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CALIFORNIA LENDERS MUST BE DILIGENT NOT TO GET BURNED TWICE:

A REMINDER OF THE CONSEQUENCES OF THE FULL CREDIT BID RULE IN LIGHT OF THE CALIFORNIA WILDFIRES

by T. Robert Finlay, Esq.

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Recently, multiple wildfires swept across the State of California leaving a wake of destruction in their path. The fires destroyed a multitude of residential properties and the entire Northern California city of Paradise. While foreclosure moratoriums will temporarily stop all foreclosure activity, they will eventually be lifted, giving lenders the option to foreclose on affected properties that serve as security for defaulted loans. Before going to sale on a fire damaged property, lenders should understand the risks created by their foreclosure bids, including, but not limited to, the potential loss of the lender's right to insurance proceeds.

Rather than show up with cash at its own sale, a foreclosing lender can make a "credit bid" up to the full amount of the borrower's indebtedness, "since it would be useless to require [the lender] to tender cash which would only be immediately returned to [it]."[1] While the foreclosing lender has the option of bidding up to the full amount of the debt (i.e., a "full credit bid"), doing so can limit the lender's right to recover additional amounts due to any impairment of the security. Indeed, a successful full credit bid establishes the value of the real property and prevents the lender from claiming that the property is worth less than the amount of the bid.[2] This concept, created through case law, has become known as the "Full Credit Bid Rule."

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[1] *Cornelison v. Kornbluth* (1975) 15 Cal. 3d 590, 607 (*citing Central Sav. Bank of Oakland v. Lake* (1927) 201 Cal. 438, 447-448)

[2] *Smith v. Allen* (1968) 68 Cal.2d 93, 95; *Alliance Mortgage Co. v. Rothwell* (1995) 10 Cal. 4th 1226, 1238-39.

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Full Credit Bid Rule (continued from page 1)

Pursuant to this rather rigid rule, a full credit bid extinguishes the debt ***entirely*** and precludes the lender from recovering any additional amounts to satisfy the debt. If the lender makes a successful full credit bid, it "cannot pursue any other remedy based upon the recovery of any part of the secured debt, or recover from any other security, regardless of the actual value of the property on the date of the sale."[3] Accordingly, the lender is prohibited from recovering fire or other insurance proceeds payable for pre-sale damage to the property, pre-sale rent proceeds, or even damages for the borrower's waste.[4] The Full Credit Bid Rule also bars the foreclosing lender from recovering a condemnation award,[5] as well as any amounts that may have been payable from a guarantor of the debt prior to the foreclosure sale.[6] The rule also prohibits a lender from recovering title insurance proceeds. This is because the lender's only interest in the property (i.e. the repayment of the debt) has been satisfied and extinguished by the full credit bid; the presumption is that any further payment would necessarily result in a double recovery or windfall to the lender.[7]

Due to the foregoing, a lender making a credit bid at a foreclosure sale must be conscientious of its potential rights to rents, additional or supplemental security, ***insurance proceeds***, and/or any damages caused by the borrower's waste. As stated best by the California Supreme Court, "[t]he lender, perhaps more than a third party purchaser with fewer resources with which to gain insight into the property's value, generally bears the burden and risk of making an informed bid."[8] California courts have consistently held that the purchaser at a foreclosure sale has the duty to assess the value of property correctly.[9]

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[3] 4 Miller & Starr, Cal. Real Est. § 10:218 (3d ed.).
[4] *Alliance Mortgage Co. v. Rothwell* (1995) 10 Cal. 4th 1226, 1246; see also, *Cornelison v. Kornbluth, supra,* 15 Cal.3d at pp. 606–607 ("[T]he [lender] is not required to open the bidding with a full credit bid, but may bid whatever amount [it] thinks the property is worth. Indeed, many creditors continually enter low credit bids ... to provide access to additional security or additional funds. In such a case, a deficiency balance of the debt would have remained for which [the lender] would have had an entitlement out of the insurance policy. The extinguishment of the mortgage or deed of trust by the foreclosure would not have affected [the lender's] right to be paid the remainder of the debt under the policy.") (internal citations and quotations omitted).; *Caruso v. Great Western Savings* (1991) 229 Cal.App.3d 667, 673–674; *Duarte v. Lake Gregory Land and Water Co.* (1974) 39 Cal.App.3d 101, 105; *Washington Mut. Bank v. Jacoby* (2009) 180 Cal. App. 4th 639, 646-47.
[5] *People Ex Rel Dept. of Transportation v. Redwood Baseline, Ltd*. (1978) 84 Cal. App. 3d 662, 676.
[6] *White v. Seitzman* (1964) 230 Cal. App. 2d 756, 765.
[7] *Alliance Mortgage Co., supra,* 10 Cal. 4th at 1246*; see also, Track Mortgage Grp., Inc. v. Crusader Ins. Co.* (2002) 98 Cal. App. 4th 857, 866.
[8] *Alliance Mortgage Co. v. Rothwell* (1995) 10 Cal. 4th 1226, 1246.
[9] *Sumitomo Bank of California v. Taurus Developers* (1986) 185 Cal.App.3d 211, 221 -222 ("Given the characteristics of a trustee's sale where control over the sale rests primarily in the beneficiary, trustee, and bidders, the trustor cannot be characterized as a 'seller' under a duty to disclose known defects as exists in the normal vendor-vendee relationship.")

