



Signed and Filed: September 28, 2015

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DENNIS MONTALI
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

| | | |
|----------------------|---|----------------------------|
| In re |) | Bankruptcy Case |
| |) | No. 13-32456DM |
| ARCE RIVERSIDE, LLC, |) | |
| |) | |
| |) | Debtor. |
| |) | Chapter 11 |
| |) | (Jointly Administered with |
| In re |) | Case No. 13-32457) |
| |) | |
| KERA RIVERSIDE, LLC, |) | |
| |) | |
| |) | Debtor. |
| |) | |

MEMORANDUM DECISION ON OBJECTION TO SECOND AMENDED CLAIM

I. INTRODUCTION

On September 1st and 2nd, 2015, the court conducted a trial on the Debtors' Objection to the Second Amended Claim of Penn Equities, LLC, ("Penn"), and on September 3rd the court heard closing argument from counsel for the parties. At that point the matter was submitted for decision. The court then asked for further briefing on a discrete question, discussed, *infra*.

As explained below, the court will sustain the objection and enter an order disallowing the interest paid and ordering it repaid to Debtors (subject to possible offset); it will not award treble damages. Based upon this result, the court determines that

1 the prevailing parties, Debtors, are entitled to an award of
2 attorneys fees and costs, which should be the subject of a
3 separate motion.

4 II. FACTS¹

5 George Arce ("Arce") is the managing member of Debtor, Arce
6 Riverside, LLC. He is a California licensed real estate broker
7 and salesperson. Neil Wachsberger ("Wachsberger") is the managing
8 member of Debtor, Kera Riverside, LLC. He is also a California
9 licensed real estate broker. Arce Riverside, LLC and Kera
10 Riverside, LLC at all material times owned real estate in
11 Riverside, California ("the Property").

12 In 2007 Debtors borrowed \$3.5 million on a Promissory Note
13 (the "CIBC Note") (Exhibit B) from CIBC Inc., ("CIBC)", a bank
14 affiliate that was then the holder of a California commercial
15 finance lenders license. No evidence suggested that Arce acted as
16 the broker for this loan, nor on Debtors' 2004 acquisition of the
17 Property.

18 The CIBC Note contains in Paragraph 5, Default and
19 Acceleration, a prevailing party's attorney fee provision that the
20 parties agree is applicable to the outcome of the present dispute.
21 An unnumbered paragraph, Applicable Law; Jurisdiction, provides a
22 choice of law, namely the state in which the Property is located.
23 Thus California law applies.

24 The CIBC Note was secured by a first deed of trust on the
25 Property. It was modified in 2009 at a time when the principal
26 balance was slightly more than \$2.4 million.

27 ¹ The following discussion constitutes the court's findings
28 of fact and conclusions of law. Fed. R. Bankr. P. 7052(a).

1 The CIBC Note had matured by August 2010, although CIBC did
2 not declare a default, institute foreclosure, or apply a default
3 rate of interest. This situation was reflected in several written
4 communications between CIBC and Debtors (Exhibits L, M & N).
5 Debtors continued to make interest-only payments on the CIBC Note
6 at approximately four percent.

7 Prior to February 14, 2011, Arce negotiated a letter of
8 intent with a prospective lessee of the Property, Crunch Fitness
9 ("Crunch"). Because Wachsberger had a prior working relationship
10 with Hank Dayani, Arce called upon him to discuss with Hank Dayani
11 a prospective \$350,000 loan to Debtors to finance tenant
12 improvements at the Property in anticipation of Crunch becoming
13 the lessee. Wachsberger drafted a letter of intent to that effect
14 for Luxor Properties, Inc. to submit to Debtors.

15 Hank Dayani discussed Wachsberger's request with his brother,
16 H. Sean Dayani ("Dayani", and together with Hank Dayani, the
17 "Dayani brothers"). The Dayani brothers are co-owners of several
18 entities including Luxor Properties, Inc. and Dayco Funding
19 Corporation ("Dayco"), a California licensed real estate broker.
20 They each own 50 percent of the shares of Dayco. They also each
21 have a 25 percent membership interest in Penn; the remaining 50
22 percent is owned by Don R. Hankey ("Hankey"). At the time of the
23 preliminary discussions and later at the time of the loan
24 modification, discussed *infra*, Penn did not have a California
25 finance lenders license or a California real estate brokers
26 license.

27 On April 20, 2011, Dayani, on behalf of Dayco, as a
28 principal, approached CIBC with an offer to purchase the CIBC

1 Note. Dayani drafted the initial proposal; Arce suggested changes
2 including an increase in Dayco's proposed purchase price from
3 \$2,000,000 to \$2,100,000. (Exhibit T(A)-1). When he agreed to
4 some of Arce's suggested changes, Dayani wrote to Arce:

5 Ok, dayco (sic) is buying the loan, correct?? So, from
6 now on, dayco (sic) is in charge what is buying and how
7 it goes about it. ok?? Since I can not spend more time
8 on this, I will go along with this but sorry, from now
9 on I have to deal with the lender and you will be
10 informed as to my progress but how the deal gets done is
11 my business. You will know about the purchase price and
12 timing. In terms of how we will modify the loan, you
13 have every right to get a term sheet and approve it and
14 your attorneys will have the right to take a look at the
15 loan modification docs and comment.

16 (Exhibit T-1)(Emphasis added).

