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Warehouse Lines of Credit: Drafting Financing Agreements, Custodial Agreements, Reps and Warranties

Perfecting a Security Interest in Mortgage Loans, Analyzing Repurchase
Obligations, Bankruptcy Treatment Under Financing Agreements

WEDNESDAY, NOVEMBER 7, 2018

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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WAREHOUSE LENDING 2018

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- Overview
 - Warehouse lending is a specialized form of commercial credit provided to mortgage originators in the form a short-term credit facility to fund mortgage loans from the initial closing to sale in the secondary market.
 - Warehouse lenders include large commercial banks, community banks, investment banks and mortgage lenders. Many warehouse lenders utilize warehouse lines to drive production to their correspondent divisions.
 - In 2005 there were over 100 warehouse lenders in the U.S. By early 2010, that number had fallen to less than 30. Today's estimate is that there are over 150 warehouse lenders, primarily dominated by large banks (from an availability of credit perspective) and by community banks (from a number of lenders perspective).

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- Legal Agreement Structure—Principal Agreements
 - **Typical Structures**
 - Repurchase agreements
 - Purchase and sale agreements
 - Participation agreements
 - Traditional secured lines of credit.
 - **Market Practice.** Most major financial institutions use repurchase agreements, while many community banks and smaller lenders use a purchase and sale agreement or a participation agreement. Very few warehouse lenders presently use a secured line of credit.

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- Legal Agreement Structure—Principal Agreements – Repurchase Agreements
 - **Repurchase Agreement.** The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 amended the definition of “repurchase agreement” contained in the United States Bankruptcy Code (12 U.S.C. §101(47)) to include “an agreement...which provides for the transfer of one or more...mortgage loans...[or]...interests in mortgage loans...against the transfer of funds by the transferee of such...mortgage loans, or interests, with a simultaneous agreement by such transferee to transfer to the transferor thereof mortgage loans, or interests of the kind described in this clause, at a date certain not later than 1 year after such transfer or on demand, against the transfer of funds”.

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- Legal Agreement Structure—Principal Agreements—Repurchase Agreements
 - **Repurchase Agreements Not Subject to Automatic Stay in Bankruptcy.** Pursuant to Sections 362 and 559 of the Bankruptcy Code, mortgage loans held by a warehouse lender pursuant to a repurchase agreement are not subject to the automatic stay in bankruptcy and ipso facto clauses are enforceable. Properly drafted repurchase agreements are also treated as “securities contracts” for purposes of the Bankruptcy Code, providing further protections to the warehouse lender. Mr. Calandra will discuss this further in his portion of the presentation.

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- Legal Agreement Structure—Principal Agreements—Repurchase Agreements
 - As a result, most large warehouse lenders use a repurchase agreement to govern their warehouse lines.
 - Repurchase agreements are treated as sales for insolvency purposes and as loans for accounting and tax purposes, thus allowing warehouse lenders to have “the best of both worlds”.
 - Throughout the mortgage crisis, repurchase agreements were challenged by various mortgage originators, who argued that the commonly used forms of repurchase agreements did not meet the Bankruptcy Code requirements. Each of those cases resulted in victories for the warehouse lenders, with one minor exception discussed below relating to servicing rights.

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- Legal Agreement Structure—Principal Agreements—Purchase and Sale Agreement
 - **Purchase and Sale Agreement.** Many community banks utilize a “purchase and sale” agreement, otherwise known as a “true sale” agreement. Like a repurchase agreement, a warehouse lender using a purchase and sale agreement purchases the mortgage loans from the mortgage originator. However, purchase and sale agreements are structured so as to reflect a “true sale” for all purposes, with no obligation to repurchase the mortgage loans except upon the occurrence of an event of default following a breach of a representation and warranty. This allows the warehouse lender to treat each underlying mortgage loan as its loan for loan to one borrower (“LTOB”) and risk-based capital purposes. While structures vary widely, the mortgage originator generally “arranges” for a sale of the mortgage loan to an investor and is then paid “deferred purchase price” or a “fee” for its services.

