

BEFORE YOU BEGIN **LITIGATION**

presented by:
J. Patrick Haywood
and
Mark K. York
Carruthers & Roth, P.A.
Phone: 336-478-1152
e-mail: mky@crlaw.com



2

Overview

- 5 Ws
- *RL Regi NC, LLC v. Lighthouse Cove, LLC*
- *Highpoint Bank v. Highmark Properties*
- Post *Highpoint Bank* Expectations
- Past Experiences
- Questions



The Five W's

- Who are the parties
- What kind of debt is at issue
- When to sue or foreclose
- Where are your documents
- Why conduct pre-lawsuit analysis



What are the Parties

- Creditor (aka the Bank)
- Borrower (aka the Debtor)
- Guarantor (aka the Deep Pockets)
- The Court (Judge v. Jury)



What Kind of Debt is at Issue

- Real Property Loan
- HELOC
- Operating Capital Loan
- Inventory or Receivables
- Equipment Loan
- Consumer Goods



When to Sue or Foreclose

- Foreclosure
 - What is the Bank's priority to the collateral
 - What is the Bank's goal
- Lawsuit
 - Post foreclosure
 - Pre foreclosure
 - Collection



Where are the Bank's Documents

- Original Loan Documents
- Emails
- Written correspondence
- Bank's policies
- Account records



Why Conduct Pre-Lawsuit Analysis

- Potential for counterclaims
- Potential for collection
- Potential for extensive discovery
- Potential for jury trial
- Cost / Benefit analysis



RL Regi NC, LLC v. Lighthouse Cove, LLC

- The Facts:
 - Regions Bank loaned \$4M+ for acquisition and development of 57 Acres (Lighthouse)
 - Secured by:
 - Deed of trust on real property
 - Personal guaranties of Lighthouse Members
 - Personal guaranties of Members' spouses
 - 3 years later, Lighthouse defaulted on loan
 - Parties enter into Forbearance Agreement
 - Bank waives rights under loan documents
 - Guarantors waive "any and all claims, defenses and causes of action that occurred prior to the date of the forbearance agreement"



RL Regi NC, LLC continued

- The Facts continued:
 - Regions Bank sold loan to RL Regi
 - After expiration of Forbearance period, Lighthouse again defaults
 - RL Regi sues Lighthouse and Guarantors
 - One spousal guarantor raises ECOA Defense
 - Trial and CoA found the guaranty violated ECOA and denied RL Regi recovery
 - RL Regi appealed to NC Supreme Court



RL Regi NC, LLC continued

- The Law:
 - ECOA prohibits creditors from discriminating against applicants in credit transactions “on the basis of race, color, religion, national origin, sex or marital status, or age.”
 - While a creditor may not automatically require that a spouse be a party to a loan, it can do so if it first finds the applicant is not independently creditworthy



RL Regi NC, LLC continued

- The Supreme Court holding:
 - The Court did not evaluate the ECOA defense because it found the trial court improperly allowed the spousal guarantor to assert a defense that she waived under the forbearance agreement, thus depriving the lender of its rights under the forbearance agreement.
 - Specifically, the Court held that parties are free to waive various rights, including those arising under statutes.



RL Regi NC, LLC continued

- The holding continued:
 - Although the spousal guarantor did not specifically waive the ECOA defense in the forbearance agreement, the Court found the “comprehensive language contained in the agreement” and “overall expansive language of the waiver” to be sufficient to include any potential claim or defense.
 - Ultimately, the Court stated that “a waiver of potential defenses to the guaranty, including a potential defense for a violation of the ECOA, was a part of defendant’s decision to accept the benefits of the forbearance agreement.”



Highpoint Bank v. Highmark Properties

- The Facts:
 - The Bank issued two loans, promissory notes for \$4.7 million and \$1.75 million, to Highmark
 - The promissory notes were secured by deeds of trust on two parcels of real estate owned by Highmark.
 - Also the promissory notes were guaranteed by the principals of the Highmark
 - Highmark defaulted on the promissory notes, leaving an indebtedness of \$3,541,356 on the first note and \$1,336,556 on the second note.



Highpoint Bank continued

- The Facts continued:
 - The Bank filed a lawsuit against the Highmark and the Guarantors.
 - Contemporaneously, the Bank instituted foreclosure proceedings on the two parcels of real estate.
 - At the foreclosure sale, the Bank was the only bidder, paying \$2,578,000 for one property and \$720,000 for the other property.
 - The Bank filed a motion for summary judgment seeking to recover the deficiencies from the Guarantors.
 - Three weeks later, the Bank voluntarily dismissed without prejudice all claims against Highmark.



Highpoint Bank continued

- The Facts continued:
 - The Bank brought a motion seeking a ruling that the Guarantors were not entitled to raise any defense based upon the fair market value of the collateral properties pursuant to N.C. Gen. Stat. § 45-21.36.
 - The trial court denied the Bank's request and held that a jury needed to decide the value of the properties.
 - The jury determined the fair market value of the first parcel as \$3,723,000 and that of the second parcel as \$1,034,000.
 - Accordingly, the trial court ruled that Highmark's indebtedness on the First Note was reduced to \$0.00, because the jury had determined that the fair market value of the first parcel was greater than Highmark's remaining debt of \$3,541,356.



Highpoint Bank continued

- The Facts continued:
 - Next, the trial court ruled that Highmark's indebtedness on the Second Note was reduced to \$302,556—the difference between the jury's determination of the fair market value of the second parcel and Highmark's remaining debt of \$1,336,556.
 - The trial court ruled that Highmark and the Guarantors were **jointly and severally liable** and ordered payment to the Bank in the amount of \$302,556 for the remaining uncollected debt, plus attorney's fees and interest.
 - The Bank appealed.



Highpoint Bank continued

- The Law:
 - N.C.G.S. § 45-21.36 permits a person whose property has been purchased by the lender at foreclosure sale to assert that the property was worth more than the amount bid by the lender.
 - If a jury finds that lender bid less than fair market value, the deficiency amount can be reduced or eliminated.
 - Given that most foreclosure sales end with the lender taking title to the property and a deficiency owed, defenses under N.C.G.S. § 45-21.36 are frequently raised and tried before a jury.



Highpoint Bank continued

- The Law continued:
 - Since 1979, the North Carolina Court of Appeals has held that N.C.G.S. § 45-21.36 does not apply to guarantors and that the statute was limited “to those persons who held a property interest in the mortgaged property.”
 - This distinction became crucial for lenders since it meant pursuing a post-foreclosure deficiency judgment against a guarantor was often much easier than pursuing that same judgment against a borrower.



Highpoint Bank continued

- The Supreme Court holding:
 - The Court rejected the prior decisions from the Court of Appeals, and held that because N.C.G.S. § 45-21.36 was passed in 1933 as part of depression era laws designed to protect debtors, it must be construed “more broadly.”
 - N.C.G.S. § 45-21.36 is not really a defense but “an equitable method of calculating the indebtedness;” and
 - The protections of the statute are “not subject to waiver.”



Post *Highpoint Bank* Expectations

- N.C.G.S. § 45-21.36 will now be raised in every post-foreclosure deficiency case in which the lender takes title, whether the action is against borrowers or guarantors.
- Jury trials in post-foreclosure deficiency actions will become the norm because the value of real estate is almost always a question of “material fact” to be determined by a jury not a judge.
- Lenders will most likely obtain judgments on the note/guaranty **prior** to foreclosing on the real property securing the note.
- Lenders may start pursuing judicial foreclosures rather than power of sale foreclosures because N.C.G.S. § 45-21.36 does not apply to judicial foreclosures.



Past Experiences



QUESTIONS?

