



Points of Interest

A Publication of the California Mortgage Association

Fall 2015

**Perspectives From the Battlefield:
The Down and Dirty of Laundry Leases**

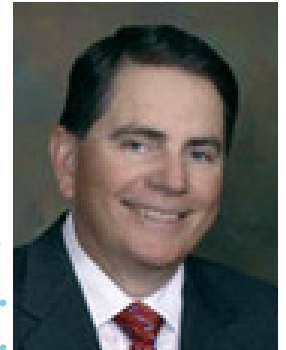
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Personal Property Liens: How Such Liens May Impact Your Business Activities



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Lien Issues in Personal Property Purchases

One must be careful in dealing with personal property purchases or personal property security.¹ We are so accustomed to dealing with real property loans and purchases in our business and relying just on preliminary reports that we sometimes forget the impact of liens regarding personal property that may be involved either in the same real estate transaction or in an independent personal property transaction.

For example, let us assume you purchase existing servicing rights to a loan portfolio from a loan broker who is retiring. This is not a usual everyday transaction in which brokers engage. In other words, it is not part of your traditional business model. The “ins and outs” of such a transaction may not be familiar.

To accomplish one’s goal of a successful transaction, one must first obtain a clearly drafted and well thought-out purchase agreement, including possible buy-backs of bad loans under certain circumstances. A thorough vetting of the loans purchased is mandatory. Once an agreement is signed, and notice is ready

to go out to the lenders and borrower(s), are you ready to go? Should the purchase price simply be paid? Was the possibility of a lien (either voluntary or involuntary), against the broker’s interest in the portfolio considered? Perhaps not. If not, it must be. The servicing rights to the loan portfolio are personal property; they can be lien.

What liens could exist against the personal property being purchased?

There are two types of liens which could exist against the broker’s personal property: (1) voluntary, or (2) involuntary.

A voluntary lien would exist, for example, where the broker used the loan portfolio income as security for a bank loan. Such a loan would traditionally be well-documented. Thus, a search of the California Secretary of State’s Uniform Commercial Code register of liens is mandatory. That is easily accomplished.

An involuntary lien exists when the debtor did not consent to its making. We all know what these are. But, we do not always think of the possibility that such a lien may exist in the out-of-the-ordinary transaction. Examples of involuntary liens are local, state and federal tax liens, judgment liens,

equitable liens, mechanic’s liens (real property only), design professional liens and artisan’s liens. There are other, more exotic, liens such as a “thresher’s lien” or an “animal breeder’s lien.” (Not too pertinent here. But they do exist. Some are so-called “hidden liens”).

The “perfection”² of different liens can take different paths. Some liens are perfected by possession (such as possession of the original promissory note); others are perfected by filing documentation with the Secretary of State (a Uniform Commercial Code filing, or UCC-1). Sometimes, there is more than one way to perfect the security interest. To determine where one must look for the type of lien being protected against, one must determine how the lien is perfected. Perfection methods are established by the California Uniform Commercial Code.

Federal liens are governed by the United States Code and state law. The Uniform Federal Lien Registration Act (California Code of Civil Procedure, section 2100 et seq.) governs how federal liens are perfected in California. Usually, again, filing with the Secretary of State for

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personal property, but also with the county recorder for real property interests are the appropriate methods.

Most voluntary and involuntary personal property liens about which the average businessperson should have concerns will show up in a UCC search with the Secretary of State.³ In our example, if a security interest were granted in the servicing rights to the loan portfolio sought to be purchased, it must be properly perfected by the filing of a UCC-1. Failure to do so will render the lien invalid as to any bona fide third-party purchaser or encumbrancer of the servicing rights. Note: Actual knowledge of a lien will defeat one's rights as a bona fide purchaser, even if a search of the UCC system has not occurred and even if a UCC-1 financing statement has not been made.

Accordingly, before concluding the purchase of any personal property, such as servicing rights, find out what third party interests exist in the personal property. Do a UCC search. (It is possible to get UCC

lien insurance, similar to a policy of title insurance.) Then, contact the holder of the lien to arrange for a payoff of the lien from the purchase price proceeds.

Consequences of Failing to Pay an Existing Lien

What are the consequences of failing to pay a valid perfected personal property lienholder when purchasing personal property from a debtor/seller? The lien remains with the property and is fully enforceable. In other words, the lienholder can ignore the fact that the purchaser has already paid the seller of the personal property (in our example, the servicing rights to the loan portfolio) and can enforce the lien through foreclosure up to the amount of the debt, which is obviously undesirable.

Conclusion

Transactions which do not occur often in one's business require close attention. When undertaking a transaction out of the

ordinary, good legal advice is invaluable. Third-party interests in personal property can be devastating if ignored and can result in the destruction of proposed transaction's entire economic viability. Buyer beware! ☹

Endnotes

- 1 It is beyond the ken of this article to discuss licensing requirements for personal property loans. However, the scope of one's license must always be considered when making other than purely real property loans.
- 2 "Perfection" is the method of protecting the lien's interest against third party claims, similar to the "perfection" that occurs by recording a deed of trust against real property.
- 3 A significant exception to this would be the perfection of a security interest in a "deposit account" by the obtaining of a "deposit account control agreement." Thus, if one is seeking to secure a debt with a bank account, make certain that it is not already secured. Inquiry of the bank holding the account should accomplish this goal.

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