

LERCH EARLY &amp; BREWER

## Commercial Lending Bulletin

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OUR  
PROFESSIONALS

**Lawrence G. Lerman**  
Chair  
[Email](#)  
301-657-0163

Welcome to another issue of the *Commercial Lending Bulletin*, a newsletter published monthly by the Commercial Lending Group at Lerch, Early & Brewer as a service to our clients. Here, you will find articles written by our attorneys covering a variety of current legal issues as they affect lending law. We publish the *Bulletin* as part of our ongoing efforts to provide our clients with responsive service and practical advice when needed.

This newsletter is sent via email in HTML format. If you wish to print a copy of the newsletter, you may access a .pdf version by following the "Printer-Friendly version" link below.

We appreciate any feedback and invite you to contact us with any questions. If you do not want to receive any further newsletters from us, follow the link at the bottom of this email to be removed from our list of recipients.

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#### In This Issue:

##### **Lender Succeeds in Obtaining a Deficiency Judgment**

A Texas district court determined that a lender is able to recover on a deficiency judgment after foreclosure on a deed of trust failed to yield enough proceeds to pay off the loans secured by the deed of trust. In *Rabo Agrifinance, Inc. v. Veigel Farm Partners*, the Northern District of Texas refused to allow a defendant debtor to avoid liability by protesting the lender's request for a deficiency judgment of \$1,964,355.06.

##### **Choice of Laws Provision in Loan Commitment Prohibits Claim**

A U.S. District Court in New Jersey found that a debtor was not able to bring a claim based on Florida law when the debtor's commitment letter contained a New Jersey choice-of-law provision and the claim was not recognized under New Jersey law.

##### **Allegations of Failure of Service of Process Must Be Substantiated**

The New York State Supreme Court struck down the motion of a commercial lender to set aside a default judgment against it for lack of service of process. The Supreme Court held that there was evidence that service on the lender was effected through the state Secretary of State's office by certified, return-receipt mail, and while the designated agent disputed proper service, he offered no proof it was not made.

##### **Follow-Up Regarding Documents Under Seal**

As a follow up to last month's newsletter practice tip about documents under seal, the Daily Washington Law Reporter reported a case, *Murray v. Wells Fargo Mortgage* (D.D.C.A. No. 06-CV-1383, July 17, 2008), which held that the mere recitation on the signature page that "we have hereunto set our hands and seal" was insufficient to create a document under seal and that the law requires that there either be an actual seal or some typed, printed or handwritten symbol as a substitute for the seal intending to operate as a seal.

##### **Seminar Alert!**

Look out for a seminar scheduled for October 28 discussing issues concerning governance and operation of business entities and their impact on business lending. Arthur Lafionatis and Raymond Sherbill will discuss issues such as the death, disability or bankruptcy of members, partners and managers, owner loans, subordination and intercreditor agreements, along with asset versus stock sales and their impact on business lenders.



**Joel S. Aronson**  
[Email](#)  
301-347-1276



**Cindi E. Cohen**  
[Email](#)  
301-657-0169



**Arthur F. Lafionatis**  
**Email**  
 301-657-0731



**Alison W. Rind**  
**Email**  
 301-657-0750



**Arnold D. Spevack**  
**Email**  
 301-657-0749



**Vicki R. Canales**  
**Email**  
 301-907-2803



**Jeremy I. Goldman**  
**Email**  
 301-657-0732

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## Lender Succeeds in Obtaining a Deficiency Judgment

**A TEXAS DISTRICT COURT DETERMINED THAT A LENDER IS ABLE TO RECOVER ON A DEFICIENCY JUDGMENT AFTER FORECLOSURE ON A DEED OF TRUST FAILED TO YIELD ENOUGH PROCEEDS TO PAY OFF THE LOANS SECURED BY THE DEED OF TRUST. IN *RABO AGRIFINANCE, INC. V. VEIGEL FARM PARTNERS*, THE NORTHERN DISTRICT OF TEXAS REFUSED TO ALLOW A DEFENDANT DEBTOR TO AVOID LIABILITY BY PROTESTING THE LENDER'S REQUEST FOR A DEFICIENCY JUDGMENT OF \$1,964,355.06.**

