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PERSPECTIVE

Avoiding juries: a transactional lawyer lesson

By Michael Cypers and Brett J. Cohen

In a nationwide economy, transactions increasingly involve multiple factors located in different states. In a complex real estate secured loan transaction where the property is located in California, it is not uncommon for the operating partner, the finance partner and the lender to each be located outside California, perhaps all in different states. And as a result of negotiations, parties can agree to select the law governing disputes as the law of one of their states, such as New York, or even a state in which none of parties is located but which has a well-developed commercial law, such as Delaware.

There are certain bedrock principles of California law. One is that parties cannot waive jury trial in advance of suit except by use of either of two methods which have been long approved by our Legislature: arbitration or judicial reference.

In *Rincon EV Realty LLC v. CP III Rincon Towers Inc.*, 2017 DJDAR 929 (Cal. App. 1st Dist. Jan. 31, 2017), which dealt with complex financing arrangements relating to a property in San Francisco and was filed and tried in California, the parties agreed in their transactional financing documents to the application of New York law and an express waiver of jury trial. When significant litigation was filed in California, this set up a direct clash between the parties' right to select governing law and the right to jury trial in California.

In *Rincon*, the right to jury trial in California won.

The California Court of Appeal concluded that, based on the facts before it, with both the property and the court located in California, using established California choice-of-law principles, it was error for the trial court to strike plaintiff's jury demand notwithstanding the express contractual jury trial waiver.

The parties (and the court) completed a bench trial, which the defendant won. The result was largely reversed because the appellate court concluded that trial plaintiffs were deprived the right of jury trial.

What the *Rincon* Court Ruled

The *Rincon* court noted that the California Supreme Court in *Grafton Partners v. Superior Court*, 36 Cal. 4th 944 (2005), stated: "[T]he Legislature has expressly authorized agreements to submit future disputes to arbitration or to a referee," citing Sections 638 and 1281 of the Code of Civil Procedure. "But neither Section 631 [specifying the ways in which a party can waive the right to jury trial] nor any other statute authorizes predispute waivers of the right to jury trial by parties who submit their disputes to a judicial forum." "Such waivers therefore are not enforceable."

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A typical structure for California real estate secured loans, particularly with respect to syndicated loans, provides for the California real property as security, a newly formed Delaware entity (often, a newly formed bankruptcy remote, single purpose entity) as the borrower, and loan documents governed by New York law, other than provisions for the creation, perfection or enforcement of the security interests, which, when dealing with California property, will be governed by California law. This was the deal structure in *Rincon*. The loan documents generally contain a host of waivers by the borrower and guarantor. Often among them, a waiver of jury trial. A waiver of jury trial was contained in the *Rincon* loan documents.

The *Rincon* court held that the combination of the property and the forum being located in California required that the jury trial waivers under New York law be set aside — even though the litigants were from out of state, not California. The court again cited *Grafton*, stating that "protection of the right to jury trial for litigants

in California courts unless they waive the right in a manner prescribed by the Legislature — is not only directly implicated, but is central to California's system for resolving civil cases, for all litigants." The *Rincon* court further rejected defendant's argument for a "sophisticated party exception," ruling that the right to jury trial applies to sophisticated and non-sophisticated parties alike who litigate their disputes in our courts.

Accordingly, the trial that went forward as a bench trial on both legal and equitable claims after the trial court struck the jury demand was reversed on all the legal claims. The Court of Appeal ruled that eliminating the right to jury trial was "error per se, and no showing of prejudice is required of a party who lost at trial." By contrast, the trial court's rulings on the equitable claims were affirmed, as the plaintiff had no right to jury trial of those claims.

What Transactional Lawyers Should Know

Transactional lawyers need to know that if a dispute regarding a transaction they are negotiating is later litigated in California, the parties simply cannot "waive jury" in advance, as they can in most other states, including commercial headquarters states like New York and Delaware. There are established ways in California for the parties to agree to waive jury trial in advance, namely arbitration and judicial reference. These clauses need to be carefully drawn. For a recent cautionary tale regarding the drafting of an arbitration clause in a limited liability company agreement, see *Rice v. Downs*, 248 Cal. App. 4th 175 (2016).

As a condition to closing the loan (particularly with respect to securitized loans), lenders require opinions of counsel — for matters under California, New York and Delaware law with respect to the entities, governing law and the enforceability of the loan documents, among other things. This often results in multiple firms providing the requisite opinions. The opinions are delivered and can be re-

lied upon by not just the lender (often multiple lenders), but also rating agencies, participants and assignees of all or a portion of the loan, among others. This creates potential exposure to the issuing firms with respect to the matters addressed in their respective opinions.

Accordingly, and given the decision in *Rincon*, great care should be given by the firms delivering such opinions to make sure they do not inadvertently opine that the waiver of a jury trial is enforceable in California. Depending on the construct of the opinion by a particular firm, a choice-of-law opinion may touch on the subject or, on a broader basis, the more general enforceability opinion might suggest that the waiver is effective. To avoid being a target by the recipients of those opinions, the issuing firms should make sure that their form includes a broad carve out for certain waivers that might be deemed unenforceable or, given the *Rincon* opinion, perhaps an express carve out as the potential unenforceability of the jury waiver.

While *Rincon* does not enunciate new law, it re-emphasizes established principles of great interest to litigants, litigators and transactional lawyers alike.

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