17 On April 29, 2011, the Dayani brothers, Arce and Wachsberger
18 met and discussed what the parties have called the Three Options
19 Memo (Exhibit W). The three options proposed in that memo were:

- 20 1. a loan by Dayco to Debtors in the amount of \$2 million;
- 21 2. a loan by Dayco to Debtors in the amount of \$400,000 for
22 tenant improvements, secured by a second deed of trust on the
23 Property;
- 24 3. Dayco and/or its investor affiliate Penn would purchase
25 the CIBC Note and modify it to provide for a reduced principal
26 balance of \$2.31 million at an interest rate of 12 percent for a
27 term of one year with no prepayment penalty. Arce and Wachsberger
28 would guarantee the modified note.

29 The second option was a variation on the earlier proposal
30 drafted for Luxor Properties, Inc. The third option, setting
31 forth what later became the basis of the modification of the CIBC
32 Note when it was acquired by Penn, was proposed by Dayco. At the
33 time of that proposal it was not engaged to act as a broker for
34 Penn nor was it acting for Penn. In fact, there was no discussion
35 about Penn or about Dayco, Dayani, Arce or Wachsberger acting as a
36 broker in any capacity. Dayani knew that Arce and Wachsberger

1 were acting as principals.

2 A few days after the meeting, Arce sent an email to the
3 Dayani brothers, stating that "[Wachsberger] and I have made the
4 decision to go with option 3." He did not express any choice
5 between Dayco or Penn to purchase the CIBC Note and to modify it.
6 Thus, the choice was entirely up to Dayco. That was the last time
7 Debtors had anything approaching a negotiation about the critical
8 elements of forbearance, namely the extension of the maturity date
9 of the CIBC Note and the increase of the interest to twelve
10 percent.

11 Dayani testified that he was planning for Dayco to act as
12 Penn's agent, but there is no evidence that it actually did so.
13 In fact, Dayco did not file with the California Department of Real
14 Estate or deliver to Penn any of the documents required of a
15 broker acting in such a capacity. Dayani's self-serving testimony
16 that he did not need to report anything to himself is consistent
17 with Debtors' contentions and the court's determination that it
18 was not acting as Penn's broker or agent at all.

19 Penn offered into evidence an Agreement Regarding Loan
20 Purchase, Placement of Modification and Servicing (the "Broker
21 Agreement") (Exhibit Y), dated as of June 1, 2011.² The Broker
22 Agreement was signed by both Dayani brothers, on behalf of Dayco
23 and Penn, and Hankey, Penn's other member. Among the recitals was

24
25 ² Debtors argued strenuously that the Broker Agreement was
26 fabricated after-the-fact to provide a defense to their usury
27 claim. But all Debtors have is inference and innuendo, and the
28 testimony of Hankey who could not recall such an agreement ever
being entered into before. That is not enough for the court to
find any date of execution other than June 1, 2011, but based upon
the court's decision, the date is not pertinent.

1 a statement that Dayco had already informed CIBC and Debtors that
2 Penn would purchase that CIBC Note. That recital was untrue.
3 There is no evidence that CIBC or Debtors were aware of that
4 intention until September, 2011. Further, there is no evidence
5 that as of June 1, 2011, Dayco had been negotiating on behalf of
6 anyone other than itself.

7 Penn uses the Broker Agreement to establish that Dayco was
8 engaged as the licensed broker for Penn as principal. If so, as
9 discussed, *infra*, the modification of the CIBC Note would be
10 exempt from the usury laws. To further bolster its case, Penn
11 points to Paragraphs 3 and 4 of the Broker Agreement, wherein it
12 contends that Dayco has become entitled to \$50,000 as a fee for
13 its services as the loan broker. Those two paragraphs provide as
14 follows:

- 15 3. Beside the benefits which [the Dayani brothers]
16 will receive from Penn as members of Penn and the
17 only two (2) shareholders of Dayco, Dayco shall be
18 entitled to receive the sum of \$50,000.00 from Penn
when the Loan is fully paid off. Penn shall also
reimburse Dayco fully for all of its expenses
related to the modification;
- 19 4. In the event Penn is forced to foreclosure (sic)
20 upon the Property, then Dayco shall be entitled to
21 the following compensation: (I) if the Property is
22 sold at the trustee's sale to a successful bidder,
23 then Dayco shall be entitled to \$50,000.00 from the
24 proceeds, (ii) if the Property is reverted back to
25 Penn, then Dayco and Penn shall enter into a
26 separate Asset Management Agreement, in which Dayco
27 shall manage the Property, market the Property and
eventually sell the Property. Regardless of the
management fee negotiated by the parties, Dayco
shall be entitled to receive the sum of \$50,000.00
from the net sale proceeds, regardless of the
selling price.

28 Since there never was a foreclosure sale of the Property,

1 paragraph 4 is not applicable, and the only source of Dayco's
2 compensation is paragraph 3.

3 In Recital E of the Broker Agreement, the parties state that
4 Dayco shall continue to negotiate with CIBC

5 "and at the same time discuss modification terms and
6 conditions with [Debtors] on behalf of Penn and upon the
7 purchase of the [CIBC Note], negotiate, finalize and
8 place the modification on behalf of Penn ..."

9 The first paragraph setting forth the parties' agreement
10 tracks the same language quoted above.

11 Presumably these recitals described what Dayco would do "on
12 behalf of Penn" and for which it would have an expectation of
13 compensation under paragraph 3.

14 On August 16, 2011, Dayco and CIBC entered into a Loan Sale
15 Agreement (Exhibit BB). That agreement contemplated that Dayco
16 would purchase the CIBC Note from CIBC as of August 31, 2011, and
17 included as exhibits several documents the parties intended to
18 sign at the closing of the loan purchase. There is nothing in
19 that agreement about Penn.