Defendant Veigel Farm Partners and its affiliates signed notes in favor of Plaintiff Rabo Agrifinance and its affiliates entitling it to borrow a total of up to \$2,807,468.40. The transactions took place as four separate loans between March, 1997 and May, 1999. The loans were secured by deeds of trust that allowed the trustees to foreclose on the liens and sell the property at public auction in the event of a default under the notes. When Veigel filed for bankruptcy, the principal amount outstanding under the loans as of October 21, 2002 was determined to be \$1,500,000 plus interest. Veigel again defaulted under the bankruptcy settlements and a foreclosure sale was held on the deed of trust in second lien position, yielding \$20,000 in proceeds. Rabo now requests a deficiency judgment for \$1,964,355.06.

The court determined that in order to allow a judgment under the notes, it required proof that i) Veigel signed the notes, ii) Rabo was the present holder of the notes, and iii) the notes were in default. First, Veigel did not challenge its signature on the notes which it provided for the court to review. Second, while the notes were assigned several times among Rabo and its affiliates, and, while the entities further reorganized during this time, Veigel provided no evidence to dispute the present ownership of the notes by Rabo, nor did the court find any. Third, because of the prior foreclosure action, the court found that it was clear the notes were in default.

Next, the court determined that recovery of a deficiency judgment after foreclosure required proof of i) the amount due at the time of foreclosure, ii) proper notice of acceleration, iii) valid foreclosure sale, and iv) credit given for the amount received at foreclosure and for other legitimate credits. Here, the court reviewed various affidavits, the previous state court case and the foreclosure sale and found that Rabo had met all requirements. The court stated further that Veigel had not created any genuine issues of material fact to call any of these elements into question and prevent judgment in favor of Rabo.

Veigel next tried to argue that Rabo's claim for deficiency in this case had been a compulsory counterclaim in the previous state court case and that since this counter-claim had not been filed, Rabo had missed its opportunity for judgment. Again, the court sided with Rabo, stating that in Texas a lender is not required to counterclaim for a deficiency judgment so as to protect its right to choose from among various remedies. Further, Veigel argued that Rabo was barred by the statute of limitations from pursuing its claim any further. The court disagreed, stating that this issue had been tried in the prior, state-level case and decided in favor of Rabo since its claim was made within two years of the foreclosure sale. Absent error, the court would not overturn the prior decision.

The court finally stated that, although Rabo was entitled to its deficiency judgment, it could not determine the exact amount of the deficiency judgment, since it lacked information regarding the credits to which Veigel was entitled. Yet, the case provides an example for other lenders to follow, as it confirms the lender's procedure and rewards it with a judgment.

The case above is cited as *Rabo Agrifinance, Inc. v. Veigel Farm Partners*, 2008 WL 341425 (N.D. Tex.)

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## Choice of Laws Provision in Loan Commitment Prohibits Claim

**A U.S. DISTRICT COURT IN NEW JERSEY FOUND THAT A DEBTOR WAS NOT ABLE TO BRING A CLAIM BASED ON FLORIDA LAW WHEN THE DEBTOR'S COMMITMENT LETTER CONTAINED A NEW JERSEY CHOICE-OF-LAW PROVISION AND THE CLAIM WAS NOT RECOGNIZED UNDER NEW JERSEY LAW.**

In 2003 Brauser Real Estate LLC, a Florida company, received financing for a commercial property development from Meecorp Capital Markets, LLC, a New Jersey company. Meecorp delivered to Brauser a loan commitment which contained a choice-of-law provision that stated that the commitment would be governed by and construed in accordance with the "laws of the State of New Jersey without regard to the principals of conflict of laws thereof." Brauser subsequently executed the loan commitment and paid a \$200,000 commitment fee. The loan did not close in accordance with the commitment letter and Brauser requested the return of its commitment fee and the \$25,000



**Shannon N. Mandel**  
**Email**  
 301-907-2815

application fee, making the claim that the loan commitment was illegal. Meecorp refused to refund the fees and Brauser brought suit in Florida state court for violation of the Florida Loan Broker Act, restitution, unjust enrichment and rescission. Meecorp removed the case to federal court and subsequently transferred the case to the U.S. District Court of New Jersey pursuant to the choice-of-law provision in the loan commitment.

