

PUBLICATION

Some Lenders May Soon Be Forced to Follow Through With Residential Foreclosures

August 13, 2010

Since the onset of the financial crisis and accompanying stagnant real estate market, many lenders have been reluctant to foreclose on delinquent residential properties, especially those subject to a condominium or homeowners association (HOA) regime. This approach lies partly in the fact that banks have not been eager to show "upside-down" properties on their books. In most states, a lender steps into the shoes of the delinquent borrower and becomes liable for condominium and HOA assessments once it takes back title to the property. However, this highly common practice of lenders delaying the foreclosure process to avoid financial responsibility for distressed residential properties soon may be coming to an end.

Lenders typically file the foreclosure action on delinquent properties in an effort to preserve their rights to foreclose. Once filed, there is little incentive for the lender to complete the process and take title to the property until it has found a buyer for the property or is otherwise ready to take responsibility for the liabilities associated with the property. Given the judicial backlog in many courts today, lenders can often delay taking back title to a property for several years, thus allowing the lender to avoid assuming significant financial liability for such maintenance costs and assessments. This practice has caused considerable financial strain on many homeowners and condominium associations. In fact, it has been reported that over 60 percent of condominium and HOA associations in Florida currently are struggling from unpaid association dues; these associations have reported recently that more than 50 percent of their unit owners have already missed paying two months or more of their association dues and maintenance fees. Every month of delay usually means another month of potential bad debt write-off for an association, which becomes a common expense to be paid by the rest of the unit or home owners.

In a recent ground-breaking state court decision in Florida, a state particularly hard hit by residential mortgage foreclosures, one court has upheld the HOA's right to recoup these past due assessments and costs from the lender, despite the fact that the lender has yet to take back title to the delinquent property. In *HSBC Bank USA, et al. vs. Keys Gate Community Association, Inc.*, A Florida Non Profit Corporation, et al., the homeowners' association successfully introduced a new procedure, dubbed a "reverse foreclosure."

In *Keys Gate Community Association*, the homeowners' association filed and foreclosed its own claim of lien on the delinquent property and acquired title to the property through its own foreclosure sale in April 2007. However, the home-owners' association could not sell the property because of the lender's senior priority mortgage. In June 2007, the lender filed its foreclosure against the delinquent property. Yet, two and a half years later, the lender had not completed the foreclosure process. As a last resort to move the case forward, the homeowners' association set for hearing a summary judgment motion against itself, and asked the court to issue partial summary judgment in favor of the lender and to immediately grant the lender's request to take title to the unit as stated in the lender's foreclosure complaint. As part of this procedure, the association waived its rights to the property, and as the current unit owner, waived its rights to a public sale. The court granted the homeowners' association's motion, and directed the Clerk of Court to issue a certificate of title immediately transferring ownership of the property to the lender, thus triggering the lender's requirement to pay its share of past due assessments, legal fees, court costs and all assessments going forward.

It is important to point out that the reverse foreclosure procedure can only be filed after a home-owner is out of the picture and the home is legally the property of the homeowner's association.

The use of this new legal strategy saved the Keys Gate Community Association a minimum of eight months or more of bad debt write-offs. Furthermore, given the current logjam of foreclosure cases pending in many state courts, clerks of court have enthusiastically endorsed this new procedure as an effective means of reducing their backlogs. Until the financial crisis subsides and the housing market regains steam, undoubtedly many homeowners' associations will increasingly use this procedure in their quest to force lenders to take title to financially upside down properties much faster than the lender may have anticipated.

Mr. Tanner is an attorney in our Baton Rouge office.