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- Legal Agreement Structure—Principal Agreements—Purchase and Sale Agreement
 - **RESPA and Accounting Issues.** In recent years, regulators have raised substantial questions regarding the use of purchase and sale agreements for two different reasons. First, regulators argued that the “true sale” nature, combined with the warehouse lender providing closing funds “at the table”, was table funding for RESPA purposes. However, the industry was successful in getting HUD to agree that it is not table funding if a purchase and sale agreement treats failure to arrange a secondary market sale within a short period of time as a default that requires repurchase (thus creating an unconditional obligation to repurchase). While the industry initially viewed the HUD determination as a success, it created a second problem. If there is an absolute and unconditional obligation to repurchase, then how can the transactions be treated as true sales? In late 2012, the OCC became the first regulator to direct those it regulates to treat purchase and sale agreements used for warehouse lending purposes as loans rather than as true sales. The state of accounting for purchase and sale agreements used for warehouse lending purposes remains in flux, though the OCC has recently begun asking the FDIC to take a closer look at the issue. In addition, there is no certainty that the CFPB will agree with the guidance provided by HUD on these issues.

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- Legal Agreement Structure—Principal Agreements—Purchase and Sale Agreement
 - Because there is no obligation on the part of the mortgage originator to repurchase mortgage loans within one year, purchase and sale agreements do not meet the requirements for treatment as “repurchase agreements” and thus are not entitled to insolvency protection.
 - Purchase and sale agreements also generally do not contain a prophylactic security interest grant, thus further exposing the warehouse lender.
 - Lastly, while some in the industry argue that purchase and sale agreements have held up in bankruptcy court, to our knowledge no bankruptcy case has directly addressed the issue since the 2005 amendments to the Bankruptcy Code.

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- Legal Agreement Structure—Principal Agreements—Participation Agreement
 - **Participation Agreement.** A participation agreement is a variation of a purchase and sale agreement in which the warehouse lender purchases a “participation” in originated mortgage loans. Like purchase and sale agreements, participation agreements do not qualify as “repurchase agreements” and generally do not contain prophylactic security interest grants. However, participation agreements generally receive favorable LTOB and risk-based capital treatment.

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- Legal Agreement Structure—Principal Agreements—Secured Line of Credit
 - **Secured Line of Credit.** A secured line of credit is essentially the same as any other secured credit facility except that it is secured by mortgage loans. Secured lines of credit were once the principal warehouse lending structure, but they have been largely supplanted among major lenders by repurchase agreement structures. A secured line of credit does not meet “repurchase agreement” requirements because there is no sale. As a result, a secured line of credit is subject to the automatic stay in bankruptcy and is treated as a loan for LTOB and risk-based capital purposes.

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- Legal Agreement Structure—Ancillary Agreements
 - **Pricing Side Letter.** Because most warehouse lenders view pricing, advances rates, financial covenants and other terms as proprietary, industry practice is to put such terms in a side letter that is not filed publicly or otherwise disclosed by those required to make public disclosures. Note that there is no legal basis for this practice—because the terms in the side letter are generally material, the proper method for avoiding filing would be to utilize a confidential treatment request. However, no warehouse lender or mortgage originator actually does so.

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- Legal Agreement Structure—Ancillary Agreements
 - **Electronic Tracking Agreement.** This is an agreement among MERS, the warehouse lender and the mortgage originator. The agreement provides that MERS will take direction from the warehouse lender and change the registration to the warehouse lender's name following the occurrence of an event of default. Note that there are two designations for warehouse lenders at MERS—“interim funder” and “warehouse lender”. Our view is that warehouse lenders should always choose “interim funder” because that designation gives the warehouse lender broader control and consent rights.

