AND LOAN AGREEMENTS IN A CHANGING MARKET: **NINE KEY AREAS TO CONSIDER**

John L. Hosack, Esq., Jason E. Goldstein, Esq., and Rick Rodriguez

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John L. Hosack—*Presenter*

John L. Hosack is a Shareholder in the firm's Litigation Practice Group in Los Angeles and a member of the firm's Mortgage Banking Group. Mr. Hosack represents mortgage brokers, secured lenders and property owners at trial and on appeal in real property disputes including, broker liability, lender liability, fraud, breaches of contract, mechanic's liens, stop notices, judicial foreclosures, receiverships, escrow claims and title insurance claims. His transactional practice includes commercial real property loan documentation, loan workouts, REO sales and foreclosures. He is an Affiliate Member of the California Mortgage Association and a member of the Los Angeles Mortgage Association, a Fellow of the American College of Real Estate Lawyers and a Fellow of the American College of Mortgage Attorneys. He is the author of "California Title Insurance Practice (First Ed., Calif. Cont. Ed. Bar), the first book on title insurance, and is a past Chair of the ABA's Title Insurance Litigation Committee.



John L. Hosack
Shareholder
Los Angeles Office

Jason E. Goldstein—*Presenter*

Jason Goldstein is Chairman of the Firm's Mortgage Banking Group and specializes in real property related litigation, "private money," trade secrets, title and escrow. Mr. Goldstein's practice involves defending lenders, brokers and servicers in court (negligence, fraud, TILA, RESPA, HBOR, wrongful foreclosure, lender/servicer liability defense, etc.), prosecuting escrow and title insurance litigation (on behalf of the insured) and litigating misappropriation of trade secret claims. Mr. Goldstein's practice also includes judicial foreclosures and general civil litigation. Mr. Goldstein is a fellow of the American College of Mortgage Attorneys ("ACMA") and a member of the ACMA Title Insurance Committee.

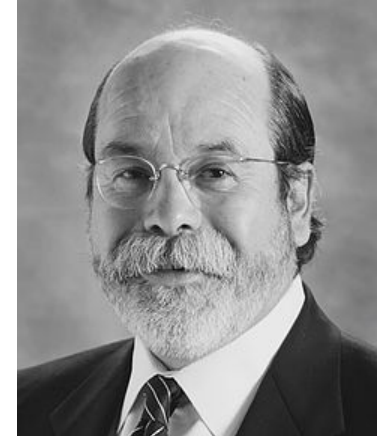


Jason E. Goldstein
Shareholder
Irvine Office

Rick Rodriguez

Mr. Rodriguez is the founder and principal of Rodriguez and Associates Advisory Group (“R&A”), a Los Angeles based consultancy firm that has provided a unique array of services to its clients since 1992. For the past 24 years, R&A has successfully formulated creative workout and loan restructure resolutions to complex multi-party debtor-creditor transactions in judicial and non-judicial settings.

Having spent approximately 20 years as a banker, primarily with Security Pacific National Bank, Mr. Rodriguez has personal experience in due diligence, loan administration and workout of all types of loans, from consumer credit to large commercial complex syndicated credits. Mr. Rodriguez is a seasoned expert witness in banking, finance and real estate matters who testifies at jury trials, bench trials, arbitration proceedings, and mediation sessions; both by deposition and declaration. Mr. Rodriguez has testified equally for plaintiffs and defendants.



Rick Rodriguez
Principal
Rodriguez Associates
Advisory Group

I. INTRODUCTION

II. THE INTERACTION AMONG THE NOTE, LOAN AGREEMENT, DEED OF TRUST AND ESCROW INSTRUCTIONS

1. The Note:

- *The principal obligations of the borrower. If conflicting provisions, the note should control.*

2. The Loan Agreement:

- *Further obligations of the borrower (and guarantor, if any).*

3. The Deed of Trust:

- *The security for the loan.*

4. The Escrow Instructions:

- *Coordinates the disbursement of the funds in return for the properly executed loan documents and required lien position.*

III. FOUR CRITICAL PROVISIONS WHICH SHOULD BE IN EVERY LENDER'S ESCROW INSTRUCTIONS (1 of 5)

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1. Introduction.