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Full Credit Bid Rule (continued from page 2)

The full credit bid rule can result in harsh consequences for a lender who makes a successful full credit bid on real property with a substantially lower fair market value. It is well established that a lender who purchases an encumbered property at a foreclosure sale by making a full credit bid is not entitled to insurance proceeds payable for pre-foreclosure damage.[10] For example, in *Altus Bank v. State Farm Fire & Cas. Co.*,[11] the Court relied on the Full Credit Bid Rule to prohibit the lender from recovering ***any*** insurance proceeds resulting from ***a pre-sale fire that completely destroyed the residence on the property***. Despite the fact that the lender made a claim under the insurance policy *prior to the sale* and maintained that the full credit bid was a mistake, the Court held that the lender was completely barred from recovering anything based on the diminution of value of the property that secured the loan because the credit bid established the value of the property and extinguished the debt in full.[12] The Court further noted that it was unreasonable for the lender to "acquire the mortgaged property by choking-off any offers in the range of the true value of the property with a preemptive bid and then…assert that its insurance loss was measured by anything other than the price which it bid at auction to acquire the property."[13]

Similarly, in *Bank of America v. Quackenbush*,[14] the Court held that the lender could not recover against an insurer that issued financial guarantee bonds as additional security for a pool of high risk loans after the lender inadvertently made full credit bids on the properties in question, even though the originating lender grossly overinflated the property values in a scheme to defraud investors. In *Quackenbush*, the Court concluded that it was reasonable to hold the lender to the Full Credit Bid Rule because the lender "controlled the timing of the sales and admittedly knew the true value of the properties [and] nothing precluded it from bidding less than the amount it was owed."[15] As a result, the lender ultimately sustained a loss of approximately $12 million, which it could not recoup.[16]

Adding insult to injury, lenders who have tried to rescind or reform the foreclosure sale in an effort to avoid the effect of the Full Credit Bid Rule, are rarely successful. In *Universal Mortgage Co., Inc. v. Prudential Ins. Co.,*[17] the foreclosing lender made a successful full credit bid based on its agent's external observations of the property. However, it was subsequently discovered that the interior had extensive damage due to the borrower's removal of most of the fixtures and appliances.[18] The lender sued the insurer, who denied the lender's claim under the operative insurance policy in reliance upon the Full Credit Bid Rule.[19] The lender sought to amend its complaint to allege a cause of action for reformation of the trustee's deed to reflect a lower bid; however, this request was denied by the trial court and judgment was ultimately entered in favor of the insurer.[20]

On appeal, the Ninth Circuit upheld the judgment and denial of leave to amend, reasoning that reformation was not a proper remedy under the circumstances since "there was no mistake" because the lender clearly intended to make the full credit bid based on its exterior inspection.[21] The Court further held that the lender's lack of actual or constructive knowledge of a loss at the time of a full credit bid was irrelevant to the policy or application of the Full Credit Bid Rule.[22]

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[10] See, e.g., *Track Mortgage Group, Inc. v Crusader Insurance Co.* (2014) 98 Cal.App.4th 857 at 864–867; *Najah v. Scottsdale Ins. Co.* (2014) 230 Cal. App. 4th 125, 142 ("claim against Scottsdale for preforeclosure damage was therefore precluded by the full credit bid rule.").
[11] (C.D. Cal., 1991) 758 F. Supp. 567, 568-570, *aff'd*, 979 F.2d 854 (9th Cir. 1992).
[12] *Id.*
[13] *Id.* at 570-571.
[14] (1997) 56 Cal. App. 4th 1167, 1173-74.
[15] *Id.* at 1174.
[16] *Id.* at 1170.
[17] (9th Cir.1986) 799 F.2d 458, 460.
[18] *Id.* at 459.
[19] *Id.*
[20] *Id.*
[21] *Id.* at 459.
[22] *Id.* at 460; *see also*, *Rosenbaum v. Funcannon* (9th Cir. 1962) 308 F.2d 680, 684; *Reynolds v. London & Lancashire Fire Ins. Co.* (1900) 128 Cal. 16 (holding that the lender holding title to property after the foreclosure sale, but before the period wherein the borrower could have redeemed the property by paying the purchase price, was not entitled to insurance proceeds as a result of a post-foreclosure destruction of the property by fire due to the full credit bid rule).

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Full Credit Bid Rule (continued from page 3)

Even something short of a full credit bid can have dangerous consequences. As explained above, the credit bid at the foreclosure sale establishes the value of the property for purposes of recovering fire or other additional proceeds. Therefore, a bid of $300,000 when the amount owed is $500,000, effectively limits the lenders' right to recovery insurance proceeds to $200,000 [$500,000 less the established value of the property ($300,000)]. Accordingly, it's important to establish an accurate bid, after factoring in the extent of the damage to the property.

Despite the harsh consequences of a full credit or other limiting bid, the courts have only carved out two very limited exceptions. The first exception applies where the lender's full credit bid is induced by the lender's reliance upon fraudulent misrepresentations.[23] In *Alliance Mortgage Co. v. Rothwell*, [24] the lender sued a real estate appraiser and a broker, among others, claiming that they fraudulently induced the lender to originate several loans secured by properties that were insufficient collateral for the debt. The California Supreme Court identified an exception to the Full Credit Bid Rule, holding fraud claims against third parties who fraudulently induced the lender to make the loans were not barred by the full credit bid rule.[25] However, this is a limited exception. Absent fraud affecting the bid, the Full Credit Bid Rule will apply.

The second limited exception applies where the lender incurs damages caused by negligent construction of improvements. Under these circumstances, the lender may be entitled to recover damages even though it has purchased the property at a trustee's sale following a full credit bid. In *Sumitomo Bank v. Taurus Developers, Inc.,*[26] the foreclosing lender discovered several latent defects on the property due to faulty construction and brought suit against the borrower/developer for failing to adequately oversee the construction and notify the lender of the defects known to him. While the Court held that the lender could not recover based upon fraud, bad-faith waste, or breach of contract, it found that a cause of action for negligence could be maintained by the lender regardless of its full credit bid.[27]

Given the strict nature and application of California's Full Credit Bid Rule and its very limited exceptions, it is imperative that lenders consider every potential source of recovery on the unpaid debt before making a credit bid at a foreclosure sale. A failure to do so will limit or ***completely deny*** the lender's ability to recover insurance or other proceeds that would otherwise help offset its loss. Thus, where property values have been affected by natural disaster, such as those destroyed in the recent California wildfires, lenders and their servicers should consider the damage to the property, the value of the property in its current state and the amount of available insurance proceeds in determining its intended credit bid at the foreclosure sale.

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[23] 4 Miller & Starr, Cal. Real Est. § 10:218 (3d ed.).
[24] (1995) 10 Cal. 4th 1226, 1246.
[25] *Id.* at pp. 1246–1247. ("[T]o the extent Alliance's full credit bids were proximately caused by defendants' fraudulent misrepresentations ..., Alliance's bids cannot be deemed an admission of the properties' value.... Hence the full credit bid rule would not apply.")
[26] (1986) 185 Cal. App. 3d 211, 226.
[27] *Id.* at 227-228.