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- Legal Agreement Structure—Ancillary Agreements
 - **Guaranty.** Requirements vary, but most warehouse lenders require major shareholders of non-public companies to guaranty obligations.
 - **Custodial Agreement.** If the warehouse lender is not going to serve as document custodian, the warehouse lender and the mortgage originator must have a document custodian. The custodial agreement allows the warehouse lender to maintain “possession” of the mortgage note for perfection purposes while utilizing a third-party custodian to check in and hold collateral documents.
 - **Servicing Agreement.** Often, the originator will continue to service the mortgage loans that are subject to the warehouse facility. If there is a third party servicer engaged to service the mortgage loans, then the warehouse lender should review the underlying Servicing Agreement and enter into a letter agreement with such servicer acknowledging the warehouse lender’s rights in the underlying mortgage loans.

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- Legal Agreement Structure—Ancillary Agreements
 - **Bailee Letter.** Mortgage loans are delivered to investors along with a bailee letter providing that the investor is holding the mortgage loans on behalf of the warehouse lender. Bailee letters generally provide wire information, require the investor to purchase the mortgage loans or return them within a specified period of time and require that the investor return the mortgage loans and related notes only to the warehouse lender or the custodian. Bailee letters are generally self-effectuating.
 - **Master Netting Agreement.** An agreement between the warehouse lender and the mortgage originator providing for netting across various agreements between the parties. Some lenders simply include a provision in their repurchase agreement providing that the repurchase agreement itself is a netting agreement.
 - **Deposit/Securities Account Control Agreements.** Required if deposit/securities accounts are held other than at warehouse lender.
 - **A word about eMortgages.**

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- Primary Terms of Warehouse Facilities
 - Committed versus uncommitted facility
 - Eligible mortgage loans
 - Advance rates/haircut
 - Non-use fee
 - Determination of market value
 - Aging
 - Prophylactic security interest
 - Margin maintenance
 - Compare ratios
 - Indemnity provisions
 - Representations, warranties and covenants

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- Risks and Legal Issues
 - **Fraud.** The single biggest risk to any warehouse lender is fraud, either in the origination or in the secondary market sale of mortgage loans through double-pledging or double-sale of mortgage loans. Warehouse lenders can mitigate those risks by:
 - Following established processes for wet and dry loans. As competition has increased, warehouse lenders have become increasingly willing to loosen requirements for delivery of collateral.
 - **Dry Loans.** The proper method of perfecting collateral for dry loans is that the warehouse lender should be in possession of the mortgage note prior to funding.
 - **Wet Loans.** The proper method of perfecting collateral for wet loans is that the closing agent should be instructed pursuant to a closing letter to deliver the original mortgage note directly to the warehouse lender. The warehouse lender should also receive a copy of the closing documents prior to funding.

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- Risks and Legal Issues
 - In practice, however, warehouse lenders frequently allow dry fundings to occur without physical possession of the mortgage note and they allow wet funding closing agents to deliver mortgage notes to the mortgage originator for “review”. While the UCC does provide some protection to warehouse lenders in a dry funding (because the warehouse lender is automatically perfected for 20 days even if not in possession of the collateral), in a wet funding scenario the closing letter provides that the closing agent is holding the mortgage note for the warehouse lender, thus perfecting the interest. Allowing the mortgage note to then return to the possession of the mortgage originator “un-perfects” the warehouse lender’s security interest and the warehouse lender is thus not perfected until it regains possession of the mortgage note.

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- Risks and Legal Issues
 - **Enabling/Aiding and Abetting.** While warehouse lenders have generally not been required to account for the activities of mortgage originators, the Lehman case in Orange County, California proved that there is a limit to immunity. Lehman provided a warehouse line to a mortgage originator that was engaged in various wrongful acts. Internal e-mails showed that Lehman was aware of—and even joked about—those wrongful acts. The court held that by continuing to provide a warehouse line to the mortgage originator even after it became aware of the wrongful acts, Lehman enabled the wrongful activities and thus bore some responsibility, resulting in a multi-million dollar judgment against Lehman.