20 In fact, Section 3.05, entitled "No Broker" states that Dayco
21 nor any of its affiliates has dealt with, or engaged on its own
22 behalf or for its benefit, any broker, agent or dealer entitled to
23 a commission or a fee. And Section 7.05(a) states that the
24 parties to the agreement are the sole and exclusive beneficiaries
25 of it. Again, there was no suggestion or intimation that Dayco
26 was acting for anyone else.

27 Shortly thereafter, on September 12th, Arce and
28 Wachsberger learned that Penn would actually acquire the CIBC
Note. Dayani made the decision for Penn. The acquisition

1 occurred, effective September 16, 2011.

2 On the date Dayco assigned its rights in the Loan Sale
3 Agreement to Penn and Penn and CIBC completed the sale of the CIBC
4 Note to Penn (Exhibit EE), with formal notice given to Debtors
5 (Exhibit FF).

6 Four days later, on September 20, 2011, the Debtors and Penn
7 executed a document entitled Basic Terms and Conditions Regarding
8 Loan Modification ("Term Sheet") (Exhibit GG), which was prepared
9 by Dayani on behalf of Penn. While Penn makes much of the fact
10 that the letterhead of the Term Sheet shows Penn "c/o" Dayco,
11 Dayani signed as "Managing Member", a title he had in Penn and not
12 Dayco. The letterhead proves nothing. The only other mention of
13 Dayco in the Term Sheet is a statement that it is not waiving any
14 rights. In fact, the Term Sheet directed Debtors to pay
15 delinquent real property taxes (\$21,219.63) to Penn, and also to
16 pay the increased interest (\$23,100) and \$8,500 for the August 10
17 - September 10 CIBC Payment.³ It also pointed out that the
18 payments being demanded of Debtors did not cover the October 16,
19 2011, payment of interest. There was no mention there that Dayco
20 had any role in the ongoing relationship. On September 21, 2011,
21 however, Dayco informed Arce that it would be servicing the CIBC
22 Note.⁴

23 _____
24 ³ CIBC was only owed \$8,000. The court finds the \$500
25 discrepancy to be an innocent error having no bearing on the
outcome of this case.

26 ⁴ The parties agree that a loan servicer needs to have a
27 license but Dayco's legal ability to service the CIBC Note is not
28 relevant to Debtors' usury claim. As discussed in the text,
Dayco did not act as an agent in connection with the forbearance
of the CIBC Note.

1 Before the definitive Agreement Regarding Loan Modification
2 ("LMA") was finally executed on January 3, 2012 (Exhibit QQ), the
3 parties acted as though the provisions of the Term Sheet were in
4 effect. Debtors began paying the increased rate of interest
5 (\$23,100 per month) and the one-year extension had begun. In the
6 months following the acquisition of the CIBC Note and up to the
7 execution of the LMA, Dayani negotiated additional terms (other
8 than the interest rate increase, principal reduction and one-year
9 extension that were set forth in the Three Options Memo) of the
10 modification on behalf of Penn, dealing with Debtors' real estate
11 counsel, Judith Rentschler. The foreclosure aspects of the
12 modification had already been fully negotiated.

13 One of the Terms and Conditions of the LMA is ¶ E. After
14 nine lines of boilerplate language, the paragraph concludes with
15 the following sentence:

16 "Borrower acknowledges that this Agreement has been
17 *negotiated on behalf of the Lender, Dayco Funding*
18 *Corporation, a California corporation, which is licensed*
19 *by the California Department of Real Estate (License*
20 *number :01167099).*" (Emphasis added)

21 Debtors have seized on the emphasized recital that Dayco is
22 the Lender. That interpretation, however, is not consistent with
23 the preamble to the LMA which identifies Penn as the Lender. The
24 court believes that a fair reading of the quoted language would
25 imply the word "by" before "Dayco." The real question before the
26 court, however, is whether Dayco in fact had been negotiating a
27 forbearance on behalf of Penn. The mere recital does not make it
28 so. Nor does the evidence.

29 Penn and Debtors later negotiated an Agreement Regarding
30 Loan Extension in April, 2013 (Exhibit ZZ). In Terms and

1 Conditions, ¶ E, the same boilerplate language quoted from ¶ E of
2 the LMA appears except this time there is no recital about Dayco
3 acting as broker. Maybe the omission was an oversight; more
4 likely it confirms the court's finding that Dayco had not acted as
5 Penn's agent or broker.

6 From September, 2011, until March, 2012, Debtors paid Penn
7 interest in the total amount of \$164,380, including three post-
8 dated checks of \$5,000 each in later 2011.⁵ They also paid a
9 \$25,000 extension fee in April, 2013. (Wachsberger testimony).
10 This totals \$189,380 they hope to recover for payments made
11 outside of the one-year period for which they claim treble
12 damages.

13 In March, 2012, with the consent of Penn, Debtors obtained
14 secondary financing from MIC Infinity Fund, LLC ("MIC"). MIC made
15 thirteen interest advances of \$23,100 per month directly to Penn
16 from April, 2012, through April, 2013, for a total of \$300,300.
17 (Wachsberger testimony). While MIC is an exempt lender, and
18 charged Debtors a higher rate of interest on these advances,
19 Debtors reimbursed MIC later for the \$300,300 that was paid to
20 Penn as interest, and correctly they include that total in the
21 amount they seek to recover from Penn.

22 Subsequently Debtors went into default, Penn initiated
23 foreclosure of the Property, and Debtors filed these chapter 11
24 cases on November 12, 2013 to stop the foreclosure.

25 In the course of the chapter 11 cases Debtors made one
26

27 ⁵ Debtors paid Penn \$8,500 in September, 2011, of which
28 \$8,000 was forwarded to CIBC. The remaining \$500 has been
disregarded. See footnote 3.