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TO FEE OR NOT TO FEE

THE PROS AND CONS OF SEEKING ATTORNEY FEES FROM BORROWERS

by Matthew S. Carter, Esq.

Few types of commercial litigation are as volatile and emotionally charged as that between mortgage financial institutions (particularly lenders, servicers and trustees) and borrowers involving foreclosures of mortgages and deeds of trust. Often, borrowers will represent themselves *in propia persona* and, being unfamiliar with the forms and procedural rules lawyers take for granted, those borrowers will often unnecessarily complicate or prolong what should be a fairly routine judicial or non-judicial process. Even in the best of situations, where borrowers have obtained counsel who understand the applicable law and how to navigate the court system, the borrowers might take actions that only make litigation--and even non-judicial foreclosure-- vastly more expensive than it should be. This understandably leads a prevailing financial institution, who, even before legal fees, might have already expended considerable amounts of time and money trying to informally resolve the dispute, to consider seeking recovery of its attorney fees against the recalcitrant borrowers.

There is no uniform, one-size-fits-all answer to whether a financial institution should seek a fee award against a losing borrower. Each situation needs to be assessed separately and might depend on factors as varied as the egregiousness of the borrower's conduct in the litigation, whether the borrower is a serial filer or vexatious litigant, the amount of fees and costs incurred, the collectability from the borrower, and, of course, public perception of pursuing someone who is already losing their home.

In fact, as a general matter, recovering attorney fees in any American jurisdiction is a difficult proposition. A chief difference between the United States and other common-law jurisdictions, such as the United Kingdom, is that, in the United States, prevailing parties in litigation do *not* receive awards of attorney fees as a matter of course.[1] Despite the general prohibition on fee awards to a prevailing party, American jurisdictions have several narrow routes to attorney fee recovery. Below is a discussion of these methods in Nevada,[2] as well as an assessment of the strategic considerations when determining whether to seek a fee award against a borrower.

Fee Awards: How to Get There

In Nevada, awards of attorney fees are governed by statute. Nevada Revised Statutes section 18.010 provides for the possibility of a fee award in the following situations: (1) where provided by contract; (2) where allowed by a specific statute or rule; (3) where the prevailing party recovers *less than* $20,000; and (4) where the losing party's claim or defense "was brought or maintained without reasonable ground or to harass the prevailing party." Finally, attorney fees may also be awarded as special damages in cases where a cloud on title has been lifted *and* there was an allegation of wrongdoing against the losing party (*e.g.*, a slander of title claim).

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[1] The "English Rule," in which the losing party in litigation pays the winning party's fees, has been extensively discussed as an alternative in American legal circles for decades. For example, Walter K. Olson of the Cato Institute urged the adoption of the English Rule by American courts in his book The Litigation Explosion: What Happened When America Unleashed the Lawsuit (Dutton 1991). Theodore Eisenberg of Cornell University and Geoffrey Miller of New York University also conducted a study of various contracts in January 2013 and found that, about 60% of the time, Americans chose a scheme more like the English Rule in their own contracts. Theodore Eisenberg and Geoffrey P. Miller, The English Versus the American Rule on Attorney Fees: An Empirical Study of Public Company Contracts, 98 Cornell L. Rev. 327 (2013).

[2] Though the legal references in this article are from Nevada, the methods described are available in most, if not all, American jurisdictions. The best practice is to consult with local counsel to determine whether and how to seek fees in any particular forum.

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Seeking Attorney Fees from Borrowers (continued from page 5)

Getting a Fee Award Under a Contract

Perhaps the easiest way to obtain a fee award from a court is with a contract providing for that fee award.[3] In the context of a borrower, these provisions can sometimes be found in the Note or, more often, the security instrument if the Note is secured. For example, a Note or Deed of Trust might require a borrower to pay attorney fees in the event that the borrower fails to pay as required by the Note with a provision like this one:

> If the Note Holder has required the Borrower to pay immediately in full as described above, the Note Holder will have the right to be paid back by the Borrower for all of its costs and expenses in enforcing this Note to the extent not prohibited by applicable law. Those expenses include, for example, reasonable attorney fees.

This particular fee provision may not lead to a fee award on the basis that it only favors the lender, not the borrower.[4] Other, more modern attorney fee provisions may provide that, in the event there is legal action to enforce the contract, the prevailing party in that action may recover its costs of litigation and attorney fees. In Nevada, as in many other jurisdictions, the award of attorney fees is squarely within the trial court's discretion, and if the court perceives unfairness or one-sidedness in an underlying contract, it may decline to award fees.[5] Therefore, to the extent that a lender is seeking fees from a borrower pursuant to contract, more balanced fee provisions will be looked upon more favorably by courts.

All of the above analysis assumes that a lender or servicer moves for and obtains a fee award under Nevada law. While a party may attempt to obtain fees pursuant to contract without a motion and resulting award, this process is not grounded in the black-letter law of Nevada and may be subject to reversal upon appeal. That said, some parties have recovered fees as part of a default judgment (*i.e.*, a judgment taken against a party who has failed to answer a complaint). In those situations, the fee award is not normally held to the scrutiny of an appeal; otherwise, there likely would not have been a default judgment in the first place. So, although there are occasionally Nevada fee awards granted as part of default judgment without a specific motion made to the trial court, that is not the best practice before the courts of this State.

Statutory or rule-based fee awards

Certain state and federal statutes themselves will provide for a fee award; however, some of those statutes either limit the award to a prevailing *consumer* or impose a greater burden on the prevailing creditor before fees will be awarded to it. In addition to awards under particular statutes, awards in favor of a financial institution may commonly come up in the following contexts, among others:

(a) Offers of Judgment/recovery-contingent fee statutes

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[3] See United States Design & Constr. Corp. v. I.B.E.W. Local 357 Joint Trust Funds, 118 Nev. 458, 462, 50 P.3d 170, 173 (2002) (acknowledging the validity of contractual fee awards).
[4] It should be noted that certain jurisdictions, like California, have codified that fee provisions must be reciprocal. See Cal. Civ. Code § 1717.
[5] Edwards v. Emperor's Garden Rest., 122 Nev. 317, 330, 130 P.3d 1280, 1288 (2006) and McCrary v. Bianco, 122 Nev. 102, 109, 131 P.3d 573, 577 (2006) (indicating that attorney fee provisions ought to be interpreted in a reciprocal way). Cf. Rowland v. Lepire, 99 Nev. 308, 316, 662 P.2d 1332, 1337 (1983) (holding that there was no reciprocal right to attorney fees based on a one-sided provision in a contract).