III. FOUR CRITICAL PROVISIONS WHICH SHOULD BE IN EVERY LENDER'S ESCROW INSTRUCTIONS (2 of 5)

- 2. The Lender's Written Escrow Instructions To The Title Company Should Require That the Lender's Deed of Trust To Be Recorded As a First Priority Lien On The Borrower's Real Property**

III. FOUR CRITICAL PROVISIONS WHICH SHOULD BE IN EVERY LENDER'S ESCROW INSTRUCTIONS (3 of 5)

3. On a Construction Loan, the Lender's Escrow Instructions to the Title Company Should Disclose the Fact That in the Event of a Default Under the Loan Documents that the Lender Has the Right to Terminate Any Further Loan Disbursements and State That if the Title Company is to Use the Lender's Documents or Loan Funds That the Lender's Right to Terminate Further Advances is Consented To by the Title Company

III. FOUR CRITICAL PROVISIONS WHICH SHOULD BE IN EVERY LENDER'S ESCROW INSTRUCTIONS (4 of 5)

4. **The Lender's Escrow Instructions Should Address Its Disclosure Obligations Under California *Insurance Code* § 332 And The Loan Policy's Exclusion From Coverage 3(b)**

III. FOUR CRITICAL PROVISIONS WHICH SHOULD BE IN EVERY LENDER'S ESCROW INSTRUCTIONS (5 of 5)

5. **If a Construction Loan is Being Made, the Lender's Escrow Instructions Should Disclose To The Title Company The Potential For The Commencement Of The Work Of Improvement and for Mechanic's Liens To Attach.**

IV. DEFINING “EVENTS OF DEFAULT” SUFFICIENTLY BROAD TO ADEQUATELY PROTECT THE LENDER’S INTERESTS

1. Introduction.
2. Lack Of A Valid And Enforceable First Priority Lien (“Deed of Trust”) On the Borrower’s Property.
3. Violation Of The Federal Controlled Substances Act.
4. A Judicial Or Non-Judicial Foreclosure.
5. Seizure Commanded By A Governmental Entity.

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RISK MANAGEMENT FOR CONSTRUCTION LOANS: 2019 UPDATE

John L. Hosack, Esq., Jason E. Goldstein, Esq., Mr. Joffrey Long and Mr. Rick Rodriguez

February 12, 2019 @ 12:00 Noon PST
Buchalter
1000 Wilshire Boulevard, Suite 1500
Los Angeles, California 90017

V. CONSEQUENCES OF “EVENTS OF DEFAULT”

1. Purpose.
2. Compensation.
3. Performing Loan vs. Non-Performing loan.

VI. BORROWER'S OBLIGATIONS FOR THE LENDER'S CONSEQUENTIAL LOSS IN THE EVENT OF PREPAYMENT

1. Prepayment.
2. Premium vs. Penalty.
3. Careful Drafting To Provide Compensation For Loss Suffered Due To Prepayment.

VII. NO USURY PROVISION

1. **What Is Usury?**
2. **What Is The Usury Exemption?**
3. **What Happens If The Exemption Changes?**
4. **No Usury “Savings Clause.”**
5. **Usury Endorsement.**
6. **How Is This Affected By “Default Interest?”**

VIII. BORROWER'S LIABILITY FOR ANY INCREASED COST TO LENDER

1. How Are Loans Priced?
2. Changes Which May Raise A Lender's Costs.
3. Increased Cost Provision.

IX. REPRESENTATIONS AND WARRANTIES SURVIVE PAYMENT OF THE LOAN AND RECONVEYANCE OF THE DEED OF TRUST

1. **When Problems Arise After The Loan Is Paid Off And The Deed Of Trust Reconveyed.**
2. **Title Issues.**
3. **Attorneys' Fees Issues. See, *Hart v. Clear Recon Corp.* (2018) 27 Cal.App.5th 322 and *Chacker v. JP Morgan Chase Bank, N.A.* (2018) 27 Cal.App.5th 35.**

X. EXPRESSLY PROVIDE FOR A WAIVER OF THE DEFENSE OF THE STATUTE OF LIMITATIONS

1. Enforceable (California) – maybe not in other states.
2. For How Long – Four (4) Years In California.
3. Waiver Of Statute Of Limitations Provisions.

XI. LOAN MODIFICATION AGREEMENT

1. Purpose – Avoid A Default.
2. How - Increase Loan Amount; Extend Maturity Date; Change Interest Rate, Etc.
3. Loan Modification Endorsement.
4. Concerns:
 - A. Usury.
 - B. Loss Of Lien Priority.
 - C. Future Advances.
 - D. Exonerating Loan Guarantees.
 - All Issues Disclosed.
 - All Questions Answered.
 - Everything Documented.

XII. DEALING WITH OUT-OF-STATE BORROWERS

1. Numerous Issues.
2. Choice Of Law Provisions.
3. Selection Of Location For Any Dispute Resolution.
4. Service Of Process.