1 monthly interest payment of \$23,100 to Penn. Then the Property
 2 was sold, effective January 23, 2015. Concurrent with the close
 3 of escrow, Debtors paid additional interest of \$40,000 to Penn
 4 from their debtor-in-possession account. According to the closing
 5 statement (Exhibit CCC) Penn received \$3,158,067 plus interest of
 6 \$2,181.⁶ The principal portion of that total owing to Penn on the
 7 CIBC Note, as modified, was \$2,310,000. Because Penn had acquired
 8 the note for \$2,100,000, Debtors contend that the principal
 9 discount, \$210,000, is recoverable as usurious interest.⁷ Thus
 10 they believe that they can recover the following amounts they paid
 11 (interest except where indicated otherwise):

| Date | Paid By | Amount |
|--------------------------|---------------------------------|--------------------|
| Sept, 2011 - Mar, 2012 | Debtors | \$ 164,380 |
| April, 2013 | Debtors - extension fee | \$ 25,000 |
| April, 2012- April, 2013 | MIC | \$ 300,300 |
| January, 2015 | Debtors | \$ 23,100 |
| January, 2015 | DIP Account | \$ 40,000 |
| January 23, 2015 | Debtors - Principal Discount | \$ 210,000 |
| January 23, 2015 | Debtors - COE | \$ 848,067 |
| TOTAL | | \$1,610,847 |

22 Penn filed a Second Amended Claim (Claim No. 4-2) on December
 23

25 ⁶ The closing statement reflects this additional interest at
 26 \$1,093.83 per day for two days. Debtors did not include this
 27 small payment in their calculations of usurious interest so the
 28 court will ignore it.

⁷ They say nothing about Penn's voluntary reduction of the
 principal from over \$2,400,000 to \$2,310,000.

1 15, 2014, and Debtors filed their Objection to Second Amended
2 Claim on February 19, 2015 (Dkt. No. 174).

3 Pursuant to Stipulation Re Trial Issues and Scheduling filed
4 on March 18, 2015 (Dkt. No. 184), Debtors, Penn, Wachsberger and
5 Arce and Antonette Arce, individually and as Trustees of the Arce
6 Family Trust dated October 17, 2012, as Guarantors, agreed that
7 this court could adjudicate the dispute involving whether or not
8 the California usury laws had been violated and the right of
9 either Penn or Debtors to an award of attorneys fees and costs.

10 The parties also agreed that the court could enter a money
11 judgment in favor of the prevailing parties and against the losing
12 parties. There is a cap of \$3,198,067, which the parties agree is
13 the total amount paid to Penn during these bankruptcy cases. The
14 cap does not apply to any award of attorneys fees and costs.

15 III. DISCUSSION

16 **A. California Usury Law**

17 The parties have briefed the California usury law applicable
18 to the present dispute, including the statutory safe-harbor that
19 Penn believes protects it from Debtors' challenge. Only a brief
20 summary is in order.

21 The California Constitution, Article XV, section 1, states
22 that a party may not charge a fee, bonus, commission, discount or
23 other compensation from a borrower more than the interest
24 authorized by that section "upon any loan or forbearance of any
25 money, goods or things in action." The parties agree that the
26 maximum rate applicable here, absent an exemption, is ten percent.

27 In California Civil Code § 1916.1, ("CC 1916.1") the
28 California legislature has provided an exemption from the

1 applicability of the California Constitution's proscription on
2 charging usury by exempting "any loan or forbearance made or
3 arranged" by a licensed real estate broker, and secured by real
4 estate. That section provides, in part, as follows:

5 For purposes of this section, a loan or forbearance is
6 arranged by a person licensed as a real estate broker
7 when the broker (1) acts for compensation or in
8 expectation of compensation for soliciting, negotiating,
9 or arranging the loan for another, (2) acts for
10 compensation or in expectation of compensation for
11 selling, buying, leasing, exchanging, or negotiating the
12 sale, purchase, lease, or exchange of real property or a
13 business for another and (A) arranges a loan to pay all
14 or any portion of the purchase price of, or of an
15 improvement to, that property or business or (B)
16 arranges a forbearance, extension, or refinancing of any
17 loan in connection with that sale, purchase, lease,
18 exchange of, or an improvement to, real property or a
19 business, or (3) arranges or negotiates for another a
20 forbearance, extension, or refinancing of any loan
21 secured by real property in connection with a past
22 transaction in which the broker had acted for
23 compensation or in expectation of compensation for
24 selling, buying, leasing, exchanging, or negotiating the
25 sale, purchase, lease, or exchange of real property or a
26 business.

27 Calif. Civ. Code, § 1916.1 (Emphasis added).

28 The California Supreme Court has made abundantly clear that:

The intent sufficient to support the judgment [of usury]
does not require a conscious attempt, with knowledge of
the law, to evade it. The conscious and voluntary
taking of more than the legal rate of interest
constitutes usury and the only intent necessary on the
part of the lender is to take the amount of interest
which he receives; if that amount is more than the law
allows, the offense is complete.

Ghirardo v. Antonioli, 8 Cal. 4th 791, 798 (1994), quoting *Thomas v. Hunt Mfg. Co.* 42 Cal. 2d 734, 740 (1954).

The *Ghirardo* court also recites at least three other
principles that are pertinent here. First, intent is relevant in
determining the true purpose of the transaction in question
because the trier of fact must look to the substance of the

1 transaction rather to its form. Second, a transaction is
2 rebuttably presumed not to be usurious. Third, the borrower bears
3 the burden of proving the essential elements of a usurious
4 transaction. *Ghirardo v. Antonioli*, 8 Cal. 4th, at 798-99.