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Seeking Attorney Fees from Borrowers (continued from page 6)

Statutory or rule-based fee awards can vary greatly from jurisdiction to jurisdiction. The most common situation for a fee award in Nevada state and federal courts is an award made pursuant to an offer of judgment. Authorized by Nevada Rule of Civil Procedure 68, an offer of judgment is most appropriate where money damages are sought by a borrower. The financial institution in such a case would make an offer, prior to trial, to settle the case for a lesser result than it thinks it can achieve. For example, if a lender thought that its liability on a borrower's claim was no greater than $5,000, it may offer for judgment to be taken against it in the amount of $6,000 in exchange for a dismissal of all claims. If the offer of judgment is then rejected (or not accepted within a specified period of time) and the borrower obtains a judgment for less than $6,000 at trial, the borrower would be subject to a fee award for all of the lender's post-offer fees. Note that, in this situation, a fee award is *not* automatic. The lender must still move for fees and have that request granted by the trial court.

The drawback to an offer of judgment is that, in real property cases, there is often confusion by the courts as to how to apply the rule when the recovery is of real property as opposed to a damages award. Though Nevada courts have yet to squarely rule on whether an offer of judgment is valid on a prospective claim regarding title to real property,[6] the results from jurisdiction to jurisdiction (and even among judges of the same court) may be so variable as not to render these statutes and/or rules a reliable option.

(b) Awards for prevailing against "vexatious" claims

Under NRS 18.010(2) (b), courts allow prevailing parties to recover fee awards where a claim or defense is "without reasonable ground" or was brought for the purpose of harassment. These awards tend to be easier to obtain than Rule 11 awards, discussed below, because they do not have as many procedural requirements. The Nevada legislature also intended for this statute to be read "liberally" so that attorney fees would be awarded "in all appropriate situations." It must be remembered, however, that these awards are *not* given simply because one party prevailed; there *must* be a record indicating that a claim or defenses was brought or maintained without reasonable ground or to harass the prevailing party. To that end, if a lender wants to collect attorney fees based on this statute, it is important for the lender to create a paper trail demonstrating that a borrower's claim or defense is groundless – communications between the borrower and lender, or between counsel, will likely be necessary to prevail upon this theory.

(c) Rule 11 sanctions

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[6] Nevada courts have not yet overturned a fee award based on judgment providing declaratory relief or quieting title, though the Nevada Supreme Court has made a distinction between these types of "prospective" claims for relief and claims for "retrospective relief," such as monetary damages. See City of Fernley v. State, 366 P.3d 699 (Nev. 2016). The Nevada Supreme Court has also indicated a concern that Rule 68 offers of judgment not be used to "force plaintiffs unfairly to forego legitimate claims." See Beattie v. Thomas, 99 Nev. 579, 588, 668 P.2d 268, 274 (1983).

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Seeking Attorney Fees from Borrowers (continued from page 7)

Perhaps the most commonly known method (among lawyers, anyway) to obtain a fee award is pursuant to Rule of Civil Procedure 11. Nevada's version of this Rule provides for a fee award by the Court when a claim or defense is asserted without an adequate basis by a party or its counsel. Though this Rule may seem straightforward, in practice it is often complicated and rarely results in a win for the moving party. Judges are often reticent to hold that a party or attorney has violated Rule 11 and, even in situations where they find that a party has asserted a claim or defense without adequate basis, will often give a litigant multiple chances to withdraw that claim or defense before awarding sanctions.[7] While it remains possible for courts to award attorney fees under this Rule, it remains one of the rarer sanctions, and therefore it is not usually effective.[8]

Attorney fees as special damages

Finally, in Nevada, lenders can move for and obtain an award of attorney fees as special damages in real property cases where slander of title is alleged in addition to a claim for quiet title/declaratory relief.[9] Similarly, an award of attorney fees may also available where a lender is defending a breach of contract claim or similar claim by a borrower.[10] The important thing to remember about an award under this doctrine is that the litigants must be seeking something *more* than declaratory relief. Otherwise, fees are not available as damages.

***Should* you seek an award of attorney fees?**

Once a financial institution has determined that it is in the correct legal posture to seek an award of attorney fees under contract or statute, it should consult with its counsel about whether pursuing fees in a particular case is wise. Though it may seem that seeking fees would always inure to the benefit of the financial institution, this is not always the case.

On the other hand, it may be a more prudent decision to pursue a borrower where that borrower has shown a protracted history of lawsuits against lenders. In that case, though recovery may be doubtful, the value of a fee award lies in potentially deterring future frivolous lawsuits by the borrower. In any event, when considering seeking a fee award against a borrower, especially a large fee award, it is wise to consider the size of the award, as well as the potential negative publicity associated with a lender seeking attorney fees from someone who has lost his or her home to foreclosure.

Another important consideration when determining whether to seek fees is the presiding judge. Trial judges have almost complete discretion over fee award decisions, which are rarely overturned by appellate courts. Outside of the context of a contractual provision or offer or judgment, Nevada state court judges are often reluctant to award large amounts of attorney fees, particularly where there is any doubt as to the operative facts. Many judges are far more sympathetic to borrowers than lenders, and will resolve any doubts in the borrower's favor. Therefore, to the extent that a lender is seeking a fee award, a solid evidentiary basis for that award, along with an analysis tailored to the trial judge's specific sensibilities, is necessary.

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[7] The so-called "safe harbor" provision of Rule 11, found in Rule 11(c)(1)(a), further requires that a fee motion must be served upon the party against whom an award is sought 21 days prior to filing the motion. While Nevada courts have some discretion in awarding Rule 11 sanctions on their own initiative under Rule 11(c)(1)(b), they almost never use that power.