Brauser's claim was that Meecorp violated Florida statutes that required mortgage brokers and mortgage lenders to be licensed by the State of Florida and prohibited any loan broker from collecting advance fees from a borrower to provide services. Brauser argued that the loan commitment was illegal and unenforceable because Meecorp was an unlicensed mortgage broker. Meecorp countered that even if it did violate Florida law, the New Jersey choice-of-law provision in the loan commitment governed and the loan commitment was still enforceable, as New Jersey had no comparable law regarding mortgage brokers licensing or fees.

When determining whether a choice-of-law provision in a contract is enforceable, the court applies the choice-of-law rules of the forum state, in this case, New Jersey. New Jersey's choice-of-law rules state that a choice-of-law provision will govern unless: 1) the state chosen has no substantial relationship to the parties or the transaction; or 2) the application of the law chosen would conflict with a fundamental public policy of a state having a greater interest in a determination of a particular issue.

In this case, the Court found that Meecorp was a New Jersey limited liability with its principal place of business in the State of New Jersey. Also, the intention of the parties to choose New Jersey choice-of-law was stated unambiguously in the loan commitment. Finally, the Court found that the loan commitment was prepared in New Jersey and the money loaned was to come from New Jersey. The Court found that while Florida did have an interest in the matters, Florida did not have a materially greater interest than New Jersey. The Court found that the applicable New Jersey choice-of-law provisions were enforceable and that the claims Brauser brought against Meecorp based on Florida statutes were dismissed.



**Michael D. Smith**  
**Email**  
 301-657-0166

## OUR SERVICES

Providing lenders with only the highest and most knowledgeable levels of lending counsel in all phases of commercial lending transactions.

Representing both borrowers and lenders in complex real estate and development transactions.

Advising and counseling in the structuring, documenting and closing of asset-based loans, and in the perfection of the lender's security interest.

Providing counsel to bank and non-bank lenders in closing government guaranteed loans under the 7(a), 504, B&I and "piggyback" loan programs.

Providing our clients with the

Lenders should consider the issues presented here when deciding on choice-of-law provisions for their loan commitments. Ideally, choice-of-law provision would be from a state that has a substantial relationship to the parties or the transaction. Choice-of-law is an area that can give lenders additional rights, but only if they are in compliance with the law and aware of any statutory obligations they may have. When in doubt, consult legal counsel to ensure that your you are complying with your chosen state's choice-of-law rules.

The case above is cited as *Brauser Real Estate, LLC v. Meecorp Capital Markets, LLC*, et. al., No. 06-cv-01816 (SDW) (D.N.J. 02/04/08)

## Allegations of Failure of Service of Process Must Be Substantiated

**THE NEW YORK STATE SUPREME COURT STRUCK DOWN THE MOTION OF A COMMERCIAL LENDER TO SET ASIDE A DEFAULT JUDGMENT AGAINST IT FOR LACK OF SERVICE OF PROCESS. THE SUPREME COURT HELD THAT THERE WAS EVIDENCE THAT SERVICE ON THE LENDER WAS EFFECTED THROUGH THE STATE SECRETARY OF STATE'S OFFICE BY CERTIFIED, RETURN-RECEIPT MAIL, AND WHILE THE DESIGNATED AGENT DISPUTED PROPER SERVICE, HE OFFERED NO PROOF IT WAS NOT MADE.**

In March 2005, 1450 Gun Hill Road LLC and Sterling Trust Co. provided \$2.7 million in financing to enable Capital Hill Partners, LLC to purchase commercial property in Manhattan from Columbia Estates LLC. As collateral to secure the financing, Capital executed a mortgage in favor of Gun Hill and Sterling. Without the knowledge of Gun Hill and Sterling, Capital also borrowed \$1M from Columbia and granted Columbia a second mortgage on the property, dated the same day as the Gun Hill and Sterling transaction. The Columbia mortgage expressly provided that it was subordinate to Gun Hill and Sterling's mortgage.