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- Initiation of a Transaction
 - Conditions Precedent
 - Facility Documents executed
 - Delivery of Assets
 - Due Diligence Complete
 - No Default/Compliance with representations and warranties
 - No Material Adverse Change
 - Maximum Purchase Price, Minimum Purchase Price on a Purchase Date
 - Transaction Request
 - Trust Receipt
 - Confirmation
 - Opinions
 - Most warehouse facilities require the mortgage originator's counsel to issue a legal opinion. Some warehouse lenders require an opinion that a master repurchase agreement is a "repurchase agreement", "securities contract" and "master netting agreement" as defined in the Bankruptcy Code. These opinions can be costly for originators to obtain, and many smaller originators tend to object to this request. Common industry practice is to allow outside counsel to give enforceability, perfection and no violation of law opinions and to allow in-house counsel to render more "fact-based" opinions, such as due formation, due authorization and no material litigation.
 - Organizational Documents
 - Insurance

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- Cash Flow Mechanics
 - Payment of Purchase Price
 - Payments to Warehouse Lender – Monthly and Upon Repurchase
 - Price Differential
 - Prior to Event of Default: A rate of interest equal to an adjustable rate (typically One-Month LIBOR) plus a pricing spread.
 - After an Event of Default: Post-Default Rate - this is typically a much higher rate.
 - A note about LIBOR.
 - Amortization payments toward Repurchase Price.
 - Repurchase Price
 - Typically equal to the Purchase Price, plus all accrued and unpaid Price Differential, minus all amounts previously applied or credited to the Repurchase Price.
 - Income from Purchased Assets
 - Cash may be deposited in Collection Account which is in Buyer's name or over which Buyer has a first priority security interest under a Control Agreement.
 - Depending on business agreement, income may be applied toward payment of Price Differential, Repurchase Price and other costs, expenses and fees. Often, excess cash is remitted to Seller.

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- Margin Maintenance
 - The Buyer will purchase the Purchased Assets at a discount - i.e., the Buyer will pay 65 cents (or some other amount) for each dollar of Market Value of the Purchased Assets. This idea is expressed in various ways in term sheets and repurchase agreements, depending on how the internal systems are established to track the concept. Using the example of 65 cents on the dollar:
 - Purchase Price Percentage = 65%
 - Haircut = 35%
 - The Buyer will require that the ratio of the amount of this discount in the Purchase Price to the Market Value of the Purchased Assets is maintained by the Seller throughout the course of the transaction. Usually this is done by determining a minimum Market Value of Purchased Assets necessary to maintain such discount, which is typically referred to as the Buyer's Margin Amount.
 - Typically the Market Value of the Purchased Assets is determined by the Buyer in its sole discretion, although various valuation schemes can be used depending on the business agreement
 - Sometimes counterparties negotiate a Threshold Amount before which a Margin Call can be made
 - Margin Excess

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- Margin Maintenance (con't)
 - The Market Value of the Purchased Assets may vary for a number of reasons during the course of a Transaction:
 - Market movements
 - Interest rate movements
 - The zero valuing of the Purchased Assets pursuant to the definition of Market Value.
 - Typically, the Market Value of a Purchased Asset may be deemed to be zero by the Buyer if certain events occur:
 - A violation of an asset-level representation and warranty.
 - The Purchased Asset violates a concentration limit.
 - The Purchased Asset remains subject of a Transaction for longer than the maximum period permitted.
 - The Purchased Asset is released from the possession of the Custodian for an unacceptable period of time.
 - The Purchased Asset is unacceptable because it is delinquent or in default.