5 **B. What is a Forbearance?**

6 Penn argues that the LMA was a modification of the CIBC Note,
7 and thus it is not a forbearance. The court accepts Penn's
8 contention that the CIBC Note was modified and that the LMA was a
9 modification; that does not mean that the modification did not
10 include a forbearance.

11 A forbearance is an agreement not to insist upon payment at
12 the date of maturity of a debt, or the giving of further time to
13 pay. *Buck v. Dahlgren*, 23 Cal. App. 3d 775, 785 (1972), citing
14 Witkin, Summary of Cal. Law (7th Ed. 1960) pp. 183-184 and
15 *Calimpc Inc. v. Warden*, 100 Cal. App. 2d 429 (disapproved on
16 other grounds *Fazzi v. Peters*, 68 Cal. 2d 590) and *Eisenberg v.*
17 *Greene*, 175 Cal. App. 2d, 326.

18 In *Buck* the creditor agreed to postpone a trustee's sale from
19 November 6, 1967 until December 6, 1967 for the sum of \$500. By
20 that payment, the borrower was given one month further in which to
21 pay the matured loan. Consequently the creditor received .99
22 percent of a \$50,560 debt for a one-month forbearance, or an
23 annual usurious rate of nearly twelve percent. Here, the one-year
24 extension of the maturity of the CIBC Note was a forbearance,
25 albeit part of a more detailed modification of Debtors'
26 obligations. *DCM Partners v. Smith*, 228 Cal. App. 3d 729 (1991)
27 is of no help to Penn. That case involved a credit sale, not a
28 forbearance of a loan of money. The increase of the interest to

1 twelve percent (over the maximum rate of ten percent) implicated
2 California usury law.

3 **C. A Licensed Real Estate Broker Acting as a Principal is**
4 **Not Exempt**

5 When a licensed real estate broker acts as a lender, and not
6 as the agent for another, the statutory exemption of CC 1916.1
7 does not apply. For example, in *Winnett v. Roberts*, 179 Cal. App.
8 3d 909 (1986), a licensed real estate broker made the loan in
9 question. The court held that in a transaction between a borrower
10 and a lender, each acting on its own behalf, where there is no
11 third party licensed real estate broker acting for compensation as
12 intermediary, the loan is not "arranged" by a broker within the
13 meaning of the usury law. 179 Cal. App. 3d at 921. Here, the
14 forbearance contained in the Three Options Memo that Debtors
15 accepted was negotiated by Dayco acting for itself, not as a third
16 party broker. It was its later choice alone to have Penn take its
17 place. No loan was "made" by anyone except CIBC years earlier so
18 the focus is on the "forbearance."⁸ But what does it mean for a
19 loan (or forbearance) to be arranged?

20 In *Creative Ventures LLC v. Jim Ward & Associates*, 195 Cal.
21 App. 4th at 1430 (2011), the court described what is involved when
22 a broker "arranges" a loan:

23 Broker 'arranged' loans are those in which the
24 broker acts as an intermediary and causes a
25 loan to be obtained or procured as by
26 structuring the loan as the agent for the
27 lender, setting the interest rate and points
28 to be paid, reviewing the loan and forbearance
documents, conducting title searches, or
drafting the terms of the loan.

⁸ See discussion, *infra*, whether a forbearance arranged under these circumstances is exempt in any event.

1 *Creative Ventures, Id.*, citing *Gibbo v. Berger*, 123 Cal. App. 4th
2 396 (2004).

3 **D. One Can Act as a Broker for Another When Acting for a**
4 **Wholly Owned Corporation or Other Form of Entity**

5 In *Stickel v. Harris*, 196 Cal. App. 3d 575 (1987), a broker
6 was acting on his own behalf and on behalf of certain fellow
7 partners when they borrowed from a lender and later challenged
8 the loan as usurious. The court distinguished the *Winnett*
9 situation and concluded that the involvement of a licensed broker,
10 not acting exclusively as a borrower, but simultaneously acting as
11 an agent soliciting the loan on behalf of others, was sufficient
12 to trigger the CC 1916.1 safe harbor. The benefit to the broker's
13 partnership and his expectation of a pro rata share of ultimate
14 profits was sufficient to satisfy the statute's requirement that
15 the broker be acting on behalf of another for compensation, or
16 expectation of compensation.

17 Stated otherwise, the compensation can be satisfied by an
18 indirect benefit to an entity owned or controlled by the licensed
19 broker. See, also *Bock v. California Capital Loans, Inc.*, 216
20 Cal. App. 4th 264 (2013); *Stoneridge Parkway Partners v. MW*
21 *Housing Partners III*, 153 Cal. App. 4th 1373 (2007).

22 Here, had Dayani acted as a third party broker for Dayco, or
23 later had either he or Dayco acted as a third party broker for
24 Penn, the CC 1916.1 defense would be available. The "expectation
25 of compensation" element would have been satisfied. That is not
26 what happened. Dayco, then Penn, acted as principals. The Broker
27 Agreement is of no help since its recitals of Dayco's role vis-a-
28 vis Penn are simply not so.

E. Debtors are not estopped from raising the usury defense.

1 Penn argues that Debtors acted in bad faith and with unclean
2 hands by signing documents that purported to comply with law and
3 by waiving defenses, claims and offsets. Those arguments are not
4 convincing.

5 In order to effectuate the statutory policy of
6 protection, the courts have also regularly held a
7 borrower and a lender are not *in pari delicto* in a
8 usurious transaction and the lender may not assert an
9 estoppel against the borrower simply because the
10 borrower took the initiative in seeking the loan, knew
11 of the usurious nature of the transaction, and paid usurious
12 interest without protest.

13 *Buck v. Dahlgren* (1972) 23 Cal. App. 3d 779, 787 (citations
14 omitted).