[8] It should also be noted that, unlike other rules allowing for award of fees or costs, Rule 11 has a slightly different purpose: to deter abuses of the litigation system by lawyers and parties. "It is the intent of the Legislature that the court award attorney's fees pursuant to this paragraph and impose sanctions pursuant to Rule 11 of the Nevada Rules of Civil Procedure in all appropriate situations to punish for and deter frivolous or vexatious claims and defenses because such claims and defenses overburden limited judicial resources, hinder the timely resolution of meritorious claims and increase the costs of engaging in business and providing professional services to the public." Trustees of Plumbers & Pipefitters Union Local 525 Health & Welfare Tr. Plan v. Developers Sur. & Indem. Co., 84 P.3d 59, 63 (Nev. 2004)

[9] Horgan v. Felton, 123 Nev. 577, 579, 170 P. 3d 982 (2007).

[10] See Liu v. Christopher Homes, LLC, 321 P.3d 875, 880 (Nev. 2014).

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Seeking Attorney Fees from Borrowers (continued from page 8)

The first and most practical consideration by a lender must be whether it can ultimately recover any fees it is awarded. Any award of attorney fees will either be included in an existing judgment or reduced to its own judgment. It is much easier to obtain a judgment than to obtain satisfaction of one. Many times, borrowers are in foreclosure-related litigation because of their financial troubles. If it is likely that they do not have the liquid assets to satisfy a judgment, lender's counsel will have to conduct a judgment debtor's examination and potentially attach the property of the borrower. Garnishment of wages or freezing of bank accounts, sometimes across jurisdictions, may also be necessary. In the event that a borrower's assets are not located in the United States, separate application may have to be made to a foreign court system, an expensive and time-consuming process that is not always guaranteed to work because of its reliance on foreign judges who are often hostile to the idea of enforcing American judgments.[11] Even if those difficulties can be overcome, the point may become moot if a borrower declares bankruptcy. In these cases, while it may provide some advantage to *threaten* an award of attorney fees, the reality is that recovery of the award may present more problems if it is clear that the borrower cannot pay what is awarded.

When determining whether to bring a motion in front of a specific judge, it is important to consider that judge's recent history in cases involving banks. Fortunately, in Nevada, the recent explosion in HOA-lien litigation provides plenty of data for this analysis. With a judge who is decidedly pro-lender, there should be no question regarding whether the motion should be filed. Judges who could be characterized as more pro-borrower should be carefully evaluated to determine whether the expense of a motion for attorney fees, which requires full briefing and, most often, oral argument, is worth the relatively slim chance of recovering fees. Additionally, if a judge who is already inclined to be pro-borrower perceives that a lender or servicer is engaging in behavior that the judge feels is inappropriate or overly harsh, he or she may be more inclined to listen to a motion for reconsideration from the borrower.[12]

In conclusion, fee awards are not only possible in American courts; they are a reality. Careful consideration to how and when to seek an award, however, will be critical factors in determining the success of the application.

Of course, before addressing any fee award issues, a financial institution should consult with competent counsel in the applicable jurisdiction.

If you have questions about the subject matter of this article or desires assistance regarding post-judgment motions or fee awards, please feel free to contact Robert Finlay at rfinlay@wrightlegal.net, who will coordinate with our team of attorneys in Arizona, California, Nevada, Oregon, Utah or Washington, as appropriate.

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[11] See The Law on Recognition and Enforcement of Foreign Judgments: Is It Broken and How Do We Fix It?, 31 Berkeley J. Int'l L. 150 (2013) for a more in-depth discussion of the problems inherent in international enforcement of American judgments.
[12] Note that, under Nevada Rule of Civil Procedure 54(b), a trial judge may reconsider and change any order prior to entry of a final judgment adjudicating all claims against all parties.

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THERE IS NO SUCH THING AS A FREE HOUSE…

WELL, IN THE STATE OF WASHINGTON, THERE COULD BE…

by Lukasz I. Wozniak, Esq. and T. Robert Finlay, Esq.

Over the past several years, those who service loans in the State of Washington[1] have seen a dramatic rise in the number of lawsuits in which delinquent borrowers seek to quiet title to their homes on the grounds that lenders are barred from foreclosing based on Washington's six year statute of limitations.

Historically, these lawsuits allege that the foreclosure is time-barred because Notice of Acceleration letters have been issued more than six years prior to the initiation of the foreclosure process. However, based on recent case law, we foresee a very real danger of an increase in the amount of lawsuits brought by borrowers who have had their debts discharged in bankruptcy and either continued to make their monthly payments following their discharge, or engaged in a game of cat-and-mouse with the servicer, as result of which the servicer did not commence foreclosure within the six-year period following the discharge. Indeed, in at least one instance, the borrowers who obtained a bankruptcy discharge order successfully quieted title to their home against Fannie Mae based on Fannie Mae's failure to foreclose with the six-year period. The potential of these lawsuits – and given the result discussed above – creates a significant risk to the mortgage industry, which should be addressed, assessed, and mitigated by lenders and servicers.

Washington RCW 7.28.300 permits title owners – not necessarily borrowers – to commence quiet title actions against secured lenders to eliminate liens secured by the property based on the lender's failure to timely foreclose:

> The record owner of real estate may maintain an action to quiet title against the lien of … deed of trust on the real estate where an action to foreclose such… deed of trust would be barred by the statute of limitations, and, upon proof sufficient to satisfy the court, may have judgment quieting title against such a lien.

The applicable statute of limitations within which a lender can foreclose for purposes of RCW 7.28.300 is six years from the date of acceleration of the debt.

Recently, in *Edmundson v. Bank of Am., NA*, 194 Wn.App. 920, 931 (2016) ("*Edmundson*"), *Silvers v. U.S. Bank Nat. Ass'n*, 2015 WL 5024173 (W.D. Wash. Aug. 25, 2015)) ("*Silvers*"), and *Jarvis v. Fed. Nat'l Mortg. Ass'n*, 2017 WL 1438040 (W.D. Wash. Apr. 24, 2017 ("*Jarvis*"), Washington's State and Federal Courts addressed the impact of a bankruptcy discharge on the lenders' ability to foreclose within the purview of RCW 7.28.300.

In *Edmundson,* the Court of Appeals held that the borrowers' bankruptcy discharge, which terminated their personal liability under the promissory note, triggered the statute of limitations within which the lender was entitled to foreclose. The Court reasoned that since the borrowers owed no future payments after the discharge of their personal liability, the date of their last-owed payment kick-started the deed of trust's final limitations period. *Id.* at 931.