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- Margin Maintenance (con't)
 - If the value of the Purchased Assets falls such that the Market Value of the Purchased Assets multiplied by the Purchase Price Percentage is less than the Repurchase Price (such shortfall is called a Margin Deficit), the Buyer delivers a Margin Call to the Seller.
 - Failure to cure a Margin Deficit within the required period of time (which may vary, but typically is within one Business Day) will be an Event of Default unless the Margin Deficit is cured by the Seller.
- Curing a Margin Deficit
 - Repay Purchase Price in whole or in part
 - Deliver additional Purchased Assets or additional cash to be held as Purchased Assets

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- Security Interest
 - In order to make sure that the Buyer has rights in the Purchased Assets, the Buyer takes a grant of security interest in the Purchased Assets:
 - Mortgage Loan Documents
 - Mortgage Notes, indorsed “in blank”
 - Mortgages
 - Assignments of Mortgage
 - Intervening assignments and assignment “in blank”
 - Title Policies
 - Consolidation, extension, modification or assumption agreements
 - Powers of attorney
 - Servicing Rights
 - Rights to service, administer and/or collect on the Purchased Assets and the payment of any ancillary income with respect thereto
 - Income on Purchased Assets
 - Typically in the form of payments on the underlying Mortgage Notes
 - Other contractual rights and general intangible with respect to the Purchased Assets

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- Security Interest (con't)
 - Elements of Establishing a Valid Security Interest
 - Creation – grant of a security interest
 - Attachment (NY UCC § 9-203(b))
 - Value has been given by the Buyer
 - The grantor has rights in the collateral or the power to transfer rights in the collateral to the lender
 - The grantor has authenticated a security agreement that provides a description of the collateral

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- Security Interest (con't)
 - Perfection
 - Possession (Actual or Constructive)
 - Mortgage Notes are “instruments” (NY UCC § 9-102(a)(47) and Buyer perfects by taking possession (NY UCC § 9-313-(a))
 - Indorsement in “in blank” is important – if an indorsement is made by the holder of an instrument and it is not a special indorsement, it is a "blank indorsement." When indorsed in blank, an instrument becomes payable to bearer and may be negotiated by transfer of possession alone until specially indorsed (NY UCC § 3-205(b).
 - Constructive control through Custodian who authenticates a record acknowledging that it holds for the collateral for the Buyer’s benefit (NY UCC § 9-313(c)).
 - Filing
 - Cannot perfect in a “deposit account” or “letter-of-credit rights” through filing
 - UCC Financing Statement is filed to perfect a security interest in:
 - Servicing Rights
 - General Intangibles
 - Contractual Rights with respect to Purchased Asset
 - Other records in the Custodial or Servicing File
 - Authorization – A person may file an initial financing statement, amendment that adds collateral covered by a financing statement, or amendment that adds a debtor to a financing statement only if it is authorized under NY UCC § 9-509
 - UCC Searches
 - Priority Issues
 - Terminations

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- Security Interest (con't)
 - Perfection (con't)
 - Control
 - Buyer perfects in income related to the Purchased Assets by establishing a “deposit account”, requiring such income to be remitted to the deposit account and obtaining control under NY UCC § 9-104(a):
 - Buyer is a bank with which the deposit account is maintained;
 - The Buyer, the Seller and a bank have agreed in an authenticated record (typically in the form of a deposit account control agreement) that the bank will comply with instructions originated by the secured party directing disposition of the funds in the deposit account without further consent by the debtor
 - the secured party becomes the bank's customer with respect to the deposit account;
 - the name on the deposit account is the name of the secured party or indicates that the secured party has a security interest in the deposit account; or
 - another person has control of the deposit account on behalf of the secured party or, having previously acquired control of the deposit account, acknowledges that it has control on behalf of the secured party.

