

A Practical Guide to Non-Judicial Foreclosure

By Maggie Loates

Many lenders have become intimately familiar lately with the sharp end of a non-judicial foreclosure, but still may be a bit hazy about the process. The purpose of this article is to clarify the procedure.

Considering the Penultimate Sanction: Non-Judicial Foreclosure

When a borrower has failed to repay its loan despite having agreed to Plans A, B, C, D and E, then it is time to think about Plan F, Non-Judicial Foreclosure.

At this point, notice should have already been given to the borrower that it is in default, and that the lender has opted to accelerate the loan (if not already matured) and charge the default interest rate provided for in the promissory note.

Preliminary Matters: Do the Recent Residential Foreclosure Statutes Apply?

In the last few years, the California legislature has revised the California Civil Code to give (temporarily) individuals whose loans are secured by owner-occupied residential real property the opportunity to work out alternative payment options with their lenders so they do not lose their homes in foreclosure, although many provisions expired January 1, 2011. Before a non-judicial foreclosure can be initiated, it still must be determined whether the property and the loan are covered under California Civil Code section 2923.5.

The criteria which subject a loan to Section 2923.5 (which sunsets January 1, 2013) are:

(1) The deed of trust was recorded between January 1, 2003 and December 31, 2007, (2) the encumbered property is a single family residence or contains no more than 4 dwelling units, and (3) one of the units is occupied by the borrower as his/her principal residence and indicated to be such in the loan documents.

If all of these conditions exist, then it will be necessary for the lender to comply with the provisions of Section 2923.5(a), including contacting, or attempting to contact, the borrower to assess his/her financial situation and to explore options for the borrower to avoid foreclosure. In that event, FRBC can advise and assist its clients in complying with the legal requirements.

Under Section 2923.5, if the property is subject to the above conditions, a lender may not record a Notice of Default until 30 days after either (1) the lender's initial contact with the delinquent borrower, or (2) if the lender has not been able to contact the borrower, 30 days after the due diligence requirements of Section 2923.5(g) have been satisfied.

In addition, as discussed in the accompanying article by Albert Moon, effective April 1, 2012, three new requirements relating to the issuance of a Notice of Sale for a non-judicial foreclosure involving property containing one to four single-family residences must be satisfied.

On the other hand, if the property securing the loan is

commercial, multi-family residential, in development, raw land, or some other kind of non-owner occupied housing, then these restrictions do not apply.

Getting Started: Initiating the Non-Judicial Foreclosure Process

When the lender has made the decision to resort to Plan F and non-judicially foreclose on the property securing a borrower's loan, the first thing that needs to be done is to determine if the loan is subject to California Civil Code section 2923.5. Once that has been clarified, and the appropriate actions taken if that section does apply, a Declaration of Default is prepared for the client's signature, and sent to the Foreclosure Trustee ("Trustee"). In addition, a Declaration re Compliance will be necessary, evidencing the lender's compliance with the residential statutory requirements.

In the Declaration of Default, it is usual to request a unified sale, which will include the foreclosure sale of the personal property described in the deed of trust as well as the real property. If the lender has personal property collateral other than as described in the deed of trust and wishes to have it included in a unified sale, the Trustee will require copies of the executed Security Agreement and any filed or recorded UCC-1 Financing Statements. The Trustee also finds it useful to have a copy of the lender's Policy of Title Insurance.

The following information is required for the Declaration of Default: (1) the amount of

the unpaid principal balance on the loan, (2) the date to which interest is paid, (3) the interest rate currently being charged, (4) the per diem interest amount, and (5) any late charges which have accrued.

Depending on the status of the loan, certain additional information may be required by the Trustee: (1) if the loan has not matured, the Trustee will need: (a) the date the first missed installment payment was due, and (b) the total amount of all unpaid installments from that date to the present; or (2) if the loan has matured, the Trustee will need the amount of unpaid interest that has accrued through the present date.

If the lender has expended any funds on post-default appraisals or property inspections, forced-placed insurance, maintenance of the property, or other costs associated with preserving the property, those must be itemized for the Trustee to be included in the default amount. Legal fees related to the foreclosure process can be added at a later stage.

If the loan is being accelerated due to a non-monetary default, a description of that default must be set forth in the Declaration of Default so the Trustee can include that in the Notice of Default as the cause of the breach.

The Trustee will then prepare a draft Notice of Default ("NOD"), which is the document that will be recorded with the County Recorder and will start the clock ticking on the foreclosure. Some Trustees require the lender to sign other documents in addition to the Declaration of

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Default. In any event, the client will have the opportunity to review and approve the draft NOD before it is recorded.

