

LAW REVIEW

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PROTECTING TENANTS AFTER A FORECLOSURE

We have been cranking out columns about short sales, deeds in lieu of foreclosure, loan modifications, home equity sales and bankruptcies—strategies for folks who are “upside-down” on their property.

But what happens after a foreclosure when the lender takes back the property or someone buys the property at the bank’s foreclosure? Can the family living in the house be evicted?

Protecting Tenants at Foreclosure Act of 2009

On May 20, 2009, the Helping Families Save Their Homes Act of 2009 was signed into law by President Obama. The legislation included Title VII—the Protecting Tenants at Foreclosure Act of 2009.

The Act provides that in the case of any foreclosure on a federally-related mortgage or on any dwelling or residential real property, the party taking title to the property following the foreclosure, either the original foreclosing lender or a buyer at the foreclosure sale, assumes the property, buys the property, subject to the rights of any bona fide tenant. That’s huge. The Act applies to condos, single family homes and multi-family dwellings.

Bona Fide Tenant

In order to qualify as a bona fide tenant under the Act, three things must take place: (1) the tenant must not be the borrower who is foreclosed upon, or immediate family (such as a child, spouse or a parent of the borrower); (2) the tenant's lease must be an arms-length transaction (not a last minute phony lease); and (3) the rent due under the lease must not be substantially less than fair market rent for the property.

If a bona fide tenant resides on the foreclosed property, the tenant cannot be evicted before the expiration of the lease term; but if the lender or party buying at the foreclosure sale intends to utilize the property as a primary residence or sells the property to a new owner to use as a primary residence, the tenant can be evicted with 90-days' notice. The Act does not specify what qualifies as using the property as a primary residence, but I suspect that excludes use as a vacation rental or second home.

90-days' notice to vacate is required when there is no written lease or when the lease is terminable on short notice, like month to month.

The new law requires 90-days' notice; 30-days more than recent California law gives tenants following foreclosures. The Act does not protect the original borrower (versus a tenant) being foreclosed upon. A borrower residing on the foreclosed property must be given a 3-day notice to vacate.

Purpose of Law

With the unprecedented number of foreclosures occurring across the country, it was increasingly evident that not only were homeowners the victims of the downturn of the economy, but tenants residing in residential properties were also victims. All too often tenants were caught unaware that the home they were living in was being foreclosed on and were given little or no notice of the need to vacate, so the objective of this new Act is to ensure that tenants receive notice of the foreclosure so they are not abruptly displaced.

Some Issues

Some writers contend that the way the Act is written (“all foreclosures”) it may apply to homeowner association lien foreclosures, which makes no sense; however the Act recites that it applies to any “residential foreclosure.”

The new law is silent on whether a party taking ownership after foreclosure may terminate the lease of a bona fide tenant if the tenant defaults, like fails to pay rent. My take is the Act does not prevent early termination of a lease (e.g. 3-day notice) if the tenant defaults.

The Act is set to expire on December 31, 2012 unless it is extended by Congress prior to that date, and that probably depends on the state of the economy. Let's hope it is not renewed.

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