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- Bankruptcy Code Safe Harbors
 - General Bankruptcy Rules
 - Automatic stay generally prevents creditors from enforcing pre-petition contracts and exercising rights and remedies against the (Bankruptcy Code § 362)
 - *Ipsa Facto* clauses with respect to executory contracts are unenforceable (Bankruptcy Code § 365(e)(1)):
 - **(e)(1)** Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on—
 - **(A)** the insolvency or financial condition of the debtor at any time before the closing of the case;
 - **(B)** the commencement of a case under this title; or
 - **(C)** the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.
 - Safe Harbors Allow Creditors to Circumvent the General Rules

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- Bankruptcy Code Safe Harbors (con't)
 - Repurchase Agreement Safe Harbor (Bankruptcy Code § 559)
 - The exercise of a contractual right of a repo participant or financial participant to cause the liquidation, termination, or acceleration of a repurchase agreement because of a condition of the kind specified in section 365(e)(1) of this title shall not be stayed, avoided, or otherwise limited by operation of any provision of this title or by order of a court or administrative agency in any proceeding under this title, unless, where the debtor is a stockbroker or securities clearing agency, such order is authorized under the provisions of the Securities Investor Protection Act of 1970 or any statute administered by the Securities and Exchange Commission.

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- Bankruptcy Code Safe Harbors (con't)
 - What Qualifies?
 - The term “repurchase agreement” —
 - (A) means—
 - **(i) an agreement**, including related terms, **which provides for the transfer of one or more** certificates of deposit, mortgage related securities (as defined in section 3 of the Securities Exchange Act of 1934), **mortgage loans**, interests in mortgage related securities or mortgage loans, eligible bankers' acceptances, qualified foreign government securities (defined as a security that is a direct obligation of, or that is fully guaranteed by, the central government of a member of the Organization for Economic Cooperation and Development), or securities that are direct obligations of, or that are fully guaranteed by, the United States or any agency of the United States **against the transfer of funds by the transferee of such** certificates of deposit, eligible bankers' acceptances, securities, **mortgage loans**, or interests, **with a simultaneous agreement by such transferee to transfer to the transferor thereof** certificates of deposit, eligible bankers' acceptance, securities, **mortgage loans**, or interests of the kind described in this clause, **at a date certain not later than 1 year after such transfer or on demand, against the transfer of funds;**
 - **(ii)** any combination of agreements or transactions referred to in clauses (i) and (iii);
 - **(iii)** an option to enter into an agreement or transaction referred to in clause (i) or (ii);
 - **(iv)** a master agreement that provides for an agreement or transaction referred to in clause (i), (ii), or (iii), together with all supplements to any such master agreement, without regard to whether such master agreement provides for an agreement or transaction that is not a repurchase agreement under this paragraph, except that such master agreement shall be considered to be a repurchase agreement under this paragraph only with respect to each agreement or transaction under the master agreement that is referred to in clause (i), (ii), or (iii); or
 - **(v) any security agreement or arrangement or other credit enhancement related to any agreement or transaction referred to in clause (i), (ii), (iii), or (iv), including any guarantee or reimbursement obligation by or to a repo participant or financial participant in connection with any agreement or transaction referred to in any such clause**, but not to exceed the damages in connection with any such agreement or transaction, measured in accordance with section 562 of this title; and
 - **(B)** does not include a repurchase obligation under a participation in a commercial mortgage loan. (Bankruptcy Code § 101(47)).

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- Bankruptcy Code Safe Harbors (con't)
 - Who can exercise contractual rights?
 - A “repo participant” – an entity that, at any time before the filing of the petition, has an outstanding repurchase agreement with the debtor. (Bankruptcy Code § 101(46)).
 - A “financial participant” – an entity that at the time it enters into a securities contract, repurchase agreement, swap agreement, forward contract *or* at the time of the date of the filing of the petition has one or more agreements or transactions that are the foregoing (including master netting agreements) with persons other than affiliates with a total gross dollar value of not less than \$1 billion in notional *or* actual principal amount outstanding *or* has gross mark to market positions of not less than \$100 million (across counterparties) *on any day* during the prior 15-month period (Bankruptcy Code § 101(22A)).