The Long Wait: The 90-Day Reinstatement Period (Possibly Longer)

Recording the NOD commences the first reinstatement period, during which, if the loan has not matured, the borrower may bring the loan current by paying all of the delinquent installments, plus late charges, and any other costs incurred by the lender. If this has occurred, the Trustee will be advised to stop the foreclosure and record a Notice of Rescission of the NOD. If the loan has matured, the borrower may stop the foreclosure during this period by paying off the entire amount owing, including interest, late charges and other fees and costs.

Ten days (or less) after the commencement of the 90-day period, the Trustee will mail a conformed copy of the recorded NOD to all interested parties, and again within 30 days of recording of the NOD. The Trustee obtains issuance of a Trustee's Sale Guarantee ("TSG") from its title company, which lists all of the parties required to be notified in the 10- and 30-day mailings. The TSG is similar to a Preliminary Title Report and will show all the exceptions on the property that would be disclosed by a "Prelim," including any junior deeds of trust. If the loan was for construction purposes, the TSG will often show multiple mechanic's liens filed by contractors and

sub-contractors who have not been paid. In many cases, the TSG also reveals unpaid property taxes and tax delinquencies for prior years.

The TSG guarantees the lender against any loss up to the amount of the Guarantee by reason of any incorrectness in the vesting of the property, the legal description of the property, the names and addresses of lienors, taxing authorities, and those requesting notice, and the name, address and publication schedule of the legally mandated newspaper in which the Notice of Sale must be published.

Almost There: Setting the Sale

At the end of the 90-day period, assuming the borrower has not brought the loan current, the Trustee will be free to set a date for sale of the property and commence publication of the Notice of Sale ("NOS"). However, the borrower retains the right to reinstate the loan and stop the foreclosure by paying the delinquent amounts up to five (5) days before any sale date.

An Authorization to Publish will be forwarded to the client for review and completion. The client will need to bring the accrued interest amount current and if the per diem rate has changed, to include that figure. Any expenditures should also be added, including legal fees. The finalized Authorization will be delivered to the client for signature, and then forwarded to the Trustee, who will then draft a Notice of Sale based on the updated figures.

At some point during the foreclosure process, the lender will probably need to sign a Substitution of Trustee form, which will substitute the Trustee for the original

trustee under the deed of trust (unless they are the same), thus enabling the Trustee to conduct the foreclosure sale. This document must be signed under notary and the original returned to FRBC, since a document to be recorded in the County Recorder's records must be an original.

Once the draft NOS has been approved by the client, the Trustee will have it recorded with the County Recorder, and arrange for the Notice to be published once a week for three (3) weeks in the designated newspaper for the area in which the property is located. This may not necessarily be the newspaper with which the lender is most familiar. The sale date will be set for approximately one week after completion of publication.

The Final Stretch: Preparing for the Sale

Shortly before the date set for the sale, Bidding Instructions will be prepared based on information provided by the client. The Instructions will include all outstanding unpaid loan amounts, including interest through the projected sale date, and updated legal fees and costs. The Trustee will add its fees and costs to the outstanding loan amount so the total owing will also include those sums.

The client will have the choice of adding the Trustee's fees to its credit bid, thereby insuring that any over-bidder will pay those fees as part of its bid. Bidding Instructions are an art, not a science, and the amounts of a lender's credit bid will be affected by factors such as the value of the property and the existence of other collateral or Guarantors as a source of repayment for the loan.

The Bidding Instructions

offer the lender three (3) options for its credit bid: (1) the Trustee may be instructed to credit bid the full amount owing; (2) the Trustee may be instructed to bid a specific amount which is less than the amount owing; or (3) the Trustee may be instructed to commence the bidding at a certain figure, then make certain incremental bids in the event there is another bidder at the sale, and be given a maximum amount he is authorized to bid on the client's behalf. FRBC can advise its clients on strategies for determining the bid amount and which option to choose.

Once the Bidding Instructions have been completed and signed by the client, they are forwarded to the Trustee, who will instruct its agent accordingly. If a representative of the lender wishes to attend the sale in person, he or she is certainly welcome to do so. However, the Trustee's agent has full authority to make all bids on behalf of the lender and the client's representative will not be required to do anything unless he or she wishes to do so.

In the event a borrower decides it doesn't want to lose its property and makes the lender an offer to resolve the delinquencies shortly prior to the sale date, the Trustee's sale can be postponed as many times as necessary for 365 days from the initial date set for the sale.

The Deed Is Done: The Property Reverts to the Lender

After the sale, the Trustee will prepare a Trustee's Deed Upon Sale for the lender's review. The Trustee will provide a copy of the recorded Deed, and some time later, the original Trustee's Deed will be mailed to the client by the County Recorder.