Capital failed to make its final principal and interest payment on the maturity date of the Gun Hill and Sterling loan and on May 1, 2007, Gun Hill and Sterling commenced a foreclosure action. On May 11, 2007, Columbia was served with the summons and complaint by service upon the New York Secretary of State. Once served, the Secretary of State sent a copy of the summons and complaint, by certified mail, return receipt requested, to Columbia, in care of its designated agent for service of process, Itzhak Katan, at the address on file with the Secretary of State. On May 17, 2007, Katan, or someone on his behalf, signed the Secretary of State's certified mail receipt.

Columbia did not appear in the action within the thirty days allotted by statute. However, on Sept.

necessary resources to deal constructively with problem loans and the implementation of creative loan work-out arrangements.

## PRACTICE AREAS

**Business and Taxation**

**Commercial Lending**

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**Elder Law**

**Employment and Labor**

**Estate Planning and Probate**

**Family Law**

**Health Care**

**Land Use and Zoning**

**Litigation**

**Real Estate Transactions**



17, 2007, after Gun Hill and Sterling had moved for a judgment of foreclosure but before the judgment was entered, Columbia filed a notice of appearance. Columbia took no further action at that time. On Oct. 11, 2007, the Court issued a judgment of foreclosure and sale on default against Capital. On Nov. 27, 2007, Columbia then filed a motion to vacate the default. In a related affidavit, Katan said he did not recall receiving the summons and complaint in the mail. He also contended that he first learned of the action when he returned from a trip overseas at the end of September, 2007.

The New York Supreme Court noted that the New York Civil Practice Law and Rules provide that a person served with a summons, other than by personal delivery to him or to his agent for service, who does not appear, may be allowed to defend the action within one year after he obtains knowledge of the entry of judgment, provided that the Court finds that the person did not personally receive notice of the summons in time to defend, and has a meritorious defense.

Gun Hill and Sterling argued that despite Katan's affidavit, the evidence demonstrated that Columbia was duly served with the summons and complaint through the New York Secretary of State at the correct address of Columbia's agent for service of process, Katan. They also argued that Columbia did not have a meritorious defense to this action because Columbia's mortgage stated that it was a second position mortgage, and could not stop the foreclosure of the priority lienholders.

The Supreme Court explained that Katan did not deny that he was Columbia's duly appointed agent for service of process, or that the address for service of process on file with the Secretary of State was his current home address. Moreover, Katan did not expressly state that he failed to receive process, or that he did not sign the certified mailing receipt. Finally, while he said he returned from overseas in September 2007, he did not submit evidence to document that he was, in fact, not in the country on the date that process was served. Therefore, the Court found the evidence established that Columbia was properly served with process at the current and correct address on file with the Secretary of State and Katan, or someone on his behalf, actually received and signed for the summons and complaint on May 17, 2007. Thus, the Court found that Columbia personally received notice of the complaint in time to defend the action and struck down Columbia's motion to set aside the default judgment due to lack of service of process.

It is important to remember that service of process can be made in many ways. Should you receive notice in any form of the existence of court action to which you may have been made a party, you should consult with counsel to determine if service was effective and what steps you should take to protect your interests.

Case Cited: 1450 *Gun Hill Road LLC, et al. v. Capital Hill Partners, LLC, et al.*, No. 601510/2007 (N.Y. Sup. Ct. 01/16/08).

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Lenders should review their forms to make sure the actual signature line includes the word "seal," otherwise, the shorter statute of limitations period may apply.

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### We Would Like To Hear From You

We publish this newsletter as a service to our clients as a means to make them aware of certain aspects of the law. As always, we would like to hear feedback from our readers regarding the content

of the newsletter. If there are items or topics you would like to see covered in future issues, or you have a suggestion concerning the newsletter itself, you may send them to Bill Melchior at [wgmelchior@lercheearly.com](mailto:wgmelchior@lercheearly.com).

Additionally, a number of the Firm's other departments periodically issue highly informative newsletters on a variety of other subjects, including Real Estate, Community Associations, and Employment and Labor. If you would like to view one or more of these newsletters, you may access them through our website, [www.lercheearly.com](http://www.lercheearly.com).

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SUITE 460 | 3 BETHESDA METRO CENTER | BETHESDA MD 20814-5367

TEL: 301.986.1300 | [www.lercheearly.com](http://www.lercheearly.com)

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