15 Penn has cited to cases that apply estoppel to assert usury
16 by borrowers. But a common theme in those cases is the
17 questionable conduct of the borrower in connection with the
18 original transaction who later makes the usury claim. For
19 example, in *Buck, supra*, the court imposed the principle of
20 estoppel on a borrower, a real estate developer, whose conduct it
21 described as "avaricious machinations" (23 Cal. App. 3d at 790).
22 The borrower was in full control of the transaction and made
23 fraudulent misrepresentations to the lender, an individual from
24 another country with little experience in real estate lending. He
25 knowingly withheld information about the true value of the real
26 estate collateral and his intentions about repaying the loan.

27 In *Lakeview Meadows Ranch v. Bintliff*, 36 Cal. App. 3d 418
28 (1973), the principal of the borrower was an attorney who was
selected to draft the operative document because of his knowledge
of California law. The lender plainly lacked an intent to charge
an unlawful amount and the borrower, who did not suggest the
agreement was unlawful, believed that what he drafted conformed to

1 the law and did not suggest to the lender that it did. That
2 conduct created an estoppel against the borrower's usury claim.

3 Here, Ms. Rentschler was hired for a limited purpose of
4 reviewing the document Dayani drafted (the LMA). Dayani was the
5 author of that document and he accepted few of her suggested
6 changes. She had little effect on the final version the parties
7 signed. She believed the transaction had been brokered by Dayco,
8 a licensed broker, because the agreement said so and she had no
9 reason, nor was she hired, to question that recital. Had she
10 known otherwise, maybe the outcome would be different. On the
11 record presented, there is no reason for denying Debtors the
12 relief they seek based upon estoppel.⁹

13 **F. Penn has no defense under CC 1916.1.**

14 As noted above, after trial the court asked for further
15 briefing on a very discrete question. That question was:

16 "Where is there a statutory exemption that extends to a
17 licensed real estate broker's "arranged" forbearance
18 other than one that relates to a sale, etc., of property
19 or a business or to a past transaction?"

20 Both parties submitted briefs as requested. Having reviewed
21 those briefs, the court is satisfied that the Debtors are correct
22 and that the California legislature has very narrowly defined the
23 type of forbearances that may be arranged by a licensed real
24 estate broker and thus be exempt from the usury laws.

25 CC 1916.1 extends the usury exemption, in its opening
26 sentence, to "any loan or forbearance" made or arranged by a
27 licensed real estate broker. The second sentence narrows the

28 ⁹ Penn has conceded that release provisions in the various
documents to not apply to a release of usury claims as a matter of
public policy.

1 field where it indicates that "for purposes of this section" the
2 exemption applies only in three circumstances. The first applies
3 to a loan (not applicable here). The second applies to "selling,
4 buying, leasing, exchanging or negotiating the sale, purchase,
5 lease, or exchange of real property or a business for another" and
6 the broker either (A) arranges a loan or (B) "arranges a
7 forbearance" in connection with that sale, purchase, lease, etc.
8 That second alternative is not applicable here either since there
9 was no sale, lease or exchange of the Property.¹⁰ The third
10 exemption is found where the broker "arranges or negotiates for
11 another a forbearance, extension, or refinancing of any loan ...
12 in connection with a past transaction in which the broker had
13 acted for compensation."

14 Note that there are only two instances of forbearance
15 mentioned: in connection with a sale and in connection with a past
16 sale in which the broker acted as such. Neither occurred here.

17 Penn would have the court apply the "past transaction"
18 exception of CC 1916.1(3) to the fact that Arce was involved in
19 the original acquisition of the Property and in arranging and
20 negotiating the CIBC Note. Penn overlooks the qualifying language
21 in the statute that the broker to be exempt in a present
22 transaction must have been the broker in the prior transaction.
23 Arce was not the broker in the present transaction, as discussed,
24 *supra*, and he acted only as a principal in the negotiations to
25 acquire the Property and later to borrow from CIBC.

26 Penn points to the legislative history and finds that the

27 _____
28 ¹⁰The lease of the Property to Crunch is irrelevant to the
usury analysis as it did not involve Dayco or Penn.

1 phrase "for purposes of this section" only sets forth examples
2 because the word "only" is not present. Penn does not want the
3 court to insert that word "only" but it does want the court to
4 insert "for example." It is axiomatic, however, that the court is
5 obligated to apply the words of the statute without consulting
6 legislative history, ballot initiatives, or other secondary
7 sources when the language is clear. Here the language is clear.
8 There are only two types of forbearance that are exempt.

9 The court assumes the Legislature "knew what it was saying
10 and meant what it said." *Del Mar v. Caspe*, 222 Cal. App. 3d 1316,
11 1328 (1990), quoting *Pac. Gas & E. Co. v. Shasta Dam etc. Dist.*,
12 135 Cal. App. 2d 463, 468. If it wanted the section merely to
13 "include" the stated examples it certainly could have. The court
14 cannot graft the expansion Penn seeks into the limiting words "for
15 purposes of this section."

16 From the foregoing the court concludes that there is no
17 exemption for a forbearance that was granted here under CC 1961.1
18 and that Penn's defense must fail.

19 **G. Even if CC 1916.1 applies, the result is the same**

20 Penn cannot prevail even if its interpretation of CC 1916.1
21 is correct.

22 **1. The acquisition of the CIBC Note**

23 The critical event in this case has to do with the
24 forbearance, originally found in the Three Options Memo, then set
25 forth in the Term Sheet, and finally reflected in the LMA. The
26 negotiation by Dayco to acquire the CIBC Note from CIBC is of no
27 consequence. In any event, as summarized, *supra*, Dayco was acting
28 on its own behalf until the time it assigned its contractual

1 rights to Penn in September, 2011. While the usury laws are not
2 implicated in that first transaction, had they been, Dayco could
3 not have claimed an exemption because it was acting on its own
4 behalf and the fact that it was a licensed broker is of no moment.
5 That is all irrelevant.