The same outcomes were reached by the Federal Courts in *Silvers* and *Jarvis.* In *Silvers,* the Court reasoned that because the bankruptcy discharge relieved the borrowers' personal liability on the note, no future payments were owed and no installments capable of triggering the limitations period remained. *Id.* at *4. Accordingly, the Court held that the six-year limitations period accrued at the time of the borrowers' last missed payment preceding their discharge of personal liability. *Id.*

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[1] While the purpose of this article is to discuss Washington State law, the analysis herein could be equally applicable to any State which has laws governing statute of limitations on foreclosure.

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There's No Such Thing as a Free House (continued from page 10)

In *Jarvis*, the Court actually granted the borrowers motion for summary judgment and quieted title pursuant to RCW 7.28.300 in borrowers' favor and against Fannie Mae, finding that the borrowers' bankruptcy discharge order triggered Washington's statute of limitations for foreclosure. The Court noted that "[t]he [bankruptcy] discharge … alert[s] the lender that the limitations period to foreclose on a property held as security has commenced" and that "[t]he last payment owed commences the final six-year period to enforce a deed of trust securing a loan. This situation occurs… at the payment owed immediately prior to the discharge of a borrower's personal liability in bankruptcy, because after discharge, a borrower no longer has forthcoming installments that he must pay." *Id.* at 2. The Court rejected Fannie Mae's public policy argument that "tying the discharge of a borrower's personal liability to a lender's right to enforce a deed of trust would automatically accelerate future installments secured by the deed of trust without the lender's consent and to the borrower's detriment." Instead, the Court found that Washington law supported the termination of Fannie Mae's secured interest under RCW 7.28.300:

> The discharge of a borrower's personal liability on his loan—the cessation of his installment obligations—is the analog to a note's maturation. In both cases, no more payments could become due that could trigger RCW 4.16.040's limitations period. The last-owed payment before the discharge of a borrower's personal liability on a loan is the date from which a secured creditor has six years to enforce a deed of trust securing the loan.
>
> The Jarvises stopped repaying their loan, Fannie Mae did not accelerate their obligation, and the Bankruptcy Court discharged their debts on February 23, 2009. They did not reaffirm. Their last installment payment owed, therefore, was the one immediately prior to their discharge. Over six years passed between that date and the date they filed for quiet title, February 11, 2016. RCW 4.16.040 forecloses Fannie Mae's right to enforce the deed of trust against them.
>
> *Jarvis* at**3-4.

This result clearly demonstrates the potential danger to secured lenders in situations involving accounts discharged in bankruptcy and makes it imperative that lenders and servicers remain vigilant in tracking all of such discharged accounts to ensure that their security interests remain protected. This is especially important in situations where the borrowers, having obtained orders discharging their debts, continue to make monthly payments on their loans, thus precluding foreclosure.

While the *Jarvis* court noted that, following bankruptcy, "a borrower and a lender may agree to reaffirm or renegotiate the borrower's dischargeable debt", clearly more effort is needed, as the borrowers are not required to agree to reaffirm their debt and/or to re-negotiate. Accordingly, in situations where the borrowers continue making their monthly payments (or at least a portion of them), we recommend tracking the file and discussing the lender's options with an attorney *before* the statute of limitations expires rendering the security unenforceable. On the other hand, in situations where the borrowers remain delinquent on their payments, we recommend that lenders ensure that the foreclosure proceedings are initiated before the expiration of the six-year statute of limitation period.

If you have any questions regarding the statute of limitations in Washington or in any of the states Wright, Finlay & Zak, LLP covers (including Oregon, Utah, New Mexico, Arizona, Nevada and California), please feel free to contact Luke Wozniak at lwozniak@wrightlegal.net or Robert Finlay @ rfinlay@wrightlegal.net.

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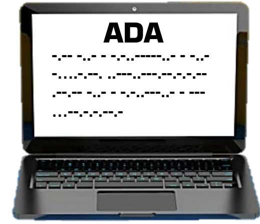
LOAN ORIGINATOR AND SERVICER WEBSITES FIND THEMSELVES IN THE ADA'S CROSSHAIRS

by Olivier J. Labarre, Esq. and T. Robert Finlay, Esq.



When George H.W. Bush signed into law the Americans with Disabilities Act in 1990 ("ADA") Title III, it was intended to provide equal access to those with disabilities. At the time, the internet as we now know it did not exist. As a result, no one could have predicted how the ADA would interact with online services. Flash forward to 2018 and there were nearly 5,000 ADA lawsuits filed in Federal Court for alleged website violations, filed in the ***first half of 2018 alone.***[1] At this point, the number is expected to rise nearly 10,000 for the calendar year, an increase of 30% over the number of similar suits in 2017.[2] As more providers tout their web access, one can expect those numbers will continue to increase in the future.

While many of the website-access ADA complaints targeted retailers, restaurants and universities, a number of our servicer and lender clients have been recently hit with a rash of demand letters and, in some instances, lawsuits under the ADA alleging that public accommodations' websites are not accessible to blind individuals. The claimants contend that they visited our clients' website, and were denied full and equal access to the client's services as well as the ability to enjoy the services offered to the public through the website. The demand letters and lawsuits allege various violations of both Federal and State law. Generally, these demands and lawsuits seek early settlement with the proviso that the client remediates its website. A brief overview of the law in this area, as well as potential exposure for clients, is set forth below.

There is no longer any meaningful dispute that business websites are places of public accommodation under the ADA. The Department of Justice ("DOJ"), charged with implementing regulations for compliance with ADA mandates, has stated as much on numerous occasions and courts across the country have rejected arguments that websites do not fall under the ADA. Moreover, courts in California have held that a website's noncompliance with the ADA is in and of itself sufficient to trigger a violation of the ADA without requiring the claimant to first establish that he or she genuinely sought the goods or services of the business. Such a violation calls for a statutory penalty of $4,000.00 and, more importantly, potentially triggers the claimant's right to recover attorneys' fees under the ADA and various state law corollaries.