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- Bankruptcy Code Safe Harbors (con't)
 - Securities Contract Safe Harbor (Bankruptcy Code § 555)
 - The exercise of a contractual right of a stockbroker, financial institution, financial participant, or securities clearing agency to cause the liquidation, termination, or acceleration of a securities contract, as defined in section 741 of this title, because of a condition of the kind specified in section 365(e)(1) of this title shall not be stayed, avoided, or otherwise limited by operation of any provision of this title or by order of a court or administrative agency in any proceeding under this title unless such order is authorized under the provisions of the Securities Investor Protection Act of 1970 or any statute administered by the Securities and Exchange Commission. As used in this section, the term “contractual right” includes a right set forth in a rule or bylaw of a derivatives clearing organization (as defined in the Commodity Exchange Act), a multilateral clearing organization (as defined in the Federal Deposit Insurance Corporation Improvement Act of 1991), a national securities exchange, a national securities association, a securities clearing agency, a contract market designated under the Commodity Exchange Act, a derivatives transaction execution facility registered under the Commodity Exchange Act, or a board of trade (as defined in the Commodity Exchange Act), or in a resolution of the governing board thereof, and a right, whether or not in writing, arising under common law, under law merchant, or by reason of normal business practice.

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- Bankruptcy Code Safe Harbors (con't)
 - What Qualifies?
 - A “securities contract” is a contract for the purchase, sale or loan of a security, mortgage loan or interest in a mortgage loan, including any repurchase or reverse repurchase transaction on any security, mortgage loan or interest therein and any combination of the agreements or transactions referred to herein. (Bankruptcy Code § 741(7)).

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- Bankruptcy Code Safe Harbors (con't)
 - Who can exercise contractual rights?
 - A “financial participant”
 - A “financial institution” is a Federal reserve bank, or a foreign or domestic commercial savings bank, industrial savings bank, savings and loan association, trust company, federally-insured credit union (Bankruptcy Code § 101(22))
 - Stockbrokers (Bankruptcy Code § 101(53A))
 - Securities clearing agencies (Bankruptcy Code § 101(48))

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- Bankruptcy Code Safe Harbors (con't)
 - Master Netting Agreement (Bankruptcy Code § 561)
 - The exercise of a contractual right because of a condition of the kind specified in section 365(e)(1) to cause the termination, liquidation, or acceleration of **or to offset or net termination values, payment amounts, or other transfer obligations arising under or in connection with one or more (or the termination, liquidation, or acceleration of one or more) [safe harbored] contracts** shall not be stayed, avoided, or otherwise limited by operation of any provision of this title or by any order of a court or administrative agency in any proceeding under this title.

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- Bankruptcy Code Safe Harbors (con't)
 - What Qualifies?
 - A “master netting agreement” is an agreement providing for the exercise of rights, including rights of netting, setoff, liquidation, termination, acceleration, or close out, under or in connection with one or more [safe harbored] contracts, or any security agreement or arrangement or other credit enhancement related to one or more of the foregoing, including any guarantee or reimbursement obligation related to 1 or more of the foregoing.
 - Who can exercise contractual rights?
 - Any person exercising contractual rights in the underlying safe harbored contract

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- Bankruptcy Code Safe Harbors (con't)
 - *In re American Home Mortg., Inc.* (Bankr. D. Del. 2008, 379 B.R. 503)
 - First notable case litigated in connection with “safe harbors” after they were enhanced in the Bankruptcy Abuse and Prevention and Consumer Protection Act of 2005
 - Upheld the safe harbors
 - UCC did not apply to remedies under a repurchase agreement
 - Identified Servicing Rights as a separate asset the court would not compel the debtor to release. As a result, while the court held that the warehouse lender could exercise its rights to sell the mortgage loans that it purchased under a repurchase agreement, by allowing the mortgage originator to retain the servicing rights the warehouse lender only had the right to sell the mortgage loans servicing retained
 - Most repurchase agreements treat the Servicing Rights as a separate asset
 - Identify the originator/seller as a subservicer, with a servicing term that automatically terminates every 30 days unless extended
 - “Servicing Rights” as other credit enhancement related to a “safe harbored” agreement

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