6 **2. The Broker Agreement**

7 When Penn and Dayco, joined by Hankey, signed the Broker
8 Agreement they purported to acknowledge in some fashion that Dayco
9 would be acting on behalf of Penn. Taking that agreement at its
10 face, it does say that Dayco will discuss modification terms with
11 Debtors "on behalf of Penn" and after the CIBC Note is acquired,
12 it will "negotiate, finalize and place the modification" on behalf
13 of Penn. It is not unreasonable to say that the \$50,000
14 compensation was contemplated or expected for those functions
15 Dayco was to perform.

16 While language in the Broker Agreement comes close to
17 describing the expectations of the parties as to the role Dayco
18 might have played in connection with the acquisition of the CIBC
19 Note by Penn and the subsequent modification with the Debtors, the
20 facts betray those expectations.

21 As Dayani made clear to Debtors in Exhibit T-1, Dayco was
22 buying the CIBC Note; Dayco was in charge! Thus by early May,
23 2011, the new twelve percent interest rate and the one-year
24 extension of maturity had been arranged - but not by a third party
25 broker.

26 Dayco acted solely for itself up until Penn took over its
27 position and acquired the CIBC Note. Thereafter, Penn handled all
28 of the remaining modifications on its own. Dayani acted solely

1 for Penn, as shown in the Term Sheet and the LMA. In any event,
2 the forbearance, namely the extension of time and the increased
3 interest, had been negotiated by Dayco in April 2011, acting
4 solely on its own. Penn and Dayco's attempts to paper the
5 arrangement in the Broker Agreement fail based on the events as
6 they occurred.

7 **3. The Assignment from Dayco to Penn**

8 In connection with the payoff to CIBC, Dayco assigned all of
9 its contractual rights to Penn and CIBC transferred the CIBC Note
10 to Penn, with Penn providing the agreed consideration both from
11 its own funds and from money borrowed from one of Hankey's
12 business entities. That transaction is of no particular relevance
13 to the issues presented here since it did not require the
14 involvement of a licensed California real estate broker nor did it
15 implicate the usury laws.

16 **4. The Term Sheet and the Ultimate LMA Constituted a
17 Forbearance and a Modification**

18 Dayani proposed the Three Options Memo on behalf of Dayco and
19 later drafted and executed the Term Sheet on behalf of Penn.
20 Thus, any contention that Dayco was negotiating or "arranging" the
21 modification and the included forbearance is not found anywhere in
22 the documentation. The after-the-fact recital by Dayani that he
23 was acting in dual capacities is insufficient for the court to
24 find to the contrary. The later obtaining of a California
25 licensed finance lender license by Penn was too little too late.
26 *Whittemore Homes, Inc. v. Fleishman*, 190 Cal. App. 2d 554 (1961),
27 *Westman v. Dye*, 214 Cal. 28 (1931).

28 Based upon the authorities cited above, the negotiation of

1 the terms of the forbearance, either as originally set forth by
2 Dayani on behalf of Dayco in the Three Options Memo, or ultimately
3 formulated in the Term Sheet between Penn and Debtors, or the
4 ultimate LMA between the same parties (and others), involved one
5 principal then another acting on its own behalf. Thus cases such
6 as *Stickel* and *Park Terrace Ltd.* offer no consolation to Penn
7 because there simply was no broker involved at all. *Buck* and
8 *Winnett* compel the court, on the facts presented, to conclude that
9 there is no exemption under CC 1916.1 available to Penn, assuming
10 it applies at all.

11 Penn intended to collect twelve percent interest. Debtors
12 have carried their burden and rebutted the presumption against
13 usury and they are entitled to recover the interest they paid.

14 **5. What damages may Debtors recover?**

15 Debtors contend that because Penn acquired the CIBC Note at a
16 \$210,000 principal discount, they should recover that \$210,000 as
17 part of their usury damages. That is not a convincing argument.

18 In *Lee v. Marchetti*, 4 Cal. App. 3d 97 (1970), the court
19 dealt with a situation where a series of transactions supported an
20 inference that the parties were involved, albeit for different
21 motives, in a conspiracy to evade the usury laws. There the court
22 reversed a grant of summary judgment and remanded the matter for
23 trial to determine the material facts in support of a discount of
24 a note. In doing so the court described a situation more like the
25 present case. It indicated that the purchase of a note at a
26 discount does not, per se, prove that a transaction is usurious.
27 One who loans \$100,000 and takes back a note in that amount can
28 sell it to another for \$75,000. The buyer has not loaned the

1 money at the discounted rate of twenty-five percent, but has
2 simply purchased the debt at a discounted price. 4 Cal. App. 3d
3 at 101-102, citing *Janisse v. Winston Investment Co.*, 154 Cal.
4 App. 2d 580, 582.

5 The court went on to indicate that if the original note
6 holder is a dummy, and if in fact the form of a transaction is a
7 sham and subterfuge to cover up a loan from the discount-buyer to
8 the original borrower, then the discount is deemed to be usurious
9 interest.

10 In this case, Debtors received all of the money loaned by
11 CIBC; the fact that Penn acquired that loan at a discount does not
12 suggest anything other than the simple hypothetical identified in
13 *Lee v. Marchetti*. There is no evidence of any sham transaction;
14 Debtors received the total amount they borrowed; the usury laws
15 were violated with the forbearance's extension of the maturity
16 date and increase of the rate of interest on the CIBC Note that
17 represented the full amount still owing by Debtors. The \$210,000
18 discount will be disallowed as part of Debtors' damage claim.