To complicate matters, there are no firm guidelines on exactly how a website must be formatted or implemented to comply with current ADA mandates against nondiscrimination and communication. The DOJ has yet to issue formal guidelines for website compliance under the ADA and, based upon its most recent public statements, has no plans to do so and instead has taken the position that such guidelines are the responsibility of the legislature or the Attorney General. Courts have generally accepted that compliance with the privately developed Web Content Accessibility Guidelines (WCAG) 2.0 technical standards are sufficient to satisfy current ADA mandates, but again the DOJ recently announced in October of 2018 that "public accommodations have flexibility in how to comply with the ADA's general requirements of nondiscrimination and effective communication. Accordingly, noncompliance with a voluntary technical standard for website accessibility does not necessarily indicate noncompliance with the ADA," indicating, at the very least, that noncompliance with WCAG 2.0 is not in and of itself a violation of the ADA, but again refusing to establish firm guidelines for private businesses to follow.

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[1] Los Angeles Times, November 11, 2018: Lawsuits Target Access to Websites.
[2] Id.

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ADA (continued from page 12)

Based on the state of the law and the right to recover attorneys' fees under the ADA and its State law corollaries, plaintiffs' attorneys are scouring websites for potential violators. Most attorneys first send demand letters; but, if their demands are not met, quickly file suit against businesses and service providers. These demands and lawsuits pose a significant risk in the terms of statutory damages, remediation costs and potential attorneys' fees.

With the law in this area developing on a near daily basis, there are several defenses that loan originators, servicers or other providers can assert. However, the best defense is to take preventative measures now to avoid these demands and lawsuits in the future. We encourage you to take this opportunity to evaluate your own websites and, if necessary, work towards updating them in an effort to both avoid these demands and lawsuits, and to ensure a viable defense in the event such a demand or lawsuit is served on you.

If you have any questions, please do not hesitate to contact Robert Finlay at rfinlay@wrightlegal.net or Olivier Labarre at olabarre@wrightlegal.net.

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LENDERS AND SERVICERS FACE INCREASED RISK WITH CALIFORNIA'S NEW AFFORDABLE HOUSING

by Lukasz I. Wozniak, Esq. and T. Robert Finlay, Esq.

Although enacted just over one year ago, the impact of California Senate Bill 2 – commonly referred to as the Building Homes and Jobs Act ("SB 2" or the "Act"), has not yet been felt by lenders and loan servicers. But, as the revenue from the Act comes pouring in at a higher than expected rate,[1] lenders and servicers will start to see more affordable housing construction throughout California, which in turn will mean more loans on affordable housing units to originate and service.

The Act was designed to address California's affordable housing dilemma[2] by bringing in an estimated annual revenue of $250 million through an increase in the recording fees for the recording of documents in real estate transactions. The funds would be dedicated to developing affordable, low income housing in California.

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[1] See, Toni G. Atkins, "Building homes and jobs" <https://sandiegodowntownnews.com/building-homes-and-jobs/>; see also, <http://www.hcd.ca.gov/policy-research/housing-package/cahp-faq.shtml#sb2>;
Senate Bill 2 Planning Grant Program Year 1 Guidelines < http://www.hcd.ca.gov/policy-research/docs/sb2-plng-grant-draft-guidelines.pdf>

[2] According to the CA Treasurer's Office, CA needs approximately 1.5 million additional affordable housing units. <https://www.treasurer.ca.gov/ctcac/factsheet.pdf>

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California's New Affordable Housing (continued from page 13)

It seems that this revenue goal has been achieved, as California's 2018-19 budget allotted $5 billion to addressing the affordable housing and homelessness issues, $255 million of which came from the SB 2 fund.[3] Accordingly, in the near future Californians will likely be provided with new, affordable, low income housing units for purchase. While this is great news for Californians and local governments (which will obtain additional funding from State and Federal government), it is important to understand the potential impact of an influx of low income housing units will have on lenders and servicers who fund and service loans secured by low income housing units.

California generates new "affordable" of "low income" housing units through either new construction or rehabilitation/reclassification of the existing housing units. These new units are then offered for sale through various housing programs administered by local (city) governments and are eventually sold to qualified individuals at below-market-rate prices. Because of this, these units are subject to various value and/or use restrictions, which restrictions are enforceable over a period of time (generally, between 30 and 45 years), are binding on lenders as well as the borrowers, and are senior to any mortgage liens. Generally, these restrictions limit the use of property to a principal residence use only, constrain the borrower's right to refinance or sell the property, and provide the locality where the property is located with a "right of first refusal" and other rights in the event of the borrower's default, a catastrophic event, or condemnation of the property. Failure to comply with these restrictions subjects the lenders, servicers, and foreclosure trustees to potential liability from not only the borrower, but also the locality, exposing the industry to damages not generally foreseeable in regular residential mortgage transactions.[4]

With the volume of loans on low income projects likely to increase in the near future, lenders and servicers should understand the risks associated with these loans and limit their potential exposure and liability through a thorough investigation process.

As part of their due diligence in connection with *purchase* loan transactions, in addition to obtaining a title report/guarantee, the lender should specifically review and understand the restriction agreement recorded against the property. ***Note – Wright, Finlay & Zak has seen many instances where the title company excepted from coverage the low income housing restrictions, leaving the lender and subsequent investors and servicers subject to the often onerous restrictions without any knowledge of their existence and/or understanding of the consequences of failure to comply with them.*** The lender should study the restriction agreement in detail to ensure that the loan transaction does not violate its terms. The lender should also ensure that the restriction agreement is included in the collateral file, provided to the loan servicer and the system noted for future use, i.e., at the time of foreclosure.

In addition, since the localities that offer affordable housing units for sale ensure that they have certain rights in the event of the borrower's default, restriction agreements and requests for notice of default (recorded by the city or agency) should be reviewed and studied before the commencement of (and also during) the foreclosure process to ensure that these rights are not violated.[5]

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[3] The 2018-19 budget is located as <http://www.ebudget.ca.gov/FullBudgetSummary.pdf>

[4] As a general matter, the lender can be held responsible for all damages caused by the violation to the city, including the damages resulting from the use of property as a low income housing unit, potential loss of federal and state funding, cost of a potential replacement property, etc.

[5] While the trustee should itself obtain the request for notice, given the potential liability to the lender/servicer resulting from a failure to provide notice, it is a better business practice for the servicer to provide that document to the trustee.

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California's New Affordable Housing (continued from page 14)

While this additional due diligence is recommended in purchase loan transactions, it is even more important in *refinance* transactions. The restriction agreements placed on low income housing units often prohibit or significantly constrain refinance loans. Accordingly, it is imperative for the potential lender to study the restriction agreement and ensure that the refinance loan is permitted in the first place, or whether additional steps are required to satisfy the restriction agreement – such as, for instance, obtaining pre-approval of the refinance from the city.