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XIII. DISPUTE RESOLUTION (1 of 9)

1. **Mediation.**
2. **Jury Trial Waivers (Enforceable Or Not?).**
3. **Binding Arbitration.**
4. **Judicial Reference.**

XIII. DISPUTE RESOLUTION – PROTOCOL AGREEMENT (2 of 9)

1. **What Is A Protocol Agreement?**
2. **Why Is A Protocol Agreement Important?**
3. **What Should Be In One – And What Should Not Be?**

XIII. DISPUTE RESOLUTION – CHOICE OF FORUM (3 of 9)

1. **What Is A Choice Of Forum?**
2. **Why Is A Choice Of Forum Important?**
3. **What Can Be Gained By A Choice Of Forum?**

XIII. DISPUTE RESOLUTION – CHOICE OF LAW (4 of 9)

1. **What Is A Choice Of Law?**
2. **Why Is A Choice Of Law Important?**
3. **What If There Are More Than One Jurisdiction Involved?**

XIII. DISPUTE RESOLUTION – CLASS ACTION WAIVER (5 of 9)

1. What Is A Class Action Waiver?
2. Is A Class Action Waiver Enforceable?
 - *Epic Systems Corp. v. Lewis* (2018) 138 S.Ct. 1612
 - *Ernst & Young LLP et al. v. Morris* (2018) 138 S.Ct. 51
 - *National Labor Relations Board v. Murphy Oil USA, Inc.* (2018) 137 S.Ct. 809
3. Put In A Savings Clause In Case It Is Held To Be Unenforceable.

XIII. DISPUTE RESOLUTION – MEDIATION (6 of 9)

1. **What Is A Mediation?**
2. **What Are Its Benefits?**
 - *Confidentiality.*
 - *Potential Early Resolution.*
3. **What Are Its Drawbacks?**
 - *Non-Binding.*
 - *Mediator Can Only Recommend A Resolution.*
 - *Costs Money.*

XIII. DISPUTE RESOLUTION – ARBITRATION (7 of 9)

1. **What Is An Arbitration?**
2. **What Are Its Benefits?**
 - *No Jury.*
 - *Potentially Efficient.*
3. **What Are Its Drawbacks?**
 - *No Jury.*
 - *Costs Money.*

XIII. DISPUTE RESOLUTION – CERTAIN ARBITRATION TERMS (8 of 9)

1. The arbitrator shall only be a retired Judge who served on the bench for at least ten (10) years.
2. The arbitrator shall only consider evidence which is admissible under the law of the forum.
3. The arbitrator shall only apply the procedural and substantive law of the forum.
4. The arbitrator shall issue a reasoned decision which is based only on admissible evidence and the substantive law of the forum state.
5. An ADR service provider (i.e., JAMS, ADR Services, Inc., etc.) is selected to provide the arbitrator. If the parties are unable to agree on the selection of an arbitrator within 15 calendar days of a demand for arbitration, then the ADR service provider shall select the arbitrator in accordance with its rules which are in effect as of the date of the demand for arbitration.
6. The rules applicable to the arbitration (i.e., the rules of ADR Services, Inc. at the time of the demand.
7. The arbitrator should be the person to decide if a dispute is subject to arbitration.
8. The scope of any judicial review.

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XIII. DISPUTE RESOLUTION – JUDICIAL REFERENCE (9 of 9)

1. What Is An Judicial Reference?
2. What Are Its Benefits?
3. What Are Its Drawbacks?

XIV. Provision for Default Interest Should be Documented To Have Resulted From A Good Faith Attempt by the Lender and the Borrower to Estimate the Damages Which the Lender Would Suffer In the Event of A Default (1 of 2)

1. In general, default interest provisions in commercial loans are enforceable. See, *General Electric Capital Corp. v. Future Media Productions, Inc.* (9th Cir.) 547 F. 3d 956, 961.
2. Without a prior good faith attempt by the lender and the borrower to estimate the amount of damages which the lender could suffer in the event of a default by the borrower - this lack of negotiation before the execution of the loan documents, creates an opportunity for the borrower to attempt to prove that the provisions for the lender's right to recover default interest were not reasonable under the circumstances which existed on the date that the loan was made.

XIV. Provision for Default Interest Should be Documented To Have Resulted From A Good Faith Attempt by the Lender and the Borrower to Estimate the Damages Which the Lender Would Suffer In the Event of A Default (1 of 2)

3. California case law analyzes the enforceability of default interest in a commercial, non-consumer loan, under California Civil Code Section 1671 (b). Therefore, a default interest clause might be considered to be unreasonable and hence unenforceable under Section 1671 (b) if it bears no reasonable relationship to the range of actual damages which the parties could have estimated would result from an event of default by the borrower.

See, *Garrett v. Coast Sav. & Loan Assn.* (1973) 9 Cal. 3d 731, 739; *Perdue v. Crocker Nat'l Bank* (1985) 38 Cal. 3d. 913, 931; and *Ridgley v. Topa Thrift & Loan Ass'n* (1988) 17 Cal. 4th 970, 977-978.

4. Examples.

XV. CONCLUSION