19 Debtors also seek to recover the \$25,000 extension fee. In
20 their trial brief they did not articulate a reason why that should
21 be part of their recovery. An extension of maturity of a debt is
22 not itself usurious. For these reasons, the court will not allow
23 that amount.

24 In their trial brief Debtors subtract from their damage
25 summary \$75,144.00 paid to Penn's counsel as legal fees, then they
26 add that amount back in, plus \$51,043.00 apparently paid outside
27 of escrow. These items have not been explained either in the
28 briefs or the Debtors' witnesses' testimony. For that reason they

1 will not be allowed as part of Debtors' recovery.

2 The remaining amount, representing the total amount of
3 interest paid, (\$1,610,847 - \$210,000 and - \$25,000 = 1,375,847),
4 subject to possible offset discussed, *infra*, should be recovered.

5 **6. Debtors are not entitled to treble damages.**

6 Debtors' counsel in her trial brief and oral argument portray
7 the Dayani brothers and their related entities as loan sharks
8 preying on innocent borrowers, and she asks the court to punish
9 them by trebling the amount of interest paid in the last year
10 before and up to the sale of the Property. She concedes, however,
11 that such an award is solely a matter of discretion and not
12 mandatory as a matter of law.

13 The court will not impose such a drastic remedy. Regardless
14 of what Debtors and their counsel believe, the facts presented
15 show the Dayani brothers' businesses as successful and them as
16 generally careful businessmen. Here, however, they were careless
17 in their drafting and in their communicating to Debtors, nothing
18 more. The usury laws present a minefield that people in the
19 Dayani brothers' position, with their and Dayco's status as
20 licensed brokers, can readily navigate. This time they did not
21 navigate carefully. The court has little doubt that Debtors would
22 have taken Option Three had Dayco been identified and in fact had
23 acted as Penn's agent from the outset. And clearly Dayani could
24 have memorialized in writing and in fact what he stated at trial
25 was his intention, namely that Dayco act for Penn. He did not,
26 and it did not.

27 The court cannot reach a result based upon what might -
28 indeed should - have happened, but only upon what DID happen. The

1 Dayani brothers and their two companies chose not to seek
2 independent legal advice, or even apply their own legal training,
3 nor did they cross their T's or dot their I's carefully, but they
4 should not be punished beyond the very significant result of Penn
5 having to repay all of the interest it received plus Debtors'
6 attorneys fees and costs.¹¹

7 **7. Penn may be entitled to an offset.**

8 From the foregoing it is clear that the court must eliminate
9 the usurious interest paid by Debtors to Penn. It is not so
10 obvious that Penn is not entitled to a non-usurious rate of
11 interest accruing after maturity. The CIBC Note, held by Penn,
12 was extended to a new maturity date of October 15, 2013, (Exhibit
13 ZZ). Accordingly, Penn may be entitled to recover by way of
14 offset interest at the maximum non-usurious default rate from
15 October 31, 2013 until January 23, 2015, the date the Property was
16 sold.

17 The principle the court considers is drawn from *Epstein v.*
18 *Frank*, 125 Cal. App. 3d 111 (1981). In that case the court framed
19 the question as follows: Is the payee of a usurious note entitled
20 to recover post-maturity interest?

21 In answering the question in the affirmative, the court
22 stated:

23 "The denial of interest up until the maturity of the
24 note is a sufficient deterrent against the exacting of

25 ¹¹ In her post trial brief Debtors' counsel continued her
26 unfounded attack on Penn and Dayco by mentioning their "standard
27 business model" and a "stunning foreclosure rate of 90%" with
28 absolutely no support for those statements in the record. The
court admonishes her for such inappropriate remarks at this point
in the proceedings, and cautions against the possibility of
sanctions for any further conduct of this nature.

1 usurious interest. The payee, notwithstanding the
2 usury, has the right to recover the principal of the
3 note in full on the date of its maturity. If the
4 obligor improperly withholds payment of this obligation
5 it is neither unjust nor contrary to policy that he be
6 chargeable with interest at the legal rate from the date
7 he was obligated to pay the note until the date he
8 discharges that obligation, or to the date a judgment is
9 rendered against him."

10 125 Cal. App. 3d at 123.

11 Penn did not say anything about this offset, or even cite
12 *Epstein*, in its trial brief, but it did mention the case and the
13 possibility of such a recovery in its closing argument. Debtors
14 had no warning about this possibility. Accordingly, the court
15 desires further briefing on the following limited issues:

16 Can a party forced to repay usurious interest paid
17 before and after maturity claim an offset for post-
18 maturity interest at a lawful rate of interest from the
19 date of maturity, October 31, 2013, to the date of
20 payment January 23, 2015? If so, what is the correct
21 rate, seven or ten percent?

22 The parties are to submit simultaneous briefs, not to exceed
23 seven pages, on this limited issue on October 9, 2015.

24 IV. DISPOSITION

25 Once the additional briefs have been filed and considered the
26 court will issue a decision on the remaining issues. Then counsel
27 for Debtors should prepare, serve and upload an order and judgment
28 in favor of Debtors and against Penn in the amount of 1,375,847
29 (perhaps reduced in an amount to be decided by the court) for the
30 reasons stated in this Memorandum Decision and any subsequent
31 decision, with an award of attorneys fees and costs to be the
32 subject of a post-judgment motion in accordance with Civil L.R.
33 54-5, made applicable by B.L.R. 1001-2(a).

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Service List

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