Finally, in the event of a lawsuit involving a low income housing unit, the lender, servicer, and/or trustee should consult attorneys who are experienced in litigating the low income housing matters to fully understand its potential liability and exposure.

Wright, Finlay & Zak, LLP specializes in mortgage-related litigation, compliance and regulatory matters for its clients throughout the Western United States, including California, Nevada, Arizona, Washington, Utah and Oregon. If you have any questions regarding this issue or any other matter, please contact Robert Finlay at rfinlay@wrightlegal.net or Luke Wozniak at lwozniak@wrightlegal.net.

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WFZ PROFILE:
BRIAN J. WAGNER, ESQ.
PARTNER

Brian J. Wagner, Esq.
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Brian J. Wagner joined Wright, Finlay & Zak in 2018 and recently celebrated his one year anniversary with the firm. For the last nine years, his practice has focused on the representation of lenders, banks, loan servicers and credit unions in litigation and transactional matters. His experience ranges from advising companies on the front end of transactions and when necessary, through a jury trial or appeal. Mr. Wagner has an understanding of the goals and needs of his clients and focuses his efforts on a targeted and cost-effective strategy.

Mr. Wagner is originally from New Jersey, but has lived in California for more than 25 years. He earned his B.A. degree from California State University Long Beach in 2001 and then attended Thomas Jefferson School of Law. During law school, Mr. Wagner worked as a law clerk at a well-respected San Diego law firm handling medical malpractice matters. After graduation, he spent six years representing doctors and dentists in malpractice lawsuits, as well as companies sued for product liability.

Mr. Wagner takes pride in his relationship with his clients and is always available to them, no matter how big or small the issue is. He has a passion for philanthropic causes, volunteering with various Orange and San Diego County organizations.

Mr. Wagner is active with the Mortgage Bankers Association, California Mortgage Bankers Association and Construction Financial Management Association, and has spoken on industry panels. Mr. Wagner is licensed to practice in California and Texas, and is in the process of seeking admission to practice in New Mexico.

When is not working, he enjoys traveling, watching sports and spending time with family.

UPCOMING INDUSTRY EVENTS

Date	Organization	Event	Location
April 7-9	CMBA	2nd Annual California MBA Chairman's Conference	La Jolla, CA
April 15-16	IMN	6th Annual Residential Mortgage Servicing Rights Forum	New York, NY
April 28-30	Texas MBA	103rd Annual Convention	San Antonio, TX
April 29-30	WBA	2019 Diversity Forum	Anaheim, CA
April 30 – May 1	ALFN	Willpower Summit	Dallas, TX
May 5-8	MBA	Legal Issues and Regulatory Compliance Conference	New Orleans, LA
May 8	AMDC	2019 Five Star Diversity Symposium	Dallas, TX
May 7-8	CREFC	Commercial Real Estate Finance Summit – West	Santa Monica, CA
May 14-17	MBA	Commercial/Multifamily Servicing & Technology Conference	Los Angeles, CA
May 19-22	ICSC	RECon The Global Retail Real Estate Convention	Las Vegas, NV
June 3-4	IMN	4th Annual The Mortgage Notes & NPL/RPL Forum (West)	Dana Point, CA
June 10-12	CREFC	CREFC Annual Conference 2019	New York, NY
June 24-26	NBA	Nevada, Oregon & Idaho Annual Convention	Coeur d'Alene, ID

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WFZ FIRM NEWS

ROBERT FINLAY APPOINTED AS GENERAL COUNSEL FOR THE CALIFORNIA MORTGAGE ASSOCIATION (CMA)

Robert Finlay has been appointed as General Counsel for the California Mortgage Association (CMA). The CMA is not only the largest mortgage trade association in the United States, it is also the only private mortgage trade association in the country. It is dedicated to the ongoing education of California-licensed private money lenders, as well as the preservation of our industry through legislative review and advocacy. The CMA prides itself in being the voice of trust deed lenders and investors throughout the state and representing our industry's best interests at all times. Its members represent individuals, sole proprietorships, corporations and partnerships involved with the origination, selling, or servicing of trust deed loans.

As CMA General Counsel, Mr. Finlay will help the Board tackle challenging DRE and CFL licensing issues, draft amicus briefs on key legal issues, participate in legislative issues, present at the quarterly conferences and generally advise the Board and its membership. "I am very honored, excited and humbled by the selection," Mr. Finlay said. "I look forward to devoting myself and the firm's resources to helping the CMA grow and thrive."

WFZ WELCOMES ITS NEW ATTORNEYS!

JOEL F. NEWELL

Mr. Newell joins our Scottsdale, Arizona office as a Senior Associate. His practice focuses on creditor rights in both commercial and consumer bankruptcy law including Chapter 11, 13 and 7 matters, adversary litigation, relief from stay matters, proofs of claim, plan objections and all other substantive bankruptcy motions. He also focuses on real estate litigation, including lender and servicer liability defense, wrongful foreclosure defense, fair debt collection practices defense, and title disputes. Prior to joining the firm, Mr. Newell represented creditors and landlords in Chapter 11 commercial bankruptcy cases and Chapter 7, 11, and 13 bankruptcy trustees. Mr. Newell is licensed to practice in Arizona.

YAO WEN

Yao "Kelvin" Wen joins our Las Vegas office as an Associate. During his time at Brigham Young University's J. Reuben Clark School of Law, Mr. Wen was a summer associate at several big law firms in Taiwan, New York, and China, and was a law clerk at the Fourth District Court of Utah. Since joining Wright, Finlay & Zak, Mr. Wen has focused primarily on employment-based immigration cases, such as EB-1, O-1, L-1, etc., business transaction and corporate law, government investigations and white collar criminal defense. Mr. Wen is licensed to practice in Nevada.

JOSHUA S. SCHAER

Mr. Schaer joins our Seattle, Washington office as a Senior Associate. He has over 17 years of experience representing financial institutions in litigation, including managing discovery, motions and appeals. From 2008-2015, Mr. Schaer served two elected terms on the Issaquah, Washington City Council and was appointed chair of a regional transportation board. He is qualified as a pro tem judge in the King County District Court in Washington. Mr. Schaer is licensed to practice in Washington.

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